

# Building Products market update

Industry Consulting Team | Q4 2022

## Matt Roth

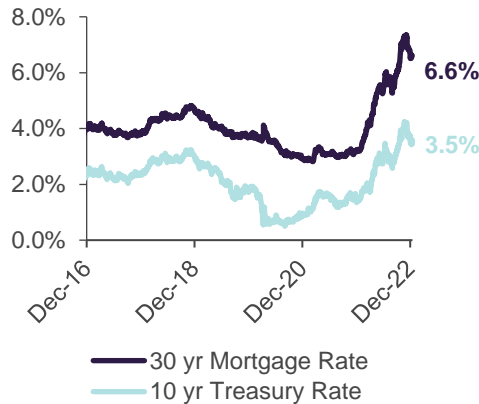
Industry Consultant  
Building Products  
202.835.9319  
[Matt.Roth@Truist.com](mailto:Matt.Roth@Truist.com)

## Highlights

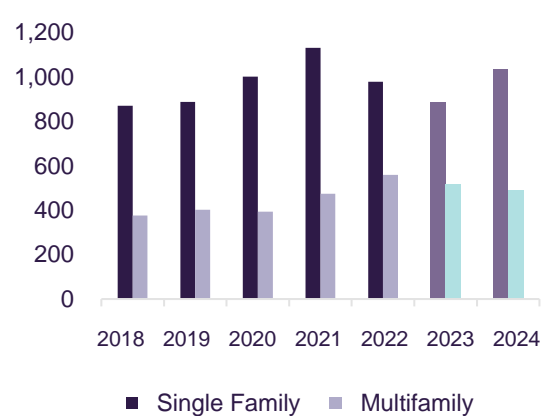
- Fed is successfully slowing down the economy
- New residential starts expected to bottom in 2023
- Non-residential backlog remains strong
- Repair and remodel slowing to more moderate growth rate
- Nearly all products remain at elevated prices compared to pre-pandemic

**Macro economic update:** The Federal Reserve (Fed) remains highly focused on slowing down the economy with hopes of not triggering a meaningful recession. On a positive note, inflation is clearly lower than peak levels seen this past summer, but questions swirl around how much further interest rates need to increase and how long will they remain at elevated levels. In order to feel better about demand prospects for 2023, the building products community wants to know when rates will stabilize and then try to quantify whether damage has occurred in other parts of the economy that could further impact housing trends. Home buyers will need some time to digest increased mortgage rates, but new home sales are expected to grind on due to growing home buyer segment of the population and the historic deficit of housing inventory. The Fed is positioning for additional short term interest rate hikes, but longer-term rates like the 10yr treasury and 30yr mortgage rates do not necessarily move in lock step. National Association of Home Builders (NAHB) is currently projecting the average 30yr mortgage for 2023 will be 6.74% and falling to 5.91% in 2024 signaling that the current rate of 6.84% could be near peak levels.

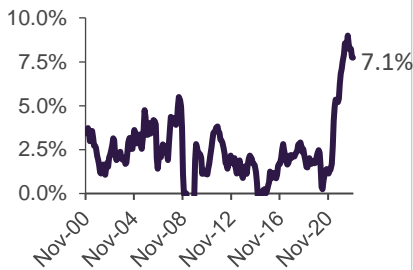
## Mortgage & Treasury



## SF & MF Housing Starts Projections



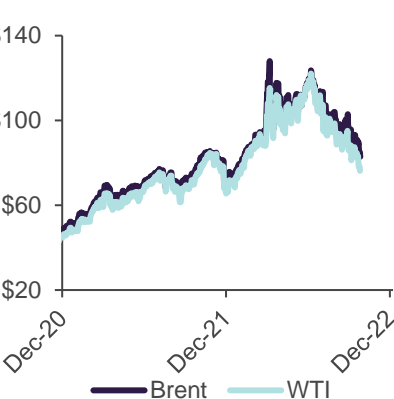
## Inflation (YoY CPI % Change)



**Single family starts:** Single family (SF) homebuilders are giving mixed signals around planned units for 2023 and forecasts vary by market. Some larger track builders dialed back production this fall and are now debating on when to ramp back up in hopes of delivering when mortgage rates are lower or at least more accepted in market. In-fill builders closer to job centers may plan for very little change in production units. A similar theme across all builders is a smaller pool of potential buyers walking through their homes for sale. This is forcing builders to compete through maximizing closing incentives and even considering cutting sales prices as a last resort. Builders now view each sale as a win taken from a competitor vs. the unlimited demand they experienced through most of the pandemic. Its clear the pandemic frenzy is over in most markets. Per NHAB, SF starts are expected to bottom out in 2023 at 886M and then rebound in 2024 to 1.035MM.

**Multifamily:** The US is currently near a record high for multifamily units under construction, but production is expected to slow in 2023 as capital becomes more difficult to procure. Banks approve the size of a construction loan based on the expected free cash flow generated by that property after debt service has been paid. Therefore, when interest rates go up, the projected debt service goes up, and the available loan proceeds go down. The owners will now have to put more money in to each deal making meeting return goals with investors more difficult. The good news is multifamily as a segment continues to be viewed as one of the safest segments of commercial real estate. Institutional capital sources understand this and will continue to invest in the space selectively.

## Brent/WTI Crude Oil Price



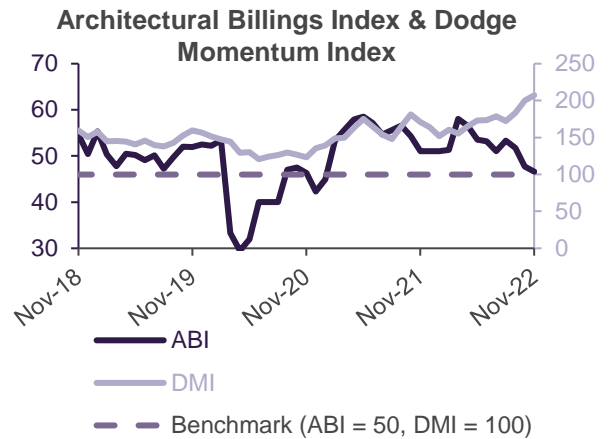
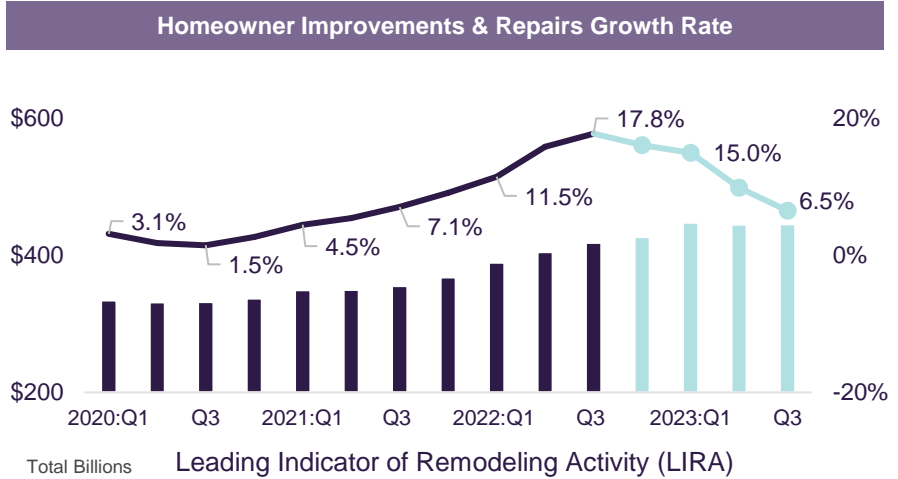
Sources: FRED, Bloomberg, IHS Markit, Brent, WTI, S&P Capital IQ, NAHB, U.S. Census Bureau, U.S. Dept. of Housing and Urban Development, Bankrate

# Building Products market update

Industry Consulting Team | Q4 2022

**Repair and Remodel (R&R):** R&R spending has been stronger than expected the past few months due to strong professional contractor renovation momentum which tends to include larger ticket items. Do-It-Yourself product sales have cooled off but the largest retailers say the flat or marginal growth in this category is still above expectations. R&R growth is likely to moderate in 2023, but high levels of home equity and the fact that roughly 3MM homes built in the early 2000's are now entering prime remodeling years continue to drive strong sales results. According to the Lowes Improvement Pro Pulse survey, roughly 70% of their contractor relationships expect more remodeling work in 2023 than 2022. This is another proof point of resilience of home improvement demand even in an uncertain macro economic environment.

**Non-Residential:** Total non-residential spending has grown 5.2% so far in 2022 and all categories were positive in October. Lodging remains to be the weakest category year to date at -6.6% but is now starting to see some activity as it rebounds off of dramatic lows during the pandemic years. Although not shown below, highway spending was up 14.7% in October, up roughly 7.0% year to date. The Architecture Billings Index (ABI) was negative for the second month in a row down from 47.7 to 46.6 in November. ABI is a forward 12-month projection of future non-residential spending and readings below 50 point indicate a contraction in spending is expected. Backlogs across non-residential contractors remains robust which will likely keep spending trends consistent well in to 2023. Additionally, it is nice to have a strong tailwind from the infrastructure bill which will use many of the same products.



|              | Jan-22       | Feb-22      | Mar-22      | Apr-22      | May-22      | Jun-22      | Jul-22      | Aug-22      | Sep-22       | Oct-22       | 2022 YTD    |
|--------------|--------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|--------------|--------------|-------------|
| Commercial   | 14.1%        | 18.2%       | 13.5%       | 11.3%       | 16.2%       | 21.9%       | 23.0%       | 26.4%       | 25.8%        | 22.5%        | 19.6%       |
| Educational  | -7.1%        | -5.9%       | -4.2%       | -3.4%       | -3.2%       | -0.3%       | 1.2%        | 0.7%        | 2.2%         | 5.1%         | -1.3%       |
| Healthcare   | 0.0%         | 6.6%        | 6.8%        | 4.8%        | 7.5%        | 9.9%        | 9.3%        | 11.4%       | 8.8%         | 7.6%         | 7.3%        |
| Lodging      | -32.0%       | -23.9%      | -22.3%      | -16.6%      | -8.2%       | -1.4%       | 2.3%        | 0.8%        | 1.9%         | 1.2%         | -6.6%       |
| Office       | -5.3%        | -1.3%       | -5.5%       | -2.9%       | -1.7%       | -1.1%       | -0.1%       | 0.8%        | 1.9%         | 1.2%         | -1.3%       |
| <b>Total</b> | <b>-1.9%</b> | <b>2.1%</b> | <b>0.6%</b> | <b>1.0%</b> | <b>3.5%</b> | <b>6.6%</b> | <b>7.7%</b> | <b>9.6%</b> | <b>10.4%</b> | <b>10.3%</b> | <b>5.2%</b> |

Source: U.S. Census Bureau, Truist Securities

**2023 Projections:** We organized data from 48 publicly traded building products companies to see how they are forecasting revenue and EBITDA for 2023. In general, distribution companies are planning for more volatility than manufacturers and heavy materials expects the strongest gain in EBITDA. Lumber related distribution companies face the most headwinds given they are coming off a season of record high prices at lower volumes. The silver lining is earnings appear to be in line or above pre-pandemic performance.

| Average 2023 Projections |                                   |         |        |
|--------------------------|-----------------------------------|---------|--------|
| # of Companies           | Category                          | Revenue | EBITDA |
| 5                        | Domestic Heavy Building Materials | 3.5%    | 6.8%   |
| 20                       | Residential Manufacturers         | -3.9%   | -8.3%  |
| 8                        | Non-Residential Manufacturers     | 1.5%    | 2.0%   |
| 11                       | Specialty Distribution            | -2.9%   | -10.1% |
| 4                        | Lumber Related Distribution       | -17.3%  | -44.1% |

**\*\*Truist Building Products is attending NAHB International Builder Show Jan 31<sup>st</sup> – Feb 2<sup>nd</sup> 2023. See you there!**



(1) Indices are based on surveys that rate market conditions. An index number of 50 or higher indicates a higher share of participants view conditions as good rather than poor.

Sources: Chicago Mercantile Exchange, NAHB, Truist Securities, U.S. Census Bureau, Bureau of Labor Statistics, LIRA