
**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 June 30, 2021

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the Transition Period From _____ To _____

Commission File Number: 001-33662

FORESTAR GROUP INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware

26-1336998

(State or Other Jurisdiction of Incorporation or Organization)

(I.R.S. Employer Identification No.)

2221 E. Lamar Blvd., Suite 790

Arlington, Texas 76006

(Address of Principal Executive Offices, including Zip Code)

(817) 769-1860

(Registrant's telephone number, including area code)

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

Title of Each Class	Trading Symbol	Name of Each Exchange on Which Registered
Common Stock, par value \$1.00 per share	FOR	New York Stock Exchange

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.

Common Stock, \$1.00 par value -- 49,527,108 shares as of July 20, 2021

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PART I—FINANCIAL INFORMATION**Item 1. Financial Statements**

**FORESTAR GROUP INC.
CONSOLIDATED BALANCE SHEETS
(Unaudited)**

	June 30, 2021	September 30, 2020
	(In millions, except share data)	
ASSETS		
Cash and cash equivalents	\$ 116.0	\$ 394.3
Real estate	1,861.4	1,309.7
Investment in unconsolidated ventures	0.7	3.6
Income taxes receivable	—	6.3
Property and equipment, net	2.2	1.1
Other assets	34.7	24.9
Total assets	<u>\$ 2,015.0</u>	<u>\$ 1,739.9</u>
LIABILITIES		
Accounts payable	\$ 45.6	\$ 29.2
Earnest money on sales contracts	146.9	98.3
Deferred tax liability, net	9.8	5.7
Accrued expenses and other liabilities	138.2	93.8
Debt	704.1	641.1
Total liabilities	<u>1,044.6</u>	<u>868.1</u>
Commitments and contingencies (Note 11)		
EQUITY		
Common stock, par value \$1.00 per share, 200,000,000 authorized shares, 49,527,108 and 48,061,921 shares issued and outstanding at June 30, 2021 and September 30, 2020, respectively	49.5	48.1
Additional paid-in capital	634.9	603.9
Retained earnings	285.1	218.9
Stockholders' equity	<u>969.5</u>	<u>870.9</u>
Noncontrolling interests	0.9	0.9
Total equity	<u>970.4</u>	<u>871.8</u>
Total liabilities and equity	<u>\$ 2,015.0</u>	<u>\$ 1,739.9</u>

See accompanying notes to consolidated financial statements.

FORESTAR GROUP INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2021	2020	2021	2020
	(In millions, except per share amounts)			
Revenues	\$ 312.9	\$ 177.9	\$ 907.1	\$ 584.3
Cost of sales	257.1	157.1	753.8	510.3
Selling, general and administrative expense	16.9	11.2	48.7	32.8
Equity in loss (earnings) of unconsolidated ventures	—	0.1	(0.2)	(0.6)
Gain on sale of assets	—	—	—	(0.1)
Interest and other income	(0.3)	(0.8)	(1.2)	(4.2)
Loss on extinguishment of debt	18.1	—	18.1	—
Income before income taxes	21.1	10.3	87.9	46.1
Income tax expense	5.2	0.2	21.5	8.9
Net income	15.9	10.1	66.4	37.2
Net income attributable to noncontrolling interests	0.1	—	0.2	0.7
Net income attributable to Forestar Group Inc.	<u>\$ 15.8</u>	<u>\$ 10.1</u>	<u>\$ 66.2</u>	<u>\$ 36.5</u>
Basic net income per common share attributable to Forestar Group Inc.	<u>\$ 0.32</u>	<u>\$ 0.21</u>	<u>\$ 1.36</u>	<u>\$ 0.76</u>
Weighted average number of common shares	<u>49.4</u>	<u>48.1</u>	<u>48.7</u>	<u>48.0</u>
Diluted net income per common share attributable to Forestar Group Inc.	<u>\$ 0.32</u>	<u>\$ 0.21</u>	<u>\$ 1.36</u>	<u>\$ 0.76</u>
Adjusted weighted average number of common shares	<u>49.5</u>	<u>48.1</u>	<u>48.7</u>	<u>48.1</u>

See accompanying notes to consolidated financial statements.

FORESTAR GROUP INC.
CONSOLIDATED STATEMENTS OF TOTAL EQUITY
(Unaudited)

	<u>Common Stock</u>	<u>Additional Paid-in Capital</u>	<u>Retained Earnings</u>	<u>Non- controlling Interests</u>	<u>Total Equity</u>
	(In millions, except share data)				
Balances at September 30, 2020 (48,061,921 shares).....	\$ 48.1	\$ 603.9	\$ 218.9	\$ 0.9	\$ 871.8
Net income.....	—	—	22.0	0.1	22.1
Stock issued under employee benefit plans (14,722 shares).....	—	—	—	—	—
Cash paid for shares withheld for taxes.....	—	(0.1)	—	—	(0.1)
Stock-based compensation expense.....	—	0.3	—	—	0.3
Balances at December 31, 2020 (48,076,643 shares).....	\$ 48.1	\$ 604.1	\$ 240.9	\$ 1.0	\$ 894.1
Net income.....	—	—	28.4	—	28.4
Issuance of common stock (1,018,503 shares).....	1.0	22.3	—	—	23.3
Purchase of noncontrolling interest, net.....	—	(1.7)	—	(0.2)	(1.9)
Stock issued under employee benefit plans (29,655 shares).....	—	—	—	—	—
Cash paid for shares withheld for taxes.....	—	(0.3)	—	—	(0.3)
Stock-based compensation expense.....	—	0.9	—	—	0.9
Balances at March 31, 2021 (49,124,801 shares).....	\$ 49.1	\$ 625.3	\$ 269.3	\$ 0.8	\$ 944.5
Net income.....	—	—	15.8	0.1	15.9
Issuance of common stock (378,736 shares).....	0.4	8.9	—	—	9.3
Stock issued under employee benefit plans (23,571 shares).....	—	—	—	—	—
Cash paid for shares withheld for taxes.....	—	(0.1)	—	—	(0.1)
Stock-based compensation expense.....	—	0.8	—	—	0.8
Balances at June 30, 2021 (49,527,108 shares).....	<u>\$ 49.5</u>	<u>\$ 634.9</u>	<u>\$ 285.1</u>	<u>\$ 0.9</u>	<u>\$ 970.4</u>

See accompanying notes to consolidated financial statements.

FORESTAR GROUP INC.
CONSOLIDATED STATEMENTS OF TOTAL EQUITY (Continued)
(Unaudited)

	Common Stock	Additional Paid-in Capital	Retained Earnings	Non- controlling Interests	Total Equity
(In millions, except share data)					
Balances at September 30, 2019 (47,997,366 shares).....	\$ 48.0	\$ 602.2	\$ 158.1	\$ 0.6	\$ 808.9
Net income (loss).....	—	—	16.9	(0.1)	16.8
Stock issued under employee benefit plans (27,993 shares).....	—	—	—	—	—
Cash paid for shares withheld for taxes.....	—	(0.2)	—	—	(0.2)
Stock-based compensation expense.....	—	0.5	—	—	0.5
Distributions to noncontrolling interests.....	—	—	—	(0.4)	(0.4)
Balances at December 31, 2019 (48,025,359 shares).....	\$ 48.0	\$ 602.5	\$ 175.0	\$ 0.1	\$ 825.6
Net income.....	—	—	9.6	0.8	10.4
Stock-based compensation expense.....	—	0.8	—	—	0.8
Balances at March 31, 2020 (48,025,359 shares).....	\$ 48.0	\$ 603.3	\$ 184.6	\$ 0.9	\$ 836.8
Net income.....	—	—	10.1	—	10.1
Stock issued under employee benefit plans (34,562 shares).....	0.1	—	—	—	0.1
Cash paid for shares withheld for taxes.....	—	(0.1)	—	—	(0.1)
Stock-based compensation expense.....	—	0.3	—	—	0.3
Distributions to noncontrolling interests.....	—	—	—	(0.3)	(0.3)
Balances at June 30, 2020 (48,059,921 shares).....	\$ 48.1	\$ 603.5	\$ 194.7	\$ 0.6	\$ 846.9

See accompanying notes to consolidated financial statements.

FORESTAR GROUP INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Nine Months Ended June 30,	
	2021	2020
	(In millions)	
OPERATING ACTIVITIES		
Net income	\$ 66.4	\$ 37.2
Adjustments:		
Depreciation and amortization	2.1	4.2
Deferred income taxes	4.6	17.5
Equity in earnings of unconsolidated ventures	(0.2)	(0.6)
Stock-based compensation expense	2.0	1.6
Land option charges	1.6	0.5
Loss on extinguishment of debt	18.1	—
Gain on sale of assets	—	(0.1)
Changes in operating assets and liabilities:		
Increase in real estate	(540.7)	(258.8)
Decrease (increase) in income taxes receivable	6.3	(5.7)
Increase in other assets	(13.4)	(4.2)
Increase (decrease) in accounts payable and other accrued liabilities	60.8	(0.2)
Increase in earnest money on sales contracts	51.8	2.9
Net cash used in operating activities	<u>(340.6)</u>	<u>(205.7)</u>
INVESTING ACTIVITIES		
Expenditures for property, equipment and other	(0.5)	(0.6)
Return of investment in unconsolidated ventures	2.2	2.4
Proceeds from sale of assets	—	1.3
Net cash provided by investing activities	<u>1.7</u>	<u>3.1</u>
FINANCING ACTIVITIES		
Proceeds from debt	425.0	300.0
Repayments of debt	(389.0)	(118.9)
Deferred financing fees	(5.0)	(4.8)
Proceeds from issuance of common stock	32.6	—
Purchase of noncontrolling interest	(2.4)	—
Distributions to noncontrolling interests, net	(0.1)	(0.7)
Cash paid for shares withheld for taxes	(0.5)	(0.2)
Net cash provided by financing activities	<u>60.6</u>	<u>175.4</u>
Net decrease in cash and cash equivalents	(278.3)	(27.2)
Cash and cash equivalents at beginning of period	394.3	382.8
Cash and cash equivalents at end of period	<u>\$ 116.0</u>	<u>\$ 355.6</u>
SUPPLEMENTAL DISCLOSURES OF NON-CASH ACTIVITIES		
Note payable issued for real estate	<u>\$ 12.5</u>	<u>\$ —</u>

See accompanying notes to consolidated financial statements.

FORESTAR GROUP INC.
Notes to Consolidated Financial Statements
(Unaudited)

Note 1—Basis of Presentation

The accompanying unaudited, consolidated financial statements include the accounts of Forestar Group Inc. (Forestar) and all of its 100% owned, majority-owned and controlled subsidiaries, which are collectively referred to as the Company unless the context otherwise requires. The Company accounts for its investment in other entities in which it has significant influence over operations and financial policies using the equity method. All intercompany accounts, transactions and balances have been eliminated in consolidation. Noncontrolling interests in consolidated pass-through entities are recognized before income taxes. The transactions included in net income in the consolidated statements of operations are the same as those that would be presented in comprehensive income. Thus, the Company's net income equates to comprehensive income.

The financial statements have been prepared in accordance with U.S. Generally Accepted Accounting Principles (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. In the opinion of management, these financial statements reflect all adjustments considered necessary to fairly state the results for the interim periods shown, including normal recurring accruals and other items. These financial statements, including the consolidated balance sheet as of September 30, 2020, which was derived from audited financial statements, do not include all of the information and notes required by GAAP for complete financial statements and should be read in conjunction with the consolidated financial statements and accompanying notes included in the Company's annual report on Form 10-K for the fiscal year ended September 30, 2020. Certain items have been reclassified in the prior year financial statements to conform to the presentation and classifications used in the current year.

In October 2017, Forestar became a majority-owned subsidiary of D.R. Horton, Inc. (D.R. Horton) by virtue of a merger with a wholly-owned subsidiary of D.R. Horton. Immediately following the merger, D.R. Horton owned 75% of the Company's outstanding common stock. In connection with the merger, the Company entered into certain agreements with D.R. Horton including a Stockholder's Agreement, a Master Supply Agreement, and a Shared Services Agreement. D.R. Horton is considered a related party of Forestar under GAAP. At June 30, 2021, D.R. Horton owned approximately 64% of the Company's outstanding common stock.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions. These estimates and assumptions 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 materially from those estimates.

Pending Accounting Standards

In December 2019, the FASB issued ASU 2019-12 related to simplifying the accounting for income taxes. The guidance is effective for the Company beginning October 1, 2021, although early adoption is permitted. The Company is currently evaluating the impact of this guidance, and it is not expected to have a material impact on its consolidated financial position, results of operations or cash flows.

In March 2020, the FASB issued ASU 2020-04, "Reference Rate Reform," which provides optional expedients and exceptions for applying U.S. GAAP to contracts, hedging relationships and other transactions affected by the discontinuation of the London Interbank Offered Rate (LIBOR) or by another reference rate expected to be discontinued. The guidance was effective beginning March 12, 2020 and can be applied prospectively through December 31, 2022. In January 2021, the FASB issued ASU 2021-01, "Reference Rate Reform - Scope," which clarified the scope and application of the original guidance. The Company will adopt these standards when LIBOR is discontinued and does not expect them to have a material impact on its consolidated financial statements and related disclosures.

Note 2—Segment Information

The Company manages its operations through its real estate segment which is its core business and generates substantially all of its revenues. The real estate segment primarily acquires land and develops infrastructure for single-family residential communities, and its revenues generally come from sales of residential single-family finished lots to local, regional and national homebuilders. The Company has other business activities for which the related assets and operating results are immaterial and therefore are included within the Company's real estate segment.

Note 3—Real Estate

Real estate consists of:

	<u>June 30, 2021</u>	<u>September 30, 2020</u>
	(In millions)	
Developed and under development projects.....	\$ 1,777.9	\$ 1,304.3
Undeveloped land.....	83.5	5.4
	<u>\$ 1,861.4</u>	<u>\$ 1,309.7</u>

In the nine months ended June 30, 2021, the Company invested \$654.7 million in the acquisition of residential real estate and \$604.3 million in the development of residential real estate. At June 30, 2021 and September 30, 2020, undeveloped land primarily consisted of undeveloped land which the Company has the contractual right to sell to D.R. Horton at a sales price equal to the carrying value of the land at the time of sale plus additional consideration of 12% to 16% per annum.

Each quarter, the Company reviews the performance and outlook for all of its real estate for indicators of potential impairment and performs detailed impairment evaluations and analyses when necessary. As a result of this process, there were no real estate impairment charges recorded for any period presented in the consolidated statements of operations.

During the three and nine months ended June 30, 2021, pre-acquisition cost write-offs related to land purchase contracts that the Company has terminated or expects to terminate were \$0.7 million and \$1.6 million, respectively, compared to \$0.1 million and \$0.5 million in the prior year periods. Real estate impairments and land option charges are included in cost of sales in the consolidated statements of operations.

Note 4—Revenues

Revenues consist of:

	<u>Three Months Ended June 30,</u>		<u>Nine Months Ended June 30,</u>	
	<u>2021</u>	<u>2020</u>	<u>2021</u>	<u>2020</u>
	(In millions)			
Residential lot sales.....	\$ 307.4	\$ 164.4	\$ 894.5	\$ 537.9
Tract sales and other.....	5.5	13.5	12.6	46.4
	<u>\$ 312.9</u>	<u>\$ 177.9</u>	<u>\$ 907.1</u>	<u>\$ 584.3</u>

Note 5—Capitalized Interest

The Company capitalizes interest costs to real estate throughout the development period (active real estate). Capitalized interest is charged to cost of sales as the related real estate is sold to the buyer. During periods in which the Company's active real estate is lower than its debt level, a portion of the interest incurred is reflected as interest expense in the period incurred. During the first nine months of fiscal 2021 and fiscal 2020, the Company's active real estate exceeded its debt level, and all interest incurred was capitalized to real estate.

The following table summarizes the Company's interest costs incurred, capitalized and expensed during the three and nine months ended June 30, 2021 and 2020.

	<u>Three Months Ended June 30,</u>		<u>Nine Months Ended June 30,</u>	
	<u>2021</u>	<u>2020</u>	<u>2021</u>	<u>2020</u>
	(In millions)			
Capitalized interest, beginning of period.....	\$ 54.3	\$ 37.9	\$ 48.7	\$ 23.7
Interest incurred.....	10.3	11.4	33.3	32.0
Interest charged to cost of sales.....	(8.1)	(4.1)	(25.5)	(10.5)
Capitalized interest, end of period.....	<u>\$ 56.5</u>	<u>\$ 45.2</u>	<u>\$ 56.5</u>	<u>\$ 45.2</u>

Note 6—Other Assets, Accrued Expenses and Other Liabilities

The Company's other assets at June 30, 2021 and September 30, 2020 were as follows:

	June 30, 2021	September 30, 2020
	(In millions)	
Receivables, net	\$ 0.5	\$ 0.4
Earnest money notes receivable on sales contracts	1.5	4.8
Lease right of use assets	5.6	3.6
Prepaid expenses	11.2	4.9
Land purchase contract deposits	11.4	5.5
Other assets	4.5	5.7
	<u>\$ 34.7</u>	<u>\$ 24.9</u>

The Company's accrued expenses and other liabilities at June 30, 2021 and September 30, 2020 were as follows:

	June 30, 2021	September 30, 2020
	(In millions)	
Accrued employee compensation and benefits	\$ 4.6	\$ 6.2
Accrued property taxes	2.9	3.8
Lease liabilities	6.0	3.8
Accrued interest	8.3	14.0
Contract liabilities	4.1	0.2
Deferred income	9.3	9.3
Income taxes payable	8.5	0.5
Accrued development costs	84.5	44.4
Other accrued expenses	8.8	10.2
Other liabilities	1.2	1.4
	<u>\$ 138.2</u>	<u>\$ 93.8</u>

Note 7—Debt

The Company's notes payable at their carrying amounts consist of the following:

	June 30, 2021	September 30, 2020
	(In millions)	
Unsecured:		
Revolving credit facility	\$ —	\$ —
8.0% senior notes due 2024 (1)	—	345.2
3.85% senior notes due 2026 (1)	395.2	—
5.0% senior notes due 2028 (1)	296.4	295.9
Other note payable	12.5	—
	<u>\$ 704.1</u>	<u>\$ 641.1</u>

(1) Unamortized debt issuance costs that were deducted from the carrying amounts of the senior notes totaled \$8.4 million and \$8.9 million at June 30, 2021 and September 30, 2020, respectively.

Bank Credit Facility

In April 2021, the Company's senior unsecured revolving credit facility was amended to increase its capacity to \$410 million with an uncommitted accordion feature that could increase the size of the facility to \$600 million, subject to certain conditions and availability of additional bank commitments. The facility also provides for the issuance of letters of credit with a sublimit equal to the greater of \$100 million and 50% of the revolving credit commitment. Borrowings under the revolving credit facility are subject to a borrowing base calculation based on the book value of the Company's real estate assets and unrestricted cash. Letters of credit issued under the facility reduce the available borrowing capacity. The maturity date of the facility was extended to April 16, 2025. Borrowings and repayments under the facility were \$25 million each during the nine months ended June 30, 2021. At June 30, 2021, there were no borrowings outstanding and \$60.2 million of letters of credit issued under the revolving credit facility, resulting in available capacity of \$349.8 million.

The revolving credit facility includes customary affirmative and negative covenants, events of default and financial covenants. The financial covenants require a minimum level of tangible net worth, a minimum level of liquidity, and a maximum allowable leverage ratio. These covenants are measured as defined in the credit agreement governing the facility and are reported to the lenders quarterly. A failure to comply with these financial covenants could allow the lending banks to terminate the availability of funds under the revolving credit facility or cause any outstanding borrowings to become due and payable prior to maturity. At June 30, 2021, the Company was in compliance with all of the covenants, limitations and restrictions of its revolving credit facility.

Senior Notes

The Company has outstanding senior notes as described below that were issued pursuant to Rule 144A and Regulation S under the Securities Act of 1933, as amended. The notes represent senior unsecured obligations that rank equally in right of payment to all existing and future senior unsecured indebtedness and may be redeemed prior to maturity, subject to certain limitations and premiums defined in the indenture agreements. The notes are guaranteed by each of the Company's subsidiaries to the extent such subsidiaries guarantee the Company's revolving credit facility.

In April 2021, the Company issued \$400 million principal amount of 3.85% senior notes that mature May 15, 2026 with interest payable semi-annually. On or after May 15, 2023, the notes may be redeemed at 101.925% of their principal amount plus any accrued and unpaid interest. In accordance with the indenture, the redemption price decreases annually thereafter and the notes can be redeemed at par on or after May 15, 2025 through maturity. The annual effective interest rate of the notes after giving effect to the amortization of financing costs is 4.1%. The net proceeds from this issuance were primarily used to redeem the Company's \$350 million principal amount of 8.0% senior notes due April 15, 2024 on May 7, 2021. The redemption price of \$365.6 million included a call premium of \$14.0 million and accrued and unpaid interest of \$1.6 million. The Company recognized an \$18.1 million loss on extinguishment of debt upon the redemption of the notes.

The Company's \$300 million principal amount of 5.0% senior notes mature March 1, 2028 with interest payable semi-annually. On or after March 1, 2023, the notes may be redeemed at 102.5% of their principal amount plus any accrued and unpaid interest. In accordance with the indenture, the redemption price decreases annually thereafter and the notes can be redeemed at par on or after March 1, 2026 through maturity. The annual effective interest rate of the notes after giving effect to the amortization of financing costs is 5.2%.

The indentures governing the senior notes require that, upon the occurrence of both a change of control and a rating decline (each as defined in the respective indenture), the Company offer to purchase the notes at 101% of their principal amount. If the Company or its restricted subsidiaries dispose of assets, under certain circumstances, the Company will be required to either invest the net cash proceeds from such asset sales in its business within a specified period of time, repay certain senior secured debt or debt of its non-guarantor subsidiaries, or make an offer to purchase a principal amount of the notes equal to the excess net cash proceeds at a purchase price of 100% of their principal amount. The indentures contain covenants that, among other things, restrict the ability of the Company and its restricted subsidiaries to pay dividends or distributions, repurchase equity, prepay subordinated debt and make certain investments; incur additional debt or issue mandatorily redeemable equity; incur liens on assets; merge or consolidate with another company or sell or otherwise dispose of all or substantially all of the Company's assets; enter into transactions with affiliates; and allow to exist certain restrictions on the ability of subsidiaries to pay dividends or make other payments. At June 30, 2021, the Company was in compliance with all of the limitations and restrictions associated with its senior note obligations.

Effective April 30, 2020, the Board of Directors authorized the repurchase of up to \$30 million of the Company's debt securities. The authorization has no expiration date. All of the \$30 million authorization was remaining at June 30, 2021.

Other Note Payable

The Company also has a note payable of \$12.5 million that was issued as part of a transaction to acquire real estate for development. The note is non-recourse and is secured by the underlying real estate, accrues interest at 4.0% per annum and matures in October 2023.

Note 8—Earnings per Share

The computations of basic and diluted earnings per share are as follows:

	<u>Three Months Ended June 30,</u>		<u>Nine Months Ended June 30,</u>	
	<u>2021</u>	<u>2020</u>	<u>2021</u>	<u>2020</u>
(In millions, except share and per share amounts)				
Numerator:				
Net income attributable to Forestar Group Inc.....	\$ 15.8	\$ 10.1	\$ 66.2	\$ 36.5
Denominator:				
Weighted average common shares outstanding — basic.....	49,419,594	48,050,379	48,653,676	48,028,957
Dilutive effect of stock-based compensation.....	89,485	24,831	83,623	45,903
Total weighted average shares outstanding — diluted	49,509,079	48,075,210	48,737,299	48,074,860
Basic net income per common share attributable to Forestar Group Inc.....	\$ 0.32	\$ 0.21	\$ 1.36	\$ 0.76
Diluted net income per common share attributable to Forestar Group Inc.....	\$ 0.32	\$ 0.21	\$ 1.36	\$ 0.76

Note 9—Income Taxes

The Company's income tax expense for the three and nine months ended June 30, 2021 was \$5.2 million and \$21.5 million compared to \$0.2 million and \$8.9 million in the prior year periods. The effective tax rate was 24.6% and 24.5% for the three and nine months ended June 30, 2021 compared to 1.9% and 19.3% in the prior year periods. The effective tax rate for the three and nine months ended June 30, 2020 includes a tax benefit of \$2.3 million related to the net operating loss (NOL) carryback provisions of the Coronavirus Aid, Relief, and Economic Security Act, which allowed the Company to carryback a portion of its 2018 NOL. The carryback provisions resulted in the recognition of previously unrecognized tax benefits and the revaluation of deferred tax assets due to the utilization of NOLs at a higher tax rate in the carryback period. The effective tax rate for all periods includes an expense for state income taxes and nondeductible expenses and a benefit related to noncontrolling interests.

At June 30, 2021, the Company had deferred tax liabilities, net of deferred tax assets, of \$8.5 million. The deferred tax assets were partially offset by a valuation allowance of \$1.3 million, resulting in a net deferred tax liability of \$9.8 million. At September 30, 2020, deferred tax liabilities, net of deferred tax assets, were \$4.2 million. The deferred tax assets were partially offset by a valuation allowance of \$1.5 million, resulting in a net deferred tax liability of \$5.7 million. The valuation allowance for both periods was recorded because it is more likely than not that a portion of the Company's state deferred tax assets, primarily NOL carryforwards, will not be realized because the Company is no longer operating in some states or the NOL carryforward periods are too brief to realize the related deferred tax asset. The Company will continue to evaluate both the positive and negative evidence in determining the need for a valuation allowance on its deferred tax assets. Any reversal of the valuation allowance in future periods will impact the effective tax rate.

Note 10—Stockholders' Equity and Stock-Based Compensation

Stockholders' Equity

The Company has an effective shelf registration statement filed with the Securities and Exchange Commission (SEC) in September 2018 registering \$500 million of equity securities, of which \$100 million was reserved for sales under its at-the-market equity offering program that became effective in August 2020. During the three and nine months ended June 30, 2021, the Company issued 0.4 million and 1.4 million shares of common stock under its at-the-market equity offering program for proceeds of \$9.3 million and \$32.6 million, respectively, net of commissions and other issuance costs. At June 30, 2021, \$361.0 million remained available for issuance under the shelf registration statement, of which \$66.7 million is reserved for sales under the Company's at-the-market equity offering program.

Restricted Stock Units (RSUs)

The Company's Stock Incentive Plan provides for the granting of stock options and restricted stock units to executive officers, other key employees and non-management directors. Restricted stock unit awards may be based on performance (performance-based) or on service over a requisite time period (time-based). RSU equity awards represent the contingent right to receive one share of the Company's common stock per RSU if the vesting conditions and/or performance criteria are satisfied. The RSUs have no voting rights until vested.

During the nine months ended June 30, 2021, a total of 234,000 time-based RSUs were granted. The weighted average grant date fair value of these equity awards was \$23.13 per unit, and they vest annually in equal installments over a period of three to five years. Total stock-based compensation expense related to the Company's restricted stock units for the three and nine months ended June 30, 2021 was \$0.8 million and \$2.0 million compared to \$0.3 million and \$1.6 million in the prior year periods. Stock-based compensation expense in the nine months ended June 30, 2021 and 2020 included \$0.7 million and \$0.6 million, respectively, of expense recognized for employees that were retirement eligible on the date of grant.

Note 11—Commitments and Contingencies

Contractual Obligations and Off-Balance Sheet Arrangements

In support of the Company's residential lot development business, it issues letters of credit under the revolving credit facility and has a surety bond program that provides financial assurance to beneficiaries related to the execution and performance of certain development obligations. At June 30, 2021, the Company had outstanding letters of credit of \$60.2 million under the revolving credit facility and surety bonds of \$436.6 million issued by third parties to secure performance under various contracts. The Company expects that its performance obligations secured by these letters of credit and bonds will generally be completed in the ordinary course of business and in accordance with the applicable contractual terms. When the Company completes its performance obligations, the related letters of credit and bonds are generally released shortly thereafter, leaving the Company with no continuing obligations. The Company has no material third-party guarantees.

Litigation

The Company is involved in various legal proceedings that arise from time to time in the ordinary course of business and believes that adequate reserves have been established for any probable losses. The Company does not believe that the outcome of any of these proceedings will have a significant adverse effect on its financial position, long-term results of operations or cash flows. It is possible, however, that charges related to these matters could be significant to the Company's results or cash flows in any one accounting period.

Note 12—Related Party Transactions

The Company has a Shared Services Agreement with D.R. Horton whereby D.R. Horton provides the Company with certain administrative, compliance, operational and procurement services. During the nine months ended June 30, 2021 and 2020, selling, general and administrative expense in the consolidated statements of operations includes \$2.9 million and \$3.8 million for these shared services, \$3.4 million and \$1.9 million for the cost of health insurance and other employee benefits and \$5.5 million and \$3.4 million for other corporate and administrative expenses paid by D.R. Horton on behalf of the Company.

Under the terms of the Master Supply Agreement with D.R. Horton, both companies identify land development opportunities to expand Forestar's portfolio of assets. At June 30, 2021 and September 30, 2020, the Company owned or controlled through purchase contracts approximately 96,600 and 60,500 residential lots, of which D.R. Horton had the following involvement.

	June 30, 2021	September 30, 2020
	(Dollars in millions)	
Residential lots under contract to sell to D.R. Horton	21,500	14,000
Residential lots subject to right of first offer with D.R. Horton	17,900	16,400
Earnest money deposits from D.R. Horton for lots under contract	\$ 142.5	\$ 92.2
Earnest money notes from D.R. Horton for lots under contract	\$ 1.5	\$ 4.8
Remaining purchase price of lots under contract with D.R. Horton	\$ 1,611.5	\$ 1,022.2

In the three months ended June 30, 2021 and 2020, the Company's residential lot sales totaled 3,858 and 2,023, and lot sales revenues were \$307.4 million and \$164.4 million. In the nine months ended June 30, 2021 and 2020, the Company's residential lot sales totaled 11,013 and 6,396, and lot sales revenues were \$894.5 million and \$537.9 million. Revenues recognized from sales to D.R. Horton during those periods were as follows.

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2021	2020	2021	2020
	(Dollars in millions)			
Residential single-family lots sold to D.R. Horton.....	3,719	1,991	10,466	6,287
Residential lot sales revenues from sales to D.R. Horton... \$	300.4	\$ 159.3	\$ 860.0	\$ 526.0
Tract acres sold to D.R. Horton.....	7	30	21	66
Tract sales revenues from sales to D.R. Horton..... \$	3.0	\$ 13.4	\$ 6.0	\$ 20.6
Other revenue from transactions with D.R. Horton..... \$	2.4	\$ —	\$ 2.4	\$ —

In addition, the net impact of the change in contract liabilities decreased revenues on lot sales to D.R. Horton by \$3.9 million in both the three and nine months ended June 30, 2021 and increased revenues on lot sales to D.R. Horton by \$2.8 million and \$2.1 million in the three and nine months ended June 30, 2020.

During the three and nine months ended June 30, 2021, the Company reimbursed D.R. Horton approximately \$3.5 million and \$27.7 million for previously paid earnest money and \$14.9 million and \$43.1 million for pre-acquisition and other due diligence and development costs related to land purchase contracts whereby D.R. Horton assigned its rights under these land purchase contracts to the Company. During the three and nine months ended June 30, 2020, the Company reimbursed D.R. Horton approximately \$7.0 million and \$23.2 million for previously paid earnest money and \$12.9 million and \$26.2 million for pre-acquisition and other due diligence and development costs.

During the three and nine months ended June 30, 2021, the Company paid D.R. Horton \$1.3 million and \$4.2 million for land development services compared to \$1.0 million and \$3.9 million for these services in the prior year periods. These amounts are included in cost of sales in the Company's consolidated statements of operations.

At June 30, 2021 and September 30, 2020, undeveloped land was \$83.5 million and \$5.4 million. Undeveloped land primarily consists of undeveloped land which the Company has the contractual right to sell to D.R. Horton at a sales price equal to the carrying value of the land at the time of sale plus additional consideration of 12% to 16% per annum.

At June 30, 2021 and September 30, 2020, accrued expenses and other liabilities on the Company's consolidated balance sheets included \$6.5 million and \$8.4 million, respectively, owed to D.R. Horton for any accrued and unpaid shared service charges, land purchase contract deposits and due diligence and other development cost reimbursements.

Note 13—Fair Value Measurements

Fair value is the exchange price that would be received for an asset or paid to transfer a liability in an orderly transaction between market participants. In arriving at a fair value measurement, the Company uses a fair value hierarchy based on three levels of inputs, of which the first two are considered observable and the last unobservable. The three levels of inputs used to establish fair value are the following:

- Level 1 — Quoted prices in active markets for identical assets or liabilities;
- Level 2 — Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities; and
- Level 3 — Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

The Company elected not to use the fair value option for cash and cash equivalents and debt.

For the financial assets and liabilities that the Company does not reflect at fair value, the following tables present both their respective carrying value and fair value at June 30, 2021 and September 30, 2020.

	Carrying Value	Fair Value at June 30, 2021			
		Level 1	Level 2	Level 3	Total
		(in millions)			
Cash and cash equivalents (1)	\$ 116.0	\$ 116.0	\$ —	\$ —	\$ 116.0
Debt (2) (3)	704.1	—	715.4	12.5	727.9

	Carrying Value	Fair Value at September 30, 2020			
		Level 1	Level 2	Level 3	Total
		(in millions)			
Cash and cash equivalents (1)	\$ 394.3	\$ 394.3	\$ —	\$ —	\$ 394.3
Debt (2)	641.1	—	673.5	—	673.5

- (1) The fair values of cash and cash equivalents approximate their carrying values due to their short-term nature and are classified as Level 1 within the fair value hierarchy.
- (2) At June 30, 2021 and September 30, 2020, the Company's debt primarily consisted of its senior notes. The fair value of the senior notes is determined based on quoted market prices, which is classified as Level 2 within the fair value hierarchy.
- (3) The fair value of the Company's other note payable approximates its carrying value due to its short-term nature and is classified as Level 3 within the fair value hierarchy.

Non-financial assets measured at fair value on a non-recurring basis primarily include real estate assets which the Company reviews for indicators of potential impairment and performs impairment evaluations when necessary.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our consolidated financial statements and related notes included in this quarterly report and with our annual report on Form 10-K for the fiscal year ended September 30, 2020. Some of the information contained in this discussion and analysis constitutes forward-looking statements that involve risks and uncertainties. Actual results could differ materially from those discussed in these forward-looking statements. Factors that could cause or contribute to these differences include, but are not limited to, those described in the "Forward-Looking Statements" section following this discussion.

Our Operations

We are a residential lot development company with operations in 55 markets in 22 states as of June 30, 2021. In October 2017, we became a majority-owned subsidiary of D.R. Horton. Through our alignment with and support from D.R. Horton, we have grown our business into a national, well-capitalized residential lot developer selling lots to D.R. Horton and other homebuilders. As our controlling shareholder, D.R. Horton has significant influence in guiding our strategic direction and operations. Our strategy is focused on making investments in land acquisition and development to expand our residential lot development business across a geographically diversified national platform and consolidating market share in the fragmented U.S. lot development industry. We are primarily investing in short duration, phased development projects that generate returns similar to production-oriented homebuilders. This strategy is a unique, lower-risk business model that we expect will produce more consistent returns than other public and private land developers. We also make short term investments in finished lots (lot banking) and undeveloped land with the intent to sell these assets within a short time period, primarily to D.R. Horton, utilizing available capital prior to its deployment into longer term lot development projects.

COVID-19

During March 2020, the impacts of the COVID-19 pandemic and the related widespread reductions in economic activity began to temporarily affect our business operations and the demand for our residential lots. However, as economic activity and housing market conditions began to improve, our lot sales pace increased during the last half of fiscal 2020 and has remained strong throughout the first nine months of fiscal 2021. We believe we are well positioned to effectively operate through changing economic conditions due to our low net leverage and strong liquidity position, our low overhead model and our strategic relationship with D.R. Horton. However, multiple disruptions in the supply chain, combined with the improvement in economic conditions and strong demand for residential lots, have resulted in shortages in certain construction materials and tightness in the labor market, which has caused our development cycles to lengthen in certain markets.

Business Segment

We manage our operations through our real estate segment which is our core business and generates substantially all of our revenues. The real estate segment primarily acquires land and develops infrastructure for single-family residential communities and generates revenues from sales of residential single-family finished lots to local, regional and national homebuilders. We have other business activities for which the related assets and operating results are immaterial, and therefore, are included in our real estate segment.

Results of Operations

The following tables and related discussion set forth key operating and financial data as of and for the three and nine months ended June 30, 2021 and 2020.

Operating Results

Components of income before income taxes were as follows:

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2021	2020	2021	2020
	(In millions)			
Revenues	\$ 312.9	\$ 177.9	\$ 907.1	\$ 584.3
Cost of sales	257.1	157.1	753.8	510.3
Selling, general and administrative expense	16.9	11.2	48.7	32.8
Equity in loss (earnings) of unconsolidated ventures	—	0.1	(0.2)	(0.6)
Gain on sale of assets	—	—	—	(0.1)
Interest and other income	(0.3)	(0.8)	(1.2)	(4.2)
Loss on extinguishment of debt	18.1	—	18.1	—
Income before income taxes	<u>\$ 21.1</u>	<u>\$ 10.3</u>	<u>\$ 87.9</u>	<u>\$ 46.1</u>

Lot Sales

Residential lots sold consist of:

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2021	2020	2021	2020
Development projects	3,330	1,556	9,606	4,234
Lot banking projects	528	467	1,407	2,162
	<u>3,858</u>	<u>2,023</u>	<u>11,013</u>	<u>6,396</u>
Average sales price per lot (1)	\$ 80,700	\$ 79,900	\$ 81,600	\$ 83,800

(1) Excludes any impact from change in contract liabilities.

Revenues

Revenues consist of:

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2021	2020	2021	2020
	(In millions)			
Residential lot sales:				
Development projects	\$ 274.8	\$ 124.5	\$ 797.0	\$ 340.8
Lot banking projects	36.5	37.1	101.4	195.0
(Increase) decrease in contract liabilities	(3.9)	2.8	(3.9)	2.1
	<u>307.4</u>	<u>164.4</u>	<u>894.5</u>	<u>537.9</u>
Tract sales and other	5.5	13.5	12.6	46.4
	<u>\$ 312.9</u>	<u>\$ 177.9</u>	<u>\$ 907.1</u>	<u>\$ 584.3</u>

Residential lots sold and residential lot sales revenues have increased as we have grown our business primarily through our strategic relationship with D.R. Horton. In the three months ended June 30, 2021, we sold 3,719 residential lots to D.R. Horton for \$300.4 million compared to 1,991 residential lots sold to D.R. Horton for \$159.3 million in the prior year period. In the nine months ended June 30, 2021, we sold 10,466 residential lots to D.R. Horton for \$860.0 million compared to 6,287 residential lots sold to D.R. Horton for \$526.0 million in the prior year period. In the three months ended June 30, 2021, we sold 139 residential lots to builders other than D.R. Horton for \$10.8 million compared to 32 residential lots sold to builders other than D.R. Horton for \$2.3 million in the prior year period. In the nine months ended June 30, 2021, we sold 547 residential lots to builders other than D.R. Horton for \$38.4 million compared to 109 residential lots sold to builders other than D.R. Horton for \$9.8 million in the prior year period.

Tract sales and other revenue in the three months ended June 30, 2021 primarily consisted of 7 tract acres sold to D.R. Horton for \$3.0 million. Tract sales and other revenue in the nine months ended June 30, 2021 primarily consisted of 11 tract acres sold to third parties for \$1.4 million and 21 tract acres sold to D.R. Horton for \$6.0 million. Tract sales and other revenue in the three months ended June 30, 2020 primarily consisted of 30 tract acres sold to D.R. Horton for \$13.4 million. Tract sales and other revenue in the nine months ended June 30, 2020 primarily consisted of 588 acres sold to third parties for \$25.3 million and 66 tract acres sold to D.R. Horton for \$20.6 million.

Cost of sales in the three and nine months ended June 30, 2021 increased as compared to the prior year periods primarily due to the increases in the number of lots sold. Cost of sales related to tract sales and other revenue was \$3.1 million and \$7.4 million in the three and nine months ended June 30, 2021, respectively, compared to \$12.8 million and \$36.7 million in the three and nine months ended June 30, 2020.

Selling, General and Administrative (SG&A) Expense and Other Income Statement Items

SG&A expense in the three and nine months ended June 30, 2021 was \$16.9 million and \$48.7 million compared to \$11.2 million and \$32.8 million in the prior year periods. SG&A expense as a percentage of revenues was 5.4% in both the three and nine months ended June 30, 2021 compared to 6.3% and 5.6% in the prior year periods. Our SG&A expense primarily consists of employee compensation and related costs. Our business operations employed 232 and 128 employees at June 30, 2021 and 2020, respectively.

Equity in earnings of unconsolidated ventures in all periods reflects our share of earnings in ventures that we account for using the equity method.

Loss on extinguishment of debt of \$18.1 million in the three and nine months ended June 30, 2021 was due to the redemption of our \$350 million principal amount of 8.0% senior notes due 2024 in May 2021.

Interest and other income primarily represents interest earned on our cash deposits.

Income Taxes

Our income tax expense for the three and nine months ended June 30, 2021 was \$5.2 million and \$21.5 million compared to \$0.2 million and \$8.9 million in the prior year periods. Our effective tax rate was 24.6% and 24.5% for the three and nine months ended June 30, 2021 compared to 1.9% and 19.3% in the prior year periods. Our effective tax rate for the three and nine months ended June 30, 2020 includes a tax benefit of \$2.3 million related to the net operating loss (NOL) carryback provisions of the Coronavirus Aid, Relief, and Economic Security Act, which allowed us to carryback a portion of our 2018 NOL. The carryback provisions resulted in the recognition of previously unrecognized tax benefits and the revaluation of deferred tax assets due to the utilization of NOLs at a higher tax rate in the carryback period. Our effective tax rate for all periods includes an expense for state income taxes and nondeductible expenses and a benefit related to noncontrolling interests.

At June 30, 2021, we had deferred tax liabilities, net of deferred tax assets, of \$8.5 million. The deferred tax assets were partially offset by a valuation allowance of \$1.3 million, resulting in a net deferred tax liability of \$9.8 million. At September 30, 2020, deferred tax liabilities, net of deferred tax assets, were \$4.2 million. The deferred tax assets were partially offset by a valuation allowance of \$1.5 million, resulting in a net deferred tax liability of \$5.7 million. The valuation allowance for both periods was recorded because it is more likely than not that a portion of our state deferred tax assets, primarily NOL carryforwards, will not be realized because we are no longer operating in some states or the NOL carryforward periods are too brief to realize the related deferred tax asset. We will continue to evaluate both the positive and negative evidence in determining the need for a valuation allowance on our deferred tax assets. Any reversal of the valuation allowance in future periods will impact our effective tax rate.

Land and Lot Position

Our land and lot position at June 30, 2021 and September 30, 2020 is summarized as follows:

	June 30, 2021	September 30, 2020
Lots owned	64,200	42,400
Lots controlled through land and lot purchase contracts	32,400	18,100
Total lots owned and controlled	<u>96,600</u>	<u>60,500</u>

At June 30, 2021, our lot position consisted of approximately 96,600 residential lots, of which 64,200 were owned and 32,400 were controlled through purchase contracts. Of our total owned residential lots, approximately 21,500 were under contract to sell to D.R. Horton. Additionally, D.R. Horton has the right of first offer on approximately 17,900 of these lots based on executed purchase and sale agreements. At June 30, 2021, lots owned included approximately 4,400 that were fully developed, of which approximately 600 are related to lot banking. At June 30, 2021, we had approximately 900 lots under contract to sell to builders other than D.R. Horton.

Liquidity and Capital Resources

At June 30, 2021, we had \$116.0 million of cash and cash equivalents and \$349.8 million of available borrowing capacity on our revolving credit facility. We have no senior note maturities until fiscal 2026. We believe we are well positioned to effectively operate through changing economic conditions because of our low net leverage and strong liquidity position, our low overhead model and our strategic relationship with D.R. Horton.

At June 30, 2021, our ratio of debt to total capital (debt divided by stockholders' equity plus debt) was 42.1% compared to 42.4% at September 30, 2020 and 43.1% at June 30, 2020. Our ratio of net debt to total capital (debt net of unrestricted cash divided by stockholders' equity plus debt net of unrestricted cash) was 37.8% compared to 22.1% at September 30, 2020 and 25.2% at June 30, 2020. Over the long term, we intend to maintain our ratio of net debt to total capital at or below 40%. We believe that the ratio of net debt to total capital is useful in understanding the leverage employed in our operations.

We believe that our existing cash resources and revolving credit facility will provide sufficient liquidity to fund our near-term working capital needs. Our ability to achieve our long-term growth objectives will depend on our ability to obtain financing in sufficient amounts. We regularly evaluate alternatives for managing our capital structure and liquidity profile in consideration of expected cash flows, growth and operating capital requirements and capital market conditions. Subject to market conditions we may, at any time, be considering or preparing for the purchase or sale of our debt securities, the sale of our common stock or a combination thereof.

Bank Credit Facility

In April 2021, our senior unsecured revolving credit facility was amended to increase its capacity to \$410 million with an uncommitted accordion feature that could increase the size of the facility to \$600 million, subject to certain conditions and availability of additional bank commitments. The facility also provides for the issuance of letters of credit with a sublimit equal to the greater of \$100 million and 50% of the revolving credit commitment. Borrowings under the revolving credit facility are subject to a borrowing base calculation based on the book value of our real estate assets and unrestricted cash. Letters of credit issued under the facility reduce the available borrowing capacity. The maturity date of the facility was extended to April 16, 2025. Borrowings and repayments under the facility were \$25 million each during the nine months ended June 30, 2021. At June 30, 2021, there were no borrowings outstanding and \$60.2 million of letters of credit issued under the revolving credit facility, resulting in available capacity of \$349.8 million.

The revolving credit facility includes customary affirmative and negative covenants, events of default and financial covenants. The financial covenants require a minimum level of tangible net worth, a minimum level of liquidity, and a maximum allowable leverage ratio. These covenants are measured as defined in the credit agreement governing the facility and are reported to the lenders quarterly. A failure to comply with these financial covenants could allow the lending banks to terminate the availability of funds under the revolving credit facility or cause any outstanding borrowings to become due and payable prior to maturity. At June 30, 2021, we were in compliance with all of the covenants, limitations and restrictions of our revolving credit facility.

Senior Notes

We have outstanding senior notes as described below that were issued pursuant to Rule 144A and Regulation S under the Securities Act of 1933, as amended. The notes represent senior unsecured obligations that rank equally in right of payment to all existing and future senior unsecured indebtedness and may be redeemed prior to maturity, subject to certain limitations and premiums defined in the respective indenture. The notes are guaranteed by each of our subsidiaries to the extent such subsidiaries guarantee our revolving credit facility.

In April 2021, we issued \$400 million principal amount of 3.85% senior notes that mature May 15, 2026 with interest payable semi-annually. On or after May 15, 2023, the notes may be redeemed at 101.925% of their principal amount plus any accrued and unpaid interest. In accordance with the indenture, the redemption price decreases annually thereafter and the notes can be redeemed at par on or after May 15, 2025 through maturity. The annual effective interest rate of the notes after giving effect to the amortization of financing costs is 4.1%. The net proceeds from this issuance were primarily used to redeem our \$350 million principal amount of 8.0% senior notes due April 15, 2024 on May 7, 2021. The redemption price of \$365.6 million included a call premium of \$14.0 million and accrued and unpaid interest of \$1.6 million. We recognized an \$18.1 million loss on extinguishment of debt upon the redemption of the notes.

Our \$300 million principal amount of 5.0% senior notes mature March 1, 2028 with interest payable semi-annually. On or after March 1, 2023, the notes may be redeemed at 102.5% of their principal amount plus any accrued and unpaid interest. In accordance with the indenture, the redemption price decreases annually thereafter and the notes can be redeemed at par on or after March 1, 2026 through maturity. The annual effective interest rate of the notes after giving effect to the amortization of financing costs is 5.2%.

The indentures governing the senior notes require that, upon the occurrence of both a change of control and a rating decline (each as defined in the respective indenture), we offer to purchase the notes at 101% of their principal amount. If we or our restricted subsidiaries dispose of assets, under certain circumstances, we will be required to either invest the net cash proceeds from such asset sales in our business within a specified period of time, repay certain senior secured debt or debt of our non-guarantor subsidiaries, or make an offer to purchase a principal amount of the notes equal to the excess net cash proceeds at a purchase price of 100% of their principal amount. The indentures contain covenants that, among other things, restrict our ability and the ability of our restricted subsidiaries to pay dividends or distributions, repurchase equity, prepay subordinated debt and make certain investments; incur additional debt or issue mandatorily redeemable equity; incur liens on assets; merge or consolidate with another company or sell or otherwise dispose of all or substantially all of our assets; enter into transactions with affiliates; and allow to exist certain restrictions on the ability of subsidiaries to pay dividends or make other payments. At June 30, 2021, we were in compliance with all of the limitations and restrictions associated with our senior note obligations.

Effective April 30, 2020, our Board of Directors authorized the repurchase of up to \$30 million of our debt securities. The authorization has no expiration date. All of the \$30 million authorization was remaining at June 30, 2021.

Other Note Payable

We also have a note payable of \$12.5 million that was issued as part of a transaction to acquire real estate for development. The note is non-recourse and is secured by the underlying real estate, accrues interest at 4.0% per annum and matures in October 2023.

Issuance of Common Stock

We have an effective shelf registration statement filed with the SEC in September 2018, registering \$500 million of equity securities, of which \$100 million was reserved for sales under our at-the-market equity offering program that became effective August 2020. During the three and nine months ended June 30, 2021, we issued 0.4 million and 1.4 million shares of common stock under our at-the-market equity offering program for proceeds of \$9.3 million and \$32.6 million, respectively, net of commissions and other issuance costs. At June 30, 2021, \$361.0 million remained available for issuance under the shelf registration statement, of which \$66.7 million is reserved for sales under our at-the-market equity offering program.

Contractual Obligations and Off-Balance Sheet Arrangements

In support of our residential lot development business, we issue letters of credit under our revolving credit facility and we have a surety bond program that provides financial assurance to beneficiaries related to the execution and performance of certain development obligations. At June 30, 2021, we had outstanding letters of credit of \$60.2 million under the revolving credit facility and surety bonds of \$436.6 million, issued by third parties to secure performance under various contracts. We expect that our performance obligations secured by these letters of credit and bonds will generally be completed in the ordinary course of business and in accordance with the applicable contractual terms. When we complete our performance obligations, the related letters of credit and bonds are generally released shortly thereafter, leaving us with no continuing obligations. We have no material third-party guarantees.

Operating Cash Flow Activities

In the nine months ended June 30, 2021, net cash used in operating activities was \$340.6 million compared to \$205.7 million in the nine months ended June 30, 2020. The cash used in operating activities in both periods was primarily due to the increase in real estate as we continue to grow our land development operations.

Investing Cash Flow Activities

In the nine months ended June 30, 2021, net cash provided by investing activities was \$1.7 million compared to \$3.1 million in the nine months ended June 30, 2020. The cash provided by investing activities in both periods was primarily the result of distributions received from our unconsolidated ventures.

Financing Cash Flow Activities

In the nine months ended June 30, 2021, net cash provided by financing activities was \$60.6 million compared to \$175.4 million in the nine months ended June 30, 2020. Cash provided by financing activities in the nine months ended June 30, 2021 was primarily the result of proceeds from the issuance of \$400 million principal amount of 3.85% senior notes and the issuance of common stock under our at-the-market equity offering program for net proceeds of \$32.6 million, which were partially offset by the redemption of our \$350 million principal amount of 8.0% senior notes and the related call premium of \$14.0 million. Net proceeds in the prior year period primarily consisted of the issuance of \$300 million principal amount of 5.0% senior notes, partially offset by the repayment of \$118.9 million principal amount of our 3.75% convertible senior notes at maturity.

Critical Accounting Policies and Estimates

There have been no significant changes in our critical accounting policies or estimates from those disclosed in our 2020 Annual Report on Form 10-K.

New and Pending Accounting Pronouncements

Please read **Note 1—Basis of Presentation** to the consolidated financial statements included in this Quarterly Report on Form 10-Q.

Forward-Looking Statements

This Quarterly Report on Form 10-Q and other materials we have filed or may file with the Securities and Exchange Commission contain “forward-looking statements” within the meaning of the federal securities laws. These forward-looking statements are identified by their use of terms and phrases such as “believe,” “anticipate,” “could,” “estimate,” “likely,” “intend,” “may,” “plan,” “expect,” and similar expressions, including references to assumptions. These statements reflect our current views with respect to future events and are subject to risks and uncertainties. We note that a variety of factors and uncertainties could cause our actual results to differ significantly from the results discussed in the forward-looking statements. Factors and uncertainties that might cause such differences include, but are not limited to:

- the effect of D.R. Horton's controlling level of ownership on us and the holders of our securities;
- our ability to realize the potential benefits of the strategic relationship with D.R. Horton;
- the effect of our strategic relationship with D.R. Horton on our ability to maintain relationships with our customers;
- the impact of COVID-19 on the economy and our business;
- the cyclical nature of the homebuilding and lot development industries and changes in economic, real estate and other conditions;
- competitive conditions in our industry;
- changes in our business strategy and our ability to achieve our strategic initiatives;
- continuing liabilities related to assets that have been sold;
- the impact of governmental policies, laws or regulations and actions or restrictions of regulatory agencies;
- the cost and availability of property suitable for residential lot development;
- general economic, market or business conditions where our real estate activities are concentrated;
- our dependence on relationships with national, regional and local homebuilders;
- our ability to obtain or the availability of surety bonds to secure our performance related to construction and development activities and the pricing of bonds;
- obtaining reimbursements and other payments from governmental districts and other agencies and timing of such payments;
- our ability to succeed in new markets;
- the conditions of the capital markets and our ability to raise capital to fund expected growth;
- our ability to manage and service our debt and comply with our debt covenants, restrictions and limitations;
- the volatility of the market price and trading volume of our common stock;
- our ability to hire and retain key personnel; and
- the strength of our information technology systems and the risk of cybersecurity breaches and our ability to satisfy privacy and data protection laws and regulations.

Other factors, including the risk factors described in Item 1A of our 2020 Annual Report on Form 10-K, may also cause actual results to differ materially from those projected by our forward-looking statements. New factors emerge from time to time and it is not possible for us to predict all such factors, nor can we assess the impact of any such factor on our business or the extent to which any factor, or combination of factors, may cause results to differ materially from those contained in any forward-looking statement.

Any forward-looking statement speaks only as of the date on which such statement is made, and, except as required by law, we expressly disclaim any obligation or undertaking to disseminate any updates or revisions to any forward-looking statement to reflect events or circumstances after the date on which such statement is made or to reflect the occurrence of unanticipated events.

Item 3. *Quantitative and Qualitative Disclosures About Market Risk*

Interest Rate Risk

We are subject to interest rate risk on our senior debt, revolving credit facility and our other note payable. We monitor our exposure to changes in interest rates and utilize both fixed and variable rate debt. For fixed rate debt, changes in interest rates generally affect the fair value of the debt instrument, but not our earnings or cash flows. Conversely, for variable rate debt, changes in interest rates generally do not impact the fair value of the debt instrument, but may affect our future earnings and cash flows. Except in very limited circumstances, we do not have an obligation to prepay fixed-rate debt prior to maturity and, as a result, interest rate risk and changes in fair value would not have a significant impact on our cash flows related to our fixed-rate debt until such time as we are required to refinance, repurchase or repay such debt.

At June 30, 2021, our fixed rate debt consisted of \$400 million principal amount of 3.85% senior notes due May 2026, \$300 million principal amount of 5.0% senior notes due March 2028 and \$12.5 million principal amount of 4.0% other note payable due October 2023. Our variable rate debt consists of the outstanding borrowings on our \$410 million senior unsecured revolving credit facility, of which there were none at June 30, 2021.

Foreign Currency Risk

We have no exposure to foreign currency fluctuations.

Commodity Price Risk

We have no significant exposure to commodity price fluctuations.

Item 4. *Controls and Procedures*

(a) Disclosure controls and procedures

Our management, with the participation of the Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act)), as of the end of the period covered by this report. Based on such evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of such period, our disclosure controls and procedures were effective in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by us in the reports that we file or submit under the Exchange Act and were effective in ensuring that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

(b) Changes in internal control over financial reporting

There have been no changes in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the quarter ended June 30, 2021 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II—OTHER INFORMATION

Item 1. *Legal Proceedings*

We are involved in various legal proceedings that arise from time to time in the ordinary course of our business. We believe we have established adequate reserves for any probable losses and that the outcome of any of the proceedings should not have a material adverse effect on our financial position or long-term results of operations or cash flows. It is possible, however, that charges related to these matters could be significant to our results of operations or cash flow in any single accounting period.

Item 6. *Exhibits*

Exhibit	Description
4.1	Indenture, dated as of April 21, 2021, by and among the Company, the subsidiary guarantors party thereto and U.S. Bank National Association, as trustee (incorporated by reference to Exhibit 4.1 of the Company's Current Report on Form 8-K filed with the Commission on April 21, 2021).
10.1	Amendment No. 2 to Credit Agreement, dated April 16, 2021 by and among the Company, JPMorgan Chase Bank, N.A., as administrative agent, and the Lenders named therein (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed with the Commission on April 20, 2021).
31.1*	Certification of Chief Executive Officer pursuant to Exchange Act rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Certification of Chief Financial Officer pursuant to Exchange Act rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1*	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2*	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS**	XBRL Instance Document - the instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document.
101.SCH**	Inline XBRL Taxonomy Extension Schema Document.
101.CAL**	Inline XBRL Taxonomy Extension Calculation Linkbase Document.
101.DEF**	Inline XBRL Taxonomy Extension Definition Linkbase Document.
101.LAB**	Inline XBRL Taxonomy Extension Label Linkbase Document.
101.PRE**	Inline XBRL Taxonomy Extension Presentation Linkbase Document.
104**	Cover Page Interactive Data File (embedded within the Inline XBRL document contained in Exhibit 101).

* Filed or furnished herewith.

** Submitted electronically herewith.

SIGNATURE

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.

FORESTAR GROUP INC.

Date: July 23, 2021

By: /s/ James D. Allen

James D. Allen, on behalf of Forestar Group Inc.
as Executive Vice President and Chief Financial Officer
(Principal Financial and Principal Accounting Officer)