Beazer Homes USA Inc.

NYSE:BZH

Analyst: Andrew Varone
Sector: Consumer Discretionary

BUY

Price Target:$8.39

Key Statistics as of 5/5/2016

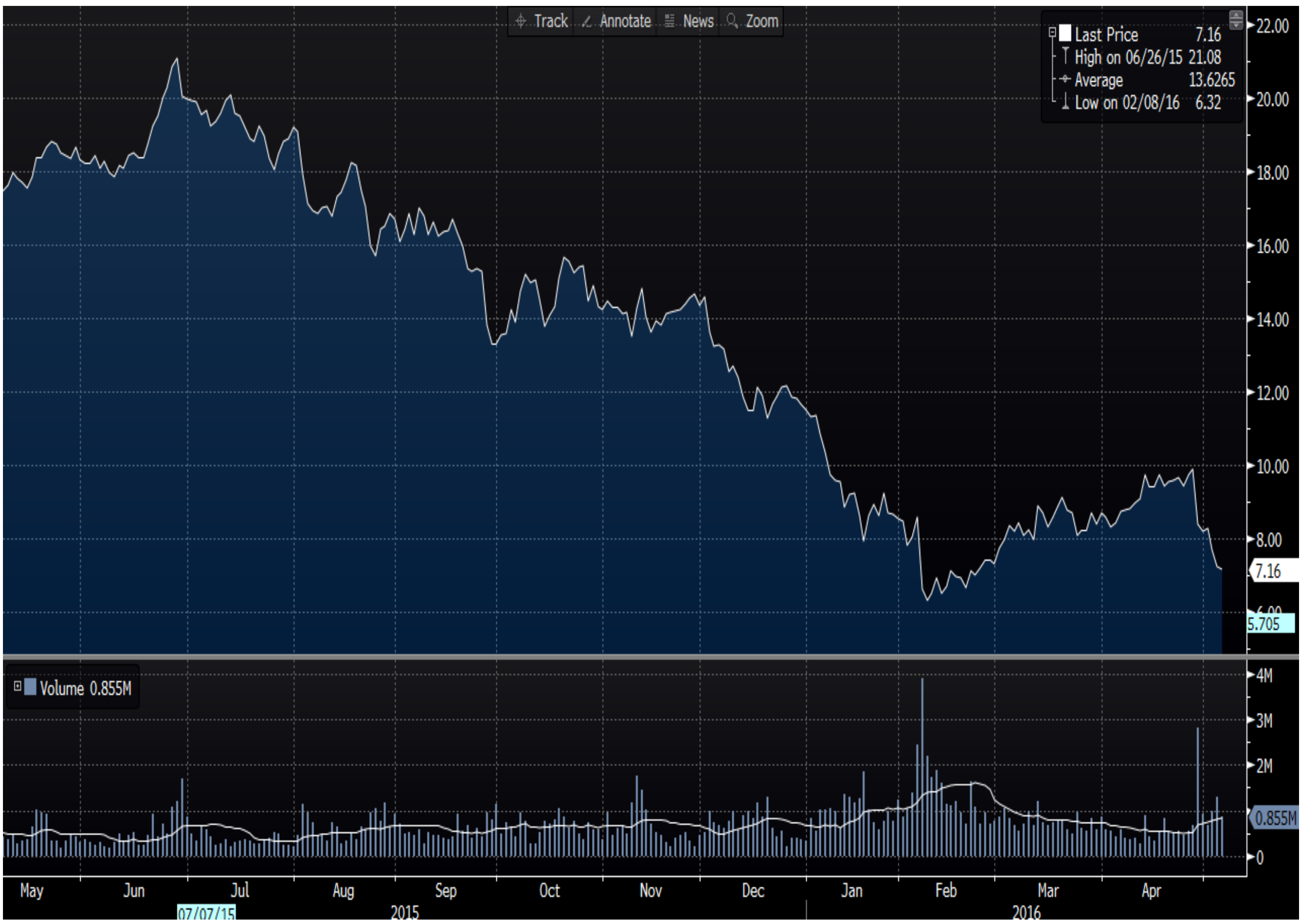
Market Price:	$7.16
Industry:	Household Durables
Market Cap:	$227.76M
52-Week Range:	$6.07-$21.19
Beta:	0.60

Thesis Points:

- Millennials, one of the biggest generations, are entering the housing market.
- With interest rates increased set for June and the recovering of the economy, ideal time for buyers to purchase a home.
- Undervalued due to slow recovery and negative speculation from investors.
- Improving income statements based on the repayment of outstanding debts.

Company Description:

Beazer Homes USA, Inc. operates as a homebuilder in the United States. They design, build and sell single-family and multiple homes in the United States. Their main geographically segments are in the West, East and Southeast regions.



Thesis

Beazer Homes USA is a designer, building and seller of single-family and multiple homes in the United States. They produce homes in Arizona, California, Delaware, Florida, Georgia, Indiana, Maryland, Nevada, North and South Carolina, Tennessee, Texas and Virginia. The stock price is currently near its 52 week low and provides a key entry point to those looking to invest. The growth will be driven by macroeconomic conditions that will improve revenues through the demand for homes. With a current price of $7.16, Beazer Homes USA is considered a BUY. With a one-year target of $8.39, a return of over 17% can be experienced.

Porter's 5 Forces

Threat of New Entrants: Low
There are high capital requirements that are need for building houses. There is also holding cost that is associated with holding all of the raw materials needed to build homes. There is a learning curve that is present due to the demand for skill labor to start building houses. Lastly, there is high risk associated with construction. If not even homes are build and sold in a certain amount of time, the possibility of bankruptcy is likely.

Threat of Substitution: Neutral
As technology has advanced, there have been more innovative ways to build homes that are cheaper. Contrary, when steps are skipped in making homes, and costs are reduced there can be an impact on the quality of the homes that are produced. Consumers may be willing to pay extra to have a better quality home.

Bargaining Power of Suppliers: Low
A lot of members of the construction industry have either integrated backwards or build up relations with suppliers that make them readily available. There is low switching costs that are present when going from one supplier to another. Lastly, construction materials are readily available and there are a lot of suppliers ready to sell their materials.

Bargaining Power of Buyers: High
There is a multitude of contractors to build homes and do renovations. This means that the buyer can price shop and find the lowest or best deals that suits the consumer's needs. Lastly, if they are rebuilding all or part of a building that is covered by insurance, the insurance company has the say in what rate will be paid to contractors.

Competitive Rivalry: High
Construction companies are in rivalry with each other, competing in order to win contracts. The industry is overcrowded with many small construction companies and a few larger ones.

Millennials Buying Power

There has been a slow recovery for the housing market. This is about to change as the Millennials are about to be one of the largest generations to enter the home buying ages. The Millennials age range from those born in the early 1980s to 2000. They are currently the largest group of individuals that make up the United States population, 25%. The vast majority of Millennials are going to be turning 25-26. This is the average age that most people get married which means that the housing market will be driven by this. Lastly, the Millennials are the most educated generation based on the percentage that went to college. Higher education translates to higher pay which mean Millennials will be able to afford more expensive houses than previous generations. This bodes well for the housing industry as more expensive houses can be sold. Currently, home ownership is around 4% below its historical average. It is forecasts that the number of single-family homes will double from 645,000 in 2014 to 1.1 million in 2019.

New Home Sales

There are two economic types of home sales, new home sales and existing home sales. For a construction company, the number of new homes sales is more important than existing home sales as there are more revenues to be made. Since the recession, new home sales took a huge hit. The number of buyers is starting increase faster than the number of sellers. This means that some individuals are in the market for new homes.

This is a graph taken off FRED based on new home sales over the past five years. As can be seen, the number of new home sales has been increasing and has hit its highest point as of this last month. This trend is likely to continue as discussed earlier, more people are entering the market for homes.

Interest Rate Increases

The Federal Reserve set interest rates to 0% in response to the Great Recession. This was done through quantitate easing and setting the federal funds rate to 0%. With the economy improving, the Federal Reserve has stated that they plan on increasing the federal funds rate. It was supposed to occur four times this year in 2016 but, they decreased it to two increases in 2016. The first increase of 2016 is set to take place in June. This will make future homebuyers eager to buy homes sooner than later and experience lower rates on their mortgages. This will help expand revenues in the near future.

Backlog

With anything to do with construction, there will always be backlog that builds up from the orders of houses. Backlog can have positive and negative implications. The positive implications are that there is sustained revenue growth for the future. If they do not have any more orders for housing in the upcoming year, they will still generate revenue based on the backlog that they have. The negative implication is that oil is its cheapest currently. If it takes a while to complete these projects, the price of oil could rise. The rise in the price of oil will also cause a rise in the price of all raw materials. This is problematic as it will squeeze and lessen margins.

		Q2 FY15		Q2 FY16
Quarter Ending Backlog (units)		2,533		2,300
Quarter Ending Backlog ($ in millions)	$	814.5	$	772.7
ASP in Backlog ($ in thousands)	$	321.6	$	336.0
Quarter Beginning Backlog		1,771		1,912
Scheduled to Close in Future Quarters		(914)		(953)
Backlog Scheduled to Close in the Quarter		857		959
Backlog Activity:				
Cancellations		(91)		(86)
Pushed to Future Quarters		(124)		(105)
Close Date Brought Forward		33		97
Sold & Closed During the Quarter		261		285
Total Closings in the Quarter		936		1,150
Backlog Conversion Rate		**52.9%**		**60.1%**

As seen here, Beazer Homes did a better job at completed backlogged jobs and had a better backlog conversation ratio than a year ago. The leader driver was their ability to pick up production and finish houses faster than the previous year. Though some backlog will occur because a house cannot be built over night, being able to produce a house faster and reduce backlog will be beneficial in improving margins.

Undervaluation

BZH has seen a large decrease in its stock price which has left it undervalued. The current macroeconomic conditions have set it up to see an increase in its revenues over the next few months. A lot of investment firms have downgraded their ratings of BZH despite it being at its most attractive entry point. With the stock price around $7, there is little downside and great upside if BZH can continue to improve its financial position.

Financial Statements

On the balance sheet side, BZH has started to reduce leverage that they currently have. They have fully paid off their 2016 notes and have retired more than $41 million in net debt. This has saved them more than $6 million in interest rate expenses.

Improvements on the income statement are led by an increase in the price of a new house sold is. The increase from a year ago is just above $20k rising from $306k to $328k. This is an increase of 7.3%. This increase can help the company to see an increase in their margins.

Conclusion

Beazer Homes USA is a designer, building and seller of single-family and multiple homes in the United States. Due to favorable market conditions, the housing industry should continue to improve. This is due to the Millennials entering the housing market and wants to purchase homes before the next federal funds rate increase that will come in June. Beazer Homes USA has also been to improve on their backlog numbers and reducing their debt will help increase income based on paying lower interest rates.

Beazer Homes USA Inc. (BZH)

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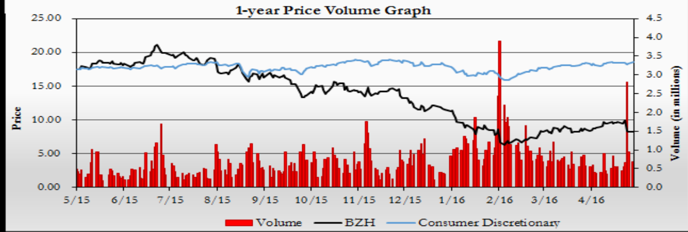
NEUTRAL

Analysis by P.C. Principal	Current Price:	$7.16	Intrinsic Value	$6.02	Target 1 year Return: 17.21%
5/5/2016	Divident Yield:	0.0%	Target Price	$8.39	Probability of Price Increase: 72.5%

1-year Price Volume Graph



Description

Beazer Homes USA, Inc. operates as a homebuilder in the United States.

General Information

Sector	Consumer Discretionary
Industry	Household Durables
Last Guidance	November 3, 2015
Next earnings date	July 28, 2016
Estimated Country Risk Premium	6.00%
Effective Tax rate	40%
Effective Operating Tax rate	51%

Market Data

Market Capitalization	$227.76
Daily volume (mil)	0.85
Shares outstanding (mil)	31.81
Diluted shares outstanding (mil)	34.43
% shares held by institutions	78%
% shares held by investments Managers	61%
% shares held by hedge funds	25%
% shares held by insiders	3.72%
Short interest	17.76%
Days to cover short interest	6.28
52 week high	$21.19
52-week low	$6.07
Levered Beta	1.92
Volatility	56.99%

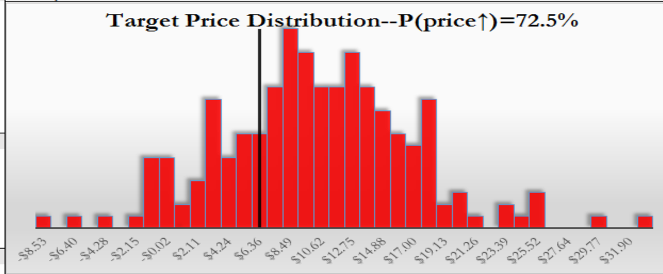
Past Earning Surprises

Quarter ending	Revenue	EBITDA
3/31/2015	1.15%	-85.16%
6/30/2015	-18.64%	-72.22%
9/30/2015	-6.36%	N/A
12/31/2015	5.98%	-116.77%
3/31/2016	-0.84%	N/A
Mean	-3.74%	-91.38%
Standard error	4.2%	13.2%

Peers

MDC Holdings Inc.
Meritage Homes Corporation
M/I Homes, Inc.
CalAtlantic Group, Inc.
Hovnanian Enterprises Inc.
KB Home
William Lyon Homes
Lennar Corporation

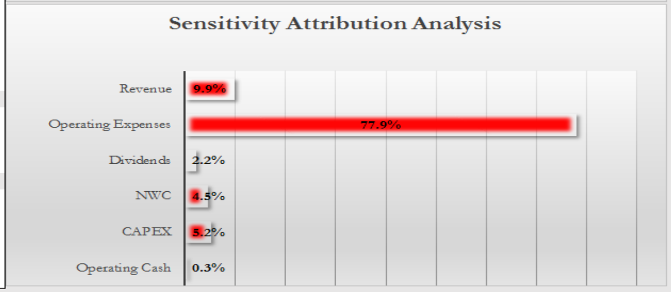
Target Price Distribution--P(price↑)=72.5%



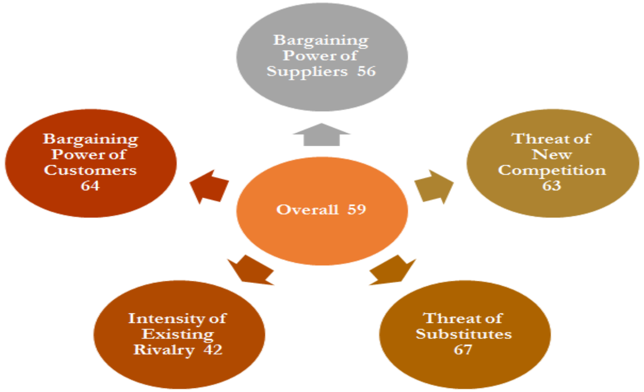
Management	Position	Total compensations growth	Total return to shareholders
Merrill, Allan	Chief Executive Officer, Pre	13.08% per annum over 5y	-14.85% per annum over 5y
Salomon, Robert	Chief Financial Officer, Chi	23.83% per annum over 5y	-14.85% per annum over 5y
Khoury, Kenneth	Chief Administrative Officer	8.17% per annum over 5y	-14.85% per annum over 5y
Goldberg, David	Vice President of Treasury &	N/M	N/M
James, Kathi	Chief Marketing Officer and	N/M	N/M
Gates, Jerry	Head of California, Los Ange	N/M	N/M

Profitability	BZH (LTM)	BZH (5 years historical average)	Industry (LTM)
ROIC	0.8%	-6.24%	9.00%
NOPAT Margin	1%	-7.01%	7.7%
Revenue/Invested Capital	0.92	0.89	1.17
ROE	-18.1%	-86.74%	10.89%
Adjusted net margin	0%	-10.35%	6.5%
Revenue/Adjusted Book Value	165.14	8.38	1.67
Invested Funds	**BZH (LTM)**	**BZH (5 years historical average)**	**Industry (LTM)**
Total Cash/Total Capital	6.8%	17.2%	11%
Estimated Operating Cash/Total Capital	6.8%	6.2%	N/A
Non-cash working Capital/Total Capital	82.5%	71.2%	33%
Invested Capital/Total Capital	99.5%	87.7%	84%
Capital Structure	**BZH (LTM)**	**BZH (5 years historical average)**	**Industry (LTM)**
Total Debt/Common Equity (LTM)	5.39	3.59	0.28
Cost of Existing Debt	9.66%	11.41%	3.58%
Estimated Cost of new Borrowing	3.77%	4.77%	3.58%
CGFS Risk Rating	BB	CCC	BBB
Unlevered Beta (LTM)	0.60	0.55	1.21
WACC	8.00%	9.10%	10.39%

Sensitivity Attribution Analysis



Porter's 5 forces (scores are out of 100)



Valuation

Period	Revenue growth	NOPAT margin	ROIC/WACC
Base Year	22.3%	0.8%	0.09
3/31/2017	5.4%	8.0%	0.96
3/31/2018	6.4%	7.9%	0.97
3/31/2019	6.1%	7.7%	0.97
3/31/2020	5.7%	7.5%	0.95
3/31/2021	5.2%	7.3%	0.94
3/31/2022	4.7%	7.2%	0.92
3/31/2023	4.2%	7.1%	0.90
3/31/2024	3.7%	7.0%	0.88
3/31/2025	3.2%	6.9%	0.86
3/31/2026	2.6%	6.8%	0.83
Continuing Period	2.1%	6.7%	0.92

Period	Invested Capital	Net Claims	Price per share
Base Year	$1,526.34	$1,488.84	$6.57
3/31/2017	$1,543.28	$1,491.08	$8.10
3/31/2018	$1,524.29	$1,491.45	$9.94
3/31/2019	$1,811.53	$1,493.34	$12.01
3/31/2020	$1,955.46	$1,495.60	$14.32
3/31/2021	$1,976.90	$1,498.08	$16.87
3/31/2022	$2,046.67	$1,500.43	$19.68
3/31/2023	$2,126.75	$1,504.00	$22.79
3/31/2024	$2,217.84	$1,506.06	$26.20
3/31/2025	$2,315.77	$1,507.90	$29.94
3/31/2026	$2,420.93	$1,509.50	$34.03
Continuing Period			