

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

(Mark One)

Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended APRIL 30, 2019

OR

Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Commission file number 1-8551

Hovnanian Enterprises, Inc. (Exact Name of Registrant as Specified in Its Charter)

Delaware (State or Other Jurisdiction of Incorporation or Organization)

22-1851059 (I.R.S. Employer Identification No.)

90 Matawan Road, 5th Floor, Matawan, NJ 07747 (Address of Principal Executive Offices)

732-747-7800 (Registrant's Telephone Number, Including Area Code)

N/A (Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

Securities registered pursuant to Section 12(b) of the Act.

| Title of each class | Trading symbol(s) | Name of each exchange on which registered |
|---|-------------------|---|
| Class A Common Stock \$0.01 par value per share | HOV | New York Stock Exchange |
| Preferred Stock Purchase Rights(1) | N/A | New York Stock Exchange |
| Depository Shares each representing 1/1,000th of a share of 7.625% Series A Preferred Stock | HOVNP | Nasdaq Global Market |

(1) Each share of Common Stock includes an associated Preferred Stock Purchase Right. Each Preferred Stock Purchase Right initially represents the right, if such Preferred Stock Purchase Right becomes exercisable, to purchase from the Company one ten-thousandth of a share of its Series B Junior Preferred Stock for each share of Common Stock. The Preferred Stock Purchase Rights currently cannot trade separately from the underlying Common Stock.

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer Accelerated Filer

Non-Accelerated Filer Smaller Reporting Company Emerging Growth Company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. 5,316,396 shares of Class A Common Stock and 622,788 shares of Class B Common Stock were outstanding as of June 3, 2019.

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HOVNANIAN ENTERPRISES, INC.

FORM 10-Q

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HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(In Thousands)

| | April 30, 2019 (Unaudited) | October 31, 2018 |
|--|----------------------------------|---------------------|
| ASSETS | | |
| Homebuilding: | | |
| Cash and cash equivalents | \$123,998 | \$187,871 |
| Restricted cash and cash equivalents | 17,223 | 12,808 |
| Inventories: | | |
| Sold and unsold homes and lots under development | 993,477 | 878,876 |
| Land and land options held for future development or sale | 120,146 | 111,368 |
| Consolidated inventory not owned | 154,435 | 87,921 |
| Total inventories | 1,268,058 | 1,078,165 |
| Investments in and advances to unconsolidated joint ventures | 135,562 | 123,694 |
| Receivables, deposits and notes, net | 29,154 | 35,189 |
| Property, plant and equipment, net | 20,307 | 20,285 |
| Prepaid expenses and other assets | 41,058 | 39,150 |
| Total homebuilding | 1,635,360 | 1,497,162 |
| Financial services | 119,912 | 164,880 |
| Total assets | <u>\$1,755,272</u> | <u>\$1,662,042</u> |
| LIABILITIES AND EQUITY | | |
| Homebuilding: | | |
| Nonrecourse mortgages secured by inventory, net of debt issuance costs | \$190,655 | \$95,557 |
| Accounts payable and other liabilities | 285,293 | 304,899 |
| Customers' deposits | 37,953 | 30,086 |
| Liabilities from inventory not owned, net of debt issuance costs | 123,348 | 63,387 |
| Revolving and term loan credit facilities, net of debt issuance costs | 201,459 | 201,389 |
| Notes payable (net of discount, premium and debt issuance costs) and accrued interest | 1,298,899 | 1,273,446 |
| Total homebuilding | 2,137,607 | 1,968,764 |
| Financial services | 100,054 | 143,448 |
| Income taxes payable | 2,090 | 3,334 |
| Total liabilities | <u>2,239,751</u> | <u>2,115,546</u> |
| Equity: | | |
| Hovnanian Enterprises, Inc. stockholders' equity deficit: | | |
| Preferred stock, \$0.01 par value - authorized 100,000 shares; issued and outstanding 5,600 shares with a liquidation preference of \$140,000 at April 30, 2019 and at October 31, 2018 | 135,299 | 135,299 |
| Common stock, Class A, \$0.01 par value – authorized 16,000,0000 shares; issued 5,786,826 shares at April 30, 2019 and 5,783,858 shares at October 31, 2018 | 58 | 58 |
| Common stock, Class B, \$0.01 par value (convertible to Class A at time of sale) – authorized 2,400,000 shares; issued 650,457 shares at April 30, 2019 and 649,673 shares at October 31, 2018 | 6 | 6 |
| Paid in capital – common stock | 711,517 | 710,349 |
| Accumulated deficit | (1,216,565) | (1,183,856) |
| Treasury stock – at cost – 470,430 shares of Class A common stock and 27,669 shares of Class B common stock at April 30, 2019 and October 31, 2018 | (115,360) | (115,360) |
| Total Hovnanian Enterprises, Inc. stockholders' equity deficit | <u>(485,045)</u> | <u>(453,504)</u> |
| Noncontrolling interest in consolidated joint ventures | 566 | - |
| Total equity deficit | <u>(484,479)</u> | <u>(453,504)</u> |
| Total liabilities and equity | <u>\$1,755,272</u> | <u>\$1,662,042</u> |

See notes to condensed consolidated financial statements (unaudited).

HOVNIANIAN ENTERPRISES, INC. AND SUBSIDIARIES
 CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
 (In Thousands Except Per Share Data)
 (Unaudited)

| | Three Months Ended April 30, | | Six Months Ended April 30, | |
|--|------------------------------|-----------|----------------------------|------------|
| | 2019 | 2018 | 2019 | 2018 |
| Revenues: | | | | |
| Homebuilding: | | | | |
| Sale of homes | \$427,552 | \$468,117 | \$789,687 | \$869,694 |
| Land sales and other revenues | 832 | 21,373 | 9,683 | 26,074 |
| Total homebuilding | 428,384 | 489,490 | 799,370 | 895,768 |
| Financial services | 12,307 | 13,054 | 21,915 | 23,942 |
| Total revenues | 440,691 | 502,544 | 821,285 | 919,710 |
| Expenses: | | | | |
| Homebuilding: | | | | |
| Cost of sales, excluding interest | 355,477 | 393,012 | 660,404 | 722,539 |
| Cost of sales interest | 13,898 | 19,364 | 24,140 | 31,656 |
| Inventory impairment loss and land option write-offs | 1,462 | 2,673 | 2,166 | 3,087 |
| Total cost of sales | 370,837 | 415,049 | 686,710 | 757,282 |
| Selling, general and administrative | 44,179 | 45,544 | 86,915 | 88,775 |
| Total homebuilding expenses | 415,016 | 460,593 | 773,625 | 846,057 |
| Financial services | 8,678 | 8,798 | 17,152 | 17,139 |
| Corporate general and administrative | 16,169 | 16,144 | 33,833 | 35,279 |
| Other interest | 22,663 | 26,088 | 44,936 | 55,219 |
| Other operations | 329 | 402 | 571 | 792 |
| Total expenses | 462,855 | 512,025 | 870,117 | 954,486 |
| Loss on extinguishment of debt | - | (1,440) | - | (1,440) |
| Income (loss) from unconsolidated joint ventures | 7,252 | 1,343 | 16,814 | (3,833) |
| Loss before income taxes | (14,912) | (9,578) | (32,018) | (40,049) |
| State and federal income tax provision: | | | | |
| State | 345 | 245 | 691 | 583 |
| Federal | - | - | - | - |
| Total income taxes | 345 | 245 | 691 | 583 |
| Net (loss) | \$(15,257) | \$(9,823) | \$(32,709) | \$(40,632) |
| Per share data: | | | | |
| Basic and assuming dilution: | | | | |
| Net (loss) per common share | \$(2.56) | \$(1.65) | \$(5.49) | \$(6.85) |
| Weighted-average number of common shares outstanding | 5,962 | 5,937 | 5,960 | 5,929 |

See notes to condensed consolidated financial statements (unaudited).

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HOVNIANIAN ENTERPRISES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
SIX MONTH PERIOD ENDED APRIL 30, 2019
(In Thousands Except Share Amounts)
(Unaudited)

| | A Common Stock | | B Common Stock | | Preferred Stock | | Paid-In Capital | Accumulated Deficit | Treasury Stock | Non Controlling Interest | Total |
|---|-------------------------------|-------------|-------------------------------|------------|--------------------------------|------------------|------------------|----------------------|--------------------|--------------------------|--------------------|
| | Shares Issued and Outstanding | Amount | Shares Issued and Outstanding | Amount | Shares- Issued and Outstanding | Amount | | | | | |
| Balance, October 31, 2018 | 5,313,428 | \$58 | 622,004 | \$6 | 5,600 | \$135,299 | \$710,349 | \$(1,183,856) | \$(115,360) | \$- | \$(453,504) |
| Stock options, amortization and issuances | | | | | | | 107 | | | | 107 |
| Restricted stock amortization, issuances and forfeitures | 2,830 | | 922 | | | | 485 | | | | 485 |
| Conversion of Class B to Class A common stock | 20 | | (20) | | | | | | | | - |
| Net (loss) | | | | | | | | (17,452) | | | (17,452) |
| Balance, January 31, 2019 | <u>5,316,278</u> | <u>\$58</u> | <u>622,906</u> | <u>\$6</u> | <u>5,600</u> | <u>\$135,299</u> | <u>\$710,941</u> | <u>\$(1,201,308)</u> | <u>\$(115,360)</u> | <u>\$-</u> | <u>\$(470,364)</u> |
| Stock options, amortization and issuances | | | | | | | 108 | | | | 108 |
| Restricted Stock, amortization, issuances and forfeitures | | | | | | | 468 | | | | 468 |
| Conversion of Class B to Class A common stock | 118 | | (118) | | | | | | | | - |
| Changes in noncontrolling interest in consolidated joint ventures | | | | | | | | | | 566 | 566 |
| Net (loss) | | | | | | | | (15,257) | | | (15,257) |
| Balance, April 30, 2019 | <u>5,316,396</u> | <u>\$58</u> | <u>622,788</u> | <u>\$6</u> | <u>5,600</u> | <u>\$135,299</u> | <u>\$711,517</u> | <u>\$(1,216,565)</u> | <u>\$(115,360)</u> | <u>\$566</u> | <u>\$(484,479)</u> |

See notes to condensed consolidated financial statements (unaudited).

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HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES
 CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
 SIX MONTH PERIOD ENDED APRIL 30, 2018
 (In Thousands Except Share Amounts)
 (Unaudited)

| | A Common Stock | | B Common Stock | | Preferred Stock | | Paid-In Capital | Accumulated Deficit | Treasury Stock | Total |
|--|-------------------------------|-------------|-------------------------------|------------|-------------------------------|------------------|------------------|----------------------|--------------------|--------------------|
| | Shares Issued and Outstanding | Amount | Shares Issued and Outstanding | Amount | Shares Issued and Outstanding | Amount | | | | |
| Balance, October 31, 2017 | 5,291,412 | \$58 | 612,304 | \$6 | 5,600 | \$135,299 | \$708,002 | \$(1,188,376) | \$(115,360) | \$(460,371) |
| Stock options, amortization and issuances | 960 | | | | | | 210 | | | 210 |
| Restricted stock amortization, issuances and forfeitures | 13,291 | | 6,573 | | | | (219) | | | (219) |
| Conversion of Class B to Class A common stock | 58 | | (58) | | | | | | | - |
| Net (loss) | | | | | | | | (30,809) | | (30,809) |
| Balance, January 31, 2018 | <u>5,305,721</u> | <u>\$58</u> | <u>618,819</u> | <u>\$6</u> | <u>5,600</u> | <u>\$135,299</u> | <u>\$707,993</u> | <u>\$(1,219,185)</u> | <u>\$(115,360)</u> | <u>\$(491,189)</u> |
| Stock options, amortization and issuances | | | | | | | 92 | | | 92 |
| Restricted stock, amortization, issuances, and forfeitures | | | | | | | 944 | | | 944 |
| Conversion of Class B to Class A common stock | | | | | | | | | | - |
| Net (loss) | | | | | | | | (9,823) | | (9,823) |
| Balance, April 30, 2018 | <u>5,305,721</u> | <u>\$58</u> | <u>618,819</u> | <u>\$6</u> | <u>5,600</u> | <u>\$135,299</u> | <u>\$709,029</u> | <u>\$(1,229,008)</u> | <u>\$(115,360)</u> | <u>\$(499,976)</u> |

See notes to condensed consolidated financial statements (unaudited).

HOVNIANIAN ENTERPRISES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In Thousands)
(Unaudited)

| | Six Months Ended April 30, | |
|---|-------------------------------|------------|
| | 2019 | 2018 |
| Cash flows from operating activities: | | |
| Net (loss) | \$(32,709) | \$(40,632) |
| Adjustments to reconcile net (loss) to net cash used in operating activities: | | |
| Depreciation | 1,938 | 1,509 |
| Compensation from stock options and awards | 1,191 | 2,075 |
| Amortization of bond discounts, premiums and deferred financing costs | 3,880 | 4,150 |
| Gain on sale and retirement of property and assets | (12) | (3,592) |
| (Income) loss from unconsolidated joint ventures | (16,814) | 3,833 |
| Distributions of earnings from unconsolidated joint ventures | 6,917 | - |
| Loss on extinguishment of debt | - | 1,440 |
| Noncontrolling interest income in consolidated joint venture | (28) | - |
| Inventory impairment and land option write-offs | 2,166 | 3,087 |
| (Increase) decrease in assets: | | |
| Origination of mortgage loans | (435,012) | (456,828) |
| Sale of mortgage loans | 474,457 | 501,227 |
| Receivables, prepaids, deposits and other assets | 4,712 | (16,349) |
| Inventories | (192,059) | (20,267) |
| (Decrease) increase in liabilities: | | |
| State income tax payable | (1,244) | (325) |
| Customers' deposits | 7,867 | (2,775) |
| Accounts payable, accrued interest and other accrued liabilities | (24,119) | (46,511) |
| Net cash used in operating activities | (198,869) | (69,958) |
| Cash flows from investing activities: | | |
| Proceeds from sale of property and assets | 16 | 38,273 |
| Purchase of property, equipment and other fixed assets and acquisitions | (1,956) | (3,208) |
| Investments in and advances to unconsolidated joint ventures | (7,727) | (18,879) |
| Distributions of capital from unconsolidated joint ventures | 5,756 | 28,754 |
| Net cash (used in) provided by investing activities | (3,911) | 44,940 |
| Cash flows from financing activities: | | |
| Proceeds from mortgages and notes | 171,045 | 75,962 |
| Payments related to mortgages and notes | (74,696) | (82,121) |
| Proceeds from model sale leaseback financing programs | 14,905 | 746 |
| Payments for model sale leaseback financing programs | (6,627) | (22,741) |
| Proceeds from land bank financing programs | 61,155 | 3,766 |
| Payments related to land bank financing programs | (8,765) | (19,890) |
| Proceeds from partner contribution to consolidated joint venture | 594 | - |
| Proceeds from senior unsecured term loan facility | - | 132,500 |
| Proceeds from senior secured notes, net of discount | 21,348 | - |
| Payments for senior notes and senior amortizing notes | - | (215,093) |
| Net payments related to mortgage warehouse lines of credit | (36,606) | (43,439) |
| Deferred financing costs from land bank financing programs and note issuances | (3,962) | (5,523) |
| Net cash provided by (used in) financing activities | 138,391 | (175,833) |
| Net decrease in cash and cash equivalents, and restricted cash and cash equivalents | (64,389) | (200,851) |
| Cash, cash equivalents, and restricted cash and cash equivalents balance, beginning of period | 232,992 | 493,742 |
| Cash, cash equivalents, and restricted cash and cash equivalents balance, end of period | \$168,603 | \$292,891 |

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HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In Thousands - Unaudited)
(Continued)

| | Six Months Ended April 30, | |
|---|-------------------------------|------------------|
| | 2019 | 2018 |
| Supplemental disclosure of cash flow: | | |
| Cash paid during the period for: | | |
| Interest, net of capitalized interest (see Note 3 to the Condensed Consolidated Financial Statements) | \$43,840 | \$59,707 |
| Income taxes | \$1,936 | \$909 |
| Reconciliation of Cash, cash equivalents and restricted cash | | |
| Homebuilding: Cash and cash equivalents | \$123,998 | \$248,815 |
| Homebuilding: Restricted cash and cash equivalents | 17,223 | 13,957 |
| Financial Services: Cash and cash equivalents, included in Financial services assets | 5,424 | 4,960 |
| Financial Services: Restricted cash and cash equivalents, included in Financial services assets | 21,958 | 25,159 |
| Total cash, cash equivalents and restricted cash shown in the statement of cash flows | \$168,603 | \$292,891 |

See notes to condensed consolidated financial statements (unaudited).

Supplemental disclosure of noncash investing activities:

In the first quarter of fiscal 2018, we acquired the remaining assets of one of our joint ventures, resulting in a \$13.0 million reduction in our investment in the joint venture and a corresponding increase to inventory.

Supplemental disclosure of noncash financing activities:

In the second quarter of fiscal 2018, we completed a debt for debt exchange of existing 8.0% Senior Notes due November 1, 2019 for newly issued 13.5% Senior Notes due 2026 and 5.0% Senior Notes due 2040. See Note 11 for further information.

1. Basis of Presentation

Hovnanian Enterprises, Inc. (“HEI”) conducts all of its homebuilding and financial services operations through its subsidiaries (references herein to the “Company,” “we,” “us” or “our” refer to HEI and its consolidated subsidiaries and should be understood to reflect the consolidated business of HEI’s subsidiaries). HEI has reportable segments consisting of six Homebuilding segments (Northeast, Mid-Atlantic, Midwest, Southeast, Southwest and West) and the Financial Services segment (see Note 16).

The accompanying unaudited Condensed Consolidated Financial Statements include HEI’s accounts and those of all of its consolidated subsidiaries after elimination of all of its significant intercompany balances and transactions. Noncontrolling interest represents the proportionate equity interest in a consolidated joint venture that is not 100% owned by the Company. One of HEI’s subsidiaries owns a 99% controlling interest in the consolidated joint venture and therefore HEI is required to consolidate the joint venture within its Condensed Consolidated Financial Statements. The 1% that we do not own is accounted for as noncontrolling interest.

The accompanying unaudited Condensed Consolidated Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States (“GAAP”) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X and accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. These Condensed Consolidated Financial Statements should be read in conjunction with the consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the fiscal year ended October 31, 2018. In the opinion of management, all adjustments for interim periods presented have been made, which include normal recurring accruals and deferrals necessary for a fair presentation of our condensed consolidated financial position, results of operations and cash flows. The preparation of Condensed Consolidated Financial Statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates, and these differences could have a significant impact on the Condensed Consolidated Financial Statements. Results for interim periods are not necessarily indicative of the results which might be expected for a full year.

Reclassifications - Effective October 31, 2018 we early adopted Accounting Standards Update (“ASU”) 2016-18 “Statement of Cash Flows (Topic 230): Restricted Cash” (“ASU 2016-18”). As a result, restricted cash amounts are no longer shown within the operating and investing activities as these balances are now included in the beginning and ending cash balances in our Condensed Consolidated Statements of Cash Flows. The adoption of ASU 2016-18 also resulted in the reclassification of restricted cash in operating and investing activities of \$2.6 million and \$12.1 million, respectively, for the six months ended April 30, 2018. These amounts are now included in the beginning and ending cash balances for the respective periods. See also the reconciliation of cash, cash equivalents and restricted cash on the Condensed Consolidated Statements of Cash Flows.

Reverse Stock Split – As discussed in Note 14, in March 2019, the Company’s stockholders approved and the Board of Directors determined to effectuate a reverse stock split (the “Reverse Stock Split”) of the Company’s common stock at a ratio of 1-for-25, and a corresponding decrease in the number of authorized shares of the common stock. The Reverse Stock Split became effective on March 29, 2019, and every 25 issued shares (including treasury shares) of Class A Common Stock, par value \$0.01 per share (the “Class A Common Stock”), were combined into one share of Class A Common Stock, and every 25 issued shares (including treasury shares) of Class B Common Stock, par value \$0.01 per share (the “Class B Common Stock”), were combined into one share of Class B Common Stock. All share and per share amounts throughout this report have been retroactively adjusted to reflect the reverse stock split.

2. Stock Compensation

The Company’s total stock-based compensation expense was \$0.6 million and \$1.2 million for the three and six months ended April 30, 2019, respectively, and \$1.0 million and \$2.1 million for the three and six months ended April 30, 2018, respectively. Included in this total stock-based compensation expense was the vesting of stock options of \$0.1 million and \$0.2 million for the three and six months ended April 30, 2019, respectively, and \$0.1 million and \$0.3 million for the three and six months ended April 30, 2018, respectively.

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3. Interest

Interest costs incurred, expensed and capitalized were:

| (In thousands) | Three Months Ended April 30, | | Six Months Ended April 30, | |
|---|---------------------------------|-----------------|-------------------------------|-----------------|
| | 2019 | 2018 | 2019 | 2018 |
| Interest capitalized at beginning of period | \$74,455 | \$70,793 | \$68,117 | \$71,051 |
| Plus interest incurred (1) | 41,383 | 40,014 | 80,236 | 81,179 |
| Less cost of sales interest expensed | 13,898 | 19,364 | 24,140 | 31,656 |
| Less other interest expensed (2)(3) | 22,663 | 26,088 | 44,936 | 55,219 |
| Interest capitalized at end of period (4) | <u>\$79,277</u> | <u>\$65,355</u> | <u>\$79,277</u> | <u>\$65,355</u> |

- (1) Data does not include interest incurred by our mortgage and finance subsidiaries.
- (2) Other interest expensed includes interest that does not qualify for interest capitalization because our assets that qualify for interest capitalization (inventory under development) do not exceed our debt, which amounted to \$15.1 million and \$19.9 million for the three months ended April 30, 2019 and 2018, respectively, and \$32.7 million and \$39.5 million for the six months ended April 30, 2019 and 2018, respectively. Other interest also includes interest on completed homes, land in planning and fully developed lots without homes under construction, which does not qualify for capitalization, and therefore, is expensed. This component of other interest was \$7.6 million and \$6.2 million for the three months ended April 30, 2019 and 2018, respectively, and \$12.3 million and \$15.8 million for the six months ended April 30, 2019 and 2018, respectively.
- (3) Cash paid for interest, net of capitalized interest, is the sum of other interest expensed, as defined above, and interest paid by our mortgage and finance subsidiaries adjusted for the change in accrued interest on notes payable, which is calculated as follows:

| (In thousands) | Three Months Ended April 30, | | Six Months Ended April 30, | |
|--|---------------------------------|----------------|-------------------------------|-----------------|
| | 2019 | 2018 | 2019 | 2018 |
| Other interest expensed | \$22,663 | \$26,088 | \$44,936 | \$55,219 |
| Interest paid by our mortgage and finance subsidiaries | 514 | 585 | 1,203 | 1,186 |
| (Increase) decrease in accrued interest | (19,776) | (23,448) | (2,299) | 3,302 |
| Cash paid for interest, net of capitalized interest | <u>\$3,401</u> | <u>\$3,225</u> | <u>\$43,840</u> | <u>\$59,707</u> |

- (4) Capitalized interest amounts are shown gross before allocating any portion of impairments, if any, to capitalized interest.

4. Reduction of Inventory to Fair Value

We record impairment losses on inventories related to communities under development and held for future development when events and circumstances indicate that they may be impaired and the undiscounted cash flows estimated to be generated by those assets are less than their related carrying amounts. If the expected undiscounted cash flows are less than the carrying amount, then the community is written down to its fair value. We estimate the fair value of each impaired community by determining the present value of the estimated future cash flows at a discount rate commensurate with the risk of the respective community. For the six months ended April 30, 2019, our discount rate used for the impairments recorded ranged from 18.0% to 18.3%. For the six months ended April 30, 2018, our discount rate used for the impairments recorded ranged from 16.8% to 19.8%. Should the estimates or expectations used in determining cash flows or fair value decrease or differ from current estimates in the future, we may need to recognize additional impairments.

During the six months ended April 30, 2019 and 2018, we evaluated inventories of all 398 and 377 communities under development and held for future development or sale, respectively, for impairment indicators through preparation and review of detailed budgets or other market indicators of impairment. We performed detailed impairment calculations during the six months ended April 30, 2019 and 2018 for six and five of those communities (i.e., those with a projected operating loss or other impairment indicators), respectively, with an aggregate carrying value of \$51.6 million and \$11.2 million, respectively. As a result of our impairment analysis, we recorded aggregate impairment losses of \$1.0 million in two communities (which had an aggregate pre-impairment values of \$3.9 million) for the three months ended April 30, 2019, and \$1.0 million in three communities (which had an aggregate pre-impairment values of \$10.2 million) for the six months ended April 30, 2019. For both the three and six months ended April 30, 2018, we recorded aggregate impairment losses of \$2.1 million in all five communities (which had an aggregate pre-impairment value of \$11.2 million). These impairment losses are included in the Condensed Consolidated Statements of Operations on the line entitled "Homebuilding: Inventory impairment loss and land option write-offs" and deducted from inventory. The pre-impairment value represents the carrying value, net of prior period impairments, if any, at the time of recording the impairment. Of those communities tested for impairment during the six months ended April 30, 2019, three communities with an aggregate carrying value of \$41.3 million had undiscounted future cash flows that exceeded the carrying amount by less than 20%. During the six months ended April 30, 2018, none of the five communities tested for impairment had undiscounted future cash flows that exceeded the carrying amount by less than 20%.

The Condensed Consolidated Statements of Operations line entitled "Homebuilding: Inventory impairment loss and land option write-offs" also includes write-offs of options and approval, engineering and capitalized interest costs that we record when we redesign communities and/or abandon certain engineering costs and we do not exercise options in various locations because the communities' pro forma profitability is not projected to produce adequate returns on investment commensurate with the risk. Total aggregate write-offs related to these items were \$0.5 million and \$0.6 million for the three months ended April 30, 2019 and 2018, respectively, and \$1.2 million and \$1.0 million for the six months ended April 30, 2019 and 2018, respectively. Occasionally, these write-offs are offset by recovered deposits (sometimes through legal action) that had been written off in a prior period as walk-away costs. Historically, these recoveries have not been significant in comparison to the total costs written off. The number of lots walked away from during the three months ended April 30, 2019 and 2018 were 680 and 714, respectively, and 2,170 and 1,341 during the six months ended April 30, 2019 and 2018, respectively.

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We decide to mothball (or stop development on) certain communities when we determine that the current performance does not justify further investment at the time. When we decide to mothball a community, the inventory is reclassified on our Condensed Consolidated Balance Sheets from “Sold and unsold homes and lots under development” to “Land and land options held for future development or sale.” During the first half of fiscal 2019, we did not mothball any additional communities, but sold two previously mothballed communities and re-activated two previously mothballed communities. As of April 30, 2019 and October 31, 2018, the net book value associated with our 14 and 18 total mothballed communities was \$14.2 million and \$24.5 million, respectively, which was net of impairment charges recorded in prior periods of \$146.9 million and \$186.1 million, respectively.

From time to time we enter into option agreements that include specific performance requirements whereby we are required to purchase a minimum number of lots. Because of our obligation to purchase these lots, for accounting purposes in accordance with Accounting Standards Codification (“ASC”) 360-20-40-38, we are required to record this inventory on our Condensed Consolidated Balance Sheets. As of April 30, 2019 and October 31, 2018, we had no specific performance options.

We sell and lease back certain of our model homes with the right to participate in the potential profit when each home is sold to a third party at the end of the respective lease. As a result of our continued involvement, for accounting purposes in accordance with ASC 606-10-55-68, these sale and leaseback transactions are considered a financing rather than a sale. Therefore, for purposes of our Condensed Consolidated Balance Sheets, at April 30, 2019 and October 31, 2018, inventory of \$58.4 million and \$50.5 million, respectively, was recorded to “Consolidated inventory not owned,” with a corresponding amount of \$52.1 million and \$43.9 million (net of debt issuance costs), respectively, recorded to “Liabilities from inventory not owned” for the amount of net cash received from the transactions.

We have land banking arrangements, whereby we sell our land parcels to the land bankers and they provide us an option to purchase back finished lots on a predetermined schedule. Because of our options to repurchase these parcels, for accounting purposes, in accordance with ASC 606-10-55-70, these transactions are considered a financing rather than a sale. For purposes of our Condensed Consolidated Balance Sheets, at April 30, 2019 and October 31, 2018, inventory of \$96.0 million and \$37.4 million, respectively, was recorded to “Consolidated inventory not owned,” with a corresponding amount of \$71.2 million and \$19.5 million (net of debt issuance costs), respectively, recorded to “Liabilities from inventory not owned” for the amount of net cash received from the transactions.

5. Variable Interest Entities

The Company enters into land and lot option purchase contracts to procure land or lots for the construction of homes. Under these contracts, the Company will fund a stated deposit in consideration for the right, but not the obligation, to purchase land or lots at a future point in time with predetermined terms. Under the terms of the option purchase contracts, many of the option deposits are not refundable at the Company's discretion. Under the requirements of ASC 810, certain option purchase contracts may result in the creation of a variable interest in the entity (“VIE”) that owns the land parcel under option.

In compliance with ASC 810, the Company analyzes its option purchase contracts to determine whether the corresponding land sellers are VIEs and, if so, whether the Company is the primary beneficiary. Although the Company does not have legal title to the underlying land, ASC 810 requires the Company to consolidate a VIE if the Company is determined to be the primary beneficiary. In determining whether it is the primary beneficiary, the Company considers, among other things, whether it has the power to direct the activities of the VIE that most significantly impact the VIE's economic performance. Such activities would include, among other things, determining or limiting the scope or purpose of the VIE, selling or transferring property owned or controlled by the VIE, or arranging financing for the VIE. The Company also considers whether it has the obligation to absorb losses of the VIE or the right to receive benefits from the VIE. As a result of its analyses, the Company determined that as of April 30, 2019 and October 31, 2018, it was not the primary beneficiary of any VIEs from which it is purchasing land under option purchase contracts.

We will continue to secure land and lots using options, some of which are with VIEs. Including deposits on our unconsolidated VIEs, at April 30, 2019, we had total cash deposits amounting to \$69.2 million to purchase land and lots with a total purchase price of \$1.3 billion. The maximum exposure to loss with respect to our land and lot options is limited to the deposits plus any pre-development costs invested in the property, although some deposits are refundable at our request or refundable if certain conditions are not met.

6. Warranty Costs

General liability insurance for homebuilding companies and their suppliers and subcontractors is very difficult to obtain. The availability of general liability insurance is limited due to a decreased number of insurance companies willing to underwrite for the industry. In addition, those few insurers willing to underwrite liability insurance have significantly increased the premium costs. To date, we have been able to obtain general liability insurance but at higher premium costs with higher deductibles. Our subcontractors and suppliers have advised us that they have also had difficulty obtaining insurance that also provides us coverage. As a result, we have an owner controlled insurance program for certain of our subcontractors whereby the subcontractors pay us an insurance premium (through a reduction of amounts we would otherwise owe such subcontractors for their work on our homes) based on the risk type of the trade. We absorb the liability associated with their work on our homes as part of our overall general liability insurance at no additional cost to us because our existing general liability and construction defect insurance policy and related reserves for amounts under our deductible covers construction defects regardless of whether we or our subcontractors are responsible for the defect. For the six months ended April 30, 2019 and 2018, we received \$2.2 million and \$1.9 million, respectively, from subcontractors related to the owner controlled insurance program, which we accounted for as a reduction to inventory.

We accrue for warranty costs that are covered under our existing general liability and construction defect policy as part of our general liability insurance deductible. This accrual is expensed as selling, general and administrative costs. For homes delivered in fiscal 2019 and 2018, our deductible under our general liability insurance is a \$20 million aggregate for construction defect and warranty claims. For bodily injury claims, our deductible per occurrence in fiscal 2019 and 2018 is \$0.25 million, up to a \$5 million limit. Our aggregate retention for construction defect, warranty and bodily injury claims is \$20 million for fiscal 2019 and 2018. In addition, we establish a warranty accrual for lower cost-related issues to cover home repairs, community amenities and land development infrastructure that are not covered under our general liability and construction defect policy. We accrue an estimate for these warranty costs as part of cost of sales at the time each home is closed and title and possession have been transferred to the homebuyer. Additions and charges in the warranty reserve and general liability reserve for the three and six months ended April 30, 2019 and 2018 were as follows:

| (In thousands) | Three Months Ended April 30, | | Six Months Ended April 30, | |
|---|---------------------------------|------------------|-------------------------------|------------------|
| | 2019 | 2018 | 2019 | 2018 |
| Balance, beginning of period | \$93,410 | \$129,314 | \$95,064 | \$127,702 |
| Additions – Selling, general and administrative | 1,959 | 2,169 | 4,117 | 4,338 |
| Additions – Cost of sales | 1,308 | 4,154 | 3,336 | 9,899 |
| Charges incurred during the period | (4,020) | (19,862) | (10,111) | (26,164) |
| Changes to pre-existing reserves | 192 | - | 443 | - |
| Balance, end of period | <u>\$92,849</u> | <u>\$115,775</u> | <u>\$92,849</u> | <u>\$115,775</u> |

Warranty accruals are based upon historical experience. We engage a third-party actuary that uses our historical warranty and construction defect data to assist our management in estimating our unpaid claims, claim adjustment expenses and incurred but not reported claims reserves for the risks that we are assuming under the general liability and construction defect programs. The estimates include provisions for inflation, claims handling and legal fees. The majority of the charges incurred during the second quarter of fiscal 2018 represented a payment for construction defect reserves related to the settlement of a litigation matter.

Insurance claims paid by our insurance carriers, excluding insurance deductibles paid, for prior year deliveries were less than \$0.1 million for the three months ended April 30, 2019 and 2018, and less than \$0.1 million for the six months ended April 30, 2019 and 2018.

7. Commitments and Contingent Liabilities

We are involved in litigation arising in the ordinary course of business, none of which is expected to have a material adverse effect on our financial position, results of operations or cash flows, and we are subject to extensive and complex laws and regulations that affect the development of land and home building, sales and customer financing processes, including zoning, density, building standards and mortgage financing. These laws and regulations often provide broad discretion to the administering governmental authorities. This can delay or increase the cost of development or homebuilding. The significant majority of our litigation matters are related to construction defect claims. Our estimated losses from construction defect litigation matters, if any, are included in our construction defect reserves.

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We also are subject to a variety of local, state, federal and foreign laws and regulations concerning protection of health and the environment, including those regulating the emission or discharge of materials into the environment, the management of storm water runoff at construction sites, the handling, use, storage and disposal of hazardous substances, impacts to wetlands and other sensitive environments, and the remediation of contamination at properties that we have owned or developed or currently own or are developing (“environmental laws”). The particular environmental laws that apply to a site may vary greatly according to the community site, for example, due to the community, the environmental conditions at or near the site, and the present and former uses of the site. These environmental laws may result in delays, may cause us to incur substantial compliance, remediation and/or other costs, and can prohibit or severely restrict development and homebuilding activity. In addition, noncompliance with these laws and regulations could result in fines and penalties, obligations to remediate, permit revocations or other sanctions; and contamination or other environmental conditions at or in the vicinity of our developments may result in claims against us for personal injury, property damage or other losses.

We anticipate that increasingly stringent requirements will be imposed on developers and homebuilders in the future. For example, for a number of years, the EPA and U.S. Army Corps of Engineers have been engaged in rulemakings to clarify the scope of federally regulated wetlands, which included a June 2015 rule many affected businesses contend impermissibly expanded the scope of such wetlands that was challenged in court, stayed, and remains in litigation. A proposal was made in June 2017 to formally rescind the June 2015 rule and reinstate the rule scheme previously in place while the agencies initiate a new substantive rulemaking on the issue. A February 2018 rule purported to delay the effective date of the June 2015 rule until February 2020, but was enjoined nationwide in August 2018 by a federal district court in South Carolina and later by a federal district court in the State of Washington in response to lawsuits (the net result of which, according to the EPA, is that the June 2015 rule applies in 22 states, the District of Columbia, and the United States territories, and that the pre-June 2015 regime applies in the rest). The federal government has withdrawn its appeals of those decisions and the EPA and U.S. Army Corps of Engineers are focusing efforts on promulgating a new rule addressing the issue; the comment period on the proposed rule, which was published in February 2019, closed in April 2019. It is unclear how these and related developments, including at the state or local level, ultimately may affect the scope of regulated wetlands where we operate. Although we cannot reliably predict the extent of any effect these developments regarding wetlands, or any other requirements that may take effect may have on us, they could result in time-consuming and expensive compliance programs and in substantial expenditures, which could cause delays and increase our cost of operations. In addition, our ability to obtain or renew permits or approvals and the continued effectiveness of permits already granted or approvals already obtained is dependent upon many factors, some of which are beyond our control, such as changes in policies, rules and regulations and their interpretations and application.

In March 2013, we received a letter from the Environmental Protection Agency (“EPA”) requesting information about our involvement in a housing redevelopment project in Newark, New Jersey that a Company entity undertook during the 1990s. We understand that the development is in the vicinity of a former lead smelter and that tests on soil samples from properties within the development conducted by the EPA showed elevated levels of lead. We also understand that the smelter ceased operations many years before the Company entity involved acquired the properties in the area and carried out the re-development project. We responded to the EPA’s request. In August 2013, we were notified that the EPA considers us a potentially responsible party (or “PRP”) with respect to the site, that the EPA will clean up the site, and that the EPA is proposing that we fund and/or contribute towards the cleanup of the contamination at the site. We began preliminary discussions with the EPA concerning a possible resolution but do not know the scope or extent of the Company’s obligations, if any, that may arise from the site and therefore cannot provide any assurance that this matter will not have a material impact on the Company. The EPA requested additional information in April 2014 and again in March 2017 and the Company responded to the information requests. On May 2, 2018 the EPA sent a letter to the Company entity demanding reimbursement for 100% of the EPA’s costs to clean-up the site in the amount of \$2.7 million. The Company responded to the EPA’s demand letter on June 15, 2018 setting forth the Company’s defenses and expressing its willingness to enter into settlement negotiations. The parties have subsequently executed a Tolling Agreement to toll the statute of limitations on collection until December 20, 2019 to allow the parties time to discuss settlement. We believe that we have adequate reserves for this matter.

In 2015, the condominium association of the Four Seasons at Great Notch condominium community (the “Great Notch Plaintiff”) filed a lawsuit in the Superior Court of New Jersey, Law Division, Passaic County (the “Court”) alleging various construction defects, design defects, and geotechnical issues relating to the community. The operative complaint (“Complaint”) asserts claims against Hovnanian Enterprises, Inc. and several of its affiliates, including K. Hovnanian at Great Notch, LLC, K. Hovnanian Construction Management, Inc., and K. Hovnanian Companies, LLC. The Complaint also asserts claims against various other design professionals and contractors. The Great Notch Plaintiff has also filed a motion, which remains pending, to permit it to pursue a claim to pierce the corporate veil of K. Hovnanian at Great Notch, LLC to hold its alleged parent entities liable for any damages awarded against it. To date, the Hovnanian-affiliated defendants have reached a partial settlement with the Great Notch Plaintiff as to a portion of the Great Notch Plaintiff’s claims against them for an amount immaterial to the Company. On its remaining claims against the Hovnanian-affiliated defendants, the Great Notch Plaintiff has asserted damages of approximately \$119.5 million, which amount is potentially subject to treble damages pursuant to the Great Notch Plaintiff’s claim under the New Jersey Consumer Fraud Act. On August 17, 2018, the Hovnanian-affiliated defendants filed a motion for summary judgment seeking dismissal of all of the Great Notch Plaintiff’s remaining claims against them, which was withdrawn without prejudice to re-file with supplemental evidence. Trial is currently scheduled for September 9, 2019. Court ordered mediation sessions have been re-scheduled for July and August 2019. The Hovnanian-affiliated defendants intend to defend these claims vigorously.

8. Cash and Cash Equivalents, Restricted Cash and Cash Equivalents and Customer's Deposits

Cash represents cash deposited in checking accounts. Cash equivalents include certificates of deposit, Treasury bills and government money-market funds with maturities of 90 days or less when purchased. Our cash balances are held at a few financial institutions and may, at times, exceed insurable amounts. We believe we help to mitigate this risk by depositing our cash in major financial institutions. At April 30, 2019 and October 31, 2018, \$121.7 million and \$199.6 million, respectively, of the Cash and cash equivalents and Restricted cash and cash equivalents was in cash equivalents, the book value of which approximates fair value.

Homebuilding - Restricted cash and cash equivalents on the Condensed Consolidated Balance Sheets totaled \$17.2 million and \$12.8 million as of April 30, 2019 and October 31, 2018, respectively, which primarily consists of cash collateralizing our letter of credit agreements and facilities as discussed in Note 11.

Financial services restricted cash and cash equivalents, which are included in Financial services other assets on the Condensed Consolidated Balance Sheets, totaled \$22.0 million and \$25.4 million as of April 30, 2019 and October 31, 2018, respectively. Included in these balances were (1) financial services customers' deposits of \$20.0 million at April 30, 2019 and \$23.4 million as of October 31, 2018 which are subject to restrictions on our use, and (2) \$2.0 million at both April 30, 2019 and October 31, 2018, respectively, of restricted cash under the terms of our mortgage warehouse lines of credit.

Total Homebuilding Customers' deposits are shown as a liability on the Condensed Consolidated Balance Sheets. These liabilities are significantly more than the applicable periods' restricted cash balances because in some states the deposits are not restricted from use and, in other states, we are able to release the majority of these customer deposits to cash by pledging letters of credit and surety bonds.

9. Mortgage Loans Held for Sale

Our wholly owned mortgage banking subsidiary, K. Hovnanian American Mortgage, LLC ("K. Hovnanian Mortgage") originates mortgage loans, primarily from the sale of our homes. Such mortgage loans are sold in the secondary mortgage market within a short period of time of origination. Mortgage loans held for sale consist primarily of single-family residential loans collateralized by the underlying property. We have elected the fair value option to record loans held for sale and therefore these loans are recorded at fair value with the changes in the value recognized in the Condensed Consolidated Statements of Operations in "Revenues: Financial services." We currently use forward sales of mortgage-backed securities ("MBS"), interest rate commitments from borrowers and mandatory and/or best efforts forward commitments to sell loans to third-party purchasers to protect us from interest rate fluctuations. These short-term instruments, which do not require any payments to be made to the counterparty or purchaser in connection with the execution of the commitments, are recorded at fair value. Gains and losses on changes in the fair value are recognized in the Condensed Consolidated Statements of Operations in "Revenues: Financial services."

At April 30, 2019 and October 31, 2018, \$78.8 million and \$115.2 million, respectively, of mortgages held for sale were pledged against our mortgage warehouse lines of credit (see Note 10). We may incur losses with respect to mortgages that were previously sold that are delinquent and which had underwriting defects, but only to the extent the losses are not covered by mortgage insurance or resale value of the home. The reserves for these estimated losses are included in the "Financial services" liability balances on the Condensed Consolidated Balance Sheets. As of April 30, 2019 and 2018, we had reserves specifically for 20 and 45 identified mortgage loans, respectively, as well as reserves for an estimate for future losses on mortgages sold but not yet identified to us.

The activity in our loan origination reserves during the three and six months ended April 30, 2019 and 2018 was as follows:

| (In thousands) | Three Months Ended | | Six Months Ended | |
|---|--------------------|----------------|------------------|----------------|
| | April 30, | | April 30, | |
| | 2019 | 2018 | 2019 | 2018 |
| Loan origination reserves, beginning of period | \$1,264 | \$3,188 | \$2,563 | \$3,158 |
| Provisions for losses during the period | 37 | 38 | 78 | 68 |
| Adjustments to pre-existing provisions for losses from changes in estimates | (32) | 45 | (22) | 45 |
| Payments/Settlements | - | - | (1,350) | - |
| Loan origination reserves, end of period | <u>\$1,269</u> | <u>\$3,271</u> | <u>\$1,269</u> | <u>\$3,271</u> |

10. Mortgages

We have nonrecourse mortgage loans for certain communities totaling \$190.7 million and \$95.6 million (net of debt issuance costs) at April 30, 2019 and October 31, 2018, respectively, which are secured by the related real property, including any improvements, with an aggregate book value of \$374.9 million and \$241.9 million, respectively. The weighted-average interest rate on these obligations was 8.4% and 6.1% at April 30, 2019 and October 31, 2018, respectively, and the mortgage loan payments on each community primarily correspond to home deliveries.

K. Hovnanian Mortgage originates mortgage loans primarily from the sale of our homes. Such mortgage loans and related servicing rights are sold in the secondary mortgage market within a short period of time. In certain instances, we retain the servicing rights for a small amount of loans. K. Hovnanian Mortgage finances the origination of mortgage loans through various master repurchase agreements, which are recorded in financial services liabilities on the Condensed Consolidated Balance Sheets.

Our secured Master Repurchase Agreement with JPMorgan Chase Bank, N.A. (“Chase Master Repurchase Agreement”) is a short-term borrowing facility that provides up to \$50.0 million through its maturity on January 31, 2020. The loan is secured by the mortgages held for sale and is repaid when we sell the underlying mortgage loans to permanent investors. Interest is payable monthly on outstanding advances at an adjusted LIBOR rate, which was 2.48% at April 30, 2019, plus the applicable margin of 2.5% or 2.63% based upon type of loan. As of April 30, 2019 and October 31, 2018, the aggregate principal amount of all borrowings outstanding under the Chase Master Repurchase Agreement was \$35.2 million and \$40.3 million, respectively.

K. Hovnanian Mortgage has another secured Master Repurchase Agreement with Customers Bank (“Customers Master Repurchase Agreement”) which was amended on February 15, 2019 and is a short-term borrowing facility that provides up to \$50.0 million through its maturity on February 14, 2020. The loan is secured by the mortgages held for sale and is repaid when we sell the underlying mortgage loans to permanent investors. Interest is payable daily or as loans are sold to permanent investors on outstanding advances at the current LIBOR rate, plus the applicable margin ranging from 2.25% to 5.0% based on the type of loan and the number of days outstanding on the warehouse line. As of April 30, 2019 and October 31, 2018, the aggregate principal amount of all borrowings outstanding under the Customers Master Repurchase Agreement was \$30.6 million and \$40.2 million, respectively.

K. Hovnanian Mortgage also has a secured Master Repurchase Agreement with Comerica Bank (“Comerica Master Repurchase Agreement”), which is a short-term borrowing facility that provides up to \$50.0 million through its maturity on December 20, 2019. The loan is secured by the mortgages held for sale and is repaid when we sell the underlying mortgage loans to permanent investors. Interest is payable monthly at the current LIBOR rate, subject to a floor of 0.25%, plus the applicable margin of 2.25% or 3.25% based upon the type of loan. As of April 30, 2019 and October 31, 2018, the aggregate principal amount of all borrowings outstanding under the Comerica Master Repurchase Agreement was \$10.7 million and \$32.7 million, respectively.

The Chase Master Repurchase Agreement, Customers Master Repurchase Agreement and Comerica Master Repurchase Agreement (together, the “Master Repurchase Agreements”) require K. Hovnanian Mortgage to satisfy and maintain specified financial ratios and other financial condition tests. Because of the extremely short period of time mortgages are held by K. Hovnanian Mortgage before the mortgages are sold to investors (generally a period of a few weeks), the immateriality to us on a consolidated basis of the size of the Master Repurchase Agreements, the levels required by these financial covenants, our ability based on our immediately available resources to contribute sufficient capital to cure any default, were such conditions to occur, and our right to cure any conditions of default based on the terms of the applicable agreement, we do not consider any of these covenants to be substantive or material. As of April 30, 2019, we believe we were in compliance with the covenants under the Master Repurchase Agreements.

11. Senior Notes and Credit Facilities

Senior notes and credit facilities balances as of April 30, 2019 and October 31, 2018, were as follows:

| (In thousands) | April 30, 2019(1)(2) | October 31, 2018(1)(2) |
|--|-------------------------|---------------------------|
| Senior Secured Notes: | | |
| 9.5% Senior Secured Notes due November 15, 2020 | \$74,666 | \$74,561 |
| 2.0% Senior Secured Notes due November 1, 2021 (net of discount) | 53,112 | 53,094 |
| 5.0% Senior Secured Notes due November 1, 2021 (net of discount) | 136,533 | 135,571 |
| 10.0% Senior Secured Notes due July 15, 2022 | 436,066 | 435,461 |
| 10.5% Senior Secured Notes due July 15, 2024 (net of discount) | 416,375 | 394,736 |
| Total Senior Secured Notes, net of debt issuance costs | \$1,116,752 | \$1,093,423 |
| Senior Notes: | | |
| 8.0% Senior Notes due November 1, 2019 (3) | \$- | \$- |
| 13.5% Senior Notes due February 1, 2026 (including premium) | 100,687 | 101,162 |
| 5.0% Senior Notes due February 1, 2040 (net of discount) | 43,564 | 43,264 |
| Total Senior Notes, net of debt issuance costs | \$144,251 | \$144,426 |
| Senior Unsecured Term Loan Credit Facility due February 1, 2027, net of debt issuance costs | \$201,459 | \$201,389 |
| Senior Secured Revolving Credit Facility (4) | \$- | \$- |

(1) “Notes payable” on our Condensed Consolidated Balance Sheets as of April 30, 2019 and October 31, 2018 consists of the total senior secured and senior notes shown above, as well as accrued interest of \$37.9 million and \$35.6 million, respectively.

(2) Unamortized debt issuance costs at April 30, 2019 and October 31, 2018 were \$13.0 million and \$14.1 million, respectively.

(3) \$26.0 million of 8.0% Senior Notes due 2019 are owned by a wholly-owned consolidated subsidiary of HEI. Therefore, in accordance with GAAP, such notes are not reflected on the Condensed Consolidated Balance Sheets of HEI.

(4) Availability under the Secured Credit Facility will terminate on December 28, 2019 and any loans thereunder on such date will convert to secured term loans maturing on December 28, 2022.

General

Except for K. Hovnanian, the issuer of the notes and borrower under the Credit Facilities (as defined below), our home mortgage subsidiaries, joint ventures and subsidiaries holding interests in our joint ventures and certain of our title insurance subsidiaries, we and each of our subsidiaries are guarantors of the Credit Facilities, the senior secured notes and senior notes outstanding at April 30, 2019 (collectively, the “Notes Guarantors”). In addition to the Notes Guarantors, the 5.0% Senior Secured Notes due 2021 (the “5.0% 2021 Notes”), the 2.0% Senior Secured Notes due 2021 (the “2.0% 2021 Notes” and together with the 5.0% 2021 Notes, the “2021 Notes”) and the 9.50% Senior Secured Notes due 2020 (the “9.50% 2020 Notes” and collectively with the 2021 Notes, the “JV Holdings Secured Group Notes”) are guaranteed by K. Hovnanian JV Holdings, L.L.C. and its subsidiaries, except for certain joint ventures and joint venture holding companies (collectively, the “JV Holdings Secured Group”). Members of the JV Holdings Secured Group do not guarantee K. Hovnanian's other indebtedness.

The credit agreements governing the Credit Facilities and the indentures governing the notes (together, the “Debt Instruments”) outstanding at April 30, 2019 do not contain any financial maintenance covenants, but do contain restrictive covenants that limit, among other things, the Company’s ability and that of certain of its subsidiaries, including K. Hovnanian, to incur additional indebtedness (other than nonrecourse indebtedness, certain permitted indebtedness and refinancing indebtedness (under the 9.50% 2020 Notes, any new or refinancing indebtedness may not be scheduled to mature earlier than January 15, 2021 (so long as no member of the JV Holdings Secured Group is an obligor thereon), or February 15, 2021 (if otherwise), and under the 10.0% Senior Secured Notes due 2022 (the “10.0% 2022 Notes”), any refinancing indebtedness of K. Hovnanian's previously outstanding 7.0% Senior Notes due 2019 (the “7.0% Notes”) (which includes the Term Loans (as defined below)) and 8.0% Senior Notes due 2019 (the “8.0% Notes” and together with the 7.0% Notes, the “2019 Notes”) (which includes the New Notes (as defined below) and the Term Loans) may not be scheduled to mature earlier than July 16, 2024 (such restrictive covenant in respect of the 10.5% Senior Secured Notes due 2024 (the “10.5% 2024 Notes”) was eliminated as described below under “—Fiscal 2018”), pay dividends and make distributions on common and preferred stock, repurchase subordinated indebtedness and common and preferred stock, make other restricted payments, including investments, sell certain assets (including in certain land banking transactions), incur liens, consolidate, merge, sell or otherwise dispose of all or substantially all assets, enter into certain transactions with affiliates and make cash repayments of the 2019 Notes and refinancing indebtedness in respect thereof (with respect to the 10.0% 2022 Notes). The Debt Instruments also contain events of default which would permit the lenders or holders thereof to exercise remedies with respect to the collateral (as applicable), declare the loans made under the Term Loan Facility (defined below) (the “Term Loans”) and loans made under the Secured Credit Facility (as defined below) (the “Secured Revolving Loans”) or notes to be immediately due and payable if not cured within applicable grace periods, including the failure to make timely payments on the Term Loans, Secured Revolving Loans or notes or other material indebtedness, cross default to other material indebtedness, the failure to comply with agreements and covenants and specified events of bankruptcy and insolvency, with respect to the Term Loans and Secured Revolving Loans, material inaccuracy of representations and warranties and with respect to the Term Loans and Secured Revolving Loans, a change of control, and, with respect to the Secured Revolving Loans and senior secured notes, the failure of the documents granting security for the Secured Revolving Loans and senior secured notes to be in full force and effect, and the failure of the liens on any material portion of the collateral securing the Secured Revolving Loans and senior secured notes to be valid and perfected. As of April 30, 2019, we believe we were in compliance with the covenants of the Debt Instruments.

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If our consolidated fixed charge coverage ratio, as defined in the agreements governing our debt instruments, is less than 2.0 to 1.0, we are restricted from making certain payments, including dividends, and from incurring indebtedness other than certain permitted indebtedness, refinancing indebtedness and nonrecourse indebtedness. As a result of this ratio restriction, we are currently restricted from paying dividends, which are not cumulative, on our 7.625% Series A Preferred Stock. We anticipate that we will continue to be restricted from paying dividends for the foreseeable future. Our inability to pay dividends is in accordance with covenant restrictions and will not result in a default under our debt instruments or otherwise affect compliance with any of the covenants contained in our debt instruments.

Under the terms of our Debt Instruments, we have the right to make certain redemptions and prepayments and, depending on market conditions and covenant restrictions, may do so from time to time. We also continue to evaluate our capital structure and may also continue to make debt purchases and/or exchanges for debt or equity from time to time through tender offers, open market purchases, private transactions, or otherwise, or seek to raise additional debt or equity capital, depending on market conditions and covenant restrictions.

Fiscal 2019

On January 15, 2019, pursuant to the Commitment Letter (defined below) the Company issued \$25.0 million in aggregate principal amount of the Additional 10.5% 2024 Notes (defined below) to the GSO Entities (defined below) at a discount for a purchase price of \$21.3 million in cash. The Additional 10.5% 2024 Notes were issued as additional notes of the same series as the 10.5% 2024 Notes. The Additional 10.5% 2024 Notes and the guarantees are secured (subject to perfection timing requirements) by pari passu liens with the 10.5% 2024 Notes on substantially all of the assets of K. Hovnanian and the Notes Guarantors, subject to permitted liens and certain exceptions. See “—Secured Obligations” below.

Fiscal 2018

On December 1, 2017, our 6.0% Senior Exchangeable Note Units were paid in full, which units consisted of \$53.9 million principal amount of our Senior Exchangeable Notes that matured and the final installment payment of \$2.1 million on our 11.0% Senior Amortizing Notes.

On December 28, 2017, the Company and K. Hovnanian announced that they had entered into a commitment letter (the “Commitment Letter”) in respect of certain financing transactions with GSO Capital Partners LP (“GSO”) on its own behalf and on behalf of one or more funds managed, advised or sub-advised by GSO (collectively, the “GSO Entities”), and had commenced a private exchange offer with respect to the 8.0% Notes (the “Exchange Offer”).

Pursuant to the Commitment Letter, the GSO Entities agreed to, among other things, provide the principal amount of the following: (i) a senior unsecured term loan credit facility (the “Term Loan Facility”) to be borrowed by K. Hovnanian and guaranteed by the Company and the Notes Guarantors, pursuant to which the GSO Entities committed to lend K. Hovnanian Term Loans consisting of \$132.5 million of initial term loans (the “Initial Term Loans”) on the settlement date of the Exchange Offer for purposes of refinancing K. Hovnanian’s 7.0% Notes, and up to \$80.0 million of delayed draw term loans (the “Delayed Draw Term Loans”) for purposes of refinancing certain of K. Hovnanian’s 8.0% Notes, in each case, upon the terms and subject to the conditions set forth therein, and (ii) a senior secured first lien credit facility (the “Secured Credit Facility” and together with the Term Loan Facility, the “Credit Facilities”) to be borrowed by K. Hovnanian and guaranteed by the Notes Guarantors, pursuant to which the GSO Entities committed to lend to K. Hovnanian up to \$125.0 million of senior secured first priority loans to fund the repayment of K. Hovnanian’s then outstanding secured term loans and for general corporate purposes, upon the terms and subject to the conditions set forth therein. In addition, pursuant to the Commitment Letter, the GSO Entities committed to purchase, and K. Hovnanian agreed to issue and sell, on January 15, 2019, \$25.0 million in aggregate principal amount of additional 10.5% 2024 Notes (the “Additional 10.5% 2024 Notes”), upon the terms and subject to conditions set forth therein.

On January 29, 2018, K. Hovnanian, the Notes Guarantors, Wilmington Trust, National Association, as administrative agent, and the GSO Entities entered into the Term Loan Facility. K. Hovnanian borrowed the Initial Term Loans on February 1, 2018 to fund, together with cash on hand, the redemption on February 1, 2018 of all \$132.5 million aggregate principal amount of 7.0% Notes, which resulted in a loss on extinguishment of debt of \$0.5 million for the three and six months ended April 30, 2018. The Term Loans bear interest at a rate equal to 5.0% per annum and interest is payable in arrears, on the last business day of each fiscal quarter. The Term Loans will mature on February 1, 2027.

On January 29, 2018, K. Hovnanian, the Notes Guarantors, Wilmington Trust, National Association, as administrative agent, and the GSO Entities entered into the Secured Credit Facility. Availability under the Secured Credit Facility will terminate on December 28, 2019 and any outstanding Secured Revolving Loans on such date shall convert to secured term loans maturing on December 28, 2022. The Secured Revolving Loans and the guarantees thereof are secured (subject to perfection timing requirements under the terms of the Secured Credit Facility) by substantially all of the assets owned by K. Hovnanian and the Notes Guarantors, subject to permitted liens and certain exceptions, on a first lien basis relative to the liens securing K. Hovnanian’s 10.0% 2022 Notes and 10.5% 2024 Notes and Additional 10.5% 2024 Notes pursuant to an intercreditor agreement. The collateral securing the Secured Revolving Loans will be the same as that securing the 10.0% 2022 Notes and the 10.5% 2024 Notes and Additional 10.5% 2024 Notes. The Secured Revolving Loans bear interest at a rate equal to 10.0% per annum, and interest will be payable in arrears, on the last business day of each fiscal quarter.

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On February 1, 2018, K. Hovnanian accepted all of the \$170.2 million aggregate principal amount of 8.0% Notes validly tendered and not validly withdrawn in the Exchange Offer (representing 72.14% of the aggregate principal amount of 8.0% Notes outstanding prior to the Exchange Offer), and in connection therewith, K. Hovnanian issued \$90.6 million aggregate principal amount of its 13.5% Senior Notes due 2026 (the “New 2026 Notes”) and \$90.1 million aggregate principal amount of its 5.0% Senior Notes due 2040 (the “New 2040 Notes” and together with the New 2026 Notes, the “New Notes”) under a new indenture. Also, as part of the Exchange Offer, K. Hovnanian at Sunrise Trail III, LLC, a wholly-owned subsidiary of the Company (the “Subsidiary Purchaser”), purchased for \$26.5 million in cash an aggregate of \$26.0 million in principal amount of the 8.0% Notes (the “Purchased 8.0% Notes”). The New Notes were issued by K. Hovnanian and guaranteed by the Notes Guarantors, except the Subsidiary Purchaser, which does not guarantee the New Notes. The New 2026 Notes bear interest at 13.5% per annum and mature on February 1, 2026. The New 2040 Notes bear interest at 5.0% per annum and mature on February 1, 2040. Interest on the New Notes is payable semi-annually on February 1 and August 1 of each year to holders of record at the close of business on January 15 or July 15, as the case may be, immediately preceding each such interest payment date. The Exchange Offer was treated as a substantial modification of debt, and resulted in a loss on extinguishment of debt of \$0.9 million for the three and six months ended April 30, 2018. The New Notes were recorded at fair value (based on management’s estimate using available trades for similar debt instruments) on the date of the issuance of the New Notes.

K. Hovnanian’s New 2026 Notes are redeemable in whole or in part at K. Hovnanian’s option at any time prior to February 1, 2026 at a redemption price equal to 100% of their principal amount plus an applicable “Make Whole Amount”. At any time and from time to time on or after February 1, 2019, K. Hovnanian may also redeem some or all of the New 2026 Notes at a redemption price equal to 100.0% of their principal amount.

K. Hovnanian’s New 2040 Notes are redeemable in whole or in part at K. Hovnanian’s option at any time prior to February 1, 2040 at a redemption price equal to 100.0% of their principal amount plus an applicable “Make-Whole Amount”. At any time and from time to time on or after February 1, 2040, K. Hovnanian may also redeem some or all of the New 2040 Notes at a redemption price equal to 100.0% of their principal amount.

On January 16, 2018, K. Hovnanian, the Notes Guarantors and Wilmington Trust, National Association, as trustee and collateral agent, executed the Second Supplemental Indenture, dated as of January 16, 2018, to the indenture governing the 10.0% 2022 Notes and 10.5% 2024 Notes, dated as of July 27, 2017 (as supplemented, amended or otherwise modified), among K. Hovnanian, the Notes Guarantors and Wilmington Trust, National Association, as trustee and collateral agent, giving effect to the proposed amendments to such indenture solely with respect to the 10.5% 2024 Notes, which were obtained in a consent solicitation of the holders of the 10.5% 2024 Notes, and which eliminated the restrictions on K. Hovnanian’s ability to purchase, repurchase, redeem, acquire or retire for value the 2019 Notes and refinancing or replacement indebtedness in respect thereof.

Secured Obligations

The 10.0% 2022 Notes have a maturity of July 15, 2022 and bear interest at a rate of 10.0% per annum payable semi-annually on January 15 and July 15 of each year, to holders of record at the close of business on January 1 and July 1, as the case may be, immediately preceding such interest payment dates. The 10.0% 2022 Notes are redeemable in whole or in part at our option at any time prior to July 15, 2019 at 100.0% of their principal amount plus an applicable “Make-Whole Amount.” K. Hovnanian may also redeem some or all of the 10.0% 2022 Notes at 105.0% of principal commencing July 15, 2019, at 102.50% of principal commencing July 15, 2020 and at 100.0% of principal commencing July 15, 2021. In addition, K. Hovnanian may also redeem up to 35.0% of the aggregate principal amount of the 10.0% 2022 Notes prior to July 15, 2019 with the net cash proceeds from certain equity offerings at 110.0% of principal.

The 10.5% 2024 Notes have a maturity of July 15, 2024 and bear interest at a rate of 10.5% per annum payable semi-annually on January 15 and July 15 of each year, to holders of record at the close of business on January 1 and July 1, as the case may be, immediately preceding such interest payment dates. The 10.5% 2024 Notes are redeemable in whole or in part at our option at any time prior to July 15, 2020 at 100.0% of their principal amount plus an applicable “Make-Whole Amount.” K. Hovnanian may also redeem some or all of the 10.5% 2024 Notes at 105.25% of principal commencing July 15, 2020, at 102.625% of principal commencing July 15, 2021 and at 100.0% of principal commencing July 15, 2022. In addition, K. Hovnanian may also redeem up to 35.0% of the aggregate principal amount of the 10.5% 2024 Notes prior to July 15, 2020 with the net cash proceeds from certain equity offerings at 110.50% of principal.

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All of K. Hovnanian's obligations under the 10.0% 2022 Notes and the 10.5% 2024 Notes are guaranteed by the Notes Guarantors. In addition to pledges of the equity interests in K. Hovnanian and the subsidiary Notes Guarantors which secure the 10.0% 2022 Notes and the 10.5% 2024 Notes, the 10.0% 2022 Notes and the 10.5% 2024 Notes and the guarantees thereof are also secured in accordance with the terms of the indenture governing such Notes and security documents related thereto by pari passu liens on substantially all of the assets owned by K. Hovnanian and the Notes Guarantors, in each case, subject to permitted liens and certain exceptions (the collateral securing the 10.0% 2022 Notes and the 10.5% 2024 Notes is the same as that which, subject to perfection timing requirements, secures the Secured Revolving Loans and the additional 10.5% 2024 Notes). The liens securing the 10.0% 2022 Notes and the 10.5% 2024 Notes rank junior to the liens securing the Secured Revolving Loans and any future secured obligations that are senior in priority with respect to the assets securing the 10.0% 2022 Notes and the 10.5% 2024 Notes.

At April 30, 2019, the aggregate book value of the real property that constituted collateral securing the 10.0% 2022 Notes and 10.5% 2024 Notes was \$396.1 million, which does not include the impact of inventory investments, home deliveries or impairments thereafter and which may differ from the value if it were appraised. Cash and cash equivalents collateral that secured the 10.0% 2022 Notes and 10.5% 2024 Notes was \$85.7 million as of April 30, 2019, which included \$17.0 million of restricted cash collateralizing certain letters of credit. Subsequent to such date, fluctuations as a result of cash uses include general business operations and real estate and other investments along with cash inflow primarily from deliveries.

The 9.50% 2020 Notes have a maturity of November 15, 2020, and bear interest at a rate of 9.5% per annum, payable semi-annually on February 15 and August 15 of each year, to holders of record at the close of business on February 1 and August 1, as the case may be, immediately preceding such interest payment dates. The 9.50% 2020 Notes are redeemable in whole or in part at our option at any time prior to November 15, 2018 at 100% of their principal amount plus an applicable "Make-Whole Amount." At any time and from time to time on or after November 15, 2018, K. Hovnanian may also redeem some or all of the 9.50% 2020 Notes at a redemption price equal to 100% of their principal amount.

The 5.0% 2021 Notes and the 2.0% 2021 Notes were issued as separate series under an indenture, but have substantially the same terms other than with respect to interest rate and related redemption provisions, and vote together as a single class. The 5.0% 2021 Notes bear interest at a rate of 5.0% per annum and mature on November 1, 2021 and the 2.0% 2021 Notes bear interest at a rate of 2.0% per annum and mature on November 1, 2021. Interest on the 2021 Notes is payable semi-annually on May 1 and November 1 of each year, to holders of record at the close of business on April 15 and October 15, as the case may be, immediately preceding such interest payment dates. The 2021 Notes are redeemable in whole or in part at our option at any time, at 100.0% of the principal amount plus the greater of 1% of the principal amount and an applicable "Make-Whole Amount."

The 9.5% 2020 Notes and the 2021 Notes are guaranteed by the Notes Guarantors and the members of the JV Holdings Secured Group. The guarantees of the JV Holdings Secured Group with respect to the 2021 Notes and the 9.50% 2020 Notes are secured, subject to permitted liens and certain exceptions, by a first-priority lien on substantially all of the assets of the members of the JV Holdings Secured Group. As of April 30, 2019, the collateral securing the guarantees included (1) \$44.5 million of cash and cash equivalents (subsequent to such date, fluctuations as a result of cash uses include general business operations and real estate and other investments along with cash inflow primarily from deliveries); (2) \$133.2 million aggregate book value of real property of the JV Holdings Secured Group, which does not include the impact of inventory investments, home deliveries or impairments thereafter and which may differ from the value if it were appraised; and (3) equity interests owned by guarantors that are members of the JV Holdings Secured Group. Members of the JV Holdings Secured Group also own equity in joint ventures, either directly or indirectly through ownership of joint venture holding companies, with a book value of \$181.0 million as of April 30, 2019; this equity is not pledged to secure, and is not collateral for, the 9.50% 2020 Notes or the 2021 Notes. Members of the JV Holdings Secured Group are "unrestricted subsidiaries" under K. Hovnanian's other senior secured notes and senior notes and Credit Facilities, and thus have not guaranteed such indebtedness.

Other

We have certain stand-alone cash collateralized letter of credit agreements and facilities under which there was a total of \$16.2 million and \$12.5 million letters of credit outstanding at April 30, 2019 and October 31, 2018, respectively. These agreements and facilities require us to maintain specified amounts of cash as collateral in segregated accounts to support the letters of credit issued thereunder, which will affect the amount of cash we have available for other uses. At April 30, 2019 and October 31, 2018, the amount of cash collateral in these segregated accounts was \$17.0 million and \$12.7 million, respectively, which is reflected in "Restricted cash and cash equivalents" on the Condensed Consolidated Balance Sheets.

12. Per Share Calculation

Basic earnings per share is computed by dividing net income (loss) (the “numerator”) by the weighted-average number of common shares outstanding, adjusted for nonvested shares of restricted stock (the “denominator”) for the period. Computing diluted earnings per share is similar to computing basic earnings per share, except that the denominator is increased to include the dilutive effects of options and nonvested shares of restricted stock. Any options that have an exercise price greater than the average market price are considered to be anti-dilutive and are excluded from the diluted earnings per share calculation.

All outstanding nonvested shares that contain nonforfeitable rights to dividends or dividend equivalents that participate in undistributed earnings with common stock are considered participating securities and are included in computing earnings per share pursuant to the two-class method. The two-class method is an earnings allocation formula that determines earnings per share for each class of common stock and participating securities according to dividends or dividend equivalents and participation rights in undistributed earnings in periods when we have net income. The Company’s restricted common stock (“nonvested shares”) are considered participating securities.

There were 0.1 million incremental shares attributed to nonvested stock and outstanding options to purchase common stock for both the three and six months ended April 30, 2019, and 0.1 million for both the three and six months ended April 30, 2018, respectively, which were excluded from the computation of diluted earnings per share because we had a net loss for the period. Also, for the six months ended April 30, 2018, 0.1 million shares of common stock issuable upon the exchange of our senior exchangeable notes (which were issued in fiscal 2012 and matured and were fully paid in December 2017) were excluded from the computation of diluted earnings per share because the Company had a net loss for the period.

In addition, shares related to out-of-the money stock options that could potentially dilute basic earnings per share in the future that were not included in the computation of diluted earnings per share were 0.3 million for both the three and six months ended April 30, 2019, respectively, and 0.2 million for both the three and six months ended April 30, 2018, respectively, because to do so would have been anti-dilutive for the periods presented.

13. Preferred Stock

On July 12, 2005, we issued 5,600 shares of 7.625% Series A Preferred Stock, with a liquidation preference of \$25,000 per share. Dividends on the Series A Preferred Stock are not cumulative and are payable at an annual rate of 7.625%. The Series A Preferred Stock is not convertible into the Company’s common stock and is redeemable in whole or in part at our option at the liquidation preference of the shares. The Series A Preferred Stock is traded as depositary shares, with each depositary share representing 1/1000th of a share of Series A Preferred Stock. The depositary shares are listed on the NASDAQ Global Market under the symbol “HOVNP.” During the three and six months ended April 30, 2019 and 2018, we did not pay any dividends on the Series A Preferred Stock due to covenant restrictions in our debt instruments. We anticipate that we will continue to be restricted from paying dividends, which are not cumulative, for the foreseeable future.

14. Common Stock

Each share of Class A Common Stock entitles its holder to one vote per share, and each share of Class B Common Stock generally entitles its holder to ten votes per share. The amount of any regular cash dividend payable on a share of Class A Common Stock will be an amount equal to 110% of the corresponding regular cash dividend payable on a share of Class B Common Stock. If a shareholder desires to sell shares of Class B Common Stock, such stock must be converted into shares of Class A Common Stock at a one to one conversion rate.

On March 19, 2019, the Company’s stockholders approved at an annual meeting an amendment to our Certificate of Incorporation to effect a reverse stock split (the “Reverse Stock Split”) of the Company’s common stock at a ratio of 1-for-25, and a corresponding decrease in the number of authorized shares of the common stock. Following the stockholders’ approval, the Board of Directors, on March 19, 2019, determined to effectuate the Reverse Stock Split, which became effective on March 29, 2019, and every 25 issued shares (including treasury shares) of Class A Common Stock, par value \$0.01 per share (the “Class A Common Stock”), were combined into one share of Class A Common Stock, and every 25 issued shares (including treasury shares) of Class B Common Stock, par value \$0.01 per share (the “Class B Common Stock”), were combined into one share of Class B Common Stock. No fractional shares were issued in connection with the Reverse Stock Split. All share and per share amounts have been retroactively adjusted to reflect the reverse stock split.

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On August 4, 2008, our Board of Directors adopted a shareholder rights plan (the “Rights Plan”), which was amended on January 11, 2018, designed to preserve shareholder value and the value of certain tax assets primarily associated with net operating loss (NOL) carryforwards and built-in losses under Section 382 of the Internal Revenue Code. Our ability to use NOLs and built-in losses would be limited if there was an “ownership change” under Section 382. This would occur if shareholders owning (or deemed under Section 382 to own) 5% or more of our stock increase their collective ownership of the aggregate amount of our outstanding shares by more than 50 percentage points over a defined period of time. The Rights Plan was adopted to reduce the likelihood of an “ownership change” occurring as defined by Section 382. Under the Rights Plan, one right was distributed for each share of Class A Common Stock and Class B Common Stock outstanding as of the close of business on August 15, 2008. Effective August 15, 2008, if any person or group acquires 4.9% or more of the outstanding shares of Class A Common Stock without the approval of the Board of Directors, there would be a triggering event causing significant dilution in the voting power of such person or group. However, existing stockholders who owned, at the time of the Rights Plan’s initial adoption on August 4, 2008, 4.9% or more of the outstanding shares of Class A Common Stock will trigger a dilutive event only if they acquire additional shares. The approval of the Board of Directors’ decision to adopt the Rights Plan may be terminated by the Board of Directors at any time, prior to the Rights being triggered. The Rights Plan will continue in effect until August 14, 2021, unless it expires earlier in accordance with its terms. The approval of the Board of Directors’ decision to initially adopt the Rights Plan and the amendment thereto were approved by shareholders. Our stockholders also approved an amendment to our Certificate of Incorporation to restrict certain transfers of Class A Common Stock in order to preserve the tax treatment of our NOLs and built-in losses under Section 382 of the Internal Revenue Code. Subject to certain exceptions pertaining to pre-existing 5% stockholders and Class B stockholders, the transfer restrictions in our Restated Certificate of Incorporation generally restrict any direct or indirect transfer (such as transfers of our stock that result from the transfer of interests in other entities that own our stock) if the effect would be to (i) increase the direct or indirect ownership of our stock by any person (or public group) from less than 5% to 5% or more of our common stock; (ii) increase the percentage of our common stock owned directly or indirectly by a person (or public group) owning or deemed to own 5% or more of our common stock; or (iii) create a new “public group” (as defined in the applicable United States Treasury regulations). Transfers included under the transfer restrictions include sales to persons (or public groups) whose resulting percentage ownership (direct or indirect) of common stock would exceed the 5% thresholds discussed above, or to persons whose direct or indirect ownership of common stock would by attribution cause another person (or public group) to exceed such threshold.

On July 3, 2001, our Board of Directors authorized a stock repurchase program to purchase up to 0.2 million shares of Class A Common Stock. There were no shares purchased during the three and six months ended April 30, 2019. As of April 30, 2019, the maximum number of shares of Class A Common Stock that may yet be purchased under this program is 22 thousand.

15. Income Taxes

The total income tax expense for the three and six months ended April 30, 2019 was \$0.3 million and \$0.7 million, respectively, and \$0.3 million and \$0.6 million, respectively, for the same periods of the prior year. For both the three and six months ended April 30, 2019 and the three and six months ended April 30, 2018, the total income tax expense was primarily related to state tax expense from income generated that was not offset by tax benefits in states where we fully reserve the tax benefit from net operating losses.

Our federal net operating losses of \$1.6 billion expire between 2028 and 2037, and \$41.9 million have an indefinite carryforward period. Of our \$2.5 billion of state NOLs, \$145.3 million expire between 2019 through 2023; \$691.2 million expire between 2024 through 2028; \$1.3 billion expire between 2029 through 2033; \$316.1 million expire between 2034 through 2038; and \$43.2 million have an indefinite carryforward period.

Deferred federal and state income tax assets (“DTAs”) primarily represent the deferred tax benefits arising from NOL carryforwards and temporary differences between book and tax income which will be recognized in future years as an offset against future taxable income. If the combination of future years’ income (or loss) and the reversal of the timing differences results in a loss, such losses can be carried forward to future years. In accordance with ASC 740, we evaluate our DTAs quarterly to determine if valuation allowances are required. ASC 740 requires that companies assess whether valuation allowances should be established based on the consideration of all available evidence using a “more likely than not” standard.

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As of April 30, 2019, we considered all available positive and negative evidence to determine whether, based on the weight of that evidence, our valuation allowance for our DTAs was appropriate in accordance with ASC 740. Listed below, in order of the weighting of each factor, is the available positive and negative evidence that we considered in determining that it is more likely than not that all of our DTAs will not be realized. In analyzing these factors, overall the negative evidence, both objective and subjective, outweighed the positive evidence. Based on this analysis, we determined that the current valuation allowance for deferred taxes of \$642.9 million as of April 30, 2019, which fully reserves for our DTAs, is appropriate.

1. Fiscal 2017 financial results, especially the \$50.2 million pre-tax loss in the third quarter of fiscal 2017 primarily from the \$42.3 million loss on extinguishment of debt during the quarter, that put us in a cumulative three-year pre-tax loss position as of July 31, 2017. As of April 30, 2019, the Company has slightly positive pre-tax income when adjusted for permanent differences on a three year cumulative basis. However, on a US GAAP basis, the Company is still in a three year cumulative pre-tax loss position as of April 30, 2019. Therefore, it is too early to conclude whether we will continue to not be in a three-year cumulative loss position going forward on a tax accounting basis. Per ASC 740, cumulative losses are one of the most objectively verifiable forms of negative evidence. (Negative Objective Evidence)
2. In the third quarter of fiscal 2017 and second and third quarters of fiscal 2018, we completed debt refinancing/restructuring transactions which, by extending our debt maturities, will enable us to allocate cash to invest in new communities and grow our community count to get back to sustained profitability. (Positive Objective Evidence)
3. Recent financial results of \$48.1 million pre-tax income in the fourth quarter of fiscal 2018 and \$8.1 million pre-tax income for the year ended October 31, 2018. (Positive Objective Evidence)
4. Our net contracts per community declined in the fourth quarter of fiscal 2018 compared to the fourth quarter of fiscal 2017 and the second quarter of fiscal 2019 compared to the second quarter of fiscal 2018, consistent with data for the overall housing market. This slow down may be the beginning of a cyclical housing downturn or may just be temporary because of recent increases in mortgage rates. (Negative Objective Evidence)
5. We incurred pre-tax losses during the housing market decline and the slower than expected housing market recovery. (Negative Objective Evidence)
6. We exited two geographic markets in fiscal 2016 and completed the wind down of operations in two other markets in fiscal 2018, that have historically had losses. By exiting these underperforming markets, the Company will be able to redeploy capital to better performing markets, which over time should improve our profitability. (Positive Subjective Evidence)
7. The historical cyclicality of the U.S. housing market, a more restrictive mortgage lending environment compared to before the housing downturn, the uncertainty of the overall US economy and government policies and consumer confidence, all or any of which could continue to hamper a sustained, stronger recovery of the housing market. (Negative Subjective Evidence)

16. Operating and Reporting Segments

HEI's operating segments are components of our business for which discrete financial information is available and reviewed regularly by the chief operating decision maker, our Chief Executive Officer, to evaluate performance and make operating decisions. Based on this criteria, each of our communities qualifies as an operating segment, and therefore, it is impractical to provide segment disclosures for this many segments. As such, HEI has aggregated the homebuilding operating segments into six reportable segments.

HEI's homebuilding operating segments are aggregated into reportable segments based primarily upon geographic proximity, similar regulatory environments, land acquisition characteristics and similar methods used to construct and sell homes. HEI's reportable segments consist of the following six homebuilding segments and a financial services segment noted below.

Homebuilding:

- (1) Northeast (New Jersey and Pennsylvania)
- (2) Mid-Atlantic (Delaware, Maryland, Virginia, Washington D.C. and West Virginia)
- (3) Midwest (Illinois and Ohio)
- (4) Southeast (Florida, Georgia and South Carolina)
- (5) Southwest (Arizona and Texas)
- (6) West (California)

Financial Services

Operations of HEI's Homebuilding segments primarily include the sale and construction of single-family attached and detached homes, attached townhomes and condominiums, urban infill and active lifestyle homes in planned residential developments. In addition, from time to time, operations of the homebuilding segments include sales of land. Operations of HEI's Financial Services segment include mortgage banking and title services provided to the homebuilding operations' customers. Our financial services subsidiaries do not typically retain or service mortgages that we originate but rather sell the mortgages and related servicing rights to investors.

Corporate and unallocated primarily represents operations at our headquarters in New Jersey. This includes our executive offices, information services, human resources, corporate accounting, training, treasury, process redesign, internal audit, construction services, and administration of insurance, quality and safety. It also includes interest income and interest expense resulting from interest incurred that cannot be capitalized in inventory in the Homebuilding segments, as well as the gains or losses on extinguishment of debt from any debt repurchases or exchanges.

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Evaluation of segment performance is based primarily on operating earnings from continuing operations before provision for income taxes (“Income (loss) before income taxes”). Income (loss) before income taxes for the Homebuilding segments consist of revenues generated from the sales of homes and land, income (loss) from unconsolidated entities, management fees and other income, less the cost of homes and land sold, selling, general and administrative expenses and interest expense. Income before income taxes for the Financial Services segment consist of revenues generated from mortgage financing, title insurance and closing services, less the cost of such services and selling, general and administrative expenses incurred by the Financial Services segment.

Operational results of each segment are not necessarily indicative of the results that would have occurred had the segment been an independent stand-alone entity during the periods presented.

Financial information relating to HEI’s segment operations was as follows:

| (In thousands) | Three Months Ended April 30, | | Six Months Ended April 30, | |
|---|------------------------------|-----------|----------------------------|------------|
| | 2019 | 2018 | 2019 | 2018 |
| Revenues: | | | | |
| Northeast | \$13,059 | \$43,771 | \$33,000 | \$63,970 |
| Mid-Atlantic | 80,847 | 104,160 | 134,277 | 175,457 |
| Midwest | 42,937 | 42,938 | 87,858 | 83,517 |
| Southeast | 49,382 | 60,901 | 93,373 | 117,569 |
| Southwest | 143,850 | 159,147 | 262,049 | 287,452 |
| West | 97,883 | 78,098 | 187,784 | 163,148 |
| Total homebuilding | 427,958 | 489,015 | 798,341 | 891,113 |
| Financial services | 12,307 | 13,054 | 21,915 | 23,942 |
| Corporate and unallocated (1) | 426 | 475 | 1,029 | 4,655 |
| Total revenues | \$440,691 | \$502,544 | \$821,285 | \$919,710 |
| (Loss) income before income taxes: | | | | |
| Northeast | \$125 | \$5,960 | \$6,004 | \$(3,741) |
| Mid-Atlantic | 393 | 6,700 | 386 | 8,652 |
| Midwest | (594) | (1,110) | (1,443) | (3,454) |
| Southeast | (4,132) | (5,286) | (7,061) | (6,947) |
| Southwest | 4,286 | 10,047 | 6,672 | 15,558 |
| West | 10,310 | 7,172 | 22,015 | 15,239 |
| Homebuilding income before income taxes | 10,388 | 23,483 | 26,573 | 25,307 |
| Financial services | 3,629 | 4,256 | 4,763 | 6,803 |
| Corporate and unallocated (1) | (28,929) | (37,317) | (63,354) | (72,159) |
| Loss before income taxes | \$(14,912) | \$(9,578) | \$(32,018) | \$(40,049) |

(1) Corporate and unallocated for the three months ended April 30, 2019 included corporate general and administrative costs of \$16.2 million, interest expense of \$13.1 million (a component of Other interest on our Condensed Consolidated Statements of Operations), \$(0.3) million of other income and expenses primarily related to interest income and stock compensation. Corporate and unallocated for the six months ended April 30, 2019 included corporate general and administrative costs of \$33.8 million, interest expense of \$30.7 million (a component of Other interest on our Condensed Consolidated Statements of Operations), and \$(1.1) million of other income and expenses. Corporate and unallocated for the three months ended April 30, 2018 included corporate general and administrative costs of \$16.2 million, interest expense of \$19.9 million (a component of Other interest on our Condensed Consolidated Statements of Operations), loss on extinguishment of debt of \$1.4 million and \$(0.1) million of other income and expenses primarily related to interest income and gain on the sale of our former corporate headquarters building. Corporate and unallocated for the six months ended April 30, 2018 included corporate general and administrative costs of \$35.3 million, interest expense of \$39.5 million (a component of Other interest on our Condensed Consolidated Statements of Operations), loss on extinguishment of debt of \$ 1.4 million and \$(4.0) million of other income and expenses primarily related to interest income and gain on the sale of our former corporate headquarters building.

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| (In thousands) | April 30, 2019 | October 31, 2018 |
|---------------------------|--------------------|--------------------|
| Assets: | | |
| Northeast | \$175,326 | \$152,607 |
| Mid-Atlantic | 262,896 | 217,807 |
| Midwest | 114,024 | 85,398 |
| Southeast | 281,546 | 246,497 |
| Southwest | 359,129 | 320,452 |
| West | 274,723 | 244,886 |
| Total homebuilding | 1,467,644 | 1,267,647 |
| Financial services | 119,912 | 164,880 |
| Corporate and unallocated | 167,716 | 229,515 |
| Total assets | <u>\$1,755,272</u> | <u>\$1,662,042</u> |

17. Investments in Unconsolidated Homebuilding and Land Development Joint Ventures

We enter into homebuilding and land development joint ventures from time to time as a means of accessing lot positions, expanding our market opportunities, establishing strategic alliances, managing our risk profile, leveraging our capital base and enhancing returns on capital. Our homebuilding joint ventures are generally entered into with third-party investors to develop land and construct homes that are sold directly to third-party home buyers. Our land development joint ventures include those entered into with developers and other homebuilders as well as financial investors to develop finished lots for sale to the joint venture's members or other third parties.

During the first quarter of fiscal 2018, we acquired the remaining assets of one of our joint ventures, resulting in a \$13.0 million reduction in our investment in the joint venture and a corresponding increase to inventory.

The tables set forth below summarize the combined financial information related to our unconsolidated homebuilding and land development joint ventures that are accounted for under the equity method.

| (Dollars in thousands) | April 30, 2019 | | |
|--|------------------|------------------|------------------|
| | Homebuilding | Land Development | Total |
| Assets: | | | |
| Cash and cash equivalents | \$92,351 | \$2,168 | \$94,519 |
| Inventories | 469,815 | 7,987 | 477,802 |
| Other assets | 26,799 | - | 26,799 |
| Total assets | <u>\$588,965</u> | <u>\$10,155</u> | <u>\$599,120</u> |
| Liabilities and equity: | | | |
| Accounts payable and accrued liabilities | \$69,621 | \$508 | \$70,129 |
| Notes payable | 240,571 | - | 240,571 |
| Total liabilities | 310,192 | 508 | 310,700 |
| Equity of: | | | |
| Hovnanian Enterprises, Inc. | 124,344 | 4,608 | 128,952 |
| Others | 154,429 | 5,039 | 159,468 |
| Total equity | 278,773 | 9,647 | 288,420 |
| Total liabilities and equity | <u>\$588,965</u> | <u>\$10,155</u> | <u>\$599,120</u> |
| Debt to capitalization ratio | 46% | 0% | 45% |

| (Dollars in thousands) | October 31, 2018 | | |
|--|------------------|------------------|------------------|
| | Homebuilding | Land Development | Total |
| Assets: | | | |
| Cash and cash equivalents | \$50,010 | \$2,275 | \$52,285 |
| Inventories | 506,650 | 8,004 | 514,654 |
| Other assets | 35,105 | - | 35,105 |
| Total assets | <u>\$591,765</u> | <u>\$10,279</u> | <u>\$602,044</u> |
| Liabilities and equity: | | | |
| Accounts payable and accrued liabilities | \$79,108 | \$746 | \$79,854 |
| Notes payable | 236,665 | - | 236,665 |
| Total liabilities | 315,773 | 746 | 316,519 |
| Equity of: | | | |
| Hovnanian Enterprises, Inc. | 114,950 | 4,369 | 119,319 |
| Others | 161,042 | 5,164 | 166,206 |
| Total equity | 275,992 | 9,533 | 285,525 |
| Total liabilities and equity | <u>\$591,765</u> | <u>\$10,279</u> | <u>\$602,044</u> |
| Debt to capitalization ratio | 46% | 0% | 45% |

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As of April 30, 2019 and October 31, 2018, we had advances and a note receivable outstanding of \$6.0 million and \$4.6 million, respectively, to these unconsolidated joint ventures. These amounts were included in the “Accounts payable and accrued liabilities” balances in the tables above. On our Condensed Consolidated Balance Sheets, our “Investments in and advances to unconsolidated joint ventures” amounted to \$135.6 million and \$123.7 million at April 30, 2019 and October 31, 2018, respectively. In some cases our net investment in these joint ventures is less than our proportionate share of the equity reflected in the table above because of the differences between asset impairments recorded against our joint venture investments and any impairments recorded in the applicable joint venture. Impairments of joint venture investments are recorded at fair value while impairments recorded in the joint venture are recorded when undiscounted cash flows trigger the impairment. During the six months ended April 30, 2019 and 2018, we did not write-down any of our joint venture investments; however, during the six months ended April 30, 2018, one of our joint ventures in the Northeast recorded an asset impairment. We recorded our proportionate share of this impairment charge of \$0.7 million as part of our share of the net loss of the venture.

| (In thousands) | For the Three Months Ended April 30, 2019 | | |
|----------------------------|---|-------------|-----------|
| | Land | | Total |
| | Homebuilding | Development | |
| Revenues | \$125,739 | \$2,591 | \$128,330 |
| Cost of sales and expenses | (118,019) | (2,146) | (120,165) |
| Joint venture net income | \$7,720 | \$445 | \$8,165 |
| Our share of net income | \$7,083 | \$223 | \$7,306 |

| (In thousands) | For the Three Months Ended April 30, 2018 | | |
|---------------------------------|---|-------------|-----------|
| | Land | | Total |
| | Homebuilding | Development | |
| Revenues | \$96,931 | \$2,343 | \$99,274 |
| Cost of sales and expenses | (102,230) | (2,123) | (104,353) |
| Joint venture net (loss) income | \$(5,299) | \$220 | \$(5,079) |
| Our share of net (loss) income | \$1,296 | \$109 | \$1,405 |

| (In thousands) | For the Six Months Ended April 30, 2019 | | |
|----------------------------|---|-------------|-----------|
| | Land | | Total |
| | Homebuilding | Development | |
| Revenues | \$221,513 | \$3,596 | \$225,109 |
| Cost of sales and expenses | (207,331) | (3,117) | (210,448) |
| Joint venture net income | \$14,182 | \$479 | \$14,661 |
| Our share of net income | \$16,624 | \$240 | \$16,864 |

| (In thousands) | For the Six Months Ended April 30, 2018 | | |
|---------------------------------|---|-------------|------------|
| | Land | | Total |
| | Homebuilding | Development | |
| Revenues | \$155,496 | \$3,618 | \$159,114 |
| Cost of sales and expenses | (174,366) | (3,281) | (177,647) |
| Joint venture net (loss) income | \$(18,870) | \$337 | \$(18,533) |
| Our share of net (loss) income | \$(3,903) | \$168 | \$(3,735) |

“Income (loss) from unconsolidated joint ventures” is reflected as a separate line in the accompanying Condensed Consolidated Statements of Operations and reflects our proportionate share of the income or loss of these unconsolidated homebuilding and land development joint ventures. The difference between our share of the income or loss from these unconsolidated joint ventures in the tables above compared to the Condensed Consolidated Statements of Operations is due primarily to the reclassification of the intercompany portion of management fee income from certain joint ventures and the deferral of income for lots purchased by us from certain joint ventures. For the six months ended April 30, 2019, the difference can also be attributed to a return of capital from a joint venture in which we had previously written off our investment. To compensate us for the administrative services we provide as the manager of certain joint ventures, we receive a management fee based on a percentage of the applicable joint venture’s revenues. These management fees, which totaled \$5.1 million and \$2.9 million for the three months ended April 30, 2019 and 2018, respectively, and \$8.5 million and \$4.9 million for the six months ended April 30, 2019 and 2018, respectively, are recorded in “Homebuilding: Selling, general and administrative” on the Condensed Consolidated Statements of Operations.

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In determining whether or not we must consolidate joint ventures that we manage, we assess whether the other partners have specific rights to overcome the presumption of control by us as the manager of the joint venture. In most cases, the presumption is overcome because the joint venture agreements require that both partners agree on establishing the operations and capital decisions of the partnership, including budgets in the ordinary course of business.

Typically, our unconsolidated joint ventures obtain separate project specific mortgage financing. For some of our joint ventures, obtaining financing was challenging, therefore, some of our joint ventures are capitalized only with equity. The total debt to capitalization ratio of all our joint ventures is currently 45%. Any joint venture financing is on a nonrecourse basis, with guarantees from us limited only to performance and completion of development, environmental warranties and indemnification, standard indemnification for fraud, misrepresentation and other similar actions, including a voluntary bankruptcy filing. In some instances, the joint venture entity is considered a VIE under ASC 810-10 "Consolidation – Overall" due to the returns being capped to the equity holders; however, in these instances, we have determined that we are not the primary beneficiary, and therefore we do not consolidate these entities.

18. Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board ("FASB") issued ASU No. 2014-09, "Revenue from Contracts with Customers" (Topic 606), ("ASU 2014-09"). ASU 2014-09 requires entities to recognize revenue that represents the transfer of promised goods or services to customers in an amount equivalent to the consideration to which the entity expects to be entitled to in exchange for those goods or services. The following steps should be applied to determine this amount: (1) identify the contract(s) with a customer; (2) identify the performance obligations in the contract; (3) determine the transaction price; (4) allocate the transaction price to the performance obligations in the contract; and (5) recognize revenue when (or as) the entity satisfies a performance obligation. ASU 2014-09 supersedes the revenue recognition requirements in ASC 605, "Revenue Recognition," and most industry-specific guidance in the Accounting Standards Codification. The FASB has also issued a number of updates to this standard. The standard was effective for us for annual and interim periods beginning November 1, 2018 and we applied the modified retrospective method of adoption. The implementation did not result in any significant changes to our business processes, systems, or internal controls, or have a material impact on our Condensed Consolidated Financial Statements.

In February 2016, the FASB issued ASU No. 2016-02, "Leases (Topic 842)" ("ASU 2016-02"), which provides guidance for accounting for leases. ASU 2016-02 requires lessees to classify leases as either finance or operating leases and to record a right-of-use asset and a lease liability for all leases with a term greater than 12 months regardless of the lease classification. The lease classification will determine whether the lease expense is recognized based on an effective interest rate method or on a straight line basis over the term of the lease. Accounting for lessors remains largely unchanged from current GAAP. ASU 2016-02 is effective for the Company beginning November 1, 2019. Early adoption is permitted. In July 2018, the FASB issued ASU No. 2018-10 "Codification Improvements to Topic 842, Leases" ("ASU 2018-10") and ASU No. 2018-11 "Leases (Topic 842) Targeted Improvements" ("ASU 2018-11"). ASU 2018-10 provides certain amendments that affect narrow aspects of the guidance issued in ASU 2016-02. ASU 2018-11 allows all entities adopting ASU 2016-02 to choose an additional (and optional) transition method of adoption, under which an entity initially applies the new leases standard at the adoption date and recognizes a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption. ASU 2018-11 also allows lessors to not separate nonlease components from the associated lease component if certain conditions are met. We are currently evaluating both the method and the impact of adopting this guidance on our Condensed Consolidated Financial Statements.

In July 2018, the FASB issued ASU No. 2018-09, "Codification Improvements" ("ASU 2018-09"). ASU 2018-09 provides amendments to a wide variety of topics in the FASB's Accounting Standards Codification, which applies to all reporting entities within the scope of the affected accounting guidance. The transition and effective date guidance are based on the facts and circumstances of each amendment. Some of the amendments in ASU 2018-09 do not require transition guidance and were effective upon issuance of ASU 2018-09. However, many of the amendments do have transition guidance with effective dates for annual periods beginning after December 15, 2018. We are currently evaluating the potential impact of adopting the applicable guidance on our Condensed Consolidated Financial Statements.

In August 2018, the FASB issued ASU No. 2018-13, "Fair Value Measurement (Topic 820) - Disclosure Framework" ("ASU 2018-13"), which improves the disclosure requirements for fair value measurements. ASU 2018-13 is effective for us beginning November 1, 2020. Early adoption is permitted for any removed or modified disclosures. We are currently evaluating the potential impact of adopting this guidance on our Condensed Consolidated Financial Statements.

In August 2018, the FASB issued ASU No. 2018-15 "Intangibles-Goodwill and Other-Internal-Use Software (Subtopic 350-40): Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That is a Service Contract" ("ASU 2018-15"). ASU 2018-15 aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software. ASU 2018-15 is effective for us beginning November 1, 2020. Early adoption is permitted. We are currently evaluating the potential impact of adopting this guidance on our Condensed Consolidated Financial Statements.

19. Fair Value of Financial Instruments

ASC 820, “Fair Value Measurements and Disclosures,” provides a framework for measuring fair value, expands disclosures about fair-value measurements and establishes a fair-value hierarchy which prioritizes the inputs used in measuring fair value summarized as follows:

- Level 1: Fair value determined based on quoted prices in active markets for identical assets.
- Level 2: Fair value determined using significant other observable inputs.
- Level 3: Fair value determined using significant unobservable inputs.

Our financial instruments measured at fair value on a recurring basis are summarized below:

| (In thousands) | Fair Value Hierarchy | Fair Value at April 30, 2019 | Fair Value at October 31, 2018 |
|----------------------------------|-------------------------|------------------------------------|--------------------------------------|
| Mortgage loans held for sale (1) | Level 2 | \$91,211 | \$130,709 |
| Interest rate lock commitments | Level 2 | 17 | (28) |
| Forward contracts | Level 2 | 21 | 13 |
| Total | | \$91,249 | \$130,694 |

(1) The aggregate unpaid principal balance was \$88.3 million and \$127.6 million at April 30, 2019 and October 31, 2018, respectively.

We elected the fair value option for our loans held for sale, in accordance with ASC 825, “Financial Instruments,” which permits us to measure financial instruments at fair value on a contract-by-contract basis. Management believes that the election of the fair value option for loans held for sale improves financial reporting by mitigating volatility in reported earnings caused by measuring the fair value of the loans and the derivative instruments used to economically hedge them without having to apply complex hedge accounting provisions. Fair value of loans held for sale is based on independent quoted market prices, where available, or the prices for other mortgage loans with similar characteristics.

The Financial Services segment had a pipeline of loan applications in process of \$544.2 million at April 30, 2019. Loans in process for which interest rates were committed to the borrowers totaled \$47.2 million as of April 30, 2019. Substantially all of these commitments were for periods of 60 days or less. Since a portion of these commitments is expected to expire without being exercised by the borrowers, the total commitments do not necessarily represent future cash requirements.

The Financial Services segment uses investor commitments and forward sales of mandatory MBS to hedge its mortgage-related interest rate exposure. These instruments involve, to varying degrees, elements of credit and interest rate risk. Credit risk is managed by entering into MBS forward commitments, option contracts with investment banks, federally regulated bank affiliates and loan sales transactions with permanent investors meeting the segment’s credit standards. The segment’s risk, in the event of default by the purchaser, is the difference between the contract price and fair value of the MBS forward commitments and option contracts. At April 30, 2019, the segment had open commitments amounting to \$18.0 million to sell MBS with varying settlement dates through May 21, 2019.

The assets accounted for using the fair value option are initially measured at fair value. Gains and losses from initial measurement and subsequent changes in fair value are recognized in the Condensed Consolidated Financial Statements in “Revenues: Financial services.” The fair values that are included in income are shown, by financial instrument and financial statement line item, below:

| (In thousands) | Three Months Ended April 30, 2019 | | |
|--|------------------------------------|--------------------------------------|----------------------|
| | Mortgage Loans Held For Sale | Interest Rate Lock Commitments | Forward Contracts |
| Fair value included in net loss all reflected in financial services revenues | \$946 | \$(208) | \$406 |

| (In thousands) | Three Months Ended April 30, 2018 | | |
|--|------------------------------------|--------------------------------------|----------------------|
| | Mortgage Loans Held For Sale | Interest Rate Lock Commitments | Forward Contracts |
| Fair value included in net loss all reflected in financial services revenues | \$127 | \$178 | \$(143) |

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| (In thousands) | Six Months Ended April 30, 2019 | | |
|--|------------------------------------|--------------------------------------|----------------------|
| | Mortgage Loans Held For Sale | Interest Rate Lock Commitments | Forward Contracts |
| Fair value included in net loss all reflected in financial services revenues | \$2,942 | \$17 | \$21 |

| (In thousands) | Six Months Ended April 30, 2018 | | |
|--|------------------------------------|--------------------------------------|----------------------|
| | Mortgage Loans Held For Sale | Interest Rate Lock Commitments | Forward Contracts |
| Fair value included in net loss all reflected in financial services revenues | \$2,541 | \$(70) | \$125 |

The Company's assets measured at fair value on a nonrecurring basis are those assets for which the Company has recorded valuation adjustments and write-offs during the three and six months ended April 30, 2019 and 2018. The assets measured at fair value on a nonrecurring basis are all within the Company's Homebuilding operations and are summarized below:

Nonfinancial Assets

| (In thousands) | Fair Value Hierarchy | Three Months Ended April 30, 2019 | | Fair Value |
|---|----------------------------|--------------------------------------|-----------------|------------|
| | | Pre-Impairment Amount | Total Losses | |
| Sold and unsold homes and lots under development | Level 3 | \$3,906 | \$(968) | \$2,938 |
| Land and land options held for future development or sale | Level 3 | \$- | \$- | \$- |

| (In thousands) | Fair Value Hierarchy | Three Months Ended April 30, 2018 | | Fair Value |
|---|----------------------------|--------------------------------------|-----------------|------------|
| | | Pre-Impairment Amount | Total Losses | |
| Sold and unsold homes and lots under development | Level 3 | \$11,170 | \$(2,117) | \$9,053 |
| Land and land options held for future development or sale | Level 3 | \$- | \$- | \$- |

| (In thousands) | Fair Value Hierarchy | Six Months Ended April 30, 2019 | | Fair Value |
|---|----------------------------|------------------------------------|-----------------|------------|
| | | Pre-Impairment Amount | Total Losses | |
| Sold and unsold homes and lots under development | Level 3 | \$3,906 | \$(968) | \$2,938 |
| Land and land options held for future development or sale | Level 3 | \$6,302 | \$(43) | \$6,259 |

| (In thousands) | Fair Value Hierarchy | Six Months Ended April 30, 2018 | | Fair Value |
|---|----------------------------|------------------------------------|-----------------|------------|
| | | Pre-Impairment Amount | Total Losses | |
| Sold and unsold homes and lots under development | Level 3 | \$11,170 | \$(2,117) | \$9,053 |
| Land and land options held for future development or sale | Level 3 | \$- | \$- | \$- |

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We record impairment losses on inventories related to communities under development and held for future development when events and circumstances indicate that they may be impaired and the undiscounted cash flows estimated to be generated by those assets are less than their related carrying amounts. If the expected undiscounted cash flows are less than the carrying amount, then the community is written down to its fair value. We estimate the fair value of each impaired community by determining the present value of its estimated future cash flows at a discount rate commensurate with the risk of the respective community. Should the estimates or expectations used in determining cash flows or fair value decrease or differ from current estimates in the future, we may be required to recognize additional impairments. We recorded inventory impairments, which are included in the Condensed Consolidated Statements of Operations as “Inventory impairment loss and land option write-offs” and deducted from inventory, of \$1.0 million for both the three and six months ended April 30, 2019, and \$2.1 million for both the three and six months ended April 30, 2018. See Note 4 for further detail of the communities evaluated for impairment.

The fair value of our cash equivalents, restricted cash and cash equivalents and customer’s deposits approximates their carrying amount, based on Level 1 inputs.

The fair value of each series of our Notes are listed below. Level 2 measurements are estimated based on recent trades or quoted market prices for the same issues or based on recent trades or quoted market prices for our debt of similar security and maturity to achieve comparable yields. Level 3 measurements are estimated based on third-party broker quotes or management’s estimate of the fair value based on available trades for similar debt instruments.

Fair Value as of April 30, 2019

| (In thousands) | Level 1 | Level 2 | Level 3 | Total |
|---|------------|------------------|------------------|--------------------|
| Senior Secured Notes: | | | | |
| 9.5% Senior Secured Notes due November 15, 2020 | \$- | \$- | \$71,250 | \$71,250 |
| 2.0% Senior Secured Notes due November 1, 2021 | - | - | 46,978 | 46,978 |
| 5.0% Senior Secured Notes due November 1, 2021 | - | 129,780 | - | 129,780 |
| 10.0% Senior Secured Notes due July 15, 2022 | - | 387,200 | - | 387,200 |
| 10.5% Senior Secured Notes due July 15, 2024 | - | 347,438 | - | 347,438 |
| Senior Notes: | | | | |
| 13.5% Senior Notes due February 1, 2026 | - | 84,815 | - | 84,815 |
| 5.0% Senior Notes due February 1, 2040 | - | 35,485 | - | 35,485 |
| Senior Unsecured Term Loan Credit Facility due February 1, 2027 | - | - | 110,389 | 110,389 |
| Total fair value | \$- | \$984,718 | \$228,617 | \$1,213,335 |

Fair Value as of October 31, 2018

| (In thousands) | Level 1 | Level 2 | Level 3 | Total |
|---|------------|--------------------|------------------|--------------------|
| Senior Secured Notes: | | | | |
| 9.5% Senior Secured Notes due November 15, 2020 | \$- | \$- | \$74,250 | \$74,250 |
| 2.0% Senior Secured Notes due November 1, 2021 | - | - | 40,434 | 40,434 |
| 5.0% Senior Secured Notes due November 1, 2021 | - | 124,781 | - | 124,781 |
| 10.0% Senior Secured Notes due July 15, 2022 | - | 424,670 | - | 424,670 |
| 10.5% Senior Secured Notes due July 15, 2024 | - | 366,720 | - | 366,720 |
| Senior Notes: | | | | |
| 13.5% Senior Notes due February 1, 2026 | - | 88,148 | - | 88,148 |
| 5.0% Senior Notes due February 1, 2040 | - | 35,628 | - | 35,628 |
| Senior Unsecured Term Loan Credit Facility due February 1, 2027 | - | - | 114,328 | 114,328 |
| Total fair value | \$- | \$1,039,947 | \$229,012 | \$1,268,959 |

The Senior Secured Revolving Credit Facility is not included in the above tables because there were no borrowings outstanding thereunder as of April 30, 2019 and October 31, 2018.

20. Transactions with Related Parties

During the three months ended April 30, 2019 and 2018, an engineering firm owned by Tavit Najarian, a relative of Ara K. Hovnanian, our Chairman of the Board of Directors and our Chief Executive Officer, provided services to the Company totaling \$0.3 million and \$0.2 million, respectively. During the six months ended April 30, 2019 and 2018, the services provided by such engineering firm to the Company totaled \$0.4 million and \$0.3 million, respectively. Neither the Company nor Mr. Hovnanian has a financial interest in the relative’s company from whom the services were provided.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Hovnanian Enterprises, Inc. ("HEI") conducts all of its homebuilding and financial services operations through its subsidiaries (references herein to the "Company," "we," "us" or "our" refer to HEI and its consolidated subsidiaries and should be understood to reflect the consolidated business of HEI's subsidiaries).

Overview

Our community count increased 7.3% sequentially during the second quarter of fiscal 2019, from 137 communities at January 31, 2019 to 147 at April 30, 2019, and also increased 11.4% from 132 communities at April 30, 2018. Our total number of lots controlled increased in the second quarter of fiscal 2019, as compared to the same period of the prior year, which is the sixth consecutive quarter for which we have experienced a year-over-year quarterly increase. We believe continued growth in lots controlled should lead to further community count growth, and our fiscal 2017 and 2018 financing transactions have provided us with the capital needed to implement our investment strategy to grow our business. However, there is typically a significant time lag from when we first control lots until the time that we open a community for sale. This timeline can vary significantly from a few months (in a market such as Houston) to three to five plus years (in a market such as New Jersey). Given the mix of land that we control and the land investment we anticipate, we currently believe that our community count will continue to grow in the third quarter of fiscal 2019. Ultimately, community count growth, absent adverse market factors, should lead to delivery and revenue growth in the future.

Our cash position during the first half of fiscal 2019 allowed us to spend \$252.6 million on land purchases and land development during the period, and still have total liquidity of \$266.0 million, including \$124.0 million of homebuilding cash and cash equivalents as of April 30, 2019. We continue to see opportunities to purchase land at prices that make economic sense in light of our current sales prices, sales pace and construction costs and plan to continue actively pursuing such land acquisitions. New land purchases at pricing that we believe will generate appropriate investment returns and drive greater operating efficiencies are needed to return to sustained profitability. However, given the slower sales absorption pace in the fourth quarter of fiscal 2018 and the second quarter of fiscal 2019 compared to the same periods of the prior years, we remain cautious and are carefully evaluating market conditions when pursuing new land acquisitions. For example, among other market conditions, we are carefully monitoring the potential impact of the current trade and tariff negotiations and the related market volatility on our business and results of operations. Although the tariffs recently imposed on products from China and elsewhere have not had a material impact on our financial results to date, future tariffs or the threat thereof may have a more significant impact on our business and on our customers' budgets.

Additional results for the three and six months ended April 30, 2019 were as follows:

- For the three and six months ended April 30, 2019, sale of homes revenues decreased 8.7% and 9.2%, respectively, as compared to the same periods of the prior year, as a result of a 10.7% and 8.4% decrease in deliveries, respectively.
- Gross margin percentage decreased from 13.8% and 14.3% for the three and six months ended April 30, 2018, respectively, to 13.3% and 14.0% for the three and six months ended April 30, 2019, respectively. Gross margin percentage, before cost of sales interest expense and land charges, decreased from 17.7% and 17.8% for the three and six months ended April 30, 2018 to 16.9% and 17.3% for the three and six months ended April 30, 2019, respectively.
- Selling, general and administrative costs (including corporate general and administrative expenses) decreased \$1.3 million for the three months ended April 30, 2019 and \$3.3 million for the six months ended April 30, 2019, respectively, as compared to the same periods of the prior year. As a percentage of total revenue, such costs increased from 12.3% for the three months ended April 30, 2018 to 13.7% for the three months ended April 30, 2019 and increased from 13.5% for the six months ended April 30, 2018 to 14.7% for the six months ended April 30, 2019.
- Active selling communities increased 11.4% over last year's second quarter. Net contracts increased 10.1% and 2.0% for the three and six months ended April 30, 2019, respectively, compared to the same periods of the prior year.
- Net contracts per average active selling community decreased slightly to 10.5 for the three months ended April 30, 2019 compared to 10.6 in the same period of the prior year, and increased slightly to 18.2 for the six months ended April 30, 2019 compared to 18.1 in the same period of the prior year.
- Contract backlog increased from 2,193 homes at April 30, 2018 to 2,254 homes at April 30, 2019, with a dollar value of \$949.9 million, representing a 5.5% increase in dollar value compared to the prior year.

When comparing sequentially from the first quarter of fiscal 2019 to the second quarter of fiscal 2019, our gross margin percentage decreased from 14.8% to 13.3% primarily due to increased land charges and increased incentives, particularly on spec homes that were sold and delivered during the quarter. Gross margin percentage, before cost of sales interest expense and land charges, decreased from 17.8% to 16.9% primarily due to the increased incentives during the quarter. Selling, general and administrative costs (including corporate general and administrative expenses) decreased slightly from \$60.4 million in the first quarter of fiscal 2019 to \$60.3 million in the second quarter of fiscal 2019, and, as a percentage of total revenues, these costs decreased from 15.9% in the first quarter of fiscal 2019 to 13.7% in the second quarter of fiscal 2019 due to the increase in revenues. Improving the efficiency of our selling, general and administrative expenses continues to be a significant area of focus.

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CRITICAL ACCOUNTING POLICIES

As disclosed in our annual report on Form 10-K for the fiscal year ended October 31, 2018, our most critical accounting policies relate to income recognition from mortgage loans; inventories; unconsolidated joint ventures; post-development completion, warranty and insurance reserves; and deferred income taxes. Since October 31, 2018, there have been no significant changes to those critical accounting policies.

CAPITAL RESOURCES AND LIQUIDITY

Our operations consist primarily of residential housing development and sales in the Northeast (New Jersey and Pennsylvania), the Mid-Atlantic (Delaware, Maryland, Virginia, Washington D.C. and West Virginia), the Midwest (Illinois and Ohio), the Southeast (Florida, Georgia and South Carolina), the Southwest (Arizona and Texas) and the West (California). In addition, we provide certain financial services to our homebuilding customers.

We have historically funded our homebuilding and financial services operations with cash flows from operating activities, borrowings under our credit facilities, the issuance of new debt and equity securities and other financing activities. Due to covenant restrictions in our debt instruments, we are currently limited in the amount of debt we can incur that does not qualify as refinancing indebtedness with certain maturity requirements (a limitation that we expect to continue for the foreseeable future), even if market conditions would otherwise be favorable, which could also impact our ability to grow our business.

Operating, Investing and Financing Activities – Overview

Our homebuilding cash balance at April 30, 2019 decreased \$63.9 million from October 31, 2018. We spent \$252.6 million on land and land development during the period. After considering this land and land development and all other operating activities, including revenue received from deliveries, we used \$198.9 million of cash from operations. However, as of April 30, 2019, we had \$125.0 million of borrowing capacity under our Secured Credit Facility (defined below), and therefore, our total liquidity at April 30, 2019 was \$266.0 million, which is above our target liquidity range of \$170.0 to \$245.0 million. During the first half of fiscal 2019, we used \$3.9 million of cash for investing activities, primarily for investments in joint ventures, partially offset by distributions from joint ventures. Cash provided by financing activities was \$138.4 million during the first half of fiscal 2019 which included proceeds of \$21.3 million from a debt issuance, \$60.7 million from land banking and model sale leaseback programs and \$96.3 million of net proceeds from nonrecourse mortgages, partially offset by a \$36.6 million reduction in mortgage warehouse lines of credit. We intend to continue to use nonrecourse mortgage financings, model sale leaseback, joint ventures, and, subject to covenant restrictions in our debt instruments, land banking programs as our business needs dictate.

Our cash uses during the six months ended April 30, 2019 and 2018 were for operating expenses, land purchases, land deposits, land development, construction spending, debt payments, state income taxes, interest payments, litigation matters and investments in joint ventures. During these periods, we provided for our cash requirements from available cash on hand, housing and land sales, financing transactions, model sale leasebacks, land banking transactions, joint ventures, financial service revenues and other revenues. We believe that these sources of cash together with our Secured Credit Facility will be sufficient through fiscal 2019 to finance our working capital requirements.

Our net income (loss) historically does not approximate cash flow from operating activities. The difference between net income (loss) and cash flow from operating activities is primarily caused by changes in inventory levels together with changes in receivables, prepaid and other assets, mortgage loans held for sale, interest and other accrued liabilities, deferred income taxes, accounts payable and other liabilities, and noncash charges relating to depreciation, stock compensation awards and impairment losses for inventory. When we are expanding our operations, inventory levels, prepaids and other assets increase causing cash flow from operating activities to decrease. Certain liabilities also increase as operations expand and partially offset the negative effect on cash flow from operations caused by the increase in inventory levels, prepaids and other assets. Similarly, as our mortgage operations expand, net income from these operations increases, but for cash flow purposes net income is partially offset by the net change in mortgage assets and liabilities. The opposite is true as our investment in new land purchases and development of new communities decrease, causing us to generate positive cash flow from operations. In fiscal 2019 and 2018, with continued spending on land purchases and land development, we used cash in operations. As we continue to actively seek land investment opportunities, we will also remain focused on liquidity.

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Debt Transactions

As of April 30, 2019, we had \$1,135.0 million of outstanding senior secured notes (\$1,116.8 million, net of discount and debt issuance costs), comprised of \$53.2 million 2.0% 2021 Notes (defined below), \$141.8 million 5.0% 2021 Notes (defined below), \$75.0 million 9.5% 2020 Notes (defined below), \$440.0 million 10.0% Senior Secured Notes due 2022 and \$425.0 million 10.5% Senior Secured Notes due 2024. As of April 30, 2019, we also had \$180.7 million of outstanding senior notes (\$144.3 million net of discount, premium and debt issuance costs), comprised of \$90.1 million 5.0% Senior Notes due 2040 and \$90.6 million 13.5% Senior Notes due 2026 (\$26.0 million of 8.0% Senior Notes due 2019 are owned by a wholly-owned consolidated subsidiary of HEI and therefore, in accordance with GAAP, such notes are not reflected on the Condensed Consolidated Balance Sheets of HEI). In addition, as of April 30, 2019, there were \$202.5 million (\$201.5 million net of debt issuance costs) of borrowings under our senior unsecured term loan facility (“Term Loan Facility”). As of April 30, 2019, we did not have any borrowings outstanding under our \$125.0 million secured revolving credit facility (the “Secured Credit Facility” and together with the Term Loan Facility, the “Credit Facilities”).

Except for K. Hovnanian, the issuer of the notes and borrower under the Credit Facilities (as defined below), our home mortgage subsidiaries, joint ventures and subsidiaries holding interests in our joint ventures and certain of our title insurance subsidiaries, we and each of our subsidiaries are guarantors of the Credit Facilities, the senior secured notes and senior notes outstanding at April 30, 2019 (collectively, the “Notes Guarantors”). In addition to the Notes Guarantors, the 5.0% Senior Secured Notes due 2021 (the “5.0% 2021 Notes”), the 2.0% Senior Secured Notes due 2021 (the “2.0% 2021 Notes” and together with the 5.0% 2021 Notes, the “2021 Notes”) and the 9.50% Senior Secured Notes due 2020 (the “9.50% 2020 Notes” and collectively with the 2021 Notes, the “JV Holdings Secured Group Notes”) are guaranteed by K. Hovnanian JV Holdings, L.L.C. and its subsidiaries, except for certain joint ventures and joint venture holding companies (collectively, the “JV Holdings Secured Group”). Members of the JV Holdings Secured Group do not guarantee K. Hovnanian's other indebtedness.

The credit agreements governing the Credit Facilities and the indentures governing the notes (together, the “Debt Instruments”) outstanding at April 30, 2019 do not contain any financial maintenance covenants, but do contain restrictive covenants that limit, among other things, the Company's ability and that of certain of its subsidiaries, including K. Hovnanian, to incur additional indebtedness (other than nonrecourse indebtedness, certain permitted indebtedness and refinancing indebtedness (under the 9.50% 2020 Notes, any new or refinancing indebtedness may not be scheduled to mature earlier than January 15, 2021 (so long as no member of the JV Holdings Secured Group is an obligor thereon), or February 15, 2021 (if otherwise), and under the 10.0% Senior Secured Notes due 2022 (the “10.0% 2022 Notes”), any refinancing indebtedness of K. Hovnanian's previously outstanding 7.0% Senior Notes due 2019 (the “7.0% Notes”) (which includes the Term Loans (as defined below)) and 8.0% Senior Notes due 2019 (the “8.0% Notes” and together with the 7.0% Notes, the “2019 Notes”) (which includes the 13.5% Senior Notes due 2026 and the 5.0% Senior Notes due 2040 and the Term Loans) may not be scheduled to mature earlier than July 16, 2024 (such restrictive covenant in respect of the 10.5% Senior Secured Notes due 2024 (the “10.5% 2024 Notes”) was eliminated in fiscal 2018)), pay dividends and make distributions on common and preferred stock, repurchase subordinated indebtedness and common and preferred stock, make other restricted payments, including investments, sell certain assets (including in certain land banking transactions), incur liens, consolidate, merge, sell or otherwise dispose of all or substantially all assets, enter into certain transactions with affiliates and make cash repayments of the 2019 Notes and refinancing indebtedness in respect thereof (with respect to the 10.0% 2022 Notes). The Debt Instruments also contain events of default which would permit the lenders or holders thereof to exercise remedies with respect to the collateral (as applicable), declare the loans made under the Term Loan Facility (the “Term Loans”) and loans made under the Secured Credit Facility (the “Secured Revolving Loans”) or notes to be immediately due and payable if not cured within applicable grace periods, including the failure to make timely payments on the Term Loans, Secured Revolving Loans or notes or other material indebtedness, cross default to other material indebtedness, the failure to comply with agreements and covenants and specified events of bankruptcy and insolvency, with respect to the Term Loans and Secured Revolving Loans, material inaccuracy of representations and warranties and with respect to the Term Loans and Secured Revolving Loans, a change of control, and, with respect to the Secured Revolving Loans and senior secured notes, the failure of the documents granting security for the Secured Revolving Loans and senior secured notes to be in full force and effect, and the failure of the liens on any material portion of the collateral securing the Secured Revolving Loans and senior secured notes to be valid and perfected. As of April 30, 2019, we believe we were in compliance with the covenants of the Debt Instruments.

If our consolidated fixed charge coverage ratio, as defined in the agreements governing our debt instruments, is less than 2.0 to 1.0, we are restricted from making certain payments, including dividends, and from incurring indebtedness other than certain permitted indebtedness, refinancing indebtedness and nonrecourse indebtedness. As a result of this ratio restriction, we are currently restricted from paying dividends, which are not cumulative, on our 7.625% Series A Preferred Stock. We anticipate that we will continue to be restricted from paying dividends for the foreseeable future. Our inability to pay dividends is in accordance with covenant restrictions and will not result in a default under our debt instruments or otherwise affect compliance with any of the covenants contained in our debt instruments.

Under the terms of our Debt Instruments, we have the right to make certain redemptions and prepayments and, depending on market conditions and covenant restrictions, may do so from time to time. We also continue to evaluate our capital structure and may also continue to make debt purchases and/or exchanges for debt or equity from time to time through tender offers, open market purchases, private transactions, or otherwise, or seek to raise additional debt or equity capital, depending on market conditions and covenant restrictions.

Any liquidity-enhancing or other capital raising or refinancing transaction will depend on identifying counterparties, negotiation of documentation and applicable closing conditions and any required approvals. Due to covenant restrictions in our Debt Instruments, we are currently limited in the amount of debt we can incur that does not qualify as refinancing indebtedness with certain maturity requirements as discussed above (a limitation that we expect to continue for the foreseeable future), even if market conditions would otherwise be favorable, which could also impact our ability to grow our business.

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In addition to the Secured Credit Facility, we have certain stand-alone cash collateralized letter of credit agreements and facilities under which there was a total of \$16.2 million and \$12.5 million letters of credit outstanding at April 30, 2019 and October 31, 2018, respectively. These agreements and facilities require us to maintain specified amounts of cash as collateral in segregated accounts to support the letters of credit issued thereunder, which will affect the amount of cash we have available for other uses. At April 30, 2019 and October 31, 2018, the amount of cash collateral in these segregated accounts was \$17.0 million and \$12.7 million, respectively, which is reflected in “Restricted cash and cash equivalents” on the Condensed Consolidated Balance Sheets.

See Note 11 to the Condensed Consolidated Financial Statements included elsewhere in this Quarterly Report on Form 10-Q for a further discussion of the Term Loan Facility, the Secured Credit Facility and K. Hovnanian’s senior secured notes and senior notes.

Mortgages and Notes Payable

We have nonrecourse mortgage loans for certain communities totaling \$190.7 million and \$95.6 million (net of debt issuance costs) at April 30, 2019 and October 31, 2018, respectively, which are secured by the related real property, including any improvements, with an aggregate book value of \$374.9 million and \$241.9 million, respectively. The weighted-average interest rate on these obligations was 8.4% and 6.1% at April 30, 2019 and October 31, 2018, respectively, and the mortgage loan payments on each community primarily correspond to home deliveries.

Our wholly owned mortgage banking subsidiary, K. Hovnanian American Mortgage, LLC (“K. Hovnanian Mortgage”), originates mortgage loans primarily from the sale of our homes. Such mortgage loans and related servicing rights are sold in the secondary mortgage market within a short period of time. In certain instances, we retain the servicing rights for a small amount of loans. The loans are secured by the mortgages held for sale and repaid when we sell the underlying mortgage loans to permanent investors. As of April 30, 2019 and October 31, 2018, we had an aggregate of \$76.5 million and \$113.2 million, respectively, outstanding under several of K. Hovnanian Mortgage’s short-term borrowing facilities.

See Note 10 to the Condensed Consolidated Financial Statements for a discussion of these agreements.

Inventory Activities

Total inventory, excluding consolidated inventory not owned, increased \$123.4 million during the six months ended April 30, 2019 from October 31, 2018. Total inventory, excluding consolidated inventory not owned, increased in the Northeast by \$17.4 million, in the Mid-Atlantic by \$44.9 million, in the Midwest by \$28.6 million, in the Southeast by \$5.5 million, in the Southwest by \$15.8 million and in the West by \$11.2 million. The increases were primarily attributable to new land purchases and land development, partially offset by home deliveries during the period. During the six months ended April 30, 2019, we had impairments in the amount of \$1.0 million. We wrote-off costs in the amount of \$1.2 million during the six months ended April 30, 2019 related to land options that expired or that we terminated, as the communities’ forecasted profitability was not projected to produce adequate returns on investment commensurate with the risk. In the last few years, we have been able to acquire new land parcels at prices that we believe will generate reasonable returns under current homebuilding market conditions. There can be no assurances that this trend will continue in the near term. Substantially all homes under construction or completed and included in inventory at April 30, 2019 are expected to be delivered during the next six to nine months.

Consolidated inventory not owned increased \$66.5 million. Consolidated inventory not owned consists of options related to land banking and model financing transactions that were added to our Condensed Consolidated Balance Sheets in accordance with US GAAP. The increase from October 31, 2018 to April 30, 2019 was primarily due to an increase in land banking transactions along with an increase in the sale and leaseback of certain model homes during the period. We have land banking arrangements, whereby we sell land parcels to the land bankers and they provide us an option to purchase back finished lots on a predetermined schedule. Because of our options to repurchase these parcels, for accounting purposes in accordance with ASC 606-10-55-70, these transactions are considered a financing rather than a sale. For purposes of our Condensed Consolidated Balance Sheets, at April 30, 2019, inventory of \$96.0 million was recorded to “Consolidated inventory not owned,” with a corresponding amount of \$71.2 million (net of debt issuance costs) recorded to “Liabilities from inventory not owned” for the amount of net cash received from the transactions. In addition, we sell and lease back certain of our model homes with the right to participate in the potential profit when each home is sold to a third party at the end of the respective lease. As a result of our continued involvement, for accounting purposes in accordance with ASC 606-10-55-68, these sale and leaseback transactions are considered a financing rather than a sale. Therefore, for purposes of our Condensed Consolidated Balance Sheets, at April 30, 2019, inventory of \$58.4 million was recorded to “Consolidated inventory not owned,” with a corresponding amount of \$52.1 million (net of debt issuance costs) recorded to “Liabilities from inventory not owned” for the amount of net cash received from the transactions. From time to time, we enter into option agreements that include specific performance requirements, whereby we are required to purchase a minimum number of lots. Because of our obligation to purchase these lots, for accounting purposes in accordance with ASC 360-20-40-38, we are required to record this inventory on our Condensed Consolidated Balance Sheets. As of April 30, 2019, we had no specific performance options.

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When possible, we option property for development prior to acquisition. By optioning property, we are only subject to the loss of the cost of the option and predevelopment costs if we choose not to exercise the option (other than with respect to specific performance options discussed above). As a result, our commitment for major land acquisitions is reduced. The costs associated with optioned properties are included in “Land and land options held for future development or sale” on the Condensed Consolidated Balance Sheets. Also included in “Land and land options held for future development or sale” are amounts associated with inventory in mothballed communities. We mothball (or stop development on) certain communities when we determine the current performance does not justify further investment at the time. That is, we believe we will generate higher returns if we decide against spending money to improve land today and save the raw land until such time as the markets improve or we determine to sell the property. As of April 30, 2019, we had mothballed land in 14 communities. The book value associated with these communities at April 30, 2019 was \$14.2 million, which was net of impairment charges recorded in prior periods of \$146.9 million. We continually review communities to determine if mothballing is appropriate. During the first half of fiscal 2019, we did not mothball any additional communities, but we sold two previously mothballed communities and re-activated two previously mothballed communities.

Inventories held for sale, which are land parcels where we have decided not to build homes and are actively marketing the land for sale, represented \$0.1 million and \$6.4 million, respectively, of our total inventories at April 30, 2019 and October 31, 2018, and are reported at the lower of carrying amount or fair value less costs to sell. In determining fair value for land held for sale, management considers, among other things, prices for land in recent comparable sale transactions, market analysis studies, which include the estimated price a willing buyer would pay for the land (other than in a forced liquidation sale) and recent bona fide offers received from outside third parties.

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The following tables summarize home sites included in our total residential real estate.

| | Active Communities(1) | Active Communities Homes | Proposed Developable Homes | Total Homes |
|--|--------------------------|--------------------------------|----------------------------------|----------------|
| April 30, 2019: | | | | |
| Northeast | 6 | 646 | 3,371 | 4,017 |
| Mid-Atlantic | 20 | 2,054 | 3,597 | 5,651 |
| Midwest | 16 | 1,670 | 2,855 | 4,525 |
| Southeast | 15 | 2,432 | 1,901 | 4,333 |
| Southwest | 71 | 4,633 | 2,654 | 7,287 |
| West | 19 | 2,492 | 3,019 | 5,511 |
| Consolidated total | <u>147</u> | <u>13,927</u> | <u>17,397</u> | <u>31,324</u> |
| Unconsolidated joint ventures(2) | <u>18</u> | <u>3,343</u> | <u>230</u> | <u>3,573</u> |
| Owned | | 8,171 | 4,314 | 12,485 |
| Optioned | | <u>5,519</u> | <u>13,083</u> | <u>18,602</u> |
| Controlled lots | | 13,690 | 17,397 | 31,087 |
| Construction to permanent financing lots | | <u>237</u> | - | <u>237</u> |
| Consolidated total | | <u>13,927</u> | <u>17,397</u> | <u>31,324</u> |

(1) Active communities are open for sale communities with ten or more home sites available.

(2) Represents active communities and home sites for our unconsolidated homebuilding joint ventures for the period. We provide this data as a supplement to our consolidated results as an indicator of the volume managed in our unconsolidated joint ventures. See Note 17 to the Condensed Consolidated Financial Statements for a further discussion of our unconsolidated joint ventures.

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| | Active Communities(1) | Active Communities Homes | Proposed Developable Homes | Total Homes |
|--|-----------------------|--------------------------|----------------------------|-------------|
| October 31, 2018: | | | | |
| Northeast | 4 | 691 | 3,229 | 3,920 |
| Mid-Atlantic | 20 | 1,681 | 3,114 | 4,795 |
| Midwest | 14 | 1,774 | 2,984 | 4,758 |
| Southeast | 14 | 2,323 | 2,348 | 4,671 |
| Southwest | 56 | 3,884 | 2,899 | 6,783 |
| West | 15 | 2,040 | 3,590 | 5,630 |
| Consolidated total | 123 | 12,393 | 18,164 | 30,557 |
| Unconsolidated joint ventures(2) | | | | |
| | 19 | 2,607 | 1,422 | 4,029 |
| Owned | | 8,018 | 4,711 | 12,729 |
| Optioned | | 4,157 | 13,453 | 17,610 |
| Controlled lots | | 12,175 | 18,164 | 30,339 |
| Construction to permanent financing lots | | 218 | - | 218 |
| Consolidated total | | 12,393 | 18,164 | 30,557 |

(1) Active communities are open for sale communities with ten or more home sites available.

(2) Represents active communities and home sites for our unconsolidated homebuilding joint ventures for the period. We provide this data as a supplement to our consolidated results as an indicator of the volume managed in our unconsolidated joint ventures. See Note 17 to the Condensed Consolidated Financial Statements for a further discussion of our unconsolidated joint ventures.

The following table summarizes our started or completed unsold homes and models, excluding unconsolidated joint ventures, in active and substantially completed communities.

| | April 30, 2019 | | | October 31, 2018 | | |
|---|----------------|--------|-------|------------------|--------|-------|
| | Unsold Homes | Models | Total | Unsold Homes | Models | Total |
| Northeast | 27 | 13 | 40 | 24 | 5 | 29 |
| Mid-Atlantic | 48 | 13 | 61 | 38 | 19 | 57 |
| Midwest | 39 | 10 | 49 | 19 | 10 | 29 |
| Southeast | 80 | 12 | 92 | 62 | 11 | 73 |
| Southwest | 325 | 9 | 334 | 335 | 14 | 349 |
| West | 133 | 18 | 151 | 93 | 12 | 105 |
| Total | 652 | 75 | 727 | 571 | 71 | 642 |
| Started or completed unsold homes and models per active selling communities | | | | | | |
| (1) | 4.4 | 0.5 | 4.9 | 4.6 | 0.6 | 5.2 |

(1) Active selling communities (which are communities that are open for sale with ten or more home sites available) were 147 and 123 at April 30, 2019 and October 31, 2018, respectively. This ratio does not include substantially completed communities, which are communities with less than ten home sites available.

[Table of Contents](#)*Other Balance Sheet Activities*

Homebuilding – Restricted cash and cash equivalents increased \$4.4 million from October 31, 2018 to \$17.2 million at April 30, 2019. The increase was primarily due to cash collateral for new letters of credit issued during the period.

Investments in and advances to unconsolidated joint ventures increased \$11.9 million to \$135.6 million at April 30, 2019 compared to October 31, 2018. The increase was primarily due to the income from two of our joint ventures in the first half of fiscal 2019, along with new capital contributions for existing joint ventures during the period. As of April 30, 2019 and October 31, 2018, we had investments in nine homebuilding joint ventures and one land development joint venture. We have no guarantees associated with our unconsolidated joint ventures, other than guarantees limited only to performance and completion of development, environmental indemnification and standard warranty and representation against fraud, misrepresentation and similar actions, including a voluntary bankruptcy.

Receivables, deposits and notes, net decreased \$6.0 million from October 31, 2018 to \$29.2 million at April 30, 2019. The decrease was primarily due to the return of a municipal receivable during the period, along with a decrease in receivables due to the timing of home closings during the period.

Prepaid expenses and other assets were as follows as of:

| (In thousands) | April 30, 2019 | October 31, 2018 | Dollar Change |
|-----------------------|-------------------|---------------------|------------------|
| Prepaid insurance | \$1,489 | \$2,514 | \$(1,025) |
| Prepaid project costs | 30,468 | 28,667 | 1,801 |
| Other prepaids | 7,934 | 7,505 | 429 |
| Other assets | 1,167 | 464 | 703 |
| Total | \$41,058 | \$39,150 | \$1,908 |

Prepaid insurance decreased during the six months ended April 30, 2019 due to the timing of premium payments. These costs are amortized over the life of the associated insurance policy, which can be one to three years. Prepaid project costs consist of community specific expenditures that are used over the life of the community. Such prepaids are generally spent at the beginning of a community's life and expensed as homes are delivered. Therefore prepaid project costs have increased as our community count increased during the period. Other assets increased primarily due to the timing of property tax payments in certain communities during the period.

Financial services assets consist primarily of residential mortgages receivable held for sale of which \$89.8 million and \$129.0 million at April 30, 2019 and October 31, 2018, respectively, were being temporarily warehoused and are awaiting sale in the secondary mortgage market. The decrease in mortgage loans held for sale from October 31, 2018 is related to a decrease in the volume of loans originated during the second quarter of 2019 compared to the fourth quarter of 2018, primarily due to the decrease in deliveries. Also contributing to the decrease in financial services other assets was a decrease in restricted cash due to the timing of home closings at the end of the fourth quarter of fiscal 2018 compared to the end of the second quarter of fiscal 2019.

Nonrecourse mortgages secured by inventory increased to \$190.7 million at April 30, 2019 from \$95.6 million at October 31, 2018. The increase was primarily due to a new mortgage on several communities that are part of a consolidated joint venture entered into in the second quarter of fiscal 2019, along with new mortgages for other communities in most of our segments obtained during the six months ended April 30, 2019, as well as additional loan borrowings on existing mortgages, partially offset by the payment of existing mortgages during the period.

Accounts payable and other liabilities are as follows as of:

| (In thousands) | April 30, 2019 | October 31, 2018 | Dollar Change |
|----------------------|-------------------|---------------------|-------------------|
| Accounts payable | \$131,662 | \$127,795 | \$3,867 |
| Reserves | 96,067 | 99,229 | (3,162) |
| Accrued expenses | 12,550 | 14,884 | (2,334) |
| Accrued compensation | 31,241 | 53,200 | (21,959) |
| Other liabilities | 13,773 | 9,791 | 3,982 |
| Total | \$285,293 | \$304,899 | \$(19,606) |

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Accrued expenses decreased primarily due to the timing of property tax payments. The decrease in accrued compensation was primarily due to the payment of our fiscal year 2018 bonuses during the first quarter of fiscal 2019, partially offset by the accrual of fiscal 2019 bonuses in the first six months of fiscal 2019. Other liabilities increased primarily due to several new municipal loans and bonds issued during the period. Both accounts payable and reserves had only minor fluctuations as a percentage of the total balance.

Customers' deposits increased \$7.9 million to \$38.0 million at April 30, 2019, primarily as a result of the increase in backlog during the period.

Liabilities from inventory not owned increased \$60.0 million to \$123.3 million at April 30, 2019. The increase was primarily due to an increase in land banking activity during the period, along with an increase in the sale and leaseback of certain model homes, both accounted for as financing transactions as described above.

Financial Services (liabilities) decreased \$43.3 million from \$143.4 million at October 31, 2018, to \$100.1 million at April 30, 2019. The decrease is primarily due to a decrease in amounts outstanding under our mortgage warehouse lines of credit, and directly correlates to the decrease in the volume of mortgage loans held for sale during the period.

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RESULTS OF OPERATIONS FOR THE THREE AND SIX MONTHS ENDED APRIL 30, 2019 COMPARED TO THE THREE AND SIX MONTHS ENDED APRIL 30, 2018

Total revenues

Compared to the same prior period, revenues decreased as follows:

| (Dollars in thousands) | Three Months Ended | | | |
|-------------------------------|--------------------|-------------------|-------------------|----------------------|
| | April 30, 2019 | April 30, 2018 | Dollar Change | Percentage Change |
| Homebuilding: | | | | |
| Sale of homes | \$427,552 | \$468,117 | \$(40,565) | (8.7)% |
| Land sales and other revenues | 832 | 21,373 | (20,541) | (96.1)% |
| Financial services | 12,307 | 13,054 | (747) | (5.7)% |
| Total revenues | <u>\$440,691</u> | <u>\$502,544</u> | <u>\$(61,853)</u> | <u>(12.3)%</u> |

| (Dollars in thousands) | Six Months Ended | | | |
|-------------------------------|-------------------|-------------------|-------------------|----------------------|
| | April 30, 2019 | April 30, 2018 | Dollar Change | Percentage Change |
| Homebuilding: | | | | |
| Sale of homes | \$789,687 | \$869,694 | \$(80,007) | (9.2)% |
| Land sales and other revenues | 9,683 | 26,074 | (16,391) | (62.9)% |
| Financial services | 21,915 | 23,942 | (2,027) | (8.5)% |
| Total revenues | <u>\$821,285</u> | <u>\$919,710</u> | <u>\$(98,425)</u> | <u>(10.7)%</u> |

Homebuilding

For the three and six months ended April 30, 2019, sale of homes revenues decreased \$40.6 million, or 8.7%, and \$80.0 million or 9.2%, respectively, as compared to the same periods of the prior year. These decreases were primarily due to the number of home deliveries decreasing 10.7% and 8.4% for the three and six months ended April 30, 2019, respectively, as compared to the prior year periods. The average price per home increased to \$394,057 in the three months ended April 30, 2019 from \$385,281 in the three months ended April 30, 2018. The average price per home decreased to \$384,838 in the six months ended April 30, 2019 from \$388,256 in the six months ended April 30, 2018. The changes in average prices were primarily the result of the geographic and community mix of our deliveries as opposed to home price changes (which we increase or decrease in communities depending on the respective community's performance). Land sales are ancillary to our homebuilding operations and are expected to continue in the future but may significantly fluctuate up or down. For details on the changes in segment revenues, see "Homebuilding Operations by Segment" below. For further details on the decreases in land sales and other revenues, see the section titled "Land Sales and Other Revenues" below.

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Information on homes delivered by segment is set forth below:

| (Dollars in thousands) | Three Months Ended April 30, | | | Six Months Ended April 30, | | |
|---|------------------------------|-----------|----------|----------------------------|-----------|----------|
| | 2019 | 2018 | % Change | 2019 | 2018 | % Change |
| Northeast: | | | | | | |
| Dollars | \$13,040 | \$23,513 | (44.5)% | \$25,545 | \$43,705 | (41.6)% |
| Homes | 23 | 47 | (51.1)% | 45 | 87 | (48.3)% |
| Mid-Atlantic: | | | | | | |
| Dollars | \$80,818 | \$104,058 | (22.3)% | \$133,997 | \$175,067 | (23.5)% |
| Homes | 142 | 206 | (31.1)% | 253 | 341 | (25.8)% |
| Midwest: | | | | | | |
| Dollars | \$42,870 | \$42,816 | 0.1% | \$87,759 | \$83,333 | 5.3% |
| Homes | 141 | 143 | (1.4)% | 290 | 283 | 2.5% |
| Southeast: | | | | | | |
| Dollars | \$49,346 | \$60,974 | (19.1)% | \$93,229 | \$117,648 | (20.8)% |
| Homes | 123 | 158 | (22.2)% | 231 | 290 | (20.3)% |
| Southwest: | | | | | | |
| Dollars | \$143,634 | \$158,958 | (9.6)% | \$261,497 | \$287,162 | (8.9)% |
| Homes | 431 | 466 | (7.5)% | 796 | 850 | (6.4)% |
| West: | | | | | | |
| Dollars | \$97,844 | \$77,798 | 25.8% | \$187,660 | \$162,779 | 15.3% |
| Homes | 225 | 195 | 15.4% | 437 | 389 | 12.3% |
| Consolidated total: | | | | | | |
| Dollars | \$427,552 | \$468,117 | (8.7)% | \$789,687 | \$869,694 | (9.2)% |
| Homes | 1,085 | 1,215 | (10.7)% | 2,052 | 2,240 | (8.4)% |
| Unconsolidated joint ventures(1) | | | | | | |
| Dollars | \$124,776 | \$96,296 | 29.6% | \$219,803 | \$154,395 | 42.4% |
| Homes | 195 | 208 | (6.3)% | 347 | 324 | 7.1% |

(1) Represents housing revenues and home deliveries for our unconsolidated homebuilding joint ventures for the period. We provide this data as a supplement to our consolidated results as an indicator of the volume managed in our unconsolidated joint ventures. See Note 17 to the Condensed Consolidated Financial Statements for a further discussion of our unconsolidated joint ventures.

As discussed above, the overall decrease in consolidated housing revenues during the three and six months ended April 30, 2019 as compared to the same periods of the prior year was primarily attributed to a decrease in the volume of deliveries as a result of new communities that are not yet delivering homes.

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An important indicator of our future results are recently signed contracts and our home contract backlog for future deliveries. Our sales contracts and homes in contract backlog by segment are set forth below:

| (Dollars in thousands) | Net Contracts (1) for the Three Months Ended April 30, | | Net Contracts (1) for the Six Months Ended April 30, | | Contract Backlog as of April 30, | |
|---|--|-----------|--|-----------|-------------------------------------|-----------|
| | 2019 | 2018 | 2019 | 2018 | 2019 | 2018 |
| Northeast: | | | | | | |
| Dollars | \$62,580 | \$15,278 | \$97,530 | \$40,641 | \$102,481 | \$48,715 |
| Homes | 104 | 26 | 156 | 72 | 162 | 83 |
| Mid-Atlantic: | | | | | | |
| Dollars | \$118,245 | \$117,399 | \$199,759 | \$180,612 | \$246,307 | \$199,279 |
| Homes | 199 | 212 | 350 | 337 | 393 | 324 |
| Midwest: | | | | | | |
| Dollars | \$68,744 | \$67,308 | \$105,790 | \$116,724 | \$125,181 | \$132,360 |
| Homes | 235 | 220 | 362 | 385 | 466 | 484 |
| Southeast: | | | | | | |
| Dollars | \$64,772 | \$62,741 | \$105,232 | \$113,196 | \$120,140 | \$115,930 |
| Homes | 155 | 154 | 250 | 281 | 270 | 276 |
| Southwest: | | | | | | |
| Dollars | \$192,630 | \$198,487 | \$307,968 | \$339,945 | \$227,325 | \$230,600 |
| Homes | 559 | 587 | 921 | 998 | 648 | 657 |
| West: | | | | | | |
| Dollars | \$120,616 | \$93,213 | \$177,634 | \$162,610 | \$128,422 | \$173,794 |
| Homes | 294 | 205 | 441 | 358 | 315 | 369 |
| Consolidated total: | | | | | | |
| Dollars | \$627,587 | \$554,426 | \$993,913 | \$953,728 | \$949,856 | \$900,678 |
| Homes | 1,546 | 1,404 | 2,480 | 2,431 | 2,254 | 2,193 |
| Unconsolidated joint ventures(2) | | | | | | |
| Dollars | \$131,282 | \$178,973 | \$216,851 | \$316,194 | \$228,730 | \$436,715 |
| Homes | 229 | 302 | 363 | 525 | 382 | 636 |

(1) Net contracts are defined as new contracts executed during the period for the purchase of homes, less cancellations of contracts in the same period.

(2) Represents net contract dollars, net contract homes and contract backlog dollars and homes for our unconsolidated homebuilding joint ventures for the period. We provide this data as a supplement to our consolidated results as an indicator of the volume managed in our unconsolidated joint ventures. See Note 17 to the Condensed Consolidated Financial Statements for a further discussion of our unconsolidated joint ventures.

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In the first half of 2019, our open for sale community count increased to 147 from 123 at October 31, 2018, which is the net result of opening 48 new communities and closing 24 communities since the beginning of fiscal 2019. Our reported level of sales contracts (net of cancellations) increased as a result of our higher community count for the six months ended April 30, 2019 as compared to the same period of the prior year. With respect to our sales absorption, net contracts per average active selling community for the six months ended April 30, 2019 was 18.2 compared to 18.1 for the same period of the prior year. Net contracts per average active selling community was 10.5 for the three months ended April 30, 2019 compared to 10.6 for the three months ended April 30, 2018.

Cancellation rates represent the number of cancelled contracts in the quarter divided by the number of gross sales contracts executed in the quarter. For comparison, the following are historical cancellation rates, excluding unconsolidated joint ventures:

| <u>Quarter</u> | <u>2019</u> | <u>2018</u> | <u>2017</u> | <u>2016</u> | <u>2015</u> |
|----------------|-------------|-------------|-------------|-------------|-------------|
| First | 24% | 18% | 19% | 20% | 16% |
| Second | 19% | 17% | 18% | 19% | 16% |
| Third | | 19% | 19% | 21% | 20% |
| Fourth | | 23% | 22% | 20% | 20% |

Another common and meaningful way to analyze our cancellation trends is to compare the number of contract cancellations as a percentage of beginning backlog. The following table provides this historical comparison, excluding unconsolidated joint ventures:

| <u>Quarter</u> | <u>2019</u> | <u>2018</u> | <u>2017</u> | <u>2016</u> | <u>2015</u> |
|----------------|-------------|-------------|-------------|-------------|-------------|
| First | 16% | 12% | 12% | 13% | 11% |
| Second | 20% | 15% | 16% | 14% | 14% |
| Third | | 14% | 13% | 12% | 13% |
| Fourth | | 13% | 12% | 11% | 12% |

Most cancellations occur within the legal rescission period, which varies by state but is generally less than two weeks after the signing of the contract. Cancellations also occur as a result of a buyer's failure to qualify for a mortgage, which generally occurs during the first few weeks after signing. As shown in the tables above, contract cancellations over the past several years have been within what we believe to be a normal range.

Total cost of sales on our Condensed Consolidated Statements of Operations includes expenses for consolidated housing and land and lot sales, including inventory impairment loss and land option write-offs (defined as "land charges" in the tables below). A breakout of such expenses for housing sales and homebuilding gross margin is set forth below.

Homebuilding gross margin before cost of sales interest expense and land charges is a non-GAAP financial measure. This measure should not be considered as an alternative to homebuilding gross margin determined in accordance with GAAP as an indicator of operating performance.

Management believes this non-GAAP measure provides investors with another way to understand our operating performance. This measure is also useful internally, helping management evaluate our operating results on a consolidated basis and relative to other companies in our industry. In particular, the magnitude and volatility of land charges for the Company, and for other homebuilders, have been significant and, as such, have made financial analysis of our industry more difficult. Homebuilding metrics excluding land charges, as well as interest amortized to cost of sales, and other similar presentations prepared by analysts and other companies are frequently used to assist investors in understanding and comparing the operating characteristics of homebuilding activities by eliminating many of the differences in companies' respective level of impairments and levels of debt.

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| (Dollars in thousands) | Three Months Ended April 30, | | Six Months Ended April 30, | |
|---|---------------------------------|-----------|-------------------------------|-----------|
| | 2019 | 2018 | 2019 | 2018 |
| Sale of homes | \$427,552 | \$468,117 | \$789,687 | \$869,694 |
| Cost of sales, excluding interest expense and land charges | 355,477 | 385,302 | 653,047 | 714,829 |
| Homebuilding gross margin, before cost of sales interest expense and land charges | 72,075 | 82,815 | 136,640 | 154,865 |
| Cost of sales interest expense, excluding land sales interest expense | 13,898 | 15,309 | 24,140 | 27,601 |
| Homebuilding gross margin, after cost of sales interest expense and before land charges | 58,177 | 67,506 | 112,500 | 127,264 |
| Land charges | 1,462 | 2,673 | 2,166 | 3,087 |
| Homebuilding gross margin | \$56,715 | \$64,833 | \$110,334 | \$124,177 |
| Gross margin percentage | 13.3% | 13.8% | 14.0% | 14.3% |
| Gross margin percentage, before cost of sales interest expense and land charges | 16.9% | 17.7% | 17.3% | 17.8% |
| Gross margin percentage, after cost of sales interest expense and before land charges | 13.6% | 14.4% | 14.2% | 14.6% |

Cost of sales expenses as a percentage of consolidated home sales revenues are presented below:

| | Three Months Ended April 30, | | Six Months Ended April 30, | |
|---|---------------------------------|-------|-------------------------------|-------|
| | 2019 | 2018 | 2019 | 2018 |
| Sale of homes | 100% | 100% | 100% | 100% |
| Cost of sales, excluding interest expense and land charges: | | | | |
| Housing, land and development costs | 72.8% | 72.5% | 72.3% | 72.1% |
| Commissions | 3.6% | 3.5% | 3.5% | 3.5% |
| Financing concessions | 1.3% | 1.3% | 1.3% | 1.3% |
| Overheads | 5.4% | 5.0% | 5.5% | 5.3% |
| Total cost of sales, before interest expense and land charges | 83.1% | 82.3% | 82.6% | 82.2% |
| Cost of sales interest | 3.3% | 3.3% | 3.1% | 3.2% |
| Land charges | 0.3% | 0.6% | 0.3% | 0.3% |
| Gross margin percentage | 13.3% | 13.8% | 14.0% | 14.3% |
| Gross margin percentage, before cost of sales interest expense and land charges | 16.9% | 17.7% | 17.3% | 17.8% |
| Gross margin percentage, after cost of sales interest expense and before land charges | 13.6% | 14.4% | 14.2% | 14.6% |

We sell a variety of home types in various communities, each yielding a different gross margin. As a result, depending on the mix of communities delivering homes, consolidated gross margin may fluctuate up or down. Total homebuilding gross margin percentage decreased to 13.3% during the three months ended April 30, 2019 compared to 13.8% for the same period last year and decreased to 14.0% during the six months ended April 30, 2019 compared to 14.3% for the same period last year. The decrease in gross margin percentage for the three and six months ended April 30, 2019 is primarily due to the mix of communities delivering compared to the same periods of the prior year, along with increased incentives, particularly on spec homes, that were sold and delivered in the second quarter of fiscal 2019. For the six months ended April 30, 2019 and 2018, gross margin was favorably impacted by the reversal of prior period inventory impairments of \$18.3 million and \$33.5 million, respectively, which represented 2.3% and 3.9%, respectively, of "Sale of homes" revenue. Gross margin percentage, before cost of sales interest expense and land charges, decreased from 17.7% for the three months ended April 30, 2018 to 16.9% for the three months ended April 30, 2019, and decreased from 17.8% for the six months ended April 30, 2018 to 17.3% for the six months ended April 30, 2019, primarily due to the mix of communities delivering homes in each period, along with increased incentives, particularly on spec homes, that were sold and delivered in the second quarter of fiscal 2019.

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Reflected as inventory impairment loss and land option write-offs in cost of sales, we have written-off or written-down certain inventories totaling \$1.5 million and \$2.7 million during the three months ended April 30, 2019 and 2018, respectively, and \$2.2 million and \$3.1 million during the six months ended April 30, 2019 and 2018, respectively, to their estimated fair value. During the three and six months ended April 30, 2019, we wrote-off residential land options and approval and engineering costs amounting to \$0.5 million and \$1.2 million compared to \$0.6 million and \$1.0 million for the three and six months ended April 30, 2018, which are included in the total land charges discussed above. When a community is redesigned or abandoned, engineering costs are written-off. Option, approval and engineering costs are written-off when a community's pro forma profitability is not projected to produce adequate returns on the investment commensurate with the risk and we believe it is probable we will cancel the option. Such write-offs were located in all of our segments for the first half of fiscal 2019, and in all of our segments except the Southeast for the first half of fiscal 2018. We recorded \$1.0 million and \$2.1 million of inventory impairments during the three months ended April 30, 2019 and April 30, 2018, respectively, and \$1.0 million and \$2.1 million in inventory impairments during the six months ended April 30, 2019 and April 30, 2018, respectively. The impairments recorded in the first half of fiscal 2019 were primarily related to three communities in the Northeast, Mid-Atlantic and Southeast. The impairments recorded in the first half of fiscal 2018 were primarily related to three communities in the Southeast. It is difficult to predict whether impairment levels will remain low. Should we decide to further lower prices or have further land sales, or should the estimates or expectations used in determining estimated cash flows or fair value decrease or differ from current estimates in the future, we may need to recognize additional impairments.

Land Sales and Other Revenues:

Land sales and other revenues consist primarily of land and lot sales. A breakout of land and lot sales is set forth below:

| (In thousands) | Three Months Ended April 30, | | Six Months Ended April 30, | |
|--|---------------------------------|----------|-------------------------------|----------|
| | 2019 | 2018 | 2019 | 2018 |
| Land and lot sales | \$- | \$20,505 | \$7,508 | \$20,505 |
| Cost of sales, excluding interest and land charges | - | 7,710 | 7,357 | 7,710 |
| Land and lot sales gross margin, excluding interest and land charges | - | 12,795 | 151 | 12,795 |
| Land and lot sales interest expense | - | 4,055 | - | 4,055 |
| Land and lot sales gross margin, including interest and land charges | \$- | \$8,740 | \$151 | \$8,740 |

Land sales are ancillary to our residential homebuilding operations and are expected to continue in the future but may significantly fluctuate up or down. Although we budget land sales, they are often dependent upon receiving approvals and entitlements, the timing of which can be uncertain. As a result, projecting the amount and timing of land sales is difficult. Revenue associated with land sales can vary significantly due to the mix of land parcels sold. There were no land sales in the three months ended April 30, 2019 compared to two in the same period of the prior year. There were four land sales in the six months ended April 30, 2019 compared to two in the same period of the prior year. The decrease in revenues for the six month period of fiscal 2019 occurred despite the increase in the number of land sales, demonstrating the impact the mix of land sales can have on land sale revenues.

Land sales and other revenues decreased \$20.5 million and \$16.4 million for the three and six months ended April 30, 2019, respectively, compared to the same period in the prior year. Other revenues include income from contract cancellations, where the deposit has been forfeited due to contract terminations, interest income, cash discounts and miscellaneous one-time receipts. For the three and six months ended April 30, 2019, compared to the three and six months ended April 30, 2018, the decrease was mainly due to the fluctuation in land sales revenues noted above. The decrease for the six months ended April 30, 2019 was also partially due to the \$3.6 million gain recognized from the sale of our former corporate headquarters building in the first quarter of fiscal 2018.

Homebuilding Selling, General and Administrative

Homebuilding selling, general and administrative ("SGA") expenses decreased \$1.4 million and \$1.9 million for the three and six months ended April 30, 2019, respectively, compared to the same periods last year. The decrease for the three and six months ended April 30, 2019 was attributed to an increase of joint venture management fees received, which offset general and administrative expenses and a decrease in insurance costs. SGA expenses as a percentage of homebuilding revenues increased to 10.3% and 10.9% for the three and six months ended April 30, 2019, respectively, compared to 9.3% and 9.9% for the three and six months ended April 30, 2018, respectively, as a result of the 12.5% and 10.8% decline in homebuilding revenue for the same periods, respectively.

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HOMEBUILDING OPERATIONS BY SEGMENT

Segment Analysis

| (Dollars in thousands, except average sales price) | Three Months Ended April 30, | | | |
|--|------------------------------|-----------|------------|------------|
| | 2019 | 2018 | Variance | Variance % |
| Northeast | | | | |
| Homebuilding revenue | \$13,059 | \$43,771 | \$(30,712) | (70.2)% |
| Income before income taxes | \$125 | \$5,960 | \$(5,835) | (97.9)% |
| Homes delivered | 23 | 47 | (24) | (51.1)% |
| Average sales price | \$566,957 | \$500,265 | \$66,692 | 13.3% |
| Mid-Atlantic | | | | |
| Homebuilding revenue | \$80,847 | \$104,160 | \$(23,313) | (22.4)% |
| Income before income taxes | \$393 | \$6,700 | \$(6,307) | (94.1)% |
| Homes delivered | 142 | 206 | (64) | (31.1)% |
| Average sales price | \$569,141 | \$505,139 | \$64,002 | 12.7% |
| Midwest | | | | |
| Homebuilding revenue | \$42,937 | \$42,938 | \$(1) | 0.0% |
| Loss before income taxes | \$(594) | \$(1,110) | \$516 | 46.5% |
| Homes delivered | 141 | 143 | (2) | (1.4)% |
| Average sales price | \$304,035 | \$299,415 | \$4,620 | 1.5% |
| Southeast | | | | |
| Homebuilding revenue | \$49,382 | \$60,901 | \$(11,519) | (18.9)% |
| Loss before income taxes | \$(4,132) | \$(5,286) | \$1,154 | 21.8% |
| Homes delivered | 123 | 158 | (35) | (22.2)% |
| Average sales price | \$401,187 | \$385,908 | \$15,279 | 4.0% |
| Southwest | | | | |
| Homebuilding revenue | \$143,850 | \$159,147 | \$(15,297) | (9.6)% |
| Income before income taxes | \$4,286 | \$10,047 | \$(5,761) | (57.3)% |
| Homes delivered | 431 | 466 | (35) | (7.5)% |
| Average sales price | \$333,258 | \$341,112 | \$(7,854) | (2.3)% |
| West | | | | |
| Homebuilding revenue | \$97,883 | \$78,098 | \$19,785 | 25.3% |
| Income before income taxes | \$10,310 | \$7,172 | \$3,138 | 43.8% |
| Homes delivered | 225 | 195 | 30 | 15.4% |
| Average sales price | \$434,862 | \$398,962 | \$35,900 | 9.0% |

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| (Dollars in thousands, except average sales price) | Six Months Ended April 30, | | | |
|--|----------------------------|-----------|------------|------------|
| | 2019 | 2018 | Variance | Variance % |
| Northeast | | | | |
| Homebuilding revenue | \$33,000 | \$63,970 | \$(30,970) | (48.4)% |
| Income (loss) before income taxes | \$6,004 | \$(3,741) | \$9,745 | 260.5% |
| Homes delivered | 45 | 87 | (42) | (48.3)% |
| Average sales price | \$567,667 | \$502,354 | \$65,313 | 13.0% |
| Mid-Atlantic | | | | |
| Homebuilding revenue | \$134,277 | \$175,457 | \$(41,180) | (23.5)% |
| Income before income taxes | \$386 | \$8,652 | \$(8,266) | (95.5)% |
| Homes delivered | 253 | 341 | (88) | (25.8)% |
| Average sales price | \$529,632 | \$513,393 | \$16,239 | 3.2% |
| Midwest | | | | |
| Homebuilding revenue | \$87,858 | \$83,517 | \$4,341 | 5.2% |
| Loss before income taxes | \$(1,443) | \$(3,454) | \$2,011 | 58.2% |
| Homes delivered | 290 | 283 | 7 | 2.5% |
| Average sales price | \$302,617 | \$294,463 | \$8,154 | 2.8% |
| Southeast | | | | |
| Homebuilding revenue | \$93,373 | \$117,569 | \$(24,196) | (20.6)% |
| Loss before income taxes | \$(7,061) | \$(6,947) | \$(114) | (1.6)% |
| Homes delivered | 231 | 290 | (59) | (20.3)% |
| Average sales price | \$403,589 | \$405,682 | \$(2,093) | (0.5)% |
| Southwest | | | | |
| Homebuilding revenue | \$262,049 | \$287,452 | \$(25,403) | (8.8)% |
| Income before income taxes | \$6,672 | \$15,558 | \$(8,886) | (57.1)% |
| Homes delivered | 796 | 850 | (54) | (6.4)% |
| Average sales price | \$328,514 | \$337,838 | \$(9,324) | (2.8)% |
| West | | | | |
| Homebuilding revenue | \$187,784 | \$163,148 | \$24,636 | 15.1% |
| Income before income taxes | \$22,015 | \$15,239 | \$6,776 | 44.5% |
| Homes delivered | 437 | 389 | 48 | 12.3% |
| Average sales price | \$429,428 | \$418,454 | \$10,974 | 2.6% |

Homebuilding Results by Segment

Northeast - Homebuilding revenues decreased 70.2% for the three months ended April 30, 2019 compared to the same period of the prior year. The decrease for the three months ended April 30, 2019 was attributed to a 51.1% decrease in homes delivered and a \$20.2 million decrease in land sales and other revenue, partially offset by a 13.3% increase in average sales price. The increase in average sales price was the result of new communities delivering higher priced, larger single family homes in higher-end submarkets of the segment in the three months ended April 30, 2019 compared to some communities delivering in the three months ended April 30, 2018 that are no longer delivering that had lower priced, single family homes in lower-end submarkets of the segment.

Income before income taxes decreased \$5.8 million compared to the prior year to \$0.1 million for the three months ended April 30, 2019. The decrease was mainly due to the decrease in homebuilding revenues discussed above, while gross margin percentage before interest expense for the period was relatively flat compared to the same period of the prior year.

Homebuilding revenues decreased 48.4% for the six months ended April 30, 2019 compared to the same period of the prior year. The decrease was attributed to a 48.3% decrease in homes delivered and a \$12.8 million decrease in land sales and other revenue, partially offset by a 13.0% increase in average sales price. The increase in average sales price was the result of new communities delivering higher priced, larger single family homes in higher-end submarkets of the segment in the six months ended April 30, 2019 compared to some communities delivering in the six months ended April 30, 2018 that are no longer delivering that had lower priced, single family homes and townhomes in lower-end submarkets of the segment.

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Loss before income taxes improved \$9.7 million compared to the prior year to income of \$6.0 million for the six months ended April 30, 2019. The improvement in the loss was mainly due to a \$4.6 million decrease in selling, general and administrative costs, \$12.9 million increase in income from unconsolidated joint ventures, and an increase in gross margin percentage before interest expense.

Mid-Atlantic - Homebuilding revenues decreased 22.4% for the three months ended April 30, 2019 compared to the same period in the prior year. The decrease was primarily due to a 31.1% decrease in homes delivered, partially offset by a 12.7% increase in average sales price for the three months ended April 30, 2019 compared to the same period in the prior year. The increase in average sales price was the result of new communities delivering higher priced, larger single family homes and townhomes in higher-end submarkets of the segment in the three months ended April 30, 2019 compared to some communities delivering in the three months ended April 30, 2018 that are no longer delivering that had lower priced, single family homes and townhomes in mid to higher-end submarkets of the segment. Also impacting the increase in average sales prices was higher option revenue in certain communities.

Income before income taxes decreased \$6.3 million compared to the prior year to \$0.4 million for the three months ended April 30, 2019, which was primarily due to the decrease in homebuilding revenues discussed above and a decrease in gross margin percentage before interest expense.

Homebuilding revenues decreased 23.5% for the six months ended April 30, 2019 compared to the same period in the prior year. The decrease was primarily due to a 25.8% decrease in homes delivered, partially offset by a 3.2% increase in average sales price for the six months ended April 30, 2019. The increase in average sales price was the result of new communities delivering higher priced, larger single family homes and townhomes in higher-end submarkets of the segment in the six months ended April 30, 2019 compared to some communities delivering in the six months ended April 30, 2018 that are no longer delivering that had lower priced, single family homes and townhomes in mid to higher-end submarkets of the segment. Also impacting the increase in average sales prices was higher option revenue in certain communities.

Income before income taxes decreased \$8.3 million compared to the prior year to \$0.4 million for the six months ended April 30, 2019, which was primarily due to the decrease in homebuilding revenues discussed above and a decrease in gross margin percentage before interest expense.

Midwest - Homebuilding revenues were flat for the three months ended April 30, 2019 compared to the same period in the prior year. This was primarily due to a 1.4% decrease in homes delivered, offset by a 1.5% increase in average sales price for the three months ended April 30, 2019. The increase in average sales price was the result of new communities delivering higher priced, larger single family homes and townhomes in mid to higher-end submarkets of the segment in the three months ended April 30, 2019 compared to some communities that are no longer delivering that had lower priced, smaller single family homes in lower-end submarkets of the segment in the three months ended April 30, 2018.

Loss before income taxes improved \$0.5 million to a loss of \$0.6 million for the three months ended April 30, 2019 compared to the same period in the prior year. The improvement in the loss for the three months ended April 30, 2019 was primarily due to a \$0.9 million improvement in loss from unconsolidated joint ventures, while gross margin percentage before interest expense was flat for the period.

Homebuilding revenues increased 5.2% for the six months ended April 30, 2019 compared to the same period in the prior year. The increase was primarily due to a 2.5% increase in homes delivered and a 2.8% increase in average sales price for the six months ended April 30, 2019. The increase in average sales price was the result of new communities delivering higher priced, larger single family homes and townhomes in mid to higher-end submarkets of the segment in the six months ended April 30, 2019 compared to some communities that are no longer delivering that had lower priced, smaller single family homes in lower-end submarkets of the segment in the six months ended April 30, 2018.

Loss before income taxes improved \$2.0 million compared to the prior year to a loss of \$1.4 million for the six months ended April 30, 2019, primarily due to the increase in homebuilding revenue discussed above, \$1.2 million improvement in loss from unconsolidated joint ventures, while gross margin percentage before interest expense was flat for the period.

Southeast - Homebuilding revenues decreased 18.9% for the three months ended April 30, 2019 compared to the same period in the prior year. The decrease for the three months ended April 30, 2019 was attributed a 22.2% decrease in homes delivered, partially offset by a 4.0% increase in average sales price. The increase in average sales price was the result of new communities delivering higher priced, single family homes in higher-end submarkets of the segment in the three months ended April 30, 2019 compared to some communities that are no longer delivering that had lower priced, smaller single family homes and townhomes in lower-end submarkets of the segment in the three months ended April 30, 2018.

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Loss before income taxes improved \$1.2 million to a loss of \$4.1 million for the three months ended April 30, 2019, which was primarily due to a \$0.8 million decrease in inventory impairment loss and land option write-offs, a \$0.5 million decrease in selling, general and administrative costs, and a \$1.8 million improvement in loss from unconsolidated joint ventures to income, while gross margin percentage before interest expense was flat compared to the same period of the prior year.

Homebuilding revenues decreased 20.6% for the six months ended April 30, 2019 compared to the same period in the prior year. The decrease for the six months ended April 30, 2019 was attributed a 20.3% decrease in homes delivered, while average sales price was relatively flat with a 0.5% decrease.

Loss before income taxes increased \$0.1 million to a loss of \$7.0 million for the six months ended April 30, 2019, primarily due to a \$0.7 million increase in selling, general and administrative costs, partially offset by a \$1.2 million improvement in loss from unconsolidated joint ventures, a \$0.7 million decrease in inventory impairment loss and land option write-offs, and a slight increase in gross margin percentage before interest expense.

Southwest - Homebuilding revenues decreased 9.6% for the three months ended April 30, 2019 compared to the same period in the prior year. The decrease in homebuilding revenues was primarily due to a 7.5% decrease in homes delivered and a 2.3% decrease in average sales price for the three months ended April 30, 2019. The decrease in average sales price was the result of new communities delivering lower priced, smaller single family homes in lower-end submarkets of the segment in the three months ended April 30, 2019 compared to some communities that are no longer delivering that had higher priced, larger single family homes in higher-end submarkets of the segment in the three months ended April 30, 2018.

Income before income taxes decreased \$5.8 million to \$4.3 million for the three months ended April 30, 2019. The decrease was primarily due to the decrease in homebuilding revenue discussed above and a decrease in gross margin percentage before interest expense. Partially offsetting the decrease in income before income taxes is a \$0.6 million decrease in selling, general and administrative costs and a \$1.1 million increase in income from unconsolidated joint ventures.

Homebuilding revenues decreased 8.8% for the six months ended April 30, 2019 compared to the same period in the prior year. The decrease was primarily due to a 6.4% decrease in homes delivered and a 2.8% decrease in average sales price for the six months ended April 30, 2019. The decrease in average sales price was the result of new communities delivering lower priced, smaller single family homes in lower-end submarkets of the segment in the six months ended April 30, 2019 compared to some communities that are no longer delivering that had higher priced, larger single family homes in higher-end submarkets of the segment in the six months ended April 30, 2018.

Income before income taxes decreased \$8.9 million compared to the prior year to \$6.7 million for the six months ended April 30, 2019. The decrease was due to the decrease in homebuilding revenues discussed above and a decrease in gross margin percentage before interest expense. Partially offsetting the decrease in income before income taxes is a \$1.1 million decrease in selling, general and administrative costs and a \$2.9 million increase in income from unconsolidated joint ventures.

West - Homebuilding revenues increased 25.3% for the three months ended April 30, 2019 compared to the same period in the prior year. The increase for the three months ended April 30, 2019 was primarily attributed to a 15.4% increase in homes delivered and a 9.0% increase in average sales price. The increase in average sales price was the result of new communities delivering higher priced, single family homes in mid to higher-end submarkets of the segment in the three months ended April 30, 2019 compared to some communities that are no longer delivering that had lower priced, single family homes in lower-end submarkets of the segment in the three months ended April 30, 2018.

Income before income taxes increased \$3.1 million to \$10.3 million for the three months ended April 30, 2019. The increase was primarily due to the increase in homebuilding revenues discussed above, while gross margin percentage before interest expense was flat for the three months ended April 30, 2019 compared to the same period in the prior year.

Homebuilding revenues increased 15.1% for the six months ended April 30, 2019 compared to the same period in the prior year. The increase for the six months ended April 30, 2019 was primarily attributed to a 12.3% increase in homes delivered and a 2.6% increase in average sales price. The increase in average sales price was the result of new communities delivering higher priced, single family homes in mid to higher-end submarkets of the segment in the six months ended April 30, 2019 compared to some communities that are no longer delivering that had lower priced, single family homes in lower-end submarkets of the segment in the six months ended April 30, 2018.

Income before income taxes increased \$6.8 million to \$22.0 million for the six months ended April 30, 2019. The increase was due to the increase in homebuilding revenues discussed above and an increase in gross margin percentage before interest expense for the six months ended April 30, 2019 compared to the same period in the prior year.

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Financial Services

Financial services consist primarily of originating mortgages from our home buyers, selling such mortgages in the secondary market, and title insurance activities. We use mandatory investor commitments and forward sales of mortgage-backed securities (“MBS”) to hedge our mortgage-related interest rate exposure on agency and government loans. These instruments involve, to varying degrees, elements of credit and interest rate risk. Credit risk associated with MBS forward commitments and loan sales transactions is managed by limiting our counterparties to investment banks, federally regulated bank affiliates and other investors meeting our credit standards. Our risk, in the event of default by the purchaser, is the difference between the contract price and fair value of the MBS forward commitments. For the first half of fiscal 2019 and 2018, Federal Housing Administration and Veterans Administration (“FHA/VA”) loans represented 30.0% and 25.3%, respectively, of our total loans. The origination of FHA/VA loans have increased from the first half of fiscal 2018 to the first half of fiscal 2019 and our conforming conventional loan originations as a percentage of our total loans decreased from 69.9% to 65.4% for these periods, respectively. The origination of loans which exceed conforming conventions have decreased from 4.7% for the first half of fiscal 2018 to 4.6% for the first half of fiscal 2019. Profits and losses relating to the sale of mortgage loans are recognized when legal control passes to the buyer of the mortgage and the sales price is collected.

During the three and six months ended April 30, 2019, financial services provided a \$3.6 million and \$4.8 million, respectively, of pretax profit compared to \$4.3 million and \$6.8 million of pretax profit, respectively, for the same periods of fiscal 2018. This decrease in pretax profit is attributed to the decrease in homebuilding deliveries. Further impacting the decrease in pretax profit for the six months ended April 30, 2019 compared to 2018 is the decrease in the basis point spread between the loans originated and the implied rate from the sale of the loans as a result of the competitive financial services market. In the market areas served by our wholly owned mortgage banking subsidiaries, 68.3% and 72.7% of our noncash homebuyers obtained mortgages originated by these subsidiaries during the three months ended April 30, 2019 and 2018, respectively, and 69.4% and 70.9% of our noncash homebuyers obtained mortgages originated by these subsidiaries for the six months ended April 30, 2019 and 2018, respectively. Servicing rights on new mortgages originated by us are sold with the loans.

Corporate General and Administrative

Corporate general and administrative expenses include the operations at our headquarters in New Jersey. These expenses include payroll, stock compensation, facility costs and rent and other costs associated with our executive offices, information services, human resources, corporate accounting, training, treasury, process redesign, internal audit, construction services and administration of insurance, quality and safety. Corporate general and administrative expenses increased slightly to \$16.2 million for the three months ended April 30, 2019 compared to \$16.1 million for the three months ended April 30, 2018, and decreased to \$33.8 million for the six months ended April 30, 2019 compared to \$35.3 million for the six months ended April 30, 2018. The slight increase for the three months ended April 30, 2019 compared to 2018 is primarily due to the additional costs incurred pertaining to the Reverse Stock Split in the second quarter of 2019, partially offset by an adjustment to reserves for self-insured medical claims, which were reduced based on claim estimates. The decrease for the six months ended April 30, 2019 compared to 2018 is primarily due to the adjustment to reserves for self-insured medical claims mentioned above, along with decreased legal fees (including litigation) related to financing transactions and higher costs for ongoing litigations involving the company in the first half of the prior year which did not recur in the first half of the current year.

Other Interest

Other interest decreased \$3.4 million for the three months ended April 30, 2019 compared to the three months ended April 30, 2018 and decreased \$10.3 million for the six months ended April 30, 2019 compared to the six months ended April 30, 2018. Our assets that qualify for interest capitalization (inventory under development) are less than our debt, and therefore the portion of interest not covered by qualifying assets is directly expensed. Other interest decreased for the three and six months ended April 30, 2019 compared to the three and six months ended April 30, 2018 primarily because our assets that qualify for interest capitalization increased by more than our debt, therefore the amount of directly expensed interest decreased for the three and six months ended April 30, 2019 compared to the same periods in the prior year.

Loss on Extinguishment of Debt

On February 1, 2018, K. Hovnanian closed certain of the previously announced financing transactions as follows: (i) K. Hovnanian borrowed the Initial Term Loans in the amount of \$132.5 million under the Term Loan Facility, and proceeds of such Initial Term Loans, together with cash on hand, were used to redeem all of K. Hovnanian’s outstanding \$132.5 million aggregate principal amount of 7.0% Notes (upon redemption, all 7.0% Notes were cancelled); and (ii) K. Hovnanian accepted all of the \$170.2 million aggregate principal amount of 8.0% Notes validly tendered and not validly withdrawn in the Exchange Offer (representing 72.14% of the aggregate principal amount of 8.0% Notes outstanding prior to the exchange offer), and in connection therewith, K. Hovnanian issued \$90.6 million aggregate principal amount of New 2026 Notes and \$90.1 million aggregate principal amount of New 2040 Notes, under a new indenture and as part of the Exchange Offer, the Subsidiary Purchaser, purchased for \$26.5 million in cash the Purchased 8.0% Notes. See Note 11 to the Condensed Consolidated Financial Statements. These transactions resulted in a loss on extinguishment of debt of \$1.4 million for the three and six months ended April 30, 2018, which is included in “Loss on extinguishment of debt” on the Condensed Consolidated Statements of Operations.

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Income (loss) from Unconsolidated Joint Ventures

Income (loss) from unconsolidated joint ventures consists of our share of the earnings or losses of our joint ventures. Income from unconsolidated joint ventures increased \$5.9 million to \$7.3 million for the three months ended April 30, 2019 compared to the same period of the prior year. Loss from unconsolidated joint ventures improved by \$20.6 million to income of \$16.8 million for the six months ended April 30, 2019 compared to the same period of the prior year. The improvement for both the three and six months is due to our share of income from certain of our joint ventures delivering more homes and increased profits in the current fiscal year as compared to the prior fiscal year when they reported losses primarily due to startup costs or having just begun delivering homes.

Total Taxes

The total income tax expense of \$0.3 million and \$0.7 million recognized for the three and six months ended April 30, 2019, respectively, and \$0.3 million and \$0.6 million recognized for the three and six months ended April 30, 2018, respectively, was primarily related to state tax expense from income generated that was not offset by tax benefits in states where we fully reserve the tax benefit from net operating losses.

Inflation

Inflation has a long-term effect, because increasing costs of land, materials and labor result in increasing sale prices of our homes. In general, these price increases have been commensurate with the general rate of inflation in our housing markets and have not had a significant adverse effect on the sale of our homes. A significant risk faced by the housing industry generally is that rising house construction costs, including land and interest costs, will substantially outpace increases in the income of potential purchasers and therefore limit our ability to raise home sale prices, which may result in lower gross margins.

Inflation has a lesser short-term effect, because we generally negotiate fixed price contracts with many, but not all, of our subcontractors and material suppliers for the construction of our homes. These prices usually are applicable for a specified number of residential buildings or for a time period of between three to twelve months. Construction costs for residential buildings represent approximately 54% of our homebuilding cost of sales for the six months ended April 30, 2019.

Safe Harbor Statement

All statements in this Quarterly report on Form 10-Q that are not historical facts should be considered as “Forward-Looking Statements” within the meaning of the “Safe Harbor” provisions of the Private Securities Litigation Reform Act of 1995. Such statements involve known and unknown risks, uncertainties and other factors that may cause actual results, performance or achievements of the Company to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements. Such forward-looking statements include but are not limited to statements related to the Company's goals and expectations with respect to its financial results for future financial periods. Although we believe that our plans, intentions and expectations reflected in, or suggested by, such forward-looking statements are reasonable, we can give no assurance that such plans, intentions or expectations will be achieved. By their nature, forward-looking statements: (i) speak only as of the date they are made, (ii) are not guarantees of future performance or results and (iii) are subject to risks, uncertainties and assumptions that are difficult to predict or quantify. Therefore, actual results could differ materially and adversely from those forward-looking statements as result of a variety of factors. Such risks, uncertainties and other factors include, but are not limited to:

- Changes in general and local economic, industry and business conditions and impacts of a significant homebuilding downturn;
- Adverse weather and other environmental conditions and natural disasters;
- High leverage and restrictions on the Company's operations and activities imposed by the agreements governing the Company's outstanding indebtedness;
- Availability and terms of financing to the Company;
- The Company's sources of liquidity;
- Changes in credit ratings;
- The seasonality of the Company's business;
- The availability and cost of suitable land and improved lots and sufficient liquidity to invest in such land and lots;
- Shortages in, and price fluctuations of, raw materials and labor;
- Reliance on, and the performance of, subcontractors;
- Regional and local economic factors, including dependency on certain sectors of the economy, and employment levels affecting home prices and sales activity in the markets where the Company builds homes;

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- Fluctuations in interest rates and the availability of mortgage financing;
- Increases in cancellations of agreements of sale;
- Changes in tax laws affecting the after-tax costs of owning a home;
- Operations through unconsolidated joint ventures with third parties;
- Government regulation, including regulations concerning development of land, the home building, sales and customer financing processes, tax laws and the environment;
- Legal claims brought against us and not resolved in our favor, such as product liability litigation, warranty claims and claims made by mortgage investors;
- Levels of competition;
- Successful identification and integration of acquisitions;
- Significant influence of the Company's controlling stockholders;
- Availability of net operating loss carryforwards;
- Utility shortages and outages or rate fluctuations;
- Changes in trade policies, including the imposition of tariffs and duties on homebuilding materials and products, and related trade disputes with and retaliatory measures taken by other countries.
- Geopolitical risks, terrorist acts and other acts of war;
- Loss of key management personnel or failure to attract qualified personnel;
- Information technology failures and data security breaches; and
- Negative publicity.

Certain risks, uncertainties and other factors are described in detail in Part I, Item 1 "Business" and Part I, Item 1A "Risk Factors" in our Annual Report on Form 10-K for the fiscal year ended October 31, 2018. Except as otherwise required by applicable securities laws, we undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events, changed circumstances or any other reason after the date of this Quarterly Report on Form 10-Q.

Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

A primary market risk facing us is interest rate risk on our long term debt, including debt instruments at variable interest rates. In connection with our mortgage operations, mortgage loans held for sale and the associated mortgage warehouse lines of credit under our Master Repurchase Agreements are subject to interest rate risk; however, such obligations reprice frequently and are short-term in duration. In addition, we hedge the interest rate risk on mortgage loans by obtaining forward commitments from private investors. Accordingly, the interest rate risk from mortgage loans is not material. We do not use financial instruments to hedge interest rate risk except with respect to mortgage loans. We are also subject to foreign currency risk but we do not believe this risk is material. The following table sets forth as of April 30, 2019, our long-term debt obligations, principal cash flows by scheduled maturity, weighted-average interest rates and estimated fair value ("FV").

| (Dollars in thousands) | Long Term Debt as of April 30, 2019 by Fiscal Year of Expected Maturity Date | | | | | | | FV at 4/30/19 |
|--------------------------------|--|------|----------|-----------|------|------------|-------------|------------------|
| | 2019 | 2020 | 2021 | 2022 | 2023 | Thereafter | Total | |
| Long term debt(1)(2): | | | | | | | | |
| Fixed rate | \$- | \$- | \$75,000 | \$635,000 | \$- | \$808,257 | \$1,518,257 | \$1,213,334 |
| Weighted average interest rate | -% | -% | 9.50% | 8.21% | -% | 8.84% | 8.61% | |

- (1) Does not include the mortgage warehouse lines of credit made under our Master Repurchase Agreements. Also, does not include our \$125.0 million Secured Credit Facility under which there were no borrowings outstanding as of April 30, 2019. Availability under the Secured Credit Facility will terminate on December 28, 2019 and any loans thereunder on such date will convert to secured term loans maturing on December 28, 2022.
- (2) Does not include \$190.7 million of nonrecourse mortgages secured by inventory. These mortgages have various maturities spread over the next two to three years and are paid off as homes are delivered.

Item 4. CONTROLS AND PROCEDURES

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Company's reports under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to the Company's management, including its chief executive officer and chief financial officer, as appropriate, to allow timely decisions regarding required disclosures. Any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives. The Company's management, with the participation of the Company's chief executive officer and chief financial officer, has evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures as of April 30, 2019. Based upon that evaluation and subject to the foregoing, the Company's chief executive officer and chief financial officer concluded that the design and operation of the Company's disclosure controls and procedures are effective to accomplish their objectives.

There was no change in the Company's internal control over financial reporting that occurred during the quarter ended April 30, 2019 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

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PART II. OTHER INFORMATION

Item 1. LEGAL PROCEEDINGS

Information with respect to legal proceedings is incorporated into this Part II, Item 1 from Note 7 to the Condensed Consolidated Financial Statements in Part I, Item 1 of this Quarterly Report on Form 10-Q.

Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.

Recent Sales of Unregistered Equity Securities

None.

Issuer Purchases of Equity Securities

No shares of our Class A Common Stock or Class B Common Stock were purchased by or on behalf of the Company or any affiliated purchaser during the fiscal second quarter of 2019. The maximum number of shares that may be purchased under the Company's repurchase program is 22 thousand.

Dividends

Certain debt agreements to which we are a party contain restrictions on the payment of cash dividends. As a result of the most restrictive of these provisions, we are not currently able to pay any cash dividends. We have never paid a cash dividend to our common stockholders.

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Item 6. EXHIBITS

- 3(a) [Restated Certificate of Incorporation of the Registrant.\(2\)](#)
 - 3(b) [Amended and Restated Bylaws of the Registrant.\(3\)](#)
 - 4(a) [Specimen Class A Common Stock Certificate.\(2\)](#)
 - 4(b) [Specimen Class B Common Stock Certificate.\(2\)](#)
 - 4(c) [Certificate of Designations, Powers, Preferences and Rights of the 7.625% Series A Preferred Stock of Hovnanian Enterprises, Inc., dated January 12, 2005.\(4\)](#)
 - 4(d) [Certificate of Designations of the Series B Junior Preferred Stock of Hovnanian Enterprises, Inc., dated August 14, 2008.\(1\)](#)
 - 4(e) [Rights Agreement, dated as of August 14, 2008, between Hovnanian Enterprises, Inc. and National City Bank, as Rights Agent, which includes the Form of Certificate of Designation as Exhibit A, Form of Right Certificate as Exhibit B and the Summary of Rights as Exhibit C.\(5\)](#)
 - 4(f) [Amendment No. 1 to Rights Agreement, dated as of January 11, 2018, between Hovnanian Enterprises, Inc. and Computershare Trust Company, N.A. \(as successor to National City Bank\), as Rights Agent, which includes the amended and restated Form of Rights Certificate as Exhibit 1 and the amended and restated Summary of Rights as Exhibit 2. \(6\)](#)
 - 10(a) [Form of 2019 Long-Term Incentive Program Award Agreement*](#)
 - 31(a) [Rule 13a-14\(a\)/15d-14\(a\) Certification of Chief Executive Officer.](#)
 - 31(b) [Rule 13a-14\(a\)/15d-14\(a\) Certification of Chief Financial Officer.](#)
 - 32(a) [Section 1350 Certification of Chief Executive Officer.](#)
 - 32(b) [Section 1350 Certification of Chief Financial Officer.](#)
 - 101 The following financial information from our Quarterly Report on Form 10-Q for the quarter ended April 30, 2019, formatted in Extensible Business Reporting Language (XBRL): (i) the Condensed Consolidated Balance Sheets at April 30, 2019 and October 31, 2018, (ii) the Condensed Consolidated Statements of Operations for the three and six months ended April 30, 2019 and 2018, (iii) the Condensed Consolidated Statements of Changes in Equity for the six months ended April 30, 2019 and 2018, (iv) the Condensed Consolidated Statements of Cash Flows for the six months ended April 30, 2019 and 2018, and (v) the Notes to Condensed Consolidated Financial Statements.
- * Management compensatory plan or agreement
- (1) Incorporated by reference to Exhibits to Quarterly Report on Form 10-Q of the Registrant for the quarter ended July 31, 2008.
 - (2) Incorporated by reference to Exhibits to Current Report on Form 8-K of the Registrant filed March 29, 2019.
 - (3) Incorporated by reference to Exhibits to Current Report on Form 8-K of the Registrant filed December 3, 2018.
 - (4) Incorporated by reference to Exhibits to Current Report on Form 8-K of the Registrant filed on July 13, 2005.
 - (5) Incorporated by reference to Exhibits to the Registration Statement on Form 8-A of the Registrant filed August 14, 2008.
 - (6) Incorporated by reference to Exhibits to Current Report on Form 8-K of the Registrant filed January 11, 2018.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

HOVNANIAN ENTERPRISES, INC.
(Registrant)

DATE: June 6, 2019

/S/J. LARRY SORSBY

J. Larry Sorsby

Executive Vice President and Chief Financial Officer

DATE: June 6, 2019

/S/BRAD G. O'CONNOR

Brad G. O'Connor

Vice President/Chief Accounting Officer/Corporate Controller

Exhibit 10(a)**2019 LONG-TERM INCENTIVE PROGRAM AWARD AGREEMENT**

| | | | |
|--|----------------|---|-------|
| <i>Participant:</i> | _____ | <i>Cash Percentage of Award:</i> | 50% |
| <i>Date of Grant:</i> | March 18, 2019 | <i>Phantom Share Percentage of Award:</i> | 50% |
| <i>Maximum LTIP Award (total)¹:</i> | _____ | <i>Target LTIP Award (total)¹:</i> | _____ |
| <i>Maximum Cash Amount:</i> | _____ | <i>Target Cash Amount:</i> | _____ |
| <i>Maximum Number of Phantom Shares:</i> | _____ | <i>Target Number of Phantom Shares:</i> | _____ |

1. Grant of LTIP Award. For valuable consideration, receipt of which is hereby acknowledged, Hovnanian Enterprises, Inc., a Delaware Corporation (the "Company"), hereby grants the Long-Term Incentive Program award opportunity (the "Award") listed above to the Participant, on the terms and conditions hereinafter set forth. The Award granted hereunder is made as a standalone award, separate and apart from, and outside of, the 2012 Company Amended and Restated Stock Incentive Plan (the "Plan"), and shall not constitute an Award granted under or pursuant to that Plan. Notwithstanding the foregoing, the terms, conditions and definitions set forth in the Plan and the 2019 Long-Term Incentive Program adopted in connection with the Plan (the "LTIP"), which Plan and LTIP, as amended from time to time, shall apply to the Award as though the Award had been granted under the Plan (including but not limited to the adjustment provision contained in the Plan), and the Award shall be subject to such terms, conditions and definitions which are hereby incorporated herein by reference and made a part hereof. Notwithstanding the foregoing, the Award shall not be counted for purposes of calculating the aggregate number of shares that may be issued or transferred pursuant to awards under the Plan or for purposes of calculating the award limitations under the Plan (including pursuant to Section 3 of the Plan). The Award represents an unfunded, unsecured right of the Participant to receive cash payments, a portion of which shall represent the value of a number of Shares of the Company's Class A Common Stock on the New York Stock Exchange ("Phantom Shares"), on the date(s) specified under the LTIP, subject to the performance and time vesting conditions set forth thereunder. Capitalized terms not otherwise defined herein shall have the same meanings as in the Plan or the LTIP, as applicable. A copy of the LTIP is attached hereto as Exhibit A.

2. Amount of Award; Vesting and Timing of Payments. The target amount of the Award listed above represents the amount of cash and payment of cash in respect of Phantom Shares that the Participant will be eligible to receive if the performance levels achieved during the Performance Period correspond to a payout level of 100% of target under the terms of the LTIP, assuming the time vesting requirements set forth under the LTIP are also met. The actual amount of cash, including cash in respect of Phantom Shares, payable in respect of the Award may be more or less than the targeted amounts, and the amounts (if any) that become payable under the Award will be paid to the Participant at such times and subject to such performance and time vesting conditions as set forth under the LTIP.

3. Adjustments Upon Certain Events. Subject to the terms of the Plan and the LTIP, in the event of any change in the outstanding Shares by reason of any Share dividend or split, reorganization, recapitalization, merger, consolidation, amalgamation, spin-off or combination transaction or exchange of Shares or other similar events (collectively, an "Adjustment Event"), the Committee shall, in its sole discretion, make an appropriate and equitable adjustment in the number of Phantom Shares subject to this Agreement to reflect such Adjustment Event. Any such adjustment made by the Committee shall be final and binding upon the Participant, the Company and all other interested persons.

4. No Right to Continued Employment. Neither the Plan, the LTIP nor this Agreement shall be construed as giving the Participant the right to be retained in the employ of, or in any consulting relationship to, the Company or any Affiliate. Further, the Company or an Affiliate may at any time dismiss the Participant, free from any liability or any claim under the Plan, the LTIP or this Agreement, except as otherwise expressly provided herein.

5. No Acquired Rights. The Participant acknowledges and accepts that the Board and the Committee have the power to amend or terminate the Plan and the LTIP, to the extent permitted thereunder, at any time and that the granting of this Award to the Participant is entirely at the discretion of the Committee and does not obligate the Company or any of its Affiliates to offer such participation in the future (whether on the same or different terms). The Participant further acknowledges and accepts that this Award is not to be considered part of any normal or expected compensation and that the termination of the Participant's employment under any circumstances whatsoever will give the Participant no claim or right of action against the Company or its Affiliates in respect of any loss of rights under this Agreement, the Plan or the LTIP that may arise as a result of such termination of employment.

6. No Rights of a Shareholder. The Participant shall have no voting, dividend or other rights or privileges as a shareholder of the Company.

7. Transferability. This Award may not be assigned, alienated, pledged, attached, sold or otherwise transferred or encumbered by the Participant otherwise than by will or by the laws of descent and distribution, and any purported assignment, alienation, pledge, attachment, sale, transfer or encumbrance not permitted by this Section 7 shall be void and unenforceable against the Company or any Affiliate.

8. Withholding. The Participant may be required to pay to the Company or any Affiliate and the Company or any Affiliate shall have the right and is hereby authorized to withhold from any transfer of cash due under this Agreement, or from any compensation or other amount owing to the Participant, applicable withholding taxes with respect to any transfer under this Agreement, and to take such action as may be necessary in the opinion of the Company to satisfy all obligations for the payment of such taxes. Notwithstanding the foregoing, if the Participant's employment with the Company terminates prior to the payment or transfer of all of the cash under this Agreement, the payment of any applicable withholding taxes with respect to any further payments of cash under this Award shall be made solely through withholding of cash otherwise payable under this Agreement in amounts equal to the statutory minimum withholding liability.

9. Non-Solicitation Covenants.

(a) The Participant acknowledges and agrees that, during the Participant's employment with the Company and its Affiliates and upon the Participant's termination of employment with the Company and its Affiliates for any reason, for a period commencing on the termination of such employment and ending on the second anniversary of such termination, the Participant shall not, whether on Participant's own behalf or on behalf of or in conjunction with any person, company, business entity or other organization whatsoever, directly or indirectly:

(i) solicit any employee of the Company or its Affiliates with whom the Participant had any contact during the last two years of the Participant's employment, or who worked in the same business segment or division as the Participant during that period to terminate employment with the Company or its Affiliates;

(ii) solicit the employment or services of, or hire, any such employee whose employment with the Company or its Affiliates terminated coincident

with, or within twelve (12) months prior to or after the termination of Participant's employment with the Company and its Affiliates;

(iii) directly or indirectly, solicit to cease to work with the Company or its Affiliates any consultant then under contract with the Company or its Affiliates.

(b) It is expressly understood and agreed that although the Participant and the Company consider the restrictions contained in this Section 9 to be reasonable, if a final judicial determination is made by a court of competent jurisdiction that the time or any other restriction contained in this Agreement is an unenforceable restriction against the Participant, the provisions of this Agreement shall not be rendered void but shall be deemed amended to apply as to such maximum time and territory and to such maximum extent as such court may judicially determine or indicate to be enforceable. Alternatively, if any court of competent jurisdiction finds that any restriction contained in this Agreement is unenforceable, and such restriction cannot be amended so as to make it enforceable, such finding shall not affect the enforceability of any of the other restrictions contained herein.

10. Specific Performance. The Participant acknowledges and agrees that the Company's remedies at law for a breach or threatened breach of any of the provisions of Section 9 would be inadequate and the Company would suffer irreparable damages as a result of such breach or threatened breach. In recognition of this fact, the Participant agrees that, in the event of such a breach or threatened breach, in addition to any remedies at law, the Company, without posting any bond, shall be entitled to cease making any payments or providing any benefit otherwise required by this Agreement and obtain equitable relief in the form of specific performance, temporary restraining order, temporary or permanent injunction or any other equitable remedy which may then be available.

11. Choice of Law. THE INTERPRETATION, PERFORMANCE AND ENFORCEMENT OF THIS AGREEMENT SHALL BE GOVERNED BY THE LAWS OF THE STATE OF DELAWARE WITHOUT REGARD TO PRINCIPLES OF CONFLICTS OF LAW.

12. Plan and LTIP. By entering into this Agreement, the Participant agrees and acknowledges that a copy of the Plan and the LTIP has been made available to the Participant. In the event of a conflict between any term or provision contained herein and a term or provision of the Plan or LTIP, the applicable terms and provisions of the Plan and LTIP will govern and prevail.

13. Signature in Counterparts. This Agreement may be signed in counterparts, each of which shall be an original, with the same effect as if the signatures thereto and hereto were upon the same instrument.

14. 409A. Notwithstanding any other provisions of this Agreement, the Plan or the LTIP, this Award shall not be deferred, accelerated, extended, paid out or modified in a manner that would result in the imposition of an additional tax under Section 409A of the Code upon the Participant. In the event it is reasonably determined by the Committee that, as a result of Section 409A of the Code, the transfer of cash under this Agreement may not be made at the time contemplated hereunder without causing the Participant to be subject to taxation under Section 409A of the Code (including due to the Participant's status as a "specified employee" within the meaning of Section 409A of the Code), the Company will make such payment on the first day that would not result in the Participant incurring any tax liability under Section 409A of the Code.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement.

HOVNANIAN ENTERPRISES, INC.

By: _____

PARTICIPANT

By: _____

1. Purpose

The purpose of the 2019 Long-Term Incentive Program ("LTIP") is to aid the Company in retaining key employees and to motivate them to exert their best efforts on behalf of the Company. The LTIP has been adopted pursuant to the terms of the 2012 Hovnanian Enterprises, Inc. Amended and Restated Stock Incentive Plan (the "2012 Plan") and is intended to incentivize achievement of certain Pre-tax Profit goals and certain Adjusted EBIT Return on Inventory goals. Capitalized terms used herein without definition have the meanings assigned to such terms under the 2012 Plan.

2. Participants

The Compensation Committee will designate the Participants who will be granted incentive awards under the LTIP, with the first such awards to be granted on or about March 18, 2019 (the "Initial Grant Date"). Additional Associates may be eligible to participate at the discretion of the Compensation Committee or at the discretion of the Company's Chief Executive Officer (to the extent that the Compensation Committee has delegated granting authority to the Chief Executive Officer). The awards for Participants who are selected by the Compensation Committee to participate after the Initial Grant Date will be determined based on actual performance for the full Performance Period (as defined below) and will be prorated based on the number of full months of eligible service completed during the thirty-six (36) month Performance Period, subject to the vesting requirements outlined below in section 6.

3. Performance Period

The LTIP "Performance Period" will commence on November 1, 2018 and end on October 31, 2021.

4. Details

Each Participant will be eligible to receive an award based on the achievement of certain cumulative Pre-tax Profit levels in fiscal years 2019 through 2021, and certain Average Adjusted EBIT Return on Inventory levels for fiscal years 2019, 2020 and 2021. The award will be based on the closing Share price on the date the Participant is granted the award (the "Grant Date"); provided, however, that the Share price for new Participants will be no less than the Share price on the Initial Grant Date.

For purposes of the LTIP, "Pre-tax Profit" is defined as income (loss) before income tax expense and before income (loss) from unconsolidated joint ventures as reflected on the Company's audited financial statements plus income (loss) before income tax expense for the Company's unconsolidated joint ventures as reflected on their respective financial statements for the thirty-six month period ending October 31, 2021, excluding the impact of any items deemed by the Committee to be unusual or nonrecurring items and excluding losses from land impairments and gains or losses from debt repurchases/debt retirement such as call premiums and related issuance costs. "Average Adjusted EBIT Return on Inventory" is defined as the average of the quotients resulting from dividing (A) Adjusted EBIT by (B) Average Inventory for each of fiscal years 2019, 2020 and 2021. "Adjusted EBIT" is determined from the Company's audited financial statements, excluding the impact of any items deemed by the Committee to be unusual or nonrecurring items and excluding losses from land impairments and gains or losses from debt repurchases/debt retirement such as call premiums and related issuance costs. "Average Inventory" equals the average of the ending inventory balances from the Company's audited balance sheet, excluding capitalized interest and consolidated inventory not owned, for each of the five consecutive fiscal quarters ending with the last quarter of the fiscal year.

The following table illustrates the percent of the target award that can be achieved at each performance level. Awards will be interpolated between performance levels but will not be extrapolated above the maximum performance levels listed below.

| Average Adjusted EBIT Return on Inventory for FY 2019, FY 2020 and FY 2021 | | | | | | |
|--|--------|--------|--------|--------|--------|-------------------|
| 10.50% or less | 12.00% | 13.50% | 15.00% | 16.50% | 18.00% | 19.50% or more |

| Cumulative Pre-tax Profit for FY 2019 \$100 or more through FY 2021 (in millions) | 100% | 125% | 150% | 175% | 200% | 225% | 250% |
|---|------------------------|-------------------------|-------------------------|-------------------------|-------------------------|-------------------------|-------------------------|
| | of target award | of target award | of target award | of target award | of target award | of target award | of target award |
| \$75 | 75% of target award | 100% of target award | 125% of target award | 150% of target award | 175% of target award | 200% of target award | 225% of target award |
| \$50 | 50% of target award | 75% of target award | 100% of target award | 125% of target award | 150% of target award | 175% of target award | 200% of target award |
| \$25 | 0% of target award | 15% of target award | 30% of target award | 45% of target award | 60% of target award | 75% of target award | 90% of target award |
| Less than \$25 | 0% of target award | 0% of target award | 0% of target award | 0% of target award | 0% of target award | 0% of target award | 0% of target award |

5. Examples

a. If cumulative Pre-tax Profit for fiscal years 2019 through 2021 is \$50 million and Average Adjusted EBIT Return on Inventory for fiscal years 2019, 2020 and 2021 is 13.50%, a Participant would achieve an award equal to one hundred percent (100%) of the target award, subject to the vesting requirements in section 6.

b. If cumulative Pre-tax Profit for fiscal years 2019 through 2021 is \$95 million and Average Adjusted EBIT Return on Inventory for fiscal years 2019, 2020 and 2021 is 14.40%, the Participant would achieve an award equal to one hundred and sixty percent (160%) of the target award (calculated by linear interpolation from the performance goals listed on the chart), subject to the vesting requirements in section 6.

c. If cumulative Pre-tax Profit for fiscal years 2019 through 2021 is \$25 million and Average Adjusted EBIT Return on Inventory for fiscal years 2019, 2020 and 2021 is 12.00%, a Participant would achieve an award equal to fifteen percent (15%) of the target award, subject to the vesting requirements in section 6.

6. Payout Method and Conditions For Earning Award

The award is denominated fifty percent (50%) in cash and fifty percent (50%) in Phantom Shares (as defined in the Award Agreement to which this LTIP is attached as Exhibit A) provided, however, that (i) the target amount denominated in Phantom Shares will be determined based on the Fair Market Value of a Share as of the Grant Date (subject to the limitation under Section 6(a)) and (ii) the timing of payments for installments of the award denominated in cash and denominated in Phantom Shares will be determined using the respective values of the cash and Phantom Share portions of the award as of 10/31/2021, with all cash-denominated installments of the award becoming vested and payable before any Phantom Share denominated installments of the award becomes vested and payable pursuant to Section 6(b) below. For the avoidance of doubt, all payments under this LTIP will be made in cash.

a. The target award amount denominated in Phantom Shares will be determined by dividing the portion of the target award denominated in Phantom Shares by the closing Share price on the Grant Date, provided, however, that the Share price for new Participants will be no less than the Share price on the Initial Grant Date.

b. Except as provided in Section 6(c) – (f) below, as a condition of earning each portion of the award, Participants must be employed through the vesting dates outlined below. The vesting percentages relate to the award value as of 10/31/2021.

i. Sixty percent (60%) of the award will become vested on 10/31/2021 and payable in January 2022

ii. Twenty percent (20%) of the award will become vested on 10/31/2022 and payable in January 2023

iii. Twenty percent (20%) of the award will become vested on 10/31/2023 and payable in January 2024

Suppose an original Participant's target award is \$120,000.00 and the closing Share price on the Participant's Grant Date is \$0.58. Fifty percent (50%) of the award is denominated in cash and fifty percent (50%) of the award is denominated in Phantom Shares, resulting in a target cash award of \$60,000.00 (target award x 50%) and a target Phantom Share award of 103,448 Phantom Shares (target award x 50% ÷ \$0.58, rounded). Under this example, if the Participant earns one hundred and fifty percent (150%) of the target award, based on actual performance achievement, subject to the vesting requirements in this section 6, the Participant will be eligible to receive a cash portion of \$90,000.00 (\$60,000.00 target cash portion x 150%) and a Phantom Share portion of 155,172 Shares (103,448 target Phantom Share portion x 150%, rounded).

Assume that the Share price on October 31, 2021 is \$1.25 so the value of the Phantom Share denominated portion for vesting purposes is \$193,965.00 (155,172 x \$1.25). The value of the cash denominated portion of the award is not affected by stock price fluctuations and therefore remains at \$90,000 resulting in a total award value of \$283,965.00 (\$193,965.00 + \$90,000.00) as of 10/31/2021.

Per the vesting schedule, the award vests sixty percent (60%) on 10/31/2021, twenty percent (20%) on 10/31/2022 and twenty percent (20%) on 10/31/2023 with the cash denominated portion of the award vesting before the Phantom Share portion. Sixty percent (60%) of the total award value as of 10/31/2021 is \$170,379.00 (\$283,965.00 x 60%). Since the cash denominated portion is less than this amount, \$90,000.00 in cash and 64,304 Phantom Shares (\$80,379.00 ÷ \$1.25, rounded up) will vest on 10/31/2021 and be paid in January 2022. The Phantom Shares will be valued by reference to the closing price of a share of Class A Common Stock on the New York Stock Exchange as late as administratively practicable preceding the payout date in January 2022 and the result will be paid in cash on the payout date. Continuing with the example above, if the closing stock price preceding the January 2022 payout date is \$1.50, the 64,304 Phantom Shares would be valued at \$96,456.00 (64,304 x \$1.50) for a total cash payment of \$186,456 (\$90,000.00 cash + \$96,456.00 cash value of Phantom Shares) in January 2022.

On 10/31/2022, an additional twenty percent (20%) of the total award value as of 10/31/2021, or \$56,793.00 (\$283,965.00 x 20%), is scheduled to vest. Since the entire cash denominated portion had vested in the prior year, 45,435 Phantom Shares (\$56,793 ÷ \$1.25, rounded up) will vest on 10/31/2022 and be paid in January 2023. The Phantom Shares will be valued by reference to the closing price of a share of Class A Common Stock on the New York Stock Exchange as late as administratively practicable preceding the payout date in January 2023 and the result will be paid in cash on the payout date. Continuing with the example above, if the closing stock price preceding the January 2023 payout date is \$1.50, the 45,435 Phantom Shares would be

valued at \$68,153.00 (45,435 x \$1.50) for a total cash payment of \$68,153.00 in January 2023.

On 10/31/2023, the remaining portion of the award is scheduled to vest. Since the entire cash denominated portion and 109,739 Phantom Shares (64,304 + 45,435) had vested in prior years, the remaining 45,433 Phantom Shares (155,172 – 109,739) will vest on 10/31/2023 and be paid in January 2024. The Phantom Shares will be valued by reference to the closing price of a share of Class A Common Stock on the New York Stock Exchange as late as administratively practicable preceding the payout date in January 2024 and the result will be paid in cash on the payout date. Continuing with the example above, if the closing stock price preceding the January 2024 payout date is \$1.50, the 45,433 Phantom Shares would be valued at \$68,150.00 (45,433 x \$1.50) for a total cash payment of \$68,150.00 in January 2024.

c. In the event a Participant ceases to be employed by the Company due to death prior to the end of the Performance Period, the Participant's beneficiary will be eligible for a prorata award payable in January 2022. The award will be determined based on actual performance for the full Performance Period and will be prorated based on the number of full months of eligible service completed during the thirty-six (36) month Performance Period. In the event a Participant ceases to be employed by the Company due to death following the end of the Performance Period, the Participant's beneficiary will be eligible to receive any unpaid, earned portion of the award within seventy-five (75) days.

d. In the event a Participant ceases to be employed by the Company due to Disability prior to the end of the Performance Period, the Participant will be eligible to receive a prorata award on the scheduled payout dates. The award will be determined based on actual performance for the full Performance Period and will be prorated based on the number of full months of eligible service completed during the thirty-six (36) month Performance Period. In the event a Participant ceases to be employed by the Company due to Disability following the end of the Performance Period, the Participant will be eligible to receive any unpaid, earned portions of the award on the scheduled payout dates as if there was no termination of employment.

e. In the event a Participant ceases to be employed by the Company due to "Retirement" following the end of the Performance Period, the Participant will be eligible to receive any unpaid, earned portions of the award on the scheduled payout dates as if there was no termination of employment. "Retirement" shall mean termination of employment on or after age 60, or on or after age 58 with at least 15 years of "Service" to the Company and its Subsidiaries immediately preceding such termination of employment. For this purpose, "Service" means the period of employment immediately preceding Retirement, plus any prior periods of employment with the Company and its Subsidiaries of one or more years' duration, unless they were succeeded by a period of non-employment with the Company and its Subsidiaries of more than three years' duration.

f. If a Change in Control occurs while awards remain outstanding under the LTIP, then (x) if such Change in Control occurs prior to October 31, 2021 any outstanding awards will be deemed earned at target level performance and (y) all earned awards (including any earned pursuant to the preceding clause (x)) will remain eligible to vest on the scheduled vesting dates subject to meeting the employment requirements described above; provided, however, that (i) in the event the Participant is involuntarily terminated without Cause or the Participant terminates employment for Good Reason, in either case, within two years following the Change in Control, then the remaining portion of such Participant's earned award shall become fully vested and immediately payable to the Participant; (ii) in the event the Participant terminates employment due to Retirement or Disability within two years following the Change in Control, then the Participant's earned award (as determined under Section 6(d) or (e) above) shall become immediately payable to the Participant; (iii) in the event that the surviving corporation following the Change in Control is not publicly traded or, if the surviving corporation is otherwise not willing to convert the Phantom Share denominated portion of the awards into time-based vesting phantom share awards of the surviving corporation, then the outstanding awards shall be deemed fully vested as of the Change in Control date and, to the extent permissible under Section 409A of the Code and the regulations thereunder (including, without limitation, the plan termination rules thereunder), shall be immediately payable following the Change in Control; and (iv) amounts payable upon or following a Change in Control will be subject to delay in payments to the extent necessary to avoid subjecting the Participant to additional or accelerated taxes under Section 409A of the Code.

For purposes of the LTIP, "Cause" shall mean the occurrence of any of the following: (a) the willful and continued failure of the Participant to perform substantially all of his or her duties with the Company (other than any such failure resulting from incapacity due to physical or mental illness) for a period of 10 days following a written demand for substantial performance that is delivered to such Participant by the Company, which specifically identifies the manner in which the Company believes the Participant has not substantially performed his or her duties; (b) dishonesty in the performance of the Participant's duties with the Company; (c) the Participant's conviction of, or plea of guilty or nolo contendere to, a crime under the laws of the United States or any state thereof constituting a felony or a misdemeanor involving moral turpitude; (d) the Participant's willful malfeasance or willful misconduct in connection with the Participant's duties with the Company or any act or omission which is injurious to the financial condition or business reputation of the Company or its affiliates; or (e) the Participant's breach of the provisions of Section 10 of the award agreement governing the LTIP award.

For purposes of the LTIP, "Good Reason" shall mean the occurrence of any of the following, without the Participant's express written consent: (a) any material diminution in the Participant's duties, titles or responsibilities with the

Company from those in effect immediately prior to a Change in Control or (b) any reduction in the Participant's annual base salary or any material reduction in the Participant's annual bonus opportunity, annual equity awards or Long-Term Incentive Program awards from the Participant's annual base salary or annual bonus opportunity, annual equity awards or Long-Term Incentive Program awards in effect immediately prior to a Change in Control. Notwithstanding the foregoing, no event shall constitute Good Reason unless the Participant provides the Company with written notice of such event within 60 days after the occurrence thereof and the Company fails to cure or resolve the behavior otherwise constituting Good Reason within 30 days of its receipt of such notice.

7. Non-Solicitation Covenants

a. Each Participant shall be required as a condition to receiving the award to acknowledge and agree that, during the Participant's employment with the Company and its Affiliates and upon the Participant's termination of employment with the Company and its Affiliates for any reason, for a period commencing on the termination of such employment and ending on the second anniversary of such termination, the Participant shall not, whether on Participant's own behalf or on behalf of or in conjunction with any person, company, business entity or other organization whatsoever, directly or indirectly:

i. solicit any employee of the Company or its Affiliates with whom the Participant had any contact during the last two years of the Participant's employment, or who worked in the same business segment or division as the Participant during that period to terminate employment with the Company or its Affiliates;

ii. solicit the employment or services of, or hire, any such employee whose employment with the Company or its Affiliates terminated coincident with, or within twelve (12) months prior to or after the termination of Participant's employment with the Company and its Affiliates;

iii. directly or indirectly, solicit to cease to work with the Company or its Affiliates any consultant then under contract with the Company or its Affiliates.

b. It shall be expressly understood and agreed that although the Participant and the Company consider the restrictions contained in this Section 7 to be reasonable, if a final judicial determination is made by a court of competent jurisdiction that the time or any other restriction contained in this LTIP is an unenforceable restriction against the Participant, the provisions of this LTIP shall not be rendered void but shall be deemed amended to apply as to such maximum time and territory and to such maximum extent as such court may judicially determine or indicate to be enforceable. Alternatively, if any court of competent jurisdiction finds that any restriction contained in this LTIP is unenforceable, and such restriction cannot be amended so as to make it enforceable, such finding shall not affect the enforceability of any of the other restrictions contained herein.

8. Specific Performance

Each Participant shall acknowledge and agree that the Company's remedies at law for a breach or threatened breach of any of the provisions of Section 7 would be inadequate and the Company would suffer irreparable damages as a result of such breach or threatened breach. In recognition of this fact, the Participant shall agree that, in the event of such a breach or threatened breach, in addition to any remedies at law, the Company, without posting any bond, shall be entitled to cease making any payments or providing any benefit otherwise required by this LTIP and obtain equitable relief in the form of specific performance, temporary restraining order, temporary or permanent injunction or any other equitable remedy which may then be available.

9. Adjustments

Adjustments Upon Certain Events. Subject to the terms of the 2012 Plan, in the event of any change in the outstanding Shares by reason of any Share dividend or split, reorganization, recapitalization, merger, consolidation, amalgamation, spin-off or combination transaction or exchange of Shares or other similar events (collectively, an "Adjustment Event"), the Committee shall, in its sole discretion, make an appropriate and equitable adjustment in the number of Phantom Shares subject to awards granted under this LTIP to reflect such Adjustment Event. Any such adjustment made by the Committee shall be final and binding upon the Participant, the Company and all other interested persons.

10. Amendments

The Committee may amend, alter or discontinue the LTIP at any time, provided that no such amendment, alteration or discontinuation shall be made that would materially adversely affect the rights of a Participant with respect to a previously granted award hereunder without such Participant's consent.

¹ Based on March 18, 2019 closing share price of \$0.58.

CERTIFICATIONS
Exhibit 31(a)

I, Ara K. Hovnanian, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q for the period ended April 30, 2019 of Hovnanian Enterprises, Inc. (the “registrant”);
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):

(a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and

(b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: June 6, 2019

/s/ARA K. HOVNANIAN

Ara K. Hovnanian

Chairman, President and Chief Executive Officer

CERTIFICATIONS
Exhibit 31(b)

I, J. Larry Sorsby, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q for the period ended April 30, 2019 of Hovnanian Enterprises, Inc. (the “registrant”);
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):

(a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and

(b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: June 6, 2019

/s/J. LARRY SORBSY

J. Larry Sorsby

Executive Vice President and Chief Financial Officer

Exhibit 32(a)

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Hovnanian Enterprises, Inc. (the "Company") on Form 10-Q for the period ended April 30, 2019 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Ara K. Hovnanian, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: June 6, 2019

/s/ARA K. HOVNANIAN

Ara K. Hovnanian

Chairman, President and Chief Executive Officer

Exhibit 32(b)

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Hovnanian Enterprises, Inc. (the "Company") on Form 10-Q for the period ended April 30, 2019 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, J. Larry Sorsby, Executive Vice President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: June 6, 2019

/s/J. LARRY SORSBY

J. Larry Sorsby
Executive Vice President and Chief Financial Officer