

LENNAR CORP

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11:00 AM EST

Coordinator: Welcome to 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 Alexandra Lumpkin for the reading of the forward-looking statements.

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 yesterday'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 has 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. Good morning and thank you everyone for being here. This morning I'm here in Miami once again scaled down and socially distanced crew that includes Diane Bessette, our Chief Financial Officer; Dave Collins, our Controller; Bruce Gross, the Chief Executive Officer of Lennar Financial Services; and of course Alex who you just heard from. Rick Beckwitt and Jon Jaffe, our co-Chief Executive Officers and co-Presidents are joining us from Colorado and California respectively. And they're on the line and will participate as well.

We're going to attempt to keep our remarks brief in order to have plenty of time for your questions. I'll give a brief macro overview and perspective. Rick will talk about land and community count. Jon will talk about sales, production, and construction costs. And Diane will give a more detailed financial overview with highlights and with guidance. Then we'll attempt to answer as many questions and as usual please limit questions to one question per person and one follow-up.

So with that, today I'd like to start by thanking the coast-to-coast associates of Lennar for extraordinary work in an extraordinarily challenging year. We started 2020 with great expectations in an expanding market which came to an abrupt stop with the unexpected arrival of COVID and then leapt back into high gear to address a market with unusually strong demand that was desperate for a home, a refuge and a brand new concept, the hub of everyone's life.

The associates of Lennar adapted and adjusted, learned new ways to interact and to transact, worked from home and put people first, cared for our communities across the country with acts of kindness and acts of charity and on top of all of this turned in pristine Fourth Quarter and Full Year 2020 results that are perfectly aligned with our company's strategy and once again position Lennar as America's most profitable homebuilder.

Diane, Rick, Jon, and myself, have the privilege to present their results and additionally to guide with great confidence the expectation for another excellent year in 2021.

As a macro overview let me say that the housing market is simply very strong and demand for homes, new and existing, is greater than the limited supply. It has simply never been this easy to sell as many homes as we would like, in every market in every price range, across the country.

The American dream of homeownership is once again an essential aspiration of the American population and the resolution of the current pandemic will not slow the growing demand.

Low mortgage rates and ample deposit money from savings... from vacations not taken, movies not seen, restaurants not visited and of course stimulus dollars from the government are driving customers to purchase a home, a larger home, a home with a yard, an office, a nicer kitchen and a place to call their own. Apartment dwellers can afford a first-time home and demand is strong and growing.

The iBuyer participants led by Opendoor, an early Lennar strategic investment, are providing a liquid marketplace to sell and purchase entry level

homes with clean and safe digital engagement as they evolve and provide frictionless transactions.

With constrained supply, entry level and work force homes are trading faster and prices are moving higher. This enables yesterday's first-time buyers to sell for higher prices and more accumulated equity than expected, enabling them to seek and ultimately purchase larger, more spacious homes for their growing families and pushing demand and prices higher in those ranges as well thus enabling second-time homebuyers to do the same.

The positive demand-fed pricing cycle with far less friction has been activated throughout the housing market. The underproduction of homes for the past ten years has created a housing shortage and with strong demand the home prices are moving higher. Demand is growing as the Millennial Generation which postponed family formation over the past ten years has pivoted quickly and is making up ground towards traditional family formation trends.

Concurrently the proposition of home as more than shelter is becoming a hardwired way of life rather than a "COVID driven reaction". While these trends are exacerbating the well-documented affordability crisis across the country, as workforce housing is limited and getting more expensive the solution, it seems will be in growing supply by building more housing.

We are starting to see exactly that trend in this morning's ramp up – in the ramp up with today's starts and permits numbers. But we still have a lot to make up.

These conditions have given rise to strong though controlled sales pace, pricing power, very strong gross margin, even stronger net margin, managed costs and the challenge of land scarcity.

As it relates to Lennar's strategy in the current environment, we have controlled sales pace and matched it with production and our valuable land position. Our 16% sales growth is matched with and reflects our production and delivery pace while we increased starts 28% over last year, accelerated land development, and began purchasing additional land for the future as we look ahead to sustainable growth over the next years.

Of course, alongside our Homebuilding Team our Financial Services Group has contributed exceptional earnings while creating an ever better customer experience. While some had questioned our controlled and managed sales pace, the virtue of our strategy has been borne out by our 25% Fourth Quarter gross margin, our 17.4% Fourth Quarter net margin, our \$2 billion Fourth Quarter homebuilding cash flow, and our almost \$2.5 billion bottom line for the full year.

Additionally, our expected, sustained, and orderly growth in 2021 continues the story for the future. As we noted last quarter, we're expecting historically strong margins for the foreseeable future and throughout 2021. And we expect our bottom line to grow faster than our top line.

With confidence we expect to deliver between 62,000 and 64,000 homes in 2021 with between a 23.75% and 24% gross margin as compared to the 22.8% full year gross margin in 2020.

In the First Quarter of 2021, we expect to deliver between 12,200 and 12,500 homes with a 23.5% to 23.75% gross margin. Our program is rock solid and you can expect the cash flow and returns on capital and equity will continue to improve as well. Diane, of course, will give more detail in her comments.

Let me briefly turn to our Ancillary Business Divisions and our drive to focus on our core Homebuilding and Financial Services Business. While we continue to refine and grow our excellent Ancillary Business Divisions they are becoming a decidedly smaller part of the overall company picture. Retrospectively we are very pleased that we sold our Rialto subsidiary some two years ago, before we navigated the turbulence of this past year, enabling us to focus on our core business units.

As noted in past conference calls, we've been working on strategies to better position our blue chip multifamily platform called LMC along with our emerging SFR or Single Family for Rent platform as well as our strategic investment in Five Point, our California land development company, and our new technology investments platform which we call LENx.

As a head's up we are making progress on rationalization of these divisions and will give greater clarity on our specific strategy, as it is refined and becomes certain, over the next two quarters. This resolution is no longer a long-term strategy but is more immediate as we focus on driving higher returns with less noise in our numbers from lumpy profits and losses.

In that regard, we expect Opendoor to begin trading as a public company in the near future and we expect to record a cashless profit from appreciation in our investment in that platform, although we will not have an estimate of that gain until trading begins. We will be required to record a profit on the day trading begins, but upward and downward movements in the stock will be recorded quarterly, as quarterly marks and adjustments will flow through earnings. The company is not consolidated as we do not have a control position.

Opendoor pioneered the iBuyer space and, jointly, Opendoor and Lennar developed a seamless move up program that today is becoming an industry standard. By coordinating and redefining the move up buyer sale of their first home, while moving up to a larger home, the customer experience is becoming a frictionless, coordinated, and joyful engagement. And of course, less friction means more transaction and more transaction at a lower cost to all parties involved.

Needless to say, our well-known technology initiatives have contributed meaningfully to our readiness for current economic and structural shifts, while helping to improve our core business and drive our SG&A to a historic low of 8.1% for 2020. Concurrently our meaningful investments in technology companies have not only informed change within Lennar but are proving to be successful investments in their own right.

Once again we congratulate Opendoor on their successful migration from startup to maturity to public company and we welcome them in advance to the public market.

In conclusion, let me say that our results, and our expectations for next year, are solid in all respects, and they reflect our focused strategy to balance growth, margin, cash flow and return.

Today and for the foreseeable future the home is becoming more and more essential to the way we live and the quality of our lives. The home used to be just shelter! Now it's the hub of our entire life.

It is our shelter and our multiple generation's shelter. It is also our office, our gym, our recreation center, and our school. It is Wi-Fi connected and it is automated. It is sustainable and it is environmentally sensitive. It is both a

healthy home and a health system. Home is where families thrive in the best of times and a refuge in the toughest of times.

At Lennar we've never been better positioned financially, organizationally, and technologically to thrive and grow in this evolving and exciting housing market.

With that, let me turn over to Rick.

Rick Beckwitt: Thanks Stuart. As you can tell from Stuart's opening comments the housing market is very strong. Our team is extremely well coordinated and our financial results continue to benefit from a solid execution of our core operating strategies.

Topping that list continues to be improving our returns on capital and generating increased cash flow. With that in mind, we have been laser focused on increasing our percentage of optioned home sites and reducing our years supply of owned home sites.

During Fiscal 2019, we set a goal to have 40% of our home sites controlled via options and similar arrangements by the end of Fiscal 2021. At that time, our controlled position was about 25%. We entered Fiscal 2020 with 33% of our home sites controlled and ended this year at 39%, a 600 basis point improvement.

On a nominal basis this reflected an increase of over 15,000 optioned home sites during the year. This increase reflects the strength of our relationships with local developers and other strategic partners and their desire to work with us to increase our option position given our size and scale in our markets.

In Fiscal 2021, we expect to continue to expand on our existing relationships and enter into new regional and national land platforms to further enhance our land light strategy. Based on this progress we are in excellent position to achieve our revised goal of 50% controlled home sites by the end of Fiscal 2021.

During 2020, we also made significant progress on reducing our year's owned supply of home sites by 4.1 years to 3.5 years. This represented a reduction of over 22,000 home sites. Based on this progress we are on target to achieve our previously announced goal of a three year supply by the end of Fiscal 2021.

As expected the combined impact of increasing our controlled position, reducing our owned position and our strong profitability drove significant homebuilding cash flow. During 2020, we generated \$3.8 billion of homebuilding cash flow which enabled us to pay off \$2.1 billion in debt including prepaying all of our senior debt due in Fiscal 2021. This drove a meaningful improvement in our balance sheet as we ended the year with \$2.7 billion in cash, no borrowings under our \$2.4 billion revolving credit facility, and a homebuilding debt to capital and net debt to capital of 24.9% and 15.3% respectively both all-time lows.

As we continue to execute on our land light strategy, and if we achieve our 2021 improved yearend goals, we're positioned to continue to generate significant cash flow.

Now I'd like to spend a few moments talking about growth and community count. In Fiscal 2020, our community count declined by 8%. This was driven by an accelerated pace of sales and deliveries in our active communities, a decision to get out of the lower absorption, higher price point and lesser

performing communities we acquired from CalAtlantic, and a delay in opening new communities as we paused development activities during the initial stage of the COVID-19 pandemic.

Notwithstanding the 8% decline in community count we achieved a 16% increase in new orders in the Fourth Quarter of 2020 driven by a 27% increase in sales per community. While part of that increase in absorption pace was driven by improved market conditions, part of it was due to the fact that we targeted acquiring larger, higher volume, entry level communities that can deliver more homes per month than smaller communities.

As we continue into Fiscal 2021, our growth will continue to come from a higher overall absorption pace as well as an increase in community count. In 2021, our community count should increase by about 10% most of which will happen in the middle part of the year which should put us in great shape for the back half of 2021 and provide continued growth for Fiscal 2022.

While we continue to be focused on increasing our community count, we are intensely focused on replacing our existing communities with larger, higher volume communities as this allows us to better leverage our overhead, improve our bottom line, and increase our returns and our cash flow.

Before I turn it over to Jon, I want to echo Stuart's comments and thank all of our associates and our trade partners for an excellent year. Through your hard work and collaboration we accomplished many great things in 2020 and we are in excellent shape to execute on our core operating strategies in 2021.

I'd like to turn it over to Jon now.

Jon Jaffe: Thank you, Rick, and good morning everyone. Matching sales pace with our production pace has been a key strategic focus, has enabled us to drive excellent performance. By pairing production and sales we have maximized margins and driven bottom line profitability.

In the current environment, we've been able to maximize gross margin by systemically containing construction costs even while there's upward pressure. Additionally, we've been able to manage our SG&A lower thereby increasing our net margin and overall profitability.

I would like to briefly describe our strategy, performance and expectations for sales, production, and construction costs in order to shed some light on how the strategy has been essential to our accomplishments this quarter and in Fiscal 2020.

It begins with our time-tested Everything's Included Program so our trades and construction associates know exactly what they will be building and our customers know exactly what they are buying. We work with our strategic trade partners to value engineer our plans and rationalized plan count and skews to continuously simplify the supply chain and construction process. This proved to be extremely valuable in the current COVID disrupted supply chain environment. Virtually every manufacturer in our industry has had some level of disruption at the manufacturing facilities due to COVID.

Next, we focus on being disciplined and consistent about executing the most efficient production oriented machine in the homebuilding industry. The execution begins with setting even flow production rates at each community determined by a specific start pace and a product-based cycle time template which we call Level Scheduling. This pace can be adjusted upward or downward as the market requires.

A start and production plan for forward planning is then communicated to every one of our trade partners so they can plan for labor and material needs and efficiently deploy people and provide materials and products as needed. This forward communication in coordination drives efficiencies that do not exist in a more erratic and less predictable sales driven model.

By leading with a production first process we were able to quickly increase our start pace after pausing production in March and April to understand the impact of the pandemic in Q2. We were able to evaluate the improving market conditions and quickly increase our even flow production to achieve an average start pace of 4.3 homes per month per community in Q4 which was up from 3.4 in Q4 of '19, a 41% increase in pace. We expect to increase that pace to 4.5 homes per month per community in the first quarter and to maintain that pace throughout the year.

We then match sales at the community level to the community's production pace by using pricing and incentives to determine the exact market pricing for that pace and efficiently match sales to the pace of production. In other words, Lennar's sales pace is defined by our desired maximum efficiency production pace, not by momentary changes in market conditions.

The sales process is also disciplined and simple and is best described as FIFO or First In, First Out. The first home started in each community is the first home sold. And we move right down the line, plan type by plan type, avoiding selling too fast for our production pace by restricting what is available for sale to the management of our FIFO approach. By selling homes in the same order of our starts we manage the business to have our homes sold in time to – for our customers to receive their mortgage approvals prior to the home being completed.

Additionally, in today's robust selling environment this disciplined approach allows us to maximize our pricing power to increase both margins and cash flow and we end up carrying very few completed homes on our balance sheet.

In Q4, this approach drove our 25% gross margin and we ended the quarter with 0.7 completed inventory homes per community or just 776 homes for the entire company as compared to 1.6 homes per community or 2,086 homes in the prior year.

Balancing our sales pace with our production pace also helps reduce SG&A as fewer inventory homes helps lower our broker spend while creating greater efficiencies in our divisions through the even flow of sales, starts and deliveries.

More importantly, this balanced and predictable program is key to being builder of choice for the trades and to very effectively managing costs in a market defined by labor shortages and cost pressures.

In conclusion, Lennar's strategy of a managed approach to production and sales pace certainly proved its value in the back half of 2020. As we look to next year, we are certain that we will continue to drive higher gross margins, lower S&GA, higher net margins and a stronger bottom line as a direct result of this carefully managed strategy.

I also want to add my thanks to all of our associates and trade partners for all of their great focus and hard work in a year like no other.

I'll now turn it over to Diane.

Diane Bessette: Thank you, Jon, and good morning everyone. Although you've heard some of our financial results from Stuart, Rick, and Jon, I'll begin by recapping certain of our Q4 2020 highlights and then provide guidance for 2021.

So let's start with the balance sheet. There are three areas that I want to touch on, inventory, cash flow and debt. So starting with inventory, we executed on our strategy to become land lighter, improve returns, and generate increased cash flow. At quarter end we owned 187,000 home sites and controlled 119,000 home sites. This resulted in our year supply owned decreasing to 3.5 years from 4.1 in the prior year. And our home sites controlled increasing to 39% from 33% in the prior year. We continue to make progress in reaching our goal of 3-year supply owned and 50% home sites controlled by the end of Fiscal '21.

And then turning to cash flow, we generated \$2 billion of homebuilding cash flows for the quarter and \$3.8 billion for the year. Our confidence in our operating platform and ongoing cash flow generation enabled us to increase our annual dividend payment during the quarter to \$1 per share from 50 cents per share. This increase is one component of our overall strategy of focusing on total shareholder returns.

And then looking at debt, we continue to make progress with our strategy of reducing our debt balances and leverage ratio. Our strong cash flow generation enabled us to pay off \$1.2 billion of debt during the quarter and \$2.1 billion during the year. The fourth quarter included the early redemption of all senior notes which was approximately \$900 million that were due in Fiscal '21. With that payoff we now have no senior note maturity until Fiscal 2022. These actions combined with our increased equity base resulted in a yearend debt to total capital ratio of 24.9%. This is the lowest debt to total capital ratio we have ever achieved.

And just a few final points on our balance sheet, our stockholders' equity increased to \$18 billion from \$16 billion in the prior year and our book value per share increased to \$57.55 from \$50.49 in the prior year.

And finally during the quarter we were pleased to be upgraded by Moody's to an investment grade rating. This rating joins the investment grade rating previously received by Fitch.

So in summary, our balance sheet is very strong and we will continue to remain focused on generating long-term returns for our shareholders.

And so with those balance sheet highlights, let me now briefly review our operating performance starting with homebuilding. For new orders we ended the quarter with new orders of 15,214, a 16% year-over-year increase. And as we focused on matching sales and production our new order dollar volume was \$6.3 billion up 22% from the prior year.

Our sales pace was 4.3 for the quarter compared to 3.4 in the prior year. We ended the quarter with 1,177 active communities and our cancellation rate was 12%.

For the quarter, deliveries totaled 16,090 down 2% year-over-year. This was largely a result of the production loss to COVID-19 earlier in the year. Our gross margin was 25% up 350 basis points from the prior year. This was a result of strong pricing power which allowed us to increase sales prices and our continued intense focus on reducing construction costs.

Our SG&A was 7.5% as a result of creating an efficient operating platform and continuing benefits from technology. This is the lowest quarter SG&A

percent we have ever reached. This resulted in a net margin of 17.4% for the quarter which is the highest quarter percentage ever achieved.

And our Financial Services Team also executed at high levels reporting \$151 million of operating earnings. Mortgage operating earnings increased to \$125 million compared to \$57 million in the prior year. Mortgage earnings benefited primarily from an increase in volume through a higher capture rate of increased deliveries, 81% versus 78% last year, and a lower percentage of cash buyers combined with an increase in secondary margins.

Title operating earnings were \$28 million compared to \$23 million in the prior year. Title earnings increased primarily due to an increase in closed orders and a reduction in cost per transaction.

LMF commercial had operating earnings of \$1 million compared to \$3 million in the prior year due to lower securitization volume.

And with that brief overview, now let's turn to guidance. I'll first provide detailed guidance for the first quarter and then some high level guidance for the fiscal year starting with homebuilding.

We expect Q1 new orders to be in the range of 14,500 to 14,800 homes and our Q1 deliveries to be in the range of 12,200 to 12,500 homes. Our Q1 average sales price should be around \$390,000. We expect our Q1 gross margin to be in the range of 23.5% to 23.75%. Note this margin is lower than Q4 2020 due to the normal seasonal pattern.

As a reminder, we expense field cost in the current period so there is typically a headwind to Q1 gross margin as compared to Q4 gross margins due to the lower homebuilding revenues in Q1.

We expect our Q1 SG&A to be in the range of 8.9% to 9%. And for the combined homebuilding, joint venture, land sale and other categories we expect Q1 earnings of approximately \$5 million. We believe our financial services earnings for Q1 will be in the range of \$110 to \$115 million.

And for multifamily operations we expect a loss of approximately \$2 million to \$4 million.

For the other category related to the legacy Rialto assets and our strategic investments, we expect Q1 earnings of approximately \$5 million. We expect our Q1 corporate G&A to be about 2.1% to 2.2% of total revenues. The first quarter contains certain frontloaded expenses that will not occur in the remainder of the year. Our corp. G&A expense for the year should be consistent with Fiscal 2020.

We expect our tax rate to be approximately 25.3% and the weighted average share count for the quarter should be approximately 310 million shares.

And so when you pull all this together this guidance should produce an EPS range of \$1.64 to \$1.74 per share for the quarter.

And now turning to the Full Year Fiscal 2021, here are a few high level guidance points. We expect to deliver between 62,000 and 64,000 homes with an average sales price for the year of approximately \$386,000 to \$388,000.

Our Fiscal '21 gross margin is expected to be in the range of 23.75% to 24%. We expect continued price appreciation and leverage from field expenses throughout the year somewhat offset by higher lumber and other anticipated cost increases.

Our Fiscal '21 SG&A should be in the range of 7.8% to 8%. And we expect our community count to grow 10% by the end of the year. Financial services earnings should be in the range of \$400 to \$425 million and we expect our tax rate to be approximately 25.3%.

And finally, before I turn it over to the operator, I'd like to say thank you to the accounting and planning teams whose hard work and focus enabled us to hold our yearend conference call today, December 17th, two and a half weeks after yearend. Thanks to all of you. It is very much appreciated.

And with that, let me 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 1, unmute your phone, and record your name clearly. If you need to withdraw your question press Star 2. We ask that you limit yourself to one question and one follow-up question until everyone has had the opportunity to have their question answered. Our first question comes from Stephen Kim with Evercore ISI. Your line is open.

Stephen Kim: Thanks very much guys and congratulations to everyone for, you know, your strong performance. And your guidance was also, you know, extremely interesting for us. Many aspects of the guidance, you know, were very positive and the one area that I was curious about trying to gauge the level of conservatism that you've incorporated is in your ASP guide for closings.

I observed that your order price ASP rose almost 3% sequentially from the third quarter. You know, that would seem to suggest that because I assume there was some mix shift in that negative mix shift, I assume that that means that like for like pricing is up, you know, about at least 1% per month in the quarter.

And I was curious if this level of like for like pricing accelerated throughout the quarter or not and if so if you could provide a little bit of color on the closing ASP guidance which I think is looking for a decline. I assume that's mixed but I just wanted to ask the question.

Diane Bessette: Yes Steve, I'll answer that. So a couple of points. If you look at the ASP and new orders for the third quarter remember some of that did close in Q4. So that was part of, you know, the ASP in Q4.

Additionally if you look at the ASP in backlog, which is around that same range, note that the number of homes in backlog is about 30% of the midpoint of our guidance. So the point there is that while some of that will bleed through, there are other communities coming on and quite a few during the year or those that have not started producing new orders yet that are lower down the price point as we continue to really focus on affordability.

And so while what you're seeing is a small snapshot of what you'll see in the quarter, there are other pieces - I'm sorry those - a small snapshot of the year, there are other pieces that will migrate that price down.

Stephen Kim: Got it, great. Could someone comment on the like for like pricing though that we saw in the quarter? It would I would assume that you probably saw at least 1% per month. Can you give us some color around that?

Rick Beckwitt: Yes I'm not sure we're going to give a percent Steve but we did see like for like pricing throughout the quarter.

Stephen Kim: And did it accelerate at all Rick?

Rick Beckwitt: It was a gradual increase through the quarter Steve.

Stuart Miller: You know but let's just say Steve you're clearly seeing pricing power. So when you look at like for like you're definitely seeing acceleration as we went through the quarter. Just remember that we are - we have been focusing on entry level a little bit more although that upward spiral in demand, entry-level giving like to move up and move up to second move up is taking place at the same time so we're balancing our product offering.

So everything that you're seeing is part of averaging including the like for like increases that we're clearly seeing through the quarters as we - and as we go forward.

Stephen Kim: Great. That's - thanks Stuart. That's kind of what I was looking for.

Second question relates to capital allocation. It seems clear from your opening remarks and just the results the company is moving to a higher level of profitability here for the foreseeable future with controlled land spend and an already pretty under leveraged balance sheet. And meanwhile you've got the multifamily and the other ancillary business platforms that seem to be if anything nearing a harvesting stage.

So bottom line the question of what you're going to do with all this cash flow and the cash that you're going to be having is becoming very relevant. You already, you know, retired a lot of the debt that we had coming up.

So how should we be thinking about your plans for capital allocation? And specifically I'm curious as to how you think about the appropriateness of a stock buyback -- an increase or an acceleration in your stock buyback program?

Stuart Miller: So let me start by saying - thank you for pointing that out because that's exactly what we're focused on. I hope your hearing a great deal of confidence in our operating platform and what we think is going to happen with our profitability and our cash flows and our migration and land position through 2021 because it does suggest and indicate that our cash position will continue to accelerate.

So the starting point in our office here is to focus on total shareholder return. And I think that we're - we are laser focused on thinking about and you see in the beginnings of that with the increase of our dividend. We weren't shy about that. We recognize the cash flow that we were seeing and its direction and we made a migration in dividend last quarter.

You've seen that we have accelerated some of our debt reduction which only tends to delever the company. And some might say that we're under levered. We're not apologetic about that.

But at the same time the cash flow that we are witnessing gives us a myriad of opportunity together with our ancillary businesses to think about how we generate higher returns.

As I said in my comments, you're going to hear more about this over the next couple of quarters. But a stock buyback is clearly not off the table and it is something that we're looking at as we look at how we generate higher returns as we move forward. But I hope you're hearing that there is a great deal of confidence in our earnings and cash flow picture right now.

Stephen Kim: Great. Thanks very much Stuart and good luck.

Stuart Miller: Okay thank you.

Coordinator: Thank you. Our next question comes from Alan Ratner with Zelman & Associates. You may proceed.

Alan Ratner: Hey guys, good morning, congrats on the really strong results. I'm glad to hear everyone is doing well on the line there.

Stuart Miller: Thank you.

Alan Ratner: You know, Stuart I apologize, my audio cut out for a minute or two during your comments so if you addressed this I apologize.

But a few years ago you kind of threw out a, you know, a longer term growth target of I think it was about 5% to 7%. And, you know, part of that I think was where you maybe saw the market going. But I think more of that was just where you felt the business was most efficient in terms of growth over a longer time period.

And I'm curious based on kind of, you know, some of the guidance you've given for next year sounds like your ramping your production to 4.5 starts, you know, per month which would imply something, you know, well in excess of that type of growth level.

And I'm just curious based on what's transpired this year with COVID and some of the demographic tailwinds that you're seeing whether that target range has shifted higher and you think of that perhaps the business can grow efficiently and perhaps at little bit of a stronger growth rate than that?

Stuart Miller: Good fair question Alan. The reality is that in an orderly and an orderly growth market as we were witnessing going into 2020 we felt that the

appropriate growth level and given our cash flow and returns focus was in that, it was actually 4% to 7% range.

But as COVID came into the market paused us and then accelerated the housing market, production levels and the needs of the homebuilding business in general have accelerated rather dramatically. And we have clearly adjusted our growth targets.

So what you're seeing for next year is between the 15% and 20% growth rate that we've embraced and we are focused on going forward. And we are continuing to use, you know, market driven indicators to define our growth rate as we go and work towards 2022.

If you look at the indicators right now, we're probably on target to be growing at a similar rate for 2022 so you'd have to put aside that 4% to 7% range because we're going to have to find a way and the industry's going to have to find a way to grow at an accelerated pace as we are supply constrained. And the market is just calling on the homebuilders to produce more and to produce more affordable housing.

So we're a part of that picture. You saw it in starts and permits this morning a surprise to the upside. We're starting to get to that million and a half level production. It's probably weighted a little bit more towards multifamily right now but single-family seems like it's going to follow suit. And we're just going to need more dwellings in the country. The appetite for housing is accelerating.

Alan Ratner: That's really helpful.

Jon Jaffe: And this is Jon. I also would add to Stuart's comments that as we focused on simplifying our product offering and our production machine it's also enabled us to really keep what we view as a maximum efficiency level at a higher pace. We're doing this with smaller product lower price point and just an overall more efficient production operation.

Alan Ratner: Great. No, I appreciate both of your comments there. And I think it dovetails a little bit into my follow-up which is, you know, your strategy this year I think has certainly been extremely prudent and you're seeing the benefits of that on your gross margin.

And Jon I appreciate all your comments about the, you know, kind of digging into the weeds a little bit on the moving pieces there on maintaining that consistent production level.

On the other side, you know, some of your competitors have been much lumpier in terms of their growth rates. And I think as we look at the backlogs across the industry for example and, you know, what's poised to be a huge step up in production in order to satisfy that demand it kind of feels like there's going to be some stress on the supply chain as we roll into '21.

And while you're managing your business effectively do you anticipate any repercussions from that? You know, what I'm really thinking about is labor inflation, you know, potentially the dynamic we saw a few years ago where builders were kind of stealing trades off of each other's jobsites to get homes built and delivered on time.

Do you think there's any risk to your business as a result of what you're seeing from other builders right now?

Jon Jaffe: I think there's no question as I mentioned my comments that the environment we're in today is defined by, you know, labor shortage and pricing pressure. But we've heard consistently from us for many, many quarters now about our focus on our builder of choice strategy.

And that's holding us in really good stead and being able to coordinate a forward plan with our strategic trade partners and to really manage and offset the cost increases that are out there in the environment and more importantly the predictability of our labor needs and be able to think way ahead with our trades as to those needs so they can properly plan and be ready for us.

Stuart Miller: Let me add and say that what you see and from us is a very steady hand, steady through the noise. Other builders have produced higher growth rates and sales paces. And we stayed focused on our business plan, our strategy. And I think it's a steady program that enables us to maximize the engagement with the supply chain and to remain consistent.

And I think, you know, that it - Jon and Rick have been a steady rudder through those waters and I think it's going to continue to reflect on strong bottom-line, strong cash flow and a lot of predictability.

Alan Ratner: Great. Good luck guys and happy holidays.

Stuart Miller: Thank you. You too.

Coordinator: Our next question will come from Carl Reichardt with BTIG. Your line is open.

Carl Reichardt: Thanks, morning everybody. Thanks for all the color today. Diane it's nice that you get your first I think January 1 off ever.

Stuart I had a sort of bigger picture question for you is as the vaccine, the COVID vaccine is distributed out and moves through the country hopefully quickly I think we might anticipate some shift in consumer expenditures back to all the things so many consumers have not been able to buy and do for the last year or so. Are you anticipating if that happens for there to be a negative impact on expenditures on housing and if so, how will you recognize and react to that?

Stuart Miller: No, well first of all I do hope that there is going to be a shift back to the restaurants and the movie theaters and the vacations. I think that, you know, a robust economic recovery requires some of that reversion to, you know, normal lifestyle. So I'm optimistic that there will be a kick back to normalcy.

But I don't think that that's going to have a negative impact, I think it's going to have more of a positive impact on the housing market. I think that, you know, interest rates are low and they're going to remain low. Stimulus money will come through the government. I believe that it will and I can't prove it but I think so.

And I think that a stronger economy and a broader based strong economy is going to be better for housing. I think that the current strength in the housing market derives from both the Millennial generation really kicking into high gear and family formation. And frankly in an awkward way COVID has facilitated that accelerating.

And then of course the COVID driven recalibration for how people are using their homes. I think there will be some stickiness to some of the habits changed.

So, you know, I think overall we've all learned some new habits and some new customs and tricks. But I think a lot of it revolves around having a home of your choice and having your home be the hub of your life. And so I'm pretty optimistic about where the housing market is over the next year.

Remember Carl that over the past ten years we have been under producing housing. And we're going to have to make up ground there. So for the foreseeable future I think we're going to see strength in the housing market.

Carl Reichardt: Great thank you for that Stuart. And then...

Stuart Miller: Sure.

Carl Reichardt: ...Jon or Rick can you talk a little bit about the evolution of the FIFO inventory release match to sales? And I'm kind of curious if that is becoming more of help to governing your sales rate than just raising prices to try to slow sales down? It's was an interesting walk through Jon. I'm just kind of curious how it's evolved and if it's companywide and how it's working to maximize margin and pace at the same time. Thanks very much all.

Jon Jaffe: Sure I'd be happy to address that. So our FIFO pricing and sales strategy is not something new or COVID related. We established this process in one of our divisions out West in Reno and really fine-tuned it and saw its effectiveness in not just maximizing pricing power but really creating efficiencies throughout the process that affects every part of what we do.

We actually rolled it out at a division president's meeting about two years ago and started with the pilot divisions, saw its effectiveness in all different types of markets and have rolled it out throughout the entire company. So this exists in every one of our divisions.

And it to your point, it isn't just about maximizing pricing power by having a limited number of homes available. It really allows us to very carefully manage and match that sales pace to production pace. And so to be very forward-looking about any adjustments that we need to make in pricing in the sense it's up or down as the case might be to very meticulously manage that pace. And it just creates consistency and even flow that affects really your G&A levels to be level instead of having to be positioned for peaks and valleys.

Carl Reichardt: Great, thank you Jon and thanks everybody -- happy holidays.

Stuart Miller: Thank you Carl.

Coordinator: Thank you. Our next question comes from Truman Patterson with Wells Fargo. Your line is open.

Truman Patterson: Hi. Good morning everyone. Let me add nice results as well. So the question on cash flow.

You know, you all generated \$3.8 billion in builder cash flow on net income of only, you know, I think \$2.4 billion this year. When we're looking out to 2021 how should we think about the free cash flow conversion of net income?

And clearly there, you know, likely a handful of moving parts between continuing to bring down your owned lot supply, reinvesting an optioned land, et cetera, and possibly, you know, rebuilding some of that spec pipeline? Hoping you can walk us through some of the moving parts there?

Stuart Miller: Yes, so yes I'm going to ask Rick to weigh in on this but before he does let me just say that, you know, we've learned that there are some tricky parts of

the calculation and the guidance that we can give. And we recognize that cash flow is one of those.

You know, growth at a higher level is a headwind to cash flow. The migration of land from owned to controlled a greater percentage and a lower year count is a tailwind to cash flow. So we've been careful not to lay out, because the parts will move around, to layout specificity. But go ahead Rick.

Rick Beckwitt: No, I'm not going to answer that Stuart because that's a mouse trap. I guess all I would say is as we continue to morph and execute on reducing the years owned and that gets into option, there's no doubt that that is a significant generator of cash.

And, you know, the unknowns as Stuart has identified and as you have appropriately pointed out is as we build the level of inventory to ramp up to that 62,000, to 64,000 home delivery pace, you know, that's a reinvestment of cash. And so there's a lot of moving pieces in here. And I'm sure Diane will give you more color on this in the follow-up calls.

Stuart Miller: But look let me say this. As we look ahead to 2021 we have a great deal of confidence that our cash flow is going to be very strong. You're absolutely right, this past year we earned just under \$2.5 billion net income and drove \$3.8 billion in cash flow. Some of that is migration of our land strategy.

That land strategy is going to continue through 2021. So we're fully expecting that we're going to have very strong cash flow through the year but we're not guiding in specificity.

Truman Patterson: Okay, okay. And just real quickly on that owned land supply, do you think you can bring it down below three years eventually?

Rick Beckwitt: I think that, you know, if you look at where we started at over four and the transformation that we've had in a very short period of time we're really enthusiastic about getting to three and we're just going to have to see how low we can get it. There's definitely a possibility to get it below three, definitely a possibility.

Truman Patterson: Yes. Sure.

Rick Beckwitt: You know, we, you know, but there's a balance because we have some markets, particularly the Western markets that in order to be a big large player in those markets you have to self-develop. So Jon has done a great job. Jon and the team have done a great job in working through and creating some very unique structures to help us get there. And so I would just say stay tuned.

Stuart Miller: And I think that the laser focus of the management team is to think about land and the system around land as a just-in-time delivery system and we are going to get closer and closer to that aspiration.

Truman Patterson: Okay that's very helpful. Second question on gross margins. You know, you all have focused on driving pricing to kind of cap absorption and, you know, cover the FIFO costs if you will more than other builders. And clearly based on your gross margin guidance it appears your homes are selling at a premium in the market.

You know, this might be hard to quantify or a bit of an unfair question but is there any way you could possibly quantify, you know, what magnitude your homes might be selling at a premium? And as we move forward is kind of market conditions potentially normalize where there's a bit more balance between supply and demand do you think that premium potentially shrinks over time?

Stuart Miller: I don't think it's so much a premium as I think it's an orderly process that is driving the average higher. And so I think we're competing in a market where customers understand what the value proposition is. I think it's just process driven that we are just driving a higher sales price by an orderly process of production and sales.

And so I wouldn't think of it as a like kind premium. If you go out to the market and look at our 1,500 or out 2,000 square-foot homes next door to someone else's I think it's just a matter of process.

Rick Beckwitt: And I think our product strategy our everything's included program makes it much easier for our customers to make a buy decision because they don't have to make any choices and that's a big differentiator.

Jon Jaffe: And I would just briefly add that when we think about our FIFO strategy we price to market, what the market will bear, not to what our competitors are pricing.

Truman Patterson: Okay thank you all. And good luck on the upcoming quarter.

Stuart Miller: Thank you very much. Let's take one more question.

Coordinator: Our question comes from Michael Rehaut with JP Morgan. You may proceed.

Michael Rehaut: Thanks. Thanks for sneaking me in, congrats everyone and glad to hear everyone is doing well. And congrats to Allison as well, Allison Bober, great to hear the news there.

The first question just around gross margins. You know, great success there and a real realization of the price over pace strategy or, you know, steady pace

and driving price. You know, wanted to delve in a little bit too, if you can kind of break down the upside in the 4Q results, where that came from, if it was more just, you know, better than expected pricing power during the quarter or mix.

And then as you look into '21, you know, it seems like you're, the guidance would imply, you know, 4Q margins down year over year, you know, as we get towards the end of the year. And I just didn't know if there was any conservatism there. And you had mentioned, you know, lumber and maybe labor inflation but historically, you know, when you're in an inflationary, cost inflation environment you're able to at least offset that with future pricing power oftentimes as we've seen in the past.

So kind of a two-parter there again first drivers of the 4Q upside and then, you know, how to think about margins in particular the back half of '21?

Stuart Miller: Rick?

Rick Beckwitt: I guess I'd say with regard to the overall gross margin guidance for the year and the trajectory through the year I'd really like to start off by pointing out that there's a huge over 100 basis point year over year increase in the gross margin guidance. And, you know, there are certainly are some things that are impacting the margin as we work through it.

One is, you know, lumber did increase pretty dramatically and we're now in the throes of dealing with that although we've done a great job in offsetting by raising prices.

The other driver is the overall increase in our optioned deliveries. You know, by increasing the share of optioned versus controls we have a tendency to

have a little bit lower margin, gross margin on that because someone else is taking the risk of owning that land. And so I don't think you'll see quite as much, you know, drive throughout the year as we've seen in past because of those two things.

Michael Rehaut: And then on the - thank you for that Rick and then on the 4Q upside?

Stuart Miller: I think there's an adequate amount of conservatism as we look out four quarters. We're going to have to wait and see how the pricing power plays through. And so, you know, I think we tried to give a lot of detailed guidance and some directional guidance for the - detailed guidance for the first quarter and directional guidance for the year.

And as Rick notes, you know, our averages for the - our average for the year is 100 basis point improvement which is sizable. We'll have to see how pricing power meshes with production costs.

Diane Bessette: And Mike and I probably would just add in Q4 2020 it was if you look on a per square foot basis it was equally split with increase in the ASP per square foot with, combined with equal decrease in construction cost per square foot, so pretty balanced between both of them.

Michael Rehaut: Okay appreciate it. And, you know, secondly Stuart I heard and was paying attention here in one of your answers addressing, you know, closings growth for '21 and I believe it was talking around, you know, prior kind of growth outlooks in may be mid-single digit area. And now we're looking at 21% and 15% to 20%.

I believe you had said that you could do a similar growth rate in 2022 which is, you know, at this point also, you know, solidly above, you know, consensus estimates and where the street is and probably most investors.

I just wanted to, you know, revisit that comment and if that was, you know, talking more just to, you know, your production potential and, you know, what you think you can, you know, kind of further drive through your infrastructure or, you know, based on, you know, community count growth and your shift to higher turning or I'm sorry higher volume communities that this is more of, you know, 15%, 20% growth rate based on, you know, again your community count pipeline and obviously assuming, you know, a continued, you know, steady or improving market you indeed are looking at something of a higher growth rate continuing into '22? Just wanted to, you know, get a little more definition on that comment.

Stuart Miller: Well listen Mike let me start by saying thank you for listening carefully to the things that I say, not everybody does that. And I just want to appreciate the fact that you were listening carefully. So you're exactly right, I said what I said and I said what I meant.

If you think about what we have daylighted in the entirety of the call today we have daylighted an expectation that our community count will be growing through 2021. We have daylighted that we are focused on more productive larger communities producing higher volume rather than smaller incremental communities.

We have daylighted that some of our community count has dissipated as we have worked through some of the smaller less productive CalAtlantic communities and closed them out.

The - we have daylighted our matching production together with our sales pace and migrating our production pace upward over the course of this year over the next quarter even.

We are ramping up not just our productivity per community but the style of community that we're tending to purchase. And if you kind of bring that forward through 2021 into 2022 you can't help but unless the market tells us and data tells us to tone down or turn down the spigot you can't help but start to think and project forward that '22 will continue a growth trajectory that is somewhat similar. And we're building a greater confidence in our ability to look ahead and to do that assuming market conditions remain strong.

Then going back to my comments in the opening I think that if you think about the confidence that we are projecting about market conditions thinking about a ten year hiatus or production deficit that underlies the current market conditions and the general growing demand with limited supply for the foreseeable future the market is asking us to grow at a greater growth rate and we're building confidence that we're going to be able to meet that challenge.

So you heard me right. Thank you for listening and that's exactly what we intended to say.

Michael Rehaut: Great. Thanks so much Stuart and good to talk to everyone. Have a great holiday season.

Stuart Miller: Great and I guess in closing we'll say happy holidays to everybody. Thanks for joining our year end call and we look forward to updating in the future. Thank you.

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