

# Builder

[DESIGN](#) [MONEY](#) [BUILDING](#) [LAND](#) [BUILDER 100](#) [PRODUCTS](#) [VIDEOS](#) [RESOURCES](#)

## Economics

[HOME](#) > [MONEY](#) > [ECONOMICS](#) > [MORE M&A DEALS ON THE WAY?](#)

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BUILDER

## MORE M&A DEALS ON THE WAY? Experts expect a busier M&A year in 2017 compared to 2016.

By [Brian Croce](#)

Last year wasn't particularly active in terms of home builder mergers and acquisitions, but 2017 should be much different, experts say.

There were 10 M&A deals in 2016, says Tony McGill, managing director, investment banking, for Zelman & Associates, roughly two-thirds the normal total. The volatility of the high-yield and equity markets, in addition to the low valuations of equities, led to fewer deals getting done, McGill says.



"Had those markets been not as volatile or less expensive there would have been more M&A financed by smaller public companies raising capital through those channels to buy more builders," he says.

The markets should be more stable in 2017, coupled with higher equity valuations and tighter high-yield credit spreads. "On the margin, there will probably be some of those capital market financings for deals and there's probably going to be more M&A this year because there's more access to that capital," McGill says.

He's expecting about 15 deals in 2017, which is more in line with the output in 2013 through 2015.

Michael Kahn, principal of Michael P. Kahn & Associates, is anticipating some larger transactions this year. "There's a whole group of private builders who are now in their mid-to-late 60s who were very successful, made it through the downturn, and they're beginning to question whether they want to go through more cycles," he says. "We're talking about a cyclical industry. Do they really want to keep doing that?"

And, Kahn says, there are some relatively new buyers on the scene that may be more than willing to make an acquisition. He mentioned Sumitomo Forestry America, Daiwa House USA, and Clayton as companies with deep pockets who should be active.

"Sumitomo and Daiwa are doing most interesting deals," he says, referring to deals in which the buyer secures a majority stake, but not the complete company.

For example, Sumitomo Forestry America, a subsidiary of Japan's fourth-largest domestic builder, Sumitomo Forestry Co., originally purchased a 51% stake in Dallas-based [Gehan Homes](#) in 2014, then purchased the [remaining shares](#) last year. Daiwa House USA, a subsidiary of Japan's Daiwa House Group, entered into an agreement to acquire 82% of the member interests in Northern Virginia-based Stanley-Martin last fall.

"From a sellers' standpoint, that's not a bad situation because instead of having earn outs and things like that as part of a 100% transaction, you're participating in the profitability of a recapitalized company that's going to grow much faster," Kahn says.

Kahn is anticipating Chinese companies to enter the U.S. home building fold, which could potentially ratchet up the M&A market.

And besides foreign capital, the biggest domestic companies are always looking to grow. "Most [builders] can't grow organically sufficiently to please Wall Street and to please the analysts, so another way of getting growth is through acquisition," Kahn says.

McGill says that builders are starting to hone in on lower price points, too. He points to Toll Brother's entry into the Boise, [Idaho](#) market with its [acquisition of Coleman Homes](#) in November. Boise is not a conventional spot for luxury builders, but it gave Toll the opportunity to be "the big dog in a small pen," McGill says.

Toll is moving down in price point in order to attract a different buyer segment, he adds, "which they need in order to grow because it's ...reflective of the limited growth of their luxury buyer market and [in order] to push a high-quality brand downstream you need a premium for it and a lower price point market."

McGill is anticipating more builders that have been focused on move-up and higher priced homes this cycle to get into the "first move-up or entry-level segment."

"M&A trends are moving down price point to get into deeper buyer pools for more growth," McGill concludes. "The trends are private companies will continue to look for exits and smaller public companies will continue to look for opportunities to scale up or be consolidated."

## About the Author



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