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INDUSTRY STRUCTURE AND LABOR TRENDS

Traditionally comprising many small businesses, the residential remodeling industry became even more fragmented during the sharpest downturn on record. Indeed, the severity of the recession put many contractors out of business and reduced some of the consolidation gains achieved by larger-scale firms during the boom years. Now more than eight years after the financial crisis and Great Recession, the industry is nearing full recovery in terms of both employment levels and overall spending on home improvements and repairs.

CONTINUED INDUSTRY FRAGMENTATION

During the housing and home improvement boom years of 2002–2007, the total number of residential remodelers—defined as businesses with more than half of their annual receipts from remodeling and repair activity, and including both self-employed contractors and payroll firms—swelled by nearly a quarter from 530,000 to over 650,000 **(Figure 11).** This comprehensive measure includes general contractors (full-service, design/build, handyman repair, and insurance restoration) and those in specialty trades (such as roofing, siding, windows, plumbing/HVAC, electrical, and painting).

Moreover, the number of remodeling establishments continued to grow during the subsequent downturn in 2007–2012, increasing almost another 10 percent to 716,000. Self-employed contractors accounted for nearly all (over 88 percent) of this growth, driven largely by the movement of former payroll employees to self-employment and by the conversion of smaller payroll companies to non-employer status. Smaller-scale homebuilders that refocused on the remodeling market during the worst years of the housing slump were another source of growth.

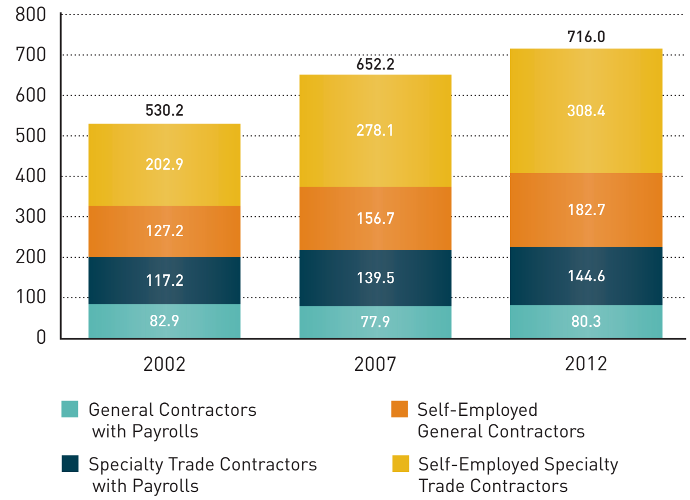
Self-employed contractors have always made up the majority of remodeling businesses, with their share rising from about 62 percent in 2002 to 69 percent in 2012. The vast majority—almost three out of four—were small operations with receipts under $100,000 in 2012. But even contracting firms with payrolls are primarily smaller-scale operations, with almost a quarter generating revenues under $100,000 in 2012 and another 30 percent with revenues between $100,000 and $249,999.

Meanwhile, the share of payroll remodeling establishments with $1 million or more in annual revenue declined somewhat during the downturn from 14.8 percent in 2007 to 13.0 percent in 2012 **(Figure 12).** Still, large-scale remodelers were respon-

Figure 11

The Number of Remodeling Businesses Continued to Expand During the Downturn

Residential Remodeling Establishments (Thousands)



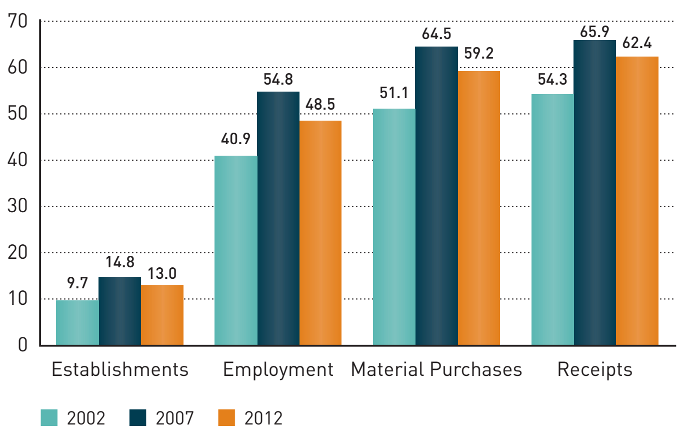
Notes: Data include establishments with more than 50% of receipts from remodeling activity (including maintenance and repair) and self-employed remodeling contractors with annual revenues of at least $25,000.

Source: JCHS estimates based on unpublished tabulations of US Census Bureau, Economic Censuses of Construction and Nonemployer Statistics.

Figure 12

The Largest Remodelers Lost Some of the Ground Gained During the Boom

Industry Shares of Remodelers with Annual Revenues of $1 Million or More (Percent)



Notes: Data include payroll establishments with more than 50% of receipts from remodeling activity (including maintenance and repair). Annual revenue is not inflation-adjusted.

Source: JCHS estimates based on unpublished tabulations of US Census Bureau, Economic Censuses of Construction.

sible for significantly higher shares of employment, material purchases, and industry receipts in 2012 than in 2002. In addition, there is evidence of increasing concentration of industry receipts among the very largest general contracting firms, with the top 50 remodelers' share rising from 5.2 percent in 2002 to 7.9 percent in 2007 and to 8.5 percent in 2012.

Remodeling companies that are able to overcome the many obstacles to scale economies realize considerable benefits. Joint Center research indicates that in addition to the typical advantages thought to accrue as companies increase in size (including lower costs of materials, marketing, capital, and overhead), larger-scale remodeling firms also see stronger growth in revenues. Indeed, while average remodeling receipts for both smaller-scale (annual revenue under $250,000) and mid-size (annual revenue from $250,000 to $999,999) payroll firms declined somewhat between 2002 and 2012, the average revenue of larger-scale establishments with $1 million or more in annual revenue was up 4.5 percent.

Larger-scale remodelers also have substantially higher revenues per employee, which suggests greater labor productivity. In 2012, average remodeling receipts per payroll employee at large firms were 50 percent higher than those of mid-size remodelers and more than 140 percent higher than those of smaller-scale firms. Comparing average construction receipts net of costs for materials, payroll, and subcontracted work (the residual being profit and overhead costs) and assuming that their fixed overhead costs account for a comparable share of revenues, larger-scale remodeling companies likely generated significantly higher profits per employee as well.

BUSINESS SURVIVORSHIP TRENDS

The number of general remodeling businesses with payrolls climbed steadily from 80,000 in 2012 to an estimated 87,000 in 2016—an increase of over 9 percent. However, the annual net change in the number of firms masks considerable churn in the remodeling industry. High rates of business openings and closing are also evident in the broader residential construction sector **(Figure 13).** Between 2003 and 2013, the annual net change in the number of homebuilding and remodeling businesses with payrolls ranged from -13.3 percent in 2008–2009 to 6.1 percent in 2003–2004. On average, however, 18.4 percent of payroll firms were newly opened each year while another 18.9 percent closed. The high rate of residential building business startups and dissolutions is largely the result of low barriers to entry and challenges to achieving scale economies.

Business exit rates in the residential remodeling industry are high. For example, during a period of relatively healthy consumer spending on home improvements in 2003–2004, 12.9

percent of general remodelers with payrolls ceased operations, compared with 10.2 percent of all payroll businesses in the United States. Relatively high "failures" clearly contributed to growing industry fragmentation during the downturn in 2007–2012, with smaller remodelers much more likely to exit, fail, or move to self-employment. Among the smallest firms with payrolls in 2007 (under $100,000 in receipts), more than 70 percent were no longer operating as payroll businesses five years later. Overall, fully half of all remodelers with payrolls either closed their businesses or moved to self-employment during this period.

In contrast, larger firms were much more likely to stay in business **(Figure 14).** More than 68 percent of general remodelers with receipts of at least $1 million in 2007 were still in operation five years later, compared with less than 38 percent of remodelers with revenues under $250,000. The larger size of surviving firms provided critical cushioning, given that almost half were able to remain in business even as their receipts dropped by 25 percent or more. Another 16 percent of surviving remodelers experienced smaller declines in revenue in 2007–2012, but declines nonetheless. The rest of the firms that remained in business over this period—about 40 percent—were able to restructure or otherwise take advantage of reduced competition to increase their revenues during the worst industry downturn on record.

CHANGING WORKFORCE SIZE AND CHARACTERISTICS

After a 23 percent drop between 2007 and 2010, the number of payroll employees at general remodeling contractors has risen steadily and is once again nearing peak levels. By 2016, payroll employment at remodeling firms had returned to an estimated 307,000, a gain of almost 31 percent since the 2010 trough.

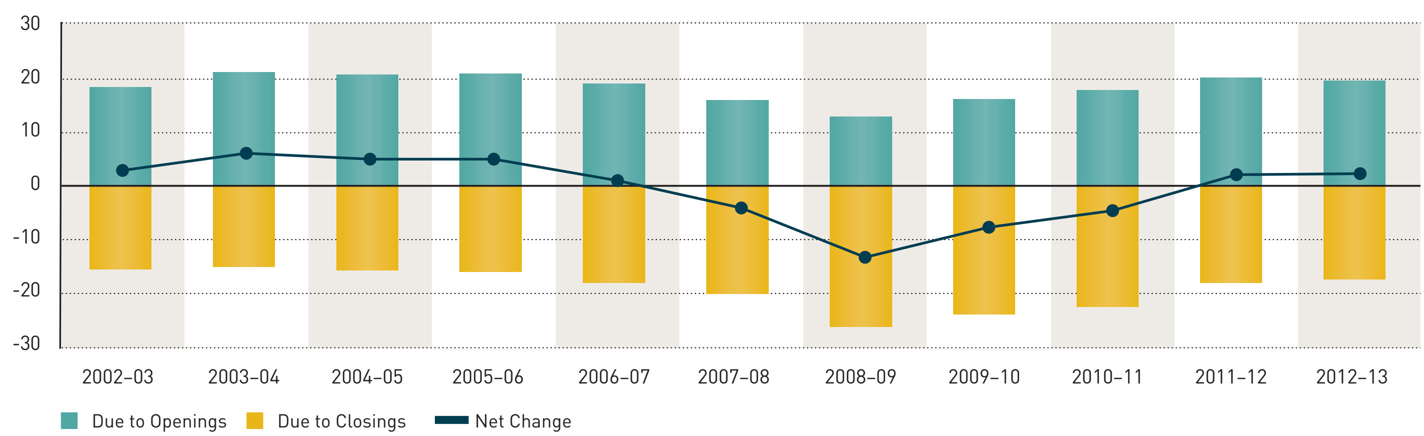
Hourly wages for nonsupervisory employees have also been rising, with growth in year-over-year wages accelerating since the third quarter of 2015. Indeed, average wage growth picked up from 2.2 percent in 2015 to 5.2 percent in 2016, driven by shortages of skilled labor. Not surprisingly, analysis of survey data from *Qualified Remodeler* publication's Top 500 Remodelers found that the share of large firms that consider finding and hiring qualified employees their biggest business challenge increased from 29.5 percent in 2015 to 33.6 percent in 2016.

Around the time of the home improvement market peak in 2007, the number of people with onsite management or trade occupations in the construction industry—including both payroll and self-employed workers, as well as those who were unemployed but looking for work—was over 9.0 million. Five years later, after the Great Recession, that number had dropped by 1.8 million, reducing the size of the construction labor force by 20 percent.

Figure 13

In Any Given Year, About One in Five Residential Construction Businesses Opens And Another One in Five Closes

Change in Number of Residential Building Establishments with Payrolls (Percent)



Source: US Census Bureau, Business Information Tracking Series.

Some of these lost workers likely took early retirement from more physically demanding trades such as framing or roofing. As for immigrants, who have long made up a disproportionate share of the construction workforce, some returned to their home countries after the crash. Many other workers looked to retrain or go back to school with the goal of switching occupations and industries. Indeed, a 2015 Census Bureau analysis estimates that this was the fate of about a third of construction payroll employees displaced by the housing bust. At last count in 2015, the construction trades workforce still held at the 2012 level of 7.2 million, but their unemployment rate was down sharply from 14.2 percent to 7.9 percent.

Meanwhile, the demographic characteristics of the construction management and trades workforce changed markedly. During the downturn, younger, less experienced workers were let go first, and if construction firms were hiring at all, they tended to take on older, more experienced workers. As a result, the share of workers age 55 and over rose from 11.1 percent in 2007 to 15.8 percent in 2012. At the same time, the number of workers under age 35 declined by nearly 1.3 million, and their share of the workforce shrank from about 41 percent to 33 percent. By 2015, the share of older workers ticked up to 16.8 percent—fully one in six workers—but the number and share of younger workers were unchanged from the 2012 trough. These trends, combined with the long-term decline in federally registered apprenticeship programs (from about 33,000 in 2001 to 21,000 in 2015), have contributed to the aging of the construction workforce.

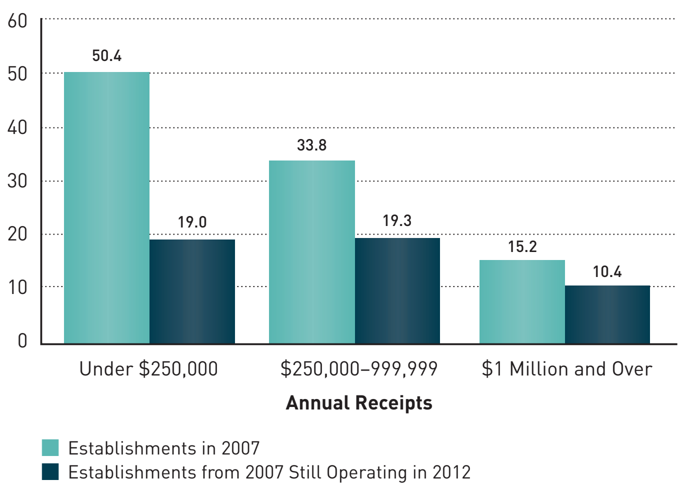
As the industry shed a disproportionate share of younger, less experienced workers, the characteristics of construction workers under age 35 changed **(Figure 15).** Reflecting broader demographic shifts, the minority share of younger workers increased from 39 percent in 2002 to 47 percent in 2015. At the same time, however, the share of younger workers that were immigrants remained unchanged after 2012 at 29 percent. Overall, younger workers in the construction industry today are better educated, with the share holding a high school diploma or GED increasing from 65 percent to 74 percent between 2002 and 2015.

Although women still make up just a fraction of the construction management and trades labor force (less than 3 percent in 2015, compared with 47 percent of the national workforce), their share of younger workers edged up slightly from 2.2 percent to 2.8 percent after the recession. Employers in the construction and remodeling industries will need to make concerted efforts to attract younger employees and workers from traditionally underrepresented segments, including women, to ensure that they have an adequate supply of labor.

Figure 14

Large Residential Remodelers Were Much More Likely to Weather the Downturn

Payroll Establishments (Thousands)

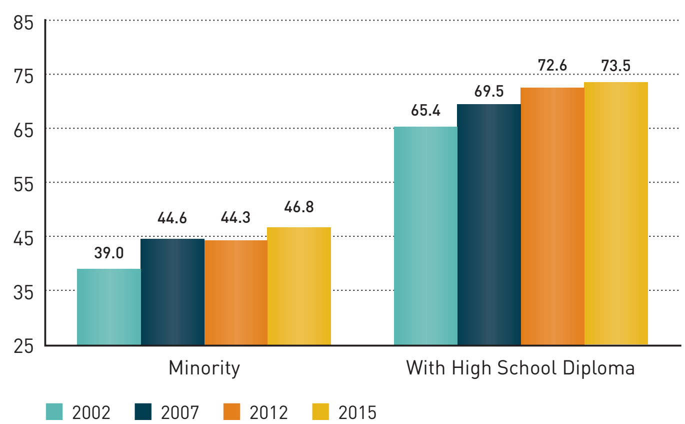


Source: US Census Bureau, Business Information Tracking Series.

Figure 15

Younger Workers in the Construction Labor Force Today Are More Diverse and Better Educated

Share of 16–34 Year Olds in the Workforce (Percent)



Notes: Data include workers housed in nongroup quarters that are either employed or unemployed but available for and seeking work. The construction labor force includes workers with construction management and trades occupations in the industry.

Source: JCHS tabulations of US Census Bureau, American Community Surveys 1-Year Estimates.

THE OUTLOOK

The home remodeling industry became more fragmented during the course of the last business cycle with strong growth in the number of firms, particularly of self-employed remodelers. Still, larger-scale firms continue to account for significant shares of industry activity as measured by revenues, material purchases, and employment. This concentration of activity provides a considerable competitive advantage, including the ability to weather difficult market conditions and large declines in revenues.

Remodeling firms may never reach the same level of consolidation as related industries such as homebuilding, but the growth of mid-size companies into larger-scale firms and the concentration of industry activity among the largest firms are likely to continue. Clearly, remodeling companies that are organized, differentiated, and focused on brand-building will pursue opportunities to capture market share and expand their businesses. The potential benefits of consolidation include improved operating efficiencies, stronger negotiating positions with suppliers, and increased revenues and profits to help buffer against market downturns.

Employment at general remodeling firms is once again nearing peak levels, but the construction management and trades workforce is significantly smaller than during the housing boom. This suggests that labor shortages will remain a serious issue for the industry. Key demographic characteristics of the construction labor force, such as age, race, and education or training, have also changed. Going forward, the construction industry must give new priority to workforce training in order to rebuild the ranks of younger workers who were either shut out during the protracted downturn or require more skills to compensate for the on-the-job experience they otherwise would have received.