

## L.E.K. Contractor Behavior Survey: The Building-Products Industry is Gaining Strength

After a period of considerable decline following the 2008 housing crash, the U.S. building and construction market is back in good health. Recently approved housing starts have recovered substantially and are on the way to approaching pre-crash levels. In the fourth installment of our annual Contractor Behavior Survey, L.E.K. Consulting found that contractors report strong year-over-year improvement in the number and dollar value of jobs, and predict that by 2016 their businesses will be healthier than before the market cycle.

Our survey of 550 residential and commercial contractors in the U.S. also revealed that renewed optimism is changing contractors' behavior in various ways; first, they are becoming more aggressive during pricing negotiations and are walking away from jobs that don't provide attractive margins; second, contractors' purchasing from big-box retailers are showing signs of plateauing and they are favoring one-stepper and broad-line specialty channels; finally, they are increasingly integrating mobile devices and tablets into their work and anticipate accelerating their use of mobile software and apps in the future.

To better understand contractor preferences, L.E.K. also asked contractors to rate manufacturers across 12 categories in order to identify the manufacturers viewed as highest performing and thus likely to command loyalty from contractors.

In this paper, we summarize the main findings from the survey and examine their implications for building-products manufacturers.

### Contractors Are Growing Their Margins

Continuing a trend we identified in previous surveys, contractors in 2013 indicated fewer jobs lost on price and claim they are now busy enough to turn down low-margin jobs. In fact, contractors' bullishness about pricing is the highest it has been in four years (see Figure 1). For instance, while 44% of respondents reported in 2010 that they were reacting to price pressure by accepting lower margins on jobs, only 26% reported dropping their prices in 2013. Approximately four out of 10 contractors in our survey reported performing extra services on a job to maintain their price – around the same proportion that reported that they are simply selecting fewer jobs that are more attractively priced.

### Contractors Remain Loyal To Brands

When choosing products, contractors continue to value their trusted brands in most building-products categories rather than purchase less expensive alternatives by other manufacturers – a loyalty that remained “sticky” even through the worst of the

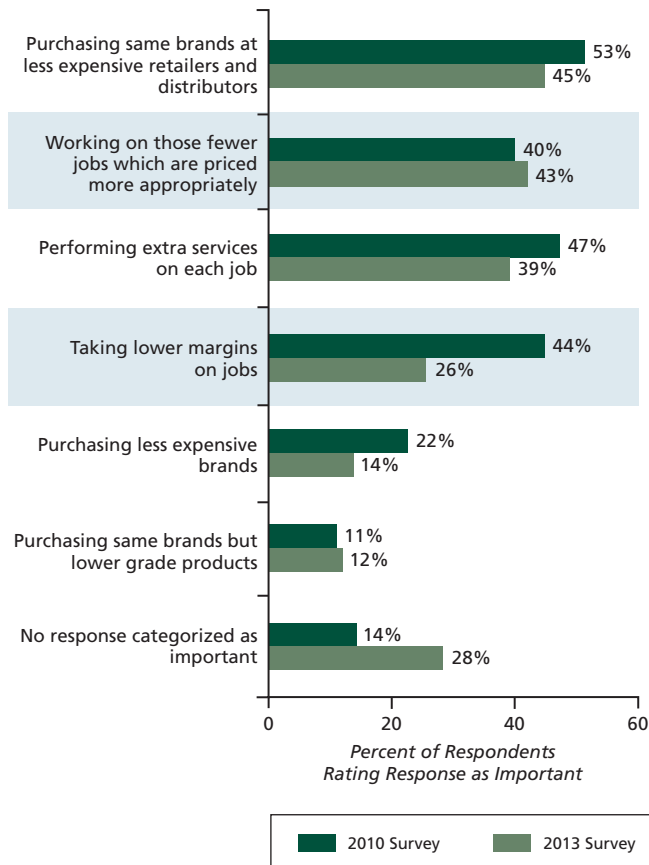
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Figure 1

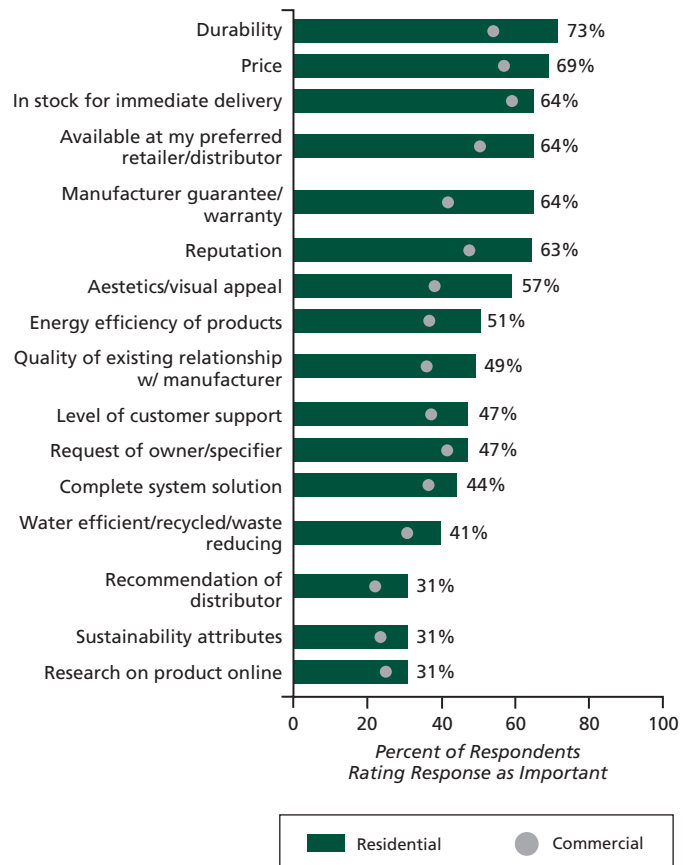
Contractor Responses to Price Pressure



Source: L.E.K.'s Contractor Behavior Survey

Figure 2

Contractor Product Purchase Criteria Importance (2013)



Source: L.E.K.'s Contractor Behavior Survey

downturn. Continuing a trend noticed in past surveys, contractors also continue to decrease their searches across multiple retailers and distributors for the lowest prices for their favored products – another sign of resurgence in the industry as well as brand loyalty. The importance of using trusted brands reflects contractors’ belief that durability is the most important quality in a product, with related attributes such as product reputation and strong warranty also among the top 10 product-selection considerations (see Figure 2).

Price remained a significant consideration for contractors during purchasing, but ran second to durability, as it has in all

four L.E.K. contractor surveys. Notably, a “green” or environmental value proposition did not turn out to be a key purchasing criteria for most contractors, ranking eighth on the list of product-selection considerations behind attributes such as visual appeal (seventh), availability at a preferred retailer (fourth), and whether the product is in stock and obtainable immediately (third). When contractors do seek green attributes in their products, they generally favor energy efficiency over sustainability. This preference is the result of homeowners, who contractors estimate could pay as much as a 10% price premium on a product if its efficiency benefits drive a payback period of fewer than five years.

## Big-Box Retailing Has Plateaued While Online is Growing

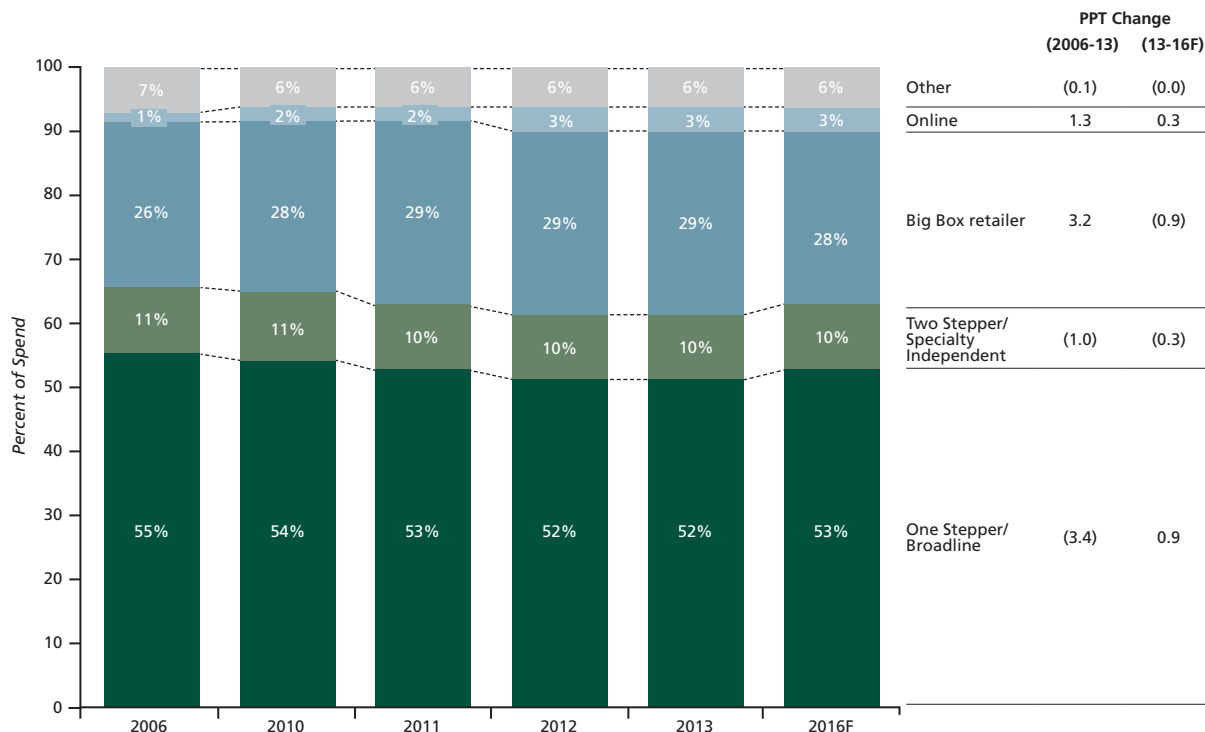
As in previous L.E.K. surveys, contractors stated price and convenience as the primary reasons for shopping at big-box stores, but professed no loyalty to these outlets, complaining that the big-box channel was underperforming on other services relative to the pro channels (one-stepper and two-steppers). Specifically, contractors felt big-box stores lack knowledgeable staff, a reliable delivery service, depth of product selection and several other valuable attributes.

Indeed, our data suggests the trend toward purchasing at big-box retailers seems to have reached its apex in most categories (see Figure 3). Contractors are moving back to one-steppers and two-steppers because those channels offer premium products with better pro services and also because contractors are find-

ing more success selling such products to homeowners in a rebounding market. Finally, big-box retailers, with their convenient locations, provided a de facto outsourced inventory for contractors during the downturn. Given the uptick in projects, however, contractors are moving through inventory more quickly and are thus less concerned about tying up working capital. The benefit of the localized inventory of the big-box is now competing with the cost of sending crews (which could otherwise be productive) out to the stores at a greater frequency.

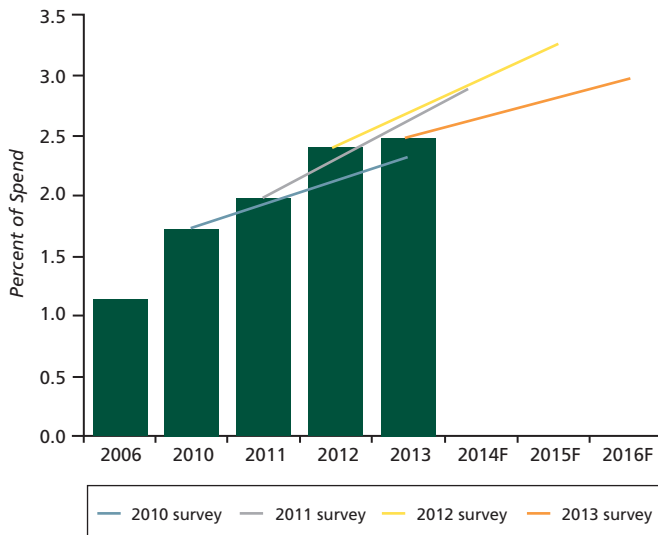
The online channel remains small, but has been growing consistently. Late to the e-commerce revolution, contractors are shifting some of their purchasing online, and potentially disruptive Internet competitors including Build.com, HomeDepot.com and Amazon.com Inc. are positioning themselves to accept their business. Although growing from a small base, online sales' market share has more than doubled since 2006, and

**Figure 3**  
Contractor Average: Purchase Frequency by Channel – Residential Contractors



Source: L.E.K. analysis

**Figure 4**  
Contractor Average: Purchase Frequency – Online Channel



Source: L.E.K. analysis

contractors indicate it now accounts for roughly 3% of sales. (see Figure 4). In general, we believe that the online channel is nascent and will grow substantially in coming years. Adding to the Internet’s disruptive influence, homeowners are increasingly becoming web-savvy and using the Internet to research products and influence contractors’ purchasing decisions (particularly for finished products such as tile and flooring). Many brands are already using social media to build loyalty among homeowners.

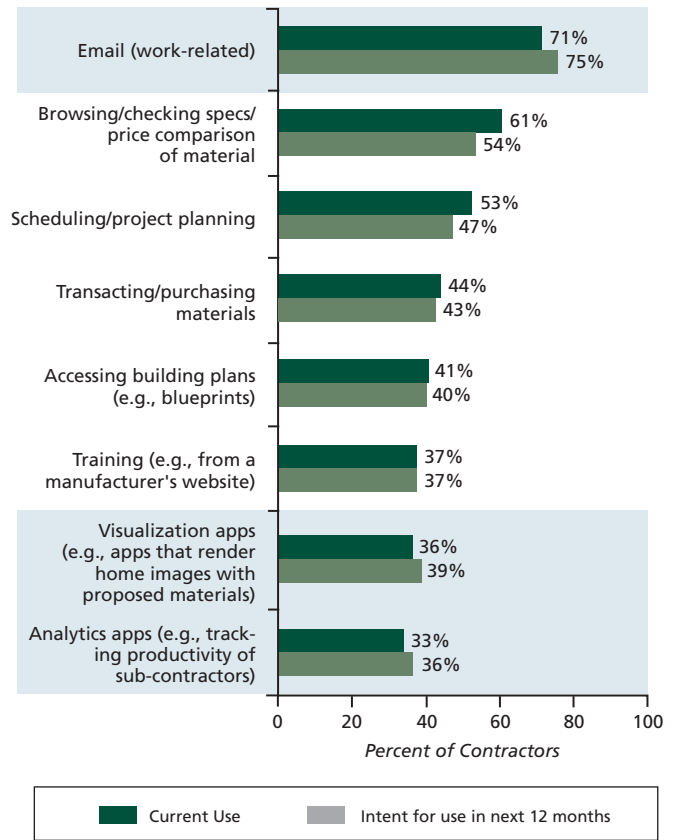
According to our survey, more than 80% of contractors own smartphones, and around 60% use a smartphone for work – these devices are commonly used to exchange emails with clients and check specs and prices for materials, among other tasks. Contractors report that they are already finding innovative ways to use mobile devices for work; some paint and roofing companies, for example, offer “visualization” software that allows contractors to take a picture of a roof or walls and then demonstrate for homeowners how the roof or walls will appear once certain colors and types of material have been applied. Contractors are also using apps to estimate how much material they might need for a given job. Respondents to our survey reported that these mobile-device apps are sales tools that they value from manufacturers, and they expect such tools to proliferate in the industry in coming years (see Figure 5).

## Rating the Product Manufacturers

We asked contractors to rate manufacturers across 12 product categories, with contractors rating only manufacturers in their own sector (e.g., plumbing, electrical, etc). L.E.K. then ranked companies based on aggregate score for the following four attributes: product breadth, quality, price and service level. (See Figure 6). Because contractors are loyal to brands, earning high performance scores is critical to product manufacturers’ success.

While receiving the highest performing score in each category is notable, these categories remain very competitive. Many of the categories have leaders that only hold a slightly higher score than the category average – including framing and drywall.

**Figure 5**  
Contractor Work-Related Mobile Device Usage  
Current vs. Next 12 Months



Source: L.E.K.’s Contractor Behavior Survey

**Figure 6**  
Top Manufacturer Performance

Category	Current Sales Performance Metrics		Highest Performer Score	Difference to Avg. Overall Score
	2012	2013		
Drywall	USG Corporation		5.9	0.2
Electrical/Lighting	GE	Hubbell Lighting	5.4	0.3
Flooring	Anderson Hardwood		5.6	0.4
Framing	Georgia-Pacific		5.2	0.2
HVAC	Trane		5.6	0.4
Insulation	Owens Corning		5.6	0.3
Paint	Sherwin-Williams		5.9	0.4
Plumbing	Toto	Elkay	5.7	0.4
Roofing	Owens Corning	GAF	5.6	0.4
Siding	James Hardie		5.6	0.3
Tile	Dal-Tile	Mohawk Industries	5.9	0.3
Windows/Doors	Andersen	Pella	5.7	0.4

Source: L.E.K. Consulting



## Implications for Branded Building Products

Contractors' renewed confidence means they are thinking beyond just price and cost containment, and are focusing more strategically on efficiency and productivity. Their strong brand ties but weak channel loyalty has clear implications for managers of branded building-product companies, who should take the following steps to maximize profitability:

- **Resist the urge to discount.** Contractors would rather switch channels than trade down brands.
- **Build a multichannel strategy.** Your brand must be positioned in all channels to capture maximum value from the market. Ideally, different products should be sold in each channel to avoid channel conflict – a trade-off made easier by the knowledge that contractors' loyalty will drive them to shop across channels for your brand.

- **Connect with customers through the web.** Mobile devices can be useful sales tools for contractors and can help them promote your brand and increase sales. Social media – both through normal “push” tactics but also “pull” tactics such as product reviews and discussion forums for homeowners – can powerfully influence homeowners' brand preferences. Finally, do not underestimate the disruptive potential of upstarts such as Build.com and Amazon.com, Inc.

In short, our survey indicates that demand in the building and construction industry is now healthy, and showing real signs of momentum. As a result, product manufacturers that can develop and position targeted products across key segments of the channel (and provide product information and other tools online) will be well-positioned to turn healthy profits and grow market share.

## INSIGHTS@WORK™

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