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CUBEWEALTH

TOLL BROTHERS EQUITY REPORT

NOVEMBER 2ND, 2020

TOLL BROTHERS

BY THE NUMBERS

TICKER: TOL
PRICE: $43.74

Toll Brothers
AMERICA'S LUXURY HOME BUILDER®

Toll Brothers, Inc., together with its subsidiaries, designs, builds, markets, sells, and arranges finance for detached and attached homes in luxury residential communities in the United States.

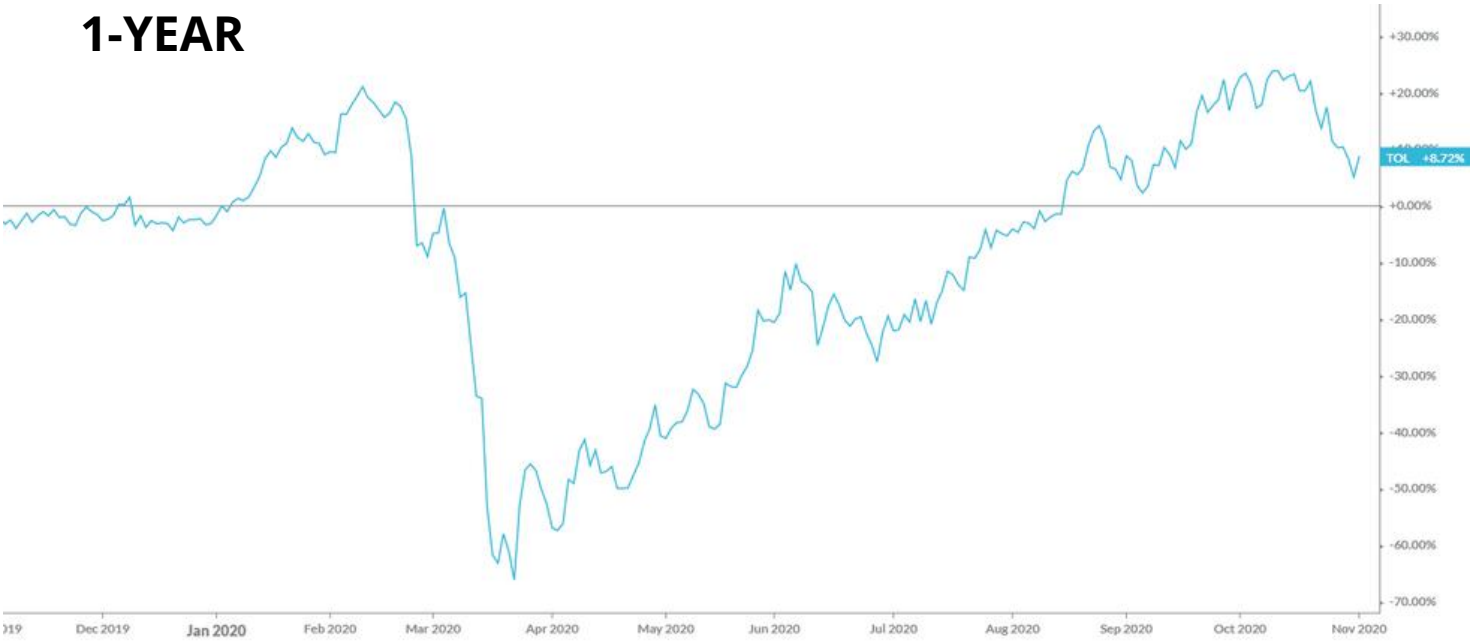
The company serves move-up, empty-nester, active-adult, and second-home buyers. Toll Brothers, Inc. was founded in 1967 and is headquartered in Horsham, Pennsylvania.

0.98%	+12.2%	$5.5B
DIVIDEND YIELD	YTD RETURN	MARKET CAP

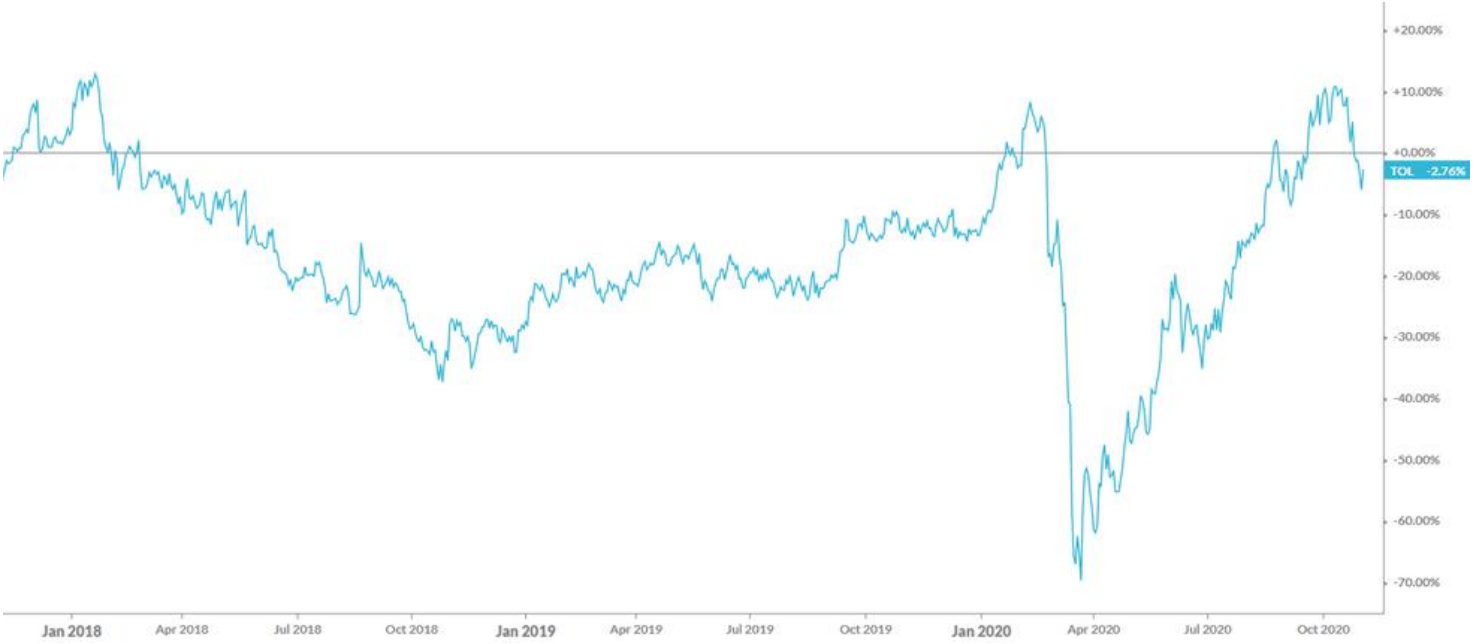
TOL

SHARE PRICE PERFORMANCE

1-YEAR



3-YEAR



ANALYSIS

Because Toll Brothers is directly related to the real estate industry, here is how the report is going to go:

1. Housing Market Data
2. Toll Brothers Properties & Market Positioning
3. Company Financials
4. Peer Comparison
5. DCF Model Results
6. Technical Analysis
7. Conclusion

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2020 YTD REAL ESTATE STATS

Looking at the data below, we see that new privately-owned housing units sold and for sale have been strong on a M/M basis since the pandemic rocked the economy in March. September saw its first decline on a M/M basis at 959,000, a drop of 3.5%, but was a gain of 32.1% vs. September 2019.

Showing the most growth in privately-owned housing sales has been the West on a Y/Y basis at a massive 49.7%. The only area to show a decline was the Northeast at -5.9% Y/Y. The South saw growth of 27.4% Y/Y while the Midwest saw growth of 34.8% Y/Y.

As far as privately owned houses for sale, the U.S. saw a 0.7% increase M/M but a decline of 11.5% Y/Y to 284,000.

New Privately-Owned Houses Sold and For Sale

(Thousands of Units. Detail may not add to total because of rounding.)

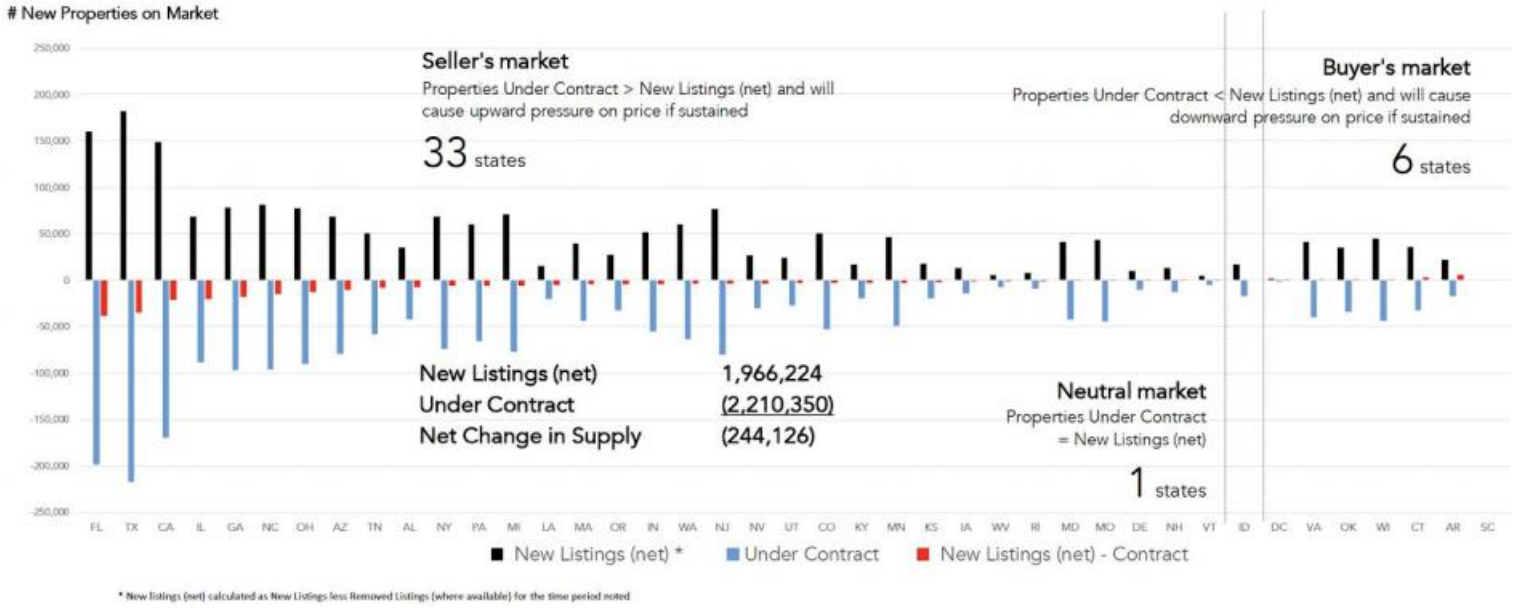
Table 1a - Seasonally adjusted

Period	Sold during period[1]					For sale at end of period					Months' supply[2]	Median sales price ($)	Average sales price ($)
	United States	North-east	Mid-west	South	West	United States	North-east	Mid-west	South	West			
2019													
September	726	34	69	442	181	321	X	X	X	X	5.3	X	X
October	706	22	72	414	198	321	X	X	X	X	5.5	X	X
November	696	33	78	393	192	322	X	X	X	X	5.6	X	X
December	731	39	83	397	212	322	X	X	X	X	5.3	X	X
2020													
January	774	34	97	391	252	325	X	X	X	X	5.0	X	X
February	716	43	81	381	211	327	X	X	X	X	5.5	X	X
March	612	23	74	365	150	330	X	X	X	X	6.5	X	X
April	570	22	75	332	141	323	X	X	X	X	6.8	X	X
May	698	32	74	420	172	311	X	X	X	X	5.3	X	X
June (r)	840	52	85	491	212	300	X	X	X	X	4.3	X	X
July (r)	965	43	127	554	241	291	X	X	X	X	3.6	X	X
August (r)	994	45	97	591	261	282	X	X	X	X	3.4	X	X
September (p)	**959**	**32**	**93**	**563**	**271**	**284**	**X**	**X**	**X**	**X**	**3.6**	**X**	**X**
Average RSE (%)[3]	*8*	*31*	*20*	*12*	*10*	*5*	*X*	*X*	*X*	*X*	*9*	*X*	*X*
Percent Change[4]													
Sep. 2020 from Aug. 2020	***-3.5%***	***-28.9%***	***-4.1%***	***-4.7%***	***3.8%***	***0.7%***	***X***	***X***	***X***	***X***	***5.9%***	***X***	***X***
90 percent confidence interval[5]	*± 19.9*	*± 21.9*	*± 29.0*	*± 31.6*	*± 28.2*	*± 2.5*	*X*	*X*	*X*	*X*	*± 26.5*	*X*	*X*
Sep. 2020 from Sep. 2019	***32.1%***	***-5.9%***	***34.8%***	***27.4%***	***49.7%***	***-11.5%***	***X***	***X***	***X***	***X***	***-32.1%***	***X***	***X***
90 percent confidence interval[5]	*± 28.8*	*± 51.9*	*± 44.1*	*± 40.5*	*± 48.9*	*± 5.1*	*X*	*X*	*X*	*X*	*± 15.8*	*X*	*X*

From that last little bit, we see that supply of homes has been pretty low. If we dive into this data and zoom out a bit we can see there is in fact a huge supply issue of housing across the States.

The total monthly supply of houses hit a 40-year low with inventory down 19.2% annually to just 1.47M homes for sale at the end of September. At the current sales pace that represents only a 2.7-month supply.

New Listings vs. Contract Pre-COVID-19, March 13, through October 23 (cumulative count)



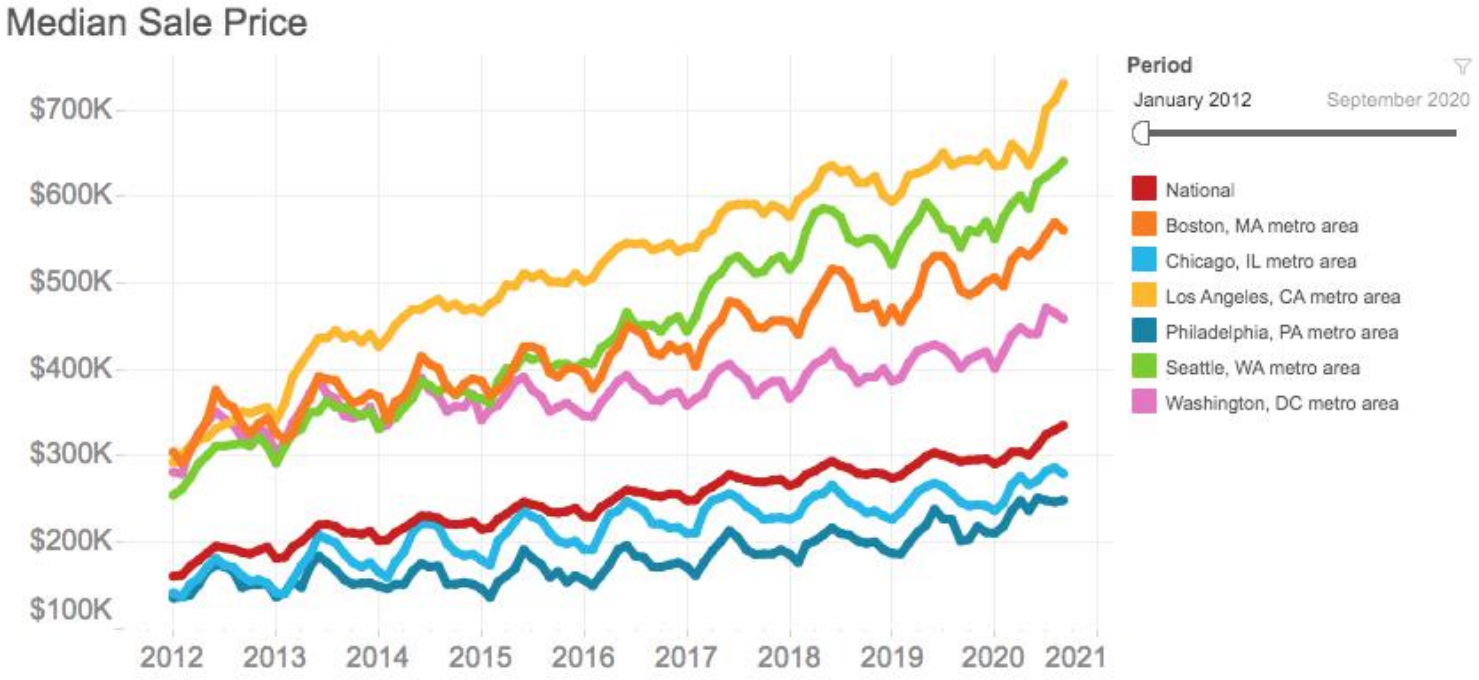
Source: HouseCanary analysis, MLS source data *Note: South Carolina data is unavailable at this time.

Basic economics tells us when supply is low, demand rises and vice versa. This is definitely the case today as ultra low rates coupled with a pandemic and low supply of homes has sent prices sky high.

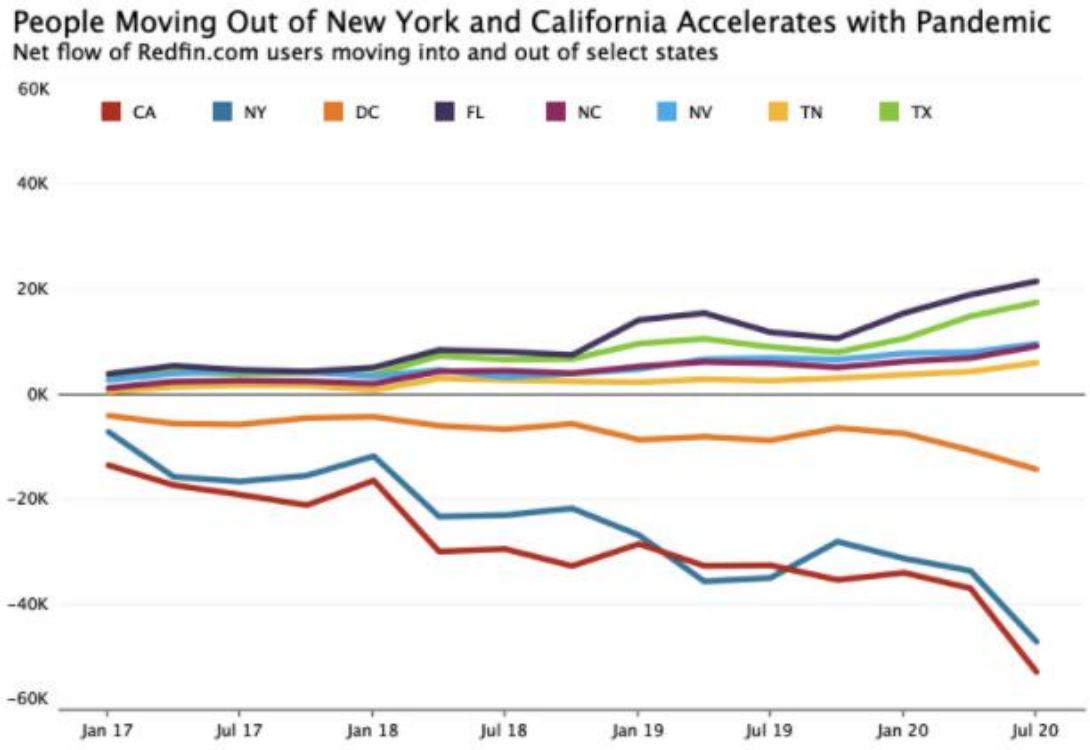
The median price of an existing home sold in September was $311,800, a 14.8% gain compared with September 2019, an all-time high when adjusted for inflation.

Furthermore, sales of newly built homes in August were a stunning 43% higher annually, but the supply of those homes is also unusually low. Builders, like Toll Brothers, are having trouble keeping up with demand. They are also raising prices to keep pace with cost increases for land, labor and materials.

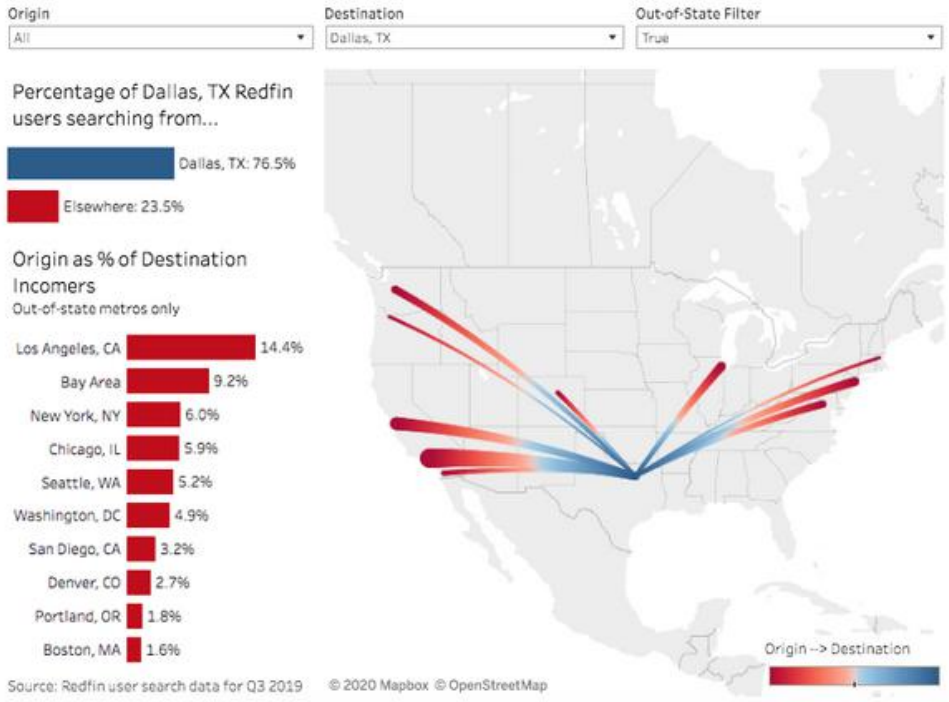
Below we see how prices have gained in large metro cities in the USA.



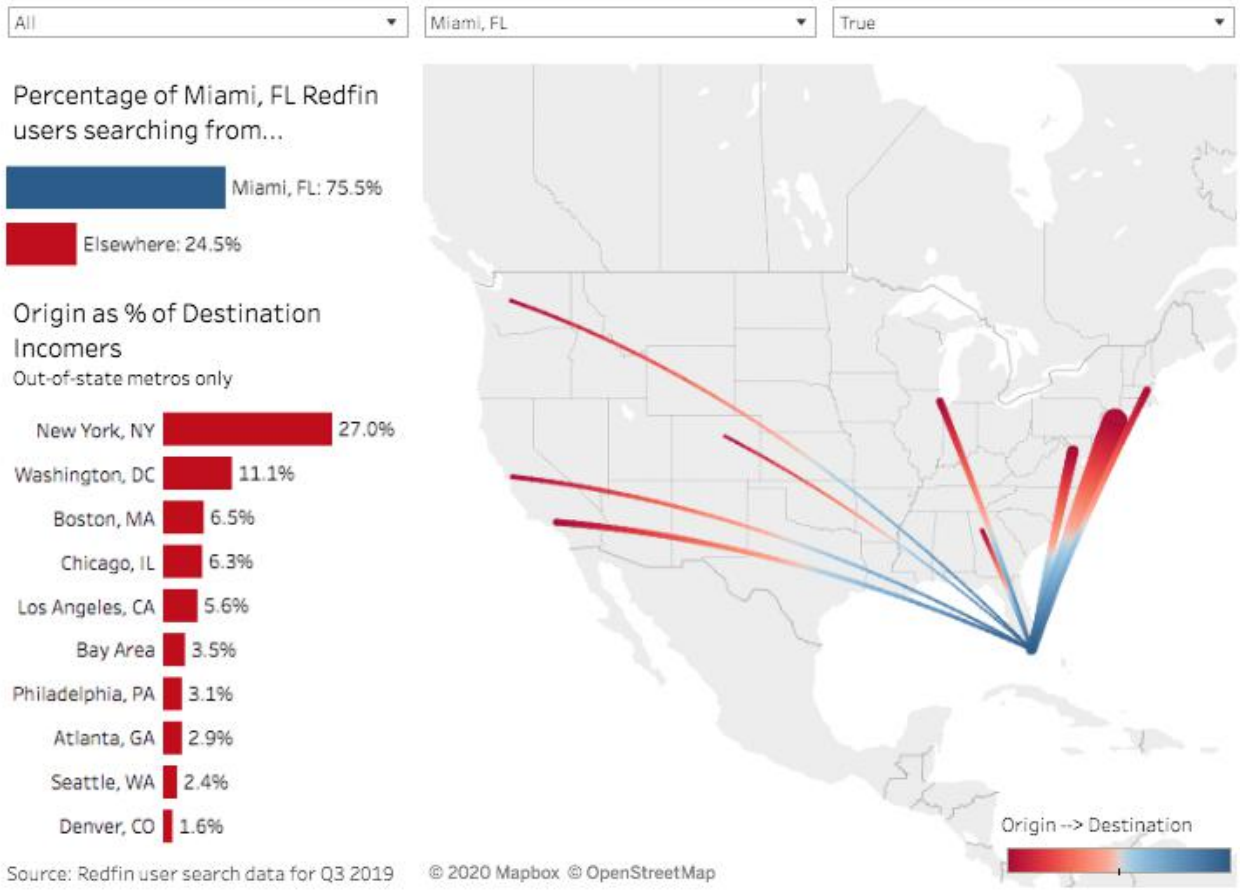
CUBE, being the data hungry company it is, dug a little deeper to see where people are migrating to and from and it appears people are generally leaving New York and California in droves.



We dug even deeper seeing that Texas has been a hot destination spot. According to Redfin, 14.4% of people moving to Dallas, TX are from Los Angeles, 9.2% are from the Bay area, 6.0% from NY, etc.



When looking at Miami, FL we see that 27.0% of people moving there are from New York, 11.1% are from DC, 6.5% are from Boston, 6.3% are from Chicago, and 5.6% are from LA.



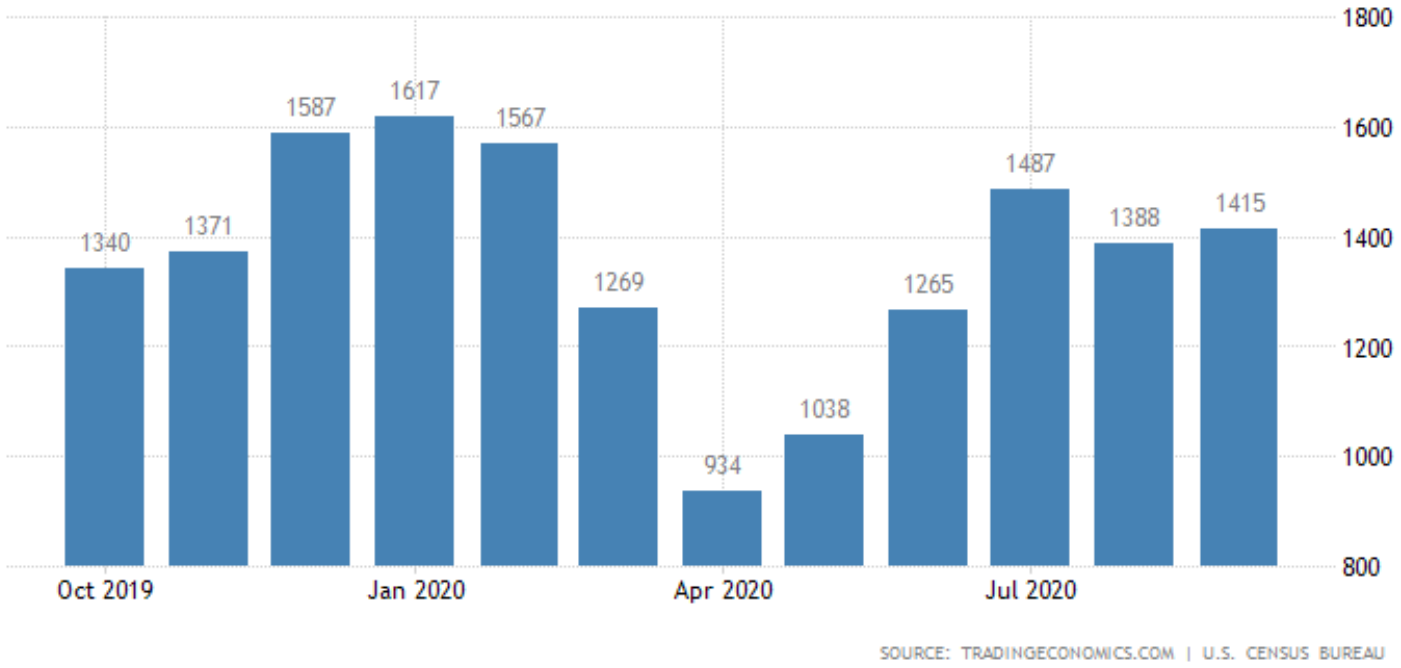
If you'd like to use the link to see specific locations for yourself use this link right here.

So how do we combat low supply of housing? Companies like Toll Brothers have to build.

Housing starts in the US rose 1.9% to a seasonally adjusted annual rate of 1.415M units in September 2020, from a downwardly revised 1.388M in the previous month and below market expectations of 1.457M.

Single-family housing starts jumped 8.5% to 1.108M, while the volatile multi-family segment dropped 16.3% to 307K.

Housing starts in certain areas were mixed. Starts rose in the South (6.2% to 755K, West (1.4% to 350K) and Northeast (66.7% to 145K); but dropped in the Midwest (-32.7% to 165K).

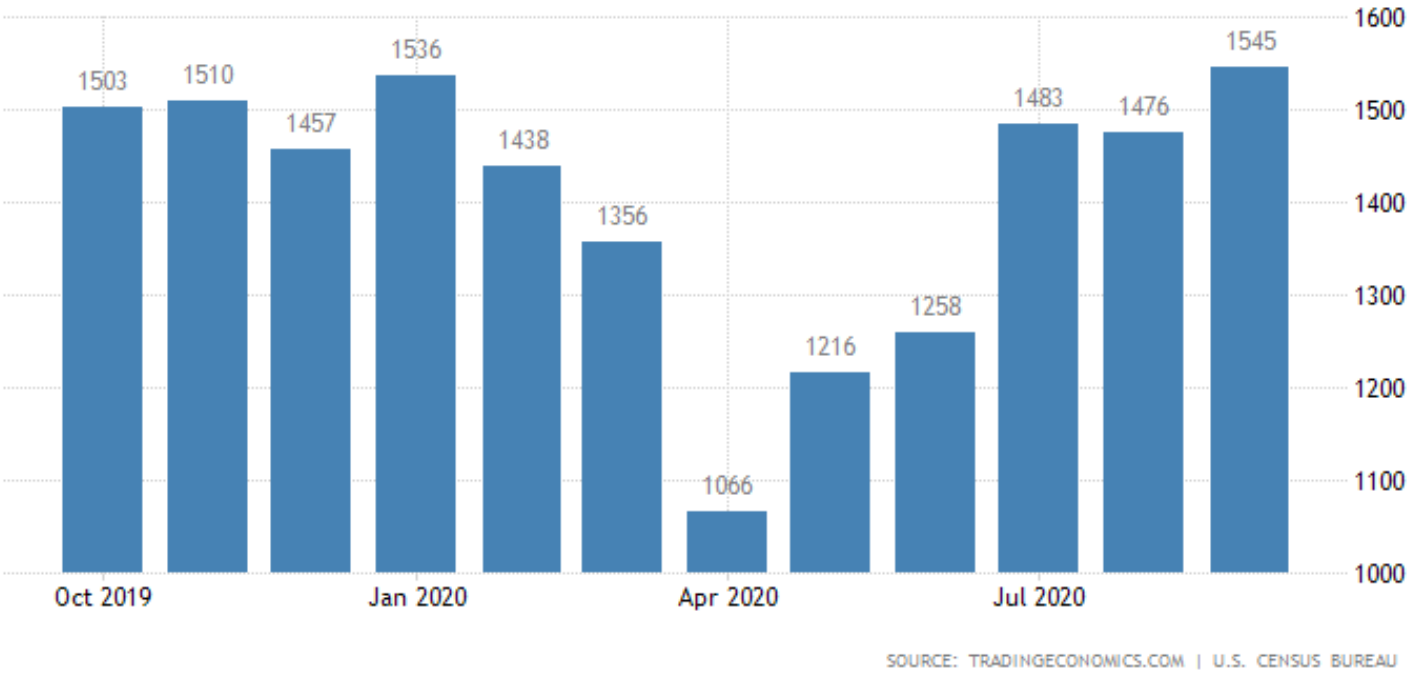


In order to start building, companies are going to need permits.

Building permits in the United States rose 4.7% from a month earlier to a seasonally adjusted annual rate of 1.545M in September 2020, the highest level since March 2007, revised data showed at the end of October.

Single-family authorizations increased 7.2% to a rate of 1.113M while permits for the volatile multi-segment fell 1.4% to a rate of 432K.

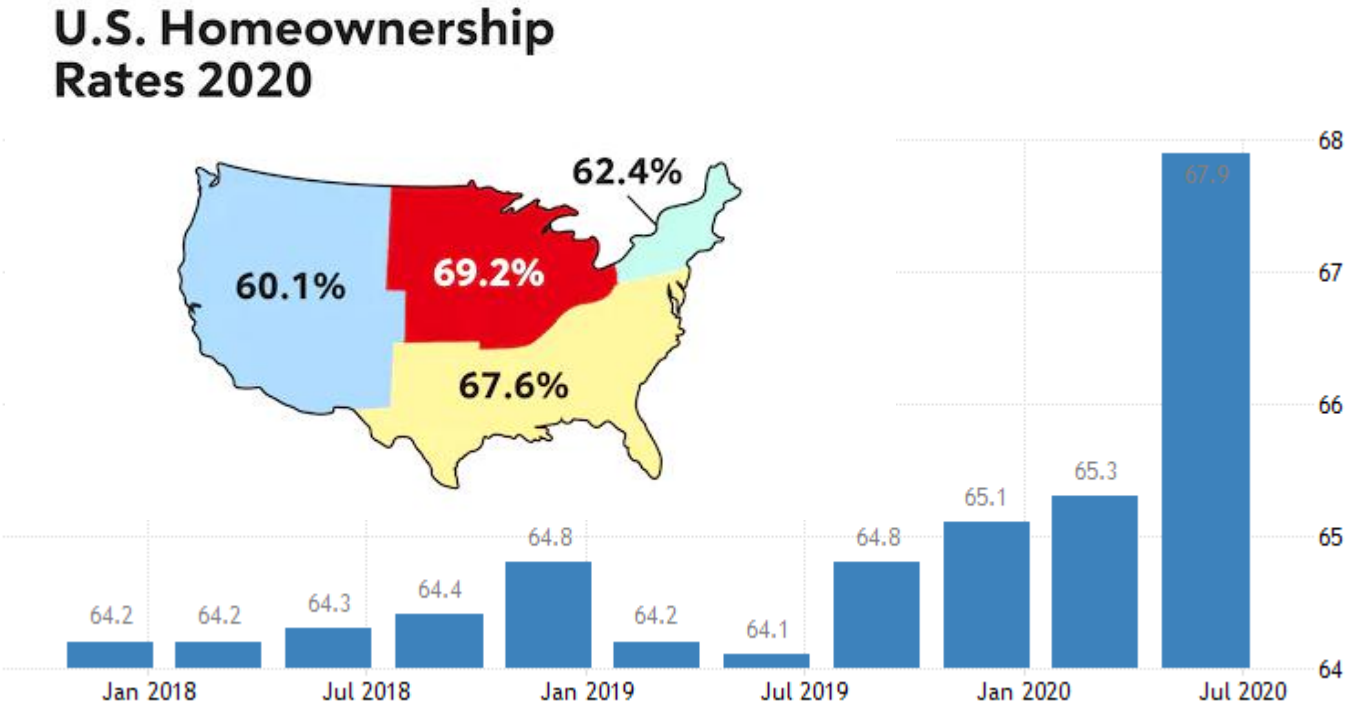
Across regions, permits went up in the South (2.1% to 815K), the West (1.4% to 375K), the Midwest (10.1% to 207K) and the Northeast (23.3% to 148K).



The home ownership rate in the United States increased to 67.9% in the second quarter of 2020, up from 65.3% in the first quarter of 2020.

The homeownership rates for households with income greater than or equal to the median family income ($68K) were:
80.5%: Q2 2020
78.8%: Q2 2019

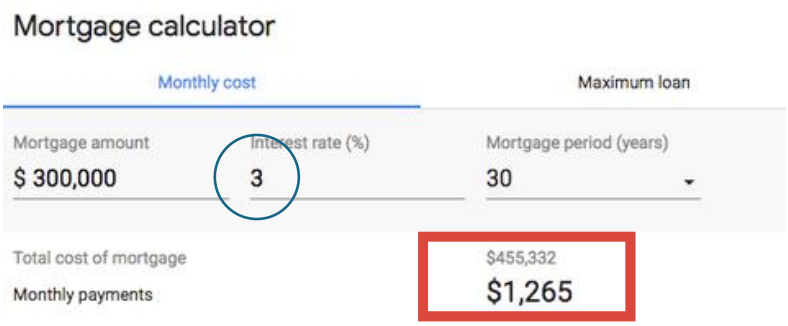
The homeownership rate for households with income less than the median family income ($68K) were:
55.2%: Q2 2020
50.0%: Q2 2019

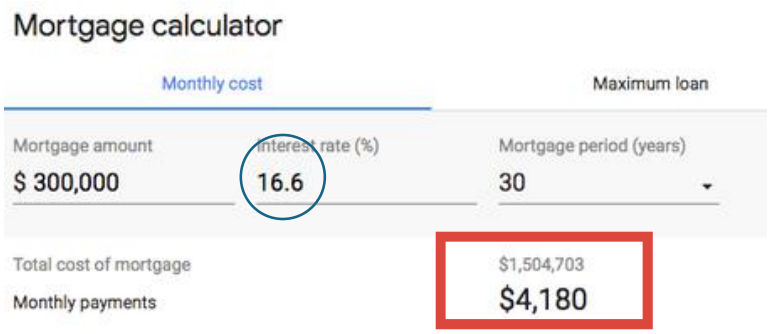


As already mentioned, a large reason for such a huge push into home ownership is because it's never been so cheap to borrow money.

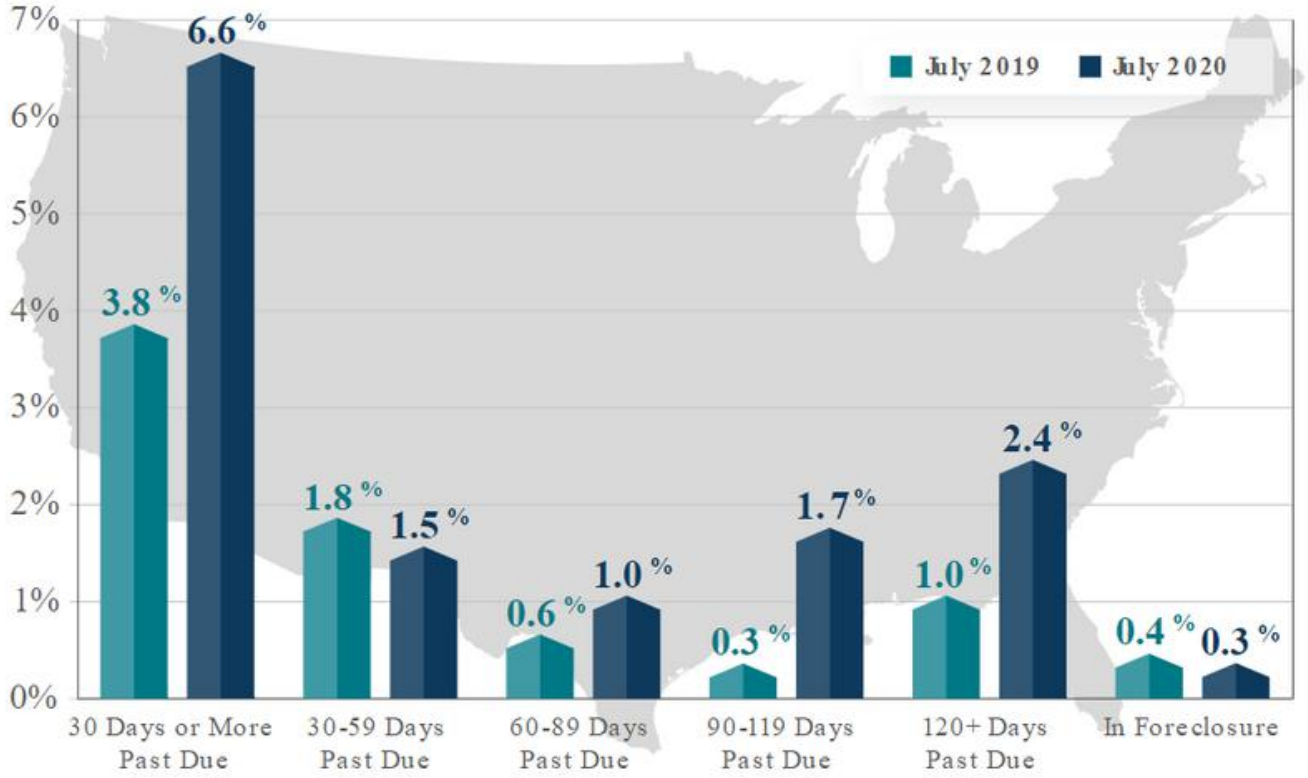
The average fixed 30-year mortgage rate in the United States increased 2 bps to 3.02% in the week ended October 16th, remaining close to last week's record low, data from the Mortgage Bankers Association showed.

Below is a chart dating back to 2010. If we go back to 1981, mortgage rates were as high at 16.6%. If we look at a $300K mortgage under both rates, the difference in the cost of the mortgage is a massive $1,050,000, or $2,915 per month.





Speaking of rates and mortgages, let's now take a look at the quality of late-stage mortgage delinquencies. They rose to 1.4% among borrowers in July, the highest level since 1999, according to a new report from CoreLogic. The July numbers represent the latest available data and stand in contrast to pre-Covid March, when late-stage delinquencies — 120 days or more — stood at just 0.1%.

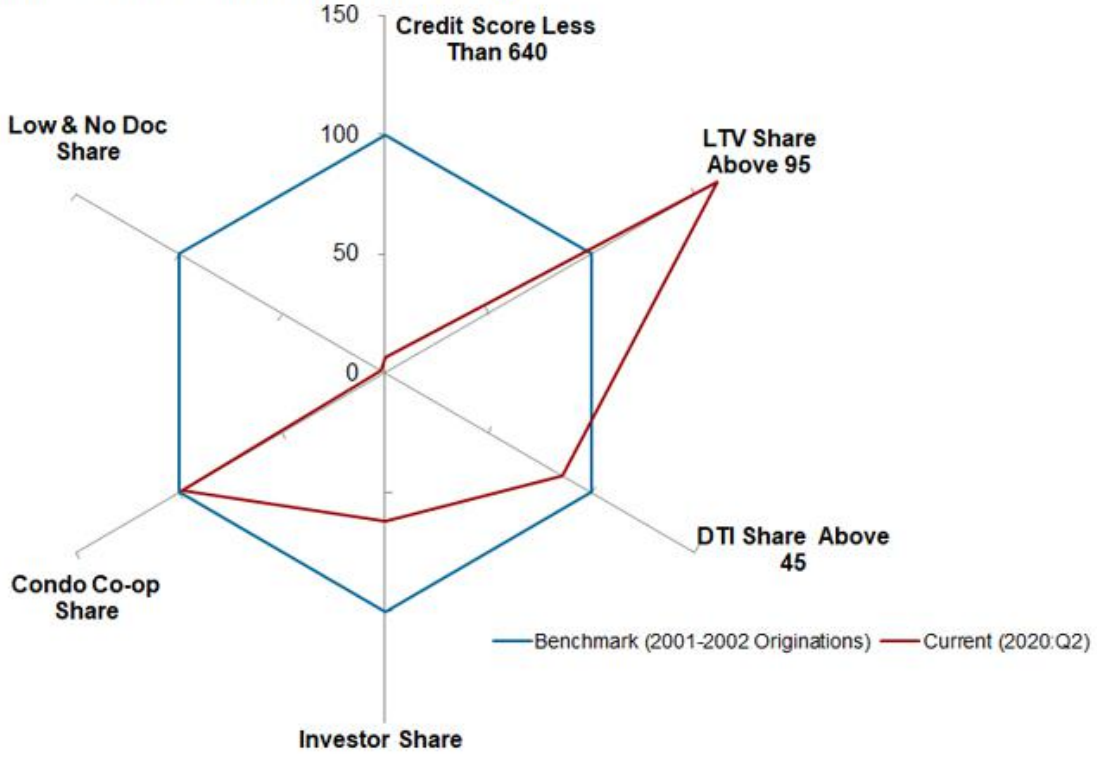


Serious delinquency is defined as 90 days or more past due including loans in foreclosure. In July, all states logged annual increases in both overall and serious delinquency rates. COVID-19 hotspots were again impacted the most, with Nevada (up 5.2 percentage points), New Jersey (up 4.8 percentage points), Hawaii (up 4.7 percentage points), New York (up 4.6 percentage points) and Florida (up 4.4 percentage points) topping the list for overall delinquency gains.

The figure below compares six indicators of underwriting and credit risk during a benchmark time period to present day for conventional conforming home-purchase loans. The blue hexagon represents an index of credit-risk attributes in the benchmark period and the red polygon represents characteristics of loans originated in the second quarter of 2020, relative to the benchmark.

The share of borrowers with a credit score less than 640 as well as the low/no documentation loan share were both down significantly compared to the 2001-2002 benchmark level. In contrast, the share of new loans with an LTV (loan to value) ratio higher than 95% was 66% higher than the benchmark level. Share of new loans with a DTI (debt to income) ratio above 45% was 12% lower than the benchmark level. The condo/co-op share was just 2% lower than the benchmark level, and the investor-owned share was 38% lower than the benchmark level.

Figure 3: Six Credit Risk Attributes For Conforming Conventional Home Purchase Loans: Q3 2019 Compared With 2001 2002



Source: Corelogic Truestandings®Servicing

How does this stack up to the years leading into the Great Recession of 2008? CUBE was able to dig up and find a research report conducted by the Fed that can be viewed here.

The mortgage market began suffering serious problems in mid-2005. According to data from the Mortgage Bankers Association, the share of mortgage loans that were "seriously delinquent" (90 days or more past due or in the process of foreclosure) averaged 1.7% from 1979 to 2006, with a low of about 0.7% (in 1979) and a high of about 2.4% (in 2002). ***But by the second quarter of 2008, the share of seriously delinquent mortgages had surged to 4.5%***. These delinquencies foreshadowed a sharp rise in foreclosures: roughly 1.2M foreclosures were started in the first half of 2008, an increase of 79% from the 650,000 in the first half of 2007 (Federal Reserve estimates based on data from the Mortgage Bankers Association).

We are seeing delinquency rates in the same ballpark and CUBE wanted to highlight this. Do we think 2020 is a completely different landscape? Yes, but there still remains cracks in the foundation.

Banks are much better capitalized today to endure continued headwinds and foreclosures are not nearly as bad as 2007. For instance, a total of 5,599 U.S. properties started the foreclosure process in August 2020. While this is up 24% from the previous month it is down 80% from a year ago.

For 2020, the national foreclosure activity total in Q2 2020 was 89% below the pre-recession average of 278,912 per quarter from Q1 2006 to Q3 2007, making Q2 2020 the 15th consecutive quarter with foreclosure activity below the pre-recession average. The biggest question? How much of this has to do with the CARES Act and what would the true foreclosure rate really be?

As a final note related to the housing market, the pandemic has done two things specifically.

1. Work from home is looking increasingly likely to be something that will remain even after the pandemic subsides - at least on a greater and more frequent level. This has been a huge plus for companies like Toll Brothers who are seeing people leave cities and move into homes in the suburbs.
2. The pandemic has been a boon for the ultra-rich

The staggering rise in the stock-market is testament to this and as we know from the previous CUBELetters, many Americans, especially those with lower incomes, do not partake in the stock market. In the past 30 years, the proportion of wealth held by those in the top 10% of household income has risen from 60.8% to 70.0%. But even more remarkably, the wealth owned by just the top 1% of income earners has gone up from 17.2% to 26.0%—meaning that more than a quarter of the country's wealth is in the hands of the top 1%.

In the US, over 44 million people lost their jobs and unemployment surged towards 15% between April and June 2020 yet the fortunes of the top five billionaires rose by $102B, increasing their wealth by 26%. In fact, the combined wealth of US billionaires increased by over $637B to a total of $3.6T, which is considerably more than the entire wealth of the 54 countries on the African continent. Between 1980 and 2020, billionaires in the US saw their wealth soar by 1,130%, increasing more than 200 faster than median wages.

While the wealth gap actually works in Toll Brother's favor to an extent, the United States housing market could be one more lockdown away from a disaster.

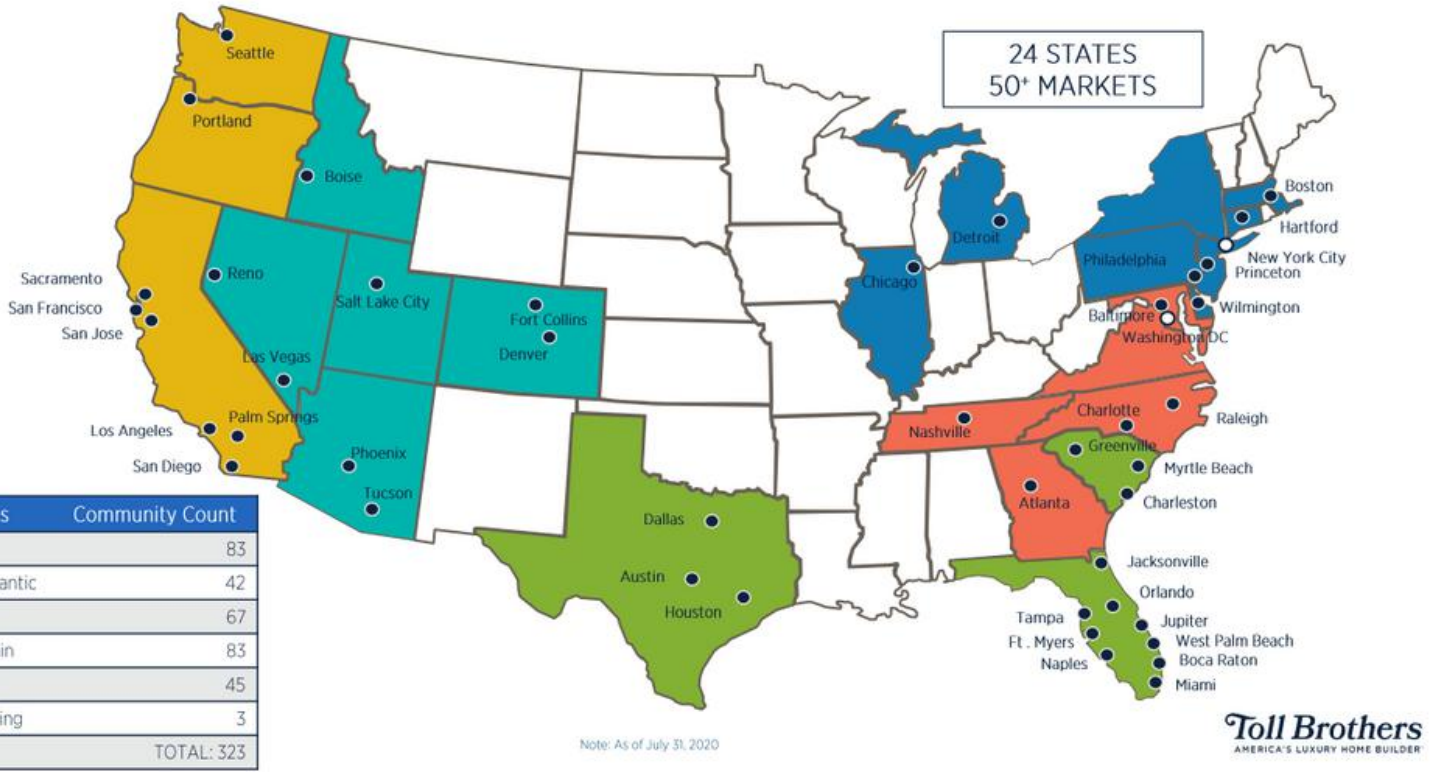
TOLL BROTHERS

Toll Brothers operates in two segments

1. Traditional Home Building
2. City Living

It also designs, builds, markets, and sells homes in urban infill markets through Toll Brothers City Living. In addition, the company develops, owns, and operates golf courses and country clubs; develops and sells land; and develops, operates, and rents apartments, as well as provides homeowners with home automation and technology options. Further, it owns and operates architectural, engineering, mortgage, title, landscaping, lumber distribution, house component assembly, and manufacturing operations.

Below, we can see that Toll Brothers is in 24 different states and 50 different markets. We consider this a pretty healthy portfolio as they are operating in very attractive and diverse regions.

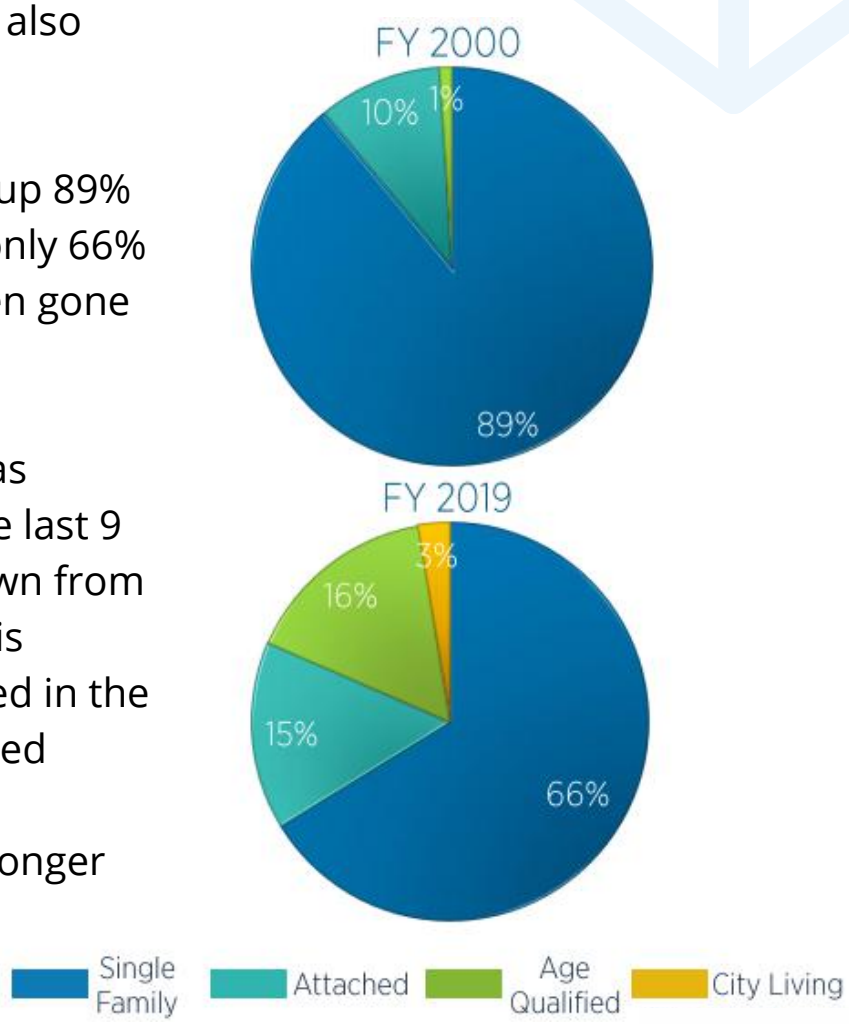


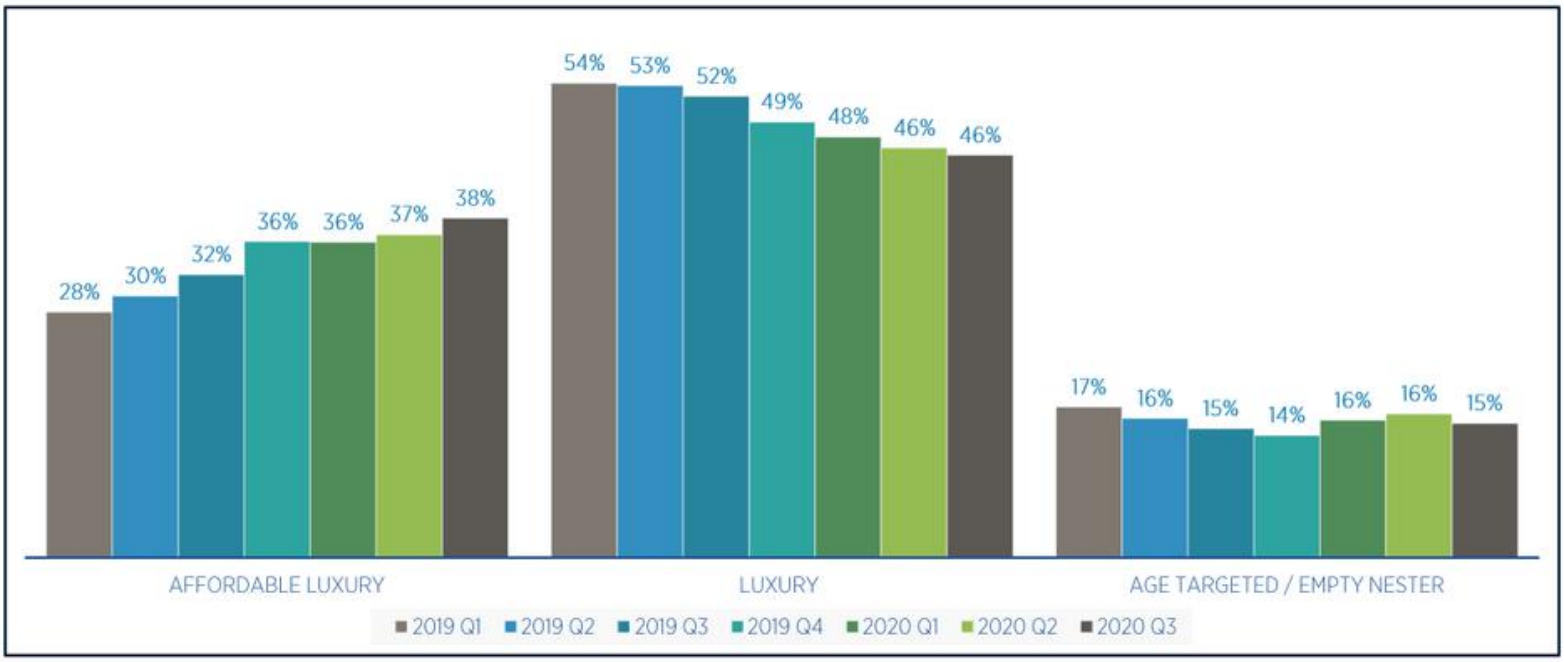
Regions	Community Count
North	83
Mid-Atlantic	42
South	67
Mountain	83
Pacific	45
City Living	3
	TOTAL: 323

On top of being diverse in location across the United States, Toll Brothers has also grown to be diverse by home type.

In 2000, single family homes made up 89% of their portfolio and today that is only 66% while age qualified homes have risen gone from 0% to 16%.

Furthermore, "affordable luxury" has increased from 28% to 38% over the last 9 quarters and "luxury" has come down from 54% to 46%. Why does CUBE like this allocation? Because as we mentioned in the data, this demographic has benefitted greatly from the increasing wealth inequality gap and tends to be a stronger market.





To reiterate, Toll Brothers is a premier homebuilder. As we see in the image below, the average home delivered to the buyer was $802K in Q3 with an overall average of $873K.

The average FICO score of their home buyer was 767 while 18% were all cash buyers.

At the end of Q3 2020, TOL had approximately $8.03B worth of inventory on their books vs. $7.8B on October 31, 2019. Operating communities include communities offering homes for sale or communities that have sold all available home sites but have not completed delivery of the homes.

Inventory at July 31, 2020 and October 31, 2019 consisted of the following (amounts in thousands):

	July 31, 2020	October 31, 2019
Land controlled for future communities	$ 167,694	$ 182,929
Land owned for future communities	963,399	868,202
Operating communities	6,903,422	6,821,917
	$ 8,034,515	$ 7,873,048

Market Conditions: Pre-Covid-19

- Economy remains supportive of housing
- Increasing volumes of new home production but still below long-term averages
- Demand improvement accelerated in late Spring of 2019 which carried into the start of FY 2020

Pause For Covid-19 Impact Then Surge In Demand

- Significant pause to the economy from mid-March to April in housing demand
- Impact varied greatly throughout the country
- At the peak, construction and/or sales activity was limited in many of our markets
- Return of web traffic, physical traffic, and deposits show signs of resilience in the housing market as economy begins to reopen

Demand Equation

- Continued population growth through recession & recovery
- Household formations are strong
- Pent-up demand
- Homeownership rate rising-still below historic norms
- Millennials Increasing; foreign buyers decreasing

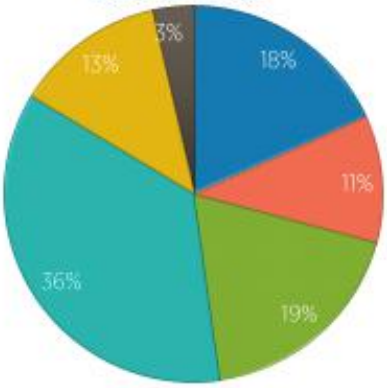
Supply Remains Constrained

- Fewer land entitlements processed for several years
- Inventory/lot shortages in some markets
- Constrained capital access favors largest builders
- The median age of existing housing stock has increased from 25 years to 40 years since 1989

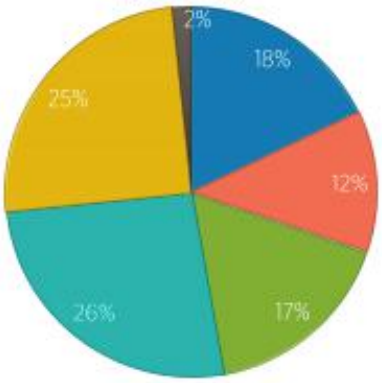
Personal Balance Sheets Had Been Improving

- Mortgage rates at all time low
- Stock market strength favors Toll buyers
- Purchase decision is a confidence-sensitive issue for Toll affluent buyer

Q3 FY 2020
Lots Owned



Q3 FY 2020
Revenue



North
Mid-Atlantic
South
Mountain
Pacific
City Living

TOL Brothers is pretty big on buying back their shares and they have been doing so aggressively here in 2020 with nearly 16M shares purchased at an average of $39.75 for a total of $634M.

This trumps their $234M in purchases in 2019 and even surpasses their previous high in 2018 of $503M.

They also did not cut their dividend this year and have kept it at $0.11 per share. The company obviously seems to favor the buybacks because the dividend unfortunately has not grown since 2017. This is something we'd like to see more of as Lennar (LEN) doubled their dividend in their previous earnings report.

FY	Shares	Cost	Average Price	Dividends (Total $/Quarterly Per Share)
2020*	15,947,727	$634 MM	$39.75	$43 MM/$0.11
2019	6,619,345	$234 MM	$35.28	$64 MM/$0.11
2018	12,108,158	$503 MM	$41.56	$62 MM/$0.11
2017	7,693,630	$291 MM	$37.81	$39 MM/$0.08
2016	13,652,384	$393 MM	$28.77	---
2015	1,665,009	$57 MM	$34.17	---
TOTAL	57,686,253	$2,112 MM	$36.22	$208 MM

CUBE'S TOP PROS FOR TOL

DIVERSIFIED PORTFOLIO, LUXURY FOCUSED

RECORD LOW RATES

NO NEAR DEBT MATURITIES

CUBE'S TOP CONS FOR TOL

COVID19 LOCKDOWNS

OVERALL ECONOMIC RISK, PRIMARILY CREDIT

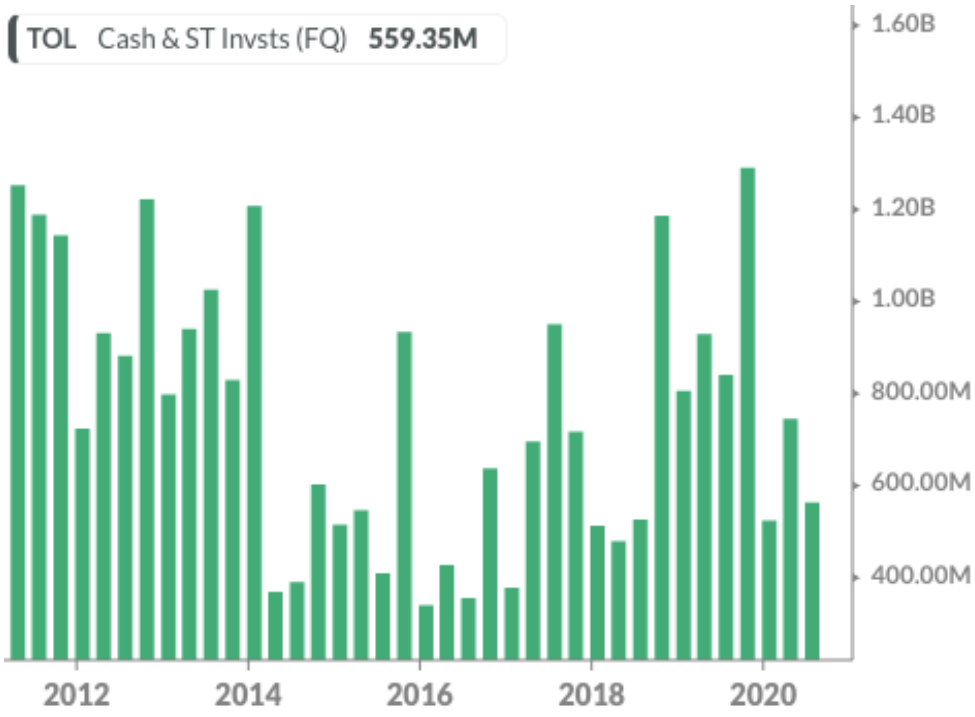
WEAKER MARGINS THAN PEERS, HIGHER VALUATION

FINANCIAL STATEMENTS

BALANCE SHEET

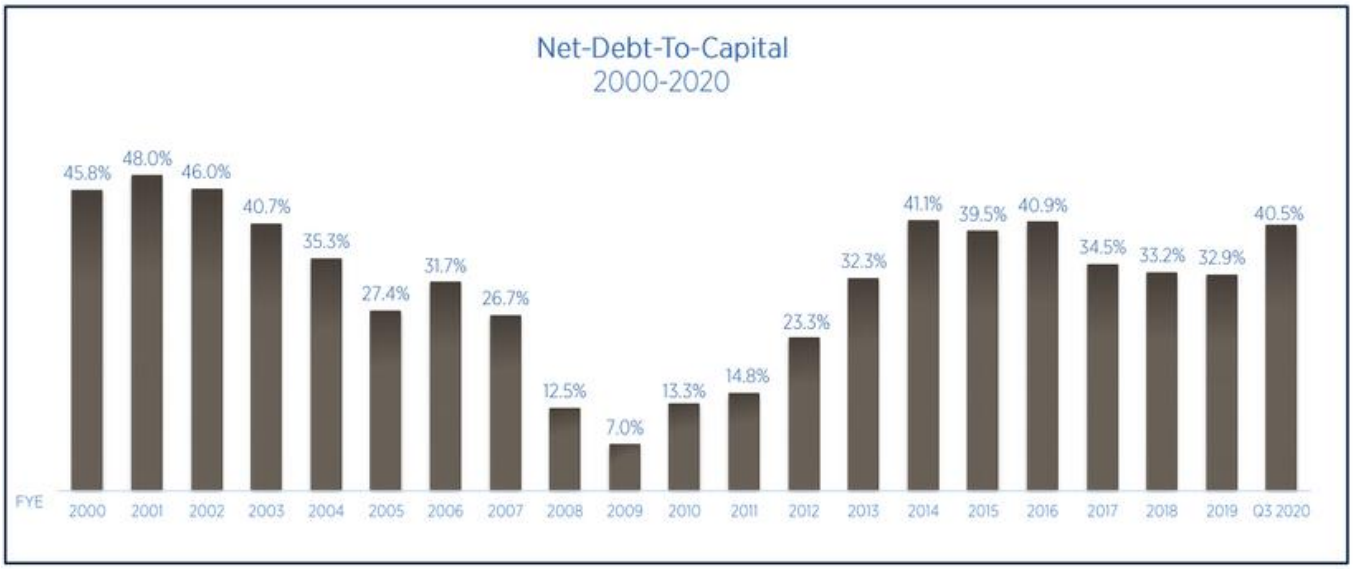
	July 31, 2020 (unaudited)	October 31, 2019
ASSETS		
Cash and cash equivalents	$ 559,348	$ 1,286,014
Inventory	8,034,515	7,873,048
Property, construction, and office equipment, net	313,513	273,412
Receivables, prepaid expenses, and other assets (1)	968,416	715,441
Mortgage loans held for sale, at fair value	161,540	218,777
Customer deposits held in escrow	78,094	74,403
Investments in unconsolidated entities	412,766	366,252
Income taxes receivable	9,239	20,791
	$ 10,537,431	$ 10,828,138
LIABILITIES AND EQUITY		
Liabilities		
Loans payable	$ 1,082,025	$ 1,111,449
Senior notes	2,661,301	2,659,898
Mortgage company loan facility	122,189	150,000
Customer deposits	437,008	385,596
Accounts payable	375,900	348,599
Accrued expenses	1,014,822	950,932
Income taxes payable	118,058	102,971
Total liabilities	5,811,303	5,709,445
Equity		
Stockholders' equity		
Preferred stock, none issued	—	—
Common stock, 152,937 shares issued at July 31, 2020 and October 31, 2019	1,529	1,529
Additional paid-in capital	722,115	726,879
Retained earnings	4,978,832	4,774,422
Treasury stock, at cost — 26,997 and 11,999 shares at July 31, 2020 and October 31, 2019, respectively	(1,022,406)	(425,183)
Accumulated other comprehensive loss	(4,996)	(5,831)
Total stockholders' equity	4,675,074	5,071,816
Noncontrolling interest	51,054	46,877
Total equity	4,726,128	5,118,693
	$ 10,537,431	$ 10,828,138

Cash & equivalents on hand stands at $559M with an additional $1.78B revolver they can tap into. While this cash balance is lower than usual, TOL does not have any debt maturities until 2022 of $420M with total debt around $3.9B. Where did the cash go? As we mentioned, TOL has purchased over $600M worth of stock this year.



Cash & Equivalents	$559MM
Revolver Availability	$1,776MM
TOTAL LIQUIDITY	$2,336MM

SUPERIOR CAPITAL MARKET ACCESS Senior/Corporate Credit Ratings		
Fitch Inc.	BBB-	(Stable)
Standard & Poor's	BB+	(Stable)
Moody's	Ba1	(Stable)



Net debt to capital is pretty steady at 40.5% while book value is at $37.12, growing at a 10% CAGR over the last decade.

FINANCIAL STATEMENTS

INCOME STATEMENT

	Nine months ended July 31,		Three months ended July 31,	
	2020	2019	2020	2019
Revenues:				
Home sales	$ 4,441,383	$ 4,788,335	$ 1,627,812	$ 1,756,970
Land sales	90,609	56,631	23,677	8,721
	4,531,992	4,844,966	1,651,489	1,765,691
Cost of revenues:				
Home sales	3,629,525	3,818,347	1,318,936	1,401,755
Land sales	80,959	43,406	22,259	6,232
	3,710,484	3,861,753	1,341,195	1,407,987
Selling, general and administrative	531,819	527,318	160,649	186,709
Income from operations	289,689	455,895	149,645	170,995
Other:				
Income (loss) from unconsolidated entities	5,304	17,759	(2,566)	7,200
Other income – net	24,917	40,867	4,786	8,721
Income before income taxes	319,910	514,521	151,865	186,916
Income tax provision	72,603	126,829	37,104	40,598
Net income	$ 247,307	$ 387,692	$ 114,761	$ 146,318
Other comprehensive income, net of tax	835	168	279	56
Total comprehensive income	$ 248,142	$ 387,860	$ 115,040	$ 146,374
Per share:				
Basic earnings	$ 1.89	$ 2.65	$ 0.91	$ 1.01
Diluted earnings	$ 1.87	$ 2.63	$ 0.90	$ 1.00
Weighted-average number of shares:				
Basic	131,024	146,041	126,722	144,750
Diluted	132,032	147,479	127,399	146,275

During the fiscal third quarter, TOL delivered 2,022 homes and generated home sales revenues of $1.63B, which were up 1.4% in units and down 7.4% in dollars from the prior year period.

- Net income and earnings per share was $114.8M and $0.90 per share diluted, compared to net income of $146.3M and $1.00 per share diluted in FY 2019's third quarter.
- Pre-tax income was $151.9M, compared to $186.9M in FY 2019's third quarter.
- Net signed contract homes were 2,833, up 26%; contract value was $2.21B, up 18%.
- Backlog in homes at third-quarter end was 7,239, up 6%; backlog value was $6.09B, up 4%.
- Home sales gross margin was 19.0%; Adjusted Home Sales Gross Margin, which excludes interest and inventory writedowns was 21.9%
- SG&A, as a percentage of home sales revenues was 9.9%.

	FY 2015	FY 2016	FY 2017	FY 2018	FY 2019	Q3 FY 2020
Pre-tax Income (000s)	$535,562	$589,027	$814,311	$933,916	$787,170	$151,865
EBITDA (000s)	$705,909	$773,628	$1,017,227	$1,153,669	$1,046,151	$211,567
Diluted EPS	$1.97	$2.18	$3.17	$4.85	$4.03	$0.90
Cash & Marketable Securities (000s)	$928,994	$633,715	$712,829	$1,182,195	$1,286,014	$559,348
Selling Community Count	288	310	305	315	333	323
Owned & Optioned Lots	44,253	48,837	48,311	53,422	59,230	61,440
Adjusted Gross Margin	25.9%	23.2%	24.8%	23.7%	23.0%	21.9%
Operating Margin	10.7%	9.5%	11.1%	11.0%	9.4%	9.1%
JV & Other Income (000s)	$88,692	$98,966	$169,375	$147,700	$106,370	$4,786
Return on Beginning Stockholders' Equity	9.4%	9.0%	12.7%	16.5%	12.4%	-

FINANCIAL STATEMENTS

CASH FLOW

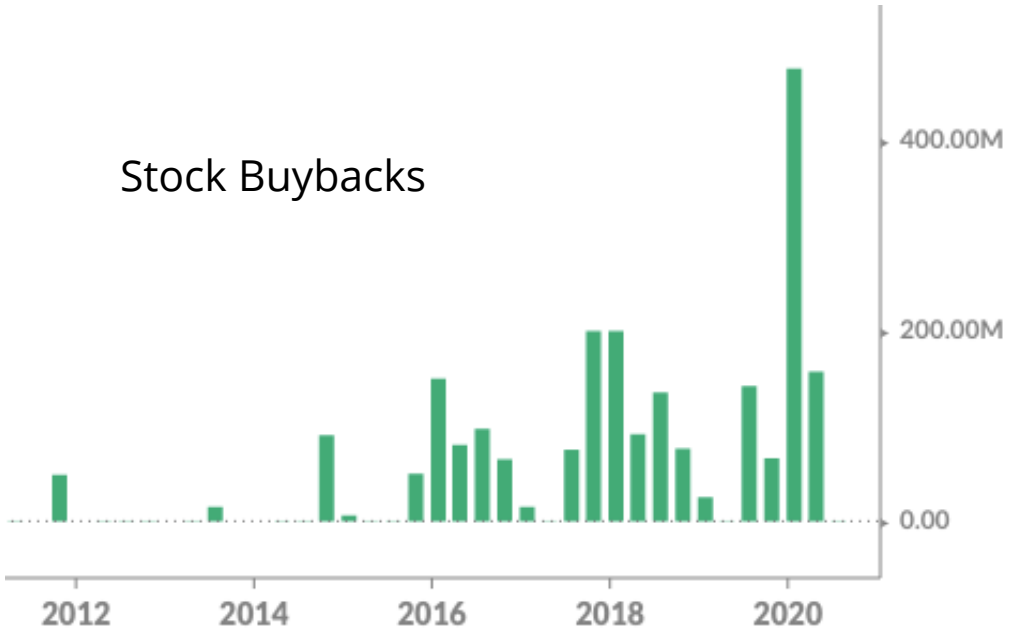
	Nine months ended July 31,	
	2020	2019
Cash flow provided by operating activities:		
Net income	$ 247,307	$ 387,692
Adjustments to reconcile net income to net provided by operating activities:		
Depreciation and amortization	46,700	51,423
Stock-based compensation	20,636	19,351
Income from unconsolidated entities	(5,304)	(17,759)
Distributions of earnings from unconsolidated entities	17,996	25,919
Income from foreclosed real estate and distressed loans	(602)	(487)
Deferred tax provision	14,804	7,045
Inventory impairments and write-offs	21,934	31,636
Gain on the sale of golf club properties and an office building	(12,970)	(13,331)
Other	44	(536)
Changes in operating assets and liabilities		
Increase in inventory	(124,235)	(264,965)
Origination of mortgage loans	(1,191,066)	(1,074,392)
Sale of mortgage loans	1,250,109	1,078,105
Increase in receivables, prepaid expenses, and other assets	(172,790)	(155,843)
Decrease in income taxes receivable	11,552	
Increase in customer deposits – net	47,222	44,726
Decrease in accounts payable and accrued expenses	(29,742)	(109,775)
Increase in income taxes payable		13,652
Net cash provided by operating activities	141,595	22,461
Cash flow used in investing activities:		
Purchase of property, construction, and office equipment – net	(75,001)	(61,278)
Investments in unconsolidated entities	(47,310)	(43,260)
Return of investments in unconsolidated entities	42,639	112,373
Investment in foreclosed real estate and distressed loans	(866)	(602)
Return of investments in foreclosed real estate and distressed loans	1,751	1,649
Proceeds from the sale of golf club properties and an office building	15,617	33,539
Business acquisitions	(60,349)	(92,840)
Net cash used in investing activities	(123,519)	(50,419)
Cash flow used in financing activities:		
Proceeds from loans payable	3,250,010	1,940,998
Debt issuance costs		(1,948)
Principal payments of loans payable	(3,334,431)	(1,696,827)
Redemption of senior notes		(350,000)
Proceeds from stock-based benefit plans, net	11,252	5,441
Purchase of treasury stock	(633,873)	(167,474)
Dividends paid	(42,650)	(48,140)
(Payments) receipts related to noncontrolling interest, net	(1,935)	49
Net cash used in financing activities	(751,627)	(317,901)
Net decrease in cash, cash equivalents, and restricted cash	(733,551)	(345,859)
Cash, cash equivalents, and restricted cash, beginning of period	1,319,643	1,182,939
Cash, cash equivalents, and restricted cash, end of period	$ 586,092	$ 837,080

TOL has generated $141M in operating cash flow during the first nine months of the year which is well above last year's $22M during the same time period despite generating $140M less in net income. This increase in operating cash flow is mainly attributed to the $200M in additional mortgage loan sales during the year.

Net cash used in investing activities was $123M as the company purchased $75M worth of property during the year and also made $47M worth of investments.

Overall cash decreased by a whopping $733M so far through 2020, why? As we mentioned, TOL has been buying stock like crazy and that is why cash from financing activities saw a burn of $751M. TOL spent a whopping $633M buying back their stock. Much of this came in Q2 as seen in the chart below.

During the year they also raised $3.25B in new debt and used it to help pay down $3.3B worth of older debt.



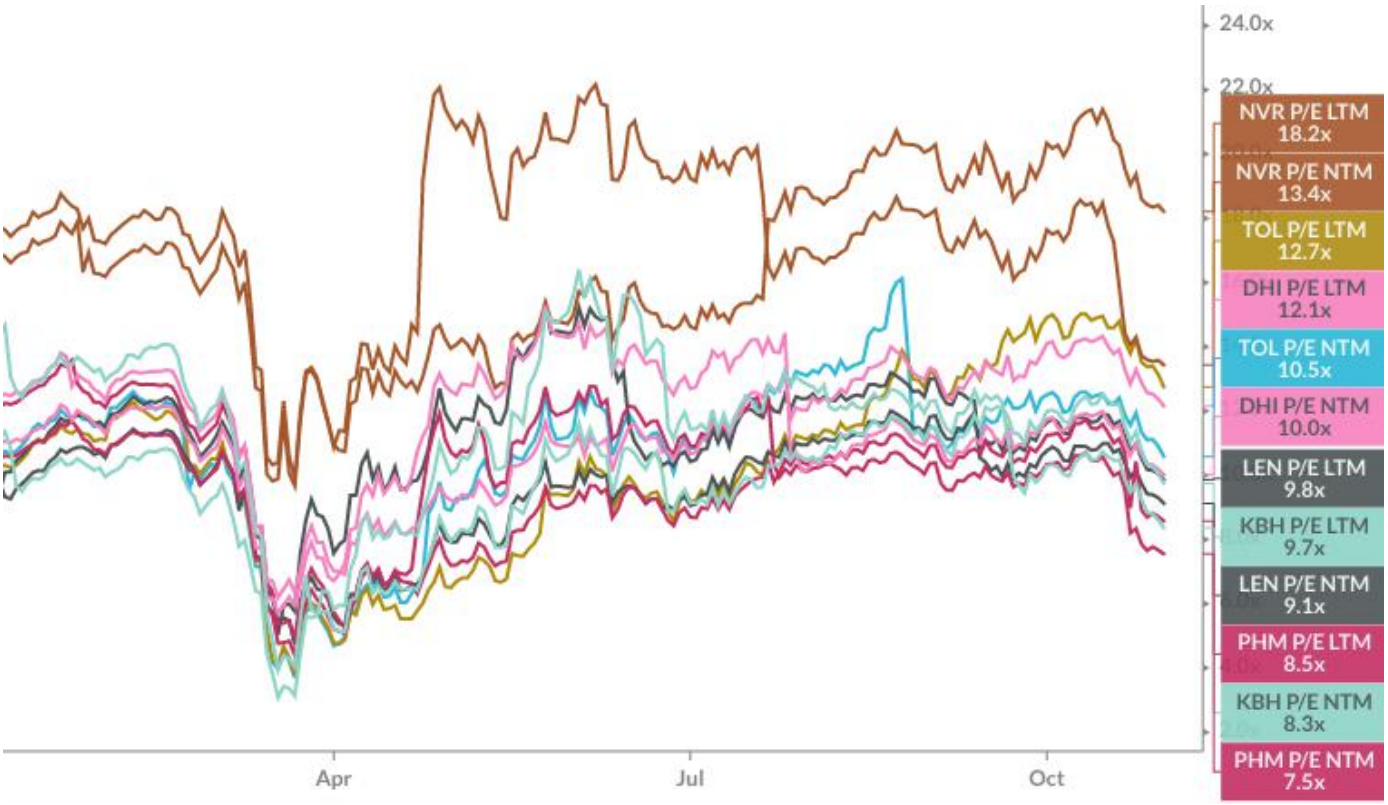
TOL FUNDAMENTALS

We are going to compare TOL to Lennar (LEN), DR Horton (DHI), KB Home (KBH), PulteGroup (PHM), and NVR Inc. (NVR).

On an enterprise value to sales basis, TOL falls right down the middle as all of the companies trade in the 0.9x-1.9x range.

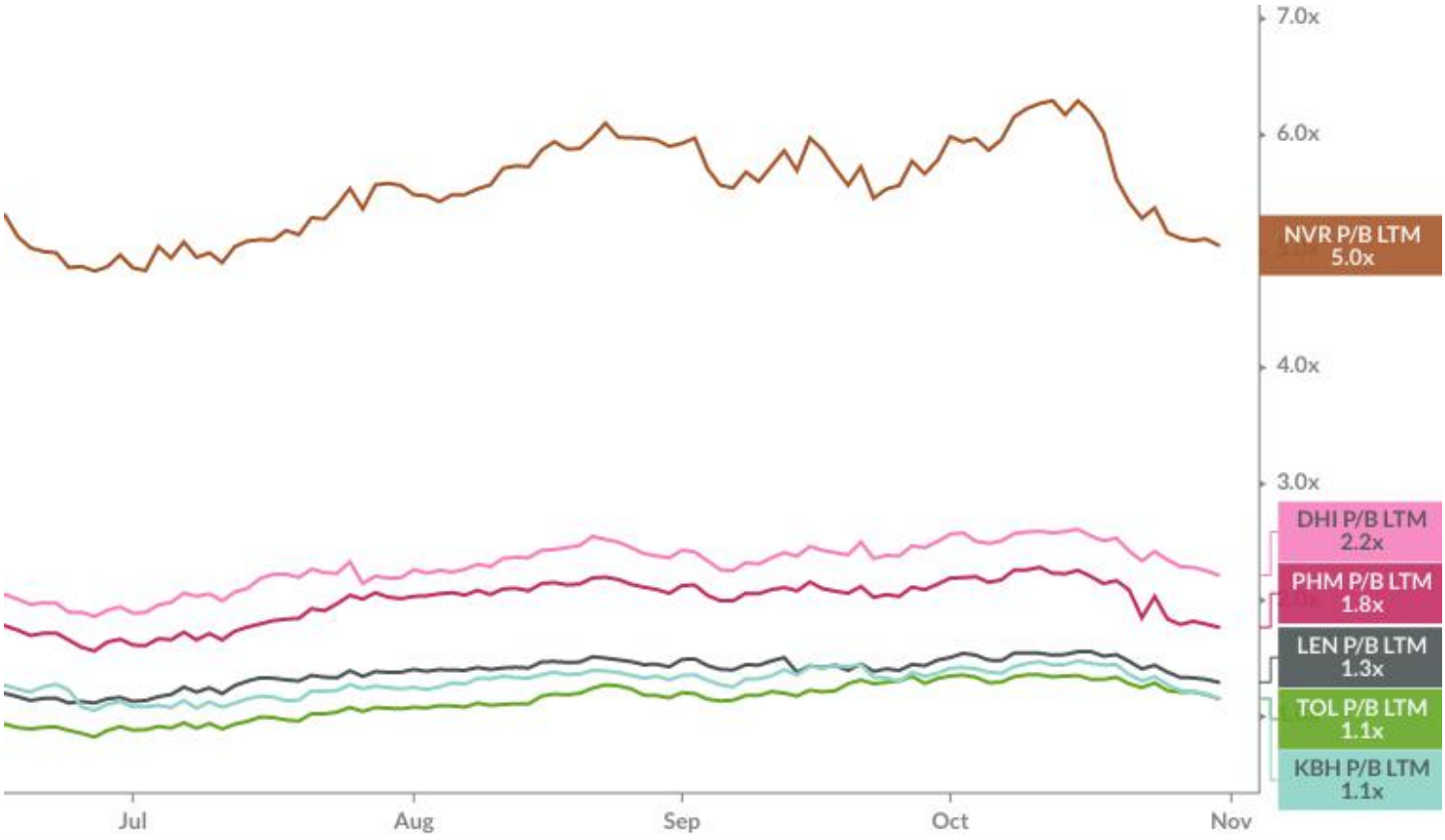
TOL FUNDAMENTALS

On a price to earnings basis, both last twelve months and forward, TOL is a little more toward the top of the range at 10.5x forward earnings and 12.7x the last twelve months earnings. NVR is the most expensive on both LTM and forward, while KBH and PHM are the cheapest.



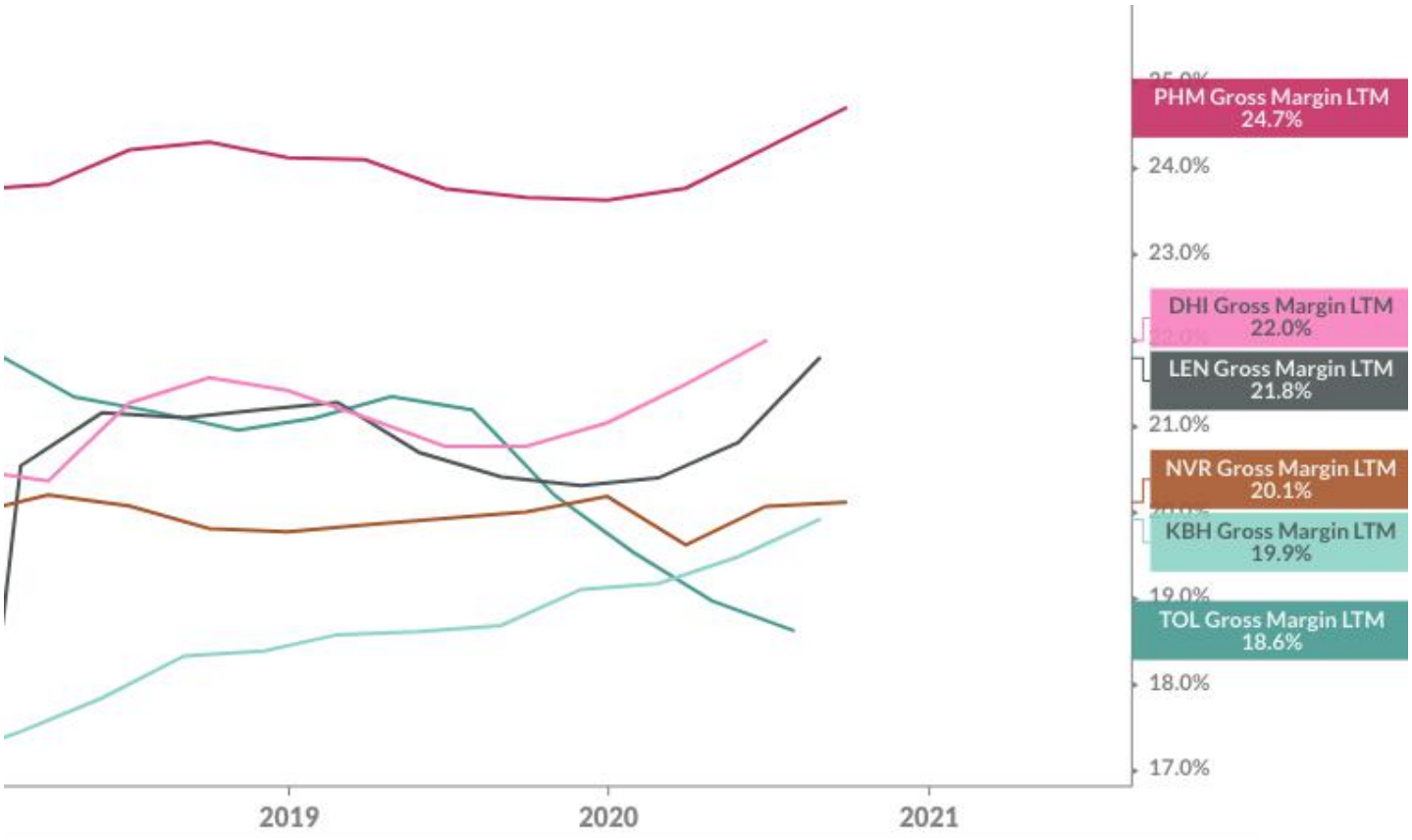
TOL FUNDAMENTALS

On a price to book value basis, TOL is tied with KBH at 1.1x. This is quite a bit cheaper than PHM at 1.8x, DHI at 2.2x and much less than NVR at 5.0x.



TOL FUNDAMENTALS

All of the players have seen margins grow over the last couple of years but TOL has the lowest gross margins over the last twelve months at 18.6% while PHM leads the group at 24.7%.

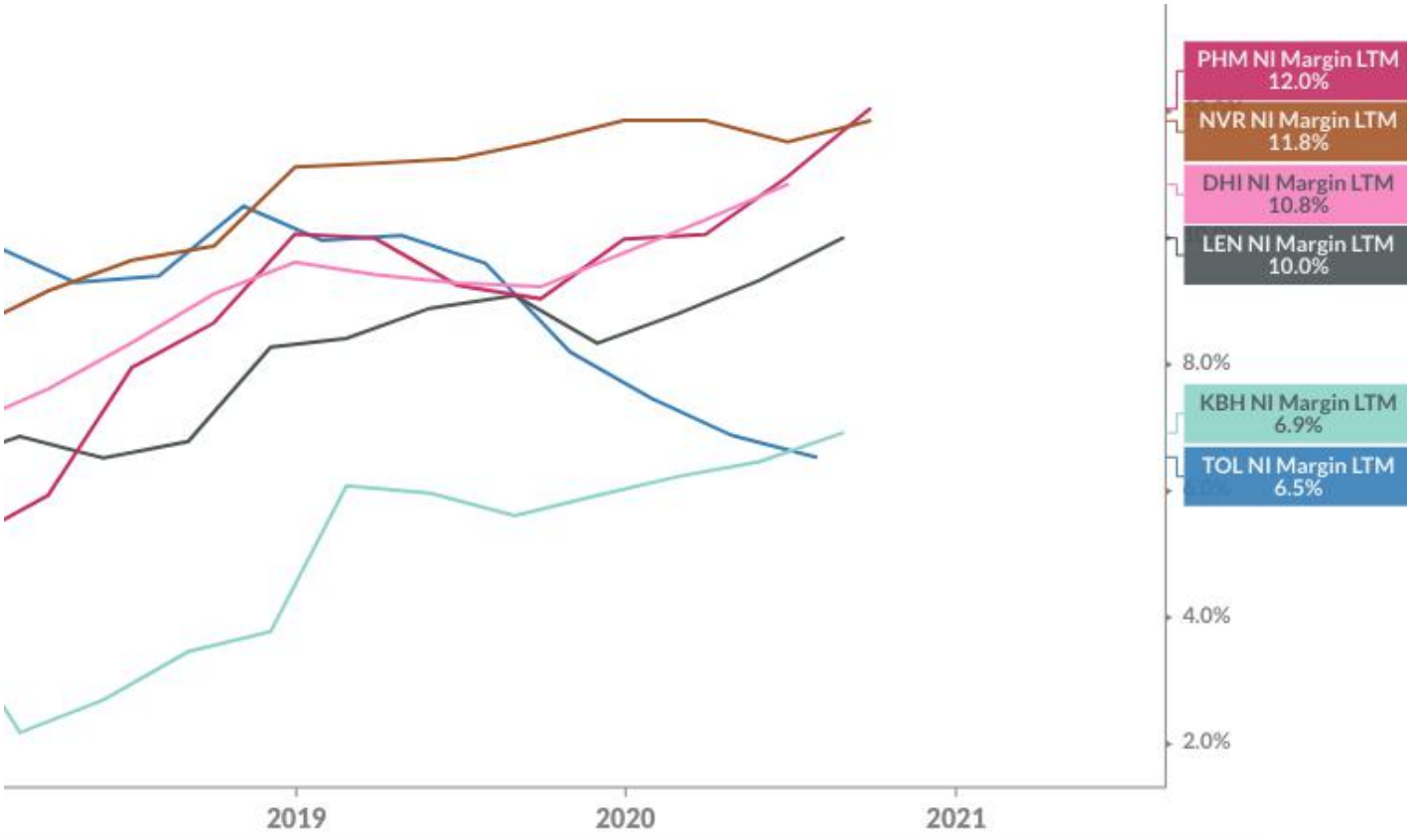


TOL FUNDAMENTALS

On an enterprise value to EBITDA (earnings before interest, taxes, depreciation, and amortization), TOL trades at the highest level at 13.4x on the last twelve months basis. Looking forward, they are tied with DHI at 10.0x which is fairly attractive. As we can see, homebuilders have gotten hit very hard alongside the market in the final weeks of October.

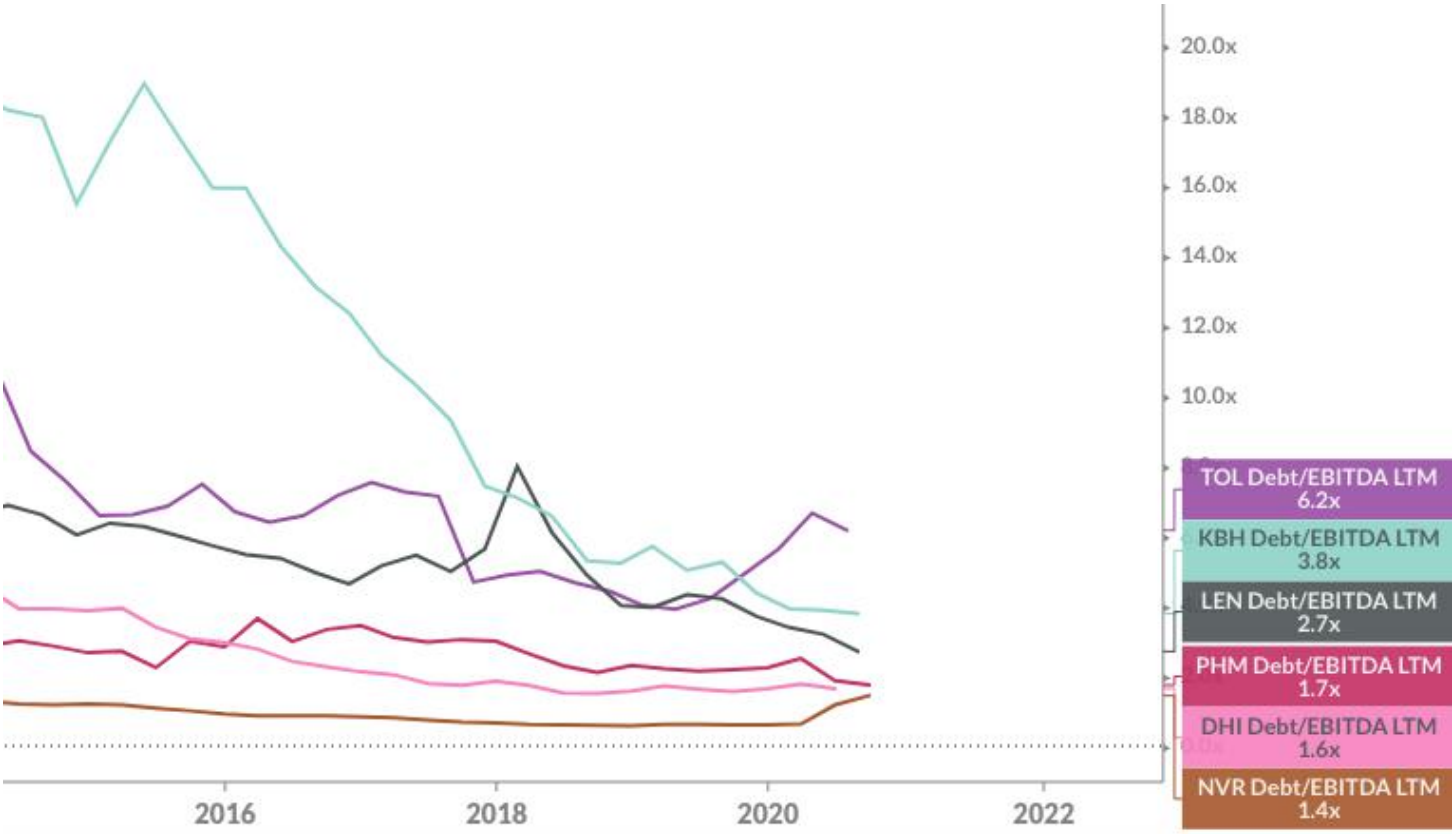
TOL FUNDAMENTALS

Similarly, TOL has the lowest net income margins at 6.5% alongside KBH at 6.9%. LEN, PHM, NVR, and DHI are generating far higher net income margins at 10.0-12.0%.



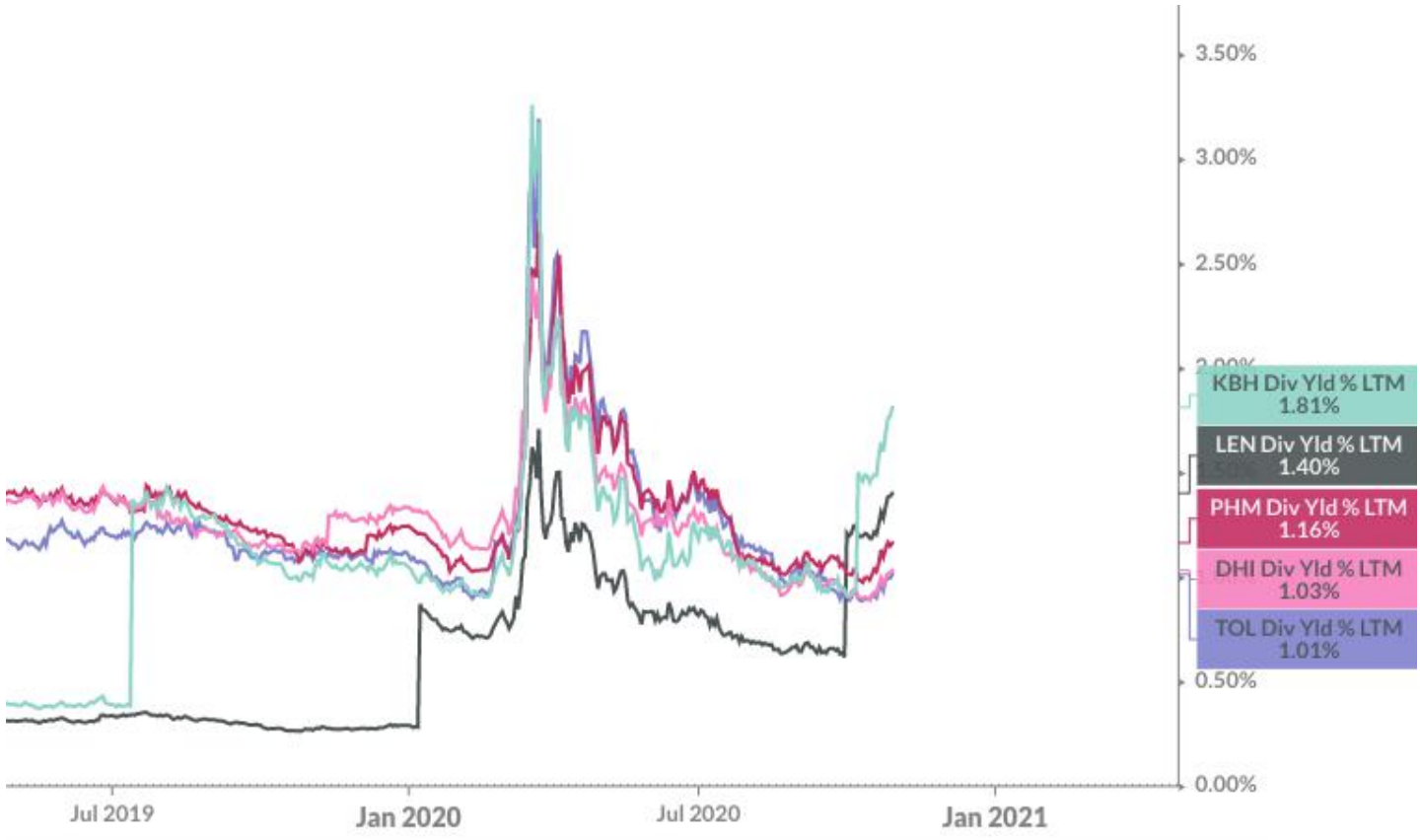
TOL FUNDAMENTALS

Unfortunately, TOL's debt to EBITDA over the last twelve months is far higher than its peers at 6.2x. NVR at the bottom is only at 1.4x . The nearest to TOL is KBH with only at $3.80 of debt for every dollar of earnings before interest, taxes, depreciation, and amortization brought in over the last twelve months.



TOL FUNDAMENTALS

As far as dividends go, TOL is at the bottom of the list here but none of the companies pay more than 2.0% and we also know that TOL is a much bigger fan of buying back stock. LEN recently doubled their dividend in their recent report.

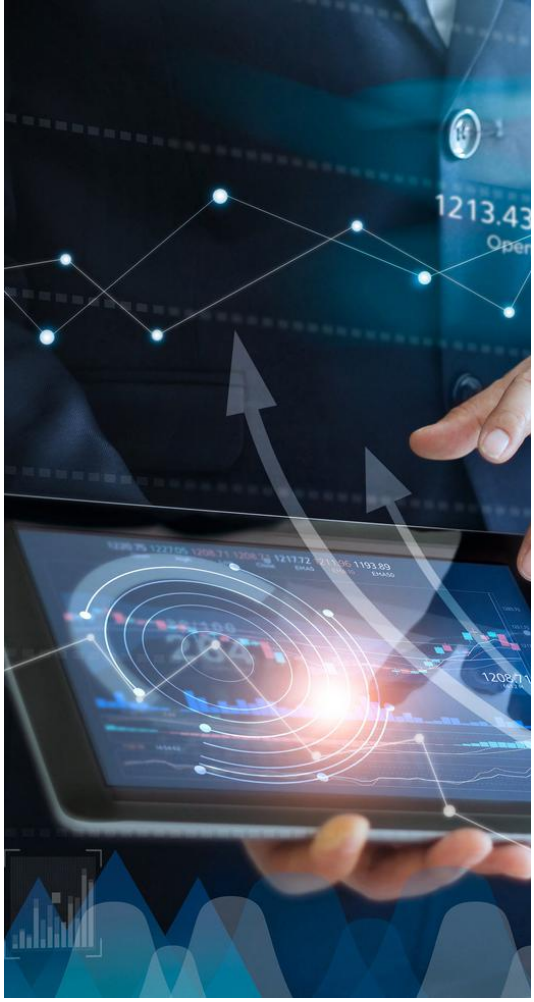


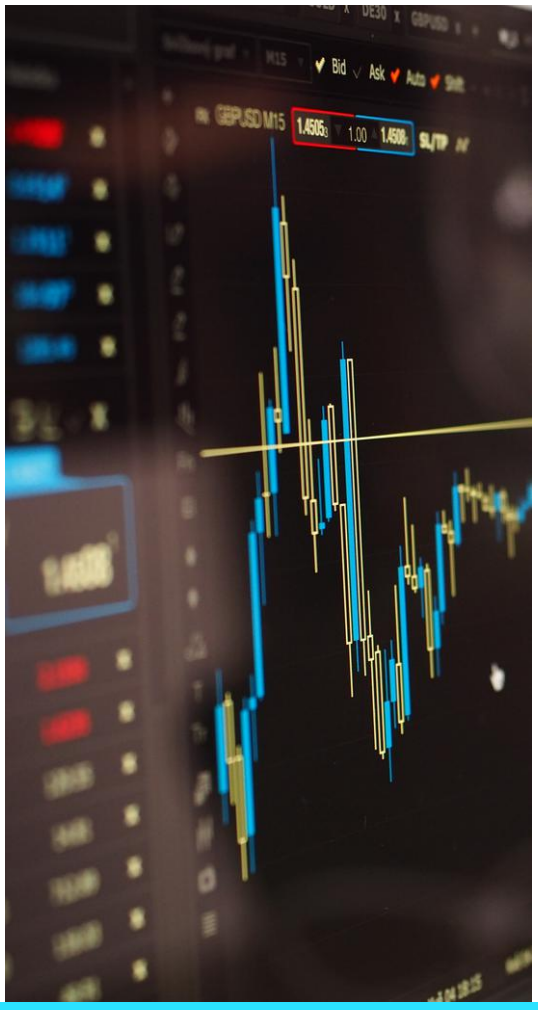
TOL
DCF MODEL

Attached in the email, as well as in the Vault, you will see the discounted cash flow model. Here are the following variables used:

- Discount Rate: 9.08% +/- 0.50%
  - Cost of Equity: 14.4%
    - Beta: 2.0
    - 30 YR Treasury (Risk Free Rate): 1.42%
    - Market Risk Premium: 6.00%
  - Cost of Debt: 4.77%
    - 45.5% weight due to capital structure ($3.9B in debt)
    - Tax Rate: 21%
- Perpetual Growth Rate: 2.00% +/- 0.50% (tracking GDP)
- CUBE expects a strong bounce back in growth in 2021 of 25% to $8.4B in revenue as economy recovers from COVID19 and housing supply catches up to demand. We then see this followed by modest revenue growth in 2022 through 2024.
- We then believe TOL will face headwinds in 2025 as we expect the Fed will attempt to raise interest rates (much further than the 2023 expected time frame) which will in turn increase mortgage rates and slow down GDP.
- Put simply, we think the real estate market still has several years of run room left before our models see headwinds
- Current Price: $43.74
- **Base case: $49.16**
- **Bull Case: $55.39**
- **Weak Case: $44.41**

TOL
TECH ANALYSIS





TECH ANALYSIS SUMMARY

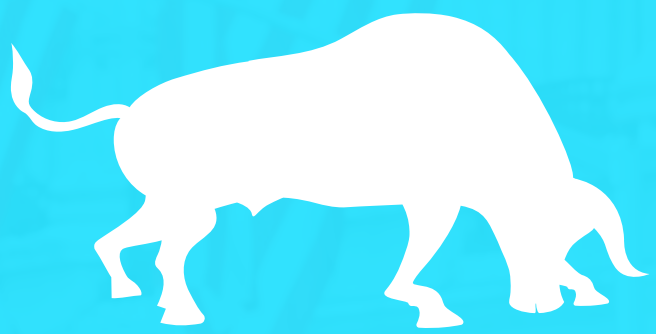
Looking at the charts, TOL has been struggling along with the broader market as shares have fallen over 13% in just a matter of two weeks.

The stock was able to reclaim its weekly R1 fibbonaci level of $43.38 by closing at $43.74.

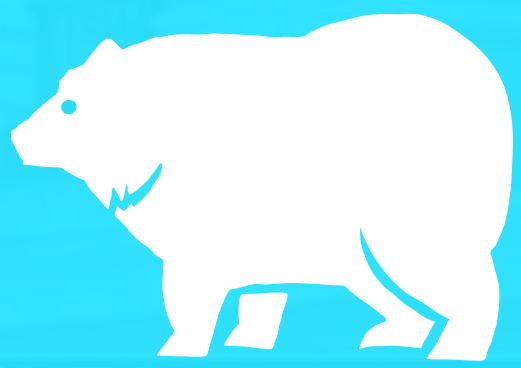
If this level holds, TOL should be making its way back to the daily pivot point of $44.91.

If $43.38 does not hold, we believe shares will fall to the 100 day moving average of $40.95.

BULLISH OR BEARISH?



VS.



MORE BULLISH (POSITIVE)

MORE BEARISH (NEGATIVE)

cube

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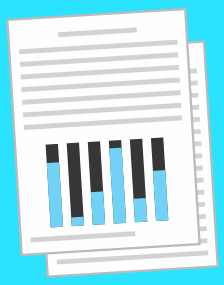

TOL CONCLUSION

Overall, CUBE likes Toll Brothers here, especially considering shares have pulled back from $50 in a matter of a few weeks.

We like the diversity of TOL's portfolio, that they cater more to wealthier individuals that are less susceptible to cyclical economic trends, purchase tons of stock, and also believe the low interest rate environment will stick around for at least the next several years, if not much longer.

At the same time, there are some risks to TOL. The company's valuation in relation to its peers is a bit on the expensive side, the company has lower margins and much greater debt on their balance sheet in comparison to their EBITDA, and there are also many economic variables that can threaten our discounted cash flow model such as continued lockdowns from COVID19, increased costs of materials, a slower than expected rebound in the economy, higher tax rates, and an attempt from the Fed to increase interest rates which will subsequently affect mortgage rates. All in all, we think shares have upside from these levels and really like the stock in the $37 area specifically as it is the book value of their portfolio, a strong technical support level, and is also the average price at which the company has been buying stock.

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