

D.R. Horton, Inc. (DHI)

\$48.53 (As of 05/11/20)

Price Target (6-12 Months): **\$51.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 03/29/20)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:C

Value: B

Growth: D

Momentum: C

Summary

D.R. Horton reported solid second-quarter fiscal 2020 results, wherein earnings topped analysts' expectations by 16.1% and grew 39.8% year over year. Although its revenues missed the same by 1.6%, the metric grew 9% from a year ago. Notably, fiscal second-quarter unit order growth was solid despite a rise in cancellations during March. Home closings were up 8% in units and 10% in value. D.R. Horton's shares have outperformed the industry year to date. It is well positioned for fiscal 2020, courtesy of its industry-leading market share, well-stocked supply of land, lots and homes, affordable product offerings and a solid balance sheet. However, uncertainties in the U.S. economy arising from the COVID-19 outbreak have raised a concern.

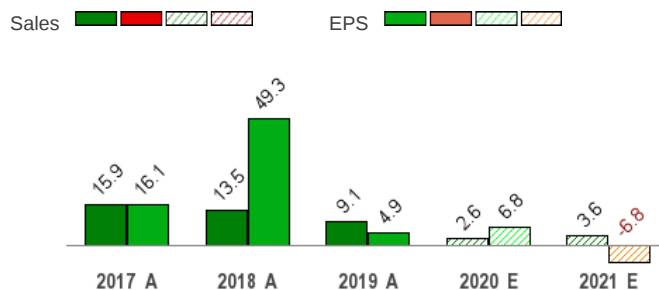
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$62.54 - \$25.51
20 Day Average Volume (sh)	4,476,815
Market Cap	\$17.6 B
YTD Price Change	-8.0%
Beta	1.57
Dividend / Div Yld	\$0.70 / 1.4%
Industry	Building Products - Home Builders
Zacks Industry Rank	Bottom 11% (226 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	16.1%
Last Sales Surprise	-1.6%
EPS F1 Est- 4 week change	-0.5%
Expected Report Date	08/04/2020
Earnings ESP	-3.4%
P/E TTM	9.9
P/E F1	10.6
PEG F1	1.0
P/S TTM	1.0

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	3,813 E	4,255 E	5,470 E	5,369 E	18,557 E
2020	4,021 A	4,500 A	4,967 E	4,543 E	17,917 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	\$0.76 E	\$0.88 E	\$1.34 E	\$1.37 E	\$4.27 E
2020	\$0.99 A	\$1.30 A	\$1.15 E	\$1.00 E	\$4.58 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 05/11/2020. The reports text is as of 05/12/2020.

Overview

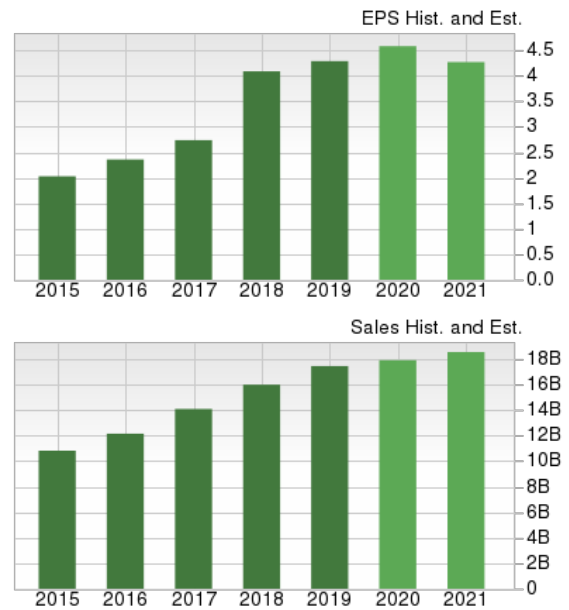
D.R. Horton, Inc., based in Texas, is one of the leading national homebuilders, primarily engaged in the construction and sale of single-family houses both in the entry-level and move-up markets. Homes vary in sizes from 1,000 to 4,000 square feet, with prices ranging from \$100,000 to more than \$1,000,000. 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 the industry year to date. The price performance was backed by the company's robust earnings surprise history, having surpassed the Zacks Consensus Estimate in seven of the trailing 10 quarters. Its revenues also surpassed the consensus mark in eight of the trailing 10 quarters. The trend is expected to continue in the near term as well, supported by its solid fiscal 2019 and first half of fiscal 2020 results. It finished 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-half 2020 as well, with adjusted earnings and revenues increasing 46.4% and 11.4%, 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

▲ **Accretive Acquisitions & Increased Capital Investments in Land:** In this unprecedented scenario, D.R. Horton has stopped new acquisitions, and deferred construction and other projects until it gets clearer visibility into market conditions.

That said, acquisitions have been an important part of D.R. Horton's growth strategy. The company 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 53% of its closings in second-quarter fiscal 2020.

▲ **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. In fiscal first-half 2020, SG&A improved 50 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 return on equity (ROE) was 19.1% in the trailing 12 months ended Mar 31, 2020 and homebuilding return on inventory (ROI) was 20.2%. Notably, 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 329,300 lots (36% were owned and 64% controlled through option contracts) in inventory at the end of the fiscal second quarter, D.R. Horton is well poised for fiscal 2020.

▲ **Healthy Balance Sheet:** Ample liquidity and a low leverage profile will help D.R. Horton tide over the unfavorable demand trends owing to the pandemic. The company ended the fiscal second quarter with \$1 billion of unrestricted homebuilding cash and \$1 billion of available capacity on the \$1.6-billion revolving credit facility, which resulted in total homebuilding liquidity of \$2 billion. The company's homebuilding debt to total capital on Mar 31, 2020 was 19.2%, down from 19.5% as of Dec 31, 2019. Its homebuilding debt (i.e. homebuilding notes payable) totaled \$2.48 billion on Mar 31, 2020 (versus \$2.47 billion as of Dec 31, 2019), with \$400 million of senior note maturities in the next 12 months.

Importantly, D.R. Horton has been actively managing cash flows, returning much of its free cash to investors through share repurchases and dividends. During the first six months of fiscal 2020, the company paid dividends worth \$128.7 million and repurchased \$360.4 million shares. It has \$535.3 million remaining under the stock repurchase authorization (as of Mar 31, 2020). Notably, 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.

Reasons To Sell:

▼ **Coronavirus-Led Uncertainties:** The recent economic slowdown resulting from shutdowns due to the coronavirus outbreak is a concern. Given uncertainties arising from the coronavirus outbreak, it experienced material slowdown in consumer traffic and sales activity beginning in mid-March, as state and local government authorities implemented various restrictions and stay-in-place orders to restrict the virus spread. Hence, the company has withdrawn its full-year guidance due to significant uncertainty surrounding the economy and duration of COVID-19.

The coronavirus outbreak, rising land/labor and material costs, competitive pricing pressure, and stretched valuation are major causes of concern

The COVID-19 outbreak and Cares Act Forbearance measures are disrupting the mortgage market. As a result, D.R. Horton experienced lower pricing and sales gains on the sale of mortgage loans and servicing rights in the secondary market in late March, stretching into April. The company suggests that purchasers and servicers of mortgages have become risk adverse, thereby limiting purchases and tightening credit standards due to liquidity and operational challenges caused by COVID-19 and the forbearance measures.

▼ **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.

▼ **Overvalued Compared to Peers:** The company's stretched valuation is another concern. Its trailing 12-month price to earnings ratio is 9.9, which is higher than the industry's 8.2. This implies that the stock is overvalued than peers.

Last Earnings Report

D.R. Horton's (DHI) Q2 Earnings Top Estimates

D.R. Horton, Inc. reported mixed results in second-quarter fiscal 2020, wherein earnings topped the Zacks Consensus Estimate but revenues lagged the same.

Its industry-leading market share, broad geographic footprint and affordable product offerings across multiple brands supported the growth. However, a drop in the demand for homes in late March on a year-over-year basis — owing to the persistent COVID-19 pandemic spread — somewhat impacted top-line growth.

The company witnessed increase in sales cancellations and decrease in orders to date in April compared with the prior-year period owing to the COVID-19 pandemic. Its net sales orders are approximately 11% lower year over year month to date in April. Its mortgage subsidiary — DHI Mortgage — has experienced lower pricing and gains on the sales of mortgage loans and servicing rights in late March and April due to disruption in secondary mortgage markets.

Uncertainties in business operations arising from the COVID-19 outbreak prompted D.R. Horton to withdraw its previously issued fiscal 2020 guidance.

Earnings & Revenue Discussion

The company reported adjusted earnings of \$1.30 per share in the quarter, surpassing the Zacks Consensus Estimate of \$1.12 by 16.1% and increasing 39.8% from the year-ago period.

Total revenues (Homebuilding, Forestar and Financial Services) came in at \$4.5 billion, up 9% year over year. However, the reported figure missed the consensus mark of \$4.57 billion by 1.6%.

Home Closings and Orders

Homebuilding revenues of \$4.38 billion increased 9.6% from the prior-year quarter. Home sales also increased 9.6% year over year to \$4.36 billion, aided by higher home deliveries. However, land/lot sales and other revenues were \$32.2 million, down from \$46.6 million a year ago.

Home closings increased 8% from the prior-year quarter to 14,539 homes and 10% in value to \$4.4 billion. It recorded growth across all regions comprising East, Midwest, Southeast, West and South Central, and Southwest.

Net sales orders in the quarter increased 20% year over year to 20,087 homes. It registered double-digit growth in all geographic regions served, except Southeast, which recorded 7% net sales order growth. Value of net orders also improved 22% year over year to \$6 billion. The cancellation rate was 19%, unchanged from the prior-year quarter.

Order backlog of homes at the end of the quarter was 19,328 homes, up 14% year over year. The value of backlogs was also up 18% from the prior year to \$5.9 billion.

Revenues from the Financial Services segment increased 2.9% from the year-ago level to \$104.5 million.

Forestar contributed \$159.1 million to its total quarterly revenues, reflecting a notable improvement from \$65.4 million a year ago.

Margins

Gross margin on home sales revenues in the quarter was 21.3%, up 200 basis points (bps) year over year and 30 bps sequentially. In the quarter, SG&A expense (as a percentage of homebuilding revenues) was 8.3%, down 70 bps from the prior year quarter. The company's consolidated pre-tax margin expanded 260 bps to 13.8% in the quarter.

Balance Sheet Details

D.R. Horton's cash, cash equivalents and restricted cash totaled \$1.52 billion as of Mar 31, 2020 compared with \$1.49 billion at fiscal 2019-end. At the end of the reported quarter, it had \$1 billion of unrestricted homebuilding cash and \$1 billion of available capacity on the \$1.6-billion revolving credit facility. Total homebuilding liquidity was \$2 billion. As of Mar 31, 2020, homebuilding debt totaled \$2.5 billion, with \$400 million of senior note maturities in the next 12 months. As of Mar 31, 2020, its homebuilding debt to total capital was 19.2%. Its trailing 12-month return on equity was 19.1%.

At the end of the fiscal second quarter, the company had 33,400 homes in inventory, of which 16,700 were unsold. It had 329,300 lots remaining, of which 36% were owned and 64% were controlled through land purchase contracts. It repurchased 4 million shares of common stock for \$197.3 million during second-quarter fiscal 2020. The company's remaining stock repurchase authorization — which has no expiration date — was \$535.3 million as of Mar 31, 2020. In the first half of fiscal 2020, cash used in operations was \$395.1 million compared with 461.7 million in the corresponding year-ago period.

Quarter Ending **03/2020**

Report Date	Apr 28, 2020
Sales Surprise	-1.60%
EPS Surprise	16.07%
Quarterly EPS	1.30
Annual EPS (TTM)	4.90

Valuation

D.R. Horton shares are down 8% in the year-to-date period but up 12.3% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Construction sector are down 15.4% and 20.9% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and sector are down 2.9% and 6.5%, respectively.

The S&P 500 index is down 9.1% in the year-to-date period but up 3.9% in the past year.

The stock is currently trading at 11.05X forward 12-month earnings, which compares to 9.97X for the Zacks sub-industry, 16.69X for the Zacks sector and 21.15X for the S&P 500 index.

Over the past five years, the stock has traded as high as 15.83X and as low as 5.44X, with a 5-year median of 11.23X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$51 price target reflects 11.62X 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 F12M	Current	11.05	9.97	16.69	21.15
	5-Year High	15.83	14.36	17.94	21.15
	5-Year Low	5.44	6.34	10.76	15.19
	5-Year Median	11.23	10.7	15.88	17.45
P/B TTM	Current	1.64	1.03	2.98	3.85
	5-Year High	2.49	2.29	6.73	4.55
	5-Year Low	1	0.66	1.7	2.84
	5-Year Median	1.81	1.53	3.27	3.65
P/S F12M	Current	0.96	0.82	1.62	3.3
	5-Year High	1.19	1.21	2.12	3.44
	5-Year Low	0.53	0.57	1.17	2.54
	5-Year Median	0.89	0.92	1.6	3.02

As of 05/11/2020

Industry Analysis Zacks Industry Rank: Bottom 11% (226 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
KB Home (KBH)	Neutral	3
Lennar Corporation (LEN)	Neutral	3
MI Homes Inc (MHO)	Neutral	4
Meritage Homes Corporation (MTH)	Neutral	4
NVR Inc (NVR)	Neutral	4
PulteGroup Inc (PHM)	Neutral	4
Toll Brothers Inc (TOL)	Neutral	3
Beazer Homes USA Inc (BZH)	Underperform	5

Industry Comparison Industry: Building Products - Home Builders				Industry Peers		
	DHI	X Industry	S&P 500	LEN	PHM	TOL
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	3	-	-	3	4	3
VGM Score	C	-	-	B	B	D
Market Cap	17.64 B	2.14 B	19.55 B	16.55 B	7.89 B	3.42 B
# of Analysts	16	5	14	7	7	7
Dividend Yield	1.44%	0.00%	2.13%	0.94%	1.63%	1.63%
Value Score	B	-	-	B	C	B
Cash/Price	0.16	0.22	0.06	0.05	0.23	0.15
EV/EBITDA	8.62	7.15	11.85	9.55	6.31	8.07
PEG Ratio	0.96	2.94	2.60	1.47	2.94	NA
Price/Book (P/B)	1.64	0.89	2.71	1.02	1.43	0.75
Price/Cash Flow (P/CF)	10.55	6.80	10.71	8.74	7.54	5.72
P/E (F1)	10.59	9.68	19.55	9.19	9.67	7.68
Price/Sales (P/S)	0.96	0.54	2.01	0.72	0.75	0.48
Earnings Yield	9.44%	10.33%	4.85%	10.87%	10.33%	13.00%
Debt/Equity	0.40	0.50	0.76	0.50	0.50	0.86
Cash Flow (\$/share)	4.60	3.90	7.01	6.06	3.90	4.72
Growth Score	D	-	-	B	A	F
Hist. EPS Growth (3-5 yrs)	23.17%	21.16%	10.82%	15.42%	32.78%	23.82%
Proj. EPS Growth (F1/F0)	6.83%	-12.54%	-9.99%	0.42%	-12.85%	-12.83%
Curr. Cash Flow Growth	3.66%	-3.09%	5.83%	-6.27%	-2.58%	-11.99%
Hist. Cash Flow Growth (3-5 yrs)	23.21%	21.78%	8.52%	22.34%	15.54%	13.21%
Current Ratio	7.25	4.63	1.27	12.65	0.81	6.82
Debt/Capital	28.63%	33.26%	44.41%	33.38%	33.26%	46.17%
Net Margin	10.26%	7.23%	10.59%	8.77%	10.02%	7.44%
Return on Equity	17.70%	12.76%	16.36%	12.76%	19.53%	10.81%
Sales/Assets	1.15	0.98	0.55	0.78	0.99	0.68
Proj. Sales Growth (F1/F0)	3.38%	-1.39%	-2.41%	1.61%	-5.58%	0.50%
Momentum Score	C	-	-	B	D	B
Daily Price Chg	-2.14%	-1.54%	-0.95%	-1.87%	-1.54%	-1.32%
1 Week Price Chg	6.55%	5.55%	3.23%	9.20%	9.69%	14.68%
4 Week Price Chg	25.63%	19.38%	4.49%	28.17%	18.63%	23.13%
12 Week Price Chg	-21.49%	-35.52%	-20.09%	-24.66%	-36.99%	-43.27%
52 Week Price Chg	12.26%	-12.37%	-7.00%	2.97%	-5.89%	-28.88%
20 Day Average Volume	4,476,815	491,769	2,530,553	3,226,253	4,710,496	2,427,518
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	-0.45%	-5.36%	-6.07%	0.00%	-23.77%	0.00%
(F1) EPS Est 12 week change	-13.00%	-26.45%	-15.69%	-7.35%	-25.59%	-10.42%
(Q1) EPS Est Mthly Chg	-3.12%	-3.12%	-12.45%	0.00%	-24.48%	0.00%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

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	B
Growth Score	D
Momentum Score	C
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.

Disclosures

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ZIR uses the following rating system for the securities it covers. **Outperform-** ZIR expects that the subject company will outperform the broader U.S. equities markets over the next six to twelve months. **Neutral-** ZIR expects that the company will perform in line with the broader U.S. equities markets over the next six to twelve months. **Underperform-** ZIR expects the company will underperform the broader U.S. equities markets over the next six to twelve months.

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