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Kimball Hill hits building blocks

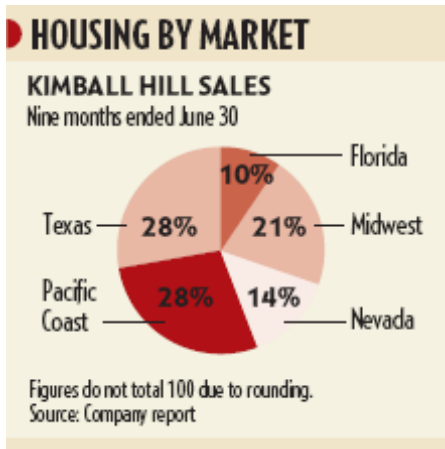
Scorched by big Sun Belt bets, homebuilder cuts prices, dangles incentives

Kimball Hill Inc., the Rolling Meadows homebuilder that bet big on hot markets like Las Vegas and California in the recent housing boom, is now paying a heavy price as those markets cool off faster than the nation as a whole.

A privately owned builder with more than \$1.1 billion in sales last year, Kimball Hill gets 42% of its revenue from these markets.

Like other homebuilders, it is now slashing prices and offering incentives in order to move homes in Sun Belt markets.

Revenue rose 9% to \$701.6 million in the nine months ended June 30, compared with the year-earlier period. But price-cutting and sales incentives, combined with higher land prices and construction costs, led to a 16% drop in net income, to \$38.5 million in



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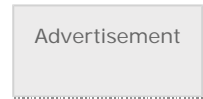
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the nine-month period. Homebuilding gross profit margin shrank to 21% from 24%, according to a Securities and Exchange Commission filing by Kimball Hill.

"We are pricing our homes to existing markets rather than clinging to the home values of yesteryear," Chairman and CEO David Hill said in a conference call with analysts last month.

SLASHING PROFITS

Kimball Hill has plenty of company. Big publicly traded builders like KB Home and Hovnanian Enterprises Inc. are slashing profit forecasts as the supply of new and existing U.S. homes for sale rises to record levels. Home prices will probably fall this year for the first time since 1993, and new-home sales will drop 16%, according to a National Assn. of Realtors forecast released last week.



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California.

It's especially tough for builders with a presence in souring markets like Las Vegas and

Kimball Hill is willing to bargain in Las Vegas, where it has 10 developments. The company has raised commissions for brokers, offered free upgrades on appliances and other amenities and given closing-cost credits of \$10,000 or more to buyers who use its loan program, says Bruce Hiatt, owner of a Las Vegas residential brokerage. Price cutting is not uncommon. "The homebuilders finally got the wake-up call to slow down," he says.

Yet Las Vegas isn't the only worry for Kimball Hill, the 24th-largest U.S. homebuilder by number of homes sold.

"Sudden demand withdrawal, incentive pressures, high cancellations and pricing uncertainty continue to characterize most of our markets," Mr. Hill said on the conference call. He didn't return calls.

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BONDHOLDERS SQUEEZED

The good news for Mr. Hill, who with his family controls about 81% of Kimball Hill stock, is that he doesn't have to placate shareholders. Nonetheless, the housing slump hasn't been easy on owners of company bonds. Kimball Hill issued \$203 million in publicly traded bonds in June. They traded recently for 87 cents on the dollar, down from 94 cents when trading started in mid-June.

Kimball Hill's overall debt-to-capitalization ratio has climbed to 64%; Mr. Hill told analysts he aims to get that down to 50%.

One thing that could help: The company is selling off excess home and land holdings, which will raise cash. "When you have a very weak earnings environment, the thing to do is hunker down and pay off debt," says Joe Snider, senior credit officer at Moody's Investors Service in New York.

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