Deutsche Bank

3 Bovis Homes – Glynis Johnson, BUY, close 1185p, 1368p tgt, 15% upside

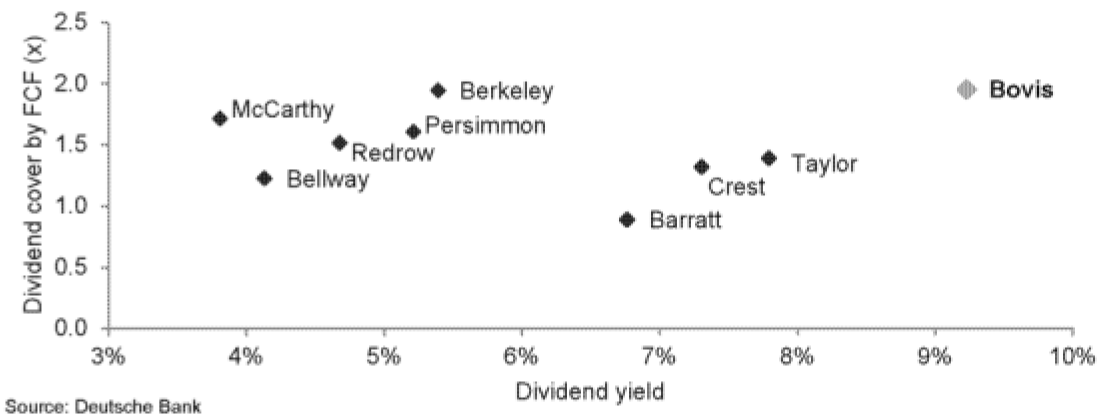
- **Management's targets for 2020 are credible** (EBIT margins >18% and ROCE >25%) and provide scope for upside. We see scope for expansion from the following sources:
  - **Land bank intake margin is 26.4%**, above the gross margin target of 23.5%
  - **Contingency costs** assumed in the current land bank and all new land intake should edge lower. These have increased from 2.5% to 4% of build cost, but the CEO has guided that these should fall.
  - We have not included any benefits from **new housetypes** from 2018. This could help bring cost savings and economies of scale.
  - **Admin costs** are targeted to be below 5% of sales. They are at the top of the peer group at present and so this target implies substantial cost savings, but we believe volume improvements could help too.
- **>9% dividend yield** from special cash return of £180m over three years.
- **Potential for higher dividends** if Bovis constrains its land buying plans. Reducing land buying by half would increase cash available by £75m. **The CEO is incentivised to pay out more than £180m in his LTIP.**
- **Organic cash flow can support the dividend post 2020.** The cash generation potential is impressive, with a 2018E FCF yield of 18.0%.
- Stock is still **cheap at 1.2x 2018E P/TNAV**, despite 30% rise in last six months.
- Catalysts: FY trading update on 12th January, FY results on 1st March.

Related DB Research:

Bovis: Benefits of strategy becoming evident (Johnson)

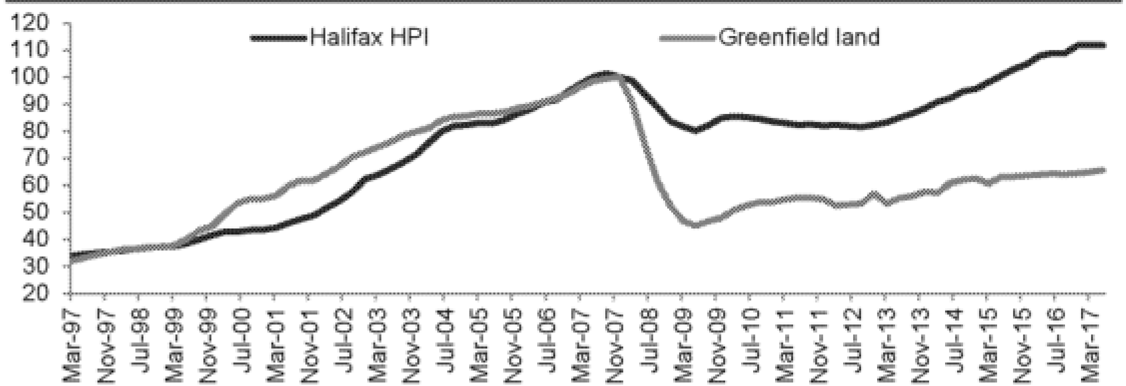
UK Housebuilders: 2018 Outlook – Better for longer (Johnson)

Bovis has the best yield in the sector, and one of the best in the market



Source: Deutsche Bank

We see margin upside from the land bank, with land trailing house prices



Source: Deutsche Bank, Halifax. Land: Savills UK resi land dev index. Rebased: Dec 2007 = 100