

D.R. Horton, Inc. (DHI)

\$57.67 (As of 02/04/20)

Price Target (6-12 Months): **\$66.00**

Long Term: 6-12 Months

Zacks Recommendation: **Outperform**
(Since: 02/03/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5) **2-Buy**

Zacks Style Scores: VGM: C

Value: C | Growth: D | Momentum: A

Summary

Shares of D.R. Horton have outperformed its industry in the past year. The trend is expected to continue, courtesy of impressive first-quarter fiscal 2020 results. Earnings and revenues not only topped analysts' expectations by 7.6% and 6.5%, but also grew 30.3% and 14.3%, respectively. It ended fiscal first quarter with 12,959 home closings (up 13% year over year). The company is well positioned for fiscal 2020, courtesy of its industry-leading market share, solid acquisition strategy, well-stocked supply of land, lots and homes, along with affordable product offerings across multiple brands. It expects to deliver an improved performance in fiscal 2020, given higher orders driven by improving housing market fundamentals, favorable mortgage rates and a solid job market. Net orders grew 19% year over year in the quarter.

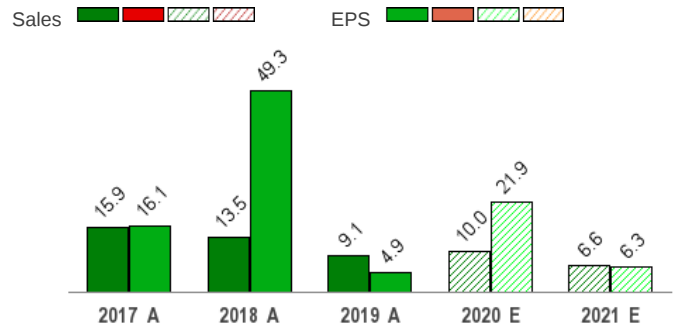
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$61.77 - \$37.16
20 Day Average Volume (sh)	3,920,977
Market Cap	\$21.1 B
YTD Price Change	9.3%
Beta	0.95
Dividend / Div Yld	\$0.70 / 1.2%
Industry	Building Products - Home Builders
Zacks Industry Rank	Top 15% (39 out of 255)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	7.6%
Last Sales Surprise	6.5%
EPS F1 Est- 4 week change	4.4%
Expected Report Date	04/23/2020
Earnings ESP	1.9%
P/E TTM	12.7
P/E F1	11.0
PEG F1	1.0
P/S TTM	1.2

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	4,120 E	4,641 E	5,746 E	5,810 E	20,484 E
2020	4,021 A	4,380 E	5,361 E	5,429 E	19,212 E
2019	3,503 A	4,097 A	4,882 A	4,977 A	17,459 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.06 E	\$1.21 E	\$1.65 E	\$1.69 E	\$5.56 E
2020	\$0.99 A	\$1.11 E	\$1.48 E	\$1.51 E	\$5.23 E
2019	\$0.76 A	\$0.93 A	\$1.26 A	\$1.35 A	\$4.29 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 02/04/2020. The reports text is as of 02/05/2020.

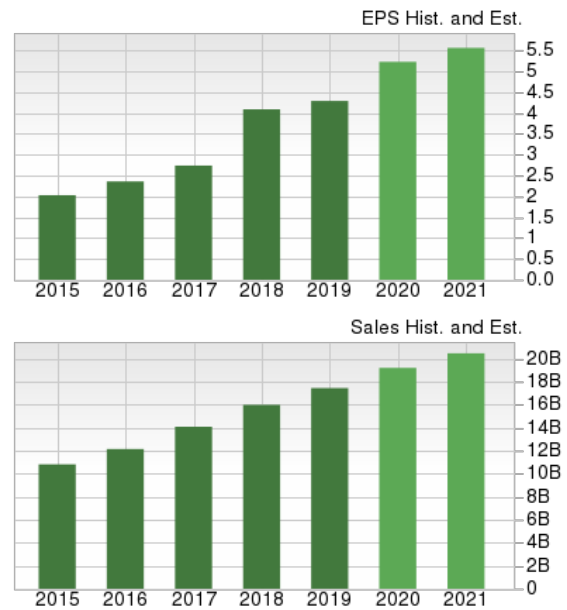
Overview

D.R. Horton, Inc., based in Texas, is one of the leading national homebuilders, primarily engaged in the construction and sale of single-family houses both in the entry-level and move-up markets. Homes vary in sizes from 1,000 to 4,000 square feet, with prices ranging from \$100,000 to more than \$1,000,000. D.R. Horton's operations are spread over 90 markets across 29 states in the East, Midwest, Southeast, South Central, Southwest and West regions of the United States. Its houses are sold under the brand names D.R. Horton - America's Builder, Emerald Homes, Express Homes and Freedom Homes.

D.R. Horton operates through three segments: **Homebuilding** (contributing 96.7% of the total revenues in fiscal 2019), **Forestar** (2.4%) and **Financial Services** (2.5%). Notably, of the total revenues, 1.8% represents the elimination of intercompany transactions. The Homebuilding segment comprises six reporting regions and derives revenues primarily from the sale of completed homes built on lots it develops and on finished lots purchased ready for home construction. In addition to single-family detached homes (accounting for around 90% of home sale revenues), the segment builds attached homes, such as town homes, duplexes, triplexes and condominiums. The segment also derives revenues by selling lands and lots. As of Dec 31, 2019, the Forestar land development reporting segment has operations in 51 markets and 20 states, where it owns, directly or through joint ventures, interests in residential and mixed-use projects. During fiscal 2018, the company had acquired a 75% share of Forestar Group, which is a residential and mixed-use real estate development company. Forestar Group Inc. (FOR), a publicly-traded residential and real estate development company, is a majority-owned subsidiary of D.R. Horton.

The Financial Services segment, through the mortgage subsidiary, DHI Mortgage, provides mortgage financing and title agency services primarily to the company's homebuilding customers.

Other Businesses — Through DHI Communities, a 100% owned subsidiary, the company develops, constructs and owns multi-family residential properties that produce rental income.



Reasons To Buy:

▲ **Strong Results and Stock Outperformance:** Shares of D.R. Horton have outperformed its industry in the past year. The price performance was backed by the company's robust earnings surprise history, having surpassed the Zacks Consensus Estimate in seven of the trailing nine quarters. Its revenues also surpassed the consensus mark in eight of the trailing nine quarters. The trend is expected to continue in the near term as well, post its solid fiscal 2019 and first-quarter fiscal 2020 results. It ended fiscal 2019 on a strong note. Earnings per share increased 10.6% and revenues grew 10.7% from a year ago. Notably, with 56,975 homes closed in fiscal 2019, D.R. Horton completed its 18th consecutive year as the largest homebuilder in the United States. The trend continued in fiscal first-quarter 2020 as well, with adjusted earnings and revenues increasing 30.3% and 14.3%, respectively.

With accretive acquisitions, robust backlog and a well-stocked inventory of land, lots and homes in place, D.R. Horton is expected to perform well in fiscal 2020.

Meanwhile, the U.S. housing market started building up strength since the beginning of 2019, after a torrid second-half 2018. Declining mortgage rates and moderate home prices have been adding strength to D.R. Horton and other homebuilders. The overall homebuilding industry remains positive owing to ongoing traffic trends that indicate higher inclination of buyers, thereby reflecting a slow but steady housing recovery. Notably, declining interest/mortgage rates, lower construction costs, low unemployment and increasing wages are somewhat offsetting the other ongoing headwinds. Moreover, as more and more millennials are leaving their parents' home, a sharp spike in household formation is likely to translate into higher demand for new homes.

Earnings estimates for fiscal 2020 have moved 0.6% north over the past seven days, reflecting analysts' optimism regarding the stock's solid growth prospects.

▲ **Accretive Acquisitions & Increased Capital Investments in Land:** D.R. Horton is fast acquiring homebuilding companies in desirable markets. Over the past five years (through fiscal 2019), the company has invested approximately \$1 billion on acquisitions. During fiscal 2019, the company purchased homebuilding operations of three private builders for approximately \$325.9 million. In December 2018, the company entered Iowa by acquiring Classic Builders, the largest builder in Des Moines. It enhanced its market position in Raleigh, NC by acquiring Terramor Homes. In November 2018, it acquired Westport Homes, a top five builder by volume in Indianapolis and Columbus, which are both in the top 50 U.S. housing markets.

The company's strong cash position and low debt/capital ratio allowed it to make strategic land purchases even during the downturn, in turn giving it a significant competitive advantage. The company has selectively invested in attractively-priced land and lots in the past few years allowing it to bring new attractive communities in desirable markets. D.R. Horton's well-stocked supply of land, plots and homes provide it with a strong competitive position to meet the demand in future quarters, thereby growing sales and home closings. The company invested \$3.7 billion in lots, land and development in fiscal 2019, almost on par with the year-ago level of \$3.8 billion. It invested \$1.3 billion in lots, land and development during the fiscal first quarter. It has plans to boost investments to replenish its land and lot supply in fiscal 2020 for supporting revenue growth.

▲ **Affordable Homes Drive D.R. Horton's Profits:** Higher building material costs, as well as land and labor shortages are prompting homebuilders to increase home prices. That said, D.R. Horton's strategic shift toward more entry-level affordable homes have been paying off, with the segment experiencing strong demand and limited supply. Notably, first-time homebuyers represented 50% of its closings in first-quarter fiscal 2020. The figure was same in the corresponding quarter of last year.

▲ **Cost Reduction and Margin Improvement:** Management has consistently made an effort to reduce both construction and selling, general and administrative (SG&A) expenses. It controls construction costs by designing homes efficiently and also by obtaining construction materials and labor at competitive prices. Further, its SG&A expenses are continuously going down due to cost control and better fixed cost leverage. In fiscal 2018, SG&A expenses improved 30 basis points (bps) year over year to 8.6%. The metric decreased 40 bps and 20 bps in fiscal 2017 and fiscal 2016, respectively. Notably, the company did not achieve SG&A leverage in fiscal 2019 after it reduced revenue growth expectation for the fiscal first quarter, and worked on aligning its inventory levels and operations with revised expectations throughout the fiscal year. Nonetheless, it remains focused on controlling SG&A and expects to improve the same in fiscal 2020. Its fiscal first-quarter SG&A improved 30 bps year over year.

The company strategically manages the pricing, incentives and sales pace across its markets in a manner that will optimize the returns on inventory investments. It believes a consistent sales pace through inventory turnover is the best way to maximize profits and returns. The company's homebuilding return on inventory (ROI) improved over the past three years from 15.4% in fiscal 2016 to 16.6% and 20.2% in fiscal 2017 and fiscal 2018, respectively. In fiscal 2019, ROI was 18.1%. With 307,300 lots (40% were owned and 60% controlled through option contracts) in inventory at the end of fiscal 2019, D.R. Horton is well poised for fiscal 2020.

▲ **Active Management of Cash Flows:** D.R. Horton has been actively managing cash flows, returning much of its free cash to investors through share repurchases and dividends. During fiscal 2019, the company returned more than \$1.4 billion to its shareholders through share repurchases and dividends, after reducing homebuilding debt by \$1.3 billion. In fiscal 2019, the company paid cash dividends of \$223.4 million and repurchased 11.9 million shares of common stock for \$479.8 million. In first-quarter fiscal 2020, the company paid dividends worth \$64.6 million and repurchased \$163.1 million shares. It has \$732.6 million remaining under the stock repurchase authorization (as of Dec 31, 2019), which has no expiration date. Management boosted its quarterly cash dividend by 17% to 17.50 cents per share in November 2019. It expects to pay dividends of approximately \$250 million in fiscal 2020.

Risks

- **Margin Pressure:** Rising land and labor costs are threatening margins as they limit homebuilders' pricing power. Labor shortages are leading to higher wages while land prices are inflating due to limited availability. Meanwhile, key cost pressures coming from finished lots, skilled labor, and rising materials costs may affect margins in all key regions. This is denting homebuilders' margins to some extent.
- **Federal Government Actions:** The housing industry is cyclical and affected by consumer confidence levels, prevailing economic conditions and interest rates. The federal government's actions related to economic stimulus, taxation and borrowing limits could affect consumer confidence and spending levels, which in turn could hurt both the economy and housing market.

Although strong economy along with labor market strength provide the basis for strong demand, its influence on the homebuilding industry is undeniable and uncertain. Indeed, any rise in interest and mortgage rates as well as land and labor shortages raise concerns, as do rising material prices. High mortgage rates dilute the demand for new homes as mortgage loans become expensive. This lower purchasing power of the buyers hurts volumes, revenues and profits of homebuilders.

- **Overvalued Compared to Peers:** The company's stretched valuation is another concern. Its trailing 12-month price to earnings ratio is 12.73, which is higher than the industry's 12.1. This implies that the stock is overvalued compared with its peers.
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Last Earnings Report

D.R. Horton Q1 Earnings & Revenues Top, Sales View Up

D.R. Horton, Inc. reported better-than-expected results in first-quarter fiscal 2020, thanks to its industry-leading market share, broad geographic footprint and affordable product offerings across multiple brands.

The homebuilder foresees demand to remain strong in the remainder of fiscal 2020. Solid demand, a limited supply of homes at affordable prices across the markets served, favorable economic fundamentals and financing availability, as well as 30,200 homes in inventory (at the end of December) make D.R. Horton well positioned for the spring selling season.

Quarter Ending **12/2019**

Report Date	Jan 27, 2020
Sales Surprise	6.48%
EPS Surprise	7.61%
Quarterly EPS	0.99
Annual EPS (TTM)	4.53

Earnings & Revenue Discussion

Adjusted earnings came in at 99 cents per share in the quarter, surpassing the Zacks Consensus Estimate of 92 cents by 7.6%. The reported figure also increased from the year-ago profit of 76 cents per share.

The quarterly results were adjusted for a tax benefit of \$32.9 million related to federal energy efficient homes tax credits that were retroactively reinstated during the quarter.

Total revenues (Homebuilding, Forestar and Financial Services) came in at \$4.02 billion, up 14.3% year over year. The reported figure also topped the consensus mark of \$3.78 billion.

Home Closings and Orders

Homebuilding revenues of \$3.88 billion increased 13.6% from the prior-year quarter. Home sales also increased 13.3% year over year to \$3.86 billion, aided by higher home deliveries. Also, land/lot sales and other revenues were \$19.7 million, increasing from \$6.7 million a year ago.

Home closings increased 13% from the prior-year quarter to 12,959 homes and 13% in value to \$3.9 billion. It recorded growth across regions comprising East, Midwest, Southeast, West and South Central, and Southwest.

Net sales orders increased 19% year over year to 13,126 homes, with improvement witnessed in East, Midwest, Southeast, South Central and West and Southwest. Value of net orders also improved 22% year over year to \$3.9 billion. The cancellation rate was 20%, lower than 24% in the prior-year quarter.

Revenues from the Financial Services segment increased 20.6% from the year-ago level to \$102.9 million. Forestar contributed \$247.2 million to its quarterly revenues, reflecting a notable improvement from \$38.5 million a year ago.

Margins

Gross margin on home sales revenue in the quarter was 21%, up 100 basis points (bps) year over year and flat sequentially. In the quarter, SG&A expense (as a percentage of homebuilding revenues) was 9.2%, down 30 bps from the prior year quarter. The company's consolidated pre-tax margin expanded 230 bps to 13% in the quarter.

Balance Sheet

D.R. Horton's cash, cash equivalents and restricted cash totaled \$1.58 billion as of Dec 31, 2019 compared with \$1.49 billion in the corresponding period of 2018. It repurchased 3 million shares of common stock for \$163.1 million during first-quarter fiscal 2020. The company has \$732.6 million remaining under the stock repurchase authorization (as of Dec 31, 2019), which has no expiration date.

Fiscal Q2 Guidance

The company expects revenues between \$4.25 billion and \$4.4 billion (indicating an increase from \$4.1 billion a year ago), homes closing within 13,800-14,300 units (depicting growth from 13,480 units of home closed a year ago), and home sales gross margin to be approximately 21% (compared with 19.3% in the year-ago period). Homebuilding SG&A expenses are expected to be around 9% of homebuilding revenues (flat year over year).

Guidance Revised Upward

The company expects revenues between \$18.5 billion and \$19.1 billion versus \$18.5-\$19 billion expected earlier, and homes closing within 60,000-61,500 compared with prior projection of 60,000-61,000. Effective tax rate is expected between 23% and 24% for the second, third and fourth quarters of fiscal 2020. Homebuilding cash flow from operations is projected in excess of \$1 billion. It intends to reduce share count by 2% in fiscal 2020.

Valuation

D.R. Horton shares are up 53.7% in the trailing 12-month period. Over the past year, the Zacks sub-industry and sector are up 47.2% and 27.2%, respectively.

The S&P 500 index is up 18.2% in the past year.

The stock is currently trading at 10.91X forward 12-month price to earnings, which compares to 11.14X for the Zacks sub-industry, 15.8X for the Zacks sector and 18.6X for the S&P 500 index.

Over the past five years, the stock has traded as high as 15.83X and as low as 7.36X, with a 5-year median of 11.39X. Our Outperform recommendation indicates that the stock will perform better than the market. Our \$66 price target reflects 12.48X forward 12-month earnings.

The table below shows summary valuation data for DHI.

Valuation Multiples - DHI					
		Stock	Sub-Industry	Sector	S&P 500
P/E F 12M	Current	10.91	11.14	15.8	18.6
	5-Year High	15.83	15.08	18.83	19.34
	5-Year Low	7.36	7.3	10.63	15.18
	5-Year Median	11.39	10.81	15.93	17.46
P/B TTM	Current	2.01	1.52	3.85	4.44
	5-Year High	2.49	2.27	7.22	4.54
	5-Year Low	1.36	1.01	2.19	2.85
	5-Year Median	1.82	1.56	3.41	3.62
P/S F12M	Current	1.07	1.05	1.89	3.45
	5-Year High	1.19	1.23	2.23	3.45
	5-Year Low	0.68	0.65	1.25	2.54
	5-Year Median	0.89	0.91	1.64	3

As of 02/04/2020

Industry Analysis Zacks Industry Rank: Top 15% (39 out of 255)



Top Peers

KB Home (KBH)	Outperform
M/I Homes, Inc. (MHO)	Outperform
Meritage Homes Corporation (MTH)	Outperform
NVR, Inc. (NVR)	Outperform
PulteGroup, Inc. (PHM)	Outperform
Beazer Homes USA, Inc. (BZH)	Neutral
Lennar Corporation (LEN)	Neutral
Toll Brothers Inc. (TOL)	Neutral

Industry Comparison Industry: Building Products - Home Builders				Industry Peers		
	DHI Outperform	X Industry	S&P 500	LEN Neutral	PHM Outperform	TOL Neutral
VGM Score	C	-	-	A	A	B
Market Cap	21.13 B	2.73 B	24.31 B	20.84 B	11.90 B	5.84 B
# of Analysts	11	3	13	6	7	7
Dividend Yield	1.21%	0.00%	1.78%	0.76%	1.09%	0.99%
Value Score	C	-	-	A	A	A
Cash/Price	0.12	0.11	0.04	0.06	0.10	0.21
EV/EBITDA	10.09	9.75	13.98	10.96	9.63	9.86
PEG Ratio	1.00	1.02	2.01	1.02	1.04	1.26
Price/Book (P/B)	2.01	1.28	3.29	1.30	2.18	1.22
Price/Cash Flow (P/CF)	12.53	9.61	13.58	10.88	11.29	9.44
P/E (F1)	11.03	10.80	18.82	10.55	10.78	11.35
Price/Sales (P/S)	1.17	0.74	2.66	0.94	1.17	0.81
Earnings Yield	9.07%	9.27%	5.30%	9.48%	9.28%	8.81%
Debt/Equity	0.36	0.50	0.71	0.49	0.51	0.77
Cash Flow (\$/share)	4.60	3.65	6.92	6.03	3.90	4.72
Growth Score	D	-	-	B	B	D
Hist. EPS Growth (3-5 yrs)	24.04%	16.66%	10.80%	15.42%	33.03%	25.00%
Proj. EPS Growth (F1/F0)	21.89%	12.77%	7.40%	8.39%	17.11%	-2.69%
Curr. Cash Flow Growth	3.66%	3.33%	10.22%	-6.27%	-2.58%	-11.99%
Hist. Cash Flow Growth (3-5 yrs)	23.21%	22.91%	8.55%	22.34%	15.54%	13.21%
Current Ratio	7.13	3.99	1.21	14.37	0.81	7.06
Debt/Capital	26.48%	32.66%	42.91%	32.66%	33.63%	43.38%
Net Margin	9.74%	6.78%	11.79%	8.31%	9.95%	8.17%
Return on Equity	16.92%	12.00%	17.24%	12.00%	19.38%	11.83%
Sales/Assets	1.16	0.97	0.55	0.76	0.99	0.69
Proj. Sales Growth (F1/F0)	9.58%	4.60%	4.10%	1.74%	9.95%	0.45%
Momentum Score	A	-	-	C	A	A
Daily Price Chg	-1.82%	-0.11%	1.49%	-1.56%	-1.30%	-0.11%
1 Week Price Chg	1.18%	-1.50%	-2.60%	-0.42%	2.15%	-2.72%
4 Week Price Chg	8.38%	8.38%	0.51%	14.84%	11.40%	8.45%
12 Week Price Chg	6.26%	10.98%	4.44%	12.13%	13.70%	12.37%
52 Week Price Chg	50.38%	32.42%	14.65%	39.88%	61.17%	19.33%
20 Day Average Volume	3,920,977	271,181	1,935,862	3,777,369	3,727,709	2,134,613
(F1) EPS Est 1 week change	0.41%	0.00%	0.00%	1.37%	1.67%	0.00%
(F1) EPS Est 4 week change	4.42%	0.00%	0.00%	3.20%	5.38%	0.00%
(F1) EPS Est 12 week change	10.59%	1.99%	-0.10%	3.93%	4.65%	-3.32%
(Q1) EPS Est Mthly Chg	5.28%	0.00%	0.00%	-5.45%	8.93%	0.00%

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	C
Growth Score	D
Momentum Score	A
VGM Score	C

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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