

Home Warranty FALL 2024



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M&A IN THE DIRECT-TO-CONSUMER HOME WARRANTY INDUSTRY

A home is often a person’s most valuable asset, yet 31% of U.S. homeowners have less than \$1,000 saved for repairs¹, despite annual costs averaging \$3,600. Home warranties provide financial protection for critical appliances like HVAC units. Unlike insurance, which covers catastrophic events, home warranties address wear-and-tear breakdowns. The service contract also simplifies the repair process by coordinating professional services, easing the burden on homeowners.

Home warranties are sold through two channels: real estate brokers and direct-to-consumer marketers. The real estate broker channel is dominated by a few large companies with national networks of real estate brokers, who often purchase or help a home seller choose a home warranty for the buyer when negotiating the purchase price. Direct-to-consumer (DTC) marketers reach existing homeowners primarily via direct mail marketing.

AVERAGE OUT OF POCKET COSTS²



UNTAPPED POTENTIAL: WHY THE DTC HOME WARRANTY SECTOR IS PRIMED FOR M&A

Despite significant growth in recent years, the DTC home warranty sector remains a fragmented industry ripe for acquisitions. DTC home warranty companies tend to generate high cash flow and are less dependent on new home sales compared to companies focused on the broker channel. Additionally, as DTC companies control their distribution, they do not have concentration risk. Currently, over 50 companies operate in the DTC space, many of which are small to mid-sized, creating a significant opportunity for consolidation.

¹"Nearly 60% of U.S. Homeowners Are Putting Off Home Repairs Due to Cost, Survey Says", *Today's Homeowner*, Kristina Zagame

²Forbes, Framework Homeownership, This Old House

Several market dynamics are driving growth in the DTC space, further increasing its attractiveness for acquisition. The U.S. housing stock is aging, with the median age of homes at an all-time high of 40 years³. As homes age, the demand for home services such as HVAC repairs increases, causing home service costs to rise faster than inflation. Home warranties are a crucial tool for budget protection against inflation. Furthermore, fewer homebuyers are obtaining warranties when purchasing their home. Sales through real estate brokers declined from 28% in 2019 to 20% in 2023. Colonnade Advisors estimates that there are now more warranties sold directly to consumers than through real estate agents. The shift underscores the growing importance of the DTC channel as more consumers seek warranties independently, creating a fertile ground for M&A activity in the sector.

The DTC home warranty sector, despite its significant size and recent growth, has seen surprisingly few M&A transactions. This contrasts with the real estate broker-sold home warranty market, which has experienced several acquisitions. The discrepancy suggests that the DTC space remains relatively untapped for consolidation opportunities, even as it represents a larger portion of the market. The fragmented DTC industry presents a compelling opportunity for investors looking to capitalize on a growing and underserved segment.

³American Community Survey Estimates

THE DTC HOME WARRANTY INDUSTRY IS \$2.5 BILLION

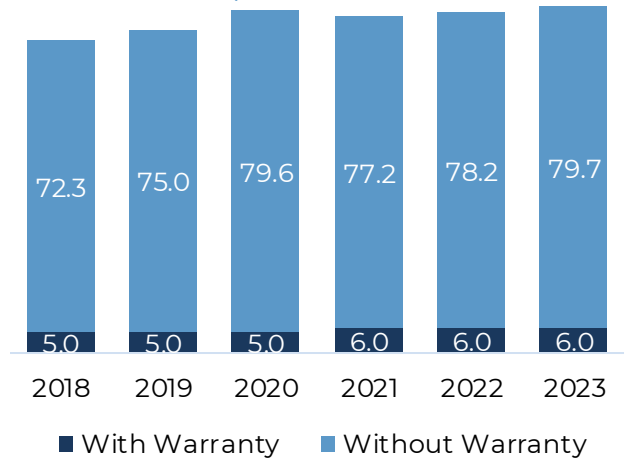
DTC home warranty marketers target the 80 million homeowners who are not covered by a warranty from when they purchased their home, representing \$2.5 billion of warranties sold in 2023 out of a \$36 billion addressable market.

The average cost of a DTC home warranty is approximately \$4,500, with most buyers opting for a 24-month payment plan. Warranties sold through DTC channels typically have a term of 36 months.

The 7.0% CAGR growth in the DTC channel is driven by declining sales through real estate brokers and increasing maintenance needs due to the aging housing stock. Consumers' positive experiences with warranties for other products, combined with the financial benefits of budget protection and inflation hedging, further fuel this expansion.

FEW HOMEOWNERS HAVE A WARRANTY^{4,5}

(homes in millions)



ADDRESSABLE DTC MARKET SIZE

\$36.0 billion

DIRECT-TO-CONSUMER HOME WARRANTY CHANNEL SIZE⁴

(\$ in billions)



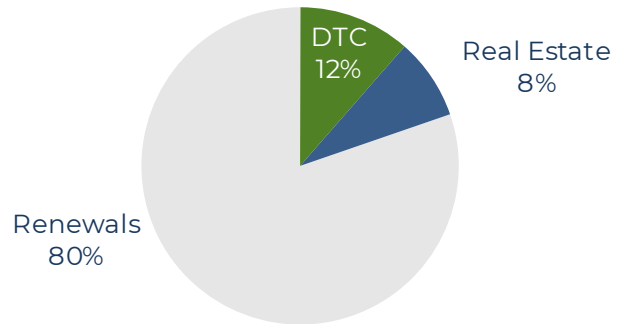
⁴Frontdoor Annual Reports, Colonnade Estimates

⁵Bankrate

DTC GROWTH IS OUTPACING BROKER GROWTH

Traditionally, home warranties were primarily marketed through real estate brokers who helped sellers select coverage for buyers during home transactions. Broker-sold warranties typically have a 12-month term, with a significant portion, around 30%, renewing after the first year due to high customer satisfaction and peace of mind.

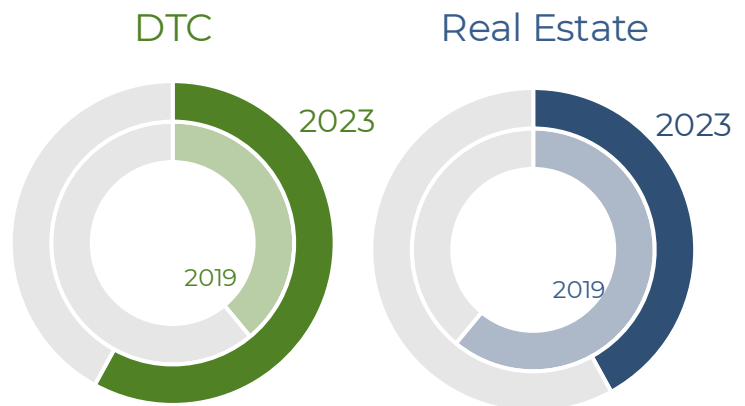
REVENUE BY CHANNEL⁶



The real estate brokers market is dominated by a few major players leveraging their large-scale operations and strong broker relationships. Frontdoor, Inc. (NASDAQ: FTDR) owns both American Home Shield and 2-10 Home Buyers Warranty, giving it a significant share of the market through its extensive network of real estate agents. Another key player is First American Home Warranty, owned by First American Financial Corporation (NYSE: FAFC).

In recent years, the DTC market for home warranties expanded rapidly, with more warranties now being sold directly than through real estate agents. DTC sales grew from \$1.9 billion in 2019 to \$2.5 billion in 2023, reflecting growing consumer demand outside of traditional real estate transactions. DTC sales are expected to continue to gain market share in upcoming years as their year-to-year renewal rates are over 70%, significantly higher than the broker channel.

HOME WARRANTY ORIGINATIONS BY CHANNEL AS A PERCENT OF TOTAL HOME SALES^{6,7}



⁶Frontdoor Annual Reports, Colonnade Estimates

⁷Excludes renewals

DTC HOME WARRANTY ECOSYSTEM

HOME WARRANTY MARKETERS

- Market home warranty service contracts to consumers via direct mail and digitally
- Marketers sometimes participate in reinsurance (acting as the obligor)
- High margins of 30-45%
- Highly fragmented universe of competitors
- Example: MyHome Protection

ADMINISTRATORS

- Designs the service contract, manages claims, and often coordinates repairs
- Frequently, the administrator is the obligor - responsible for paying covered claims and ensuring the fulfillment of contract terms
- Limited number of competitors
- Administrators include Headstart Warranty Group, Integrity Admin Group

VERTICALLY INTEGRATED COMPANIES

- Many vehicle service contract marketers also offer home warranty service contracts
- Companies are vertically integrated as an administrator, marketer, and/or payment plan provider
- Limited companies with this structure
- Examples: Capital Home and Auto, Evercare Protection, Miramar Financial Holdings (Black Diamond and Warranty Global Group)

SERVICE PROVIDERS

- Provide repair and maintenance services such as HVAC, plumbing, etc.

PAYMENT PLAN COMPANIES

- Pursuant to a contractual agreement, company purchases at a discount the right to receive the payment stream; discounts typically 7%-15%. The company funds a portion to the administrator and the marketer. The consumer pays a down payment (typically 5%) and fixed monthly payments ranging from 18 to 24 months
- The payment plan company funds the marketers net of a cash reserve for cancellations, typically 40-55%
- Generally high yielding, short term receivables
- Companies include Paylink and Walco

MULTI-CHANNEL SELLERS

- Companies selling through real estate brokers and direct-to-consumer
- Example: Choice Home Warranty

KEY TRENDS DRIVING GROWTH IN DTC HOME WARRANTIES

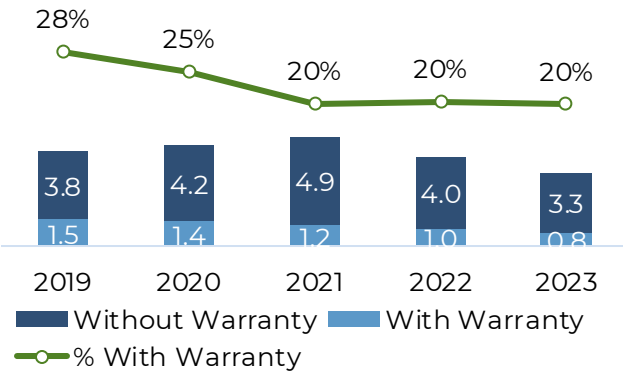
- 1 Home Warranties Sold Through Real Estate Brokers Are Declining
- 2 Housing Stock Is Getting Older, Requiring More Maintenance And Repairs
- 3 Experience with Warranties in Other Industries
- 4 Budget Protection and Inflation Hedge

1 HOME WARRANTIES SOLD THROUGH REAL ESTATE BROKERS ARE DECLINING

Real estate broker-sold warranties have dropped by 46.7% since 2018 as a result of major shifts in the \$47.5 trillion U.S. housing market. Following lockdowns, pent-up demand and low interest rates drove a strong seller's market. The seller's market continued as interest rates rose starting in 2022 as many homeowners were unwilling to give up their low-interest-rate mortgages, reducing the housing supply faster than demand. Since October 2020, home sales dropped 34%, nearing pandemic levels. Despite the decline in home sales, between 2021 and 2023, homes sold over 20 days faster than in 2019, reducing brokers' need to include warranties in sales. The strong seller's market lowered the incentive for brokers to offer warranties, leading to fewer purchases. However, demand for home warranties remains, expanding opportunities in the direct-to-consumer market.

HOMES SOLD BY HOME WARRANTY COVERAGE⁸

(homes in millions)



The shift by brokers away from including warranties as part of the sale is amplified by the recent National Association of Realtors settlement, which reduces broker commissions by removing the requirement that sellers include commissions when listing a home. As brokers stand to make less on home sales, they are increasingly opting out of purchasing warranties on behalf of clients.

⁸Frontdoor Annual Reports and Colonnade
⁹National Association of Home Builders, RedFin
¹⁰Barrons, Bankrate

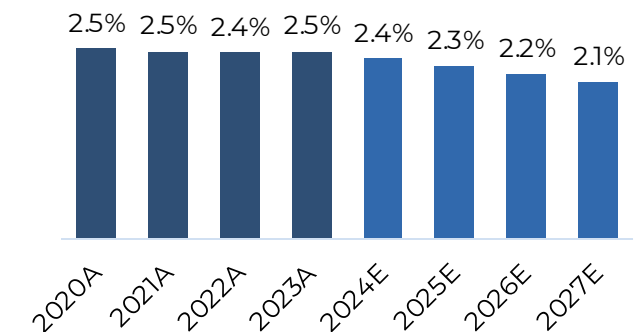
U.S. EXISTING HOME SALES⁹

(in millions)



FORECASTED REAL ESTATE BROKER COMMISSION %¹⁰

(% of home price)

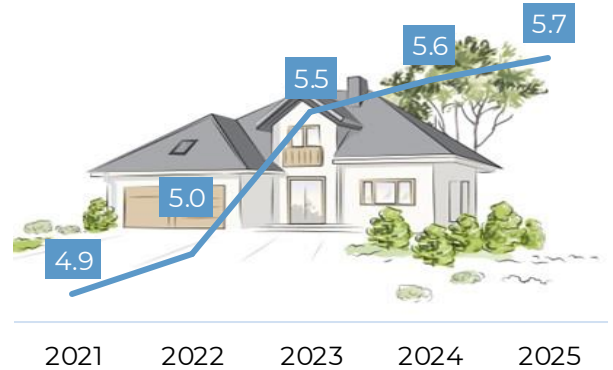


2 HOUSING STOCK IS GETTING OLDER, REQUIRING MORE MAINTENANCE AND REPAIRS

As the U.S. housing stock ages, home warranties become an increasingly efficient way for homeowners to manage the ongoing costs of maintaining their homes. Older homes are more likely to need expensive repairs on critical systems such as HVAC units and furnaces as they approach the end of their 10 to 20-year lifespans. The average cost to repair an HVAC system is \$7,500 and \$4,706 for a furnace. In 2023, over 5.5 million homes surpassed 15-years old, making them highly likely to need a major repair in the near future. DTC home warranty companies are uniquely able provide a cost-effective solution to manage the rising cost of repairs to existing owners as their home continues to age.

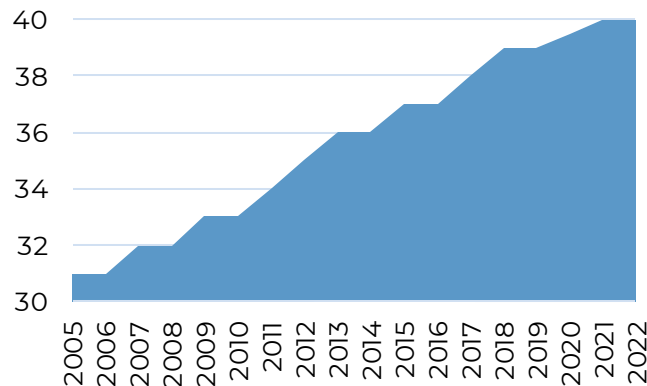
NUMBER OF HOMES AT 15 YEARS OF VINTAGE¹¹

(in millions)

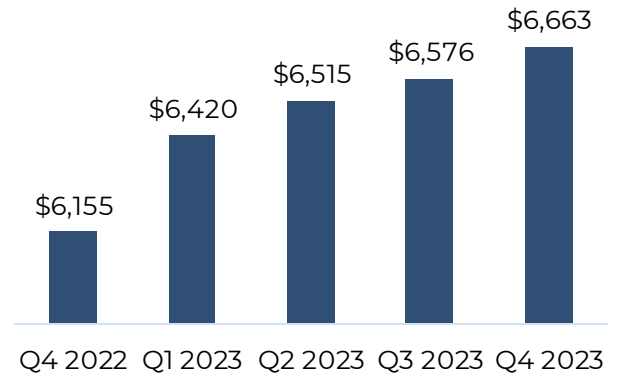


MEDIAN AGE OF U.S. HOMES¹²

(years)



AVERAGE ANNUAL COST OF HOME MAINTENANCE¹³



¹¹National Association of Realtors

¹²American Community Survey Estimates

¹³Thumbtack, excludes financing costs

3 EXPERIENCE WITH OTHER WARRANTIES

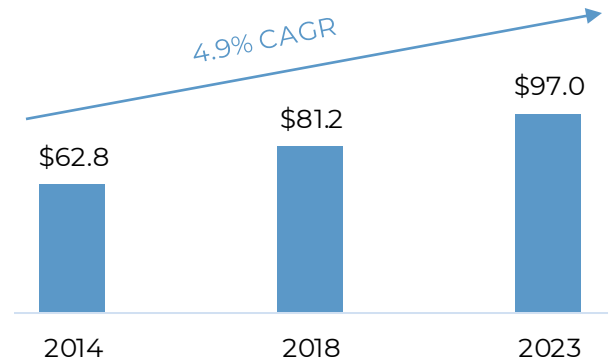
Consumers' positive experience with VSCs and electronics warranties naturally led them to consider home warranties as a way to protect their largest asset. Over the past decade, consumers increasingly embraced extended warranties across several sectors such as vehicle service contracts (VSCs) and consumer electronics. Between 2014 and 2023, the VSC industry expanded by more than 54%, while product warranties grew by over 33%. Today, 45% of Americans have a VSC and 42% have purchased an electronics warranty¹⁴.

Despite significant growth in recent years, extended warranty companies continue to maintain high customer satisfaction ratings, with over 75% of VSC holders being satisfied with the cost of their coverage.

The broad adoption of extended warranties and high customer satisfaction enhanced the reputation of the extended warranty industry overall. Homeowners, familiar with the predictability and financial security that warranties offer for vehicles and electronics, are more likely to view home warranties as essential financial safeguards to managing the rising costs of maintaining and repairing their homes.

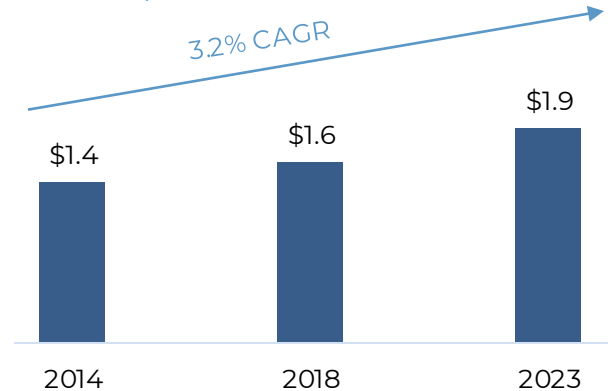
VEHICLE SERVICE CONTRACT INDUSTRY SIZE¹⁴

(\$ in billions)



PRODUCT WARRANTY INDUSTRY SIZE¹⁵

(\$ in billions)



¹⁴NADA, Auto Rental News, Colonnade estimates

¹⁵BISWorld

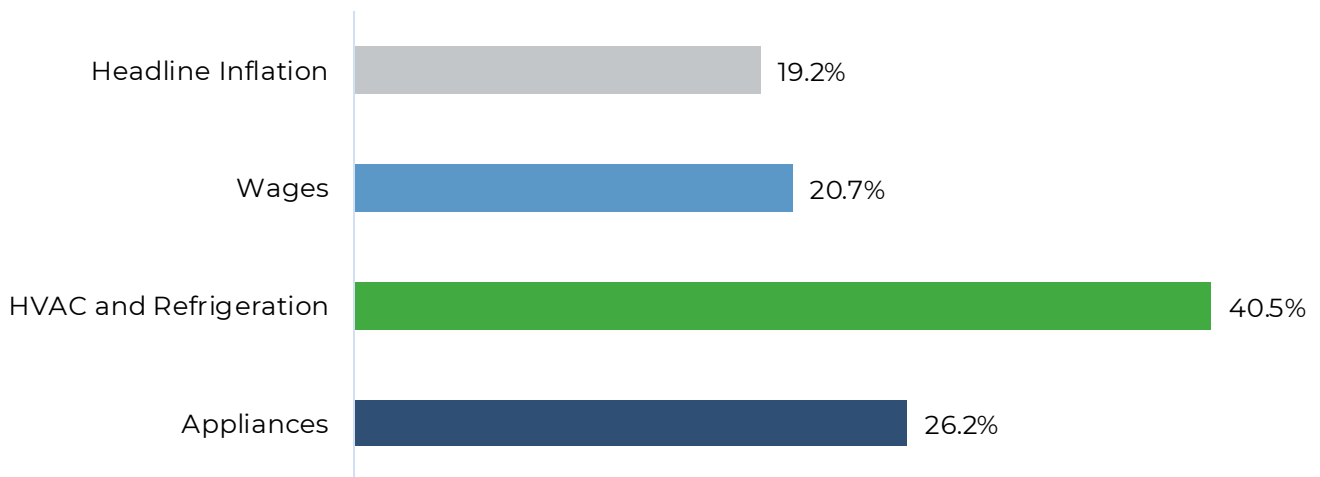
4 BUDGET PROTECTION AND INFLATION HEDGE

The rapid increase in appliance prices in 2023, significantly outpacing both inflation and wage growth, underscores the value of home warranties in managing unexpected repair costs. While overall inflation slowed to around 3% in early 2024, down from its peak of 9% in 2022, HVAC and refrigeration prices surged by more than 40% since 2020. In contrast, wages grew by only 21% during the same period, leaving many homeowners struggling to keep up with rising expenses. Supply chain disruptions, production challenges, and recent economic pressures such as rising interest rates have driven these price increases.

With 35% of U.S. homeowners having less than \$1,000 saved for home repairs, many face significant financial risk. By offering predictable repair expenses, Home warranties provide a critical buffer, helping homeowners hedge against inflation and the escalating costs of major repairs.

INFLATION OF HOUSEHOLD ITEMS SINCE 2020¹⁶

(% price increase)



¹⁶U.S. Bureau of Labor Statistics

SELECT TRANSACTIONS

	TARGET	BUYER	COMMENTS
June 2024	2-10 HOME BUYERS WARRANTY <i>(Genstar Capital)</i>	Frontdoor, Inc. <i>(NASDAQ: FTDR)</i>	Diversifies into new home structural warranties complementing existing customer base and enhancing cross-selling initiatives. 13.6x 2023 adjusted EBITDA of \$43 million for a total price of \$585 million
February 2024	CONSUMERS ENERGY APPLIANCE SERVICE PLAN BUSINESS <i>(CMS Energy (NYSE: CMS))</i>	OnCourse Home Solutions <i>(Apax Partners LLP)</i>	Provider of appliance protection and related services, including water line, sewer line, external gas line, external electric line, well line, and septic line protection, to homeowners in Michigan, serving over 150K households
August 2023	TOTALHOME WARRANTY-US <i>(Homeserve PLC owned by Brookfield Infrastructure Funds)</i>	Super Home Warranty <i>(multiple early and growth stage investors)</i>	U.S. warranty business of HomeServe plc
August 2023	AMERICAN HOME GUARDIAN, INC.	Super Home Warranty <i>(multiple early and growth stage investors)</i>	Home warranty and residential service provider in Texas, Nevada, Arizona, Idaho, and Utah
August 2023	NATIONS HOME WARRANTY	Super Home Warranty <i>(multiple early and growth stage investors)</i>	Provides home warranty products for homeowners and services such as pest control and lawn service. Customers in Texas, exclusively
January 2023	GUARDIAN PROTECTION PRODUCTS, INC.	OnPoint Warranty Solutions, LLC	OnPoint, a insuretech, mobile solutions and warranty services company, received an investment from Waterfall Asset Management, Atalaya Capital Management to supprt the accquition of Guardian. Guardian is a warranty adminiatrator for furniture retailers
November 2022	CLIMATE CONTROL SERVICES, INC.	Right Away Home Services	Warranties on most major home appliances, including air conditioning, electric heaters, dishwashers, dryers, microwaves, water heaters, and provides residential HVAC repairs, service, replacements as well as Plumbing and Appliance repairs. Focused on Palm Beach County, Florida

SELECT TRANSACTIONS (continued...)

	TARGET	BUYER	COMMENTS
August 2022	PROFESSIONAL WARRANTY SERVICE CORPORATION <i>(PWSC) (Kingsway Financial Services)</i>	PCF Insurance Services	PWSC is a home warranty company offering protection for homeowners, renters, builders, property managers and more, with a line of structural and appliance warranty products. It was purchased for \$51.2 million plus a one-year earnout. Acquired by Kingsway Financial Services for \$9.9 million from TA Associates in 2017
February 2022	PLATINUM HOME WARRANTY	Super Home Warranty <i>(multiple early and growth stage investors)</i>	Home warranty administrator with a network of third-party contractors and an inhouse team of technicians
February 2022	HOME WARRANTY OF AMERICA	Choice Home Warranty, Inc.	Choice, a DTC seller, adds home warranty service contracts sold through real estate professionals
October 2021	HOMEOWNER SERVICES GROUP <i>(American Water Works Company, INC. NYSE: AWK)</i>	Apax Partners LLP	Rebranded Oncourse Home Solutions. 3 million customer contracts across 43 states. Brands include American Water Resources and Pivotal Home Solutions. Purchase price of \$1.2 billion including a seller's note and earnout
September 2021	AMERICAN HOME PROTECT (AHP)	Porch Group <i>(NASDAQ: PRCH)</i>	AHP is a provider of whole home warranty policies across the U.S. AHP utilizes a direct-to-consumer model to acquire customers for their multi-year warranty plans.
August 2021	NATIONAL HOME WARRANTY GROUP <i>(Aviva Canada INC.)</i>	Hub International Limited	Focus on Western Canada. New home warranty coverage through 3,500 builders to 15,000 homes per year
June 2021	STRUCSURE HOME WARRANTY	Insure Homes Holdings, LLC <i>(Milestone Partners)</i>	Home warranties for new homes

CONCLUSION

The DTC home warranty sector presents a compelling opportunity for M&A activity due to its rapid growth, fragmented landscape, and high cash flow potential. The U.S. housing stock is expected to continue aging, despite recently reaching an all-time high of 40 years. The aging housing stock will increase the demand for home repair services, continuing to push repair costs above inflation. As these trends intensify, more homeowners will seek home warranties to protect their budgets from rising expenses.

As more warranties are sold directly to consumers than through traditional real estate brokers, the DTC market offers persistent opportunities to capture a disproportionate amount of this growth without being affected by short-term real estate fluctuations. Strategic acquisitions in this sector could provide immediate access to recurring revenue streams and the potential for significant value creation by consolidating the highly fragmented industry, making it a prime area for private equity firms and strategic buyers to consider.

COLONNADE IS A LEADING ADVISOR TO THE WARRANTY INDUSTRY

CrystalFusion

was sold to

APCO
HOLDINGS

COLONNADE

Reynolds & Reynolds™

acquired

XZION

COLONNADE

Reynolds & Reynolds™

acquired

AGWS

COLONNADE

SKYAUTO
PROTECTION

was sold to

FORTEGRA

COLONNADE

PMC | **PROTECT MY CAR**

was sold to

Crestview

COLONNADE

ENDURANCE

was sold to

TRP Capital Partners

COLONNADE

AutoAssure
Extended Repair Coverage

was sold to

ENDURANCE

COLONNADE

VSC Marketer

was sold to

Strategic

COLONNADE

CALTEX

was sold to

SPECTRUM
AUTOMOTIVE HOLDINGS

COLONNADE

MILESTONE
MARKETING SOLUTIONS

was sold to

SPECTRUM
AUTOMOTIVE HOLDINGS

COLONNADE

smart autocare

was sold to

Tiptree Inc.

COLONNADE

PMC | **PROTECT MY CAR**

acquired

Direct Media Partners, LLC

COLONNADE

APC

INTEGRATED SERVICES GROUP

was sold to

SOUTHFIELD

COLONNADE

MEPCO

was sold to

SEABURY
CAPITAL GROUP

COLONNADE

SOUTHFIELD

acquired

VANGUARD
DEALER SERVICES

COLONNADE

ADG
AUTOMOTIVE
Development Group

was sold to

APCO
AUTOMOBILE PROTECTION CORPORATION

COLONNADE

OMNISURE

was sold to

FORTRESS

COLONNADE

PACCO
Preferred Automobile Credit Co.

was sold to

AFS ACCEPTANCE
SURPRIME AUTOMOBILE FINANCING

COLONNADE

PWI **PREFERRED**
WARRANTIES INC.

was sold to

KAR **AUCTION**
SERVICES

COLONNADE

PayLink
Direct

was sold to

OXFORD
FINANCIAL GROUP, LTD.

COLONNADE

MEPCO
insurance premium financing

was sold to

INDEPENDENT
BANK

COLONNADE

Automotive
Digital Marketer

was sold to

Private Party

COLONNADE

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This advertisement was prepared April 2024. It is not investment advice, and Colonnade undertakes no obligation to update the information contained herein.

Sources: Today's Homeowner, Forbes, This Old House, American Community Survey, Frontdoor, Bankrate, National Association of Home Builders, RedFin, Barrons, National Association of Realtors, Thumbtack, NADA, Auto Rental News, IBISWorld, U.s Bureau of Labor Statistics and Colonnade research

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