



HOME SWEET HOME STUDY

INDEPENDENT
WE STAND™

Powered by **STIHL** and Fiat Chrysler Automobiles **BUSINESS LINK**



NRHA

North American Retail
Hardware Association



INTRODUCTION

Civic Economics is pleased to present Independent We Stand and the North American Retail Hardware Association with this analysis of the economic impact of supporting independent hardware, outdoor power equipment, paint, and lumber retailers.

This report builds on previous Civic Economics analyses comparing the local economic impact of conducting business through a locally-owned independent business (or businesses) and doing it through a major national home center chain. (See *CivicEconomics.com/retail* for summaries and downloads). While these studies have looked at various lines of goods and services in several American and Canadian communities, the essential findings are broadly consistent:

Independent businesses provide their communities with substantial, quantifiable economic benefits relative to their chain competitors, and modest changes in purchasing habits can produce meaningful impacts.

Independent We Stand and the North American Retail Hardware Association have asked Civic Economics to study whether the same is true in the hardware and outdoor power equipment sectors.

INTRODUCTION 1

HYPOTHETICAL PROJECT APPROACH 2

PROJECT DESCRIPTION 2

MERCHANT TYPES 3

Locally-owned, independent retailers 3

National Chain Competitors 3

METHODOLOGY 4

QUANTIFYING LOCAL ADVANTAGES 5

Retail Hardware Purchases 5

Power Equipment Purchases 6

Building Materials Purchases 7

Installation Services 8

CUMULATIVE LOCAL ADVANTAGE 9

CONCLUSION 10

ABOUT CIVIC ECONOMICS 11

CONTACTS 12

HYPOTHETICAL PROJECT APPROACH

The independent merchants under review are complex. Within the same business, there may be a hardware store with everything from nuts and bolts to bolts of fabric. There may be a lumberyard, with racks of building materials ready for loading onto trucks of all sizes. There may be an outdoor power equipment department, offering bigger ticket items and, often, repairs. Finally, the merchant may provide customers with installation services after the sale. Many include indoor and outdoor garden centers, as well. In some cases, all these goods and services are offered under one roof.

These varied departments may function as a single business, but the business model is different for each. Building material sales, for example, are less labor intensive than hardware sales. In order to accurately capture impacts, then, Civic Economics developed a hypothetical home improvement that might be undertaken by a typical homeowner.

PROJECT DESCRIPTION

In this hypothetical, the customer will purchase the hardware, power equipment, and building materials needed for a sizeable outdoor project. While she may intend to complete much of the work herself, she will also hire a contractor to complete a portion of the project that requires special expertise. All told, the customer plans to spend **\$10,000**, budgeted as follows:

\$4000 will be spent on a wide range of hardware from a retail hardware store.

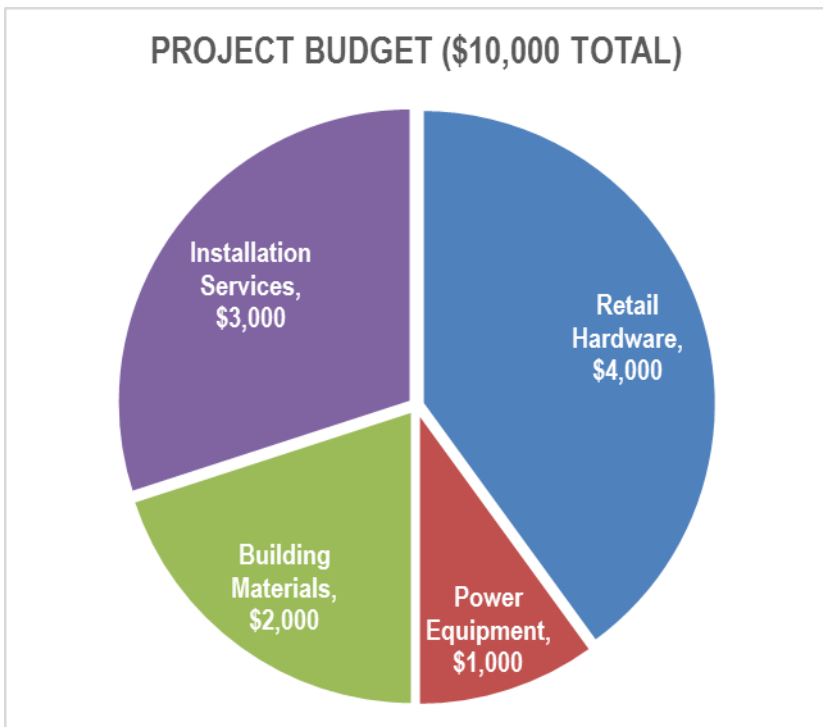
\$1000 will be spent on a single, specialized power tool needed for the job.

\$2000 will be spent on lumber and materials from a lumberyard facility.

\$3000 will be spent hiring a professional to complete a part of the project.

This budget of diverse goods and services allows us to study various business segments represented by both independents and chains within the hardware and outdoor power equipment sectors.

We also analyze the retail portions of the project separately in order to understand the impact of purchasing decisions.



MERCHANT TYPES

Our customer is fortunate to have a wide array of merchants eager to meet her needs in each of these categories. For simplicity, we will look two types of stores:

Locally-owned, independent retailers

The items needed for this project may be purchased at one or more local businesses. Most Americans live within a short distance of several locally owned businesses offering some or all of the materials and services required for this project.

Independent retailers in these lines of goods may, of course, operate branded stores, but they are not franchises. Within the hardware category, for example, there are competing merchant cooperatives that provide members with purchasing power as well as branding and advertising services. True cooperatives provide a periodic rebate to member stores rather than retaining profits. Similarly, independent lumber yards may participate in a purchasing cooperative or service and also support independent distributors.

How does the customer identify independents? Many independent stores do not carry a national brand. Do It Best, Ace, and True Value hardware stores operate on the cooperative model described above. Additionally, any outdoor power equipment dealer carrying Stihl products is an independent.

National Chain Competitors

For this exercise, the chain competition is the two largest, most easily identified home center chains. These big box stores offer hardware, outdoor power equipment, and building materials under one roof. Though the stores may feature different color schemes, they offer a remarkably similar goods and services and they procure and distribute those goods in similar fashion. Indeed, for this study, Civic Economics has culled data about each firm to craft a composite representing a typical national chain home center.

A NOTE ON PRICING

We are often asked whether these studies incorporate price differentials between independents and chains, and the short answer is no. We begin with an assumption of comparable value received, recognizing that price differences may be larger in some contexts than in others.

In this case, however, we have strong evidence of highly competitive pricing. One independent showed a workbook, updated weekly, in which employees note prices for hundreds of items at a major chain and in his own store.

Two things stood out from these numbers:

1. The independent meets or beats prices across the board.
2. Prices at the two major chains are nearly identical, requiring research into only one each week.

In these sectors, the value proposition offered by independents is highly competitive even without accounting for the enhanced service most provide.

Moreover, the inclusion of outdoor power equipment provides another reason to believe independents offer a strong value proposition. **STIHL** sells only through independents who also provide ongoing maintenance and repair services, and both professional and consumer grade products are intended for more demanding purchasers. Simply comparing the price for a particular tool from STIHL, Husky, or Kobalt does not capture the value proposition between outdoor power equipment.

METHODOLOGY

The approach to this study has been developed over years of related analyses conducted by Civic Economics. In order to develop accurate comparisons, we quantify the proportion of revenue that both independents and chains recirculate in the local economy.

The lion's share of the local economic impact of independent retail and service businesses is attributable to four factors: labor, profit, procurement, and charity.

Spending on local **labor** comprises a larger share of operating costs for a locally-owned establishment than for an outlet of a national chain. While the latter are able to consolidate administrative functions such as bookkeeping and marketing at national headquarters, independents must carry out those functions in-house or outsource within the community. The difference is clear on the shop floor, too. Upon entering an independent store, a sales associate will often walk with you to the department and help you pick out the correct part. At the chains, any assistance beyond directions to a row number will be hard to come by.

Secondly, a larger portion of **profits** earned by local ownership will remain in the local economy. These profits can be reinvested locally whether through further investment in the independent business or in the community at large. Purchases at chain outlets generate profits for the corporation, which then either reinvests in global operations or distributes a portion of profits to shareholders. In either case, chain stores profits circulating in the local economy are nominal.

Third, locally-owned businesses **procure** services locally. An independent business will hire local accountants, lawyers, and information technology firms among others. National chains have these services provided in their headquarter locations leaking that money out of the region.

A smaller yet significant share of the local advantage is **charitable giving**. The owners and employees of local firms generally live in and around their business locations and are more likely to give back to their own backyard. National firms may be more likely to donate to charities near to corporate headquarters or other large corporate facilities. And the marketing campaign around a donation often exceeds the cost of the gift.

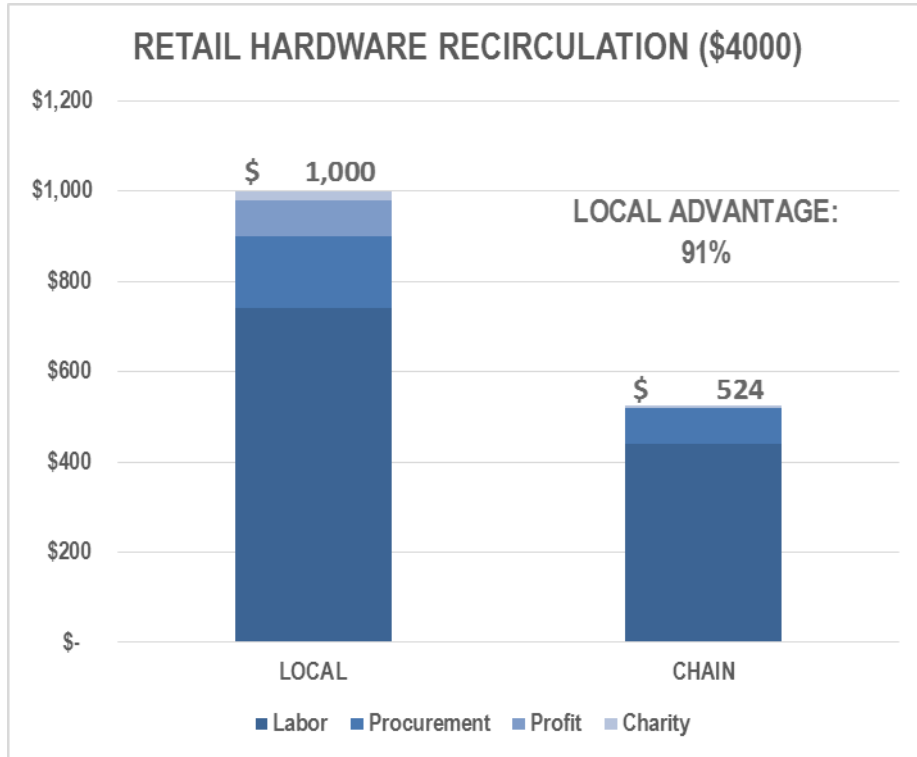
For independent businesses, Civic Economics surveys or interviews owners to quantify accurate numbers for the proportion of revenue that goes to each. In this study, interviews with business owners in the Chicago and Austin areas is supplemented by two invaluable sources. The North American Retail Hardware Association provided us with their 2014 Cost of Business Survey, which broke out costs and revenues in hardware and lumber sectors. Independent We Stand contacted Stihl, Inc. and provided an average dealer margin for the company's consumer grade power equipment. Civic Economics further estimated the local dealers likely revenue from warranty service and repairs associated with Stihl sales. To protect the company's proprietary information, we have here aggregated those two numbers and further discounted occupancy costs from the total.

For chains, we analyzed Annual Reports, in this case for fiscal year 2013, for both Home Depot and Lowe's. Additional information was gleaned from varied sources, including interviews and even a bit of message board snooping.

QUANTIFYING LOCAL ADVANTAGES

Retail Hardware Purchases

Of the \$10,000 project, our homeowner will need \$4000 of goods purchased from a retail hardware store. These might include fasteners and screws and paints, as well as a host of small purchases to make the job work.



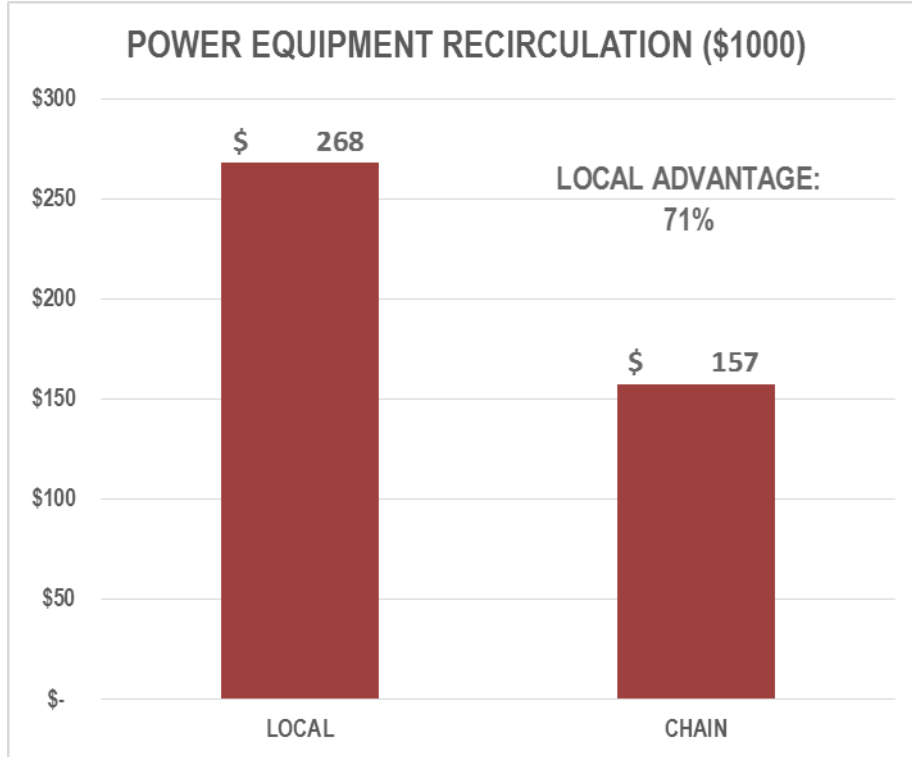
Retail hardware operations are fairly typical of the broader retail sector. Most goods are brought to the store from regional distribution centers, then employees stock the shelves and manage sales, while some goods may be purchased separately from local area suppliers. Truly local procurement is typically limited to a few items of regional interest, but independents do retain local service providers for a variety of functions that chains do not.

Labor costs are comparable to the broader retail sector, as well. The competitive nature of the segment means margins are tight.

Purchasing hardware products from an independent retailer results in a 91% increase in local economic activity compared to making the same purchase at the major chains.

Power Equipment Purchases

Of the \$10,000 project, our homeowner will need to spend \$1000 on specialized outdoor power equipment that will make the job easier and improve results. This purchase might occur at a specialized dealer or within a broader hardware and home improvement store.



The outdoor power equipment segment provides an interesting area of study, as these are typically big ticket items. Here, we compare independent outdoor power equipment dealers (using Stihl products as the representative purchase) and the major chains, which do offer higher quality items in competition with Stihl.

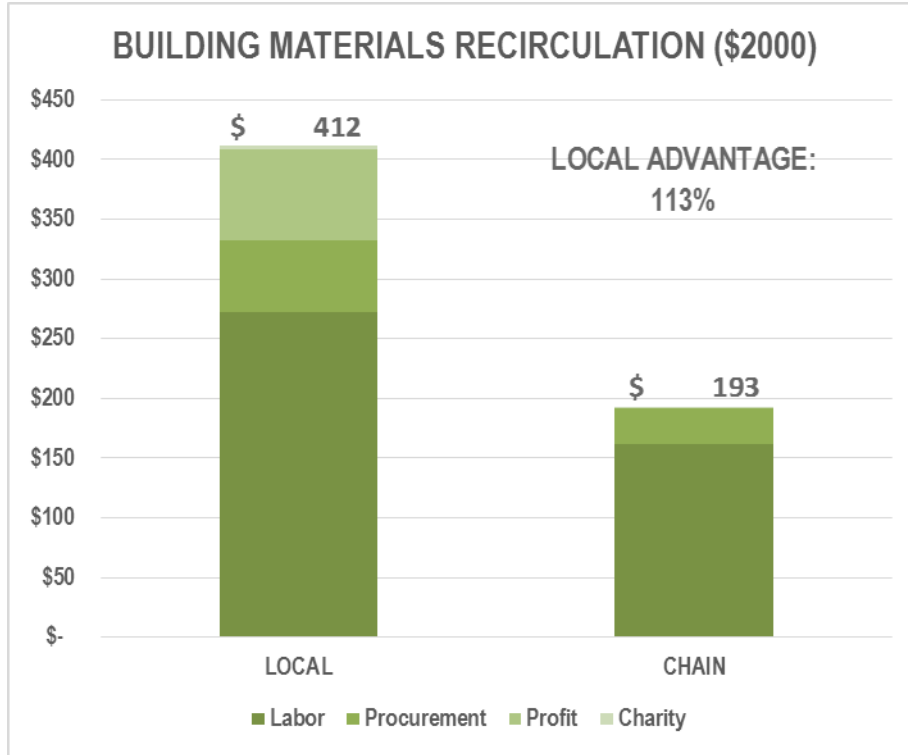
Though Stihl did provide Civic Economics with some data regarding margins and dealer cost, that data is proprietary. In order to shield that information, we have included two additional factors:

- We added maintenance and repair revenues the dealer might expect to earn during and after the warranty period.
- We deducted occupancy costs in order to properly compare merchants in this sector with others.

After all calculations, purchasing Stihl products from an independent dealer results in a 71% increase in local economic activity compared to purchasing comparable outdoor power equipment products at the major chains.

Building Materials Purchases

Of the \$10,000 project budget, our homeowner will need to spend \$2000 on materials from the lumberyard, including anything from raw boards or shingles to finished windows and doors.

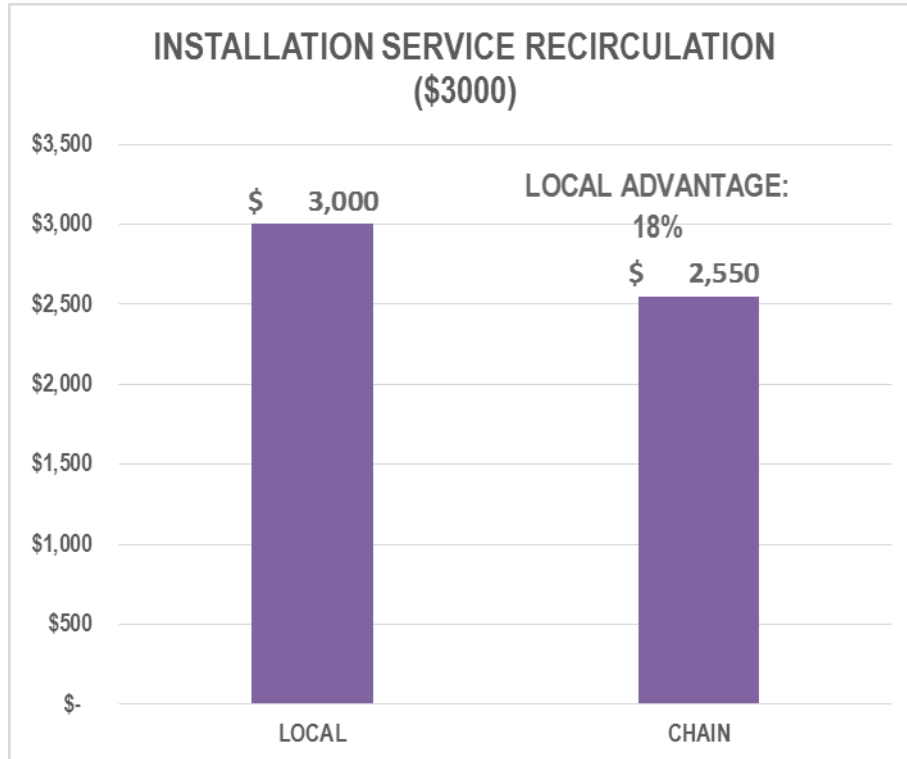


For this study, building materials comprise those goods sold from a lumberyard layout, whether indoors or out. Labor costs as a share of revenue are held down by bulk sales to professional contractors.

For lumber in particular, production and distribution networks are similar between chains and independents. Wood is harvested and processed where it is grown, as shipping whole trees would introduce excessive transportation costs. Distribution centers for the major chains and those supplying independents are comparably distributed around the nation.

Purchasing building materials from an independent lumber yard results in a 113% increase in local economic activity compared to making the same purchase at the major chains.

Installation Services



Installation services, by their very nature, generally result in most or all of the fee paid remaining in the local economy. Unlike a kitchen faucet that can be produced anywhere in the world and shipped to the end user, the labor must take place locally. However, the retailers under study here present two different ways of reaching that end.

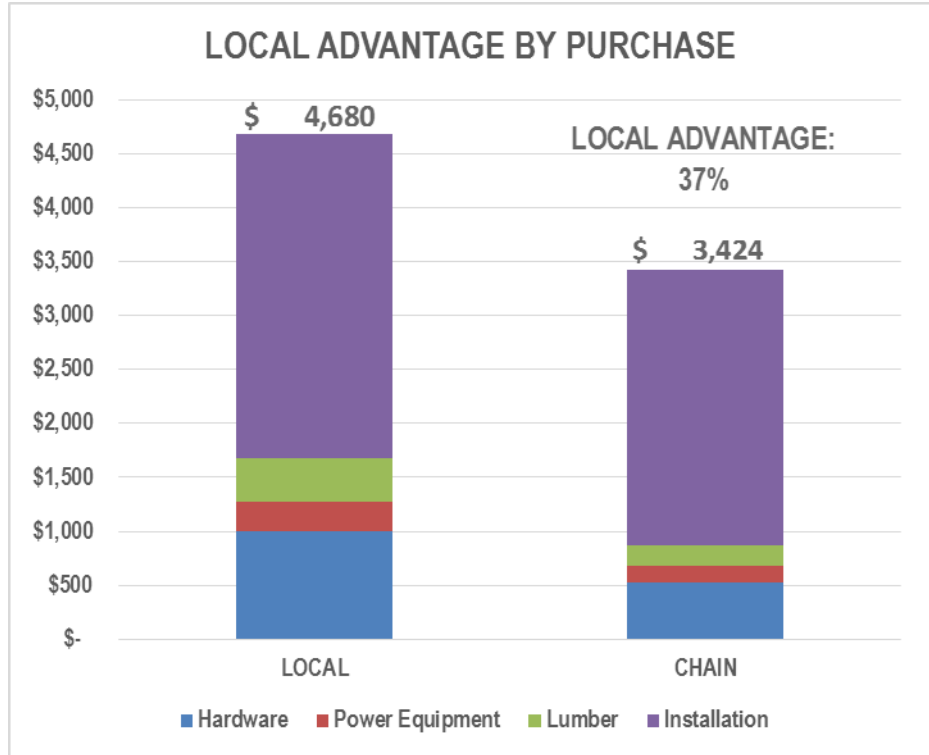
Independents generally handle referrals in an informal manner, offering customers the name of a contractor who the retailer knows to be reputable, responsible, and reliable after extensive dealings. The customer gets a solid reference; the contractor gets a job; and the retailer strengthens the relationship with that contractor. The retailer does not typically receive a referral fee. In this case, of course, a \$3000 expenditure for labor alone to a local resident contractor results in \$3000 of local economic activity.

The major national chains, on the other hand, maintain a more formal system of referrals. As with the independent, they seek to use only reliable providers, but the chain stores retain a portion of the customer charge, typically in the range of 15%. If the total price is not increased to cover that fee, the customer will get the same work for the same price, but the local economy will be deprived of those dollars. If the total price is increased, then the homeowner will have received less value for her money at the chain than at the local.

Major shifts are just beginning in the market for work of the sort contemplated here. Amazon Home Services, for example, facilitates a bidding process that will likely drive down total fees while additionally retaining a fee for the transaction. Google, too, is entering that market. How these changes will play out is uncertain, but this study takes place a bit too soon to know.

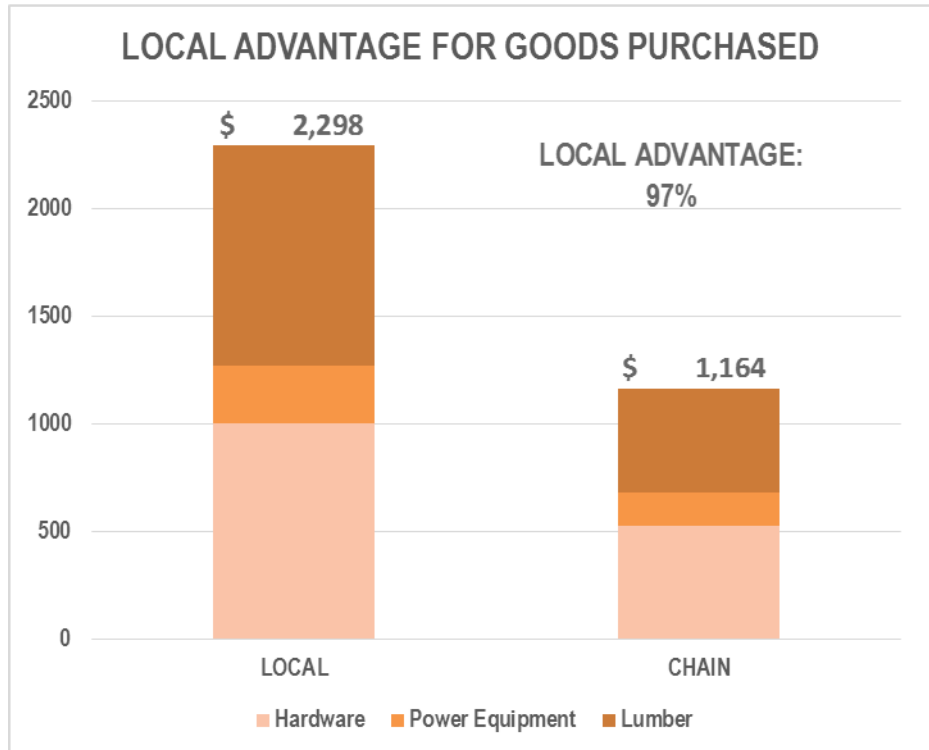
CUMULATIVE LOCAL ADVANTAGE

At the end of the project, our homeowner will have created an extra \$1250 in local economic activity simply by supporting local retailers. But that doesn't capture the real local boost to the local economy provided by the retailers under study here.



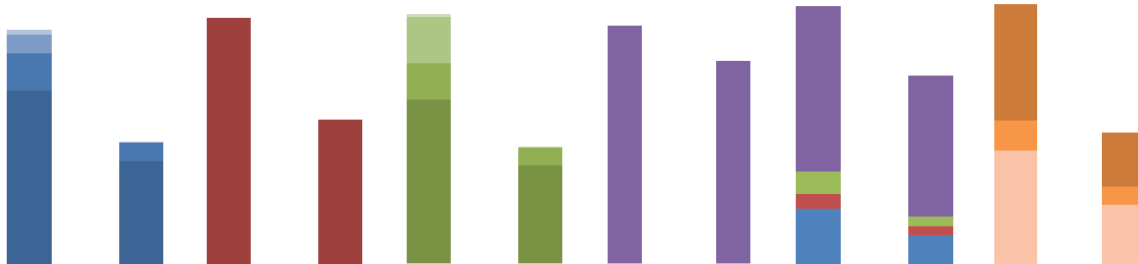
For the purchase of tangible goods, the local economic advantage associated with independents is 97% greater than that with chain stores.

In other words, independent, locally-owned hardware, power tool, and lumber sellers generate twice the local economic activity on the same revenue.



CONCLUSION

Every graph produced for this report reflects the same general outcome, with locals generating more economic activity regardless of how it is counted.



In the highly competitive businesses of hardware, outdoor power equipment, and building materials, independent retailers provide a compelling value proposition to consumers while creating significantly enhanced local economic activity compared to national chains.

In the hypothetical home improvement project reviewed here, our homeowner would have spent comparable amounts whether with the biggest chains or the smallest independents. But of that spending, 37% more would remain in her community. Excluding contracted installation services, that local economic advantage is nearly double, 97%.

That money improves job prospects for her neighbors. It ends up in other local businesses, in parks, and in collection plates in her hometown. It helps an independent, entrepreneurial local contractor make ends meet in an evolving and competitive business.

How might that knowledge help consumers and businesses change their shopping habits? Consider the following:

Together, the two largest national home center chains sold more than \$114 billion in goods in 2013 (excluding installation services).

If just 10% of that business gone instead to independents, hometowns around the country would enjoy the benefits of an additional \$1.3 billion in economic activity.

That kind of money turns home improvement into hometown improvement.

ABOUT CIVIC ECONOMICS

Civic Economics is an economic analysis and strategic planning consultancy with offices in Austin and Chicago. Since its founding in 2002, the work of Civic Economics has been nothing if not diverse, in both subject matter and geography. One area to which we frequently return, however, is the economics of regional retail and service provision - what we've taken to calling *the Civic Economics of Retail*.

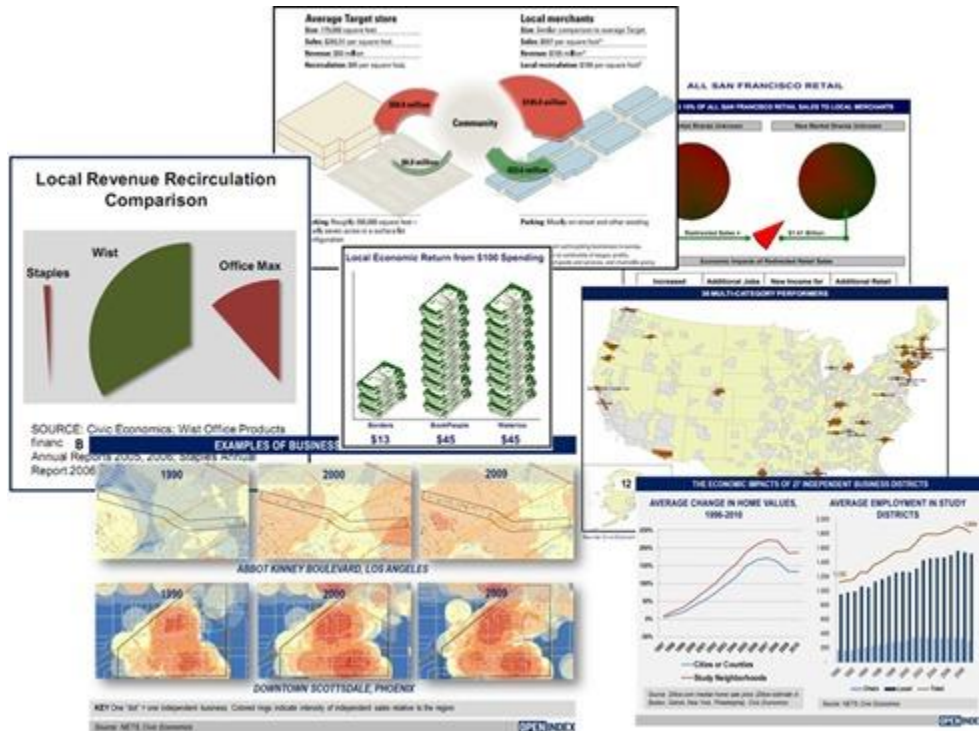
Retail development and redevelopment bring significant impacts to any community. Civic Economics provides communities with the tools to manage those impacts, magnifying the benefits and mitigating the challenges.

Civic Economics is the acclaimed leader in understanding the economics of regional retail and service activities. From its founding, the firm has focused on the critical and often misunderstood role of retail in economic development and urban planning policy.

Civic Economics analyzes the economics of retail and service provision using time-tested, industry standard approaches tailored to the needs and circumstances of each community. These include trade area analysis, demographic analysis, consumer and business surveys, retail prospect identification, retail gap analysis, adaptive reuse of mature retail centers, and economic and fiscal impact analysis.

More importantly, the partners of Civic Economics monitor the ever-evolving retail industry. We know where market forces are heading and what retailers are doing in response. We know, too, what other communities are doing, providing us with an unmatched knowledge of best and worst practices. In contrast to our larger, convention-bound peers and academic researchers, Civic Economics has developed innovative methodologies for analyzing this unique industry sector.

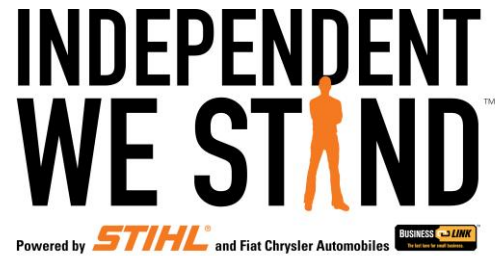
Learn more at: <http://www.civiceconomics.com/retail.html>



CONTACTS

FOR INDEPENDENT WE STAND

Bill Brunelle
888-787-8497
bill@independentwestand.org
IndependentWeStand.org



FOR THE NORTH AMERICAN RETAIL HARDWARE ASSOCIATION

Dan Tratensek
(317) 275-9407
DanT@nrha.org
NRHA.org



FOR CIVIC ECONOMICS

Matt Cunningham
mattc@civiceconomics.com
www.CivicEconomics.com



We wish to extend a special “thank you” to two independent retailers who took extended time out of their days to help us learn about their complex businesses. They showed us around, patiently answered questions about sourcing and distribution, and gave us a confidential look at actual budgeting and pricing practices that proved invaluable in the preparation of this report. The revenue recirculation numbers in this report do not reflect the specific practices of either of these firms.

Ralph Helm of **Ralph Helm, Incorporated** in Elgin and Crystal Lake, Illinois walked Matt Cunningham around the Elgin shop, which sells and services Stihl and other outdoor power equipment to professionals and consumers alike.

Bret Capelman of **Apple Lumber** in Luling, Smithville, and Yorktown, Texas showed Dan Houston around his family’s extensive Luling operation, including a full-line hardware store, Stihl outdoor power equipment, Pittsburgh Paints, a garden and gift shop, and a traditional lumber yard.