

Industrial Research
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Industrial Distribution

Baird HVAC, Plumbing & PVF Distribution Survey
In partnership with The Wholesaler

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**Please refer to Appendix:
Important Disclosures and Analyst Certification**



Introduction

Welcome to the 3Q14 Baird HVAC, Plumbing & PVF Distribution Survey. Baird’s Industrial Distribution research team is pleased to present the quarterly Baird HVAC, Plumbing & PVF Distribution Survey in partnership with The Wholesaler. Baird and The Wholesaler have partnered on the survey since 2010.

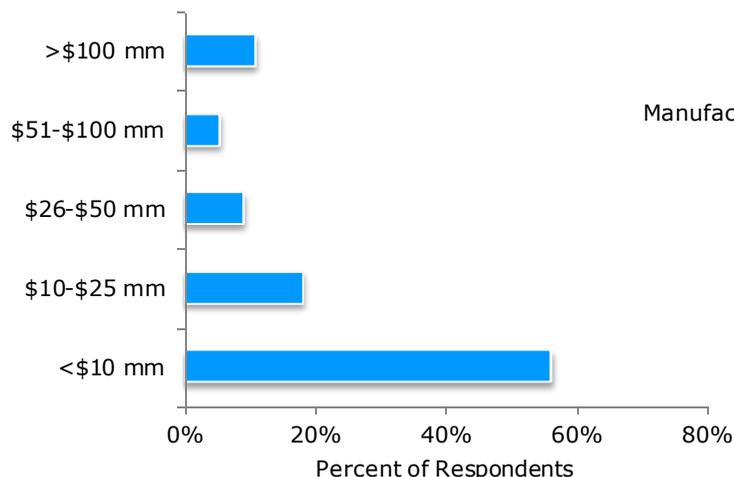
Thank you for participating in this quarter’s survey. The results are meant to provide a general indication of current market trends, and some individual responses have been edited to protect participant anonymity.

Additional information available upon request. Baird’s Industrial Distribution research team also publishes research reports on 17 public distributors, including Watsco (WSO), HD Supply (HDS), MRC Global (MRC) and DistributionNOW (DNO). Please contact us if you are interested in receiving these reports free of charge.

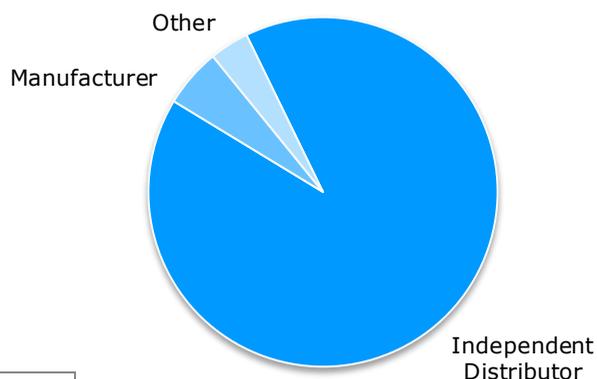
Questions/Comments. Finally, if you have any questions or comments, please feel free to contact Senior Analyst David Manthey (dmanthey@rwbaird.com) or Senior Associate Luke Junk (ljunk@rwbaird.com).

Respondent Profile: 55 respondents, ~\$5 billion aggregate annual revenue

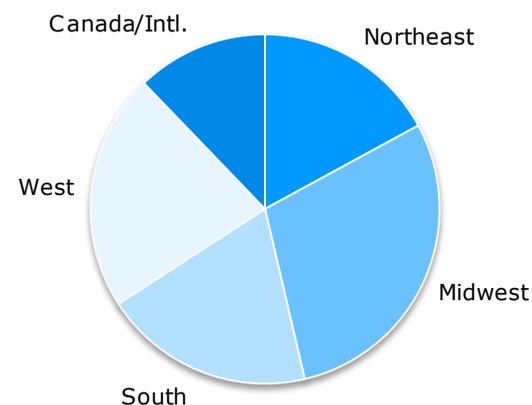
Annual Revenue



Business Model

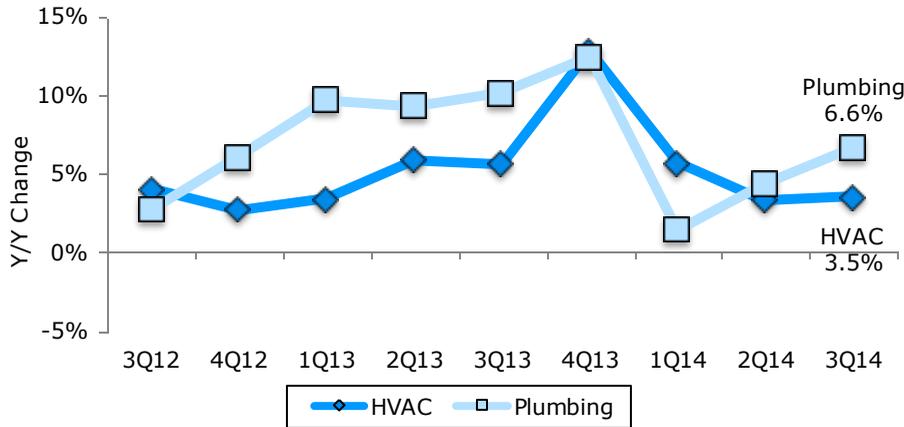


Geographies Served



Current Trends – HVAC/Plumbing

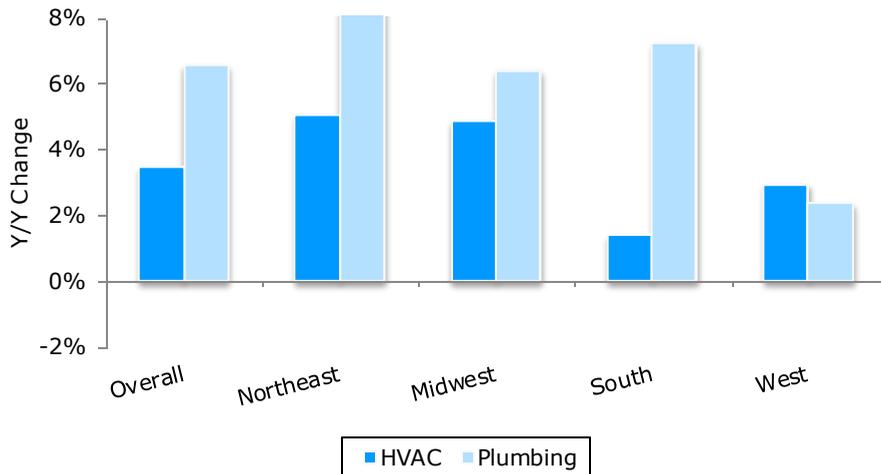
Revenue Trajectory



Respondents indicated that average y/y revenue growth in the third quarter was 6.6% in Plumbing and 3.5% in HVAC. This compares to 4.4% growth across the broader industrial distribution market.

Revenue growth was mixed vs. 2Q14 levels as cool summer weather weighed on HVAC growth. Plumbing sales growth accelerated nicely, however, consistent with moderate growth in new residential construction and remodeling activity through the summer months.

Revenue Growth by Geography

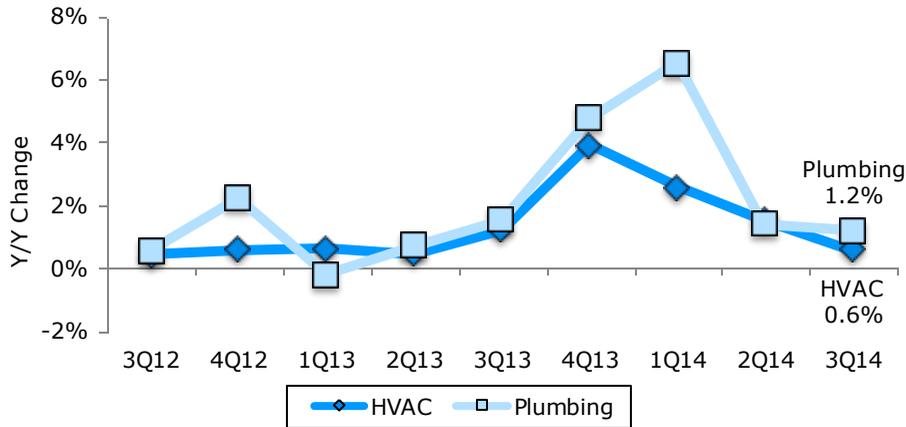


HVAC respondents reported better relative revenue growth in the Northeast and Midwest, roughly in-line growth in the West, and relative weakness in the South, as weather was largely unfavorable ex-Florida.

The Northeast was also relatively stronger for Plumbing respondents, as was the South, with in-line trends seen in the Midwest and weaker trends in the West.

Current Trends – HVAC/Plumbing

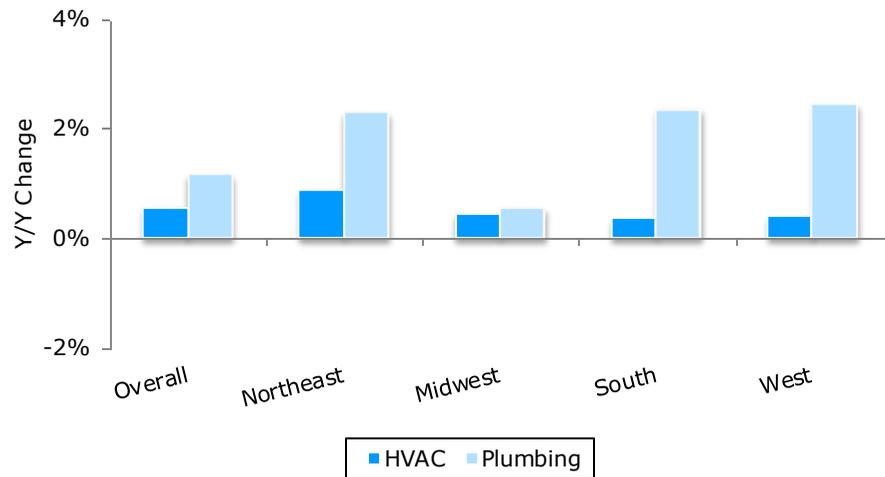
Pricing Trajectory



Respondents indicated that average y/y pricing in the third quarter was +1.2% in Plumbing and +0.6% in HVAC. This compares to +1.1% pricing across the broader industrial distribution market.

Pricing gains decelerated vs. 2Q14 levels for both product categories, although Plumbing was relatively more stable.

Pricing by Geography



HVAC respondents reported better relative pricing in the Northeast, while all other regions were relatively in line with the overall average.

Pricing was strongest in the West, South and Northeast for Plumbing respondents, offset by relatively weaker pricing in the Midwest.

Current Trends – *HVAC/Plumbing*

“Market Snapshot” and Follow-Up Conversation Quotes

HVAC

Revenue Growth

- “The cool weather has not been good for business, everyone is pretty slow. Customers are keeping busy, but not at the pace we’re used to.”
- “Our business was flattish to up slightly during the quarter, it’s been a bit of a struggle. Feedback from our customers is that they were impacted by the cool summer.”
- “Weak weather continued through July/August, but we’ll be up nicely in September.”

Pricing/Margins

- “The most recent intel is that Goodman and Rheem are stock piling 13-SEER inventory, which would argue against them doing anything tricky or self-serving with 14-SEER pricing.”
- “Because it seems like everyone is participating in the 13-SEER build ahead, it will put the industry in position to maintain 14-SEER pricing [at a premium].”
- “Ingersoll Rand’s ERP transition has changed their pricing model, which is a pain.”

Plumbing

Revenue Growth

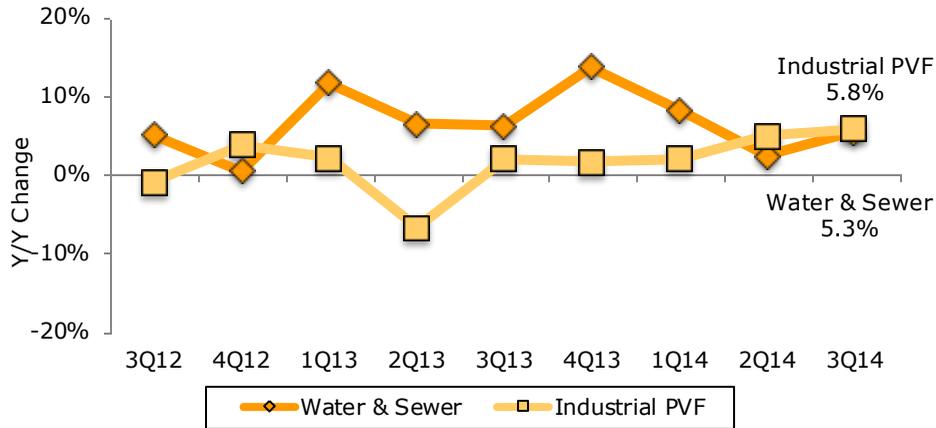
- “The pick up of the economy in the US is helping plumbing.”
- “Remodel markets are growing, economy seems to finally becoming a little more secure.”
- “New construction is more steady now than sporadic. New housing starts are up.”

Pricing/Margins

- “Cost goes up, price goes up.”
- “Very competitive market.”
- “Customers are busier, so they need stuff in a hurry. Some competitors are not raising their pricing.”

Current Trends – *Water & Sewer/Industrial PVF*

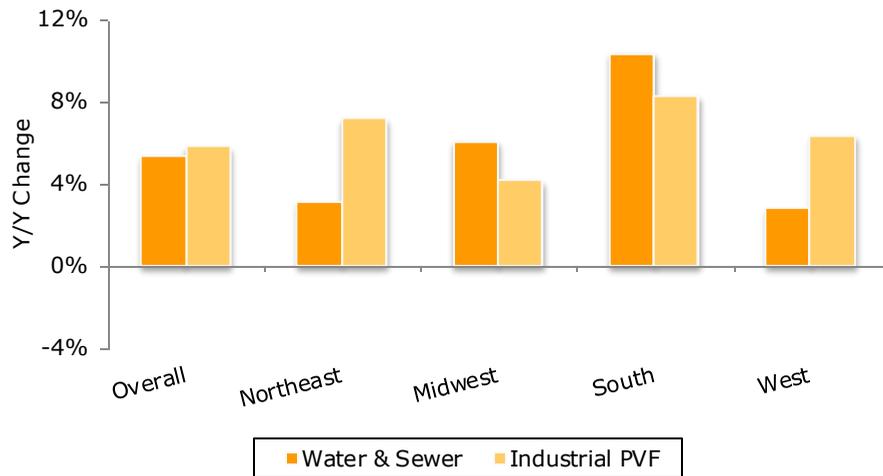
Revenue Trajectory



Respondents indicated that average y/y revenue growth in the third quarter was 5.8% in Industrial PVF and 5.3% in Water & Sewer. This compares to 4.4% growth across the broader industrial distribution market.

Revenue growth accelerated nicely vs. 2Q14 levels, with the relative outperformance in Industrial PVF again benefitting from improved oil & gas trends (especially in Texas).

Revenue Growth by Geography

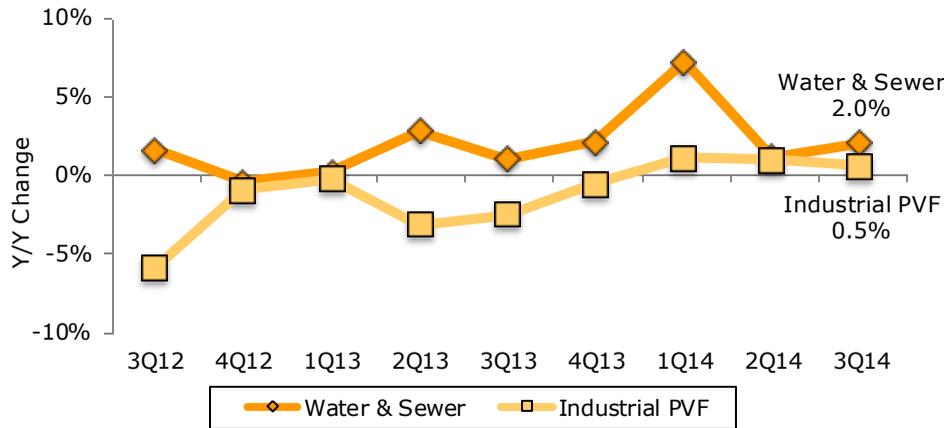


Water & Sewer respondents reported better relative revenue growth in the South, in-line trends in the Midwest, and slightly weaker growth in the Northeast and West.

Turning to Industrial PVF, relative strength was seen in the South (again, benefitting from O&G strength in Texas), Northeast and West, while the Midwest saw somewhat more modest (but still solid) growth.

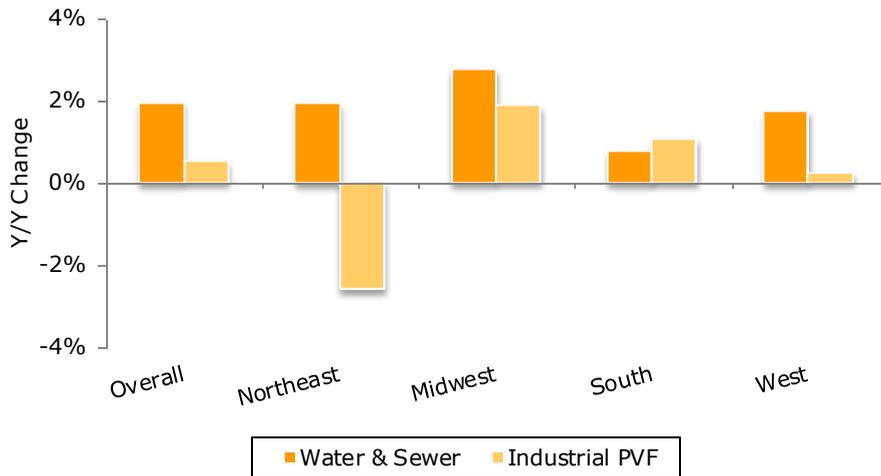
Current Trends – *Water & Sewer/Industrial PVF*

Pricing Trajectory



Respondents indicated that average y/y pricing in the third quarter was +2.0% in Water & Sewer and +0.5% in Industrial PVF. This compares to +1.1% pricing across the broader industrial distribution market. Pricing was mixed sequentially.

Pricing by Geography



Water & Sewer respondents reported better relative pricing in the Midwest, pricing in line with the overall average in the Northeast and West, and more modest gains in the South.

The Midwest was also relatively stronger for Industrial PVF respondents, as was the South, with the West slightly below and the Northeast well below (negative y/y).

Current Trends – *Water & Sewer/Industrial PVF*

“Market Snapshot” and Follow-Up Conversation Quotes

Water & Sewer

Revenue Growth

- “Good sales growth with steady margins.”
- “We see a large increase in our sales in 3Q14. We are not sure if this is going to hold for the rest of the year.”

Pricing/Margins

- “Geo-political concerns on petrol/gas price impacts for many of our primary products. We expect costs increases, and pressure to maintain sales prices (mostly on annual contracts).”
- “Diversification in both market segments and product offering continues to fuel our modest margin growth while strong sales and customer expectations continue to compress margin and increase the cost of doing business.”

Industrial PVF

Revenue Growth

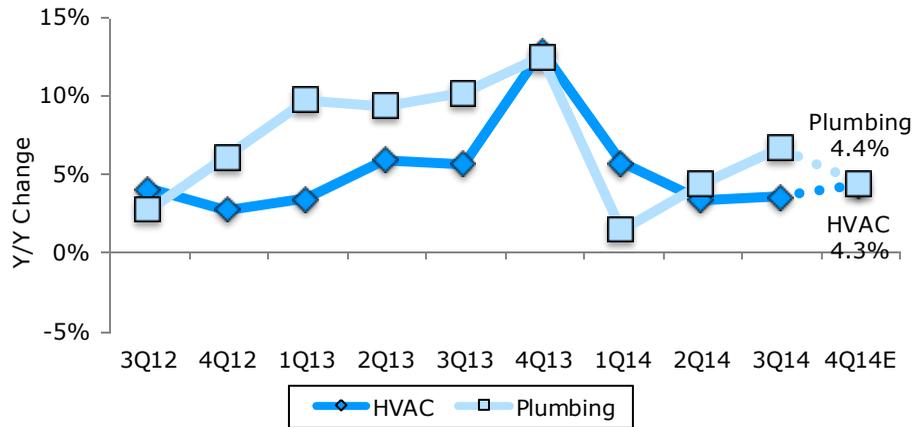
- “We had the largest booking month in the last few years in 3Q, and billings have followed suit – oil & gas has been driving that.”
- “Construction projects continue, MRO still flat.”

Pricing/Margins

- “Continued pressure on pricing as shale players look hard at overall costs. Mills continue to ‘work around’ distribution in some categories of piping products (OCTG, Line Pipe) creating additional margin pressure.”
- “Pricing pressure.”
- “Price pressures are frustrating, as usual!”

Outlook – HVAC/Plumbing

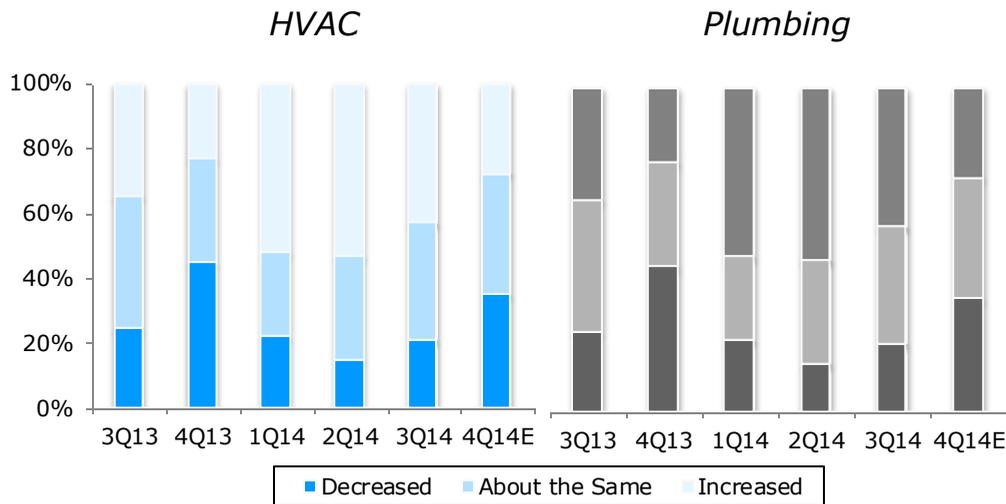
4Q14 Revenue Outlook



Looking forward, survey respondents expect Plumbing revenue growth to decelerate slightly to 4.4% in the fourth quarter, while HVAC growth is expected to come in at 4.3%. This compares favorably to forecast revenue growth of 3.8% across the broader industrial distribution market.

Overall, steadily positive trends in Plumbing appear set to persist, while HVAC trends are expected to benefit as weather headwinds subside following a cool summer.

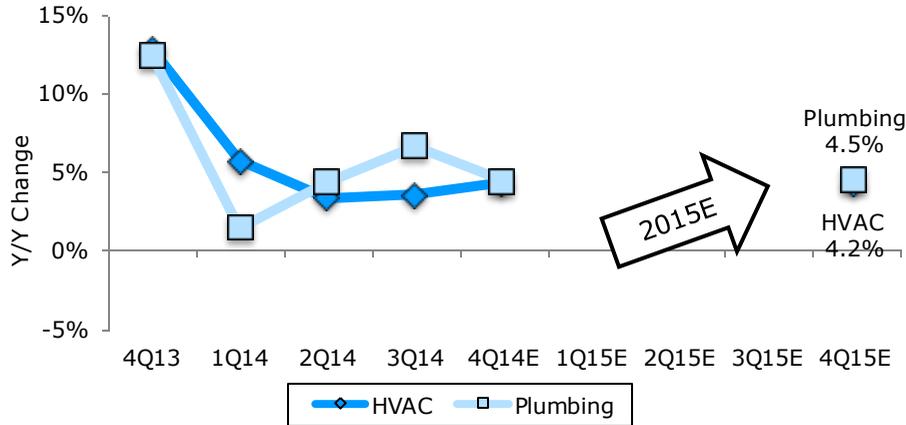
4Q14 Inventory Outlook



HVAC respondents forecast flat to slightly lower inventory levels in the fourth quarter, as 13-SEER pre-build activity in the Sunbelt is somewhat countering normal seasonal patterns. The plumbing outlook is relatively balanced, likely reflecting inventories tied to expected new residential construction activity.

Outlook – HVAC/Plumbing

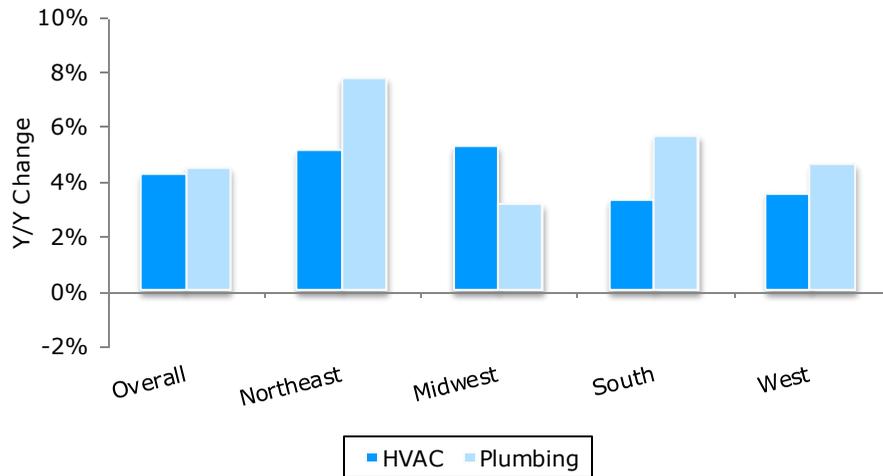
2015 Revenue Outlook



In their initial outlook for the full year 2015, respondents forecast revenue growth of 4.5% in Plumbing and 4.2% in HVAC. This compares to 4.1% expected growth across the broader industrial distribution market.

For 2014 overall (including the 4Q14 forecast), Plumbing and HVAC are both on pace to record growth of just over 4%.

2015 Outlook by Geography



HVAC respondents forecast slightly better revenue growth vs. the overall average in the Midwest and Northeast, with the remaining geographies expected to be slightly below the average.

Plumbing expectations are more varied, however, with relative strength expected in the Northeast and South, in-line growth seen in the West, and somewhat weaker trends in the Midwest.

Outlook – *HVAC/Plumbing*

“Market Snapshot” and Follow-Up Conversation Quotes

HVAC

Business Outlook

- “We think that the general health and climate of the market place continues to increase slightly. With a more normal summer, we’d be very optimistic.”
- “We’re planning on forecasting a little stronger growth next year.”
- “We think the consumer is in relatively good shape, but it’s a fragile economy.”
- “We’re hopeful that better weather equals better demand [going forward].”
- “Saw some pickup in replacement for fall heating early, due to colder than normal winter last year.”

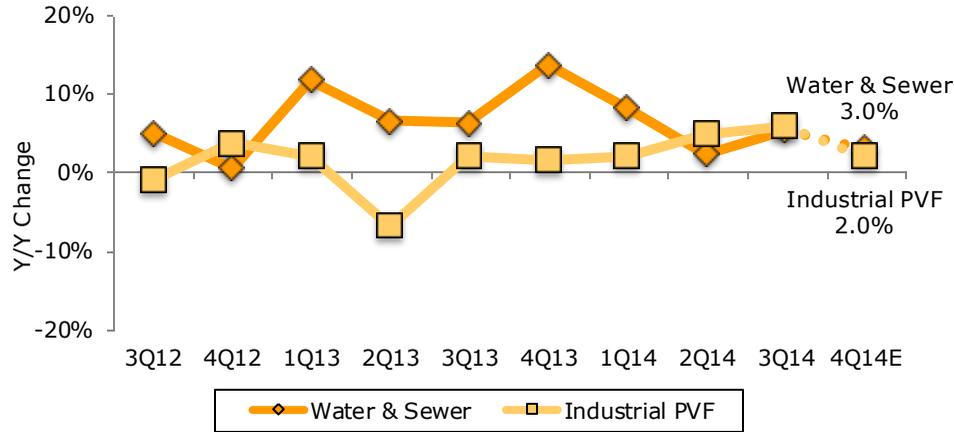
Plumbing

Business Outlook

- “Incremental improvement in the economy seems to be occurring.”
- “The overall business climate is good and expect it to continue through 2016.”
- “Higher demand on big ticket items.”
- “Business is picking up so watching inventory levels closer.”

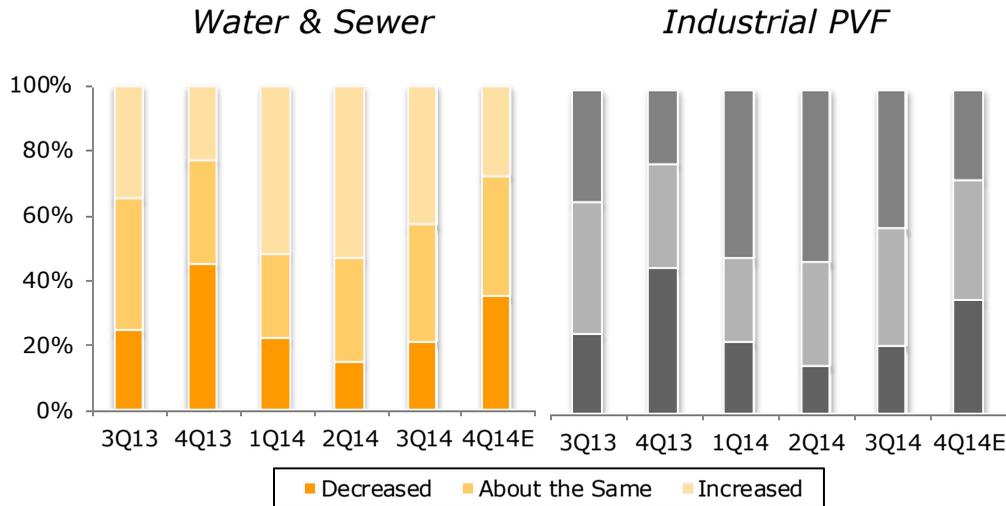
Outlook – *Water & Sewer/Industrial PVF*

4Q14 Revenue Outlook



Looking forward, survey respondents expect Water & Sewer revenue growth to come in slightly lower at 3.0% in the fourth quarter with Industrial PVF similarly seen down q/q at 2.0%. This compares to forecast revenue growth of 3.8% across the broader industrial distribution market.

4Q14 Inventory Outlook

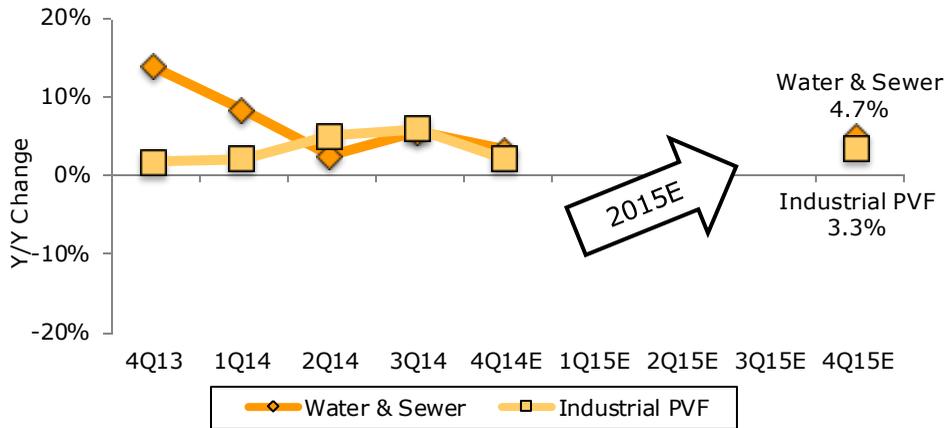


Both Water & Sewer and Industrial PVF respondents forecast net inventory to be flat to lower in the fourth quarter, consistent with normal seasonal patterns.

Compared to the prior year, however, expectations call for slightly less aggressive inventory de-stocking in Industrial PVF.

Outlook – Water & Sewer/Industrial PVF

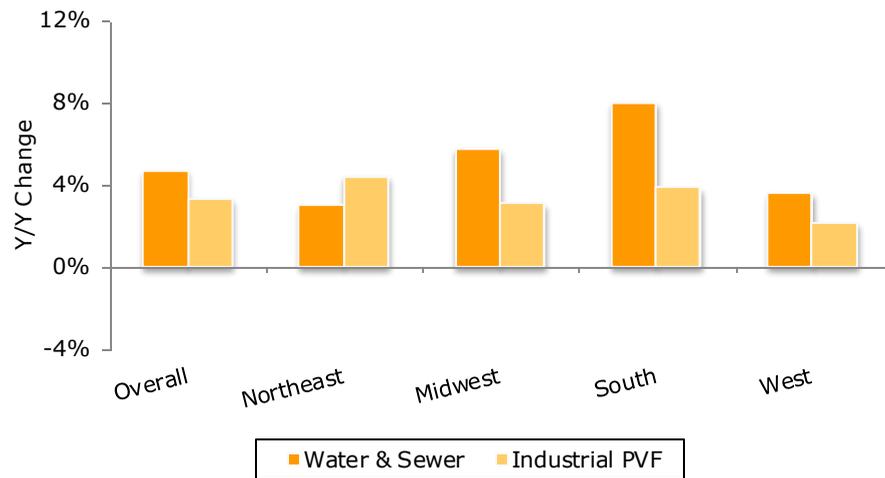
2015 Revenue Outlook



In their initial outlook for the full year 2015, respondents forecast revenue growth of 4.7% in Water & Sewer and 3.3% in Industrial PVF. This brackets 4.1% expected growth across the broader industrial distribution market.

For 2014 overall (including the 4Q14 forecast), Water & Sewer and Industrial PVF are on pace to record growth of 5% and 3.5%, respectively.

2015 Outlook by Geography



Water & Sewer respondents forecast better revenue growth vs. the overall average in the South and Midwest, and slightly weaker growth in the Northeast and West.

Turning to Industrial PVF, growth is expected to be slightly better to in line in the Northeast, South and Midwest, with somewhat more modest growth forecast in the West.

Outlook – *Water & Sewer/Industrial PVF*

“Market Snapshot” and Follow-Up Conversation Quotes

Water & Sewer

Business Outlook

- “EPA & DOE standards changing in the southwest will change my inventory.”
- “Seems to get tougher to compete with the national wholesalers who seem to just want the order, no matter the margins.”
- “The challenges will not change until housing starts increase.”
- “More job buys than usual, and more domestic only job buys than usual.”

Industrial PVF

Business Outlook

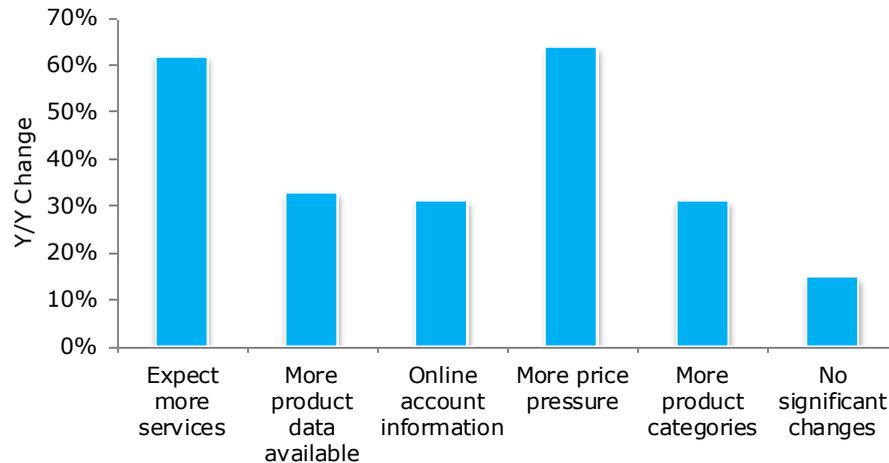
- “Houston will continue to be busy. We are hoping some of our competition will get busy enough to increase sales pricing.”
- “All customers, OEMs, and some competitors say the business environment is great and looking forward to a great 2015. We feel the opposite and look for a flat or small decrease in revenue in the fourth quarter, and possibly going into the first quarter 2015.”
- “Increase in the number of major capital projects.”
- “I would need a crystal ball.”

Rotating Question – Overall

“How have your customers’ expectations of doing business with you changed? Also, how are you adapting your business to meet these new demands?”

Expect more services

- “Increasing employee count when qualified individuals are available.”
- “Trying to do more without adding more cost.”
- “More sales people on the road.”
- “Promoting value provided by us in conjunction with greater service expectations.”



More product data available

- “Help out with websites to access information.”
- “We have installed new servers, so that our customers can get the information they need, when they need it.”

Online account information

- “Purchasing a new ERP system.”
- “Trying to keep up with technology and mobile applications.”
- “Trying to be ahead of the curve technically.”

More price pressure

- “Need to keep pricing competitive.”
- “Change product sales mix to increase margins.”
- “Optimizing pricing with discount packages.”
- “Dealing with major manufacturers on pricing and availability a lot more.”

More product categories

- “Looking at additional product categories.”
- “Bringing in more product lines.”
- “More breath of product.”
- “Adding product lines and expanding other lines.”

Appendix: Overall Survey Results

Trends by Product Line

	3Q14 Revenue Growth	3Q14 Pricing	4Q14 Forecast	2015 Forecast	Robert W. Baird & Co. Commentary
Hoses & Accessories	6.5%	1.0%	5.1%	6.9%	Highest 2015 revenue growth forecast in the survey
Cutting Tools	4.5%	1.6%	5.8%	6.5%	Trends at machine shop customers remain healthy
Datacomm	7.4%	1.3%	5.5%	6.1%	Continued shift to larger data centers a longer-term secular negative
Pool & Spa	3.2%	0.6%	3.5%	6.0%	Positive industry trends partially offset by cool summer in Snowbelt
Fasteners	2.7%	0.6%	2.9%	4.7%	Import prices out of Taiwan have risen slightly
Welding Hardgoods	3.4%	1.6%	3.8%	4.7%	Metal fab trends remain strong, driving improved consumables
PVF - Water & Sewer	5.3%	2.0%	3.0%	4.7%	Geo-political concerns could weigh on pricing
Plumbing	6.6%	1.2%	4.4%	4.5%	Competitive chatter remains high
HVAC	3.5%	0.6%	4.3%	4.2%	Cool summer weighs on industry growth, heavy 13-SEER pre-build
Electrical	4.8%	1.1%	4.9%	4.2%	Non-residential construction recovery expected to accelerate in 2015
General Industrial (MRO)	3.7%	1.3%	3.8%	4.1%	Improved industrial momentum sustained
Overall	4.4%	1.1%	3.8%	4.1%	
Roofing	1.8%	-0.3%	-0.6%	4.1%	Shingle pricing pressure increases (spotty demand/high inventory)
Gases & Cylinder Rental	3.0%	2.4%	3.4%	4.0%	Argon supply issues surface, as expected
Mechanical/Power Transmission	3.4%	1.1%	3.4%	3.6%	Second quarter of 3%+ growth following six flat-to-negative quarters
Safety	4.9%	1.6%	2.7%	3.6%	National distributors pushing the (purchasing) advantage
PVF - Industrial & Energy	5.8%	0.5%	2.0%	3.3%	Oil & gas resurgence continues, but margins coming under pressure
Building Materials	1.4%	0.3%	2.8%	2.8%	Pricing closer to flattish despite higher lumber prices
Facilities Maintenance (MRO)	3.1%	1.4%	2.6%	2.6%	Overall industry momentum remains positive
Rental Equipment	1.9%	2.0%	0.4%	0.8%	Higher capex may be leading to lower rental welder demand

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