National Remodeling Business Approaches: Preliminary Findings from Case Study Interviews

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Research Overview

• Most home improvement companies today are relatively small, single-location businesses that are unlikely to see significant growth over their life-cycle.

• Yet there are many examples of remodeling companies that have sought the benefits of scale and have been successful in establishing a large-scale or even national presence.

• This research seeks to better understand and document the various approaches that remodeling companies have used, or have attempted to use, to take advantage of scale economies and grow their business toward a national scale.
Even Payroll Contractors are Characterized by Smaller Firms

Number of residential remodeler establishments with payrolls (thousands) by annual receipts, 2007

Note: The number of general and special trade remodelers with receipts of $5 million or more is 1,400 and 2,300 respectively. Source: Unpublished tabulations of the 2007 Economic Census of Construction, U.S. Census Bureau.
The Remodeling Industry Remains Highly Fragmented Compared to Related Industries

Share of total receipts accounted for by the largest companies (Percent)

<table>
<thead>
<tr>
<th>Industry</th>
<th>Top 4</th>
<th>Top 8</th>
<th>Top 20</th>
<th>Top 50</th>
</tr>
</thead>
<tbody>
<tr>
<td>General Remodeling Contractors</td>
<td>2.5</td>
<td>3.4</td>
<td>5.2</td>
<td>7.9</td>
</tr>
<tr>
<td>Homebuilders</td>
<td>15.6</td>
<td>24.1</td>
<td>34.4</td>
<td>42.4</td>
</tr>
<tr>
<td>Building Material Supply Dealers</td>
<td>45.9</td>
<td>50.1</td>
<td>53.5</td>
<td>56.5</td>
</tr>
</tbody>
</table>

Sources: JCHS tabulations of the 2007 Economic Census and Builder magazine’s 2007 Builder 100 list.
Research Advisory Committee Participants

- Scott Baker, Paul Davis Restoration
- Charlie Chase, CertaPro Group
- Chris Edelen, LeafGuard by Beldon
- Murray Gross, US Home Systems
- Rob Levin, Statewide Remodeling
- Larry Meadows, American Exteriors
- Kevin O’Neill, Wellborn Cabinet
- Pat O’Toole, Professional Remodeler Magazine
- Mark Richardson, Case Design/Remodeling
- Tom Seibert, Paul Davis Restoration
- Seymour Turner, Hanley Wood Business Media
Main Research Questions

• What approaches or strategies have been used by remodeling companies, both successful and unsuccessful, for gaining scale?

• For each type of approach, what are the unique challenges, opportunities, and benefits of scaling?

• Are certain types of remodeling specialties or market niches more likely to attempt to establish a larger-scale or national presence?

• What are the particular conditions that allowed for scaling toward a national presence, and what conditions posed challenges to scaling?
Perceived Benefits of Economies of Scale in the Remodeling Industry

• Economies of scale refers to the various cost advantages that an enterprise obtains through expansion of their business.

• Benefits of scaling include improved costs of:
  – Purchasing
  – Marketing
  – Overhead
  – Financial

  ➢ End result is a more efficient and competitive business with increased profit for reinvestment
Larger-Scale Remodeling Firms Report Higher Revenue per Employee, Implying Greater Labor Productivity

Average construction receipts per employee for residential remodeling establishments (000s), 2007

Major Obstacles to Scale in the Remodeling Industry

- Low barriers of entry
- Inherent volatility of the construction industry
- Very customized work
- Craftspeople vs. businesspeople
- Difficult to attract capital
Main Approaches for Gaining Scale

• Organic/Traditional Growth

• Venture Capital

• Franchising and Licensing

• Manufacturer and Dealer Partnerships

• Installed Sales Programs with Manufacturers, Dealers and Retailers
Preliminary Findings: Venture Capital

• With addition of human and financial capital, can expand into new markets and become relevant very quickly without long incubation period for name and brand recognition

  – Investors attracted to established business with proven model for “scalability and portability”
  – **Benefits:** investors provide knowledge, specialized skill sets and business experience in addition to financial capital
  – **Challenges:** investors usually want controlling interest and sometimes difficult to make transition with founder
Preliminary Findings: Franchising/Licensing

• Franchising is much more likely to be a successful strategy if the type of business is well-defined and doesn’t include too many variables or possibility for variations.

  – Specialty remodeling more likely to use this approach
  – **Benefits**: expand brand recognition without managing each location
  – **Challenges**: transferring company values and culture
Preliminary Findings: Manufacturer Partnerships

- Preferred contractor programs are mutually beneficial arrangements in which the manufacturer can leverage its size and resources to improve the business of their remodeling partners

  - **Benefits**: remodeling companies receive unique distinction that differentiates their business, as well as much needed business support
  - **Challenges**: Need to specialize business
Preliminary Findings: Installed Sales Arrangements

• Strategic alliances with major retailers to sell, furnish and install are crucial for lead generation and make expansion into new markets fairly easy

  – **Benefits:**
    • Instant name recognition with trusted brand
    • Leads have very high conversion rate
    • Don’t need to test new markets

  – **Challenges:**
    • Working through corporate hierarchy
    • Jobs are not as profitable as working on your own
Takeaways:

• The remodeling industry has many unique obstacles to gaining scale, but remodeling companies are finding a variety of benefits to scale.

• There is no one-size-fits-all approach to scale in the remodeling industry.

• Peer networks and business associations are invaluable at every stage of scaling a business.

• Common consensus that future prospects for widespread consolidation in the remodeling industry remain low.
Next Steps:

- Continue conducting interviews with case study companies.

- Write-up findings as a series of case studies: summarize lessons learned from examples of efforts to establish a more concentrated presence in the home improvement industry.