

TOL Earnings Call Transcript

Date: 2025-05-21

Quarter: 2

Operator: Good morning, everyone, and welcome to the Toll Brothers Second 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 09:30 when the market opens. During the Q&A, please limit yourselves to one question and one follow-up. Please also note, today's event is being recorded. At this time, I'd like to turn the floor over to Douglas Yearley, CEO. Please go ahead.

Douglas Yearley: Thank you, Jamie. 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. I am pleased with our performance in the second quarter. In what proved to be a challenging environment, we met or exceeded our guidance across all key metrics. We delivered 2,899 homes at an average price of approximately \$934,000, generating record second quarter home sales revenue of \$2.71 billion or \$236 million better than the midpoint of our guidance. We posted an adjusted gross margin of 27.5% and an SG&A; margin of 9.5%, a 25 and 80 basis points better than guidance, respectively and we earned \$352.4 million or \$3.50 per diluted share. Adjusting for the \$175 million pretax land sale gain we recorded last year, our second quarter earnings per share were a record. We believe these results highlight the strength of our broadly diversified luxury product offerings, our balanced portfolio of build-to-order and spec homes and our strategy of prioritizing sales base and margin in the current environment as we seek to maximize returns. They also reflect the financial strength of our customers. Our results and the strength of our backlog also provide us the confidence to reaffirm all of our guidance for fiscal 2025, and including home sales revenue of \$10.9 billion at the midpoint, an adjusted gross margin of 27.25% and earnings of approximately \$14 per diluted share. Turning to market conditions. In the second quarter, we signed 2,650 net agreements for \$2.6 billion down approximately 13% in units and 11% in dollars compared to last year's strong second quarter. We experienced softer demand in the second quarter due to a decline in consumer confidence driven by increased economic uncertainty. These conditions have continued into our third quarter. In this environment, we believe prioritizing price and margin over pace makes the most strategic sense. We are confident that our balanced approach will allow us to continue successfully navigating this market. Our average sales price in the quarter was approximately \$983,000 compared to \$1 million in our first quarter and \$967,000 in the second quarter of fiscal 2024. Given the softer demand environment, we modestly increased incentives in the quarter. Overall, incentives were approximately 7% of the average sales price, up from our recent average of 5% to 6%. As we discussed last quarter, we have been reducing our spec starts to match local market conditions. Our spec strategy is calibrated to effectively balance the need to add quick moving homes available to meet buyer demand while protecting margins. Over the past decade, we have worked hard to build a nationwide platform with

operations in over 60 markets in 24 states. We now serve all buyer groups with the broadest home offerings in the industry and prices that range from the 300,000 to over \$5 million. We have entered new markets and expanded our offerings while enhancing all that sets us apart as America's luxury homebuilder, an exceptional brand, our affluent customer base, prestigious locations, distinctive architecture, unrivaled choice and an extraordinary customer experience. We've executed this growth strategy while derisking our balance sheet improving capital efficiency and returning capital to stockholders. Our performance in the second quarter and over the past many years has demonstrated the competitive advantages of our business and brand in driving high returns as well as our ability to navigate through challenging markets. And while the near-term outlook for the housing market remains cloudy due to the well-known affordability pressures, and the volatile macro environment, we continue to believe the long-term outlook for new home for the new home market remains positive, particularly for our luxury niche. With many entry-level buyers struggling with affordability challenges, we are pleased to be serving an affluent consumer. Over 70% of our business serves the move-up and empty nester segments. These buyers are wealthier, have greater financial flexibility and most have equity in their existing homes. The remaining 25% to 30% of our business serves the more affluent, older, first-time buyer. The financial strength of our customer base is highlighted by our industry low cancellation rate, high percentage of all cash buyers and low LTVs for those who take a mortgage. Consistent with the past several quarters, approximately 24% of our buyers paid all cash in the second quarter, up from our long-term average of approximately 20%. The LTVs of buyers who took a mortgage in the quarter was approximately 70%, and our contract cancellation rate was 2.8% of beginning backlog. In addition, the average spend on design studio selections, structural options and lot premiums was approximately \$200,000 per home in Q2 and consistent with our first quarter. These upgrades benefit our margins as they tend to be highly accretive. We continue to expect community count growth to help drive results in fiscal 2025 and beyond. We remain on target to reach our year-end guidance of approximately 440 to 450 communities, which would represent an 8% to 10% increase versus fiscal year-end 2024. We project similar community count growth in fiscal 2026. We also continue to see modest improvements in our construction cycle times as we focus on increasing production efficiency. We have not yet seen any impact from potential tariffs on building costs or product availability, while it is difficult to predict where tariffs will land and the precise impact to our business, we do not believe we will see any significant impact in fiscal 2025. Turning to land at our second quarter end, we controlled approximately 78,600 lots, 58% of which were optioned. Over the past years -- excuse me, over the past year, we have increased our percentage of option lots from 48% to 58% of our total lot count consistent with our focus on structuring land deals in more capital-efficient ways in order to enhance returns. Our land position allows us to continue to be highly selective and disciplined as we approach new opportunities. In today's environment, we have tightened our underwriting standards and are reducing land spend on new deals, which we expect to primarily impact fiscal 2026 land spend. At quarter end, we held approximately \$686 million of cash and cash equivalents and our net debt-to-capital ratio was 19.8%. We continue to generate strong operating cash flows. This provides us plenty of opportunity to both grow our business and return capital to stockholders. During the quarter, we repurchased \$177 million of our common stock. Given our strong financial position, healthy projected cash flow and our focus on returning capital to stockholders, we are increasing our projected share repurchases in fiscal 2025 from \$500 million to \$600 million. With that, I will turn it over to Marty.

Marty Connor: Thanks, Doug. And congrats on today being the 35th anniversary of your first day at Toll and your 60th conference call. We had a strong second quarter, beating our guidance for deliveries, homebuilding revenue, adjusted gross margin, SG&A; and earnings. In the quarter, we delivered 2,899 homes and generated home sales revenues of \$2.71 billion, up nearly 10% units and 2.3% in dollars compared to last year. Both were second quarter records. At the midpoint, we delivered nearly 300 more homes in our guidance or \$236 million of home sales revenue. The average price of homes delivered in the quarter was approximately \$934,000, a bit below the low end of our guidance as we delivered more homes in our Mountain and Mid-Atlantic regions than anticipated. We signed 2,650 net agreements for \$2.6 billion in the quarter, down 13% in units and 11% in dollars compared to the second quarter of fiscal year 2024. The average price of contracts signed in the quarter was

approximately \$983,000, up 1.6% compared to last year. At second quarter end, our backlog still stood at \$6.84 billion and 6,063 homes, down 7% in dollars and 15% units compared to a year ago. The average price of the homes in our backlog was \$113 million, a company record. Our second quarter adjusted gross margin was 27.5% and which was 25 basis points better than guidance. Our Q2 gross margin exceeded guidance primarily due to positive mix, strong cost control and increased leverage from higher-than-projected revenues. Write-offs in our home sales gross margin totaled \$9.8 million in the quarter, as compared to \$28.4 million in the second quarter of 2024. SG&A; as a percentage of home sales revenue was 9.5% in the second quarter and 80 basis points better than guidance. Again, reflecting our focus on cost controls and leverage from higher-than-expected home sales revenue. Second quarter JV land sales and other income was \$29 million versus our breakeven guidance. Approximately \$15 million of this gain was attributable to the sale of a stabilized asset in one of our Apartment Living joint ventures, with the remainder primarily attributable to interest income and income from our mortgage title and City Living operations. Our tax rate in the second quarter was approximately 26.2%. Our balance sheet is very healthy. At second quarter end, we had \$2.8 billion of liquidity, including approximately \$686 million of cash, and our net debt-to-capital ratio was 19.8%. In addition, we are generating strong cash flows with approximately \$1 billion of cash flows from operations projected for fiscal 2025. As previously reported, during the quarter, we extended the maturities of our credit facilities to February 2030 and upsized our revolver to \$2.35 billion and we increased our quarterly dividend by 9% to \$0.25 per share. We repurchased \$177 million of our common stock, bringing full year repurchases to approximately \$200 million and we bought 2,073 lots for \$362 million. As Doug mentioned, as a result of our strong financial position and healthy cash flows, we are increasing our projected share repurchases in fiscal '25 from \$500 million to \$600 million. Turning to guidance. Our outlook is subject to the usual caveats regarding forward-looking information and the assumptions, risks and uncertainties inherent to projections. Based on our backlog, recent sales activity and the number of homes currently under construction or completed, we expect to deliver between 2,800 and 3,000 homes in the third quarter. and we continue to expect to deliver between 11,200 and 11,600 homes for the full year. Our projected second half delivery cadence is consistent with what it has been over the past several years. On average, we delivered approximately 58% of full year deliveries in the second half with 26% of the total delivered in the third quarter and 32% in the fourth quarter. We are projecting essentially the same percentages this year. The average price of deliveries in the third quarter is expected to be between \$965,000 and \$985,000. We are maintaining our full year projection of \$945,000 to \$965,000 for our average price of deliveries. As Doug mentioned, in today's softer demand environment we believe it makes the most strategic sense to prioritize price and margin over pace. This strategy, combined with the gross margin embedded in our backlog, gives us confidence in maintaining our full year projected adjusted gross margin of 27.5%. For the third quarter, we also expect adjusted gross margin to be 27.25%. We expect interest in cost of sales to be approximately 1.2% of home sales revenues in the third quarter and also for the full year. Third quarter SG&A; as a percentage of home sales revenue is expected to be approximately 9.2%. For the full year, we continue to expect it to be between 9.4% and 9.5%. Other income, income from unconsolidated entities and land sales gross profit in the third quarter is expected to break even. We continue to project \$110 million for the full year much of which is projected to come from fourth quarter sales of our interest in certain stabilized department communities developed by Toll Brothers Apartment Living in joint venture with various partners. We project the third quarter tax rate to be approximately 26% and the full year rate to be approximately 25.5%. Our community count at quarter end was \$421 compared to our guide of \$4.15. We expect 430 at the end of the third quarter and reaffirm 440 to 450 communities by the end of the fiscal year. Our weighted average share count is expected to be approximately 99 million for the third quarter and 100 million for the full year. This assumes we repurchased \$400 million of common stock in the second half on top of the \$200 million we bought back so far this year, which would be consistent with the greater operating cash flow we typically generate in the second half. All of our guidance for fiscal 2025 translates to approximately \$14 per diluted share. This would result in a full year return of being return on beginning equity of approximately 18%, and we put our year-end book value per share at approximately \$90. We believe these results will once again reinforce the strength and resiliency of our business model as well as our ability to successfully navigate changing market

conditions while still delivering attractive returns to stockholders. Now let me turn it back to Doug.

Douglas Yearley: Thank you, Marty. Before I open it up for questions, I'd like to thank our Toll Brothers employees for their hard work in the first half of 2025. I am proud of your commitment to our customers and dedication to our business, which are key drivers to our long-term success. Now let's open it up to your questions. Jamie, we're ready to go.

Operator: [Operator Instructions]. And our first question comes from Stephen Kim from Evercore ISI. Please go ahead with your question.

Stephen Kim: Appreciate all the color as usual. My first question actually has a bit of a housekeeping element to it. We didn't see your spec data and your homes under completed and under construction information. So, I was wondering if you could kind of give us an update on where your specs stand, both completed as well as under construction? And my overarching question with respect to that is, you've talked about 11,500 closings, give or take. I'm kind of wondering, like how many units do you want to have under construction or completed at any point in time, given a run rate of about 11,000 closings? And where do we stand relative to that?

Douglas Yearley: So, I'll let Marty -- Steve, I'll let Marty give you the details on the spec count, and then I'll be happy to jump in and answer your question.

Marty Connor: Sure. So, Steve, we have just over 1,000 fully completed spec units right now. And we have a number...

Stephen Kim: Can we get a specific number, do you mind? Marty?

Marty Connor: 1,028. We have approximately 20...

Douglas Yearley: I just got a text from the field. We sold one, Marty.

Marty Connor: That is the number as of 430. 2,400 or so in progress, and we have permits available for another 1,000 or 2,000 behind those that we have not commenced construction on.

Douglas Yearley: Right. So, the 2,400 in progress means that we've issued a go to the field. And so, in progress could mean the survey crew is taking out the lot to anticipate a foundation going in. So, it goes all the way back to company's decision to go, but it could -- you may not visibly see anything on the site yet, but the permits in hand, and we're ready to go. So, it's a very broad definition. With respect, does that give you what you need?

Stephen Kim: Yes. Will follow cleanup later on, but sure that gets us close.

Marty Connor: I think the other aspect that may be along the lines of what you're looking for, this is about the highest concentration of work in progress and completed specs that we will have at any particular point in time during the year.

Douglas Yearley: So, you asked about our comfort level. We are comfortable with where we are in the spec business, we had gotten it up to 55% a few quarters ago. As you heard us say today, we are slowing the start of new specs. So many of those permits we talked about are sitting at permit without a go issue. And I think that is a smart way to run this business in the current environment. We are very pleased with how well we did in the second quarter in terms of the sale of specs without larger incentives. And one of the reasons we had a revenue beat in Q2 is because we call it same quarter, sell and sell right? So, it's not a spec we sold in a prior quarter to settle now, but how many cell and settles do we have intra-quarter. And we were very pleased in with that activity and that incentive levels that were manageable. And so, as we move forward, we continue to be very comfortable with Q3 and Q4 number of specs that we believe will sell and settle and we believe, based on current market conditions, we have conservatively budgeted incentives. Those incentives are consistent with what we achieved with our spec sales in Q2. And that's why we have comfort in the guide understanding that we have 1,000 completed spec homes that we intended to sell and sell. And then beyond that, of course, some of these homes in progress, many of these homes of progress would be ready to deliver by the end of October, the end of our fiscal year. We have projected that some of those will, in fact, sell over the next 5.5 months and settle, but there'll be another bunch of those that while they could settle by the end of Q4. We are not budgeting for that. We are conservatively assuming that they roll into 2026 and set up that year. But in terms of the incentive front, which I know is question out there. We've read it overnight. We're very comfortable with how we budgeted. Yes, there's more incentive needed to move spec right now in this market than build to order. We are very pleased with build-to-order margin. It actually is coming in higher than we have budgeted, particularly for the more luxury homes, the more expensive

homes. Those margins are coming in even higher. So, while the spec margin is a little bit lower, it all blends out to 27.25%, 27.5% as we did in this past quarter, and we are assuming no improvement in the market over the next 5.5 months to deliver the returns and the guidance that we have presented.

Operator: Our next question comes from John Lovallo from UBS. Please go ahead with your question.

John Lovallo: First one is, I mean, obviously, you did a really nice job managing the business. And as you talked about prioritizing price and margin over pace in the quarter. The third quarter gross margin outlook of 27% in the quarter implies pretty flat quarter-over-quarter margin in the fourth quarter. Just curious kind of what are the moving pieces impacting the second half gross margin. Any thoughts on sort of the sustainability of this into next year?

Douglas Yearley: Sure. So, it's a great question. Yes, you are right in your math that the fourth quarter margin, we expect to be about the same as the third quarter at \$272 million. While there will be some downward pressure because of the spec cell and settles, as I discussed, we have some tailwind on gross margin from mix. There's going to be more luxury delivering in the second half of the year, which is higher margin, and there's going to be more out of the Pacific and out of the Mid-Atlantic region, which both support higher gross margin. So, when you blend more spec that will have a bit -- we believe, a bit higher incentive with what I just described in the mix coming out of the Pacific and the Mid-Atlantic and more luxury nationwide. It all works out to the guidance we've given.

John Lovallo: Understood. And then you guys beat the top end of the delivery guide by about 200 homes. What drove the beat? Was this product mix, maybe a little bit more spec? Was it regional mix? And does it imply that you're incrementally less optimistic on the full year given the maintained outlook?

Marty Connor: I don't think it necessarily changes our optimism for the whole year. What we did in the second quarter is simply we outperformed by selling and settling more spec homes than we had projected, and we still had a gross margin beat. And I think that provides some evidence to the conservatism that we have in our guidance.

Operator: Our next question comes from Mike Dahl from RBC Capital Markets. Please go ahead with your question.

Mike Dahl: Just keep attacking the back half a little bit. I think when we look at it, historically, your point about the cadence being consistent. The flip side is, this is the first year that we can see looking back where your current backlog it didn't actually fully covering second half deliveries, meaning you need more deliveries in the second half than their current backlog. So, I know like Doug, Marty, you talked about you expect to sell and settle some of the completed some of the under progress. Can you just give us a little more granularity on that opportunity like of the number of homes in progress or complete what is obviously complete can close, what percentage of that 2,400 you think could actually settled by year-end? And then just given the lack of visibility on margins for homes that you have get sold, a little more detail on how that pet margin progressed through the quarter would help, I think.

Marty Connor: All right, Mike. So, we have roughly 6,400 units left to deliver this year to hit the 11,400 midpoint. Roughly 4,500 of them should deliver from our backlog. Remember, our backlog is 6,050 or so homes. So those homes are sold. We know the revenue. The build costs are contracted. So, we have limited risk on their cost growing or shrinking and we think we have adequate builder reserves in those cost estimates. So, let's take those 4,500 off the table. We have roughly 1,900 homes that will need to come from our spec inventory that haven't been sold yet. We told you -- actually 1,028 of them are completed. So there's no build cost risk there. The others are all under construction. In fact, more than the 900 we would need to sell and settle are under construction. So there's not much cost risk there because they're under contract for construction. So it's really the selling price of those 1,900 where there is some potential risk, and we believe we've accounted for that in this market based on recent comparable sales, a lot of which I just mentioned in the second quarter still allowed us to outperform our guidance for the second quarter. We sold and settled 250 to 300 more specs in the second quarter than we thought when we entered the quarter, and we beat gross margin still. So, I hope that helps give some comfort and understanding of what we foresee in the next six months.

Douglas Yearley: In those 900, we have 1,000 completed and then we need 900 more that are under construction. We have significantly more than the 900 that could deliver by October 31. So, we are not being aggressive in assuming that, oh boy, we need to sell and settle everything we're building to hit that number. There will be plenty that will be setting up 2026 that do not sell and settle by the end of

this fiscal year. It's also safe to assume that as we manage our spec production, where we have a green light for specs is probably where we're doing best.

Mike Dahl: Okay. That's perfect. Yes, very helpful. My follow-up question, maybe just on similar lines, you talked about the stronger margins on built-to-order luxury, presumably a lot of that is in your backlog. So, you talked about your backlog gross margin. Can you give us a sense of where your current backlog gross margin stands?

Marty Connor: I think that's inherent in the guidance we've given you.

Douglas Yearley: I mean the build-to-order business runs several hundred basis points above the midpoint, and the spec business runs several hundred below. Lately, that range has widened a little bit on both ends, but it still comes out in the middle. And that's why we like the business. I think we're doing a really good job of balancing our spec business with our build-to-order business. And remember, we don't hold spec off until the end where the client has no choice. We sell a lot of our spec earlier where the buyer can still go to our design studios, pick all the finishes that allow them to have a home that really fits their lifestyle and that design studio is highly accretive in margin to the Company's margin. So when we're able to sell a spec a bit earlier, even if it's incentivized a little more, there can be some residual margin left after they get to that design studio.

Operator: Our next question comes from Trevor Allinson from Wolfe Research. Please go ahead with your question.

Trevor Allinson: You talked about demand slowing throughout the quarter. I think that's not very surprising given what we've heard from other builders in the stock market volatility in April. So the question would be then, as we got into May here, the stock market obviously got a lot better. You had a pause on tariffs. Did you see demand get better as we went into May? And if so, could you put any numbers around that perhaps either relative to April or relative to 2Q, however you want to frame it?

Douglas Yearley: So it's very interesting. February was our first worst month. We sold 1.7 homes in the month of February, March and April were pretty consistent at 2.4 and 2.3 sales in those months in May is trending more like March and April now may seasonally have lower sales historically than March and April, but June and July, the next two months of this third quarter have better sales historically than May. So, we seem to be trending right now into May, consistent what we saw in March and April, which were better than February. I think we and all the other builders have explained it well. And we all know it. The market is softer than we had all anticipated back in January. There's a lot of good and understandable reasons for that with consumer confidence being down with macroeconomic volatility with the stock market moving around quite a bit. There are buyers on the sidelines. One of the reasons we are favoring pace over price is because, we believe this market is fairly inelastic and to throw more incentive at home sales, it's going to hurt your margin a lot more than is going to increase sales because the buyer is not responding over \$5,000, \$10,000, \$15,000, \$20,000 of more incentive, many of them just happen to be on the sidelines. But I am very pleased with the Company's performance through the second quarter and into the beginning of the third quarter, considering the macro environment out there. And I think it has to do with what we said earlier that over 70% of our business is move up and empty nester. Buyer is more affluent. We have 1/4 of our buyers paying all cash. Those go a mortgage are 70 LTV. They're moving up or they're moving down. They're moving on with their lives. They have equity in their homes. And so I think we're in a really good niche in the market, notwithstanding the fact that the market is a bit softer, but that's a long answer to your cadence of the quarter, but it we were surprised that February was worse, and we are -- May is where we thought it would be, which is consistent with what we've seen in March and April. June should be a bit better. July should be a bit better. We are not anticipating an improvement in this market in any of the guidance we are giving. And as I said, I think we have adequately and conservatively budgeted the incentives necessary for the sell and settle spec inventory we have.

Trevor Allinson: As a second question, I guess it would be more of a follow-up on that and kind of double-clicking on some of the comments you just made there because it sounds like your April trends were we're pretty different from what we've heard from some other builders, a lot of other builders have made it has suggested that April was much softer. So, do you think that is just purely for you guys, just a different profile for your consumer as you were just talking about? And then if that's the case, you mentioned earlier that you guys build across a pretty wide range of price points. Are you seeing big

differences here more recently in demand relative to what you were seeing earlier in the year across those price points?

Douglas Yearley: So, I apologize if I was misunderstood. Overall, the results are still softer than our expectations. I was comparing -- you asked for a cadence, and I was comparing March and April February. We are not happy with 2.4 and 2.3 sales per month in the March -- in the month of March and April. But that's the market. And so what others are describing. I think we would be consistent with that, but I just wanted to explain that we see February being best, March being next best and then April being the worst because of the cadence of what was going on with tariff conversations and macro issues. We sort of flattened out in March, and we stayed where we were. And so I just want you to understand that, that -- I want to put that perspective around it. It is a soft housing market. We all know it, and we're doing pretty well in that market. And I think we're managing the business extraordinarily well.

Operator: Our next question comes from Sam Reid from Wells Fargo. Please go ahead with your question.

Sam Reid: Wanted to drill down a bit on SG&A.; Just looking at the implied Q4 guide, the math would suggest some fairly nice leverage I did anywhere from 30 to 40 bps year-over-year, which is really great kind of on the back of a few deleverage quarter. So just talk to kind of what's driving that leverage? Just any nuances with regard to kind of your community openings, marketing spend, would just love some more perspective on kind of how you're going to exit the year on SG&A.;

Marty Connor: So, I think the biggest issue, Sam, is that we're going to have a lot more revenue. We're going to have 235 million more -- \$235 million more revenue than last year, and that's really what's driving a lot of the leverage.

Douglas Yearley: In Q4.

Marty Connor: In Q4, I'm talking about Q4. Yes. We are very focused on SG&A.; We're growing community count pretty significantly, particularly in that fourth quarter. And so there are pressures, but we've done a really nice job of managing costs. We're not immune from some of the inflationary pressures. I'll say, particularly on the health care front, it seems like something that's grown a little bit more than we'd like. but we're managing it very actively, and we have the flexibility to continue to manage it actively as the market evolves.

Douglas Yearley: And in addition to leverage, Sam, our variable sales costs component of SG&A; came down a little bit. It was a little bit below what we expected in this quarter. In this past quarter, which was a little bit of a tailwind for us.

Sam Reid: Yes, absolutely. No, that helps. And then maybe just switching gears here. I realize you guys are not offering up a '26 outlook today. You're probably knocking in for another let's call it, two quarters other than to say, it does sound like community count is going to be up year-over-year in 2026. I said, I wanted to maybe double-click a little bit on what delivery in 2026 could look like? And the basis for that is the backlog is a little smaller this year than it was last year. I would love to kind of get your sense as to sort of kind of what a good base case assumption for 2026 deliveries could be in the context of that backlog back?

Douglas Yearley: I appreciate you asking and trying to get us to give some guide on '26. We're not prepared to do that right now. That is usually the highlight of the December call. But I will -- with that, I will say that the average price of homes in '26 will be higher. That's obvious from the last couple of quarters of sales and where that average price is. We are focused and know we need a strong backlog heading into 2026. We will have a continuing spec strategy that we know is important. As we head into 2026, we will continue to be mindful of market conditions on a very local level as to where we start spec and where we are more cautious, but we are well aware and embrace the importance of our spec strategy. And we will have, as I said in my prepared comments, around 10% community count growth in 2026. So I'm not giving you any numbers, but I will give you a bit of that background and flavor.

Marty Connor: When we open communities, we often get kind of a boost to sales as there's some pent-up demand for those communities. And we can moderate that if we want or let it run if we want. So that's part of the strategy we would deploy to.

Operator: Our next question comes from Alan Ratner from Zelman & Associates. Please go ahead with your question.

Alan Ratner: Good morning nice quarter, and thanks for all the details. So, I'd love -- I appreciate the monthly cadence data, and I was hoping just to get a little bit more qualitative kind of commentary on, how do things progress for you guys with the moving pieces in your business, obviously, your buyer is probably more tied to the stock market volatility than other builders and April was obviously a very challenging month for the stock market. The last few weeks, the markets rebounded. And I'm just curious, it doesn't sound like your order date has necessarily picked up meaningfully. But have you seen any green shoots either in traffic or just kind of the commentary from your salespeople that the stabilization in the stock market is having any positive leading indicators on your buyer pool?

Douglas Yearley: Yes, Alan, it's modest. It's too early to tell. There's no question confidence, consumer confidence, I think it's the number one leading indicator at least for tolls business at the more affluent end, do rates matter, of course, they do. We celebrate a five, seven, eight, 30-year no-point mortgage, of course, we will. But a little tick in mortgage rate doesn't affect our client as much for the reasons we've talked about 25% all cash, those that get a mortgage are at 70%. We know a good part of the 30% of first-time buyers we sell to are getting some help from mom and dad with generational wealth transfer. And so that's going to take a mortgage payment down because they're probably getting able to put a bigger down payment on the house, thanks to mom and dad. So, while interest rates are important, you're right that the stock market overall confidence some positive news out of DC about resolving some of the tariff conflict, all of that matters, and it can matter in a big way. And we have significant under supply of homes in this country. We have terrific demographics that are a tailwind for future growth. And we've all seen it. I've been doing this 35 years. When this turns...

Marty Connor: Exactly 35.

Douglas Yearley: Thank you, Martin. I know it's my 60th call. I didn't know it was my 30-50 anniversary today. But we've all seen it. When this market turns with those tailwinds and with so many people on the sidelines just waiting to feel better so they can move on with their lives, look out because it's going to come. But I can't tell you in the last two, three, four weeks as the market -- the stock market has stabilized that we've seen anything definitive. There's just some modest conversations and color that we get out of sales, the traffic is up, the quality of traffic is up. We've had a few openings lately of new communities with significant interest at the opening. We've had a couple where we've gone back to best and final offer, where we let people bid up the five houses that we're offering because there's so much interest. That's the exception. I don't need that to be a headline right now. But we'll keep an eye on it. We're not heading into the spring season. We're heading into the summer. So, it's a little bit different time. It is a good time to sell finished spec. Because buyers want to get into their new home by the school year to not disrupt the kids. And so you need to buy a house in the next couple of months. to get that out to close by the end of August. And so -- and we have timed that appropriately. We're -- we know that you want to bring finish spec into the market at the right time when buyers want it, which is that generally the summer months. So we'll have to see, again, another long answer that, no, I don't see anything definitive yet, but I wouldn't be surprised if it comes if there's more stabilization in the macro market.

Alan Ratner: Got it. Appreciate the other commentary there. Second question, there's obviously a lot of headlines associated with immigration and what's going on there. And I was hoping you could just refresh my memory, what percentage of your buyers are far national, I guess, specifically kind of H1B Visa holders? And have you seen any changes in demand among that cohort of buyers year-to-date?

Douglas Yearley: It's less than 5% of for the first part of your question. And no, we haven't seen any change over the -- since the new year. The Chinese buyer in particular, and again, that may be a Chinese national, maybe Chinese American, but that buyer in particular, is still very strong for us in California.

Operator: Your next question comes from Alex Barron from Housing Research Center. Please go ahead with your question.

Alex Barron: Yes. I wanted to focus in on your comments about having more than enough expects to hit your numbers in the fourth quarter. I was kind of going back several years now. It looks like your deliveries have exceeded your orders by quite a bit as your backlog has been coming down from a peak of 11,700 or so to 5,000 now. So, can you explain that dynamic? I mean how many total homes, I

guess, are sort of not in the backlog that are under construction, I guess, back to help us kind of understand that dynamic a little bit better.

Marty Connor: Sure. Alex, I think over that period of time, you've seen us move from a 90% build-to-order business to a 50%, 55% spec business where we sit currently. So the backlog coming down is not unplanned. We opened the call mentioning that we had 1,028 completed specs that could be sold and settled in the next six months. We have another what was the number, 2,400 specs at various stages of construction. And so we will have more than enough completed specs by the end of the year. to deliver the roughly 900 additional sell and settle specs on top of 1,000 cell and settle specs to hit our delivery guidance factoring in roughly of 4,500 homes coming out of backlog as well.

Alex Barron: Got it. And then those...

Marty Connor: 2,000, we have another 2,000 pre-footing permits polled homes that we will begin production of a certain percentage of depending on how the market evolves.

Douglas Yearley: And that's the bucket that we have slowed and are making very local decisions on based on market conditions.

Alex Barron: Got it. And so when would you expect, I guess, your backlog to sort of hit bottom in a sense and start trending back up? Is it kind of towards the end of this year?

Douglas Yearley: Well, with the slowing of spec starts, I don't know if it's the end of the year exactly, but yes, there will be a point where you will -- you should see that go up. Again, it's all -- it's market conditions driven, right? But we have recently seen a bit of a move back towards a desire for build to order versus faster delivery of a spec home. And I think that's for a couple of reasons. When you have a bit of a softer market and higher rates, there are buyers that say, this is my dream home. I want to design it to exactly my taste. I want to be able to customize it. and I'm willing to wait. It may take me a little longer to sell my home. Maybe the rates come down when I have to lock in 60 days before the home is delivered. And I sort of like the idea and the comfort of this move occurring in 12 months to my Dream Home versus two, three, four months to spec inventory. And we are feeling a bit of that now, which we are encouraged by, frankly, because our special sauce is choice, and we talked about the higher margin in build to order. It's not a dramatic change, but we are beginning to see out in the field, a bit of a leaning preference towards the build-to-order versus the spec.

Operator: And our next question comes from Buck Horne from Raymond James. Please go ahead with your question.

Buck Horne: I wanted to add a little bit I want to ask a little bit about the land spend in the quarter. It seemed like it was one of the higher quarterly amounts you guys have spent in recent memory, added some additional loss. Was there any particular land deal or anything noticeable that kind of drove the surge? And should we have any other takeaways in terms of what does that mean about your confidence about the land market?

Marty Connor: Yes. So our land spend in the second quarter was \$362 million compared to \$360 million in the first quarter. So we have spent \$763 million for the full months. I think it may ratchet up in the back end of the year, but a lot of that depends on the timing of deals as they closed. There was nothing in particular in the second quarter that drove the number to be consistent with the first quarter.

Douglas Yearley: Yes. I think for us to move forward and close on the ground in this environment means it's still pencils. We may have been able to renegotiate price or take down terms. We're land banking more than we ever have, new deals coming in. I think we're at 40%, guys. Is that sort of number?

Marty Connor: Of the new -- the new deals.

Douglas Yearley: The new deals coming in are being land banks. But our comments about due to softer market conditions, we're being more cautious, and we expect land spend to probably come down to '26. I wouldn't read anything into the last few quarters or the next few quarters in terms of land spend because those deals are baked and they still work. And so we're moving forward maybe on the same terms or maybe on modified terms but it's really the next deal contracted for, which may have two or three years of entitlements ahead of it or it may have a closing in six months. It all depends on what the land deal is. But those are the ones that over time, at least at the moment, the land spend may come down a bit. But if this market improves, then that may also change and we may find ourselves buying more ground. But we're very happy to have the 80,000 plus or minus locks that we own and control.

We're very proud of moving more and more lots to the option category and that gives us great flexibility and conservatism when it comes to the next deal because our land bank is in such great shape.

Buck Horne: Got it. Got it. Very helpful clarification. And just with a little bit of timing. Can you just walk us through geographically how the markets were shaping up versus your expectations? Any standout surprises to you in terms of how things progressed during the quarter, either with economic sensitivity, either strength or downside or upside?

Douglas Yearley: Sure. So the better markets were New Jersey, Pennsylvania and New York. It did well, D.C. Metro, Charlotte and Atlanta. So that's just the Eastern Seaboard did well. out West, Las Vegas, Denver, Boise, Idaho did well and all of California did well. softer spots, Pacific Northwest, for us, that's Greater Seattle and Portland, Oregon, most of Florida, parts of Texas and Phoenix continue to be on the softer side of our business.

Operator: And ladies and gentlemen, with that, we'll be concluding today's question-and-answer session. At this point, I'd like to turn the floor back over to management for any closing remarks.

Douglas Yearley: Jamie, thank you very much. You've been terrific. Thanks, everybody, for your interest and support. We are always here to answer any follow-up questions you may have. Have a wonderful Memorial Day weekend and summer. And we'll see you soon. Thanks much. Take care.

Operator: And ladies and gentlemen, with that, we'll conclude today's conference call. We do thank you for attending today's presentation. You may now disconnect your lines.