

**LENNAR CORP**

**Moderator: Grace Santaella  
December 19, 2016  
11:00 am EST**

Coordinator: Welcome to the Lennar's Fourth Quarter Earnings Conference Call. At this time, all participants are in a listen-only mode. After the presentation, we will conduct a question-and-answer session. Today's conference is being recorded. If you have any objections, you may disconnect at this time.

I will now turn the call over to David Collins for the reading of the forward-looking statement.

David Collins: Thank you and good morning, everyone. Today's conference call may include forward-looking statements, including statements regarding Lennar's business, financial condition, results of operations, cash flows strategies and prospects. Forward-looking statements represent only Lennar's estimates on the date of this conference call and are not intended to give any assurance as to actual future results. Because forward-looking statements relate to matters that have not yet occurred, these statements are inherently subject to risks and uncertainties.

Many factors could affect future results and may cause Lennar's actual activities or results to differ materially from the activities and results

anticipated in forward-looking statements. These factors include those described in this morning's press release and our SEC filings, including those under the caption Risk Factors contained in Lennar's annual report on Form 10-K most recently filed with the SEC. Please note that Lennar assumes no obligation to update any forward-looking statements.

Coordinator: I would like to introduce your host, Mr. Stuart Miller, CEO. Sir, you may begin.

Stuart Miller: Great. Thank you and thank you, David. This morning I am joined by Bruce Gross, our Chief Financial Officer; Dave Collins, who you just heard from, Diane Bessette our Vice President and Treasurer, Rick Beckwitt our President; and Jeff Krasnoff, CEO of Rialto are all here with us, Jon Jaffe, our Chief Operating Officer is with us by phone from California and some of that group will be joining in our conversations during the Q&A period.

I am going to briefly give some remarks as I always do and Bruce is going to jump in and break down our financial detail and give some further guidance for next year as we always do at this time of year and then we'll open up to Q&A. As always, I'd like to request one question and one follow-up, so we can have as many participants as possible.

So let me go ahead and begin. Our fourth quarter and year-end results reflect our disciplined adherence to our company-wide strategies of managing our business to a clearly defined growth rate in order to run our business efficiently, while generating cash flow in order to fortify our balance sheet.

We grew our fourth quarter and full year 2016 earnings by 11% and 14% respectively, while we improved our balance sheet to a 33.4% homebuilding

net debt to total cap ratio, which is now back to our pre-downturn financial condition. We view that as quite an accomplishment.

Across our platform in each of our business segments, we improved performance and operations to position for the future and to make the overall company stronger. As we arrive at the close of 2016, we are better able to achieve our overall goal of reverting to a pure-play homebuilder with an excellent operating platform and a healthy capital structure that enables us to be both opportunistic and to ultimately return capital to shareholders in the future.

All of this was accomplished in the context of market conditions that were suboptimal in 2016, defined by overall slow, but directionally steady market improvement that was often choppy and sometimes complicated.

As we look ahead to 2017, we expect to see a generally similar economic environment to define the homebuilding landscape with some potential upside from the new administration in Washington. Our company strategies of soft pivot on land, 7% to 10% growth target and improved cash flow will remain the same for now and we expect to achieve similar growth and balance sheet improvements in 2017 as Bruce will detail in our guidance for the next year.

These expectations derive from the following general views. Even with the now clear upward momentum movement in interest rates mapped out by the Fed and the many questions around taxes in the regulatory environment raised by our incoming potentially business friendly new President, we expect to see continued slow but steady market improvement that can be choppy and erratic at times as the new administration goes to the throes of enacting an agenda of change, upside exist to this view if a general sense of optimism continues to dominate and changes happen quicker, we'll have to wait and see.

We continue to believe though that production levels in the \$1 million to \$1.2 million starts per year range are still too low for the needs of American household growth that is now normalizing. The rather large production deficit that has continued to grow over the past years should continue to drive overall growth in the housing market. Therefore we see the current levels of production forming somewhat of a downside or floor to the market.

Even with interest rates moving higher, the first time homebuyer will continue to come back to the market as stronger economic conditions should drive purchasers to the market undeterred by the marginally higher monthly payment, especially in the context of continued rent increases.

Lower unemployment, wage growth and general consumer confidence should drive household formation, which drives families to purchase homes and to rent apartments. We believe that there continues to be strong pent-up demand for dwellings of all types across the country, though stronger in some markets than in others and this demand will continue to propel a continued long cycle, slow and steady market improvement that will not be derailed by slow movements in interest rates.

This goes for both the first time and the move up purchasers. While demand has been constrained by limited access to mortgages, we feel that any relaxing of the hyper regulated banking system will normalize the mortgage market, which should enable more purchasers to find their way to home ownership.

We continue to expect that demand will build and come to the market over the next years and that will drive increased production as the deficit in housing stock ultimately needs to be replenished.

Nevertheless, availability of land and labor shortages continue to be limiting factors and constrain supply and restrict the ability to quickly respond to growing demand. We expect that these conditions will continue to result in a slow, steady though positive homebuilding market that will enable slow and steady growth throughout the industry.

These had been our consistent guiding views over the past year and we've mapped our operating strategy around these views through at this point we leave room for upside as we look ahead.

Each segment of our company has positioned itself for continued performance in 2017 and beyond and we believe - and we remain well positioned to execute our operating plans and strategies in each of our business segments going forward.

Against this backdrop, let me briefly discuss each of our operating segments. Our for-sale core homebuilding operations have operated a very high level of efficiency with a steady growth pace and a focus on operational excellence throughout 2016.

As we've noted in past conference calls, we've adjusted our for-sale housing strategy as the recovery has matured and land pricing has gotten more expensive on the retail side. We've noted three key components of our core homebuilding strategy. Number 1, soft pivot on land purchases; number 2, lower targeted growth rate and number 3, heavy focus on SG&A.

We've continued to reduce our combined land and land development spend and new orders in the fourth quarter and the full year grew at 9% while deliveries for the year were also up 9%. This is right on top of our targeted

growth rate and has enabled us to focus on reducing SG&A while driving cash flow.

We've reduced our SG&A throughout the year even while continued labor shortages, construction cost increases and land increases have tested our ability to match sales and delivery pace, our management team has managed sales prices, maximized margins and focused on SG&A in the fourth quarter to bring it to an 8.7% rate to offset pressure on gross margins and maintain a strong net margin, which came in at 14.6% for the quarter.

This was accomplished while we've also been increasing our spend on companywide technologies in order to realize additional reductions in the future. As we look ahead to 2017, we expect to continue to focus on these three pillars of our operating strategy in order to drive performance.

Our first of those pillars, we continue our soft pivot on land strategy as we are targeting high-quality "A" location land acquisition with a shorter two to three year average life. Additionally, we've focused on expanding our first time homebuyer offering organically with lower land costs as that segment of the market has continued to recover.

And finally, we've used the opportunistic, proposed purchase of WCI to fill in some blanks and partially offset land purchases, upgrading our land positions with already mature communities.

Second, we've noted in past quarterly conference calls given the now mature recovery that we will continue to manage our growth in order to concurrently grow the bottom line and drive strong cash flows. We continue to manage our growth targets to achieve a growth rate in the 7% to 10% range as we've

redirected our management efforts towards maximizing our net operating margin.

In the third prong with less pressure on top line growth rate, we've intensified management focus on driving faster bottom line growth and cash flow by maximizing pricing power and using innovative strategies to drive our SG&A down.

Under the company mantra, as I said last quarter of what we can measure, we can change, we are focused on changing and improving all elements of our operating platform. I noted the example in past quarters that we've been reducing customer acquisition costs through our digital marketing initiative.

We've expanded our focus to other operational elements of our business and are seeing reductions in expenses in those areas as well.

It is noteworthy that this quarter's SG&A of 8.7% is the lowest fourth quarter SG&A in our company's history and that follows last quarter's lowest third quarter SG&A.

Our homebuilding operations are truly becoming extremely efficient operating machines with demand growing steadily, land limited, labor tight and constrained mortgage availability, we believe that our three-pronged strategy for our homebuilding segment, positions us well for steady growth as well as the ability to use a strong balance sheet to act opportunistically.

Moving on, our financial services group has also had an outstanding year of accomplishment in 2016. While the financial services operations have grown alongside our core homebuilding business, we've also benefited from a strong,

though sometimes erratic refi market as well as from the expansion of retail opportunities in both our mortgage and title platforms.

While we expect refi opportunities to diminish as rates rise, the other sidecar opportunities have continued to expand our platform as we move through 2016 and that's reflected in our fourth quarter earnings of \$51.4 million versus \$33.8 last year.

Our strategy for 2017 for financial services continues to be to construct and maintain a fully self sufficient financial services platform that benefits from Lennar homebuilding business, but drives profitability from retail operations as well. Bruce oversees this operation and will discuss it further in his comments.

Next our multifamily program LMC Lennar Multifamily Communities, really matured in 2016 into a leading blue-chip developer of apartment communities across the country. LMC had an incredible quarter in our fourth quarter.

Earnings totaled \$41.4 million up 306% from the \$10.2 million in 2015. During the fourth quarter, we sold four of our merchant build apartment communities all with high IRRs and two plus multiples. During the fourth quarter, we started 1,155 apartment homes in five communities with a total development cost of approximately \$469 million.

As of November 30, 2016, we had a geographically diversified pipeline of 74 communities, totaling almost 23,000 apartment homes with a total development cost of approximately \$7.7 billion.

Also during the fourth quarter, we had the final close of our now \$2.2 billion Lennar Multifamily Venture, we call LMV. LMV represents the largest equity

capital raise ever completed in the multifamily industry and demonstrates the confidence venture investors have placed in LMC and our new build-to-core strategy that will allow us to maintain an ownership interest in a portfolio of income producing communities going forward.

We continue to see growing demand in housing, both in our core homebuilding business as well as our multifamily platform and this venture is a key building block for one of our growing ancillary businesses.

Next, our Rialto segment saw a nice turnaround in the back half of 2016 as the capital markets stabilized after a rough start in the first half of the year.

During the quarter, market conditions continued to improve, particularly for RMF Rialto Mortgage Finance, which has maintained its position as one of the largest non-bank CMBS originators.

RMF completed its 32nd through 35th securitization transaction during the quarter selling over \$622 million of RMF originated loans with very healthy net margins. This brings our total to over \$6.5 billion of securitized loans since RMF's inception.

On the investment management front, we also previously announced first quarter closings of commitments for our third fund. This fund will complement our other opportunistic funds with readily available capital to invest.

Our first two flagship opportunity funds have continued to be top quartile producers. Fund one as an example became fully invested in early 2013 and we've now distributed the 141% of investor's original capital from income and monetizations and with the distribution through this quarter, Rialto has now realized two times its original investment with a lot more to go.

Fund two made its final investment during the first quarter, investing including recycling over \$1.6 billion of equity in 100 transactions and similar to fund one, we've been making distributions already returning about 36% of investor's original commitments.

Rialto's investment in asset management platform had been growing its asset base as well as harvesting value for investors and us. In a little over six years, we've now raised almost \$7 billion of equity in a variety of real estate funds and investment vehicles, we've invested about \$6.1 billion of equity and we've already returned \$4.8 billion to investors who have earned almost \$2.4 billion over the years.

Overall, our Rialto platform enables us to invest across all real estate and financial products and as we look ahead to 2017, Rialto earnings will continue to grow as we work through our remaining legacy assets and refine our businesses into a two-pronged capital-light segment, focused solely on RMF Rialto Mortgage Finance and the investment management business as well.

Finally, FivePoint is now a self-sufficient standalone company that's a premier strategic large scale community builder in California. In 2016, we successfully contributed and exchanged our interest in three strategic joint ventures and our interest in the management company for an investment in this newly formed entity called FivePoint Holdings LLC.

This transaction liberated FivePoint in 2016 to start acting independently to raise capital and to use its pristine balance sheet to operate opportunistically. It also positioned FivePoint to take advantage of either a recovered IPO market should that happen or other opportunities as they arise. We simply

could not be more excited about the long-term prospects for this one of a kind leader in community development.

So overall and in conclusion let me say 2016 was a great strategic year for the company and it sets up another year of consistent performance and opportunity. We feel very confident that our view of the market and the strategies that we've successfully implemented in our business have worked very well to position us for continued performance and future growth in 2017 and beyond.

So now let me turn over to Bruce.

**Bruce Gross:** Thanks, Stuart and good morning. I'll provide some additional color on our 11% earnings increase over the prior year.

Revenues from home sales increased 11% in the fourth quarter, driven by an 8% increase in wholly-owned deliveries and a 3% year-over-year increase in average selling price to \$357,000.

Our gross margin on home sales in the fourth quarter was 23.3%, which was in line with our stated goals. The prior year's gross margin percentage was 24.6%. The gross margin decline year-over-year was due primarily to increased land costs and construction costs.

Sales incentives were 6.2% this quarter compared to 5.9% in the prior year. The slight increase was primarily due to our focus on reducing completed unsold homes, which we managed to decrease by 13% year-over-year to 975 homes.

Gross margin percentages were once again highest in the East region and our direct construction cost increases have moderated compared to the prior year. These costs were up 3% year-over-year to approximately \$54 per square foot and this was driven entirely by the labor side, which was offset just slightly by a small decrease in material costs.

Our SG&A percentage improved 50 basis points as Stuart mentioned to 8.7% in the fourth quarter. About 30 basis points of that improvement was attributable to operating leverage from growing volume organically in our existing homebuilding divisions and the other 20 basis points was due to improvement and advertising costs, which we reduced as a result of our focus on digital marketing.

Gross profits on land sales during the quarter were \$24.3 million and that was primarily driven by 3 million transactions during the quarter versus 7.9 million in the prior year.

Equity and loss from unconsolidated entities was \$24.6 million, which included our share of net operating losses from the newly created FivePoint entity. We opened 66 new communities during the fourth quarter to end the quarter with 695 active communities.

New home orders increased 9% and the new order dollar value increased 12% for the quarter. Our sales pace was higher during the quarter to 3.2 sales per community, per month, versus 3.0 in the prior year and the cancellation rate was 18%.

During the quarter, we purchased approximately 4,500 home sites, totaling \$250 million and this is the same dollar amount that we purchased in the prior year's quarter. These numbers align with what Stuart highlighted about our

soft pivot strategy, where we're focused on buying shorter duration land while continuing to grow the company.

The number of years of land owned has now been reduced to 4.8 years. Our home sites owned and controlled now total 159,000 home sites of which 33,000 are controlled. Our financial services business segment had strong results with operating earnings of \$51.4 million compared to \$33.8 million in the prior year.

Mortgage pretax income increased to \$36.6 million from \$25.9 million in the prior year. The improved earnings were driven by an increased profit per loan due to the favorable interest rate environment and higher volumes. Mortgage originations increased to \$2.7 billion compared to \$2.4 billion in the prior-year and we captured 81% of Lennar homebuyers.

As a result of a focused effort to capitalize on the low mortgage rates in the fourth quarter, we achieved a 72% increase in refinance origination volume versus the prior year. Refinance volume was 15% of the total origination volume, but the strong refinance market also drove higher margins per loan.

Our title company's profit increased to \$14.9 million in the quarter from \$8 million in the prior year and this was primarily due to higher refinance transaction volume and the focus on operational efficiencies.

Providing a little bit more color on Rialto segment, the produced operating earnings of \$8 million compared to \$7.6 million in the prior year. Both amounts are net of non-controlling interests. The investment management business contributed \$33.1 million of earnings, which included \$4.6 million of equity and earnings from the real estate funds and \$28.5 million of management fees and other.

At quarter end, the undistributed hypothetical carried interest for Rialto real estate funds one and two, now totals \$141 million. Rialto Mortgage Finance contributed \$622 million of commercial loans into four securitizations resulting in earnings of \$35.6 million compared with \$854 million and \$15.8 million in the prior year respectively, before their G&A expenses.

The increase in earnings was primarily due to an increase in average net margins of the securitizations from 2.2% in the prior year to 5.8% in the fourth quarter. The direct investments in Rialto had a loss of \$10.7 million in the quarter and Rialto's G&A and other expenses were \$43.3 million for the quarter and interest expense excluding the warehouse lines was \$6.7 million. Rialto also ended the quarter with a strong liquidity position with \$149 million of cash.

Adding to Stuart's comments on multifamily, the \$41.4 million operating profit in the quarter was driven primarily by the segment's \$47.2 million share of gains from the sale of four operating properties as well as management fee income, partially offset by G&A expenses.

We ended the quarter with five completed and operating properties and 38 under construction, 13 of which are in lease up, totaling over 11,000 apartments with a total development cost of approximately \$3.4 billion, so you could see the pipelines for the sales that we're going to talk about for 2017.

Our tax rate for the quarter was 32.5%. The rate is lower than our previous guidance, primarily as a result of the tax department's continuing efforts to maximize new home energy efficiency credit, which is currently set to expire

at the end of 2016. As a result of the expiration of this credit, we expect the tax rate for 2017 to be approximately 34%.

Turning to the balance sheet, the matching of the operating strategies with our execution has returned our balance sheet to the very healthy levels that existed before the downturn. We highlighted that the soft pivot strategy, strong profitability and the conversion of our converts will drive the path to lower leverage.

The result was an 880 basis point decline in net debt to total cap, going from 42.2% at the end of the prior year to 33.4% at this year end. This year we generated between \$400 million and \$500 million of operating cash flow in 2016. Our liquidity strength provides exceptional financial flexibility with now over \$1 billion of cash and no borrowings on our \$1.8 billion revolving credit facility.

Our balance sheet is rock solid and it's positioning us well for tomorrow's opportunities. Additionally, stockholders equity now exceeds \$7 billion and our book value per share increased to \$29.96 per share.

During the quarter, we converted the remaining \$157 million of our 3.25% convertible senior notes. Next step for the balance sheet will be continued focus on cash flow generation and retiring the \$400 million of 12.25% debt on June 1, which currently cost us approximately \$50 million of interest per year.

Now I would like to provide some goals for 2017. Please note these goals exclude the benefit from the WCI acquisition, which we will update in our first quarter conference call assuming the transaction closes as expected in our first quarter.

We still expect the transaction to be accretive to our fiscal 2017 numbers, excluding transaction costs. Number one: deliveries, we are currently geared up to deliver between 28,500 and 29,000 deliveries for 2017. We expect the backlog conversion ratio to be approximately 70% for the first quarter, between 80% and 85% for the second and third quarters and over 90% for the fourth quarter.

We are expecting an average sales price between \$365,000 and \$370,000 for the full year. We expect operating margins to be around 13% for the full year. The full year gross margin is expected to be in the range of 22% to 22.5%. We expect continuing improvement in the SG&A line from operating leverage and our investments in technology, reducing SG&A to somewhere between 9.1% and 9.3% for the full year.

There will be seasonality between the quarters with the first quarter being the lowest operating margin and the operating leverage is expected primarily in the second half of the year to match up with our highest volume quarters.

Financial services are expected to be in the range of \$155 million to \$160 million for the year. The quarterly amounts are expected to be spread fairly similar to 2016 with the first quarter anticipated to be the lowest quarter of profitability.

With rising interest rates, we expect the strong refinance market that we did see in 2016 to start to slow down as we go through 2017. Rialto is expected to generate a range of profits between \$45 million and \$55 million for the year and the second half of the year is expected to have the bulk of the profitability for this segment.

Multifamily expects to sell seven to eight multifamily communities in 2017 with a range of profits between \$70 million and \$80 million for the full year. We expect to be profitable each quarter with the fourth quarter profits similar to 2016's very strong fourth quarter.

The category of joint ventures, land sales and other income grouped together, we're expecting to have a range of \$70 million to \$80 million of profitability for this category and although we don't anticipate profitability in the first two quarters of the year out of this grouping, we do expect strong profitability in the second half of the year.

Corporate G&A is expected to be between 2.2% and 2.3% of total company revenues as we continue to invest and re-piping our systems and technology initiatives. As I mentioned our tax rate for 2017 should be approximately 34% and our net community count is expected to increase approximately 7% from our ending count of 695 with the increased spread throughout the year primarily in the second, third, and fourth quarters.

And then finally we continue to focus on cash flow generation and expect to generate a similar level of operating cash flow in 2017 as we did in 2016. With these goals in mind we are well-positioned to deliver another strong profitable year in 2017.

With that let me turn it back to the operator and open it up for questions.

Coordinator: Yes. Thank you. We will now begin the question-and-answer session. If you would like to ask a question, please press star followed by the number 1 and record your name at the prompt. To cancel your request, press star 2. Once again, please press star 1 to ask a question. And our first question is from Ivy Zelman of Zelman & Associates. Your line is now open.

Ivy Zelman: Thank you. Congratulations, guys, on another solid quarter. Stuart, if you can talk a little bit about the usage of free cash flow that's very impressive in '17 and how to increase shareholder value with that free cash flow where it gets deployed and thinking about the uncertainties, but, you know, as you've mentioned in your opening remarks, the positive potential business environment that we may or pro-business administration may be taking, thinking about the, you know, opportunities that you think will, you know, the pluses or minuses of the new administration at least what you've heard so far.

I think people are pretty interested if you go into little bit more specific obviously tax reforms, some of the things that might drive how you invest that free cash flow to drive shareholder value?

Stuart Miller: Okay. So, you know, that was a multipart question, Ivy. I'm going to give you credit for the two point questions and your follow up on that. So to start off with, you asked about free cash flow and how we might think to deploy that to enhance shareholder value and, you know, let me say hats off to Rick as he aptly negotiated our proposed deal with WCI.

He injected great deal of optionality for us in the way that we think about the use of cash versus stock and we do have optionality all the way for quite some time until closing.

And so we're thinking about the way that we use cash to enhance shareholder value in all transactions whether it's the purchase of new land, whether it's other deals that we are considering opportunistically or whether it's the way that we use cash and stock.

And we'll keep a lot of optionality injected in our program so that we can watch as the world around us given the new administration starts to really unfold. So we're very keenly considering how we think about the use of cash. We've injected lot of optionality and you can expect that that's going to be a primary focus for our corporate office.

So that was part one. You asked about some of the discussion points and administrative changes that might come along with a new administration. We've been giving a lot of thought to that.

There are some murkier waters, some questions around tax rate reductions and how they might ripple through, how they might result in cash savings. I think we're going to have to wait and see what the details are but as the landscape shifts, as a tax policy that has been articulated actually get formed, there are going to be some change agents in the way that customers think about whether or not they want to purchase or whether or not they have the capital to deploy.

We think that the tax changes are going to have some significant impact not just to the individual or potential customers, but also to our corporate tax rate in the way that we kind of configure our organization.

Corporate taxes as articulated are likely to go down, but what other elements of the tax code might change at the same time is something that we're going to have to say on top of.

Around the regulatory environment, there's a whole host of regulatory constraint that has defined the housing market not the least of which is the way the banks have been not only regulated, but also prosecuted has certainly shifted the landscape for the mortgage industry or defined the landscape for the mortgage industry.

What seems to be lightning of that regulatory or prosecutorial environment would in my opinion result in more normalization of the mortgage market and therefore greater access to the mortgage market by the lower middle class, which I think would be healthy not only for the housing industry, but also for the economy in general and I think we've been saying that for a long time.

All of these pieces as we see new administration come and as we see that confidence has been lifted, we'll see how that ripples through the selling season and how consistent it stays.

All of these provide opportunities for us to look opportunistically about as to how we deploy our cash and how we think about cash flow turning into the building of shareholder value. So I hope that answers the question.

Ivy Zelman: It did. And my follow-up, would just be thank you, it was helpful, just the word you mentioned becoming a pure play homebuilder, can you elaborate on what that means and is there any other businesses...

Stuart Miller: Yes. Listen, we've said in past conference calls that our focus had shifted last year to saying, "Okay, how do we position our ancillary businesses to bring them to where they ought to be?" The goal for the company is to be a pure play homebuilder.

Whether that includes our apartment effort or not is something that we're considering openly, that it might be inclusive of our multifamily program. So we hold that open to see how we think about it in the future, but clearly we've been focused on FivePoint and Rialto maturing and positioning those companies for, you know, other forms of ownership.

We've articulated that FivePoint, so we've looked at an IPO opportunity, the IPO market closed up on us and we're looking at other strategic opportunities. We've really refined the ownership structure for FivePoint, so that it's positioned and ready to go, should the right opportunity come along and we're focused on that and looking for that.

Likewise with Rialto, 2016 and continuing into 2017 as we resolve the legacy component of our asset base really refines Rialto to become a self-sufficient operation a lot like FivePoint already is and positions it to find its way into some different form of ownership.

As we resolve these ancillary businesses, we really clarify our position as a pure play homebuilder defined by our core homebuilding business, financial services which is a sidecar program and potentially by our multifamily group also.

But as you can see with this year's performance on the multifamily side, we've really positioned that entity to also have a lot of optionality and what we do with it because this is becoming a very valuable enterprise for the company and quite compatible with our core for-sale business.

Ivy Zelman: Great. That's very helpful. And congratulations again and happy holidays to all you guys.

Stuart Miller: Thank you.

Coordinator: Thank you. And our next question is from Stephen East of Wells Fargo. Your line is now open.

Stephen East: Thank you. Thank you, Stuart, for that explanation on your ancillary businesses. It saves me some questions there. So I'll go back to the gross margin that you all talked about 22% to 22.5%, as you look at 2017, you know, what are the moving parts in driving that down?

Is land still the biggest driver or do you see labor and materials and incentives moving up there? And then just an idea of where you all think it will bottom and roughly when you think that would occur?

Rick Beckwitt: Yes. Stephen, it's Rick. As we said the past, land is certainly one of the drivers that affects the gross margin. We benefited from some opportunistic purchases. We're now more of a wholesale buyer of land that's affecting margin and we think that in that 22% to 22.5% range, that's a solid margin and it's - as you know, it's much higher than where the rest of the industry is.

Another thing that's impacting that is our continuing shift towards the lower price market that those had lower gross margins but higher IRRs and that gets into to the overall strategy that we have as a company.

Where the bottom is, I don't think it's much lower than where we are in the 22% side, you know, and we're just going to have to see as that, that comes across. If you look at prior cycles for the industry, you know, somewhere in that 21% to 21.5% range has always been considered a pretty solid gross margin and we feel that operationally, we should be able to do better than that.

Stephen East: Okay.

Stuart Miller: Just add to that, let me say that look, you know, there's some upside to the world as we think about it right now. I think in a lot of ways, supply remains fairly constrained. As I noted in my comments, you know, the land and the

labor markets are constraining factors in terms of how quickly the building industry can really respond.

Increases in demand would give a little bit of pricing power. So, you know, there are lot of moving parts right now and a lot to consider. I think we'll have to wait and see. And Jon, do you want to comment at all on construction costs?

Jon Jaffe: Sure. As has been mentioned already, there's real constraint in labor market, but I think that operationally we been very effective in managing that. As Bruce said it's up about 2% year-over-year for our single-family detached product and that's really come from a focus on our relationships with our trade partners with a real intensity towards programs such as job site readiness and evenflow and as always our Everything's Included strategy really helps us in a labor constrained market be simpler and more efficient to build.

And we also see that in our cycle times as evidenced, it's come down consecutively from our second quarter to our third and now to our fourth quarter. We see reduction in a number of days of cycle time. So there's real pressure but I'm very proud of the way our management team is on top of that as a daily focus.

Stephen East: All right. Thanks. I appreciate that. And I did actually have one question on the ancillary businesses, on the four buildings that you sold, were the cap rate spreads between construction and what you sold them for, what you expected?

Are you seeing any change in the market? I know, you know, that the closer end A-plus luxury locations seem to be getting a bit fuller but you all are aren't there. So I'm wondering if, you know, you're seeing any change in the

profitability of these buildings as you sell them versus what you pro forma'd at?

Rick Beckwitt: Steve, it's Rick again. We were very strategic when we identified where we're going to roll out this program. And as we look at last quarter or even for last year, our underwriting has stood tall and, you know, we're having 2 plus cash-on-cash multiples. We've got high double-digit IRRs. We're just knocking it out of the park.

Stephen East: That's all right. Thank you.

Stuart Miller: Steve, if your question, are cap rates starting to move?

Stephen East: Yes.

Stuart Miller: Yes, so I think - I don't think we've seen much movement in cap rate yet and whether there's going to be as interest rates go up, there are a lot of arguments around cap rates relative to the apartment world.

We continue to have the view that, you know, the shortage in dwellings both rental and for-sale across the country that has been the result of the underproduction over the past years is going to continue to reflect in a fairly strong rental market, which makes this asset class very desirable.

We've seen this as Rick's gone out and raised the capital for this build-to-core fund that we have in place. We've continued to see that internationally, there is still a sizable demand for this asset class and while there will be some ebb and flow as certain portfolios of buyers get a little bit more full, or fully loaded in this asset class, we'll see a little ebb and flow in some of those cap rates.

I think directionally we're still going to see a fairly strong cap rate relative to the sale of these kinds of properties and their valuation.

Rick Beckwitt: And I guess that other detail I give you Steve is if you look at our portfolio, as Bruce said, we've got 74 communities in total. Forty of those in merchant build and balance 34 are in our fund as of today. So given if cap rates do moderate, we've got the ability to milk the asset through the income-producing nature of the fund and that was our strategic decision to have a dual prong strategy.

I think that we're really well positioned to maximize this and as the market recovers, if the market softens and then recovers in the future, we're going to have this portfolio of, you know, two, three, four year old properties that we can certainly monetize at that point.

Stephen East: I got you. Okay. Thank you.

Coordinator: Thank you. And our next question is from Michael Rehaut of JPMorgan. Your line is now open.

Mike Rehaut: Thanks. Good morning, everyone and nice quarter again. First question I was hoping to hit on some of the more recent sales trends that you've seen let's say over the last six weeks if it's at all possible to common, you know, obviously with the rate movement not being as dramatic as in short of a time what we saw in 2013, but we have had six weeks now of a rate move that's kind of totaled up at around 80 basis points.

So I was hoping to get a little sense of, you know, number one how, how the order growth cadence occurred during 4Q and again as you think about

November into the first half of December, if you've seen any difference in at least in terms of the year-over-year obviously seasonality wise, it's a softer period but, you know, from year-over-year or sequential period, if things seem a little different than what you would expect.

Rick Beckwitt: Yes. Michael, it's Rick. You know, we generally don't talk about anything post quarter with regard to sales. What we can tell you is that as you look at our Q4, each month showed year-over-year increases with an increase throughout the quarter in percentage of year-over-year change.

Mike Rehaut: And would that be for total order growth or sales pace when you refer to the...

Rick Beckwitt: That would be for total order growth.

Mike Rehaut: Okay. And, you know, I appreciate that Rick and, you know, I guess just secondarily, when you think about the first time business and you kind of alluded to the fact that that can also or perhaps is having an impact on the direction of gross margins in '17 perhaps even further out than that.

I was hoping if you could just remind us of what your first time business was as a percent of, you know, closings let's say in the fourth quarter, how that compares to the full year and where you might see that go over the next - over the next 12 or 24 months.

Rick Beckwitt: We've been running in the high 30s from a percentage basis. If you look at the land that we've been contracting and we've certainly made a shift on that, and you can expect that percentage to go up over the next year or two years.

Bruce Gross: To about 40%. That's where we expect to be going forward.

Stuart Miller: It's more of a historical norm too. Yes.

Mike Rehaut: So, you know, it's high 30s to 40 doesn't seem too aggressive of a shift that, you know, can go to 45. Just given the increased focus and as you talk about it, you know, I would expect something little bit more. Is there anything that's constraining that because obviously it's something that you know, I think, you know, a lot of the industry is moving towards.

Stuart Miller: Yes. Well, you know, we've never been one to follow the herd. We've been more kind of self-determined. We have a strong view that the product offerings that we have right now are pretty strong and while we are shifting back towards kind of a historical norm of where we think the percentages of first-time home buyer product that would like to have, we don't feel that, you know, with interest rates moving up, with the market, you know, still defining itself, we have the option to accelerate that pace if we want to. But we didn't feel that it was the right time to make a more dramatic shift. Rick.

Rick Beckwitt: And I think the other thing is that all this is definitional. You know, on the edges we feel that there's still a good strong market in that lower-priced first time moved up market, which is a big component of our - of our offering, product offering across U.S. So it's where you draw that line with regard to ASP.

Mike Rehaut: No it's fair points and worthwhile to be stated, so I appreciate the additional color. Thanks a lot guys.

Jon Jaffe: One more point on that, this is Jon, that we also have our Next Gen strategy, which as Stuart said is more of a leadership position than a following position, which represents about 6% of our total sales and the average sales price of our

next gen product offering is up 35% higher than our average sales price inclusive of that Next Gen pricing.

So we do have different strategies that we think balance our offerings into the marketplace as appropriate.

Mike Rehaut: Okay. Thank you.

Coordinator: Thank you and our next question is from Jade Rahmani of KBW. Your line is now open.

Jade Rahmani: Thanks for taking my question. Just on the WCI acquisition, I was wondering if you could say at this point based on what you see it had whether your intention is to keep the company's overall net leverage neutral as you look at that deal?

Stuart Miller: Jade as I said earlier, we've really maintained maximum optionality there. You know, we have a number of moving parts, number of things that we consider and are considering and so we're going to maintain that optionality and really not give additional color at this point just because we are considering other opportunities that are out there that we think, you know, compete for cash and balance sheet.

And I think as you've seen us do before, we'll allocate capital in the direction where we think we can have the greatest impact on shareholder value over the long-term. So that's kind of where we would like to leave the answer to that right now.

Jade Rahmani: On the Rialto side, can you say whether you think the current M&A environment remains fruitful in terms of opportunities to grow the platform

and whether any rollback of the Dodd Frank risk retention, you know, would have a negative impact on Rialto's business?

Stuart Miller: You know, our general view is that regardless of which way things go, relative to current regulation and some of our initial thinking around how the regulatory environment would benefit us, we're kind of positioned for prosperity, regardless of which way it goes.

Think about a rising interest rate environment relative to our conduit business, our loan origination business, our B-Piece buying business, all of these arenas tend to be activated by changes in the environment. We think there's still a very strong case to be made for the dollars that we're investing and whether risk retention remains in place defines a new environment that we will help craft or whether we revert to the way things have been working in the past, we're just very well positioned to continue with a very strong strategy of producing outsized returns.

Jade Rahmani: Thanks very much.

Stuart Miller: You bet. Next question.

Coordinator: Thank you, yes. Next question is from John Lovallo of Bank of America. Your line is now open.

John Lovallo: Hey, guys. Thanks for taking my call. First question is on the homebuilding operating profit, if you just look at the low-end of the outlook that you guys put out there, it would seem to imply, you know, call, you know, very low single-digit growth in operating income.

So I guess the question is, you know, is there - you know, what kind of macro environment are you thinking about when you put that out there and also, you know, are there additional levers on the SG&A line that you might be able to pull understanding that you guys have hit all-time lows of the past few quarters.

Bruce Gross: Okay. John as far as the macro environment, we're not assuming a very different macro environment from what you're seeing now. The reduction in gross margin is consistent with what we've been saying that some of the opportunistic land positions that we purchased, you know, they're just not as large of a percentage of those as we go forward.

And therefore, the land cost is going up a little bit and construction costs have gone up a little bit. So not a different macro environment and SG&A levers, there's a lot of focus that we have is we're re-piping all of the technology in our company and restore the benefit through digital marketing of how we've reduced advertising costs.

We think there's an opportunity to continue to make progress really on all the line items that we have with our fixed marketing costs as well as continuing to grow organically will continue to lever the overhead in our divisions because we're not growing our divisions at the same pace that we're growing our overall volume.

Stuart Miller: Let me just add to it. I wanted to be very clear in my opening remarks. We're really looking at a steady-state environment as we craft our strategy going forward. But we think that there are some unique upside potentials out there and I've tried to articulate some of those.

But the way that we're thinking about both our guidance and the way that we're crafting the strategy within the company, you know, we've seen a lot of choppiness in the economic environment over the past quarters that we've and other builders have had to navigate.

There are constraints on land. There are constraints on labor. So we recognize that the environment we have to look at is one that's consistent with where we are, but we think that there's opportunity for upside and that's kind of how we've positioned the company.

John Lovallo: Okay. That's helpful. I guess the next question would be, you know, talking about the land and labor constraints, it sounded if I heard this correctly, you're looking for 7% community count growth and I think you said that's excluding WCI. If that is the case, I mean, you know, what do you guys, you know, attributing the ability to deliver that kind of community count growth to, you know, given the aforementioned headwinds.

Bruce Gross: That's excluding WCI, so 7% although, you know, as Stuart mentioned in his remarks, there is the opportunity that some of the WCI assets might replace some of the assets we were looking to bring online.

Stuart Miller: Yes. You know, as we sit right now, it's a kind of complicated time for us to knit these pieces together because WCI as with any transaction that hasn't closed is a proposed transaction. But the WCI acquisition as it occurs and we believe it will, will knit together with some of these numbers and there won't be a clear distinction between them because some of the WCI communities are going to potentially replace communities that we might have purchased otherwise.

Remember we're purchasing excellent communities that are already mature and underway and that's very attractive to us and our platform. So this will all dovetail into a narrative that will take greater shape after a closing.

John Lovallo: Okay. Thank you, guys.

Stuart Miller: You bet.

Coordinator: Thank you. Next question is from Stephen Kim of Evercore. Your line is now open.

Trey Morrish: Hi guys, this is actually Trey Morrish on for Steve Kim. Thanks for taking the questions. First could you talk about these new operating losses that are occurring in FivePoint and how long you're expecting those to continue to persist?

Bruce Gross: Yes. This is Bruce. So really when you look at FivePoint and all the joint ventures, they have overhead associated with them each quarter, that would result in a net operating loss unless there was a transaction of a land sale. So it's really then continuing to operate their business and it's a question of what quarter the land sales occur and they tend to bunch up.

So my commentary about the quarters and the net operating losses is that the sales anticipated from the joint ventures are bunched up later in the year which means the overhead in the beginning of the year won't to be offset by any significant land sale transactions.

Stuart Miller: And that's one of the problems that we've identified relative to both Rialto and to FivePoint is that the revenues tend to be less predictable and sometimes lumpy, which really brings some confusion to the overall program wherein

our homebuilding business we're able to give much greater guidance and it is much more consistently matched.

Those two subsidiaries tend to have lumpier results and can sometimes bring a little confusion.

Trey Morrish: Got you. Thanks for that. And then secondly, you gave your land spend in acquisition, but one what was your development and two, how are you thinking about going forward, you know, given the comments of your cash flow guide for relatively flat with this year which implies, you know, higher working capital, so maybe, you know, increased, you know, dollars in land spend next year.

Bruce Gross: So we actually had a reduction on our development spend during the quarter. Last year, it was \$266 million. This year's fourth quarter was \$240 million. So overall, you know, when you look at land and land development together, even though we're growing the company, we actually spent less in total this year versus last year.

And as we look at the positive cash flow generation for next year, that's just an estimate at this point. We're very focused on continuing the progress that we made this year and we'll continue to give you updates throughout the year, but our focus is continuing to improve the balance sheet and we'll remain opportunistic with what we do with that cash.

Trey Morrish: All right. Thanks, guys. Appreciate it.

Stuart Miller: You're welcome.

Coordinator: Thank you. Our next question is from Nishu Sood of Deutsche Bank. Your line is now open.

Nishu Sood: Thank you. Wanted to ask you about the labor issue. So earlier, you know, last year and, you know, earlier this year when those problems were creeping up, but obviously expressed itself as rising direct construction costs and some delays in cycle times. Now both of those have come back, you know, the construction cost I think Bruce said were only up by 3% year-over-year down I think pretty nicely from where it was earlier.

And I think John mentioned the cycle time is coming down as well. So should we think about that as being solely the results, of you know, obviously your intense efforts to manage around that or are you seeing also some improvement in the market and, you know, your thoughts looking ahead on that issue as well that would be great, thank you.

Jon Jaffe: This is Jon. We're seeing that there is pretty consistent level of constraint in labor in all the markets across the country. I think that our management team has done a particularly good job of focusing on the relationships with those trades to make sure that we're the builder of choice and it takes a lot of effort and focus and I think we're executing very well on that front.

Nishu Sood: Got it. So it sounds like mostly just the result of efforts. Okay and on the SG&A side, you know, re-piping you know, becoming more digitally oriented and, you know, in the selling efforts, it sounds as though that might also imply less fixed base in the SG&A and more variability perhaps.

I'm trying to look into - you know, obviously the efforts have yielded terrific, you know, numbers particularly the second half of this year with the record

lows as Stuart mentioned. Only, you know, I think 20 or 30 basis points of leverage into next year on SG&A.

Does that mean a lot of that is in the business? Is it that kind of fixed versus variable distinction that I was just making? How should we think about that going forward?

Stuart Miller: I don't think that we've added variability. I don't think we've made that as a migration. I think we've just pulled cost out of the equation. When I look at and think about our migration from conventional to digital marketing, we've basically cut many of our advertising and marketing costs in half.

While we have not increased traffic, we've actually reduced actual foot traffic, but to a much higher quality of traffic. So our conversion rates have gone way up and this has really created less stress in the system. Remember that this one element is a proxy for many other areas that we're focused on around our SG&A.

But, you know, some of the results, you know, about what our digital marketing platform has done really get a little bit interesting to me because it's not just about the reduction in cost. It's about the ability to drive traffic and to continue to enhance what we're already doing.

You know, so just some stats, you know, our digital marketing resulted in Internet leads being up 35% to over 90,000. Our social media followers are up 22% to 2.7 million and our YouTube views are up by 11 million to 33 million.

These are really big numbers that derive from the ability to actually focus on something and to use digital technologies to our advantage. Now when we talk about re-piping our system, we're re-piping the operational side of our

business to be able to apply the same focuses to things like even flow and even distribution of closings through a quarter.

To focus on a number of components of our business that we think can eliminate duplication in the way that we handle our financial accounting and the distribution of information through our company. And as these things are applied, we think we can have the same meaningful actual reduction in cost as we go forward.

Nishu Sood: Got it. Thank you.

Stuart Miller: Okay. Why don't we take one more question?

Coordinator: Yes. Thank you. And our last question is from Jay McCanless of Wedbush. Your line is now open.

Jay McCanless: Hi. Thanks for taking my question. On the community count, you talked about I believe up 7% as a little bit faster than what we were expecting. Could you talk about where you expect to grow the bulk of the communities?

Rick Beckwitt: You know, I have to look most of the community growth and the asset investment really flows to our larger markets California, Texas and Florida. We have spent, intensified our effort in the Carolinas and in Georgia. So you'll see increased community count growth from those areas.

Jay McCanless: Okay. And then on the cancellation rate, looks like it was down or up about 100 basis points year-over-year. Can you guys talk about what's going on there? Is that part of what you were discussing before about vetting some of the people that come in to the community centers or that come into the Internet vetting them a little more closely before actually accepting the order.

Bruce Gross: Yes, Jay. It actually went from 17% to 18% but both of those members are below the normal averages. So I wouldn't look at going from 17% to 18%, anything other than just some rounding. There's no issue with cancellations. It's well below long-term averages that we've experienced.

Jay McCanless: Okay. Great. Thanks for taking my questions.

Stuart Miller: Okay. So we'll wrap up there. Thanks for joining. Just in conclusion let me say 2016 was a great year for the company. We're really pleased with the results not just in terms of bottom line, but also in operational positioning and we look forward to reporting throughout 2017. Thank you.

Coordinator: Thank you. And that concludes today's conference. Thank you all for joining. You may now disconnect.

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