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Analysis: Homebuilders buying land despite falling sales

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By [Helen Chernikoff](#)

NEW YORK (Reuters) - Homebuilders in the United States, who lost hundreds of millions of dollars when land they bought during the housing boom lost value after the bust, are bidding up lots despite new softness in the market.

Home sales have slumped since the federal home buyer tax credit expired in April. In July, new home sales were at their slowest pace since the Commerce Department started tracking them in 1963.

But builders keep restocking land inventories because they fear shortages and because they see rivals doing it, said industry consultant John Burns, who has been advising them to "back off for now."

If demand for new homes does not revive, these lot purchases could jeopardize profitability into 2012, when they would build on land they are currently buying.

Falling home prices would mean they are overpaying today, especially because they are increasingly focused on the same markets, where they are cannibalizing each other's business.

The economy softened more than anybody anticipated, Burns said. He and the rest of the industry is well aware economists would have builders stop altogether rather than add to the already excessive supply.

"But builders need to build enough to justify their existence," Burns said.

TIE IT UP

Some industry consultants and land brokers say the pace of land purchases has slowed, but not significantly.

Land deals are still drawing multiple offers, although the number has dropped, said Greg Vogel, Chief Executive Officer of brokerage Land Advisors, which operates in Arizona, California, Nevada, Florida, Texas and other states.

Tom Dallape of the Hoffman Company, a brokerage in California and Nevada, said he has done as many deals this year as last year. Land prices have fallen, but not by much, he added.

"A lot of these guys have been working on these deals for the last 120 days and still have corporate mandates to go out there and find land and tie it up," said broker Ryan Arp of Westland Properties Group in the Phoenix area.

No. 1 builder D.R. Horton Inc (DHI.N: [Quote](#), [Profile](#), [Research](#), [Stock Buzz](#)) has lots under contract there, as does Beazer Homes USA Inc (BZH.N: [Quote](#), [Profile](#), [Research](#), [Stock Buzz](#)). Hovnanian Enterprises Inc (HOV.N: [Quote](#), [Profile](#), [Research](#), [Stock Buzz](#)) has been active there as well, Arp said.

Horton did not respond to a request for comment.

"We probably tied up more land this quarter than in the second quarter in terms of total lots," said Hovnanian Chief Financial Officer Larry Sorsby.

In the last month, some builders have started to try to spread the risk by teaming up on big land deals, said Richard Gollis of The Concord Group, a real-estate consulting firm.

HUNKERING DOWN

But Ticonderoga Securities analyst Stephen East said there is far more talk about cooperative buying than actual deals.

The big builders "are bidding against each other. We are disappointed with the builders' lack of discipline," he said.

If the builders have stopped buying land at all, it is in smaller markets and on the periphery of larger ones.

Hovnanian, for example, will no longer buy land if it is an onerous commute from the nearest job center, Sorsby said.

KB Home (KBH.N: [Quote](#), [Profile](#), [Research](#), [Stock Buzz](#)) is leaving Charleston, South Carolina, spokesman Cara Kane said.

And on the grounds they are leaving Jacksonville, Florida, Beazer declined to be listed in the local business journal's directory, according to an article in the Jacksonville Business Journal.

Beazer did not respond to repeated requests for comment.

"All of them are evaluating whether to leave the smaller markets," said East, calling more withdrawals "inevitable."

A MISSED OPPORTUNITY

The combination of ongoing land purchases and a focus on the same prime markets, such as Phoenix, Las Vegas, the mid-Atlantic region and parts of California, is causing builders to bid up lot prices now, as East said.

"There are very few markets that generate the volume that you need to justify a division," Gollis said. "Public builders have been competing against each other for land positions."

Builders divide their business up into geographical divisions if the volume of business merits an office, staff and a division head.

Because key positions will be so crowded with public builders, it will force them to compete on price, which will pinch margins and hurt profits.

"The number of buyer profiles you can sell to is pretty limited," said Jim Belfiore, the president of a real estate consulting firm in Phoenix. "They're competing for entry-level and lower first move-up buyers. They're really they're competing head-on."

What is more, East said, the builders "are missing a golden opportunity to enter attractive markets when private competitors are flat on their backs" because banks still will not loan to them.

Most builders do not want to take the risk of starting a new division, East said, and some have told him they do not have the skills required to do so.

Ultimately, more big builders in fewer markets will produce winners and losers. In addition to departures from smaller markets, Burns expects some of the big players will have to leave the big markets, too.

"Do we need twelve public homebuilders in Riverside-San Bernardino?" Burns asked of a prime market in California. "Right now it can't justify that many companies. But nobody's willing to leave so, yes, they're just going to beat each other up in Riverside-San Bernardino for a while."

(Reporting by Helen Chernikoff; editing by [Andre Grenon](#))

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