

**LENNAR CORP**

**March 27, 2019  
11:00 am EST**

Coordinator: Welcome to Lennar's First 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 Alexandra Lumpkin for the reading of the forward-looking statement.

Alexandra Lumpkin: Thank you and good morning. 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, Executive Chairman. Sir, you may begin.

Stuart Miller: Great, thank you. Good morning everybody. This morning I am here with Rick Beckwitt, our Chief Executive Officer; Diane Bessette, our Chief Financial Officer; and of course David Collins, our Controller; Jon Jaffe, our President is joining by phone.

I'm going to start with a brief overview. Rick and Jon will give a brief operational overview, and Diane will deliver further detail on our first quarter results as well as some additional guidance for 2019.

As always when we get to Q&A, I'd like to ask that you limit your questions to just one question and one follow-up so that we can accommodate as many participants as possible.

So let me go ahead and begin and say that while the housing market continued to be choppy throughout our first quarter, we are pleased to report very solid results. Although we had slightly lower than expected deliveries and revenues, we achieved somewhat better than expected sales and margin as we did see strengthening as the quarter progressed.

Generally speaking, it seems as though the market paused in the back half of '19, corrected in the first quarter and is now on solid footing, as we begin the 2019 spring selling season.

Looking backward, the housing market continued to slow through the fourth quarter 2018 as higher home prices and rapid interest rate increases combined to create a mismatch between prices and buyer expectations. Through the first quarter, interest rates moderated and home price appreciation stalled and even pulled back.

We clearly saw traffic and sales accelerate through the first quarter as strong employment, wage growth, higher participation rate, consumer confidence and economic growth drove the consumer to return to a more affordable housing market.

Given this progression, we continue to believe as we said last quarter that the market took a natural pause, it has now adjusted and recalibrated, and we are optimistic that demand driven by fundamental economic strength will continue to accelerate through the spring selling season.

We've noted consistently that the housing market is primarily driven by the deficit in housing production that has persisted for over a decade. This production deficit continues to define an overall shortage of housing in the country and has acted as a stabilizer as affordability has been tested.

Supply of dwellings both for sale and for rent, continue to be short and underlying demand driven by the need for a place to live remain strong.

Against that backdrop, Lennar performed well in choppy conditions. While deliveries missed the low end of guidance by 2%, this small miss was simply a shift in timing attributable to well-documented unusual weather conditions around the country.

New orders on the other hand exceeded the upper end of our guidance by 5%, driven by improving demand progressively through the month of the quarter.

We achieved net earnings of almost \$240 million this quarter and our strong cash position enabled us to opportunistically repurchase another 1 million shares of stock and end up with a total cap ratio of 38.5%, which is a 580 basis point improvement over last year.

We expect to generate strong cash flow for the remainder of 2019 and expect to continue to use excess cash flow to both pay down debt while opportunistically repurchasing stock.

Additionally, our significant technology initiatives around the company continue to be a significant reservoir of opportunity as we enhance our customer interface, create efficiencies in internal operation, reduce our SG&A and reduce our cost structure as well.

We continue to be laser focused on progress on our technology adoption and change management as this is being incrementally inflected reflected in bottom line improvement. We're still at the very beginning of the opportunities that we envision as we build a better mousetrap.

On a final note, we've continued to focus on reverting to our core homebuilding platform by repositioning or opportunistically monetizing non-core assets and business lines in order to drive efficiencies and enhance cash flow.

In the first quarter, we completed the sale of our real estate brokerage business as well as the sale of the majority of our retail title business and underwriter, and our retail mortgage business.

Additionally, we have contracted to sell our hospital in the Midwest, a remnant asset from Rialto, and that asset is expected to close in the second quarter.

Before I turn over to Rick, Jon and Diane, let me just say that even with what has been a choppy housing market, we are very excited about our position and our business strategy and we're encouraged by recent market signals about the remainder of the year. Of course, we benefit from the size and scale we have amassed in each of our strategic markets and that's reflected in our consistent improvement in SG&A.

Through 2019, we'll be generating strong cash flow and bottom line profits, and we're continuing to use cash to reduce debt. Our balance sheet is strengthening while we use the weakness of markets to opportunistically repurchase shares. We are shedding non-core assets to generate additional cash and to partner with tech companies who can help enhance our customers experience while reducing overhead.

As the homebuilding market continues to stabilize and redefine itself in the wake of the recent pause, we are optimistic about the remainder of 2019.

While Diane will give further Q2 guidance and some additional general direction on our full year expectations, based on our existing land position, our operating strategy and our dynamic pricing model, we will reiterate that we fully expect to deliver between 50,000 and 51,000 homes in 2019 with increased efficiency, improving margins through the year and with strong bottom line profitability and cash flow.

And with that, let me turn over to Rick.

Richard Beckwitt: Thanks, Stuart. In spite of somewhat softer market conditions, we achieved strong top and bottom-line growth in the first quarter.

Revenues for the first quarter totaled \$3.9 billion, representing a 31% increase from 2018. This was largely driven by a 30% increase in deliveries to 8,802 homes and a 4.1% increase in average sales price.

Deliveries for the quarter fell short of our Q4 guidance and were negatively affected by development and construction delays, driven by adverse weather conditions across the country. These deliveries will shift into our second quarter and some of our scheduled second quarter deliveries will shift into our third quarter.

We expect to return to a more even flow production schedule with non-weather affected build times by the end of Q2. However, notwithstanding construction weather delay, we accelerated starts in Q1 and successfully got on track with our internal start projections cumulatively through the end of Q1.

Our gross margin totaled 20.1% in the first quarter. While this was on the lower side of our prior guidance, it was consistent with our Q4 announced strategy to price our inventory to market and to keep our production machine going. We continue to believe that this is the right strategy and that higher operating margins and IRRs will increase shareholder value.

Our SG&A in the quarter was 9.5%; this marks an all-time first quarter low and highlights the power of our increased local market scale and operating leverage.

Homebuilding operating earnings on the sale of homes totaled \$383 million in the quarter, up 48% from the prior year.

Our operating margin increased 80 basis points year-over-year. We're particularly proud of the fact that our core homebuilding earnings are growing at a much faster rate than revenues, once again demonstrating our increased operating efficiencies.

Net earnings for the quarter totaled \$240 million, up 76% from 2018.

New orders for the quarter totaled 10,463 homes exceeding the high-end of our Q4 guidance by 5%. Orders in the quarter were up 24% from the prior year with the dollar value of approximately \$4.2 billion, representing a 23% increase.

On a pro forma basis, new orders were down 4% from 2018 tied directly to a 4% decline in active communities from the prior year. The harsh weather in the quarter delayed many

community openings, but we should be on track by the beginning of the third quarter with community count.

As I mentioned last quarter, the combination of higher sales prices and mortgage rates moderated demand in our fourth quarter, leading to reduced traffic, slower absorptions and increased sales incentives.

During our first quarter, we saw a reversal of these trends driven by significantly lower mortgage rates, and lower sales prices, and/or moderating sales price increases. These market changes spurred an increase in traffic on both our website and at our welcome home centers. We saw this activity come first through our digital marketing programs and on-site community traffic picked up quickly thereafter.

The combined impact of this increased traffic led to sequential increases in new orders in each month of our first quarter, with improved year-over-year performance in each month. Most importantly, we experienced this sequential order growth in every one of our 37 homebuilding divisions.

While some of this activity is clearly seasonal, we have seen a noticeable shift in homebuyer sentiment. In addition, while we did increase sales incentives in the first quarter by 20 basis points from the fourth quarter, we are optimistic that we've reached an inflection point and that incentives will start to decline as we enter the heart of the spring selling season.

In any case, we continue to price to market and use our dynamic pricing model to maximize price with the strategic focus on volume and higher operating margins over gross margins by themselves.

We ended the first quarter with a sales backlog of 17,259 homes with a dollar value of \$7.1 billion. This backlog combined with our current housing inventory puts us in a great position to achieve strong operating results in 2019.

I'd like to briefly discuss the recent changes by FHA designed to tighten the underwriting standards on FHA originated loans. FHA now requires lenders to manually underwrite loans that have both debt-to-income ratios above 43% and FICO scores below 620 rather than rely

on the automated underwriting system. This is a reversion to a policy that was in place from 2013 to 2016.

While the loans can still be approved, the manual process takes slightly longer as it requires additional verifications, calculations and qualifying hurdles. The net impact of these changes to Lennar is insignificant. Based on our analysis of the loans that our Eagle Mortgage Company has made over the last five quarters, we believe that less than 1% of our total loans would have been impacted by these changes.

Before I turn it over to Jon, let me give you a brief update on our land initiatives. The three strategic initiatives we discussed last quarter are up and running. Each vehicle is actively pursuing and underwriting new opportunities and moving forward with the entitlement and development of their previously existing portfolios.

In addition, we have expanded the geographic territory of two of these existing structures to include markets outside of Florida. This expanded footprint will increase our asset light land strategy in many more of our homebuilding operations.

Lastly, we are continuing to use these existing structures and are in advanced discussions with several regional developers in other markets to expand this program.

Now, I'd like to turn it over to Jon.

Jonathan Jaffe: Thanks Rick. Today, I'm going to give an update on synergies, direct construction costs along with our production first operating platform and our SG&A leverage.

First, we remain on track to achieve our prior guidance for 2019 of \$380 million for merger synergies with \$265 million of this from direct construction cost savings and \$115 million from corporate and SG&A savings.

Next, I want to give some perspective on what we are accomplishing with our production first focus, what many of you refer to as pace over price. We've discussed for several quarters our goal of becoming the builder of choice for the construction trades. We

articulated a program where we would utilize our significant size and scale in each market to forge new working relationships with our trade partners.

We have made the effort to work hand in hand with our trade partners to better understand how together we can maximize efficiencies that improve the bottom line profitability for our trade partners while lowering our construction costs and improving cycle time. Simply put, we've been on a mission to be the low-cost preferred builder for the trades so they can in turn share these benefits back with us.

We're beginning to see the anticipated results from these efforts. Sequentially, for the first quarter over the fourth quarter, we had a very small increase of just 0.6% in our average construction cost per square foot. This is meaningful as the industry still faces a headwind of the ongoing labor crisis which puts pressure on labor costs along with material cost pressures that comes from tariffs, factory labor shortages, stricter energy codes and all without the benefit of the lower lumber cost which will materialize later in the year.

As we highlighted last quarter, we are focused on our production machine, delivering to the trades even flow starts and deliveries throughout the year. We presented these plans to trades in all of our divisions and delivered on the plan on Q1 by starting the homes we committed to.

As Rick noted, we have to deal with some extreme wet weather conditions that interfered with the goal of evenly spreading our production, but we still delivered on the commitments to start the homes we said we would. We heard from many of our trade partners that we stood out and maintaining our start during fourth and first quarters, where many of our peers pulled back on and start to sales slowed during this time.

The combination of working with trades as strategic partners, our commitment to even flow production and the simplicity of everything included all work to create an environment where more and more trades are concluding that Lennar is their builder of choice.

With our combined size and scale we're able to leverage our SG&A to an all-time first quarter low of 9.5%. A big contributor to this improvement is our continued focus on the sales process which has reduced our average realtor commission down to 2.27% in Q1, an



improvement of 26 basis points year-over-year and 12 basis points sequentially from Q4.

This reduction in cost is the result of our efforts to reach our customers early in the process through our digital general marketing campaigns.

We had over 190,000 total Internet leads in Q1, a year-over-year increase of 32%. An Internet lead is someone who specifically requests information from us. These leads are attended to immediately by one of our Internet sales consultants who are based in each one of our divisions.

Their responsibility is to help the customers decide which community is right for them, and then set an appointment for the customer to visit that community, and follow up with the customer to remind them of another appointment or to reschedule as needed. This produces a high quantity of high quality leads for our community-based new home consultants and on a scheduled appointment basis.

I will conclude by noting the plan to improve our net operating margin, free cash flow and return on capital is proving out. Its execution is built on four pillars; one our builder choice production first operational platform which drives cost down.

Two, our just in time selling platform driven by our dynamic pricing model which allows us to always be priced to current market conditions.

Three, a technology driven efficiently levered overhead structure.

And four, our Everything's Included platform that simplifies the homebuilding process while providing great value to the home buyer.

I would now like to turn it over to Diane.

Diane Bessette: Thank you, John and good morning to everyone. So let me summarize and reemphasize a few points from our first quarter.

And so starting with homebuilding, as you've heard, looking at deliveries, our actual Q1 2019 deliveries increased 30% from the prior year Q1 2018 deliveries and decreased 12% from pro

forma Q1 2018 deliveries. These pro forma deliveries included CalAtlantic December 2017 deliveries which was the last month of its fiscal year and thus not truly comparable.

Our first quarter gross margins on home sales was 20.1%, the prior year gross margin was 19.5% or 21.6% excluding CalAtlantic purchase accounting write-up of backlog and construction in progress.

Our Q1 2019 gross margins were impacted by an increase in sales incentive consistent with our focus on pace and an increase in construction cost due to the high point of lumber prices in 2018 flowing through Q1 delivery.

As you've heard us say, our first quarter SG&A was 9.5% compared to 9.7% in the prior year. The decrease was due to improved operating leverage as a result of increased size and scale as well as our continued focus on obtaining benefits from our technology initiatives as John detailed.

And then turning to new orders, new orders increased 24% and new order dollar value increases 23% for the first quarter, primarily result of the CalAtlantic acquisition. Our Q1 2019 new order decreased 4% from pro forma Q1 2018 new orders, and community count decreased at the same rate, and thus absorptions were flat year-over-year pro forma near at 2.7. Our Q1 cancelation rate was about 17%.

And finally, for Q1 2019 homebuilding joint venture land sales and other categories, we had a combined loss of \$13.2 million compared to our \$154.5 million of earnings in the prior year. But remember that last year included a gain of approximately \$165 million related to the sale of an 80% interest in one of our homebuilding joint ventures.

So then turning to financial services, again as you've heard us say, consistent with our reversion to pure play homebuilder.

During the first quarter, our financial services segment sold the majority of its retail title agency business and title insurance underwriter, its retail mortgage business and its real estate brokerage business. But these transactions resulted in a net gain of approximately of \$1.6 million.

As a result of these strategic transactions, financial services headcount has been reduced from approximately 3,200 at year end to approximately 1,700 after the completion of these transactions.

And then just to add a little more color on the largest transaction which was a sale of our retail title agency business and title insurance underwriter. So we sold the majority of these operations to States Title as we previously announced.

In connections with this transaction, we provided seller financing and received substantial minority equity ownership stake in States Title. The combination of both the equity and debt components of their transaction did not meet the accounting requirement of sales treatment and therefore, as you look at our numbers, you'll see that we were required to consolidate States Title's results at this time.

So then looking at the components of financial services, operating earnings, net of noncontrolling interest related to States Title combined were \$21.8 million compared to \$25.9 million in the prior year and the detail of the component are as follows; mortgage operating earnings increased to \$14.9 million from \$14.5 million in the prior year. Total originations were relatively flat at \$1.9 billion for both Q1 2019 and Q1 2018.

Originations in Q1 2019 included increased volume related to a full quarter of CalAtlantic, offset by a decline in volumes due to the sale of the retail business.

Title operating earnings increased to \$5.9 million from \$5.4 million in the prior year. Even though there was a decrease in the number of title transactions due to the businesses sold, operating earnings increased as a result of additional transactions related to a full quarter of CalAtlantic and a focus of cost reductions to right-size the business.

And then one point to note regarding financial services, in connection with Rialto investment and asset management platform sale in the fourth quarter of 2018, Rialto mortgage finance or RMF has moved into our financial services segment, and as such, all prior period information has been adjusted to conform with the current presentation.

And so looking at our RMF, for the first quarter of 2019, their operating earnings were about break even compared to \$6.5 million in the prior year. This decrease was due to lower securitization volume and margins during the quarter as compared to the prior year.

And then looking at Multifamily, in the first quarter our multifamily segment had operating earnings of \$6.8 million compared to an operating loss of \$1.2 million in the prior year.

In this first quarter, we recorded \$15.5 million related to sales during the quarter and \$1.8 million of promote revenue related to the stabilization of properties in our LMV fund.

As we've noted for a while, we have been moving from a build-to-sell to a build-to-hold platform, earnings fees and promote by creating value within our fund.

And then finally, other, just a small note, you'll see that new category on our balance sheet and P&L. So, as a reminder, we've combined with the remaining Rialto assets which are primarily the fund investments and our strategic technology investments into this category effective December 1st, earnings were \$3 million in Q1 2019 compared to \$4 million in the prior year.

Turning to the balance sheet, at February 28, we ended the quarter with \$853 million of cash. We had borrowings on our revolving credit facility of \$725 million, leaving about \$1.5 billion of available capacity.

At quarter end, our homebuilding debt to total cap was 38.5%. And during the quarter as Stuart mentioned, we repurchased 1 million shares for a total of approximately \$47 million.

At the end of the quarter, our home sites owned and controlled were 278,000, of which 210,000 are owned and 68,000 are controlled. And stockholders' equity increased to \$14.8 billion and our book value per share, grew to \$45.75 per share.

So now turning to guidance, I'd like to provide some guidance for the second quarter.

Starting with homebuilding, we expect new orders between 14,000 and 14,300. We expect to deliver between 11,700 and 12,000 homes. We expect our Q2 average sales price to be

between \$400,000 and \$405,000. We expect our Q2 gross margins to be in the range of 20% to 20.5%, and our SG&A to be in the range of 8.5% to 8.6%.

And for the combined category of homebuilding joint ventures, land sales and others, we expect a Q2 loss of approximately \$10 million to \$15 million.

And then turning to our ancillary businesses, we believe our financial services earnings will be between \$45 million and \$47 million. We believe our multifamily earnings will be about a \$5 million loss.

And for the other category related to the Rialto legacy assets and our strategic investments, we expect a Q2 loss of approximately \$10 million.

We expect our Q2 corporate G&A to be about 1.6% of total revenue and our tax rate to be about 25.5%. Our share count should be about 321 million shares. This guidance should produce an EPS range of \$1.07 to \$1.20 for the quarter.

And then turning to fiscal 2019, given that we believe the market is a bit less uncertain and on more solid ground, we thought it would be helpful to provide a few additional data points for the full year 2019. This guidance is still preliminary and we will adjust as the year progresses.

So starting with delivery, we expect, as Stuart mentioned, to deliver between 50,000 and 51,000 homes. We believe our average sales price will remain relatively flat from current level, so approximately 400,000 to 405,000.

Our gross margin is expected to be in the range of 20.5% to 21%, and our SG&A in the range of 8.3% to 8.5%.

And then finally, a couple of comments regarding our ancillary businesses, financial services earnings should be in the range of \$185 million to \$190 million, and then our Multifamily earnings should be in the range of \$5 million to \$10 million.

This reflects our migration from a build-to-sell to a build-to-hold platform. This strategic change means that instead of having GAAP earnings as we sell assets, we will have additional accumulation of profit that will be recognized in the future as assets are completed and stabilized.

The estimate of our shares accumulated changes in fair value is approximately a \$150 million on 21 completed and stabilized assets in our LNV Fund I, as we compare the market value of our investment to our basis; as additional assets complete and stabilize, this amount should increase.

So in summary, we believe we are well positioned to have strong profitability and cash flow generation in 2019, and we look forward to reporting our progress in future quarters.

And so with that, I would like to turn it over to the operator for questions.

Coordinator: 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 on your phone, unmute your phone and record your name clearly when prompted. Your name is required to introduce your question. To cancel your request, press star followed by the number 2.

Our first question comes from Buck Horne from Raymond James. Your line is now open.

Buck Horne: Thanks, good morning and congratulations to a strong start to the New Year. Just could you start with walking us through the map and just kind of characterize what you're seeing in terms of demand trends, absorption paces geographically? And maybe by price point and just any other factors with certain markets, for example, you know, foreign buyers in California as an example. Any color there is helpful.

Jonathan Jaffe: This is John. Yes, particularly in California, we saw in the first quarter the same pattern Rick described naturally, which was each month sequentially we've saw an improvement in traffic and the quality of that traffic and in sales.

And we saw what we expect would be a recovery first in the more affordable California markets of the Central Valley, in Sacramento and a slightly slower recovery in the more expensive coastal markets; Bay Area, Orange County and San Diego.

Buck Horne: Okay.

Richard Beckwitt: Yes, guys, this is Rick. As I've said in my comments, we saw sequential increases each month, each quarter by - in every division that we had. From an overall standpoint, we started in the December month with a negative comparison year-over-year, and got finally to in February a positive variance that netted to our 4% down for the quarter.

You saw increases in absorption pace month to month to month throughout the quarter and that was pretty much across every market that we saw.

Buck Horne: Okay, that's helpful. So it sounds like the trends in the margins or the margins in the backlog are stabilizing and/or improving. I'm just wondering, is that a function of any changes in the product mix you're making, or is that, you know, expectations of reduced incentives going forward that would affect the rest of 2019? And are there other tailwinds in the margins that - whether it's lumber, labor or production synergies you could quantify?

Richard Beckwitt: Well, I'll start out with the backlog and Diane's guidance with regard to Q2. The sales that we generated in the first quarter and some of the sales that we generated in the fourth quarter that will close in our second quarter are affected by some of the incentives that we use to move our inventory.

As we said, we are focused on our production model and really geared towards net operating margins. But some of those sales will have a higher incentive in them, and as a result have a lower gross margin.

As we look through the year, we're optimistic that we'll be able to get to a point where we have to offer less incentives to keep that production pace up. You know, we're just beginning the heart of sales season now and we will have to see how the year goes.

Buck Horne: All right, thank you very much.

Coordinator: Our next question comes from Stephen Kim from Evercore ISI. Your line is now open.

Stephen Kim: Yes, thanks a lot, guys. Good job in a tough environment. I wanted to ask you, Stuart, about your overall comment about the industry taking a natural pause last year. I mean I just want to make sure that when we get your perspective clearly now that last year is sort of in the record books and we've sort of gotten back to a little bit of a normalized environment, because obviously rates are continuing to be little bit jumpy.

So, when we look at the decline in demand that occurred last year in the back half, really beginning the middle of the year, I think you're characterizing it now as the industry taking a natural pause. But you didn't specifically call out the mortgage rates sort of moving north of 4.5%. But I think a lot of people sort of keyed in on that because of 4.5% mortgage rate was a little lower than I think most people's thought would be the threshold above which demand would take a pause.

And so, as we go forward here with last year in the record books, do you believe that 4.5% represents an important threshold, or do you believe that because we now have another year of economic growth, that maybe a threshold that might be in mind which should be like a 5% mortgage rate?

I just want to get your sense of the interplay of the mortgage rates in your generalized outlook for what happened last year - I'm sorry your reflection on what happened last year and what you think will happen as we go forward over the next couple of years.

Stuart Miller: So, let me go back to my comments, Steve, and highlight that both last quarter and this quarter I have talked about this natural pause in terms of two components; an accelerated rate of increase in ASP which we have seen for a number of quarters, together with a very rapid increase in interest rates.

And the reason I articulated it last quarter and even in the third quarter as the beginnings of a natural pause at that time is the rate at which sales prices had been moving up was outside of a normal rate. And when you layered on top of that a very quick kind of sticker shock approach to interest rates moving up, it just created a mismatch between buyers' needs and



buyers' expectations, and I felt that it was a natural sticker shock that came from the rapidity at which rates and ASP were moving, right?

So when I think about things today, we've seen moderation on both fronts as I articulated both on the price appreciation. We have seen price appreciation, you know, certainly slowdown. I said - I used the word "stall" and even pull back in my comments and we have seen that. In various markets we have seen, price appreciation really pulled back quite a bit in response to demand subsiding.

But, additionally, layering on top of that, we've seen a discernible or a serious reduction in interest rates. And the combination of the two has really brought the market back kind of into what I think of as equilibrium. The economy has continued to be fairly strong. Unemployment has been low. We've seen wages increasing. We've seen participation rate increasing and that reflects itself in more dual-income families.

And so these are the things that were seeing at our welcome home centers as people come to visit with us, that you know, interest rates together with average sales price, together with general economy moving in the right direction has really set a stage of stability right now in terms of the market moving forward.

Now, against that backdrop, remember that, you know, home production, the production deficit that I keep referencing, we still haven't seen home production yet to what most people still think is a normalized 1.5 million homes per year. We've been decidedly well below that number for a very long period of time.

And so, we still have a housing shortage, people need a place to live, affordability has been tested, that affordability tested and pulled back. And so, we kind of look forward and think that the market looks pretty good.

As to your question about that 4.5% rate, is that some kind of an inflection point? I think it has more to do with the rapidity at which rate - interest rate moves together with average sales price alongside of an improving economy. And I think that what we saw in the third quarter and fourth quarter was it just happened too quickly and created sticker shock.

Richard Beckwitt: Yes, Steve, just one another point on that, as we said in Q4, we didn't see a qualification issue with regard to people when they locked in at the home they could afford. And it was just really a mismatch between buyer expectations and what products they could buy.

And now that has been reset and then sort of like rebooting a computer, and that's why, you know, Stuart has gotten to the point where that pause is over and were back in action again.

Stephen Kim: Got it, that's very helpful. Talking about the rapidity with which ASPs are increasing, obviously, you've got to mix shift that's been going on as you've been targeting more affordable price points and all that which has been, you know, absolutely the right move.

But one of the things we've heard is that the ASP at the entry level is, in many cases, has been over the last couple of years growing at two to even three times the rate of the market overall. And so that's sort of hidden there in that sort of, you know, ASP mix - blended mix.

And so I was curious as to when you talk about ASPs, it seems like you're envisioning an environment where ASP growth is going to be a little bit more moderate, a little bit more sustained at a sustainable level. Did you - when you're talking about that, are you talking about a slowdown in the pace of ASP growth at the entry level as well?

And then at the back half of that question, you talked about the FHA. My question on the FHA is, were you surprised at the timing of the move? Were you surprised that they made that move the way they did when they did or did you expect that?

Stuart Miller: Well, let me start with the ASP question and by the way, we're noting that you squeezed two questions into one so - as a shoehorn.

You know, as it relates to ASP, ASPs have been moving up in part because of short supply and in part because the cost structures have been moving up and we've seen that even more at the lower end. It's very difficult to produce affordable housing at lower prices given land costs and production costs. But there has been a pause in ASP at all price points that was generated by both interest rates and an accelerated increase in price.

And I think that this is exactly why you've seen us shift and focus so dramatically to size and scale in local markets, using size and scale to recalibrate both our building partner program, our Builder of Choice program to moderate the acceleration of construction costs and as well our laser focus on technology and recalibrating our SG&A because we recognize that affordability is going to be tested if prices keep getting driven up by the cost structure. And we've got to do some things to offset that and we've been working really hard at that.

So I think you're seeing that prices are going to have some caps to them defined by affordability, and the challenge for the building community is going to be the rationalized cost both at the SG&A level and the cost structure level to accommodate what is likely to be slower price increases.

And you've seen that yesterday in Case-Shiller, the acceleration of price increases is lower and I think that that's a little bit behind the curve. We're still going to see that come down. I think that's going to be more the wave of the future.

And as it relates to FHA, I'm going to let Rick go ahead and hit that.

Richard Beckwitt: We weren't particularly surprised with the timing or the announcement. This has been something that's been rumbling for a while. And you know, but, as I said, the net impact to us is de minimis.

Stephen Kim: Yes. Thanks very much, guys.

Coordinator: Our next question comes from Michael from RBC Capital Markets. Your line is now open.

Michael Eisen: Good morning. Actually, Mike Eisen on for Mike Dahl. I just wanted to follow up on some those comments that you guys have made a few times now about pricing resets or more moderating pricing environment and I was hoping you would talk to for Lennar products specifically; what you guys are doing from a strategy standpoint whether it be taking down base prices, whether it be smaller square footage and how you guys are addressing this, and then how - where, you know, specific regions you are seeing the most success with this strategy.

Richard Beckwitt: Jon, you want to start off?

Jonathan Jaffe: Sure. For the most part we - this is a very market-by-market approach that Lennar takes with its product. So we will have some markets where we have taken square footage down, San Antonio, Texas, as an example, and we'll have other markets where the land basis really doesn't allow for that to happen on the other end of the extreme in Orange County, California, where square footage hasn't reduced in price points. It remains at a higher overall level.

Our big focus, as you've heard from all three of us, has been on how do we really moderate our cost structure, so that at whatever price we're trying to target, whether it's entry level, first-time move-up, second-time move-up buyer, we can be priced affordably in a marketplace against the competition, against the resale market as a value to that consumer.

So laser focused on efficient production program to really keep the price points down recognizing that affordability at each price point is an issue and we got to be very responsive to that.

Richard Beckwitt: Yes, and so just to get to the second point - portion of your question with regard to product adjustments, we are very laser focused on what features we should include in our Everything's Included product to capture the best value and provide the best margin for us and provide the best value for our customers.

So we look at footprints, we look at included features, we make adjustments, we have regional opportunities going on right now. So we're very focused on that.

From a footprint basis, in parts of Texas and some of the Carolina, you'll see that we're starting to deliver a little bit smaller home. And if you look at just general pricing, you know, on our sales for the last quarter, we were flat year-over-year with regard to ASP. Some of that is mix, but some of that are just lower prices on a year-over-year basis.

Our backlog year-over-year is down about - our average price and backlog is down about 6%. So that gives you a true look at some of the pricing adjustments that we've made. But as Jon and Diane said, it shouldn't really impact our margin going forward.

Jonathan Jaffe: Just to follow up on the point that Rick made, Everything's Included platform really allows us to deliver a better value to the customer because they're getting more included features without having to pay extra for it.

A good example of that I was just chatting this morning with our folks in Indianapolis through their regional president, and there they've gone from a complete CalAtlantic division -- Lennar had no presence there -- to converting their product to Everything's Included. And what they are finding is, with the offering - the value offering of Everything's Included, their sales pace is picking up in the same communities with the same product. So that product now offered at lower price, more value features included and no options available to the customer. So that allows us also address the issue of affordability.

Michael Eisen: Got it, I appreciate all the color there, very helpful. And then just following up, taking some of those comments and applying them to the impact on gross margins down the road, it seems that there's a few different buckets between the synergies, cost savings, lower lumber that are working in your favor, offset by lower pricing, and just the desire to be, you know, higher velocity.

So can you help us think longer term as you guys are operating this higher volume business model? How we can think about margins moving back higher, some of the higher levels we've seen over the last few years, or if this 20.5% to 21% is the new normal for what the company can do? Thanks and good luck.

Richard Beckwitt: Well, maybe I'll take a crack at it. You know, I think we're one or the only company right now - the only company that's given full year guidance and we really do not like to get over our skis and get into, you know, years outside of the current fiscal year.

Stuart Miller: So let me add to that and say, with that said, while we are taking a conservative look forward, as we look at the rest of this year, recognizing that we're coming out of the choppy market, we'll wait and see exactly how this spring selling season shapes up. We haven't just taken pricing as it has come.

Remember that we have spent a lot of time focusing on our cost structure using the tools that we've acquired through size and scale and through various technologies to really recalibrate our cost structure and to recalibrate our SG&A.

And while the progress is incremental, sometimes a little bit slower than we'd like, it is always with regard to our focus on the net margin that we see, that we're driving all of our internal strategies. So when you listen to Jon talk about the cost structure, and Builder of Choice initiatives and things like that, these are all focused on generating a higher gross margin.

When you hear me talk about our building a better mousetrap, and generating lower SG&A, and recalibrating our internal mechanisms and our customer interface, it's all about generating a lower or a higher net margin, lower SG&A.

So while we recognize that the market might be choppy, might be a little up, might be a little bit down and as we think ahead, we know some of these initiatives will produce results. They might be slower than expected. We can't predict them exactly. But we're focused on both the cost side of the business as well as what the pricing might be. Next question?

Coordinator: Our next question comes from Alan Ratner from Zelman Associates. Your line is now open.

Alan Ratner: Hey, guys, good morning. Nice quarter and thanks for all the color here, great to hear about the improvement in the market. First question on the 2Q guide, if I heard it correctly on new orders, I just wanted to dig in a little bit more, it seems like you expect orders to still be down a little bit year-over-year which, you know, given the momentum you saw through the quarter and slipping to positive in February, it would seem a little bit surprising.

So can you just talk a little bit more about what's going into that, is that a function of the weather delays you experienced and kind of how do you see that playing out?

Jonathan Jaffe: This is Jon. Go ahead.

((Crosstalk))

Richard Beckwitt: This is Rick. Jon, let me start off. Some of that is just a function of we've got a bunch of communities closing out this quarter and we have communities that will get back on track, but it is really late in the quarter. So you're seeing a reflection of, you know, the number of sales opportunities we have for community count. And Jon, I'll pass it to you now.

Jonathan Jaffe: Just beyond that, I would make the same point. As you look at it, for us, our projected sales pace for Q2 of '19 is actually right on top of the sales pace that we had in Q2 of '18. So it's just community count that's driving the result that you're highlighting. But we feel very good about our positioned given that we're projecting a sales pace that's equivalent with last year.

Alan Ratner: So then just to hit the year-end or the full year target then, you know, it seemed like a pretty healthy ramp in the back half of the year. Can you just talk a little bit about what your starts growth looks like to support that level of growth?

Jonathan Jaffe: We have a natural increase as we moved through the year. We are, as I mentioned and we all mentioned, trying to level that out throughout the year, but we still haven't increased in starts as we move from first quarter to second, into third, sorry, second and third quarter are our largest for starts. Third and fourth will still be our largest for deliveries. But even this year that's beginning to moderate as compared to prior years.

Alan Ratner: Got it, Okay. And if I could just add a second one, a separate topic, the iBuyer, your Opendoor investment, curious maybe, Stuart, if you can give us an update on how that's been progressing, how many markets is that kind of being active in right now, and what percentage of your orders is the buyer actually utilizing that on their resale?

Stuart Miller: So, first of all, we're really enthusiastic about our program with Opendoor. You know, first of all, Opendoor has just tremendous management team that has a very aggressive agenda in rolling out, not only rolling out to new markets, but more importantly refining their business model, focusing on both their customer interface and their unit economics. And this is a team that is just best in class.

Jon Jaffe, he has the privilege of serving on the board there. And what we have is - and I'll let Jon talk a little bit more about it in a second, but what we have is a rollout program where

as Opendoor enters each new market, we have a side-by-side launch with them of an Opendoor program within our division.

And what we have done is we've really mapped out a change management adoption program to include the Opendoor tool in our toolbox, whereas we have customers who come to visit us and say, "Gee, I love your offering, but I have a home to sell." We can turn to them and say, "We have a solution." And that mechanism for rethinking the way that we work with our customers and taking the friction out of the trade-up and the move-up programs that we have in our system is really working well.

Opendoor on its own, in its own world is doing quite well. But in coordination with Lennar, we're finding greater and greater and accelerated adoption of the program as we go market-by-market.

I have to admit I have lost track of exactly how many markets they are in together with us right now, but we are monitoring market-by-market month-by-month how many Opendoor-enabled sales we are achieving and we're really enthusiastic about the program. Jon?

Jonathan Jaffe: Just yesterday we opened our 18th market with Opendoor in Austin, Texas. And as Stuart noted, it's been a great learning process as we have, jointly with Opendoor, presented to our operating division, to our sales team the Opendoor platform.

Our divisions eagerly await the opening of that in their market and we're finding lessons learned in process toward each opening execution is better and better than the prior ones.

We have some of our first division has reached activity level of 20 transactions a month, that's in Phoenix, and we're seeing, as I said, just better and better execution. So we're very excited about that. We view it as incremental buyers.

It reduces our cancellation rate as it's a solution for our buyers that have a home to sell and it also helps lower our broker spend as that buyer very often we reach earlier in the process and they don't have a broker yet, so they are not involved in the equation.



So, all in all, as Stuart said, we're extremely enthusiastic about the program. We got a great working relationship with the management team there. We work hand-in-hand to learn from each other. We learn technology from them, they learn operations and real estate from us, and we're both improving from that.

Stuart Miller: Let me add one more point here since you've opened the door on Opendoor, maybe the most important thing that we are learning, and this is where we are working around the clock is we are learning about change management, change management from the way things have worked and worked quite well to a progressively better way to interact with our customer and pull friction out of our programs, and migrate our associates to understand that there is a better way to transact. And that change management process has friction points of its own.

We are learning as we are doing and we are evolving our ability to communicate internally, and that to me is perhaps one of the most exciting parts of the program. We're going to get better and better at this, not just with Opendoor but with Blend, with States Title and with others that we are engaged with, with Hippo.

Our technology initiatives are - we have a great deal of enthusiasm for them. But our ability to integrate and work with them is getting better and better all the time. Last question?

Alan Ratner: Thanks a lot.

Coordinator: Our last question comes from Michael Rehaut from JPMorgan. Your line is now open.

Michael Rehaut: Thanks. I guess right now it's good afternoon, everyone. Thanks for squeezing me in. I have just one question in 27 parts, just kidding obviously. First question, just on incentives, I was hoping to get a better sense, you know, you talked about the market being choppy in - you know, throughout the quarter, but at the same time improving as mortgage rates perhaps and other - you know, the spring selling season progressed. I was wondering how that's related to incentives as they progressed throughout the quarter and in particular what you saw across parts of California?

Richard Beckwitt: Well, throughout the quarter, as I said, we continue to incentivize in order to move our completed product. Again, this is something we're going to continue to do in each period as we price our inventory to market using our dynamic pricing model.

We believe that as we moved into Q2 and to Q3, the level of incentives is going to start to dissipate and we've started to see that through conversations that we've had with homeowners as we moved through the quarter.

Jonathan Jaffe: And with respect to California, Michael, we definitely are consistent with what I said earlier in the more affordable market Central Valley, Sacramento, the incentives are proportionally lower than they are on the coastal markets.

And then all those markets, particularly the central markets, we did see lessening incentives towards the end of the first quarter. And the coastal markets, let's say, just as Rick was saying that we use those incentives to generate the sales pace improvement in those markets.

Michael Rehaut: Okay, thank you for that. I guess, secondly, just shifting gears a little bit to return on equity, you know, you've obviously highlighted some of the initiatives that you are doing in terms of returning to your core business, selling off some different businesses as you highlighted with different parts of the brokerage and title, et cetera.

How do you see, you know, over the next two or three years, where do you want to be in terms total assets sales or as it relates to kind of slimming down your balance sheet let's say, as well as share repurchase? Because when you look at ROE and that has had a pretty powerful relationship between that metric and valuation multiples, and with your ROE being below some of your larger cap peers, you know, where do you want to see that metric go and what you are willing to do in terms of again additional asset sales or more aggressive share repurchase, for instance, to get there?

Stuart Miller: So, you know, we are very focused on return on equity. And let me just say I think we're going to try to get one more question in before we end the call. But I think that a combination of generating strong earnings and that strong earnings power coming from, in part, what we're doing relative to our SG&A is going to be a primary driver of stronger ROE.

As we've an opportunity to continue to pare down ancillary businesses, as we've said, we're going to do that, but we are not going to force the issue. We think that there are intrinsic values to the assets that we have, whether it's LMC multifamily program or whether it's FivePoint.

So we're not going to force the issue as we haven't and didn't with Rialto. But we're going to migrate to a core business strategy, that's where our focus is going to be. And we are certainly going to be focused on using technology, those internal initiatives and external to increase bottom line.

Let's go to one more question, operator?

Coordinator: Yes, we still have a few questions in the queue.

Stuart Miller: Let's take one more.

Coordinator: Thank you. Our next question comes from Stephen East from Wells Fargo. Your line is now open.

Stephen East: Thank you. Thank you for squeezing me in there, Stuart. You know, first, you got this big combined company, you all have talked now about the developer agreements and starting to get them off the ground. So could you talk about maybe, you know, first of all, what geographies are you in if you are willing to talk about that yet?

And then as you look at your ability to option more land at a faster pace maybe or can you all talk a little bit about where you are with that process and how fast you think you can accelerate your optioning of land off that?

Richard Beckwitt: So it's Rick, Stephen. You know, as I mentioned last quarter, the deals that we brought into place, the three deals catapulted us to about a 30% control position and we expect that over the next 18 months we'll be north of 40% based on the arrangements that we've got in place.

You know, this is - it's a program - sort of getting back to that last question, what's the biggest mover with regard to where we can enhance our return on equity? It's moving to an asset-light program that Stuart really identified our pivot going back two or three years ago.

So we are going to continue this on. You will see a higher concentration of deliveries coming from vehicles like this. And as I said last quarter, given the type of arrangement that we have in our right to purchase from these things without a contract, you may not necessarily see them directly in our controlled, owned count because of the way that they are structured.

And as far as the markets, we've expanded them to other parts of the Southeast. Let's just leave it there.

Stephen East: Alright, fair enough, fair enough. And then on your community growth, you know, a more immediate question and a bigger picture question, when will you turn positive you think in your community growth this year? And then as you think about your business in a broader sense, how fast would you all be satisfied growing your communities and really your unit growth, if you will, just a big picture question?

Richard Beckwitt: Yes, so really by the time we get into Q3, first month of Q3, you'll start to see a flat year-over-year community count.

You know, we had a double whammy come in this last quarter. We had a bunch of communities closing out where, you know, just because we had a good programs going on with regard to sales activity and we had about 30 communities that were delayed because of the weather to get us going.

So we will start to see a more normalized year-over-year comparison as we get into Q3. And you know, as we've said, we plan to grow community count as we move forward in the market.

Stephen East: So from a bigger picture, you know, where would you be comfortable and how do you think about your unit growth over time?

Richard Beckwitt: As we've said in the past, we think that we want to grow our business about a minimum of 3% to 5% to 7% with regard to unit activity. Some of that will be associated with a little bit higher absorption since the market recovers on a community-by-community basis. But some of that is going to be tied to incremental community growth. But really our zip code is 5% to 7% for the next year or a year or two.

Stephen East: Okay, thanks a lot, I appreciate that.

Stuart Miller: Okay, we're going to wrap it up there. I want to say that I appreciate everybody joining.

And let me just circle back to where we started and that is we highlighted that we felt that the home building market had entered a pause in the third and fourth quarter. We found evidence of stabilization in the first as we migrated through our first quarter. We look forward to checking back and giving an update on how we're going from here.

But with that said, we are optimistic that the housing market has found a firm ground and is ready to move forward.

Thank you for joining. We'll speak to you next quarter.

Coordinator: That concludes today's conference. Thank you for your participation. You may now disconnect.

END