

Builders FirstSource, Inc.
Form 10-Q
August 01, 2012
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

X **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended June 30, 2012

OR

.. **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from to

Commission File Number 0-51357

BUILDERS FIRSTSOURCE, INC.

(Exact name of registrant as specified in its charter)

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Delaware
*(State or other jurisdiction of
incorporation or organization)*

52-2084569
*(I.R.S. Employer
Identification No.)*

2001 Bryan Street, Suite 1600

Dallas, Texas
(Address of principal executive offices)

75201
(Zip Code)

(214) 880-3500

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer
Non-accelerated filer Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined by Rule 12b-2 of the Exchange Act). Yes No

The number of shares of the issuer's common stock, par value \$0.01, outstanding as of July 31, 2012 was 96,700,935.

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Table of Contents**PART I FINANCIAL INFORMATION****Item 1. Financial Statements (unaudited)****BUILDERS FIRSTSOURCE, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS**

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
	(Unaudited)			
	(In thousands, except per share amounts)			
Sales	\$ 271,919	\$ 206,393	\$ 491,308	\$ 369,222
Cost of sales	218,255	163,590	392,525	294,986
Gross margin	53,664	42,803	98,783	74,236
Selling, general and administrative expenses	54,960	48,965	105,793	95,666
Facility closure costs	76	1,882	204	1,904
Loss from operations	(1,372)	(8,044)	(7,214)	(23,334)
Interest expense, net	10,461	5,665	23,566	11,540
Loss from continuing operations before income taxes	(11,833)	(13,709)	(30,780)	(34,874)
Income tax expense	144	1,666	318	1,649
Loss from continuing operations	(11,977)	(15,375)	(31,098)	(36,523)
Loss from discontinued operations (net of income tax expense of \$0 for the three months and six months ended in 2012 and 2011, respectively)	(78)	(109)	(145)	(210)
Net loss	\$ (12,055)	\$ (15,484)	\$ (31,243)	\$ (36,733)
Comprehensive loss	\$ (12,055)	\$ (13,706)	\$ (31,243)	\$ (34,576)
<i>Basic and diluted net loss per share:</i>				
Loss from continuing operations	\$ (0.13)	\$ (0.16)	\$ (0.33)	\$ (0.39)
Loss from discontinued operations	(0.00)	(0.00)	(0.00)	(0.00)
Net loss	\$ (0.13)	\$ (0.16)	\$ (0.33)	\$ (0.39)
<i>Weighted average common shares outstanding:</i>				
Basic and diluted	95,427	94,905	95,344	94,905

The accompanying notes are an integral part of these condensed consolidated financial statements.

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BUILDERS FIRSTSOURCE, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

	June 30, 2012	December 31, 2011
	(Unaudited)	
	(In thousands,	
	except per share amounts)	
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 105,090	\$ 146,833
Restricted cash	12,633	13,229
Accounts receivable, less allowances of \$2,403 and \$2,138 at June 30, 2012 and December 31, 2011, respectively	113,635	76,429
Inventories	91,035	73,327
Other current assets	9,174	9,843
Total current assets	331,567	319,661
Property, plant and equipment, net	47,107	48,224
Goodwill	111,193	111,193
Other assets, net	9,230	9,725
Total assets	\$ 499,097	\$ 488,803
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	\$ 79,528	\$ 48,618
Accrued liabilities	29,980	25,183
Current maturities of long-term debt	57	54
Total current liabilities	109,565	73,855
Long-term debt, net of current maturities	298,094	297,455
Other long-term liabilities	20,130	16,269
Total liabilities	427,789	387,579
Commitments and contingencies (Note 7)		
Stockholders' equity:		
Preferred stock, \$0.01 par value, 10,000 shares authorized; zero shares issued and outstanding at June 30, 2012 and December 31, 2011		
Common stock, \$0.01 par value, 200,000 shares authorized; 96,690 and 96,806 shares issued and outstanding at June 30, 2012 and December 31, 2011, respectively	954	950
Additional paid-in capital	361,073	359,750
Accumulated deficit	(290,719)	(259,476)
Total stockholders' equity	71,308	101,224
Total liabilities and stockholders' equity	\$ 499,097	\$ 488,803

The accompanying notes are an integral part of these condensed consolidated financial statements.

Table of Contents**BUILDERS FIRSTSOURCE, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

	Six Months Ended June 30, 2012 2011 (Unaudited)	
	(In thousands)	
Cash flows from operating activities:		
Net loss	\$ (31,243)	\$ (36,733)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	5,341	7,205
Amortization of deferred loan costs	341	419
Amortization of debt discount	668	
Fair value adjustment of stock warrants	3,726	
Deferred income taxes	226	1,566
Bad debt expense	167	74
Stock compensation expense	1,725	1,980
Net gain on sales of assets	(54)	(199)
Changes in assets and liabilities:		
Receivables	(37,373)	(25,319)
Inventories	(17,708)	(5,660)
Other current assets	669	694
Other assets and liabilities	(857)	675
Accounts payable	30,910	14,888
Accrued liabilities	5,685	1,646
Net cash used in operating activities	(37,777)	(38,764)
Cash flows from investing activities:		
Purchases of property, plant and equipment	(3,988)	(1,635)
Proceeds from sale of property, plant and equipment	58	295
Decrease in restricted cash	675	
Net cash used in investing activities	(3,255)	(1,340)
Cash flows from financing activities:		
Payments of long-term debt and other loans	(26)	(25)
Deferred loan costs	(287)	
Exercise of stock options	98	
Repurchase of common stock	(496)	(2)
Net cash used in financing activities	(711)	(27)
Net change in cash and cash equivalents	(41,743)	(40,131)
Cash and cash equivalents at beginning of period	146,833	103,234
Cash and cash equivalents at end of period	\$ 105,090	\$ 63,103

The accompanying notes are an integral part of these condensed consolidated financial statements.

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BUILDERS FIRSTSOURCE, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

1. Basis of Presentation

Builders FirstSource, Inc., a Delaware corporation formed in 1998, is a leading supplier and manufacturer of structural and related building products for residential new construction in the United States. In this quarterly report, references to the company, we, our, ours or us refer to Builders FirstSource, Inc. and its consolidated subsidiaries, unless otherwise stated or the context otherwise requires.

In the opinion of management, the accompanying unaudited condensed consolidated financial statements include all recurring adjustments and normal accruals necessary for a fair statement of the company's financial position, results of operations and cash flows for the dates and periods presented. Results for interim periods are not necessarily indicative of the results to be expected during the remainder of the current year or for any future period. All significant intercompany accounts and transactions have been eliminated in consolidation.

The condensed consolidated balance sheet as of December 31, 2011 is derived from the audited consolidated financial statements but does not include all disclosures required by accounting principles generally accepted in the United States of America. This condensed consolidated balance sheet as of December 31, 2011 and the unaudited condensed consolidated financial statements included herein should be read in conjunction with the more detailed audited consolidated financial statements for the year ended December 31, 2011 included in our most recent annual report on Form 10-K. Accounting policies used in the preparation of these unaudited condensed consolidated financial statements are consistent with the accounting policies described in the Notes to Consolidated Financial Statements included in our Form 10-K.

2. Net Loss per Common Share

Net loss per common share (EPS) is calculated in accordance with the *Earnings per Share* topic of the FASB Accounting Standards Codification (Codification), which requires the presentation of basic and diluted EPS. Basic EPS is computed using the weighted average number of common shares outstanding during the period. Diluted EPS is computed using the weighted average number of common shares outstanding during the period, plus the dilutive effect of potential common shares.

Our restricted stock shares include rights to receive dividends that are not subject to the risk of forfeiture even if the underlying restricted stock shares on which the dividends were paid do not vest. In accordance with the *Earnings per Share* topic of the Codification, unvested share-based payment awards that contain non-forfeitable rights to dividends are deemed participating securities and should be considered in the calculation of basic EPS. Since the restricted stock shares do not include an obligation to share in losses, they will be included in our basic EPS calculation in periods of net income and excluded from our basic EPS calculation in periods of net loss. Accordingly, there were 1.3 million and 1.8 million restricted stock shares excluded from the computations of basic EPS for the three and six months ended June 30, 2012 and 2011, respectively, because we generated a net loss. For the purpose of computing diluted EPS, options to purchase 5.7 million and 5.8 million shares of common stock were not included in the computations of diluted EPS for the three and six months ended June 30, 2012 and 2011, respectively, because their effect was anti-dilutive. Warrants to purchase 1.6 million shares of common stock were not included in the computation of diluted EPS for the three and six months ended June 30, 2012 because their effect was anti-dilutive. No warrants were outstanding in the three and six months ended June 30, 2011.

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Long-term debt consisted of the following (in thousands):

	June 30, 2012	December 31, 2011
Term loan	\$ 160,000	\$ 160,000
Floating rate notes	139,718	139,718
Other long-term debt	4,059	4,085
	303,777	303,803
Unamortized debt discount	(5,626)	(6,294)
	298,151	297,509
Less: current maturities of long-term debt	57	54
Long-term debt, net of current maturities	\$ 298,094	\$ 297,455

We issued detachable warrants in connection with the term loan entered into in 2011. These warrants, which allow for the purchase of up to 1.6 million shares of our common stock at a price of \$2.50 per share, were exercisable immediately upon issuance and expire in December 2018.

In the past, we entered into interest rate swaps in order to mitigate a portion of the interest rate risk that we were exposed to in the normal course of business on our floating rate notes. We had two interest rate swap agreements with notional amounts of \$100 million and \$50 million, which expired in May 2011.

The only financial instruments measured at fair value on a recurring basis were our warrants and the expired interest rate swaps.

The table below presents the effect of our derivative financial instruments on the condensed consolidated statements of operations for the three and six months ended June 30 (in thousands):

Derivatives Not Designated as Hedging Instruments	Location of Loss Recognized in Income	Amount of Loss Recognized in Income*			
		Three Months Ended June 30,		Six Months Ended June 30,	
		2012	2011	2012	2011
Interest rate swaps	Interest expense, net	\$	\$ (1,779)	\$	\$ (2,165)
Warrants	Interest expense, net	(578)		(3,726)	
Total		\$ (578)	\$ (1,779)	\$ (3,726)	\$ (2,165)

* Net of tax

We use the income approach to value our warrants by using the Black-Scholes option-pricing model. Using this model, the risk-free interest rate is based on the U.S. Treasury yield curve in effect on the valuation date. The expected life is based on the period of time until the expiration of the warrants. Expected volatility is based on the historical volatility of our common stock over the most recent period equal to the expected life of the warrants. The expected dividend yield is based on our history of not paying regular dividends in the past and our current intention to not pay regular dividends in the foreseeable future.

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We do not trade in swaps or hold them for speculative purposes, therefore, the retail market that exists for swaps would have been the most advantageous market for our interest rate swaps. As such, we used the market approach to value our interest rate swaps by obtaining a quote from the counterparty that was based on a discounted cash flow analysis which incorporated information obtained from third-party market sources and was adjusted for company specific credit risk. We validated the fair value quote obtained from the counterparty by using an independent, third-party discounted cash flow analysis which also utilized market information. In addition to the term and notional amount inputs, the valuation also factored in discount rate, forward yield curves, and credit risk.

These techniques incorporate Level 1 and Level 2 inputs. Significant inputs to the derivative valuation for interest rate swaps and warrants are observable in the active markets and are classified as Level 2 in the hierarchy.

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The following fair value hierarchy table presents information about our financial instruments measured at fair value on a recurring basis using significant other observable inputs (Level 2) (in thousands):

	Carrying Value As of June 30, 2012	Fair Value Measurement as of June 30, 2012	Carrying Value As of December 31, 2011	Fair Value Measurement as of December 31, 2011
Warrants (included in Other long-term liabilities)	\$ 6,062	\$ 6,062	\$ 2,336	\$ 2,336

We have elected to continue to report the value of our term loan and floating rate notes at amortized cost. The fair value of the floating rate notes at June 30, 2012 was approximately \$128.5 million and was determined using Level 2 inputs based on market prices. The carrying value of the term loan at June 30, 2012 approximates fair value as the term loan agreement contains a variable interest rate and the value of qualified cash and specified collateral exceeded the minimum value required per the agreement. As such, the fair value measurement of the term loan was also classified as Level 2 in the hierarchy.

4. Comprehensive Loss

The following table presents the components of comprehensive loss for the three and six months ended June 30, 2012 and 2011 (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Net loss	\$ (12,055)	\$ (15,484)	\$ (31,243)	\$ (36,733)
Other comprehensive income change related to interest rate swap agreements, net of related tax effect		1,778		2,157
Comprehensive loss	\$ (12,055)	\$ (13,706)	\$ (31,243)	\$ (34,576)

5. Facility Closure Costs

During the second quarter of 2011, we closed a distribution facility in Georgia which had been idled since 2008. This facility was closed due to the continued depressed market conditions, the housing recovery taking longer than originally anticipated, our success in finding a subtenant to partially offset our remaining future lease obligations, and our ability to adequately service our customers from other existing locations in the market. In the second quarter of 2011, we recognized \$1.9 million in facility closure costs which are primarily related to the future minimum lease obligations on this facility, net of estimated sub-rental lease income. The facility and other exit cost reserves of \$2.6 million at June 30, 2012, of which \$1.9 million is recorded as other long-term liabilities, are primarily related to future minimum lease obligations on vacated facilities.

In situations where multiple facilities serve the same market we may temporarily close, or idle, facilities with plans to reopen these facilities once demand returns to the market. Should conditions in our markets worsen, or recovery take significantly longer than forecasted, we may temporarily idle or permanently close additional facilities, at which time we may incur additional facility closure costs or asset impairment charges. Future non-cash impairment charges would have the effect of decreasing our earnings or increasing our losses in such period, but would not impact our current outstanding debt obligations or compliance with covenants contained in the related debt agreements.

6. Income Taxes

In accordance with the *Income Taxes* topic of the Codification, we evaluate our deferred tax assets quarterly to determine if a valuation allowance is required. The *Income Taxes* topic requires that companies assess whether valuation allowances should be established based on the consideration of all available evidence. During the three and six months ended June 30, 2012, we recorded valuation allowances of \$4.3 million and \$11.3 million against the net deferred tax assets generated from the net losses during the periods related to our continuing operations. During the three and six months ended June 30, 2011, we recorded a valuation allowance of \$6.8 million and \$14.9 million against the net

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deferred tax assets generated from the net losses during the periods related to our continuing operations. In connection with the expiration of our interest rate swaps during 2011, we reclassified \$1.3 million of valuation allowance from accumulated other comprehensive loss to income tax expense for the six months ended June 30, 2011.

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To the extent we generate sufficient taxable income in the future to fully utilize the tax benefits of the net deferred tax assets on which a valuation allowance is recorded, our effective tax rate may decrease as the valuation allowance is reversed. However, to the extent we generate future operating losses, we would be required to increase the valuation allowance on our net deferred tax assets and our income tax expense will be adversely affected.

7. Commitments and Contingencies

We are a party to various legal proceedings in the ordinary course of business. Although the ultimate disposition of these proceedings cannot be predicted with certainty, management believes the outcome of any claim that is pending or threatened, either individually or on a combined basis, will not have a material adverse effect on our consolidated financial position, cash flows or results of operations. However, there can be no assurances that future costs related to legal proceedings would not be material to our results of operations or liquidity for a particular period.

8. Segment and Product Information

We have three regional operating segments Atlantic, Southeast and Central with centralized financial and operational oversight. We believe that these operating segments meet the aggregation criteria prescribed in the *Segment Reporting* topic of the Codification, and thus have one reportable segment.

Sales by product category for the three and six month periods ended June 30, 2012 and 2011 were as follows (in thousands):

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2012	2011	2012	2011
Prefabricated components	\$ 51,232	\$ 40,227	\$ 94,681	\$ 71,010
Windows & doors	59,294	46,577	109,020	84,842
Lumber & lumber sheet goods	87,942	60,739	154,372	108,849
Millwork	26,394	21,552	47,797	39,243
Other building products & services	47,057	37,298	85,438	65,278
Sales	\$ 271,919	\$ 206,393	\$ 491,308	\$ 369,222

9. Recent Accounting Pronouncements

There were no new accounting pronouncements or changes to existing guidance that were applicable to us.

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Item 2. *Management's Discussion and Analysis of Financial Condition and Results of Operations*

The following discussion of our financial condition and results of operations should be read in conjunction with the Management's Discussion and Analysis of Financial Condition and Results of Operations and the consolidated financial statements and notes thereto for the year ended December 31, 2011 included in our most recent annual report on Form 10-K. The following discussion and analysis should also be read in conjunction with the unaudited condensed consolidated financial statements appearing elsewhere in this report. In this quarterly report on Form 10-Q, references to the company, we, our, ours or us refer to Builders FirstSource, Inc. and its consolidated subsidiaries, unless otherwise stated or the context otherwise requires.

Cautionary Statement

Statements in this report which are not purely historical facts or which necessarily depend upon future events, including statements regarding our anticipations, beliefs, expectations, hopes, intentions or strategies for the future, may be forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended. All forward-looking statements in this report are based upon information available to us on the date of this report. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. Any forward-looking statements made in this report involve risks and uncertainties that could cause actual events or results to differ materially from the events or results described in the forward-looking statements. Readers are cautioned not to place undue reliance on these forward-looking statements. In addition, oral statements made by our directors, officers and employees to the investor and analyst communities, media representatives and others, depending upon their nature, may also constitute forward-looking statements. As with the forward-looking statements included in this report, these forward-looking statements are by nature inherently uncertain, and actual results may differ materially as a result of many factors. Further information regarding the risk factors that could affect our financial and other results are included as Item 1A of our annual report on Form 10-K.

COMPANY OVERVIEW

We are a leading supplier and manufacturer of structural and related building products for residential new construction in the U.S. We offer an integrated solution to our customers providing manufacturing, supply and installation of a full range of structural and related building products. Our manufactured products include our factory-built roof and floor trusses, wall panels and stairs, aluminum and vinyl windows, custom millwork and trim, as well as engineered wood that we design and cut for each home. We also assemble interior and exterior doors into pre-hung units. Additionally, we supply our customers with a broad offering of professional grade building products not manufactured by us, such as dimensional lumber and lumber sheet goods, various window, door and millwork lines, as well as cabinets, roofing and gypsum wallboard. Our full range of construction-related services includes professional installation, turn-key framing and shell construction, and spans all our product categories.

We group our building products into five product categories:

Prefabricated Components. Our prefabricated components consist of wood floor and roof trusses, steel roof trusses, wall panels, stairs, and engineered wood.

Windows & Doors. Our windows & doors category is comprised of the manufacturing, assembly, and distribution of windows and the assembly and distribution of interior and exterior door units.

Lumber & Lumber Sheet Goods. Lumber & lumber sheet goods include dimensional lumber, plywood, and OSB products used in on-site house framing.

Millwork. Millwork includes interior trim, exterior trim, columns and posts that we distribute, as well as custom exterior features that we manufacture under the Synboard[®] brand name.

Other Building Products & Services. Other building products & services are comprised of products such as cabinets, gypsum, roofing and insulation and services such as turn-key framing, shell construction, design assistance, and professional installation

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spanning all of our product categories.

Our operating results are dependent on the following trends, events and uncertainties, some of which are beyond our control:

Homebuilding Industry. Our business is driven primarily by the residential new construction market, which is in turn dependent upon a number of factors, including demographic trends, interest rates, consumer confidence, employment rates, foreclosure

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rates, and the health of the economy and mortgage markets. Over the past few years, many homebuilders significantly decreased their housing starts because of lower demand and an excess of home inventory. Due to the decline in housing starts and increased competition for homebuilder business, we have and will likely continue to experience pressure on our gross margins. Housing starts remain at low levels, but industry forecasters expect to see some improvement over the next few years. We also believe there are several meaningful trends that indicate U.S. housing demand will likely recover in the long term and that the current downturn in the housing industry is a trough in the cyclical nature of the residential construction industry. These trends include relatively low interest rates, the aging of housing stock, and normal population growth due to immigration and birthrate exceeding death rate.

Targeting Large Production Homebuilders. Over the past ten years, the homebuilding industry has undergone consolidation, and the larger homebuilders have increased their market share. We expect that trend to continue due to the enhanced liquidity and land positions of the larger homebuilders relative to the smaller, less capitalized homebuilders. Our focus is on maintaining relationships and market share with these customers while balancing the competitive pressures we are facing in our markets with certain profitability expectations. Our sales to the Builder 100, the country's largest 100 homebuilders, increased 42.6% compared to the first six months of 2011, while actual U.S. single-family housing starts increased 20.9% over that same time period. We expect that our ability to maintain strong relationships with the larger builders will be vital to our ability to grow market share and expand into new markets. We have also been successful in expanding our custom homebuilder base while maintaining acceptable credit standards.

Expand into Multi-Family and Light Commercial Business. We continue to look for ways to expand our multi-family and light commercial business to further diversify our customer base and lessen our dependence on single-family residential new construction.

Use of Prefabricated Components. Prior to the recent housing downturn, homebuilders were increasingly using prefabricated components in order to realize increased efficiency and improved quality. Shortening cycle time from start to completion was a key imperative of the homebuilders during periods of strong consumer demand. With the recent housing downturn, that trend decelerated as cycle time had less relevance. Customers who traditionally used prefabricated components, for the most part, still do. However, the conversion of customers to this product offering has slowed. We expect this trend to continue until the residential new construction market returns to more normal levels.

Economic Conditions. Economic changes both nationally and locally in our markets impact our financial performance. The building products supply industry is highly dependent upon new home construction and subject to cyclical market changes. Our operations are subject to fluctuations arising from changes in supply and demand, national economic conditions, labor costs, competition, government regulation, trade policies and other factors that affect the homebuilding industry such as demographic trends, interest rates, single-family housing starts, employment levels, consumer confidence, and the availability of credit to homebuilders, contractors, and homeowners. Over the past few years, the mortgage markets have experienced substantial disruption due to increased defaults. This disruption resulted in a stricter regulatory environment and reduced availability of mortgages for potential homebuyers due to an illiquid credit market and tighter standards to qualify for mortgages. Mortgage financing and commercial credit for smaller homebuilders continue to be constrained. As the housing industry is dependent upon the economy and employment levels as well as potential homebuyers' access to mortgage financing and homebuilders' access to commercial credit, it is likely that the housing industry will not significantly improve until conditions in the economy and the credit markets improve and unemployment rates decline.

Cost of Materials. Prices of wood products, which are subject to cyclical market fluctuations, may adversely impact operating income when prices rapidly rise or fall within a relatively short period of time. We purchase certain materials, including lumber products, which are then sold to customers as well as used as direct production inputs for our manufactured and prefabricated products. Short-term changes in the cost of these materials, some of which are subject to significant fluctuations, are sometimes passed on to our customers, but our pricing quotation periods may limit our ability to pass on such price changes. We may also be limited in our ability to pass on increases in in-bound freight costs on our products due to the price of fuel. Our inability to pass on material price increases to our customers could adversely impact our operating results.

Controlling Expenses. Another important aspect of our strategy is controlling costs and enhancing our status as a low-cost building materials supplier in the markets we serve. We pay close attention to managing our working capital and operating expenses. We have

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a best practices operating philosophy, which encourages increasing efficiency, lowering costs, improving working capital, and maximizing profitability and cash flow. We constantly analyze our workforce productivity to achieve the optimum, cost-efficient labor mix for our facilities. Further, we pay careful attention to our logistics function and its effect on our shipping and handling costs.

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CURRENT OPERATING CONDITIONS AND OUTLOOK

Though the level of housing starts remains near historic lows, the homebuilding industry has shown moderate improvements in recent quarters. According to the U.S. Census Bureau, the annualized rate for U.S. single-family housing starts at June 30, 2012 was 539,000, a 21.7% improvement from one year ago but approximately 63% lower than when the downturn began in 2006. For the current quarter, actual U.S. single-family housing starts were 152,200, a 23.3% increase compared to the second quarter of 2011. Actual single-family housing starts in the South Region, as defined by the U.S. Census Bureau and which encompasses our entire geographic footprint, increased to 77,400 in the current quarter, up 21.3% from the second quarter of 2011. The housing industry continues to struggle due to the limited availability of credit to smaller homebuilders and potential homebuyers, a slow economic recovery, excess home inventory and high unemployment rates, among other factors. The National Association of Homebuilders (NAHB) is forecasting 519,000 U.S. single-family housing starts for 2012, which is up approximately 19.4% from 2011, but still well below historical averages.

Our sales for the second quarter of 2012 were up 31.7% over the same period last year. We believe our broad offering of building products and construction services represents a value proposition to our customers that is superior to that of our competitors. We believe this allowed us to increase our sales volume at a rate in excess of the increase in residential new construction activity during the current quarter, as we gained market share by expanding our customer base and promoting our wide array of products and services to existing and new customers. However, our gross margin percentage decreased by 1.0 percentage point during the second quarter of 2012 compared to the second quarter of 2011. Our gross margin percentage decreased 1.7 percentage points primarily due to commodity lumber inflation relative to customer pricing commitments, which was partially offset by a 0.7 percentage point gross margin improvement due to increased sales volume. We have continued to manage our operating expenses with a key focus on conserving liquidity. Our selling, general and administrative expenses, as a percentage of sales, decreased 3.5% in the quarter compared to the same period a year ago. We have made significant changes to our business during the recent downturn that have improved our operating efficiency and allowed us to better leverage our operating costs against changes in sales. The continued execution of our cost containment strategies along with our improved operating results contributed to us ending the quarter with \$70.1 million of liquidity, consisting of \$105.1 million of cash reduced by the \$35.0 million minimum cash requirement in our term loan.

We still believe that the long-term outlook for the housing industry is positive due to growth in the underlying demographics. We believe we are well-positioned to take advantage of any construction activity in our markets and to continue to increase our market share. We will continue to focus on working capital by closely monitoring our credit exposure with our customers and by working with our vendors to improve our payment terms and pricing on our products. We will also continue to work diligently to achieve the appropriate balance of short-term cost reductions while maintaining the expertise to grow the business as market conditions improve. We want to create long-term shareholder value and avoid taking steps that will limit our ability to compete.

SEASONALITY AND OTHER FACTORS

Our first and fourth quarters have historically been, and are expected to continue to be, adversely affected by weather patterns in some of our markets, resulting in reduced construction activity. In addition, quarterly results historically have reflected, and are expected to continue to reflect, fluctuations from period to period arising from the following:

The volatility of lumber prices;

The cyclical nature of the homebuilding industry;

General economic conditions in the markets in which we compete;

The pricing policies of our competitors;

The production schedules of our customers; and

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The effects of weather.

The composition and level of working capital typically change during periods of increasing sales as we carry more inventory and receivables. Working capital levels typically increase in the second and third quarters of the year due to higher sales during the peak residential construction season. These increases have in the past resulted in negative operating cash flows during this peak season,

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which historically have been financed through available cash. Collection of receivables and reduction in inventory levels following the peak building and construction season have in the past positively impacted cash flow. In the past, we have also utilized borrowing availability under credit facilities to cover working capital needs.

RESULTS OF OPERATIONS

The following table sets forth, for the three and six months ended June 30, 2012 and 2011, the percentage relationship to sales of certain costs, expenses and income items:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Sales	100.0%	100.0%	100.0%	100.0%
Cost of sales	80.3%	79.3%	79.9%	79.9%
Gross margin	19.7%	20.7%	20.1%	20.1%
Selling, general and administrative expenses	20.2%	23.7%	21.5%	25.9%
Facility closure costs	0.0%	0.9%	0.1%	0.5%
Loss from operations	(0.5)%	(3.9)%	(1.5)%	(6.3)%
Interest expense, net	3.8%	2.8%	4.8%	3.1%
Income tax expense	0.1%	0.8%	0.1%	0.5%
Loss from continuing operations	(4.4)%	(7.5)%	(6.4)%	(9.9)%
Loss from discontinued operations, net of tax	(0.0)%	(0.0)%	(0.0)%	(0.0)%
Net loss	(4.4)%	(7.5)%	(6.4)%	(9.9)%

Three Months Ended June 30, 2012 Compared with the Three Months Ended June 30, 2011

Sales. Sales for the three months ended June 30, 2012 were \$271.9 million, a 31.7% increase from sales of \$206.4 million for the three months ended June 30, 2011. We achieved this increase in sales despite actual U.S. single-family housing starts increasing only 23.3% in the second quarter of 2012 as compared to the second quarter of 2011. In the South Region, actual single-family housing starts increased 21.3% during the second quarter of 2012 compared to the same quarter a year ago. We achieved increased sales volume across all product categories, as we continued to expand our customer base while increasing our sales to existing customers. We estimate that our sales volume increased approximately 29%, while commodity price inflation resulted in an additional 3% increase in sales during the current quarter compared to the same quarter a year ago. Commodity prices for lumber and lumber sheet goods were on average 24.8% higher in the current quarter compared to the same period a year ago.

The following table shows sales classified by product category (dollars in millions):

	Three Months Ended June 30,		Three Months Ended June 30,		% Change
	2012	% of Sales	2011	% of Sales	
Prefabricated components	\$ 51.2	18.8%	\$ 40.2	19.5%	27.4%
Windows & doors	59.3	21.8%	46.6	22.6%	27.3%
Lumber & lumber sheet goods	87.9	32.4%	60.7	29.4%	44.8%
Millwork	26.4	9.7%			