AC Smith

Water Heater Marketplace

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Water Heaters and Electric Motors
- 2007 Sales: $2.3B

Water Products Division
- 2007 Sales: $1.4B
- Water Heater Market Leader in U.S. & Canada
  - Residential & Commercial
  - Plumbing Wholesale & Retail
- Strong Position in China
  - $150M; Since 1996;
  - Growth ~ 30% / Year
- Small operation in Europe
- Entering India
U.S. Residential Water Heater Market

- 9 million units
- 50% Gas; 50% Electric
- 50% Retail; 50% Wholesale
  - Retail = more electric (more DIY)
  - Wholesale = more Gas (more DIFM)
- 80% Replacement; 20% New Const.
- 65% Emergency; 35% “Planned”
  - Most “planned” = fear of failure
U.S. Residential Water Heater Market

- Heavily Commoditized
  - A. O. Smith: over 4000 skus
    - Heavily concentrated in
      - Minimum efficiency 40 & 50 Gallon (gas)

- Large, relatively low value
  - Fills the truck
  - Takes up warehouse & “shelf” space
  - Plumbing Contractor carries only one
  - Heavy, difficult to install
U.S. Residential Water Heater Market

Obstacles and inertia in both channels
- Retail & Plumbing Wholesale
- Highly Competitive: Low margins
- Profitability dependent on “turns”
- Velocity is critical
- Channels respond to demand
  - Don’t drive it
U.S. Residential Water Heater Market

Consumer not engaged

- Doesn’t interact with water heater
- Doesn’t understand it
- Doesn’t know what it costs to run it
- Can’t replace it easily
- Scared of gas
- Scared of water
- A mystery
Market Research
Summary of Research Findings

- Decision Makers: Plumbing Contractors, Builders, Property Managers, Home Owners, Specifying engineers (influencers)
- Defined eight distinct purchasing segments
- Plumbing Contractors remain loyal to Wholesale Channel (91%)
- Plumbers desire to offer good, better, best options (71%)
- New Paradigm: Consumer (Home Owner) “Pull”
  - Proactive Residential Replacement = 37%
  - Home Owners driving Tankless Growth
  - Consumers (today) choose channel / outlet first; then brand
Engage the Consumer

Incentivize the decision maker / influencer

Facilitate distribution availability

Residential

Purchase Process

Consumer

Retailer

Plumber

Builder

Wholesaler

Mfg. Reps

Manufacturer

Engage the Consumer

Incentivize the decision maker / influencer

Facilitate distribution availability
A.O. Smith Vertex

- Unlimited hot water
- High efficiency water heating (90% TE)
- High output in small footprint (123 gal 1\textsuperscript{st} hr)
- Latest technology
- Electronic control
- Innovative Appearance
The case for higher value products

= GM$
Plumbing Industry Evolution

1946

$1089

2006
Plumbing Industry Evolution

1946

2006

$3900
Plumbing Industry Evolution

1946

$2500

2006
Water Heater Evolution

1946

2006

$212
Innovation has a name.