Reshaping of the Home Building Industry Reaches a Tipping Point

The common consolidation path for most industries has been a bifurcation of the market into “BIGS” and “SMALLS.” The largest players gravitate to a scale-driven business model that is defined by systems and processes that deliver low operating costs. Smaller players gravitate to niches, driving a business model that is based on product differentiation, a strong service orientation and leveraging relationships. This business model supports a higher cost market position—typically accompanied by higher price points. Companies in the “middle,” those that do not have sufficient scale to compete on a cost basis nor a clearly defined point of differentiation, typically disappear. Most often the businesses in the middle are acquired or driven out of a geographic market by the big players.

For many years, the home building industry resisted following this common consolidation path. The industry was defined by fragmentation—in homeowner demographics and product preferences, materials and labor supply, local building codes and construction practices. Fragmentation held any significant industry consolidation at bay…until now!

Consolidation is clearly emerging as the most important industry dynamic in 2024 and beyond. After averaging ~12 acquisitions annually since the housing crash in 2008, large builders have already announced eight acquisitions in Q1 2024. A “perfect storm” of factors will continue to support this trend:

- Large builders have stronger balance sheets than ever. These strong cash positions enable builders to be more aggressive in pursuing acquisitions. Strong balance sheets have also allowed builders to pivot back to spec homes and offer “Quick Move-in Inventory.” This fills a gap in the market for homes that are move-in ready that has been created by persistently low inventory of existing homes for sale.
- Large builders have healthy gross margins, brought on by a combination of construction efficiency (e.g., reduced cycle times) and stable material costs. This is allowing large builders to offer the incentives needed (e.g., mortgage rate buydowns; price discounts) to shore up buyer demand.
- Large builders have greater access to labor. The promise of more consistent workflow has enabled large builders to minimize labor disruptions that have plagued the industry for the last four years.
- Large builders are winning the battle for land. Given the scarcity of available lots, particularly in the most attractive geographic markets, large builders have been able to leverage their balance sheets, scale advantages and access to lower cost financing to gain access to a disproportionate share of available land.

For two decades (1997-2017), the top 20 builders held ~25% share of the market. Today, the share number is close to 40%. With a significant number of attractive regional builders still available, the top 20 are likely to reach 50% market share before leveling off.

Market Coverage Requires Multifaceted Sales Strategy

Where does all this lead?

Builder divergence must be addressed in a supplier's strategy. "BIGS" and "SMALLS" segments behave very differently in terms of buying processes, product and sourcing decisions, as well as how they approach contractor and channel relationships. As each customer segment is likely to be too big to ignore, a multifaceted sales strategy is a must.

THE "BIGS." This segment of the market will be defined by scale and efficiency. The typical large builder will enjoy a ~6-8 point operating cost advantage compared to small local independents. Contractor and channel relationships will contribute to the scale advantage, as national builders will increasingly gravitate to working with larger players. This dynamic is also likely to accelerate consolidation among contractors and distribution channels.
Your company's go-to-market approach with big builders should be *account-centric*, as each big builder is unique. Direct sales strategies will be critical to manage each big builder account and should encompass the builder's ecosystem that includes their contractor and channel partners. The "BIGS" segment prioritizes economics. They value manufacturer offerings and services that reduce their cost of doing business, as well as incentives that reward volume. Your greatest challenge may be to define account strategies that capture volume *and* deliver acceptable levels of profit to your business.
THE "SMALLS." The homebuilding market will continue to provide plenty of niches to allow the small independent builder to thrive. Be it geography (i.e., smaller, less dense areas that do not provide larger competitors sufficient scale), or type of home (i.e., custom/semi-custom), the small independent builder segment will continue to represent close to half the market. However, these builders will face ongoing challenges with the supply of both labor and materials and are likely to be working with smaller contractors and channel partners.
The ideal approach to the small builder segment will be *channel-centric*. Small builders are likely to have stronger relationships with local channels than with product brands. Strategies that engender channel loyalty and advocacy for your brand can leverage these builder/channel relationships. Advocacy will most likely be achieved through strong channel programs and channel management approaches that reward channel partners for activities and results they deliver for your brand. Channel management activities that help channel partners differentiate themselves in the local market are another way to build loyalty and spur effort.

We've helped many clients manage through industry consolidation and customer bifurcation. A proactive approach to finetuning your go-to-market strategy is required if your team wants to be prepared for the future industry structure. Now is the time to start this effort, and a good place to start would be an audit of your current approach: what is good/bad/missing relative to the needs of both the "BIGS" and "SMALLS."

We would be happy to discuss your situation and how to approach a go-to-market audit. Please contact Carl Cullotta at 224-239-2525 or cpc@lynncullotta.com. We look forward to talking to you soon.

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