

19-Feb-2025

Toll Brothers, Inc. (TOL)

Q1 2025 Earnings Call

CORPORATE PARTICIPANTS

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

Martin P. Connor

Chief Financial Officer, Toll Brothers, Inc.

OTHER PARTICIPANTS

Stephen S. Kim

Analyst, Evercore ISI

John Lovallo

Analyst, UBS Securities LLC

Trevor Allinson

Analyst, Wolfe Research LLC

Mike Dahl

Analyst, RBC Capital Markets LLC

Michael Rehaut

Analyst, JPMorgan Securities LLC

Ivy Lynne Zelman

Analyst, Zelman & Associates

Rafe Jadrosich

Analyst, BofA Securities, Inc.

Alex Barron

Analyst, Housing Research Center LLC

MANAGEMENT DISCUSSION SECTION

Operator: Good morning, and welcome to the Toll Brothers First Quarter Fiscal Year 2025 Conference Call. All participants will be in a listen-only mode. [Operator Instructions] After today's presentation, there will be an opportunity to ask questions. [Operator Instructions] The company is planning to end the call at 9:30 when the market opens. During the question-and-answer session, please limit yourself to one question and one follow-up, and please note this event is being recorded.

I would now like to turn the conference over to Mr. Douglas Yearley, CEO. Please go ahead, sir.

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

Thank you, Chuck. Good morning. Welcome and thank you all for joining us. With me today are Marty Connor, Chief Financial Officer; Rob Parahus, President and Chief Operating Officer; Wendy Marlett, Chief Marketing Officer; and Gregg Ziegler, Senior VP, Treasurer and Head of Investor Relations.

As usual, I caution you that many statements on this call are forward-looking based on assumptions about the economy, world events, housing and financial markets, interest rates, the availability of labor and materials, inflation and many other factors beyond our control that could significantly affect future results. Please read our statement on forward-looking information in our earnings release of last night and on our website to better understand the risks associated with our forward-looking statements.

Last night, we reported first quarter deliveries of 1,991 homes at an average price of \$925,000 for home sales revenues of \$1.84 billion. Our adjusted gross margin was 26.9% or 65 basis points better than guidance, and our SG&A expense, as a percentage of home sales revenue, was 13.1% or 40 basis points above guidance.

While our net income and earnings per share came in below expectations, this was due primarily to impairments and a delay in the sale of a stabilized apartment property in one of our joint ventures. Our core homebuilding operations met expectations in the quarter.

From a demand perspective, we signed 2,307 net contracts for \$2.3 billion in the first quarter, up 13% in units and 12% in dollars compared to last year's very strong first quarter, when contracts were up approximately 40% in both units and dollars. On a per community basis, contracts were up 2% compared to last year.

We also continued to see a very healthy deposit conversion ratio in the first quarter, with 82% of our deposits converted to sales, significantly higher than our five-year average of 70%. The average sales price of orders in our first quarter was approximately \$1 million, which was essentially unchanged compared to the fourth quarter of 2024. On average, net pricing after incentives was flat in the first quarter compared to the fourth quarter of 2024.

Geographically, first quarter demand was strongest in our North and Mid-Atlantic regions from Boston to Atlanta, as well as Houston, Dallas, Boise, Denver, Las Vegas and all of California. Among our buyer segments, both move-up and first-time luxury were up on a per community basis with a slight decline in empty-nester.

Although demand was solid in our first quarter, we have seen mixed results so far this spring selling season. While demand has remained healthy in many of our markets and particularly at the higher end, affordability constraints and growing inventories in certain markets are pressuring sales, especially at the lower end.

However, all that being said, we are somewhat encouraged by our sales activity this past week. Against this backdrop, we are carefully monitoring our pricing, incentives and spec inventory on a community-by-community basis to match – to best match local selling conditions and to appropriately balance pace and price with a view towards generating higher returns in our overall business.

Based on our first quarter results, the gross margin embedded in our backlog and the mix trends that we are seeing early in the spring selling season, we are maintaining all of our key homebuilding guidance for the full year, including deliveries, average price, adjusted gross margin, SG&A margin and community count growth. We continue to see the long-term outlook for the new home market to be very positive, particularly for our luxury niche.

Demand for our homes continues to be supported by our affluent customer base. Over 70% of our business is luxury move-up and empty-nester, which serves a wealthy cohort that has benefited from years of home price and stock market appreciation. The remaining 25% to 30% serves more affluent first-time buyer, many of whom are older millennials buying their first home later in life when they have higher incomes and are more financially secure.

Consistent with the past several quarters, approximately 26% of our buyers paid all cash in the first quarter, and the LTVs for buyers who took a mortgage was approximately 68%, also consistent with recent quarters. Our contract cancellation rate in the first quarter remained low at 2.4% of beginning backlog. This industry-low cancellation rate speaks to the financial strength of our buyers as well as the sizable deposits they make and how emotionally invested they become as they personalize their homes at our Design Studios.

In the first quarter, our spec homes represented approximately 55% of sales and 52% of deliveries, and we had approximately 3,200 spec homes in inventory at quarter end. Overall, we are comfortable with this level of specs in our inventory and their stage of construction.

As I mentioned, we are actively managing our spec starts and will adjust them on a community-by-community basis based on local market conditions. This will mean fewer starts in some communities where inventories are building and may mean increased starts in other communities where demand has been strong. However, on a net basis, we do expect to reduce overall spec starts in the near term.

Remember, we sell our specs at various stages of construction from foundation forward to finished home. One-third of our spec sell before framing is completed, so the risk profile and margin for these homes is not all that different from build-to-order homes. In addition, many of our spec buyers have the opportunity to visit our Design Studios and personalize their homes with finishes that match their tastes. This benefits our margins as Design Studio upgrades tend to be highly accretive.

In the first quarter, Design Studio upgrades, structural options plus lot premiums averaged \$200,000 or 25% of our average base sales price as compared to the long-term average of about 21%. At first quarter end, we were operating from 406 communities, slightly below the 410 that we guided to last quarter. We continue to target 8% to 10% community count growth in fiscal 2025, which would put us at 440 to 450 communities by fiscal year-end.

In the quarter, we saw modest improvements in our construction cycle times as we continue to focus on increasing production efficiency. We have not seen any immediate supply chain impacts from tariffs or labor shortages due to changes in immigration policies, although we are monitoring developments closely and will pivot as necessary to deal with any issues that arise. We have all learned valuable lessons from the supply chain shocks we navigated through a few years ago with the pandemic.

Turning to land. At the first quarter end, we owned or controlled approximately 77,700 lots, 56% of which were optioned. We are pleased that we continue to make progress in the quarter towards a goal of 60% optioned and 40% owned. Our solid land position provides us flexibility and allows us to be highly selective and disciplined, as we assess new land opportunities.

Our underwriting standards for the new land continue to incorporate stringent thresholds for both margins and returns. And we continue to seek out land acquisition and development opportunities that allow us to be more capital efficient, including through increased use of option arrangements, land banks, joint ventures and similar structures that allow us to defer payments and lot takedowns.

Our balance sheet is very healthy. We have increased liquidity, low net debt and no significant debt maturities this fiscal year. As announced last week, we recently extended the maturities of our credit facilities to February 2030 and upsized our revolver to \$2.35 billion. We also continue to expect strong cash flow generation from operations this year and reaffirm our \$500 million of targeted full year share repurchases. We expect to continue investing in the growth of our business while simultaneously returning excess capital to our shareholders.

With that, I will turn it over to Marty.

Martin P. Connor

Chief Financial Officer, Toll Brothers, Inc.

Thanks, Doug. First quarter net income was \$177.7 million or \$1.75 per share diluted. These results were below expectations due to impairments and lower than projected joint venture land sales and other income. The miss on

joint venture and other income was mainly due to a delay in the sale of a stabilized apartment building from one of our joint ventures. We now expect this sale, which is under contract, to close in the second half of fiscal 2025.

Positively, our core homebuilding operations met expectations. In the first quarter, we delivered 1,991 homes at an average price of \$925,000 and generated home sales revenues of \$1.84 billion. The average price of homes delivered in the quarter was at the low end of our range due primarily to mix as we delivered more homes in our Mountain region and had fewer deliveries in the North and Pacific regions than we had projected.

As Doug mentioned, we signed 2,307 net agreements for \$2.3 billion in the quarter. This was up 13% in units and 12% in dollars compared to the first quarter of fiscal year 2024. The average price of contracts signed in the quarter was approximately \$1 million, which was essentially flat compared to both the fourth quarter of fiscal 2024 and the same period last year.

Our first quarter adjusted gross margin was 26.9%, 65 basis points better than our guidance of 26.25%. Q1 gross margin exceeded our guidance due primarily to mix, increased operating efficiency and slightly better margin from sell and settle spec homes compared to what we had projected. All regions and all property segment – project – product segments exceeded our expectations.

Based on our first quarter results, the gross margin embedded in our backlog and the mix trends that we are seeing early in the spring selling season, we are maintaining our full year adjusted gross margin guidance of 27.25%. We expect our second quarter adjusted gross margin to also be 27.25%.

Write-offs in our home sale gross margin totaled \$16.4 million in the quarter. \$3.9 million of these impairments were associated with pre-development costs on deals we are no longer pursuing and the remaining \$12.5 million was related to a handful of operating communities in various markets around the country. We also had \$1.8 million of land sale impairments and \$4.4 million of pre-development write-offs in other income related to apartment projects we are no longer pursuing.

SG&A, as a percentage of revenue, was 13.1% in the first quarter compared to our guide of 12.7%. Note that our SG&A margin in the first quarter is always higher as it is generally our lowest revenue quarter and includes an accelerated employee stock-based compensation expense that only hits in that first quarter. The 40 basis point SG&A miss relative to our guidance was due to the loss of fixed cost leverage due to lower than anticipated homebuilding revenues as well as due to higher than anticipated selling and marketing expenses in the quarter.

Our tax rate in the first quarter was 19.7% or about 230 basis points lower than the guidance due entirely to the accounting benefit of stock compensation deductions on a lower base of pre-tax income. These stock compensation deductions will not repeat in the balance of the year.

We ended the first quarter with over \$2.3 billion of liquidity, including approximately \$575 million of cash and \$1.8 billion of availability under our revolving bank credit facility. We've added \$400 million to that, subsequent to the quarter end. As Doug mentioned, we increased the capacity of our revolving credit facility, and we also extended the maturities of both our revolver and our \$650 million term loan to February 2030. We thank our banks for their continuing support.

Our net debt-to-capital ratio was 21.1% at first quarter end, down from 21.4% one year ago. We have no significant maturities of our long-term debt until fiscal 2026 when \$350 million of notes come due this November. Our community count at quarter end was 406 compared to our guide of 410.

Now, let me turn to our forward guidance, which is subject to the usual caveats regarding forward-looking information. We are projecting fiscal 2025 second quarter deliveries of approximately 2,500 to 2,700 homes, with an average delivered price between \$940,000 and \$960,000. For full fiscal year 2025, we are maintaining our projected deliveries to be between 11,200 and 11,600 homes, with an average price between \$945,000 and \$965,000.

As I noted earlier, we expect adjusted gross margin to be 27.25% for both the second quarter and the full year. We expect interest and cost of sales to be approximately 1.2% in the second quarter and for the full year.

We project second quarter SG&A, as a percentage of home sales revenues, to be approximately 10.3%. For the full year, we continue to expect it to be 9.4% to 9.5%. Other income, income from unconsolidated entities and land sales gross profit in the second quarter is expected to breakeven.

We continue to expect \$110 million for the full year, which includes the sale of several stabilized apartment projects in the second half. As noted earlier, we had planned to close one of these apartment sales in the first quarter. The sale is under contract and the transaction is now expected to close in the second half of the year.

We project the second quarter tax rate to be approximately 26% and the full year rate to be approximately 25.5%. Based on land we currently own or control, we expect to grow community count by 8% to 10% by the end of fiscal 2025 and are targeting 440 to 450 communities. We expect to be operating from 415 selling communities at the end of the second quarter.

Our weighted average share count is expected to be approximately 101 million shares for the second quarter and 100.5 million shares for the full year. This assumes we repurchased a targeted \$500 million of common stock for the full year, with most of that occurring later in the year aligned with our anticipated higher cash flows.

Now, let me turn it back to Doug.

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

Thank you, Marty. Before I open it up for questions, I'd like to thank our Toll Brothers' employees for their hard work, dedication and commitment to our customers. Their talent and constant focus on our business is the driver of our long-term success.

Okay. Chuck, let's open it up to questions.

QUESTION AND ANSWER SECTION

Operator: We will now begin the question-and-answer session. As a reminder, the company is planning to end the call at 9:30 when the market opens. During the question-and-answer session, please limit yourself to one question and one follow-up. [Operator Instructions] And our first question will come from Stephen Kim with Evercore ISI. Please go ahead.

Stephen S. Kim

Analyst, Evercore ISI

Q

Yeah. Thanks very much, guys. Appreciate all the color. I guess, I wanted to start off by just talking about your inventory. You talked about the fact that your spec levels were, you were comfortable with them as well as the stage of construction. And we can see that your specs actually came in a little lighter than we were expecting. So that all seems positive.

That being said, your inventory did rise a lot, particularly the construction in progress number rose pretty significantly. And I was curious if you could talk about what drove that. Was there something about the land or the land on which you're building these homes, which has a greater value, where are you just naturally – are you at a later stage of construction, but you're just comfortable with it? Just if you could help us understand sort of what's going into the much higher inventory number that we saw this quarter.

Martin P. Connor

Chief Financial Officer, Toll Brothers, Inc.

A

Yeah. Stephen, I think you hit it at it. I think we have more specs under construction. They're at a little bit further stage of completion stage of spend than they had been in prior years or more recently. And that's with an eye towards having the inventory to hit our 11,400 delivery guidance for this year.

Stephen S. Kim

Analyst, Evercore ISI

Q

And I thought you were going to continue there because you also had talked about the fact that you were looking to maybe slow down a little bit on your specs, as you headed later in the year. Is this something that we should just – is this just the kind of the natural cadence that we should expect to see from you from this point forward as we go into the spring, just carrying more specs and that sort of thing, and then sort of bringing that down as we go later in the year?

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

A

Yeah. Steve, we definitely focus on seasonality, when most buyers are in the market, when most buyers want to move in, which is generally the summer months, and we try to time the start and the construction, and of course then the completion of our spec inventory so it lines up with seasonality. And I think that's what you're seeing right now.

We have 3,200 spec homes that are at the beginning of framing or forward, so framing and beyond. And then, we have about 1,000 specs that are sitting at foundation. Some of those are on hold at foundation, where we haven't yet released them for framing. And then we have about 1,600 specs that are sitting at permit that have not been released yet for foundations to go in.

And this is all strategic. It's all based on the timing of the year. We're very comfortable with where the level stand. We did this on purpose to set up for the spring and for the summer delivery. Over time, short – over short-term timing, we do expect to cut back a bit on the new spec starts. So when I tell you that there are 1,600 at permit, but they've been held and are not authorized to go to foundation, we're keeping an eye on that closely. When I tell you there's 1,000 at foundation that haven't yet been released for framing, that's all strategic and intentional.

It is all decided by market. There are some markets that are performing very well, where we are actually increasing our spec activity, and there's other markets, as we've talked about, that have had more mixed results lately where we are being more tempered. And so, this is the analysis we do. But at the moment, we are leaning more towards less spec starts than you've seen in the past.

Stephen S. Kim

Analyst, Evercore ISI

[indiscernible] (00:23:28)

Q

Martin P. Connor

Chief Financial Officer, Toll Brothers, Inc.

I just add to that, Doug, that it's even more specific than by market. It's by community, although the mentality often applies by market.

A

Stephen S. Kim

Analyst, Evercore ISI

Yeah. That's very helpful. And it kind of leads into the next questions I have, which is about the spring selling season. So you made the comment about it being mixed. And I think that that is something that we've been hearing from a number of folk.

Q

I guess, what I really wanted to understand is, what is the company's posture relative to your production pipeline and your anticipated land spend over the next year or two in light – if the spring selling season continues to be mixed. Is this an environment which will cause you to have to pivot in some way? And if so, what kind of pivot or nudging the dial one way or the other should we be expecting if the spring selling season remains mixed?

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

If the spring selling season remains mixed, the overall land spend will come down. We will become more conservative in certain markets in the underwriting of new land. As you know and as we brag about all the time, we have a terrific pipeline of owned and optioned land. We are in great shape in all of our markets. We have the opportunity to be very selective. While we haven't guided the 2026 community count growth, I can tell you that the land we control today provides the opportunity to continue growing communities as we have the last few years without running out and finding any more land.

A

So it's a very local business. We will still be active in the land buying business, but, overall, the land spend would come down.

Operator: The next question will come from John Lovallo with UBS. Please go ahead.

John Lovallo

Analyst, UBS Securities LLC

Q

Good morning, guys. Thanks for taking my questions as well. Maybe just starting off on the gross margin. The second quarter gross margin outlook would seem to imply sort of steady fiscal year 2Q to 4Q gross margins to achieve that full year target of 27.25%. So I guess the question is, how are you thinking about incentives in that forecast? Are you assuming pretty fairly stable levels with what we saw in the first quarter?

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

A

Sure. So, the second quarter gross margin with our guide jumping up to 27.25% is because we expect to have more Pacific, which is higher margin. We expect to have more luxury, which is higher margin, and a bit less affordable luxury and empty-nester or age targeted. So, the mix aligns with that increased guide. When you look to the second half of the year, and obviously it needs to be modestly above 27.25%...

Martin P. Connor

Chief Financial Officer, Toll Brothers, Inc.

A

Modestly. I'd just comment that it's pretty steady is a pretty good comp.

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

A

Correct, because the first quarter only had 2,000 deliveries, so the 26.9% is off of a smaller part of – it's not a quarter of the year; it's less than that. So, we continue to see in the second half of the year pretty much what I just described, which is more Pacific, more North. And North has been very high margin as the northern region, as we talked about, has been very strong, and we have more luxury than we have affordable and age targeted.

With respect to your question about our confidence level and how we have budgeted, because we do recognize there are a number of sales that haven't occurred yet, we do have 6,300 homes in backlog, we have delivered 2,000 homes in the first quarter, so that is 8,300 of the 11,400. I'm not saying every home in backlog delivers, but most of that delivers, but we do recognize that there are some homes that still have to be sold. Many of those are spec.

All I'll tell you is we have a great level of confidence in the conservatism we have brought to the pricing, the incentivizing that needs to occur community-by-community, market-by-market, to complete the year with the balance of those sales and still hit the guided margin.

John Lovallo

Analyst, UBS Securities LLC

Q

Great.

Martin P. Connor

Chief Financial Officer, Toll Brothers, Inc.

A

Yeah. I'd add to that, John, that the specs we have with roughly 1,000 of them complete, and so the cost there is known. There's no variability in that cost. And the specs we have under construction, which is another 2,300 or 2,400 behind that, are contracted for. And so the costs are pretty well locked down there, gives us further confidence in terms of what we will sell and settle from this point forward through the balance of the year. And we

base our estimates based on what we're seeing in the market most recently for the balance of the year with some conservatism.

John Lovallo

Analyst, UBS Securities LLC

Q

Okay. So you're not assuming any relief from rates or any pullback in incentives is what I was trying to get at. Okay.

Martin P. Connor

Chief Financial Officer, Toll Brothers, Inc.

A

No, no.

John Lovallo

Analyst, UBS Securities LLC

Q

Yeah. That's helpful. And then, on the lower – some of the lower priced inventory negatively impacting sales, I'm curious what price points specifically that you were seeing some of that competition? What markets you're referring to? I mean, we've heard from some of the more entry-level focused folks that the inventory at the very low level is still fairly limited. So I'm just curious where you guys were seeing that real competition intensifying.

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

A

Sure. So when we go down in price, it's not nearly as low as many of the other builders and what many define as a starter market. Our 25% to 30% of our business that is first-time buyer is still the affluent luxury end of the first-time buyer. They're a bit older, late 30s. They may have a combined family income of \$200,000 and they can afford a \$600,000, \$700,000, \$800,000 home even in today's rate market.

So we rarely go down into the territory where I think there's been the most pain and there's the most affordability pressure. I mentioned in my prepared comments our stronger markets. The softer markets in the first quarter included Jacksonville, Tampa, San Antonio, Phoenix, Reno, Salt Lake City and Portland, which are very small for us. But I will say, based on the last week or so of activity, and it's very early, this is a very fluid market, we are a bit encouraged by what's happened in the last week or so in several of these markets that were soft in Q1. So I would – if it was one week you ask me about, I probably take Jacksonville, Tampa and even Phoenix off the list. But again, I'm not going to be all that bold because it's one week, but those would be the places where we're feeling the most pressure, particularly as you come down a bit in price.

Operator: The next question will come from Trevor Allinson with Wolfe Research. Please go ahead.

Trevor Allinson

Analyst, Wolfe Research LLC

Q

Good morning and thank you for taking my questions. First, following up on the geographical question, thinking about Southern California and Washington, D.C., demand in those markets, Southern California with the wildfires, and then D.C. with the DOGE impact on potential employment there. Have you started to see any impacts to either of those markets, either from the wildfires or just from overall employment uncertainty in D.C.?

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

A

No. Washington, DC, which for us is Maryland, Northern Virginia, strong. Southern Cal, strong.

Trevor Allinson

Analyst, Wolfe Research LLC

Q

Okay, great. It's good to hear. And then second, last fall, we consistently heard of buyers postponing home purchases, expecting rates to come down in 2025. And for your buyer who generally is not battling qualification issues, the rates not moving lower here. Are you starting to see a shift where some of those buyers that were maybe waiting before for rates to come down are starting to get back into the market and transact here? And then, if not, can you talk about maybe what's holding them back? Is that still an expectation for rates to move lower or anything else to call out? Thanks.

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

A

I think in some markets we are seeing what you described. Our buyers are affluent. Nobody loves a [ph] 6.875% rate (00:32:36), but they can afford it, and they've been waiting a long time. And I think if anything, they recognize now that rates are probably not going to move significantly lower this year. I think that's where the indications are, and it's time to move on with their lives. The kids have hit middle school. It's time to get a bigger house in a more prestigious town with a better school district. And they're going to move forward.

Now, that's not everywhere. If it was, then it wouldn't be the mixed market that I have described. So in those areas where buyers are a bit more hesitant, I think it's, number one, those areas have had more significant price appreciation through the COVID years than other areas. So instead of a 40% to 50% price increase over the last five years, maybe they're in a market where there's been 60%, 70%, 80%, 100% price increase. And that includes Florida, primarily Austin, Texas as an example, where we've seen prices up dramatically. And I think that that can cause some concern to people that, boy, they just missed it. The price is up so much. That goes to affordability.

There's markets where inventory levels are growing a bit. And so the resale market is not feeling as strong as it had in the past. And there are some fears about the ability to sell my home and they – do they want to contract for a new move-up home when they're not as confident in selling their existing home as quickly or at the price that they thought they could sell it at.

A lot of this growing inventory in existing markets is not with used homes coming on the market. It's with more new spec inventory hitting the market from the builders. And so those markets where you have more national builders, there may be more inventory that those national builders have put on the market.

One of the reasons Boston down to Atlanta, and particularly Boston down to the Carolinas, has been so strong for us is because the resale market does not have a lot of the new home spec sitting on it, because the big builders don't build there. And so the resale market tends to be the older traditional resales. And there aren't a lot of those on the market and it's tight, and the opportunity is to go new. And so that's one of the reasons the Northeast, Mid-Atlantic is so strong.

So it's a really mixed story. Part of it is what you described where there is – are people are ready to move, but in other areas, there's a bit of a hesitancy. And we're just – we're managing through all of it.

Martin P. Connor

Chief Financial Officer, Toll Brothers, Inc.

A

Trevor, the one thing I'd add to Doug's comments since you mentioned rates is that 26% of our buyers pay all cash. So the rate equation is of less relevance to them. And that is a really strong number for us.

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

A

And the LTV at 68% means people have the ability, because of their financial strength, to take a bit less mortgage at a higher rate and still make the move. And since we're selling here, let's not forget mom and dad.

Martin P. Connor

Chief Financial Officer, Toll Brothers, Inc.

A

Right.

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

A

They are affluent and they are wanting to help their kids move up in life and support down payments or whatever else they can do through gifting to lower the mortgage amount.

Operator: The next question will come from Mike Dahl with RBC Capital Markets. Please go ahead.

Mike Dahl

Analyst, RBC Capital Markets LLC

Q

Good morning. Thanks for taking my questions.

Martin P. Connor

Chief Financial Officer, Toll Brothers, Inc.

A

Morning.

Mike Dahl

Analyst, RBC Capital Markets LLC

Q

Doug, at the risk of asking you to extrapolate where none of us really want to extrapolate a day, a week, a few weeks, given your comments on kind of both the mix, but then the more recent week, can you just help level set kind of what – like, quantify some level of trends quarter-to-date because, typically, you would be up very significantly sequentially in terms of order pace? So how are you stacking up compared to that? What are you thinking in terms of a 2Q kind of pace, how you're tracking?

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

A

Yeah. As you know, Mike, we're hesitant to give sales guidance, but I'll tell you that we believe that we will hit, we can hit, the market is there to hit with the margin we talked about and with – we balance pace and price. We are not margin proud. We want to drive returns, but we're also – we have a good mix and it's working really well. And we're going to continue to execute upon this strategy to stay in the middle lane between price and pace. And we think we will hit 3,000 contracts in Q2, which is 2.4 agreements per month. And there you have it. Right, Marty?

Martin P. Connor

Chief Financial Officer, Toll Brothers, Inc.

A

Yeah. I think that's an achievable number without much move in the pricing of the homes.

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

Correct.

Mike Dahl

Analyst, RBC Capital Markets LLC

Okay. So status quo, 3,000, got it. In terms of then the spec dynamics, Marty, I think you mentioned kind of modest upside to spec margins as a driver for 1Q. Can you give us an update? And I know you've got kind of mix adjusted numbers, like-for-like. There's a lot of things that go into the spec spread when you consider which specific lots you're building on. Can you give us an update on kind of where that – where those margin spreads are on the specs versus build-to-order right now?

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

Mike, I'll take this one. Spec margin is still running, as we talked in the past, about 200 to 250 basis points below average. We're comfortable with that. We did a little better in the first quarter, which is why the margin was up. And when we look at our spec that is now in our backlog that we'll be delivering at some point here, one of the reasons we're comfortable with our guide going forward is because it's doing a bit better than that.

On a related subject, which also includes spec, let's talk about incentives a little bit. The average incentive in Q4 of 2024 was \$68,000. The average incentive in Q1 of 2025 was \$62,000. So, it came in by \$6,000. We ended Q4 2024 or started Q1 2025 with an incentive at \$55,000. So, it had come down another \$7,000 from the average in Q4.

And with the mixed market we have described, in some markets we're raising prices and cutting incentives, but in other markets, we know we will be giving back some of that improvement to take it back to what might have been the average in Q4. And we have all of that built in, plus some additional cushion when we talk about the returns we expect over the balance of the year. So, that's where things stand right now.

Operator: The next question will come from Michael Rehaut with JPMorgan. Please go ahead.

Michael Rehaut

Analyst, JPMorgan Securities LLC

Great. Thanks for taking my questions. Good morning, everyone.

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

Hi, Michael.

Michael Rehaut

Analyst, JPMorgan Securities LLC

I just wanted to circle back to your comment of mixed results. And I think there was a question about if those mixed results were to continue, how would that affect the rest of the year? And the answer that you gave it was

interesting in that it didn't – it appeared that your reiteration of full year guidance is, in some ways, I guess, kind of incorporating the current state of mixed results. In other words, kind of reflecting where we are today.

So, I wanted to know if that – kind of my take on that is kind of accurate. And in other words, with maybe the present state where you just described you're maybe raising prices in some communities, raising incentives in others, if that current state, again, and some of the mix of pricing actions here, anticipating in response to that mixed results type of dynamic, if that's all kind of incorporated in your current guide?

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

A

Yes. We are anticipating – with the guidance we have given for the second quarter and the full year, we have assumed a continuation of this mixed market.

Michael Rehaut

Analyst, JPMorgan Securities LLC

Q

Right. Okay. That's helpful. And I think important just to, obviously, state explicitly.

Martin P. Connor

Chief Financial Officer, Toll Brothers, Inc.

A

Mike, I think it's also important to remember, our backlog is two-thirds of what we have left to go, right? So we're really talking about the other 3,000, 3,300 homes that we haven't sold and settled yet that have the, I'll say, variability and potential to impact positively or negatively our margin guidance.

Michael Rehaut

Analyst, JPMorgan Securities LLC

Q

Right. No, that's fair as well. And I guess, you had – it was very helpful, Doug, in terms of walking through the dollars of incentives, 4Q, 1Q, and where you stand today, which is pretty impressive. All the – I guess, just to level set that, what was the average incentive in fiscal 2024? And I guess, with any kind of forward-looking view on land cost inflation, how are you thinking about land cost inflation this year and perhaps next year?

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

A

Q1 of 2024, Gregg Ziegler tells me our incentive was \$55,000. And I'm sorry, Mike, I was focused on that number, trying to get it for you. What was the other?

Martin P. Connor

Chief Financial Officer, Toll Brothers, Inc.

A

Land cost inflation, what do we think?

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

A

Thank you. Apologies. Very happy with deal flow. We continue to find good action with our strict underwriting of a combination score of gross margin and IRR. It's modest. I would say, low- to mid-single digit. If I had – that's where I think it is. Mike, I'm very pleased.

We've had very unique opportunities lately in the land game, a lot of suburban office that is half occupied and is better suited to be torn down and rebuilt as residential with towns embracing that, because they don't want to look at a blighted, half empty office building anymore with the weeds growing, and they'd rather have some vibrancy and some people. And we're seeing a lot of cool deal flow around that, which is more infill, and the entitlements are a bit easier and more predictable, and the margins have been great.

So that's just one example, but there's a lot of that going on. And we're really well-suited for those kind of unique deals with the way we go about it, and as attractive as Toll Brothers is to many municipalities. So I'm very pleased in the land side and the inflation is low.

Martin P. Connor

Chief Financial Officer, Toll Brothers, Inc.

A

And Mike, since we've focused a lot about our projections for this year, that low inflation cost is not relevant to our projections for this year. The land we have in the projections for this year is already known. It's not going to be impacted by any inflationary pressures.

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

A

And next year, for the most part...

Martin P. Connor

Chief Financial Officer, Toll Brothers, Inc.

A

Yeah.

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

A

...it's hard to turn raw land into houses in less than 18 months.

Operator: The next question will come from Jesse Lederman with Zelman & Associates. Please go ahead.

Ivy Lynne Zelman

Analyst, Zelman & Associates

Q

Actually, it's Ivy. Good morning. So, I think with Michael Rehaut and others might be trying to get to just to circle back to guidance, is that going into the year, at the end of your fourth quarter and giving guidance for 1Q, you didn't know the market was going to be mixed. And now the market is mixed, but yet your outlook for earnings did not change.

And I guess the question is, what were you incorporating as you gave that forecast for the original guidance? I think that's the disconnect. But I think, Marty, maybe you explained it because this year is only going to have one quarter that could be at risk. So is that the framework that we should be thinking about? Just to circle back there, and then I have a follow-up.

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

A

Sure. Great to hear your voice, Ivy.

Ivy Lynne Zelman

Analyst, Zelman & Associates

Thanks.

Q

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

If you guys remember, back in the fall, we were hinting towards a 27.50% gross margin in 2025. And then, when we gave more definitive guidance in December, we cut that back modestly by 25 points to the 27.25%. So there was a little bit of conservatism in December when we were thinking about where the market was. We felt better in December, but we had a bad September and October as rates had jumped up and as we were heading into the election.

So I wouldn't say we were euphoric in December. We were still cautious and we were hopeful. And now that we sit here in mid-February, the results have been a bit more mixed than we thought, but we're still doing okay and we're outperforming, frankly. Our spec pricing has been a bit better. There's more luxury coming in the second half of the year, as we've talked about. There's more North and Pacific coming.

So, we're just feeling good about where we are. It's all I can tell you. And part of that might have been a little bit of a conservatism that we built into what we said in December, which I'm glad we did.

Ivy Lynne Zelman

Analyst, Zelman & Associates

Got it. No, that's helpful. And I think going back to the last question on land, I just don't know if you can quantify for us how much land still remains that would have been purchased pre-COVID. And if, in fact, there is a decent amount still that you will be able to go vertical on at low cost – on a low cost basis.

Q

Martin P. Connor

Chief Financial Officer, Toll Brothers, Inc.

I think we like the term contracted for rather than purchased, Ivy, just to be clear because some of it might have been purchased more recently, but based on a price that we set pre-COVID. We used December of 2020 as our pre-COVID and post-COVID. And we think it's approximately 30% of our land bank right now is still priced pre-COVID. 50% of what we owned and 40% of what we settled.

A

Operator: The next question will come from Rafe Jadrosich with Bank of America. Please go ahead.

Rafe Jadrosich

Analyst, BofA Securities, Inc.

Hi. Good morning. It's Rafe. Thanks for taking my question.

Q

Martin P. Connor

Chief Financial Officer, Toll Brothers, Inc.

How are you, Rafe?

A

Rafe Jadrosich

Analyst, BofA Securities, Inc.

Q

Just kind of following up on the comment about the kind of current absorption pace and the demand trends have been a little bit more mixed. If we see sort of the absorption pace kind of stay like this over the intermediate term or over the next few quarters, do you still think that you'll be able to hold this 27% gross margin range? Or if the absorption sort of stays at this level, you mentioned that you're not margin proud, would you kind of push or lean a little bit more into incentives?

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

A

Well, we're not going to guide beyond 2025. We're very confident in what we've given all of you for the second quarter and the balance of the year. You say if this market sticks, I think if this market sticks, since we already said we've – we're assuming it sticks with the guide we've given, then we are confident in this range of margin. However, if – to take it to the next level, if the market gets better, you're going to see better margins out of us because we love take – we love raising prices. Nothing – no better way to create urgency than price increase coming next Monday.

And if the market was to soften, we're not going to stand proud and not sell homes and try to hang on to a margin that's not attainable. We're going to manage our business, which means there will be an intelligent, thoughtful, local decision being made between pace and price. And that's how we go about it.

We are encouraged, I talked about how the incentive had come down as we started Q2 and how we're able to keep that incentive down in some markets, but we might have to give some of it back in others. We've already begun doing a little bit of that. And we are encouraged with the elasticity of demand, meaning as we throw a few more bucks at it, buyers are responding. And that is certainly a good sign. There's nothing worse than the inelasticity, where it doesn't matter what you do, the buyers are on the sidelines.

So we are encouraged by what we're seeing in those markets that have required a little bit more of an incentive.

Rafe Jadrosich

Analyst, BofA Securities, Inc.

Q

Thank you. That's helpful. And then just on the SG&A, you called out that it was higher in the first quarter. Some of it just has to do with lower deliveries, but also higher selling expenses. And then, you still have deleverage in the second quarter as well, but then leverage in the second half of the year. Can you just talk about what's driving it higher in the first half, kind of sort of where does the leverage come from in the second half? And how we think about just SG&A dollar inflation going forward?

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

A

Sure. The biggest driver we have, we had a little bit of a creep in sales and marketing expenses, but the biggest driver is just the leverage off of revenue. In the second half of 2025, we expect \$6.6 billion of revenue. In the second half of 2024, we had \$6 billion of revenue. So we have \$600 million more revenue in the second half of 2025 than 2024, and the SG&A was 8.6% in the second half of 2024. And so we believe it's going to be in the low 8s for the second half of 2025 based off of leverage with that additional revenue I just described. And that is what brings home the full year guide.

Operator: The next question will come from Sam Reid with Wells Fargo. Please go ahead.

Martin P. Connor

Chief Financial Officer, Toll Brothers, Inc.

Sam, we can't hear you.

A

Operator: [ph] Mrs. Reed (00:53:48), your line is muted. Our next question will come from Alex Barron with Housing Research Center. Please go ahead.

Alex Barron

Analyst, Housing Research Center LLC

Yes. Thank you. Good morning, guys.

Q

Martin P. Connor

Chief Financial Officer, Toll Brothers, Inc.

Good morning, Alex.

A

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

Hi, Alex.

A

Alex Barron

Analyst, Housing Research Center LLC

I wanted to ask about your specs. Are they mainly concentrated in your lower price points or are they across all price points?

Q

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

They're across all price points, but they lean a little bit towards the affordable luxury size side because we – I think we're more comfortable at specking \$800,000 houses than we are to \$2 million or \$3 million houses. But we have – it's across the board, but it leans a little bit to the more affordable end.

A

Alex Barron

Analyst, Housing Research Center LLC

Got it. And in terms of you guys stepping on the brakes, I guess, on new permitting or new specs, I think that makes a lot of sense. Is it your sense that other builders are starting to do that as well? And can you quantify, are you guys just talking about delaying what you've already sort of specked and started or you're – how can we get our arms around what stepping on the brakes would mean for you?

Q

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

Yeah. We may be pumping the brakes a little bit. I don't think we're stepping on the brakes. But we are – it's a fair comment. And Alex, I don't think we have enough intelligence in the field yet to be able to give you a definitive answer on whether the other builders are similarly pumping the brakes. I am encouraged by some builders' comments on earnings calls or elsewhere that they too are being a bit more cautious in their spec starts.

A

Operator: This concludes our question-and-answer session. I would like to turn the conference back over to management for any closing remarks. Please go ahead.

Douglas C. Yearley, Jr.

Chairman & Chief Executive Officer, Toll Brothers, Inc.

Chuck, thank you very much. Thanks, everyone, for your interest and support. As you all know, we are always here to answer any questions you may have individually, and stay warm. I think we're 24 degrees in Philadelphia today, or I hope you're somewhere where it is warm. Take care. Thank you.

Operator: The conference is now concluded. Thank you for attending today's presentation. You may now disconnect.

Disclaimer

The information herein is based on sources we believe to be reliable but is not guaranteed by us and does not purport to be a complete or error-free statement or summary of the available data. As such, we do not warrant, endorse or guarantee the completeness, accuracy, integrity, or timeliness of the information. You must evaluate, and bear all risks associated with, the use of any information provided hereunder, including any reliance on the accuracy, completeness, safety or usefulness of such information. This information is not intended to be used as the primary basis of investment decisions. It should not be construed as advice designed to meet the particular investment needs of any investor. This report is published solely for information purposes, and is not to be construed as financial or other advice or as an offer to sell or the solicitation of an offer to buy any security in any state where such an offer or solicitation would be illegal. Any information expressed herein on this date is subject to change without notice. Any opinions or assertions contained in this information do not represent the opinions or beliefs of FactSet CallStreet, LLC. FactSet CallStreet, LLC, or one or more of its employees, including the writer of this report, may have a position in any of the securities discussed herein.

THE INFORMATION PROVIDED TO YOU HEREUNDER IS PROVIDED "AS IS," AND TO THE MAXIMUM EXTENT PERMITTED BY APPLICABLE LAW, FactSet CallStreet, LLC AND ITS LICENSORS, BUSINESS ASSOCIATES AND SUPPLIERS DISCLAIM ALL WARRANTIES WITH RESPECT TO THE SAME, EXPRESS, IMPLIED AND STATUTORY, INCLUDING WITHOUT LIMITATION ANY IMPLIED WARRANTIES OF MERCHANTABILITY, FITNESS FOR A PARTICULAR PURPOSE, ACCURACY, COMPLETENESS, AND NON-INFRINGEMENT. TO THE MAXIMUM EXTENT PERMITTED BY APPLICABLE LAW, NEITHER FACTSET CALLSTREET, LLC NOR ITS OFFICERS, MEMBERS, DIRECTORS, PARTNERS, AFFILIATES, BUSINESS ASSOCIATES, LICENSORS OR SUPPLIERS WILL BE LIABLE FOR ANY INDIRECT, INCIDENTAL, SPECIAL, CONSEQUENTIAL OR PUNITIVE DAMAGES, INCLUDING WITHOUT LIMITATION DAMAGES FOR LOST PROFITS OR REVENUES, GOODWILL, WORK STOPPAGE, SECURITY BREACHES, VIRUSES, COMPUTER FAILURE OR MALFUNCTION, USE, DATA OR OTHER INTANGIBLE LOSSES OR COMMERCIAL DAMAGES, EVEN IF ANY OF SUCH PARTIES IS ADVISED OF THE POSSIBILITY OF SUCH LOSSES, ARISING UNDER OR IN CONNECTION WITH THE INFORMATION PROVIDED HEREIN OR ANY OTHER SUBJECT MATTER HEREOF.

The contents and appearance of this report are Copyrighted FactSet CallStreet, LLC 2025 CallStreet and FactSet CallStreet, LLC are trademarks and service marks of FactSet CallStreet, LLC. All other trademarks mentioned are trademarks of their respective companies. All rights reserved.