

# *The* PERPETUAL INNOVATION MACHINE

How to make one business breakthrough after another.



## Case Study: The Homebuilder

### Boosting Revenue and Profit for a Major Homebuilder

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*A few years ago, the housing market operated like a wild Vegas party. Demand for new homes was surging. And everyone seemed to believe that prices were locked into a one-way trajectory headed straight for the moon.*

*I joined a national homebuilder as the General Manager for a large region in the northeast right when this house party was in full swing. Only we weren't celebrating, because our piece of the booming national market was struggling at the time.*

*My job was to grow revenue, increase market share and profitability, and reduce costs.*

*Our efforts paid off. As a result, we were able to withstand the shock waves that swept across the country when the Great Housing Bubble burst.*

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**Presented by:** Vele J. Galovski and Hank Shaw

# The Homebuilder

## Boosting Revenue and Profit for a Major Homebuilder

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### SNAPSHOT

#### The Assignment

Reverse the declining bottom-line performance of a regional market for a national homebuilder during the great housing boom and subsequent housing crisis.

#### Primary Metrics

- ① Revenue Growth
- ① Profit Before Tax (PBT)
- ① Market Share

#### Key Drivers

- ① Construction Costs
- ① Appointments Made By Reps Each Day
- ① Price/Value of Homes in Different Market Segments

#### Major Innovations

- ① Construction cost optimization program based on national benchmarking
- ① Dramatically improved sales process utilizing training and daily performance management metrics
- ① More competitive offerings for upscale clients
- ① Brand-new portfolio of architectural plans for overlooked entry-level market

#### Breakthrough Results

- ① Share of regional market increased from 11.6% to 19.8%
- ① Before Tax (PBT) increased 50% from 5.0% to 7.6%
- ① Revenue increased from \$115 million to \$147 million
- ① Units sold increased from 427 to 623 per year
- ① Development of products for a new segment eventually accounted for 30% of regional sales

## Fixing the Anomaly in a Booming Market

When I took over the leadership role in the region, our volume was declining and we were losing market share. Clearly, we needed to turn things around. So we established an ambitious set of goals: We would double revenues in five years and increase our profitability by 100 percent.

Of course, it would be a lot easier to achieve those goals in markets that were experiencing the housing boom. All you have to do was take orders and raise prices whenever you felt like it.

But in a region where the population had flat-lined, competition was still intense for every buyer. So we couldn't raise prices without affecting our sales volume. Instead, we had to re-engineer everything from our building and sales processes to our market focus.

It was an exciting challenge. And it left us in an enviable position when our tough local market became the new national norm.

## Increasing Profitability through Strategic Cost Optimization

Since we wanted to make a measurable impact on the business as quickly as possible, we decided to develop a cost optimization program for all of our construction activities. The savings would immediately boost our profitability.

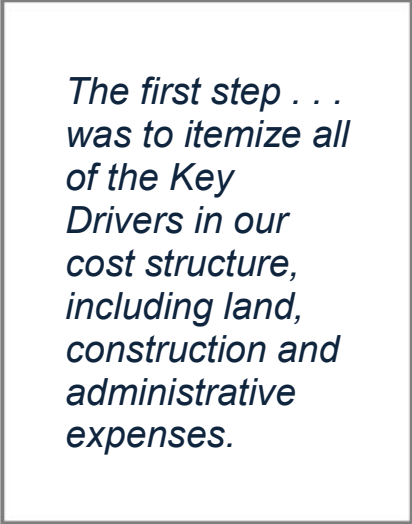
The first step in this process was to itemize all of the Key Drivers in our cost structure, including land, construction and administrative expenses. Then we benchmarked these costs with leaders inside and outside our company.

When the results were in, we could see that our overall cost structure was too high. More specifically, we found that our foundation costs were twice the benchmark. So we conducted additional research to identify the optimal cost for a linear foot of concrete. Then we used that information to re-negotiate prices with our foundation vendors.

This initiative helped us reduce our foundation costs by approximately fifty percent. And that effort paid off in a number of ways. We immediately increased our profitability in markets where we were competitive in terms of price. And we increased our competitiveness in other markets by decreasing our prices.

Next, we followed the same disciplined, analytical process to develop an optimized cost structure for the entire home-building process. The net impact was an eight percent reduction in home construction costs.

We repeated this cost optimization effort on an annual basis and achieved a ten percent overall reduction year after year.



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## Developing a Uniform Sales Process Based on Our Own Best Practices

While our cost reduction initiatives were underway, we conducted an in-depth analysis of our sales process. And what we discovered was a striking degree of variation from one local market to another.

Some markets were successful. Others lagged behind. Some reps were highly effective. Others struggled to achieve their quotas.

At first, those findings seem unsurprising: On any continuum, there's always a best and a worst. But we knew that we could identify specific factors that made the difference in market performance and individual achievement. And then we could rebuild our sales process to incorporate these Key Drivers of success.

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By examining historical data, we learned the following:

- In a good location, aggressive marketing could help us generate traffic consisting of approximately eight prospects for each model home every week.
- Our most successful reps could arrange one appointment for a model home tour per day.
- These role model reps could also close one sale for every six appointments.

The company had always tracked traffic. But we added a level of granular detail to our management process by monitoring the number of appointments each sales rep made per day along with his or her close rate. The new metrics dramatically improved staff productivity and brought real-time accountability to our performance management system.

We also developed a list of corrective actions that could be taken whenever reps fell short of their goals.

To help reps generate more prospects, we:

- Launched more aggressive marketing tactics
- Made our pricing more competitive in the local market
- Offered incentives to prospective home buyers

To help reps make more appointments and close more sales, we:

- Provided training to develop their phone skills
- Helped them learn a consultative selling style that moves prospects toward a buying decision through a structured series of closing steps.

We put these tactics to work in a revamped sales process that brought new energy to our organization.

### **Increasing Revenue by Expanding our Markets**

We also took a long, hard look at our portfolio of architectural plans. And we asked a revealing question: Do our reps have the offerings they need to generate a dramatic increase in volume and revenue?

To find the answer, we created a histogram that allowed us to see the specific price point for every home sold in the region in the previous year. We also compared the results to the best information we could gather on our competitors.

Right away we got some interesting insights. For one thing, the histogram confirmed the fact that we were the number one player in the market for homes in the \$200,000 to \$300,000 range. In fact, we had an impressive forty percent share of this “middle market.”

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On the other hand, we were only an afterthought in the market for upscale homes over \$300,000. And we had virtually no presence in the lower end of the market for properties under \$200,000.

This information forced us to reconsider our goal of doubling revenues in five years. After all, there was no way we were going to do that with our current middle market focus, because we would literally have to capture the entire market: 100 percent. And that obviously wasn't going to happen.

In fact, our predictive modeling efforts showed that we would likely make only incremental gains in this market even with a new and improved selling process.

Instead, we had to go outside the traditional comfort zone of our organization and become a significant player in the other two markets. We then used that pivotal insight to drive our innovation engineering efforts.

Of course, we faced a number of challenges. In the upscale market, we were not perceived as a high-end builder. In addition, the architectural plans and interior designs we offered did not include the luxurious amenities that were so important to prospects.

Last but not least, benchmarking indicated that the entire customer experience we offered was inferior to the market leaders.

Our response? We quickly began working to correct these shortcomings so we could become a legitimate contender in the profitable upscale segment.

### **Bucking the National Trend to Create a Competitive Edge**

Next, we focused on the market for homes under \$200,000, which was a very important market in our region. In fact, it accounted for thirty percent of new home sales.

Unfortunately, the rest of the company was not sold on this entry-level market. The conventional thinking was that we should pursue a more upscale clientele.

But our financial projections clearly showed that there was no way we could achieve our ambitious revenue goals without growing our business in the market for homes under \$200,000. So we had to become an important player. And that's exactly what we set out to do.

The first step was to do an honest appraisal of our architectural portfolio. And frankly, the plans and designs for entry-level homes—which came from the corporate office—weren't truly competitive in terms of price and value.

We did have one thing in our favor, however: Our new cost optimization program would help us compete more effectively on the basis of price. But even taking that into consideration, we were still far behind our best competitors.

To close the gap, we developed a close working relationship with the company's architectural services leader, an experienced executive with an extensive background in quality management. And together we launched a major initiative to develop a new set of plans with an attractive value proposition designed specifically for the entry-level market.

Here's a quick overview of the process we followed.

- We used benchmarking to identify a highly competitive set of customer-focused specifications...specifications that would combine our traditional strengths in floor plan design with newfound efficiency and economy.

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- Next, we developed a theoretical pricing model for houses built with those specifications based on optimized land and construction costs. The model would help us compete more effectively while maintaining profitability.
- Last but not least, we worked with our national architecture office to develop three prototypes for a brand-new class of appealing, but affordable homes in the under \$200,000 category.

Even though we encountered some resistance from people who were committed to the company's traditional market focus, we proceeded with our plans to aggressively sell entry-level homes. And our efforts proved to be very successful.

Just as our predictive modeling indicated, sales of the improved entry-level home designs soon accounted for 30 percent of the new unit sales in our region.

### **Proving that Data-Driven Innovation Works**

By implementing a series of innovations to help us compete in two nontraditional segments, we gradually increased our share of the regional home-building market from 11.6 to 19.8%.

We also improved our profitability by fifty percent.

Even though that was short of our goal, it was a commendable achievement in a nationwide industry that was just beginning to experience a major downturn. In fact, homebuilders as a whole saw their profit margins decline by more than eight percentage points over the timeframe covered in this story.

There was another important benefit besides our breakthrough improvements in profit and loss. The innovations we developed to optimize our cost structure, re-engineer our selling process, and develop new architectural plans for new markets helped our company withstand the emerging housing crisis.

Even though we represented the smallest region in the company, we proved that data-driven analysis and innovation engineering can lead to great things.

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## The Perpetual Innovation Machine

How do you make a business breakthrough? You need daring goals, skillful data analysis, highly focused innovation engineering, dynamic leadership and an inspiring approach to employee engagement.

These are the key components of the streamlined management methodology featured in *The Perpetual Innovation Machine*, a practical guide designed to help executives and emerging leaders learn how to transform their organizations...and achieve great things.

The book also covers a number of topics that should be of interest to new managers and business students, including:

- Key Driver and Predictive Lift Analysis
- Power Tools for managing innovations
- Tips on how to create “The Leadership Broadcasting Network”
- Four Case Histories
- And more



## About The Authors

### Vele Galovski The Innovation Engineer Executive



Over the past 25 years, Vele Galovski has consistently achieved breakthrough results by using his unique approach to innovation engineering.

Vele has dramatically improved the performance of a high-volume manufacturing operation, a national financial services company, a leading provider of professional outsourcing services, and one of the top home-builders in the country.

*For more information on how to turn your organization into a Perpetual Innovation Machine, visit [www.perpetualinnovationmachine.com](http://www.perpetualinnovationmachine.com) or read more at Vele's blog: [perpetualinnovationmachine.wordpress.com](http://perpetualinnovationmachine.wordpress.com)*

### Hank Shaw Intelligent Writing For the Business World



Hank Shaw is an award-winning writer who has worked for a number of Fortune 500 companies including Amgen, Bank of America, Gilead Sciences and Xerox.

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