

The U.S. Furniture Industry: Yesterday and Today ... Will There Be a Tomorrow?

This is the first installment in a two-part series

> By Al Schuler & Steve Lawser

In the United States, furniture and related manufacturing (including kitchen cabinets) is currently concentrated in three geographic locations: the Midwest (Michigan, Indiana, Ohio, Wisconsin, Illinois), the South (North Carolina, Mississippi, Virginia) and the Southwest (California, New Mexico, Texas).

The U.S. furniture industry started out in the Northeast (New York, Pennsylvania and New England), then moved to the Midwest, and then the South. Each move was essentially a move to a region with cheaper manufacturing costs and an ample supply of good quality hardwood lumber. This sort of "manufacturing capacity migration" happens in most industries, both in North America and offshore. Today, the top 12 producing states manufacture about two-thirds of the furniture and kitchen cabinets produced in the United States.

There is a growing dichotomy in the "furniture industry." For purposes of this case study, we include kitchen cabinets as part of the furniture industry — it is called "the furniture and related industry" — NAICS code 337 — which includes kitchen cabinets along with the more traditional furniture sectors. We do because the furniture and related sectors that are seeing most of the negative impact from globalization are the sectors that use wood primarily — this includes kitchen cabinets, wood household furniture, wood office furniture and upholstered furniture. The furniture industry, excluding the kitchen cabinet sector, lost 108,000 jobs or 21 percent of its workforce between 1997 and 2005. Only two sectors within the U.S. furniture industry — kitchen cabinets and office furniture — have shown growth in terms of employees, payroll and value of shipments. This is in contrast to the institutional and household furniture sectors, which experienced only slight growth and a major decline, respectively, during this same period.

For example, between 1997 and 2005*, the value of shipments for kitchen cabinets more than doubled (up 111 percent), office furniture shipments increased 22 percent, upholstered furniture shipments increased a modest 27 percent; institutional furniture shipments increased a meager 9 percent while shipments of nonupholstered furniture (i.e., wood furniture) actually fell 7 percent. The reason for this disparity is competition from cheaper imports has impacted the household furniture sector, particularly wood household furniture. For the wood household furniture sector,

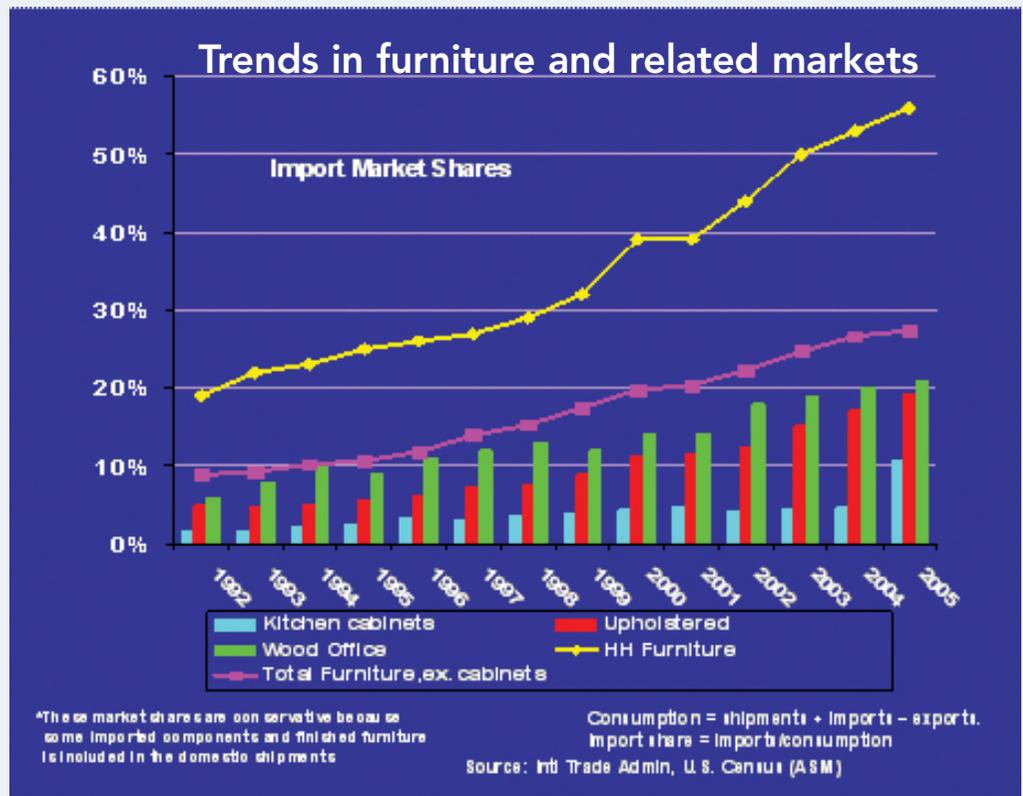


Figure 1. Furniture trade — Import market share for key furniture markets.

employment has fallen 36 percent and payrolls by 19 percent despite the fact that demand actually grew by 27 percent in the United States. In essence, imported wood furniture from Canada and offshore sources, particularly China, captured most of the growth in the wood furniture market during the past seven years. Demand was driven in large part by the phenomenal growth in residential construction over this period, but domestic manufacturers did not share in the "good times."

Unfortunately, like many mass-produced consumer goods, household furniture has become more of a commodity and is sold on price. Consumers are mainly interested in furniture that looks good and appears to be a good value. No longer do they look at furniture as a long-term investment as something to pass on to their children or keep as an antique. As a result, the consumer is spending less and less on furniture. There is also more competition for the consumer's dollar from electronic gadgets, home entertainment, travel and leisure products. Because of this emphasis on price, profit margins for U.S. furniture manufacturers are extremely low, while the costs of manufacturing continue to rise. This has created a severe profit squeeze that has led to a significant decline in plant and equipment investments. As a result, many U.S. furniture plants are not up-to-date with the latest technology and equipment.

Many U.S. furniture manufacturers are choosing to have their furniture made in China and other low-cost countries rather than produce their

own products. This has allowed offshore furniture competitors to increase their penetration into U.S. and world markets. If this does not change, most U.S. household furniture will be made offshore as U.S. furniture manufacturers continue to close their domestic manufacturing operations and become wholesalers and/or retailers. As offshore manufacturers gain more experience from supplying U.S. furniture manufacturers, they will learn enough to go around them and sell direct to retailers, or through their own retail distribution outlets. This is already happening as most of the larger Chinese furniture manufacturers sell direct to retailers and some are offering retail franchises in the United States.

The United States is experiencing a serious trade deficit, especially with China. Our dilemma is that we are exporting more raw materials, but importing more finished goods. This benefits raw material producers, retailers and consumers, but hurts producers of finished goods and their suppliers. For example, the United States is a major exporter of hardwood logs and lumber, but we are also the major importer of finished hardwood products such as furniture, flooring and mouldings. This needs to change if our secondary wood processing industry is to survive.

THE IMPACTS OF GLOBALIZATION ON THE U.S. WOOD PRODUCTS INDUSTRY

Globalization impacted trade in the furniture subsector has taken a distinct turn for the worse for U.S. manufacturers, with the kitchen cabi-

* U.S. Statistics for Furniture and Related Industries (NAICS 337) for 2005 and 1997. Source: U.S. Census; ASM; Statistics for Industry Groups and Industries (www.census.gov/mcd/asm-as1)

Wood HH Furniture Imports (Billion US\$)

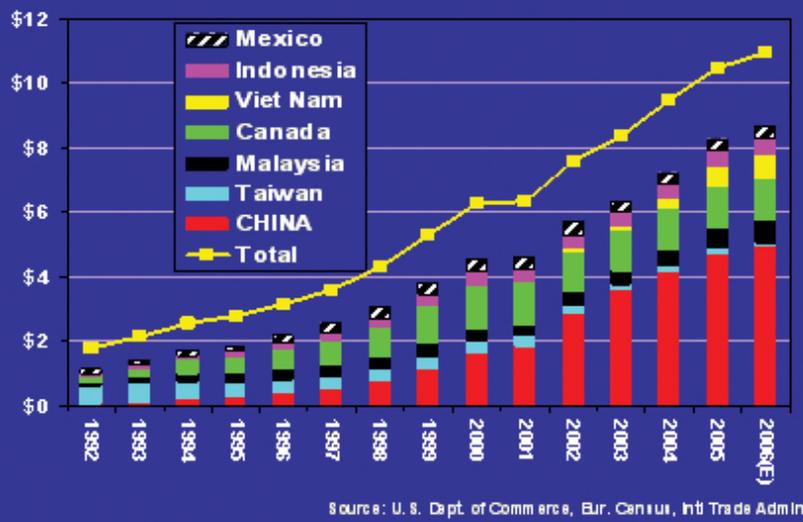


Figure 2. Import sources for wood household furniture.

net industry group more recently experiencing the beginning of a downturn in growth as well. Between 1992 and 2005, imports of all furniture products (including household, institutional and office furniture, but excluding kitchen cabinets) increased from \$4.1 billion to \$23.65 billion in 2005, an increase of almost \$20 billion or 477 percent. During this period, imports from China increased from \$208 million to \$10.8 billion, an increase of almost \$11 billion — a fifty-fold increase in 13 years.

Import market share for selected furniture and kitchen cabinet markets is shown in Figure 1. Imports now comprise 28 percent of all furniture consumption (excluding kitchen cabinets), up from 9 percent 13 years ago. In sectors where wood is the predominant material input, the loss of market share is equal, or in some cases, more substantial. Fifty-five percent of the wood household furniture, 11 percent of kitchen cabinets; 19 percent of the upholstered market; and 21 percent of the wood office furniture market consumed in the United States in 2005 consisted of imports.

Since the wood household furniture sector has been the most ravaged by imports, the major sources of imports in this sector are shown in Figure 2. China is the most important source. Chinese imports have increased 525 percent since 1998 — that's more than a six-fold increase in just eight years. A major reason for this rapid increase is that the Taiwanese furniture industry, with its management expertise, capital, knowledge of the U.S. market, and other pertinent expertise, relocated to mainland China beginning in the early 1990s.

Taiwan was a major manufacturer and exporter of wood furniture to the United States; however, as their standard of living increased, their furniture manufacturing costs, particularly the labor component, increased significantly and they were no longer as competitive as they once were. Thus, a "manufacturing capacity migration" is occurring in East and Southeast Asia from Taiwan (and to some extent mainland China) to Vietnam.

Wood furniture exports to the United States from Vietnam have increased from \$1 million to \$753 million in just five years. In fact, Vietnam is now the third largest exporter of wood household furniture to the United States, behind China and Canada — predictions point to it surpassing

Canada within five years.

Furniture isn't the only wood product sector that is having problems dealing with globalization and imports. Almost 11 percent of wood kitchen cabinets consumed in the United States are imports, and there is a growing fear that cabinets may be the next "furniture" sector to see an onslaught from imports.

For most of the past decade, the domestic kitchen cabinet industry has been able to remain globally competitive and maintain domestic market share of about 95 percent. This could be attributed to the fact that the cabinet industry was more vigilant and proactive regarding the threat from imports. They were probably the first of the "furniture sectors" to adopt "outsourcing" as a viable business model.

Over two decades ago, the segment shifted to the use of standardized components, most often made by another company, in their manufacturing strategy and essentially became "assemblers of cabinets." The traditional furniture manufacturing model is where the company "does it all" — buys lumber, manufactures the dimension lumber and other components, and then assembles these components into the finished furniture product.

When the cabinet industry adopted the "outsourcing model," this made it possible to manufacture customized cabinets at competitive prices. The customized cabinet product insulated them from cheaper standardized cabinets made offshore. The key here is attention to the customer — their market analysis told them the customer wanted customized cabinets for which they were willing to pay a bit more, but price still had to be "competitive" with standard cabinets. Outsourcing allowed them to customize, yet still provide good value to the customer.

IMPORT TRENDS

As seen in Figure 3, the share of consumption provided by domestic sources is shrinking for most wood product sectors including pulp and paper, structural panels (plywood and OSB), hardwood lumber, hardwood flooring and moulding products.

The common denominator for most of these industries is too much focus on production and not enough attention paid to the customer — i.e., a commodity mentality. Not a good strategy

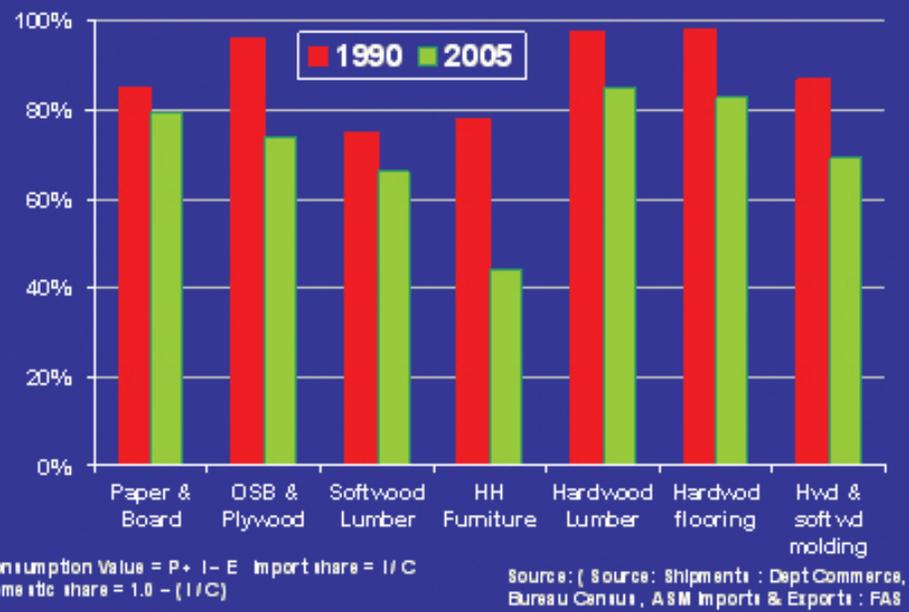


Figure 3. Share of domestic markets sourced from domestic production is falling for most wood products.

unless you are the "low cost producer" or have some other competitive advantages that serve to balance the scales for companies that have a higher cost structure. Some examples include: superior service; customization at competitive prices; faster delivery; better pricing terms; lean and flexible manufacturing; expert marketing and knowledge of your key customers; and superior quality.

RECOMMENDED STRATEGIC DIRECTION FOR THE FURNITURE INDUSTRY

We will suggest three parts to a survival strategy. As furniture markets shrink or lose market share to imports, hardwood lumber consumption has been shifting from furniture markets to construction and remodeling end uses (Figure 4). This shift points to part of the answer to a future furniture industry "survival strategy."

1. Find new and growing markets where you have a competitive advantage.

While the largest market for hardwood lumber used to be furniture, today it is construction markets — residential and nonresidential, new construction and remodeling/renovation. In contrast to softwood products, such as framing lumber and structural panels, hardwoods are being used in nonstructural applications like moulding and millwork, flooring, interior trim, stair parts, and decorative and specialty products such as fireplace mantels. The residential markets in the United States, although currently experiencing a minor "correction," have been on a tear for the past seven to eight years, and the demographic underpinnings for both new residential and remodeling markets are very positive for at least the next decade.

A big user of hardwood lumber is component manufacturers — they make mouldings, millwork, cabinet, furniture and stair parts, flooring blanks, and other products from hardwood lumber. They have made major shifts in their customer base in response to the demise of the furniture industry (Figure 5) — from supplying furniture customers to construction/remodeling customers and kitchen cabinets. They did this through better planning and marketing — understanding customer needs and finding their niche — and adapting to the furniture situation. Furthermore, think of China (and India and elsewhere) as an opportunity. As their standard of living increases and the

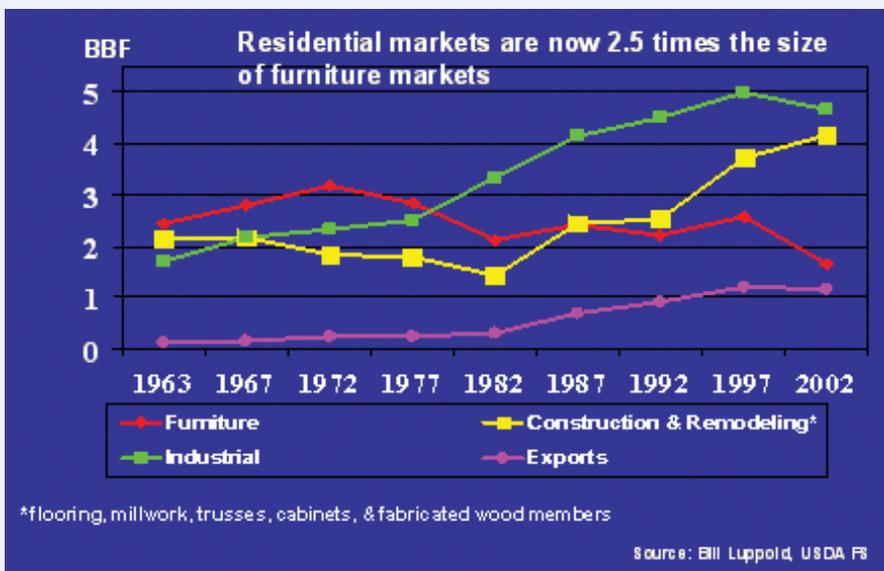


Figure 4. Hardwood lumber consumption trends.



Figure 5. Shifting component markets

middle class grows, they will want the same things you and I want — comfort, a nice house, nice furniture, etc. If we're competitive, we can sell into that market. Remember, China consumes over 75 percent of the furniture they produce — only 25 percent or less is exported.

Another part of the survival strategy is:

2. Transitioning from commodity products and services to customized products and services.

The United States is a high wage country and simply cannot remain competitive in many commodity markets where the low-cost producer has a strong advantage.

In the furniture industry, there has always been a disconnect between many furniture manufacturers and the final customer — too much emphasis was placed on the retailer to provide information on customer requirements and desires. Somehow, the furniture industry needs to figure out how to get closer to the “final customer” (you and me), and then determine how to supply the customer while remaining profitable. This will entail better marketing; better distribution systems; lean and flexible manufacturing; just-in-time supply chain operation; supply chain management; innovative thinking and leadership; and better training and education for their workforce — a new business model. It can be accomplished if the entire “supply chain” works together. The supply chain includes the integration of all key segments from the forest (or other input source) to manufacturing to distribution to marketing, culminating in a satisfied and happy customer.

This is essentially the idea of “centers of excellence” or “competitive clusters” as championed by Michael Porter, the management guru and author of the books: *The Competitive Advantage of Nations*; *Competitive Advantage: Creating and Sustaining Superior Competitive Performance*; and *Competitive Strategy*.

3. Develop relevant centers of excellence or competitive clusters.

As defined by Porter in his most recent book, *On Competition*, “a cluster is a geographically proximate group of interconnected companies and associated institutions in a particular field,

linked by commonalities and complementarities.” High Point, N.C., is an example of this for wood household furniture. Prior to globalization, a strong and large company with lots of resources could conceivably compete and be profitable for a time, even decades; however, today that company is competing with clusters from other countries, not the “sawmill in the next valley.”

In my opinion, some glaring omissions are effective market analysis; staying in touch with customers; developing a “flexible manufacturing strategy”; and keeping abreast of what goes on outside the United States — competitive intelligence. A flexible manufacturing strategy is one that adopts all the lean and efficiency techniques, but also has the capability to shift production quickly (within hours) if market conditions change.

The U.S. furniture industry needs strong and relevant clusters or centers of excellence if they are to compete globally, and hopefully regain some of their lost market share in domestic markets. An example of a recent success story is Amish furniture manufacturing in Ohio, Pennsylvania and Indiana (Bumgardner et al. 2007). Some key aspects of Amish competitiveness are quality craftsmanship in solid wood construction; the Amish name serves as a brand name; and customized products are sold in dedicated Amish stores with a wide range of species, finish and hardware. The Amish cluster has a well developed supply chain, wide use of the latest processes/technologies and shared resources/cooperation — each cluster element reinforces the others.

Today, Amish furniture is a real success story, and this cluster has become a significant factor in the U.S. furniture industry. In Ohio, the cluster is consuming an estimated 44 million bd. ft. of hardwood lumber annually or 11 percent of Ohio's total production (Bumgardner et al. 2007). Nationally, Amish furniture production might account for over 10 percent of the hardwood lumber used in U.S. furniture production.

The key question is whether the Amish model for success can be replicated throughout the United States. It won't be easy to replicate the cooperation aspects of this cluster. Likewise, Bumgardner states, to replicate the Amish commitment to

producing a top-quality product will require a significant cultural shift for some producers.

STRATEGIES FOR SUCCESS IN HIGH-WAGE ECONOMIES

There are a number of key strategies for achieving success in high-wage economies. The most important one is to produce innovative and customized products that are not being produced by low-wage competitors. This also means a greater focus on product design, finishing, marketing and distribution. There is still a good market for high-end customized products that consumers are willing to pay for.

For manufacturing operations, you must automate your production facilities whenever possible to maximize efficiencies and improve labor productivity. You also need to adopt new technologies and lean manufacturing techniques to reduce costs. High-wage countries also need to invest more in worker education, training and product research and development. We need to develop special skills that allow us to create superior products for which we can charge more. If we continue to produce commodity-type products with commodity services, we will continue to lose markets to countries where the labor supply is abundant and cheap. **W**

In Part Two of the series, Schuler and Lawser will address a number of operating strategies that U.S. furniture manufacturers are using to remain competitive in a high-wage economy. Some of these strategies are overlapping and many companies are using more than one. Look for it in July!

Ed. note: Al Schuler is a research economist with the USDA Forest Service, where he is responsible for assessing the demand/supply situation for solid wood products; the demand for engineered wood products; and the links between the softwood and hardwood forest products industry.

Steve Lawser serves as the executive director of the WCMA.