

Toll Brothers, Inc.

F4Q beats; Increased spec supports F2024 delivery and earnings growth outlook

Reiterate Rating: BUY | PO: 103.00 USD | Price: 88.90 USD

Reiterate Buy; F24 earnings outlook better than expected

Toll Brothers (TOL) reported F4Q23 (ended October) EPS ahead of our/consensus estimates. Our key takeaways: 1) F2024 earnings outlook is better than we expected, primarily due to stronger deliveries, 2) continued shift to spec building (expect 35% deliveries) should support delivery growth in F2024, 3) demand was steady through the quarter despite the spike in mortgage rates (net pricing increased sequentially in quarter), and 4) ROE in F2024 remain at elevated levels (high-teens%). We raise our F2024 EPS estimate to \$11.99 (from \$11.25) to reflect the stronger delivery. We reiterate our Buy rating; valuation remains attractive relative other builders with similar ROE profiles. We raise our PO to \$103 (from \$98) still based on 1.4X price-to-forward 12-month book value.

Orders in-line w/ normal seasonality, but could improve

TOL's F4Q orders increased 71.8% YoY to 2.0k (slightly above our forecast) and fell 9% QoQ, roughly in-line with normal seasonality. Demand was steady throughout the quarter. In the first five weeks of F1Q, customer deposits are trending in-line with historical absorption pace of down 20% QoQ. Management sees potential that demand improves from the current levels with the decline in mortgage rates quarter-to-date.

GM outlook stable as favorable pricing offsets mix

TOL is guiding to FY 2024 gross margin of 27.9%, down just 80bps YoY against a high base in F2023. Net pricing increased \$16K per home in F4Q (+\$12K base prices, -\$4K incentives), and order ASP was up 3% QoQ on mix. TOL anticipates average selling price to decline 7-8% in F2024 driven by mix to lower price affordable luxury and spec.

Spec mix driving deliveries higher in F2024; ROE accretive

TOL has increased its spec production meaningfully over the last two years. In F2023, spec sales made up 22% of orders/33% of deliveries vs. historical levels of 15%-20%. In 2024, TOL expects to maintain spec at 35% of deliveries. While spec homes carry gross margin ~250 bps lower than built-to-order, the build cycle is two months shorter, which supports a much higher return-on-inventory (and ROE).

F4Q beats on SG&A; 2024 guidance ahead of expectations

TOL reported F4Q EPS of \$4.11 above our \$3.89 estimate driven by stronger deliveries and lower SG&A. TOL initiated F2024 EPS guidance of \$12-\$12.50, above consensus of \$11.65.

| Estimates (Oct) (US\$) | 2022A | 2023A | 2024E | 2025E | 2026E |
|---------------------------|-------|-------|-------|-------|-------|
| EPS | 10.90 | 12.36 | 11.99 | 11.35 | 12.38 |
| EPS Change (YoY) | 57.5% | 13.3% | -3.0% | -5.4% | 9.1% |
| Consensus EPS (Bloomberg) | | | 11.85 | 12.75 | NA |
| DPS | 0.74 | 0.83 | 0.84 | 0.84 | 0.84 |
| Valuation (Oct) | | | | | |
| P/E | 8.2x | 7.2x | 7.4x | 7.8x | 7.2x |
| Dividend Yield | 0.8% | 0.9% | 0% | 0% | 0.9% |
| EV / EBITDA* | 6.1x | 5.7x | 6.1x | 6.7x | 6.5x |
| Free Cash Flow Yield* | 9.3% | 12.7% | 21.3% | 7.5% | 5.7% |

* For full definitions of *IQmethod*SM measures, see page 4.

07 December 2023

Equity

Key Changes

| (US\$) | Previous | Current |
|------------|----------|---------|
| Price Obj. | 98.00 | 103.00 |
| 2024E EPS | 11.24 | 11.99 |
| 2025E EPS | 10.60 | 11.35 |
| 2026E EPS | 11.34 | 12.38 |

Rafe Jadrosich

Research Analyst
BofAS
+1 646 855 5815
rafe.jadrosich@bofa.com

Shaun Calnan, CFA

Research Analyst
BofAS
shaun.calnan@bofa.com

Victoria Piskarev

Research Analyst
BofAS
victoria.piskarev@bofa.com

Stock Data

| | |
|---------------------------------|-----------------------|
| Price | 88.90 USD |
| Price Objective | 103.00 USD |
| Date Established | 7-Dec-2023 |
| Investment Opinion | B-1-7 |
| 52-Week Range | 46.72 USD - 91.10 USD |
| Mrkt Val (mn) / Shares Out (mn) | 9,869 USD / 111.0 |
| Free Float | 99.4% |
| Average Daily Value (mn) | 119.99 USD |
| BofA Ticker / Exchange | TOL / NYS |
| Bloomberg / Reuters | TOL US / TOL.N |
| ROE (2024E) | 17.4% |
| Net Dbt to Eqty (Oct-2023A) | 22.9% |
| ESGMeter TM | Medium |

ESGMeterTM is not indicative of a company's future stock price performance and is not an investment recommendation or rating. ESGMeter is independent of BofA Global Research's equity investment rating, volatility risk rating, income rating, and price objective for that company. For full details, refer to ["BofA ESGMeter Methodology"](#).

ASP: Average Selling Price

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Timestamp: 07 December 2023 02:18AM EST

iQprofileSM Toll Brothers, Inc.

iQmethodSM – Bus Performance*

| (US\$ Millions) | 2022A | 2023A | 2024E | 2025E | 2026E |
|----------------------------|-------|-------|-------|-------|-------|
| Return on Capital Employed | 15.5% | 15.6% | 13.5% | 11.4% | 11.1% |
| Return on Equity | 22.8% | 21.4% | 17.4% | 14.1% | 13.5% |
| Operating Margin | 14.7% | 17.3% | 16.5% | 15.0% | 14.4% |
| Free Cash Flow | 915 | 1,258 | 2,098 | 738 | 564 |

iQmethodSM – Quality of Earnings*

| (US\$ Millions) | 2022A | 2023A | 2024E | 2025E | 2026E |
|--------------------------|-------|-------|-------|-------|-------|
| Cash Realization Ratio | 0.8x | 1.0x | 1.8x | 0.8x | 0.6x |
| Asset Replacement Ratio | 0.9x | 1.2x | 1.5x | 1.4x | 1.4x |
| Tax Rate | 24.5% | 25.5% | 26.0% | 26.0% | 26.0% |
| Net Debt-to-Equity Ratio | 32.9% | 22.9% | -2.6% | -5.0% | -5.2% |
| Interest Cover | NM | NM | NA | NA | NA |

Income Statement Data (Oct)

| (US\$ Millions) | 2022A | 2023A | 2024E | 2025E | 2026E |
|------------------------------|--------------|--------------|--------------|---------------|--------------|
| Sales | 10,276 | 9,995 | 9,566 | 9,783 | 10,331 |
| % Change | 16.9% | -2.7% | -4.3% | 2.3% | 5.6% |
| Gross Profit | 2,486 | 2,634 | 2,524 | 2,412 | 2,480 |
| % Change | NA | NA | NA | NA | NA |
| EBITDA | 1,950 | 2,068 | 1,938 | 1,767 | 1,827 |
| % Change | 39.2% | 6.0% | -6.3% | -8.8% | 3.4% |
| Net Interest & Other Income | 195 | 118 | 120 | 60 | 80 |
| Net Income (Adjusted) | 1,287 | 1,372 | 1,259 | 1,128 | 1,163 |
| % Change | 48.2% | 6.7% | -8.3% | -10.3% | 3.1% |

Free Cash Flow Data (Oct)

| (US\$ Millions) | 2022A | 2023A | 2024E | 2025E | 2026E |
|--|------------|--------------|--------------|------------|------------|
| Net Income from Cont Operations (GAAP) | 1,287 | 1,372 | 1,259 | 1,128 | 1,163 |
| Depreciation & Amortization | 77 | 76 | 93 | 95 | 101 |
| Change in Working Capital | (353) | (205) | 931 | (363) | (551) |
| Deferred Taxation Charge | (97) | 6 | 0 | 0 | 0 |
| Other Adjustments, Net | 73 | 100 | (48) | 12 | (8) |
| Capital Expenditure | (72) | (92) | (137) | (135) | (141) |
| Free Cash Flow | 915 | 1,258 | 2,098 | 738 | 564 |
| % Change | NA | NA | NA | NA | NA |
| Share / Issue Repurchase | (543) | (389) | (440) | (440) | (440) |
| Cost of Dividends Paid | (89) | (92) | (88) | (84) | (82) |
| Change in Debt | 0 | (5) | 0 | 0 | 0 |

Balance Sheet Data (Oct)

| (US\$ Millions) | 2022A | 2023A | 2024E | 2025E | 2026E |
|---------------------------------------|---------------|---------------|---------------|---------------|---------------|
| Cash & Equivalents | 1,347 | 1,300 | 3,062 | 3,276 | 3,321 |
| Trade Receivables | NA | NA | NA | NA | NA |
| Other Current Assets | 9,481 | 9,749 | 8,741 | 9,129 | 9,715 |
| Property, Plant & Equipment | 288 | 324 | 368 | 407 | 448 |
| Other Non-Current Assets | 1,174 | 1,154 | 1,154 | 1,154 | 1,154 |
| Total Assets | 12,289 | 12,527 | 13,325 | 13,967 | 14,638 |
| Short-Term Debt | 1,334 | 1,264 | 1,264 | 1,264 | 1,264 |
| Other Current Liabilities | 2,937 | 2,853 | 2,777 | 2,801 | 2,837 |
| Long-Term Debt | 1,995 | 1,596 | 1,596 | 1,596 | 1,596 |
| Other Non-Current Liabilities | 0 | 0 | 0 | 0 | 0 |
| Total Liabilities | 6,267 | 5,714 | 5,637 | 5,662 | 5,697 |
| Total Equity | 6,022 | 6,813 | 7,688 | 8,305 | 8,941 |
| Total Equity & Liabilities | 12,289 | 12,527 | 13,325 | 13,967 | 14,638 |

* For full definitions of iQmethodSM measures, see page 4.

Company Sector

Homebuilders

Company Description

Toll Brothers is a leading US homebuilder with a focus on luxury suburban and urban markets. TOL operates in six distinct segments, focusing on highly customized homes. The company builds luxury, affordable luxury (millennial focus) and active-adult communities.

Investment Rationale

We rate TOL share Buy. Positives include: (1) TOL has yet to see the full impact of price increases due to its longer build cycles and (2) roughly 75% of the owned land on the balance sheet was purchased pre-pandemic (roughly 3 year supply) and should provide a long runway for healthy margins.

Stock Data

Average Daily Volume

1,349,663

Quarterly Earnings Estimates

| | 2023 | 2024 |
|----|-------|-------|
| Q1 | 1.70A | 1.80E |
| Q2 | 2.85A | 3.06E |
| Q3 | 3.73A | 3.35E |
| Q4 | 4.11A | 3.83E |

Price objective basis & risk

Toll Brothers, Inc. (TOL)

Our \$103 PO on TOL shares is based on a price to forward 12-month book value multiple of roughly 1.4x, a slight discount to TOL's historical multiple (1.5x price to book value), which we view as appropriate given increasing affordability concerns and difficult comparisons.

Downside risks: (1) Luxury home demand could suffer an outsized decline during economic slowdowns, (2) Mid-Atlantic and Northeastern markets tend to grow more slowly, (3) potential earnings volatility given historically lumpy City Living sales, although this segment is now a small portion of TOL's overall business, (4) worsening affordability from rising rates, (5) supply chain issues and (6) slowing US economic growth.

Upside risks: (1) Luxury home demand could benefit by an outsized amount during economic strengthening, (2) Mid-Atlantic and Northeastern markets could grow more quickly, (3) improved lending markets could positively impact potential TOL customers needing to sell an existing home.

Analyst Certification

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US - Homebuilders and Building Products Coverage Cluster

| Investment rating | Company | BofA Ticker | Bloomberg symbol | Analyst |
|---------------------|----------------------------------|-------------|------------------|-------------------|
| BUY | | | | |
| | Armstrong World Industries, Inc. | AWI | AWI US | Rafe Jadrosich |
| | D.R. Horton, Inc. | DHI | DHI US | Rafe Jadrosich |
| | Latham Group, Inc. | SWIM | SWIM US | Shaun Calnan, CFA |
| | NVR, Inc. | NVR | NVR US | Rafe Jadrosich |
| | Owens Corning | OC | OC US | Rafe Jadrosich |
| | PulteGroup Inc. | PHM | PHM US | Rafe Jadrosich |
| | The AZEK Company Inc. | AZEK | AZEK US | Rafe Jadrosich |
| | Toll Brothers, Inc. | TOL | TOL US | Rafe Jadrosich |
| | TopBuild Corp | BLD | BLD US | Rafe Jadrosich |
| | Trex Company, Inc. | TREX | TREX US | Rafe Jadrosich |
| NEUTRAL | | | | |
| | Builders FirstSource Inc | BLDR | BLDR US | Rafe Jadrosich |
| | Dream Finders Homes, Inc. | DFH | DFH US | Rafe Jadrosich |
| | KB Home | KBH | KBH US | Rafe Jadrosich |
| | Lennar Corporation | LEN | LEN US | Rafe Jadrosich |
| UNDERPERFORM | | | | |
| | Fortune Brands Innovations Inc | FBIN | FBIN US | Rafe Jadrosich |
| | Hayward Holdings, Inc. | HAYW | HAYW US | Rafe Jadrosich |
| | Masco Corp | MAS | MAS US | Rafe Jadrosich |
| | Mohawk Industries | MHK | MHK US | Rafe Jadrosich |
| | Patrick Industries, Inc. | PATK | PATK US | Rafe Jadrosich |
| | Pool Corporation | POOL | POOL US | Shaun Calnan, CFA |



US - Homebuilders and Building Products Coverage Cluster

| Investment rating | Company | BofA Ticker | Bloomberg symbol | Analyst |
|-------------------|---------|-------------|------------------|---------|
|-------------------|---------|-------------|------------------|---------|

IQmethodSM Measures Definitions**Business Performance**

Return On Capital Employed

Return On Equity

Operating Margin

Earnings Growth

Free Cash Flow

Numerator

NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization

Net Income

Operating Profit

Expected 5 Year CAGR From Latest Actual

Cash Flow From Operations – Total Capex

Denominator

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill

Amortization

Shareholders' Equity

Sales

N/A

N/A

Quality of Earnings

Cash Realization Ratio

Asset Replacement Ratio

Tax Rate

Net Debt-To-Equity Ratio

Interest Cover

Numerator

Cash Flow From Operations

Capex

Tax Charge

Net Debt = Total Debt – Cash & Equivalents

EBIT

Denominator

Net Income

Depreciation

Pre-Tax Income

Total Equity

Interest Expense

Valuation Toolkit

Price / Earnings Ratio

Price / Book Value

Dividend Yield

Free Cash Flow Yield

Enterprise Value / Sales

Numerator

Current Share Price

Current Share Price

Annualised Declared Cash Dividend

Cash Flow From Operations – Total Capex

EV = Current Share Price × Current Shares + Minority Equity + Net Debt +

Other LT Liabilities

Enterprise Value

Denominator

Diluted Earnings Per Share (Basis As Specified)

Shareholders' Equity / Current Basic Shares

Current Share Price

Market Cap = Current Share Price × Current Basic Shares

Sales

Basic EBIT + Depreciation + Amortization

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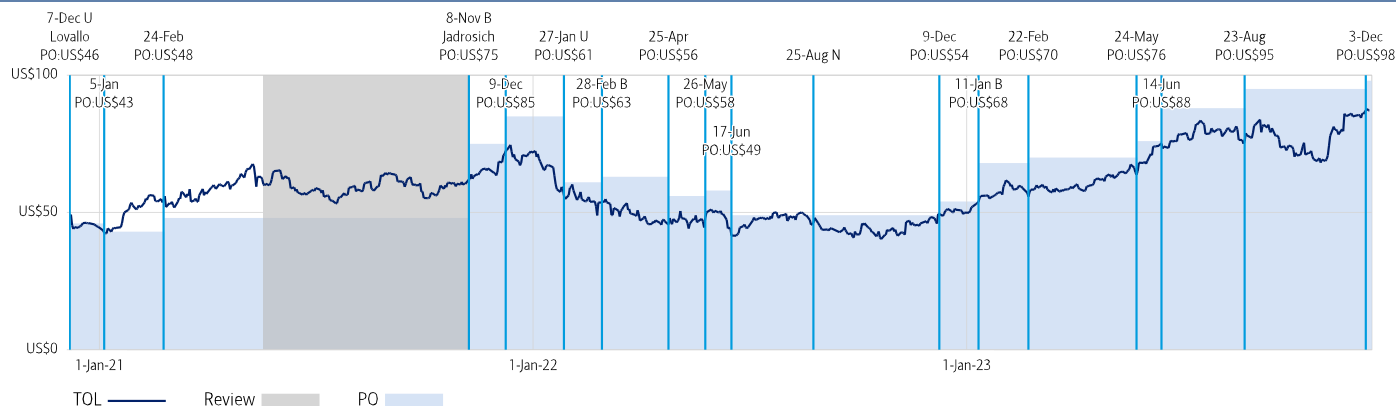
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Toll Brothers (TOL) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

Equity Investment Rating Distribution: Building Group (as of 30 Sep 2023)

| Coverage Universe | Count | Percent | Inv. Banking Relationships ^{R1} | Count | Percent |
|-------------------|-------|---------|--|-------|---------|
| Buy | 41 | 47.67% | Buy | 23 | 56.10% |
| Hold | 14 | 16.28% | Hold | 8 | 57.14% |
| Sell | 31 | 36.05% | Sell | 9 | 29.03% |

Equity Investment Rating Distribution: Global Group (as of 30 Sep 2023)

| Coverage Universe | Count | Percent | Inv. Banking Relationships ^{R1} | Count | Percent |
|-------------------|-------|---------|--|-------|---------|
| Buy | 1869 | 53.48% | Buy | 1046 | 55.97% |
| Hold | 828 | 23.69% | Hold | 461 | 55.68% |
| Sell | 798 | 22.83% | Sell | 370 | 46.37% |

^{R1} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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| Investment rating | Total return expectation (within 12-month period of date of initial rating) | Ratings dispersion guidelines for coverage cluster ^{R2} |
|-------------------|---|--|
| Buy | ≥ 10% | ≤ 70% |
| Neutral | ≥ 0% | ≤ 30% |
| Underperform | N/A | ≥ 20% |

^{R2} Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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