

Tomorrow's Management Mandate Today

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I. The Home Builder's Prayer:

“Dear God, please let there be one more housing boom and I promise I will not piss it away. Amen”

II. We have had a Wonderful Fourteen (14) Year run of Fantastic Housing Demand.

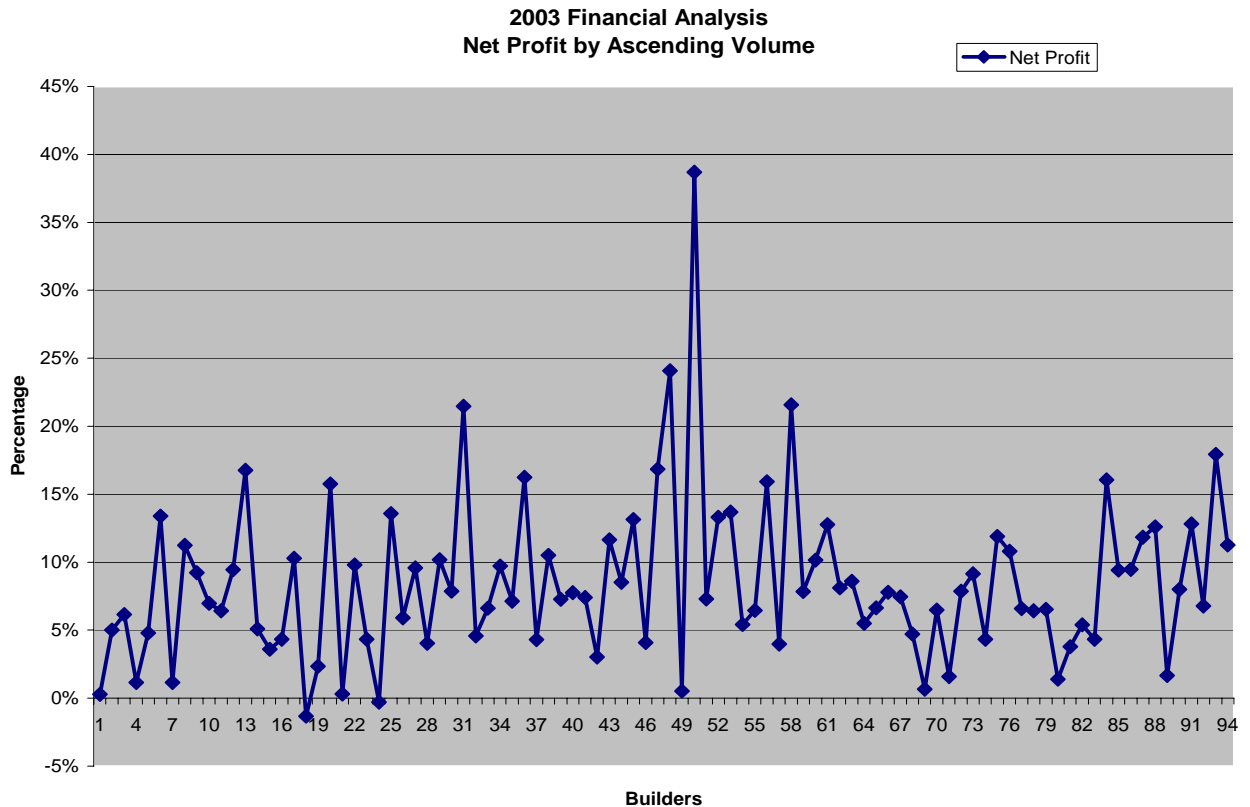
- A. Two Consecutive Record-Breaking Years.
- B. Has Violated *ALL* Historic Economy Patterns
 - Low Interest Rates
- C. Home Ownership Rate at an *ALL* Time High
 - Possibly borrowing Sales from the future
- D. Housing Prices have Risen Dramatically
 - Covering our Inefficiencies
 - Housing Affordability
 - Housing Bubble
- E. Rapid and Substantial Growth
 - Growth through Debt
 - Very Little Working Capital
 - Focused on the Top Line NOT the Bottom Line
 - High Speed Wobblies
 - Management Systems Broken

III. Looking at the World through Rose Colored Glasses

- The “Midas Touch” Syndrome
- Many Builders have *NEVER* Experienced a Downturn
- Seasoned Builders seem to have *FORGOTTEN*
- The Old Economic Model is Broken and there *WILL NOT* be another Housing Cycle.

IV. Profits are Still Low

- Have to Work Hard to Lose Money in this Market
 - Many Builders have Figured Out How!
- The Haves and the Have-Nots (34% below 5% net profit)



V. Accumulated a lot of Fat and Inefficiencies

- **Systems**
- **Direct Construction Costs**
- **Schedules**
- **Staffing**
- **Operating Expenses**

VI. We are at a Crossroads.

- **We might add another year or two to this record housing boom (Duration & Demand) or**
- **We could be at the beginning of a downturn for housing demand**
 - **Steep and Short**
 - **Shallow and Long**
- **What are the Odds?**
 - **Economy has a good head of steam**
 - **Labor market continues to increase**
 - **Inflation is back**
 - **Interest rates are increasing**
 - **Terrorist Threat**
 - **High Oil Prices**
 - **Weak Dollar**
 - **High Federal Government Deficit**
 - **High Consumer Debt**

VII. *NOT* prepared for a Slowdown

- **High Land Inventories**
- **Bloated Operating Costs**
- **Little Cash Reserves**
- **High Leverage**

- **Inefficient Construction**
- **Extended Schedules**

VIII. Mentally *NOT* Ready

- **Won't make the necessary decisions early enough**
- **Denial = Catastrophe**

IX. WHAT SHOULD I DO?

Get your House in Order!

Don't Wait Too Long!

*Proactive **NOT** Reactive*

X. Develop a Survival Strategy Now!

A. Establish Three Pre-Planned Scenarios and Budgets

- **Based on Three Sets of Economic Assumptions**
- **Project out for a Rolling Four Quarters**
- **Establish Criteria for Implementation of each Plan**

B. What is your Survival Power (*HOLDING POWER?*)

- **Length of time you can hold out under worst case scenario**
- **Assumes no further Contracts or Sales**
- **Only Income from Closing of Present Sales on Books**
- **Should be at least 2 ½ to 3 months of Operation**

C. Build a Rainy Day Fund

- **Keep it Liquid**
- **Don't Invest in Construction Loans, or Real Estate**

XI. Manage Your Risk

- **Don't Bet the Farm**
- **Keep Flexible**
- **Don't Grow Too Fast**
- **Geographical Diversification is *VERY* Risky**
- **Improve Cash Flow Projections**
- **Maintain a Minimum Level of Liquidity**
- **Reduce Leverage**
- **Close Unprofitable Operations**
- **Get Rid of Low Gross Profit Product**
- **Watch your Speculative Inventory**
- **Don't become a Land Hog**
- **Improve your Gross Profits**
- **Get Rid of Bad Deals**
- **Watch your Bottom Line**
- **Don't be Volume Greedy**
- **Keep your Breakeven Point Low**

XII. Maintain Sales Velocity

- **Set Prices to Market**
- **Adjust Construction Costs to obtain Target Gross Margin**
- **Costs *DO NOT* create Value**
- **Target Market**
- **Develop a Realtor Program**

XIII. Reduce Construction Costs

- **Maintain Construction Costs at 50% or less of Sales Price**
- **Analyze and Reduce Standard Specifications**
 - **Understand Customer Perceived Value**
 - **Conduct Customer Research**
 - **Don't Over do a Standard Feature**
 - **Put your Money In High Perceived Value Items**
- **Eliminate Waste and Excess Material Usage**
 - **Police your Trash Piles**
 - **Eliminate Excess Material Usage**
 - **Watch Diverted Materials**
- **Monitor and Eradicate Variances**
- **Develop Scopes of Work for Trades**
- **Conduct "as-built" Audits**
- **Value Engineer Plans**
- **Improve Estimating and Purchasing**
- **Implement a True Purchase Order System**

XVI. Reduce Cycle Times and Improve Inventory Turn

- **Improve Construction Schedules**
 - **Master Construction Schedules**
- **Schedule Pre-construction Activities**

XV. Improve Efficiency

- **Improve Processes**
- **Improve Systems**
- **Standardize Procedures**
- **Reliable and Consistent**
- **Efficient and Effective**
- **Get Rid of Non-Valued Added Activities**

XVI. Develop Good Control and Management Reports

- Design from Bottom Up and Top Down
- Two Minute Management Reports
- Variance Reports
- Not Data Dumps
- Reports have a Purpose

XVII. Balance Operating Expenses with Sales Volume

- Watch Staffing Levels
- Invest in Systems *INSTEAD* of People
- Analyze Processes for Efficiency

XVIII. SUMMARY

Now is the time to be proactive in developing a strategy for survival for a potential downturn. Maybe it won't come, but failure to plan could spell disaster. It is much better to be proactive than reactive.

If you wait too long you will be in denial, delay critical decisions and risk the possibility of becoming another statistic in the annals of Homebuilder failures.

Hopefully it is not too late.