While the first decade of the 21st century was a dark and bleak time for the American furniture industry—a deadly combination of the domestic economic meltdown, the competitive onslaught of offshore manufacturing and shrinking demand—there now seems to be a glimmer of hope for the furniture industry. Although not yet effusive about the future, economists and furniture insiders have begun to loosen the death grip on projections and forecasts. Unfortunately, this optimism comes too late for the legions of manufacturers and retailers who couldn’t weather the economic storm and were forced into bankruptcy and liquidation.

In August 2013, Furniture Brands International—one of the largest residential furniture makers in the United States, representing the Broyhill, Thomasville, Drexel Heritage, Lane, Hickory, La Barge, Lane Venture, Maitland-Smith, Pearson and Henredon brands—voluntarily delisted its stock from the New York Stock Exchange because its market capitalization had fallen below the NYSE’s listing requirement. In early September, the company filed for Chapter 11 bankruptcy protection. The future of the company, including opportunities for restructuring, will remain to be seen. The sale of the business seems inevitable, although the possibility that not all individual brands represented by Furniture Brands will be purchased by the same suitor is a real one. One thing is for sure – this situation will create competitive advantages for other industry players, at least in the short term.

Furniture Brands isn't the only company feeling the pressure. During the near-catastrophic period from 2002 to 2009, virtually all aspects of the industry changed. From consumer trends to technology to sourcing to energy, manufacturers were forced to reinvent themselves—as well as their products and processes—to cope with the new and emerging structure.

Many manufacturers—previously lulled into complacency by decades of the status quo—were not able to successfully embrace the change necessary to compete, and simply closed shop. While this exodus has reduced competition in certain market segments, staying solvent in the furniture industry is not for the faint hearted.

In response to the recession—and to projections that the economy is on a trajectory of recovery—the industry is changing. Upholstery manufacturing has changed; conventional wood manufacturing has virtually disappeared; some retail channels are gone, while others have emerged; and previously neglected areas like furniture technology, information systems, logistics, and global sourcing have become essential. In addition, consumer trends and preferences will be a factor in driving manufacturing into the future.

The purpose of this industry watch report is to get a good fix on the current state of the industry and to project from that some semblance of what we might expect in the future.

With labor costs on the rise, manufacturing in China may not be the most cost-effective option for U.S. furniture manufacturers.

Momentum in the U.S. housing market will continue to impact furniture manufacturing—both positively and negatively.
Significant findings continued

Consumer preferences are changing dramatically as the Baby Boomers exit and a younger generation enters the market.

Consumers control retail distribution channels, even as manufacturers try to dictate how furniture buying is done.

While quality is critical, it is no longer the most important variable in the manufacturing process. Technology, logistical efficiencies and agility are growing in importance.

For those willing to invest the time and effort, export markets may be opening up.

Inadequate marketing and branding continues to plague the industry, especially in the areas of new media.

A Snapshot of American Furniture Manufacturing

In many respects, the furniture industry is much stronger in 2013 than it was in 2009. Although most manufacturing has remained overseas, many furniture companies have seen consistent increases in sales and profits during this period. In 2012, furniture imports rose 9%. This is a trend that is expected to continue as Russia, India and Eastern Europe enter the import market.

The industry as a whole has seen great improvements over the past few years. After a 13% drop in sales in 2009, new orders have increased 4-6% every year. As of 2012, orders were up 16.5% from 2009 and up 1.38% from 2008. This steady increase is expected to continue in the coming years.

<table>
<thead>
<tr>
<th>Month</th>
<th>2008 Orders</th>
<th>2009 Orders</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>February 2010</td>
<td>$21,619 M</td>
<td>$18,816 M</td>
<td>$2,803 M decrease</td>
</tr>
<tr>
<td>February 2011</td>
<td>$18,816 M</td>
<td>$19,582 M</td>
<td>$776 M increase</td>
</tr>
<tr>
<td>February 2012</td>
<td>$19,582 M</td>
<td>$21,145 M</td>
<td>$1,563 M increase</td>
</tr>
<tr>
<td>February 2013</td>
<td>$21,145 M</td>
<td>$21,918 M</td>
<td>$773 M increase</td>
</tr>
<tr>
<td>2012 V 2009</td>
<td>$18,816 M</td>
<td>$21,918 M</td>
<td>$3,102 M increase (16.5% increase)</td>
</tr>
<tr>
<td>2012 V 2008 (peak)</td>
<td>$21,619 M</td>
<td>$21,918 M</td>
<td>$299 M increase (1.38% increase)</td>
</tr>
</tbody>
</table>

Source: Smith Leonard
### Public Companies Sales and Net Profits for the Most Recent Period

#### (in % vs. Prior Period a Year Ago)

<table>
<thead>
<tr>
<th>Furniture Manufacturers</th>
<th>Sales (in millions)</th>
<th>% Change</th>
<th>Net Profit (in millions)</th>
<th>% Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bassett*</td>
<td>$253.21</td>
<td>$296.67</td>
<td>6.50%</td>
<td>$55.34</td>
</tr>
<tr>
<td>Chromcraft-Revington*</td>
<td>$55.23</td>
<td>$56.64</td>
<td>2.65%</td>
<td>($4.36)</td>
</tr>
<tr>
<td>Ethan Allen</td>
<td>$729.37</td>
<td>$729.08</td>
<td>0.04%</td>
<td>$49.69</td>
</tr>
<tr>
<td>Flexsteel</td>
<td>$352.09</td>
<td>$386.19</td>
<td>9.69%</td>
<td>$13.07</td>
</tr>
<tr>
<td>Furniture Brands*</td>
<td>$1,110.00</td>
<td>$1,000.70</td>
<td>-9.85%</td>
<td>($43.75)</td>
</tr>
<tr>
<td>Hooker</td>
<td>$222.51</td>
<td>$218.36</td>
<td>-1.86%</td>
<td>$5.06</td>
</tr>
<tr>
<td>La-Z-Boy</td>
<td>$1,231.68</td>
<td>$1,332.53</td>
<td>8.19%</td>
<td>$88.91</td>
</tr>
<tr>
<td>Stanley*</td>
<td>$104.65</td>
<td>$98.57</td>
<td>-5.81%</td>
<td>($5.03)</td>
</tr>
</tbody>
</table>

*2012 compared to 2011

Currently, the largest 50 retail companies in the furniture industry generate 40% of the income. The top 10 retail stores are listed below. Many of these companies sell furniture at a relatively low price point of $500 to $1,500.

### Top 10 Retail Stores

- Ashley Furniture
- Ikea
- Rooms To Go
- Berkshire Hathaway
- Williams-Sonoma (Pottery Barn and West Elm)
- American Signature
- Raymour & Flanigan
- Pier 1 Imports
- La-Z-Boy
- Sleepy’s

*Source: Furniture Today*

Although overseas manufacturing has provided significant cost benefits, manufacturers are rethinking whether to stay. There are several emerging problems with manufacturing in China and other far east countries. First, labor costs are rising, with wages increasing 15-20% a year. Second, trans-Atlantic shipping rates are going up. Furniture has always been expensive to ship due to its size and weight, but rising oil prices and a slowdown in shipbuilding have pushed shipping costs up by 71% in the past four years. Third, currency challenges exist when dealing with the Thai Bhat, Vietnamese Dong, Chinese Yuan, and others. The appreciation of the Yuan continues to cut into profits, further decreasing the benefits realized in the past. Lastly, a supply chain that reaches half way around the world is fraught with challenges, including quality control, supply disruptions, language barriers and many others.
In 2011, CNN Money published an Accenture report which claims that “61% of manufacturing executives surveyed said they were considering matching supply location with demand by re-shoring manufacturing and supply.” While the survey was not limited to the furniture industry, furniture manufacturers are doing more than considering their options, they are taking action by bringing their manufacturing back to the U.S.

One example is Lincolnton Furniture. After making the move to overseas production, Lincolnton found that their customers preferred to buy USA goods. This led them to complete a $5 million renovation on the old family plant in Lincolnton, NC and hire 130 workers—many of whom had worked for the company before their move offshore. Lincolnton Furniture produces mid- to high-end furniture.

The Boston Consulting Group recently reported that U.S. firms—including furniture manufacturers—will see a “tipping point” in offshore manufacturing by around 2015, when China’s shrinking cost advantage will prompt companies to rethink where they produce certain goods meant for sale in North America. In many cases, manufacturing in some parts of the U.S. and Mexico will be just as economical as manufacturing in China.

With its wages lower than China and its proximity to the U.S., Mexico has the potential to become a major source for U.S. furniture manufacturing for less-expensive home furnishings. Goods can reach the U.S. in a fraction of the time needed to ship furniture from China, and they can enter the U.S. duty-free, thanks to the North American Free Trade Agreement. However, due to quality concerns, high-end products will likely continue to be manufactured in the U.S.

The Boston Consulting Group report also states that furniture production is among seven sectors that could create 2 to 3 million jobs as a result of manufacturing returning to the U.S. over the next five years. Obviously the furniture industry has the potential to play a large role in a U.S. manufacturing-based economic recovery.

<table>
<thead>
<tr>
<th>Rank Last Year</th>
<th>Rank</th>
<th>Company</th>
<th>Estimated U.S. Furniture Shipments in $ millions</th>
<th>Percent Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>2011</td>
<td>2012</td>
<td>Company</td>
<td>2011</td>
<td>2012</td>
</tr>
<tr>
<td>1</td>
<td>1</td>
<td>Ashley Furniture Inds.</td>
<td>$3,338.3</td>
<td>$3,032.0</td>
</tr>
<tr>
<td></td>
<td></td>
<td>U.S. sales accounted for 95% of shipments each year. Excludes sales of company-owned retail stores. Total 2011 revenues, $3,514 million.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2</td>
<td>3</td>
<td>La-Z-Boy</td>
<td>$975.0</td>
<td>$919.0</td>
</tr>
<tr>
<td>3</td>
<td>2</td>
<td>Furniture Brands Int’l</td>
<td>$932.9</td>
<td>$981.9</td>
</tr>
<tr>
<td></td>
<td></td>
<td>U.S. sales accounted for an estimated 97% of shipments each year. Excludes sales of company-owned retail stores. Total 2011 revenues, $1,107.7 million.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Rank</td>
<td>Company</td>
<td>Estimated U.S Furniture Shipments in $ millions</td>
<td>2011</td>
<td>2012</td>
</tr>
<tr>
<td>------</td>
<td>--------------------------------</td>
<td>-----------------------------------------------</td>
<td>------</td>
<td>------</td>
</tr>
<tr>
<td>4</td>
<td>Klaussner Furniture Inds.</td>
<td>$490.0</td>
<td>$490.0</td>
<td>0.0%</td>
</tr>
<tr>
<td>5</td>
<td>Dorel*</td>
<td>$450.5</td>
<td>$442.7</td>
<td>1.8%</td>
</tr>
<tr>
<td>6</td>
<td>Sauder Woodworking</td>
<td>$430.0</td>
<td>$430.0</td>
<td>0.0%</td>
</tr>
<tr>
<td>7</td>
<td>Lacquer Craft</td>
<td>$376.9</td>
<td>$397.9</td>
<td>-5.3%</td>
</tr>
<tr>
<td>8</td>
<td>Ethan Allen*</td>
<td>$344.8</td>
<td>$322.3</td>
<td>7.0%</td>
</tr>
<tr>
<td>9</td>
<td>Flexsteel Inds.</td>
<td>$308.3</td>
<td>$306.7</td>
<td>0.5%</td>
</tr>
<tr>
<td>10</td>
<td>Man Wah Holdings</td>
<td>$276.9</td>
<td>$258.4</td>
<td>7.2%</td>
</tr>
<tr>
<td>11</td>
<td>Bernhardt</td>
<td>$274.0</td>
<td>$249.0</td>
<td>10.0%</td>
</tr>
<tr>
<td>12</td>
<td>L &amp; P Consumer Products Unit</td>
<td>$242.2</td>
<td>$219.8</td>
<td>10.2%</td>
</tr>
<tr>
<td>13</td>
<td>Lexington Home Brands*</td>
<td>$236.9</td>
<td>$209.6</td>
<td>13.0%</td>
</tr>
<tr>
<td>14</td>
<td>Hooker Furniture</td>
<td>$213.6</td>
<td>$204.7</td>
<td>4.4%</td>
</tr>
<tr>
<td>15</td>
<td>Home Meridian International*</td>
<td>$212.9</td>
<td>$188.1</td>
<td>13.2%</td>
</tr>
<tr>
<td>16</td>
<td>Best Home Furnishings</td>
<td>$195.6</td>
<td>$182.7</td>
<td>7.0%</td>
</tr>
<tr>
<td>17</td>
<td>Franklin*</td>
<td>$190.1</td>
<td>$186.1</td>
<td>2.1%</td>
</tr>
</tbody>
</table>

U.S. sales accounted for 98% of shipments each year. Total 2011 revenues, $500 million.

U.S. sales estimated at 75% of shipments each year. Total 2011 revenues, $2,364.2 million.

U.S. sales accounted for 95% of shipments each year. Total 2011 revenues, $453 million.


U.S. sales accounted for 96.5% of shipments each year. Total 2011 revenues, $284 million.

Includes shipments of finished product only, including contract shipments of $9.65 million in 2011 and $10 million in 2010. Shipments of components by parent Leggett & Platt are not included. U.S. sales accounted for 97% of shipments each year. Total 2011 revenues, $3,636 million.

U.S. sales accounted for 93% of shipments each year. Total 2011 revenues, $255 million.


U.S. sales accounted for 99% of shipments each year. Total 2011 revenues, $215 million.

U.S. sales accounted for 93% of shipments each year. Total 2011 revenues, $210.3 million.

U.S. sales accounted for 99% of shipments each year. Total 2011 revenues, $192 million.
Growth in home sales in 2012 reached about 26% for new homes and 9% for existing homes. As of July 2013, new home sales were up 29% and existing homes up 7%. However, this trend did not extend into furniture sales.

Home furnishings sales started strong in 2012, but the year ended with a disappointingly weak fourth quarter. This weakness continued into the early months of 2013, but projections indicate that sales should accelerate by year’s end.

Furniture Today reports that, by 2015 and 2016, homebuilding and sales should be back to pre-recession levels, as well as measurable increases in consumers’ disposable income. This could translate into increased interest in new furniture purchases.

If stock prices are any indicator of industry health, there may be reason to celebrate. Since 2012, furniture stocks are up an average of 29.1%.

As the Baby Boomers aged, they were expected to buy a lot of furniture. Instead, they shunned elaborate purchases of home furnishings. Even the most conspicuous consumers, after spending extravagantly on oversized homes, showed little interest in fine furniture. Instead, they furnished their million dollar homes with $599 sofas—or nothing at all. Many McMansions featured rooms completely devoid of furniture. When they did buy furniture, they often selected inexpensive ‘disposable’ items from stores like IKEA, Rooms To Go or Pottery Barn.

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**U.S. Housing Market: Furniture Boom or Furniture Bust?**

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**Consumer Trends Drive Design and Manufacturing**

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Sweeping changes to new-home floor plans are also having an impact on furniture manufacturing. Many new houses now feature built-in cabinets and walk-in closets with enough storage room to eliminate the need for dressers and chests. Similarly, armoire-style entertainment centers are no longer popular, thanks to wall-mounted flat-screen televisions and smaller television stands that require far less floor space.

According to *Multifamily Executive*, as of 2013, the average apartment size is 982 square feet—and shrinking. Property developers are reducing the size of apartments in their new construction complexes. Micro apartments are also showing up in metropolitan areas, where space is always at a premium. Particularly among the 20 to 35 age group, this translates into the need for less—and smaller—furniture.

Another style trend affecting furniture manufacturing is a growing interest for increased function and storage. As the square footage of new apartments has decreased, new-home floor plans have transitioned to include more multi-purpose rooms—less distinction between kitchens, living rooms and dining rooms—forcing manufacturers to rethink, redesign and retool to address the need for multi-purpose furniture.

Furthermore, a deep and growing concern for the environment among consumers has led to an interest in used furniture. In the past decade, there has been resurgence in “retro” mid-century modern furniture. This interest in recycled furniture has led to a trend called “shabby chic,” which has infused perceived value into furniture that might otherwise have been discarded and replaced. Among the emerging younger market—consumers who may be purchasing their first home or condominium, or renting their first apartment—this interest in vintage furniture circumvents the manufacturing process, as consumers opt to forego the purchase of new furniture.

There are other implications of the eco-friendly movement as well. Consumers are beginning to question the processes used in manufacturing, demanding that manufacturers reduce overall waste and energy usage related to the manufacturing process. While these shifts may actually create long-term cost savings for manufacturers, the cost to implement such changes in processes are often costly in the short term.

In addition, consumer trends show growing demand for construction materials that are reclaimed, recycled, sustainable and environmentally safe. The costs associated with sourcing such materials directly affect margins, as consumers are only willing to offset the additional expense to a small degree at retail.

In essence, the furniture industry faces a consumer audience composed of people who are largely indifferent to the category and unwilling to spend much on it, but often expect a product that meets certain specialized guidelines. This situation is nothing new to the mass-market segment, but in the upper-end, the impact has been severe. Amazingly, no one seems to be doing any market research on consumer shopping patterns, so efforts to market the products are based on guess-work and usually resort to price discounting, which has limited appeal.
Consumers Dictate Distribution Channels

By its nature, furniture is a space-eater requiring large retail footprints and warehouses. This means high fixed costs. Furniture is hard to handle as it goes from the factory packing room to a container, to a truck or rail car, to a port, to another port, to another truck, to a warehouse, to a delivery truck, to a consumer’s home. This means high variable costs. Together, it means the consumer pays at least twice as much as the material, labor and overhead cost of the product when it was packed.

While many furniture manufacturers have tried and failed, a select few have found success in establishing and operating their own retail networks—most notably, Ethan Allen, La-Z-Boy and Ashley. However, they are the exceptions. The past decade is littered with manufacturers who expected customers to flock to their brick-and-mortar retail stores, only to find that consumer shopping patterns didn’t support this change.

Big Box retailers—like Costco and Sam’s Club—have tried unsuccessfully to capture market share. Likewise, department stores—like Macy’s and JC Penney—who once enjoyed thriving furniture sales, are no longer seeing furniture as a profitable product line. The upper-end purveyors, the ‘carriage trade’ stores, have disappeared, but interior designers remain a factor. Regional chains come and go and national chains never seem to find lasting success. Hybrids, like Crate & Barrel and Room & Board, combine ‘bricks’ and ‘clicks’ with great looking catalogs to capture the so-called ‘lifestyle’ category.

And while the Internet has become a great resource for consumers and retailers alike, consumers continue to resist purchasing furniture from a website. The desire to touch and feel a piece of furniture before buying it will continue to prevent a paradigm shift in this retail channel.

Product Drives Sales … Or Does It?

Furniture insiders have long claimed that the product itself is the key determinant of sales. During the shopping process, consumers—largely female—quickly dismiss the items they do not want and respond favorably to those that reflect their self image. No amount of marketing or selling can change this. Others—largely male—have insisted that most of the product looks the same anyway (“It’s just a sea of brown.”), so more attention should be paid to non-product variables.

Without question, the product is still king. The ‘over the top’ styling of the pre-meltdown period has been toned down somewhat, partially as a way to reduce cost. However, dependence on product while neglecting other variables can no longer be tolerated. Logistical expertise, the use of information technology and efforts to become more eco-friendly are becoming the new keys to differentiation. It’s rare that customers seek out Ethan Allen or Ashley because of their product styling, yet both brands have outperformed the field. Their differentiator is customer service.

Traditionally, the industry has not been known for exemplary customer service. Unreliable suppliers, erratic factory schedules and supply chain glitches have been blamed for many a delayed delivery to the customer. Those manufacturers who upgrade their automation and processes—and who better manage their supply chain—will be the ones with the competitive advantage in the future.
In the meantime, the new product development process is badly in need of streamlining. Fraught with waste, the old process is costly and slow. Worse still, the results are only occasionally successful. It has been estimated that less than one third of new wood product introductions actually make it into production, and only half of those retail well. Predicting winners may be an art, but the development process can be rationalized much more effectively. The idea of testing new product has always met with resistance, and only spot usage of this technique has been made.

Design piracy continues to be a real problem. Prior to the globalization of furniture, producers could keep new designs under wraps in their factories until the products were shown at market. The ‘knock-off artists’ could then copy them or wait to see if they sell at retail before doing so. Now, because Asian producers are pleased to show what they produce for their other customers, it’s not difficult to see prototypes in Asia before they get to market.

This blatant practice of copying is often encouraged by retailers, but it only serves to confuse the consumer and lead to a sameness of design offerings. Most of all, it hurts the innovative companies that invest in fresh designs needed to attract new consumers and generate sales growth. The only way for the innovators to cope with this is by staying ahead of the imitators and improving their speed to market. This can be accomplished by rationalizing the new product development process, yet scant attention has been given to this concept.

Historically, American furniture producers have considered the export market to be a waste of time, and made only token attempts to develop international sales. They had enough domestic business to keep their plants running, and the export business was tricky. American manufacturers were not comfortable dealing with currency fluctuations, style and size differences, language issues, oceangoing freight procedures and cultural idiosyncrasies. They lacked the patience required to build export sales.

Likewise, when it came to importing component parts and finished goods, the same indifference was in evidence. They paid lip service to the need to be a global organization and looked for reasons to justify the lack of imports. The easiest culprits were quality and delivery reliability, but in truth, the American factories had their own problems with these issues.

This hesitation has decreased in the past few years. Several emerging markets have made the export business more appealing. The rising middle classes in China, India and Brazil have created a market for more high-end furniture, offering new markets to those manufacturers willing to spend the time and energy to address the challenges. In addition, Canada, Mexico, Japan and the UK represent growing export markets for the furniture industry.
Furniture companies’ marketing has traditionally been weak. Leaders in the industry have long been reluctant to research consumer preferences or to try to improve the customer experience. Even dire circumstances have not induced furniture companies to try to learn from other consumer goods sectors.

Furniture executives would do well to study the fashion industry, and to learn why women will pay $500 for a simple black dress when they can get a similar garment for $100 or less. The answer, of course, is branding. The company that can sell the dress for $500 has created a perception in the consumer’s mind of what the label stands for. The company has found a way to add value to a product. It is not a weakness for furniture executives to study the marketing of Fortune 500 companies to learn new marketing techniques for their own brands.

Given the choice between investing in marketing or declaring bankruptcy, many furniture companies have begrudgingly opted for the less painful choice of implementing a marketing plan. However, many have done this with an ‘advertising campaign’ or ‘new product line promotion’ mindset instead of a comprehensive strategic marketing mindset. The most popular marketing channels remain catalogs, direct mail and TV ads. Trade shows, such as the High Point Furniture Market, also continue to be important in creating a presence with buyers. But a brand simply cannot be built at a trade show (although some manufacturers appear to think otherwise).

Brand builders must now step out of the box and fully embrace nontraditional methods of promotion. Mobile device advertising, highly targeted web advertising, guerilla marketing tactics, and social media network integration to generate word-of-mouth promotion are all keys to increasing awareness and building brand loyalty.

A furniture company that ignores branding is little more than a provider of contract or private-label furniture. Their margins will be squeezed and many will go out of business. However, those that understand branding and its importance to their long-term survival will benefit greatly. And those that develop a brand that stands for something in the consumer’s mind will be the ultimate winners. Just consider the strength of such branding champions as Polo, Nautica, Levi, Timberland, Allen Edmond, Wedgewood, IZOD, Nike, La-Z-Boy and Ethan Allen.
Conclusion

With so much transformation happening in the furniture industry, there will be endless opportunities for companies to increase market share—IF they approach the task with ingenuity, vision, creativity and patience. As difficult as the last decade has been for furniture, the long-awaited ‘recovery’ may not be any easier, but it certainly will be exciting.

Automation will offer opportunities for manufacturers to increase efficiency, and therefore their profit margins. However, not every process can be automated. For example, short runs and automation don’t mix. Also, mass producing case goods opens the door to problems with consistency, while many consumer preferences—particularly in upholstery—change too frequently for manufacturers to create efficiencies.

Further opportunities will exist for acquisition and consolidation in the market, affording new opportunities to affect market share. Only the players who can be nimble and are willing to embrace change—not something the industry is historically known for—will reap the rewards.

This report was produced by Anderson Bauman Tourtellot Vos (ABTV), a turnaround management firm headquartered in Greensboro, NC. For questions or more information about this report, contact:

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