

## Toll Brothers Inc.(TOL)

**\$44.07** (As of 01/15/20)

Price Target (6-12 Months): **\$46.00**

Long Term: 6-12 Months

**Zacks Recommendation:**

**Neutral**

(Since: 12/04/19)

Prior Recommendation: Outperform

Short Term: 1-3 Months

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

**4-Sell**

Zacks Style Scores:

VGM:C

Value: A

Growth: D

Momentum: D

## Summary

Shares of Toll Brothers have underperformed its industry over the past year. Challenging sales conditions in the luxury home markets and rising building materials and labor costs have been impacting the company's performance over the past few quarters. Estimates for the current quarter and fiscal 2020 have also witnessed downward trend depicting analysts' concern over the stock's potential. However, a solid job market, rise in new orders, falling unemployment rate, increasing wages and a limited home supply bode well for the company. Toll Brothers is well positioned to gain from geographic expansions, resilient economy, rise in demand and improving demographics in the near term. Moreover, its solid land position places it well to meet growing demand and mitigate risk. Its focus on low-priced luxury homes is encouraging.

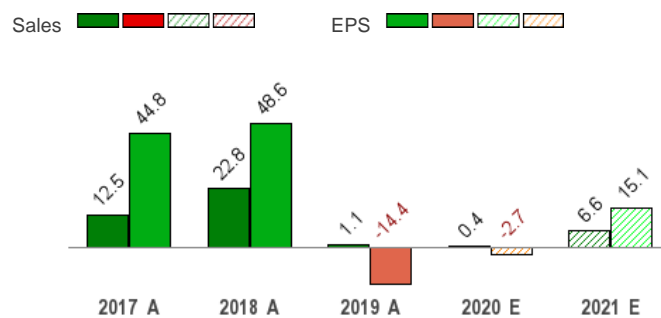
## Price, Consensus & Surprise



## Data Overview

52 Week High-Low	\$44.37 - \$33.52
20 Day Average Volume (sh)	2,076,330
Market Cap	\$6.1 B
YTD Price Change	11.5%
Beta	0.88
Dividend / Div Yld	\$0.44 / 1.0%
Industry	<a href="#">Building Products - Home Builders</a>
Zacks Industry Rank	Top 26% (67 out of 254)

## Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	9.3%
Last Sales Surprise	9.4%
EPS F1 Est- 4 week change	-1.1%
Expected Report Date	02/25/2020
Earnings ESP	-1.1%
P/E TTM	10.9
P/E F1	11.2
PEG F1	1.3
P/S TTM	0.9

## Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	1,549 E	1,759 E	2,102 E	2,678 E	7,732 E
2020	1,411 E	1,661 E	1,846 E	2,339 E	7,256 E
2019	1,363 A	1,716 A	1,766 A	2,379 A	7,224 A

## EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.59 E	\$0.88 E	\$1.34 E	\$1.95 E	\$4.51 E
2020	\$0.45 E	\$0.77 E	\$1.07 E	\$1.59 E	\$3.92 E
2019	\$0.76 A	\$0.87 A	\$1.00 A	\$1.41 A	\$4.03 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 01/15/2020. The reports text is as of 01/16/2020.

## Overview

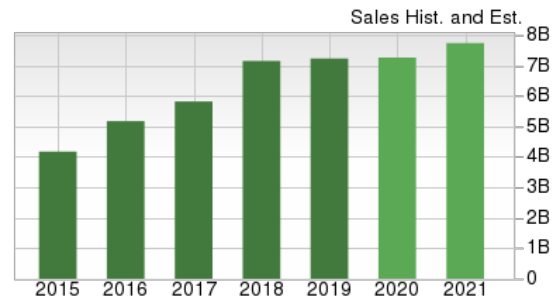
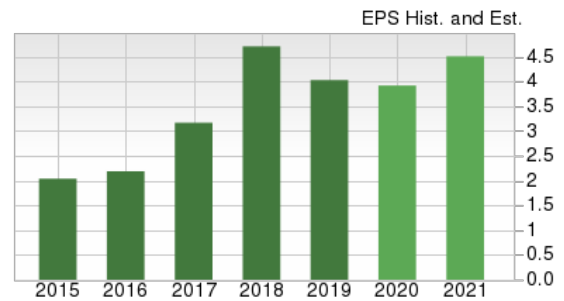
Based in Horsham, PA, Toll Brothers Inc. builds single-family detached and attached home communities; master planned luxury residential resort-style golf communities; and urban low, mid, and high-rise communities, principally on the land it develops and improves.

The company operates in Arizona, California, Florida, Delaware, Maryland, Pennsylvania, and South Carolina. Toll Brothers offers homes under two segments, namely Traditional Home Building Product and City Living.

Traditional Home Building (accounting for 98.8% of fiscal fourth-quarter 2019 revenues) include detached and attached homes for move-up, empty-nester, active-adult, age-qualified, as well as second-home buyers. Within Traditional Home Building Products, Toll Brothers operates in four geographical segments, North, Mid Atlantic, South and West. City Living (1.2%) includes homes built and sold in urban infill markets.

Since November 2018, the company started reporting land sale activities under the Land sales category (3.7%).

Toll Brothers is also building homes for rental apartment projects. Toll Brothers Apartment Living, Toll Brothers Realty Trust and Toll Brothers Campus Living are brands offered under this rental apartment projects. These rental projects operate in lucrative markets like metro-Boston to metro-Washington, D.C. corridor and Atlanta.



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## Reasons To Buy:

▲ **Limited Competition in the Luxury Housing Market:** Toll Brothers mostly offers luxury homes and its communities are located in prosperous suburban areas with easy access to major cities. Luxury homes generally face limited competition. The company mostly caters to luxury move up buyers, who already possess a residence and are looking for a shift to larger and better homes. These homebuyers are less sensitive to price changes. Toll Brothers enjoys greater pricing power than other homebuilding companies.

Strong housing demand and lack of competition in the luxury new home market is expected to drive revenues

▲ **Significant Land Positions, Boosting Presence:** Given the significant pent up housing demand, Toll Brothers has secured some of the most sought-after urban locations in the country, where land is scarce and approvals are not easy to obtain. Toll Brothers is using its strong liquidity position to secure the most sought-after urban locations in the country like New York City Market, Northern New Jersey, Washington D.C. and Philadelphia. The company's solid land position places it well to meet growing demand in these regions, thus giving it a competitive edge over its peers who are presently facing land availability constraints.

The company has been expanding geographically. In 2019, the company expanded its footprint to four new states and seven new markets. It also opened first communities in Salt Lake City, Utah and Portland, Oregon markets. Toll Brothers is expanding northward in Florida's west coast into Tampa. Meanwhile, the company has been serving urban and suburban renters. In a bid to expand its reach in Atlanta, Georgia, Charleston, Greenville, Myrtle Beach and South Carolina markets, the company acquired Sharp Residential LLC ("Sharp") and Sabal Homes LLC ("Sabal") in fiscal 2019. Through Toll Brothers Apartment Living, it had a pipeline of 20,000 units in various stages of approval and development across the country, as of fourth-quarter fiscal 2019. With improving demographics, low interest rates, record low unemployment, continued wage growth, and limited new and resale inventory in many markets, the company remains optimistic about the opportunities that lie ahead.

▲ **Housing Market Fundamentals Remain Steady:** After a torrid second-half 2018, the U.S. housing market started building up strength since the beginning of 2019. Declining mortgage rates & construction costs, along with moderate home prices have been adding strength to Toll Brothers and other homebuilders. Again, solid job market, falling unemployment rate, increasing wages and a limited home supply are somewhat offsetting the ongoing industry headwinds.

Given the favorable housing market fundamentals, Toll Brothers has witnessed a rise in consumer demand thereby resulting in growth in new orders. In the fourth quarter of fiscal 2019, its net signed contracts or orders were 2,031 units, up 18.4% year over year. The value of net signed contracts was \$1.68 billion, reflecting 11.8% increase from the year-ago quarter. Notably, the company has also witnessed strong demand in the first six weeks of first-quarter fiscal 2020 as compared with the fourth quarter of fiscal 2019. The rise in the number of contracts will thereby help the company boost revenues throughout fiscal 2020.

▲ **Active Management of Cash Flows:** Toll Brothers has been actively managing cash flows, returning much of its free cash to investors through share repurchases and dividends. During fiscal 2019, the company repurchased 6.6 million shares, at an average price of \$35.28 per share, for a total purchase price of \$233.5 million. In fiscal 2019, the company paid out cash dividends of \$0.44 per share. The company has over \$3 billion of liquidity through cash and undrawn bank credit facilities for fiscal 2020.

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## Reasons To Sell:

- ▼ **Softness in the High-End Housing Market:** Demand in the high-end housing market has been declining in recent times. The main reason behind the same was reduced activity of wealthy overseas purchasers, many of whom seek out amenity-rich, full-service communities with on-site property management. This is mostly affecting California, which typically accounts for more than one third of purchases by Chinese buyers, and the products that are sold at a high price point in New York. Again, reduced SALT deductions — particularly in high-tax states like California, New York, New Jersey and Connecticut — have been impacting higher-end real estate markets.

Precisely, the company's first quarter of fiscal 2020 guidance for deliveries reflects increased focus on the affordable luxury segment and a reduction in the number and mix of homes being delivered in California to more lower-priced and attached homes.

Softness in the high-end housing market, declining orders, lower deliveries and gross margin pressure are raising concerns.

- ▼ **Rising Material Costs:** Rising building materials and labor costs are growing concerns for the company's margin. Land prices are inflating due to limited availability. This could eat into homebuilders' margins in the forthcoming quarters. Moreover, tariff-related woes are also pressing concern.

Notably, the company's adjusted home sales gross margin also declined by 70 basis points (bps) during fiscal 2019 as compared with the year-ago period. Also, operating margin declined by 160 basis points in fiscal 2019 as compared with the year-ago period. Furthermore, Toll Brothers expects fiscal first-quarter 2020 adjusted home sales gross margin of 21.3%, implying a decline from 24.2% recorded in the year-ago period.

Also, estimates for the current quarter and fiscal 2020 have been trending downward over the past 30 days, depicting analysts' concern for future performance of the company. Also, shares of Toll Brothers have underperformed its industry in the past year.

- ▼ **Federal Government Actions:** The housing industry is cyclical and is 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 the 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, rising 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 and hurts volumes, revenues and profits of homebuilders.

Additionally, the rise in mortgage rates may impact affordability at a time when millennials are taking baby steps into the housing market. Higher interest rates will only flare up the issues and further delay home purchases by millennials.

## Last Earnings Report

### Toll Brothers Q4 Earnings Top, Orders Rise

Toll Brothers, Inc.'s (T) reported its fourth-quarter fiscal 2019 results, wherein earnings and revenues topped the respective Zacks Consensus Estimate. The company also remains optimistic about attaining higher deliveries in first-quarter fiscal 2020, courtesy of lower mortgage rates and a solid job market.

#### Earnings & Revenue Discussion

The country's leading luxury homebuilder reported earnings of \$1.41 per share in the quarter under review, surpassing the Zacks Consensus Estimate of \$1.29 by 9.3%. However, the said figure dropped 32.2% from the year-ago figure of \$2.08 as a result of lower revenues and margins.

Consolidated revenues of \$2.38 billion topped the consensus mark of \$2.18 billion by 9.4%. The reported figure, however, decreased 3.1% year over year due to lower deliveries and average selling prices.

#### Segment Detail

Toll Brothers operates under two reportable segments, namely Traditional Home Building and Urban Infill ("City Living").

Revenues from Traditional Home Building totaled \$2.26 billion, down 5.4% year over year and that of City Living decreased 54.7% to \$28.6 million during the quarter.

#### Inside the Headline Numbers

Consolidated homebuilding revenues decreased 6.6% year over year to \$2.29 billion. Homebuilding deliveries during the quarter declined 1.4% year over year to 2,672 units. Deliveries decreased in all the regions served by the company, except South. Deliveries in Citi Living declined to 28 units from 47 units a year ago. The average price of homes delivered was \$857,800 in the quarter, down 5.3% from the year-ago level of \$906,000.

Nonetheless, the number of net signed contracts or orders during the reported quarter was 2,031 units, up 18.4% year over year. The value of net signed contracts was \$1.68 billion, reflecting 11.8% increase from the year-ago quarter.

At the end of fiscal 2019, Toll Brothers had a backlog of 6,266 homes, representing a 2.6% year-over-year increase. However, potential revenues from backlog declined 4.8% year over year to \$5.26 billion owing to a 7.3% decline in average price of homes in backlog. Cancellation rate during the reported quarter was 8.9%, reflecting a decline from 9.3% in the prior-year period.

#### Margins

The company's home sales adjusted gross margin was 21.9%, contracting 220 basis points (bps) in the quarter. SG&A expenses — as a percentage of home sales revenues — were 9%, up 140 bps from the year-ago quarter. Operating margin of 9.5% was down 430 bps in the quarter.

#### Financials

Toll Brothers had \$1.29 billion cash and cash equivalents as of Oct 31, 2019 compared with \$1.18 billion at fiscal 2018-end.

During fiscal 2019, the company repurchased 6.6 million shares, at an average price of \$35.28 per share, for a total purchase price of \$233.5 million.

#### Fiscal 2019 Highlights

Earnings per share came in at \$4.03 in the fiscal year, down 16.9% year over year. Nonetheless, consolidated revenues of \$7.22 billion were up 1.1% from a year ago. Homebuilding revenues were down 0.9% year over year to \$7.08 billion. Net signed contracts of \$6.71 billion and 8,075 units were down 12% in dollars and 5% in units compared with \$7.60 billion and 8,519 units in fiscal 2018.

#### First-Quarter Fiscal 2020 Guidance

For the quarter, home deliveries are anticipated in the range of 1,650-1,850 units (indicating an increase from 1,530 units reported in the year-ago period) at an average price of \$800,000-\$820,000 (suggesting a decrease from the year-ago figure of \$862,300). Toll Brothers expects adjusted home sales gross margin of 21.3%, implying a decline from 24.2% recorded in the year-ago period. SG&A expenses, as a percentage of home sales revenues, for the quarter are projected at 13.5% (indicating an increase from 12.3% in the year-ago period).

Quarter Ending **10/2019**

Report Date	Dec 09, 2019
Sales Surprise	9.36%
EPS Surprise	9.30%
Quarterly EPS	1.41
Annual EPS (TTM)	4.04

## Valuation

Toll Brothers shares are up 20.9% in the past six month period and 25.3% in the and trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Construction sector are up 21.2% and 14.9% in the past six month period, respectively. Over the past year, the Zacks sub-industry and sector are up 41.2% and 32%, respectively.

The S&P 500 index is up 10.6% in the past six month period and 23.6% in the past year.

The stock is currently trading at 10.9X forward 12-month price to earnings, which compares to 10.75X for the Zacks sub-industry, 15.85X for the Zacks sector and 18.96X for the S&P 500 index.

Over the past five years, the stock has traded as high as 17.99X and as low as 5.48X, with a 5-year median of 9.97X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$46 price target reflects 11.39X forward 12-month earnings.

The table below shows summary valuation data for TOL

Valuation Multiples - TOL					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	10.9	10.75	15.85	18.96
	5-Year High	17.99	15.08	18.83	19.34
	5-Year Low	5.48	7.3	10.63	15.17
	5-Year Median	9.97	10.75	15.97	17.44
P/B TTM	Current	1.21	1.44	3.86	4.49
	5-Year High	1.89	2.27	7.22	4.49
	5-Year Low	0.93	1.01	2.19	2.85
	5-Year Median	1.23	1.57	3.4	3.61
P/S F12M	Current	0.83	1	1.92	3.52
	5-Year High	1.55	1.23	2.23	3.52
	5-Year Low	0.54	0.65	1.25	2.54
	5-Year Median	0.88	0.92	1.63	3

As of 01/15/2020

## Industry Analysis Zacks Industry Rank: Top 26% (67 out of 254)



## Top Peers

KB Home (KBH)	Outperform
Persimmon Plc (PSMMY)	Outperform
D.R. Horton, Inc. (DHI)	Neutral
Meritage Homes Corporation (MTH)	Neutral
NVR, Inc. (NVR)	Neutral
PulteGroup, Inc. (PHM)	Neutral
Taylor Morrison Home Corporation (TMHC)	Neutral
Taylor Wimpey PLC Unsponsored ADR (TWODY)	Neutral

Industry Comparison Industry: Building Products - Home Builders				Industry Peers		
	TOL Neutral	X Industry	S&P 500	MTH Neutral	NVR Neutral	TWODY Neutral
<b>VGM Score</b>	<b>C</b>	-	-	<b>A</b>	<b>B</b>	<b>A</b>
Market Cap	6.11 B	2.60 B	24.22 B	2.56 B	14.36 B	8.87 B
# of Analysts	6	3	13	10	2	1
Dividend Yield	1.00%	0.00%	1.75%	0.00%	0.00%	3.26%
<b>Value Score</b>	<b>A</b>	-	-	<b>B</b>	<b>C</b>	<b>B</b>
Cash/Price	0.22	0.10	0.04	0.19	0.11	0.07
EV/EBITDA	10.18	10.18	14.11	10.97	13.45	NA
PEG Ratio	1.30	1.01	2.06	1.11	1.63	-7.40
Price/Book (P/B)	1.21	1.29	3.34	1.36	6.08	2.29
Price/Cash Flow (P/CF)	9.35	9.45	13.57	10.49	17.27	9.38
P/E (F1)	11.26	10.51	18.90	9.88	17.54	10.36
Price/Sales (P/S)	0.85	0.72	2.65	0.73	1.99	NA
Earnings Yield	8.89%	9.52%	5.29%	10.13%	5.70%	9.65%
Debt/Equity	0.77	0.62	0.72	0.70	0.29	0.04
Cash Flow (\$/share)	4.72	3.60	6.94	6.36	226.10	2.88
<b>Growth Score</b>	<b>D</b>	-	-	<b>A</b>	<b>B</b>	<b>B</b>
Hist. EPS Growth (3-5 yrs)	25.00%	16.06%	10.56%	14.41%	29.89%	NA
Proj. EPS Growth (F1/F0)	-2.73%	12.95%	7.59%	19.22%	3.25%	-1.14%
Curr. Cash Flow Growth	-11.99%	18.07%	14.73%	41.54%	31.22%	10.45%
Hist. Cash Flow Growth (3-5 yrs)	13.21%	23.21%	9.00%	13.19%	23.91%	NA
Current Ratio	7.06	4.04	1.24	1.30	4.73	3.35
Debt/Capital	43.38%	36.98%	42.99%	41.15%	22.38%	3.49%
Net Margin	8.17%	6.29%	11.14%	6.29%	11.82%	NA
Return on Equity	11.83%	12.16%	17.16%	12.42%	41.69%	NA
Sales/Assets	0.69	0.97	0.55	1.02	2.07	NA
Proj. Sales Growth (F1/F0)	0.45%	4.83%	4.23%	7.88%	5.37%	0.02%
<b>Momentum Score</b>	<b>D</b>	-	-	<b>C</b>	<b>B</b>	<b>A</b>
Daily Price Chg	2.92%	1.91%	0.27%	3.47%	2.22%	0.19%
1 Week Price Chg	1.35%	1.98%	0.39%	3.24%	-0.00%	0.00%
4 Week Price Chg	11.54%	7.68%	2.17%	7.11%	4.50%	2.11%
12 Week Price Chg	7.78%	1.83%	6.65%	-10.25%	3.42%	24.60%
52 Week Price Chg	23.20%	37.73%	22.43%	67.15%	54.28%	23.18%
20 Day Average Volume	2,076,330	227,980	1,545,017	512,801	26,293	15
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	-1.12%	0.00%	0.00%	0.15%	0.00%	0.00%
(F1) EPS Est 12 week change	-3.36%	2.52%	-0.41%	5.97%	2.20%	2.76%
(Q1) EPS Est Mthly Chg	-10.75%	0.00%	0.00%	0.00%	NA	NA

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## 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.

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### 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	A
Growth Score	D
Momentum Score	D
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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