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# FINAL TRANSCRIPT

Q4 2017 Realogy Holdings Corp Earnings Call

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## PRESENTATION

### Operator

Good morning, and welcome to the Realogy Holdings Corporation's full year 2017 earnings conference call via webcast. Today's call is being recorded, and a written transcript will be made available in the Investor Information section of the company's website later today. A webcast replay will also be made available on the company's website.

At this time I would like to turn the conference over to Realogy's Senior Vice President, Alicia Swift. Please go ahead, Alicia.

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### **Alicia Swift** *Realogy Holdings Corp. - SVP of Financial Planning & Analysis and IR*

Thank you, Jack. Good morning, and welcome to Realogy's full year 2017 earnings conference call. On the call with me today are Realogy's CEO and President, Ryan Schneider; and Chief Financial Officer, Tony Hull. As shown on Slide 3 of the presentation, the company will be making statements about its future results and other forward-looking statements during the call. These statements are based on the current expectations and the current economic environment.

Forward-looking statements and projections are inherently subject to significant economic, competitive and other uncertainties and contingencies, many of which are beyond the control of management. Actual results may differ materially from those expressed or implied in the forward-looking statements.

For those who listen to the rebroadcast of this presentation, we remind you that the remarks made herein are as of today February 27, and have not been updated subsequent to the initial earnings call. Important assumptions and other important factors that could cause actual results to differ materially from those in the forward-looking statements are specified in our earnings release issued today as well as in our annual and quarterly SEC filings. Also certain non-GAAP financial measures will be discussed in this call, and as per SEC rules, important information regarding these non-GAAP financial measures is included in earnings press release.

Now I will turn the call over to our CEO and President, Ryan Schneider.

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### **Ryan M. Schneider** *Realogy Holdings Corp. - CEO, President & Director*

Thank you, Alicia, and good morning, everyone. Thank you for joining us. So this is my first webcast as Realogy's CEO. Let me share a few thoughts before we discuss our 2017 results.

I'm excited to be at Realogy because I believe it has a combination of critical and unique advantages that make it well positioned to be successful in that attractive \$70 billion-plus U.S. residential real estate market.

First, Realogy has national scale and an industry leading market position, with 15.9% market share of transaction volume in 2017, up from



15.7% in 2016. Competitors are spending millions of dollars trying to replicate Realogy's national scale only to achieve a fraction of our market share. I love starting from a position of scale.

Second, Realogy has well-known and established brands, a competitive advantage versus having to spend substantially to build brands.

Third, Realogy has technology and data scale. We spend over \$200 million annually on technology. And Realogy has access to nearly all MLS data and a huge portfolio of historical data including robust information on millions of homesale transactions in which we have been involved. Realogy has the opportunity to better leverage technology and data to help our agents succeed, to develop new products, to drive growth and to operate more efficiently as a company in ways we believe our competition, who have neither the technology, scale nor the same data access cannot do.

Fourth, Realogy has a powerful financial engine. We have generated \$1.5 billion in free cash flow in the past 3 years, and our balance sheet is strong with little exposure to rising interest rates or near-term debt maturities and \$1.4 billion of revolver capacity. While residential real estate is an intensely competitive market, I am convinced the best place to compete is from Realogy's position of strength.

Success for Realogy and our shareholders, however, clearly requires better business results. Here is what you should expect to be different going forward. First is our speed of execution. Realogy will move faster. We quickly made leadership changes in both early January and February and we quickly recruited technology leadership from outside the industry. We have already executed restructuring and other cost-saving initiatives in early 2018, which we expect to create approximately \$50 million in annualized savings to make us more efficient and to create funding for additional agent, technology and strategic investments.

Second, we will be shifting our capital allocation away from M&A, which has been approximately \$300 million over the past 3 years, to increasingly focus on organic growth and on returning capital to shareholders through additional share buybacks. Our board has just authorized a \$350 million share buyback program. While we still look at acquisitions, you should expect a lower M&A run rate.

Third, we will be enhancing our value proposition for agents by producing new technology and data products. Our goal will be to quickly develop and test products in the market. You should expect to see us disclose our new product releases including beta products and for that to be an increasing part of our conversation of how we drive value for agents and for Realogy.

Fourth is our strategy around agent commission rate economics. You have seen our agent commission rates rise substantially over the past 15 months. While we are subject to competitive market forces, we will use a different approach to this issue in 2018 including providing new, great strategic clarity and the implications of our choices.

Let me talk more about 2018 with more detail on the agent commission point I just mentioned. From 2014 to late 2016, Realogy held agent commission rates mostly constant while losing 1 percentage point of market share from 16.7% to 15.7%. Starting in Q4 of '16, Realogy shifted growing market share at 15.9% last year but with substantially increased agent commission rates that you've seen in our numbers. 2017 rates are up 173 basis points year-over-year and Q4 2017 rates are up 204 basis points year-over-year. While we continue to face upward pressure on commission rates in 2018, we expect year-over-year rate increases will substantially moderate after Q1 of '18.

In the short term, however, the impact of this strategic approach will substantially affect our Q1 2018 results. We currently expect Q1 2018 operating EBITDA to be about half of Q1 2017 operating EBITDA which was \$61 million. 1/3 of the impact comes from rising agent commission rates and 1/3 comes from the lower closing volume in our new development business, which is a very long cycle times with inherently irregular project completion timing. Both of these factors will show in our Q1 year-over-year comparative commission rate figures.

As you know, our Q1 outlook is not often indicative of our full year outlook. I wish I could give you a certain forecast for the full year, but macroeconomic factors and housing market uncertainty make that hard to do this early in the year. That said, it would be a mistake to extrapolate our full year 2018 results from Q1 2018 for the following reasons: The headwinds of significant rise in agent commission rates in Q1 will substantially moderate over the rest of 2018. While there will still be upward pressure on agent commission rates, we expect the

magnitude to be less than you've seen the last 2 quarters and you'll see in Q1 2018; the negative impact from the new development business in Q1 will also exist in Q2 at about the same magnitude but will then have less effect in Q3 and Q4; we expect to benefit increasingly over 2018 from continued organic growth through recruiting success, realization of already planned and executed operating efficiencies and improving agent productivity from new data and technology products over time; and as you know, from prior years Q1 is by far, our smallest quarter.

So pulling up, Q1 2018 should not be used to extrapolate full year 2018 results. Based on what we know today, and subject to macro uncertainty, we expect our operating EBITDA for the balance of the year following Q1, to be in line or better than the same period last year. We believe our overall trajectory for the remainder of 2018 (sic) will be positive as the Q1 headwinds moderate and we build momentum into 2019 and beyond.

While I'll come back at the end of the call to summarize my thoughts, now let me turn over to Tony to discuss our full year 2017 results.

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**Anthony E. Hull** *Realogy Holdings Corp. - Executive VP, CFO & Treasurer*

Thank you, Ryan. Turning to Slide 5 for the full year 2017 results, revenue of \$6.1 billion was up 5% compared to full year 2016. This growth was directly attributable to the combined increase in homesale transaction volume in NRT and RFG. Our operating EBITDA of \$732 million was down modestly by approximately 5%. This was due to higher commission rates and reduced earnings at Cartus along with hurricane impacts, litigation settlement and CEO transition charges, partially offset by the revenue increases. Free cash flow grew by 23% to \$559 million. Net income increased to \$431 million.

The 2017 Tax Cuts and Jobs Act is of significant benefit to Realogy. Our 2017 earnings reflect a onetime increase of \$216 million, mostly from our reduced deferred tax liability resulting from the change in the U.S. corporate tax rate. The economic benefit of our estimated effective tax rate going from 41% to 29% is dramatic when we look to becoming a cash taxpayer in 2020. The new tax rate would reduce our cash taxes by approximately \$50 million per year at our current earnings level, and have even greater impact as our earnings increase.

Adjusted net income per share was \$1.59 compared to \$1.64 in 2016. At year-end our NOL was \$1 billion which we expect to allow us to continue to pay minimal cash taxes through 2019.

Turning to Slide 6 for a discussion of the full year drivers of our business. Our overall homesale transaction volume growth was 7% year-over-year. RFG's transaction volume increased by 7% with a 1% increase in size and a 6% increase in average sales price. NRT finished the year up 8% in transaction volume with a 3% increase in size and 5% growth in average sales price.

Slide 7 provides information about our business unit operating performance in 2017. At RFG, revenue increased 6%. The growth was mainly from higher net domestic affiliate royalties and increased royalties from NRT. RFG's operating EBITDA increased \$40 million against the \$46 million or \$47 million revenue increase principally due to higher revenues. NRT revenue increased 7% or \$299 million in 2017 due to its transaction volume increase driven by both higher average sales price in our recruiting and organic growth of focus. NRT operating EBITDA decreased \$24 million to \$135 million as greater revenue was more than offset by \$285 million of increased agent commission expense of which \$79 million was due to higher commission rates and \$44 million was due to acquisitions as well as \$70 million of higher royalties paid to RFG and increases in other operating expenses. The wind down of our PHH mortgage joint venture was also contributed about \$12 million of incremental EBITDA last year.

If you look at NRT and RFG in the aggregate, their combined revenue increase 7% and operating EBITDA excluding the impact of PHH JV, improved by \$2 million in the year, rebuilding market share. As we continued to grow NRT's revenue through recruiting and agent productivity, we expect to see the combined results to deliver improved EBITDA growth for the company as a whole. Although much of the progress will be apparent in that RFG segment results in the near term.

Cartus revenue decreased \$23 million in 2017 primarily due to lower international revenue and reduced fees per move. Operating EBITDA decreased \$15 million as a result of lower revenue partially offset by an \$8 million reduction employee-related costs. Cartus also affected targeted cost reductions in the first quarter of 2018, which were aligned with the broader company-wide business optimization efforts mentioned earlier.

TRG's revenue increased \$3 million and operating million dollars decreased a \$4 million year-over-year. The revenue decrease was impacted by a 44% decline in refinance activity partially offset by higher resale revenue. Operating EBITDA also includes a \$5 million decrease in earnings from costs related to our share of a start-up of operations of our mortgage joint venture Guaranteed Rate Affinity.

Corporate expenses before restructuring legacy and extinguishment of debt in 2017 was \$35 million greater than 2016 due to higher expenses relating to investments in technology development, professional fees, supporting strategic initiatives as well as an \$8 million legal settlement and an \$8 million in CEO transition costs.

Now I'd like to make some broader comments. First the company generated \$559 million of free cash flow in 2017, which represents a 76% conversion of operating EBITDA to free cash flow. More importantly this is how we allocated that free cash flow. As part of our capital management strategy, we use the majority to repurchase shares and to reduce debt. Specifically because of our strong cash flow, the company was able to return \$325 million of capital to shareholders through share repurchases and dividends in 2017.

Our 2017 free cash flow benefited from the wind down of the PHH joint venture and other favorable working capital movements that we don't expect to be prevalent in 2018. This year, we would expect to see conversion from operating EBITDA to free cash flow closer to the 2015 rate of approximately 60%. We have a strong balance sheet. Our debt has decreased from \$3.9 billion at the end of 2013 to \$3.3 billion at the end of 2017, and our weighted average interest rate declined by approximately 200 basis points due to our constant efforts to strengthen our balance sheet.

In the beginning of February, we completed the refinancing of our term loan facilities including the extension of their maturities to 2023 and 2025, and also increased our revolver capacity to \$1.4 billion. The extension of maturities has furthered execution of our capital structure strategy of creating a staggered maturity profile on our debt.

Ryan discussed the EBITDA outlook for the first quarter. Looking at our expectation for transaction volume in the period, we forecast that Realogy's combined homesale transaction volume will increase in the range of 2% to 5% year-over-year with sides contributing between flat and up 2%, and 2% to 3% growth coming from price. Broken down by business unit we expect 4% to 6% transaction volume growth at RFG and flat to 2% growth at NRT in the first quarter.

Although we've yet to enter the prime period for housing activity this year, many forecasters are calling for existing homesale transaction volume to grow between 3% and 8% in 2018. While we are optimistic on our prospects for 2018, there are both opportunities and challenges for the year ahead, which are evident in the wideband of forecast for the year.

The 3 macro factors being faced by the industry are the impact of the 2017 Tax Act on consumers, rising mortgage rates and suppressed inventory levels. These could be positive influences or challenges to the housing market in 2018 and beyond but are difficult to predict at this point. Regardless, the current housing environment wherein the mainstream market demand for existing homesales far outstrips supply and home purchase affordability remains at elevated level is a constructive backdrop against which to evaluate these factors on consumer behavior.

In addition there was a net gain of 1.4 million U.S. households formed in 2017, which was entirely attributable to home purchases not rentals. This marks a huge change from what we saw from 2008 to 2016 and as an encouraging trend. Longer term we expect that the industry will benefit from positive demographic trends as millennials improved their current homeownership rate of 36% toward parity with the overall 64% U.S. homeownership rate.

While we cannot control the macro environment, we believe there is positive momentum related to the drivers we do control such as improvement in profitable market share and enhanced agent value proposition and cost containment, and those are among the many reasons why we're optimistic about the coming years.

Now, let me turn it over to Ryan for some closing remarks.

**Ryan M. Schneider *Realogy Holdings Corp. - CEO, President & Director***

Thank you, Tony. Pulling way up, so after 2 months in this role, I am working this than ever that the best place to compete is from Realogy's positions of strength. A few market observations to share with you from these early days. First, I am actually really excited by how much to agent remains at a center of the homebuying process across our industry. I'm encouraged by how little [traction] disruptors have gotten by attacking the average broker commission rate over the years. I am surprised by how much competitors are spending, both overall and individual offers to agents, to capture a pretty small share of the market. And potentially most importantly I am excited about the demographic trends Tony spoke about in favor of strong housing market over the longer term.

As I said in my opening remarks, Realogy is well positioned to succeed with its industry-leading national market position, great brands and technology and data scale. Our powerful financial engine generates significant free cash flow, the balance sheet is strong and we are returning substantial capital to shareholders. We do expect Q1 2018 will be challenging, likely delivering half of Q1 2017 operating EBITDA, and our view is that Q1 2018 should not be used to extrapolate full year 2018 financial results.

As I said earlier based on what we know today and subject to macro uncertainty, we expect our operating EBITDA for the balance of the year after Q1 to be in line with or better than that same period last year. We believe our overall trajectory for the remainder of 2018 will be positive as the Q1 headwinds moderate and we build momentum into 2019 and beyond.

Finally, let me hang out our shingle on what would be different. You will see us strive to execute more quickly, return more capital to shareholders, make agents more successful by improving our value proposition through technology and data products, and provide you greater clarity about our agent commission rate strategy. Success requires that we deliver better business results, and we are moving rapidly to drive change.

With that, we will open the phone lines for Q&A.

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## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions) Your first question comes from the line of Kevin McVeigh with Deutsche Bank.

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### **Kevin Damien McVeigh *Deutsche Bank AG, Research Division - Head of Business and Information Services Company Research***

Welcome aboard, Ryan. Can you just help us get a better sense of kind of the strategic clarity on the commissions. And how that kind of spans the enterprise from kind of your top-quartile agents all the way down. And as you leverage technology more or less how we get those rates as they start to come down over the balance of '18.

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### **Ryan M. Schneider *Realogy Holdings Corp. - CEO, President & Director***

Yes. It's a great question, Kevin. Let me step back a little bit and just talk about it. So as I said on the call, Kevin, our average commission rates are up about 173 basis points in '17 on a year-over-year basis. And average commission rates are up about 204 basis points for Q4 '17 also on a year-over-year basis. And you saw, reasonably, similar large increases in a few of the earlier quarters in 2017. And as I said in the call, you're going to see another kind of similar year-over-year increase in Q1 '18, all from the kind of strategic shift I highlighted at the end of '16.

But I did tell you that I expect the year-over-year increases to substantially moderate in 2018 after Q1. And here is why I believe that and then to get to the strategic answer to your question, Kevin. So first off, looking back on it. 2017 was obviously, in some ways, kind of a reset year on Realogy's price out there with agents and commissions. And while the increases were substantial, the other data that we have actually implies to me that the reset actually work. So for example, in our top 2 quartile of agents, we are at an all-time high of retention rate. We're retaining about 95% of our agents in our top 2 quartiles after kind of doing the reset that has led to the commission rate increases that you're seeing, versus the scenario in kind of '14 through part of '16 where we're actually losing agents at a much higher rates among that kind of top 2 quartile demographic, which is the most important one.





And second thing is we have a lot of success with recruiting in this new environment with the kind of how your agent commission rates, and we grew agent count at NRT by about 2,700 agents. So I look at that data, Kevin, and think, okay, this -- we kind of caught up to the market. We are still subject to market forces on however our commission rate works, but we kind of caught up and we kind of reset our price effectively.

So what do we do from here going forward? Well, the first answer is we don't just let inertia kind of carry us or let the market forces kind of carry us. I think there is 3 things that we actually start doing differently. So the first is we need to keep enhancing our value proposition to agents pretty substantially. We've got a real opportunity both with the assets we have and with some of the things that we haven't delivered to agents yet, to actually use whether it's technology products or data projects -- products, excuse me, to better support agents out there. And whether it's making agents more efficient helping them prioritize their time, helping them focus on the highest priority leads. We actually have the technology and data to enable that for our agents.

We can also, by the way, provide them more high quality leads even then we are today that I don't think anybody else in the industry can replicate when you think about our affiliate network and some other unique things that we have. And if we can keep adding to read value proposition, Kevin, both on the tech and data side, the lead side, et cetera, that will give us the ability to kind of give more value to the agents and actually get a better price for that, which translates to -- in a lower commission rates over time hopefully.

The second thing we can do differently is take a much more data-driven approach to how we do commissions with our agents. If you think about our agent population, we have 50,000 agents in our own brokerage area, 50,000-plus. Each of them is unique. Each has their own set of data, they are in different markets, they have different place in their clear direct -- trajectory, they're having different results each year, they have different commission dynamics and there is a massive set of data there that we can actually -- we can and should be doing more with to effectively leverage our scale and make more targeted "pricing decisions" and almost go to kind of much greater price segmentation in that population, and we think there's some real opportunity there that we have yet to explore.

And then third what will be different going forward is the management team has spoken to you before about some targeted recruiting that we've done over the last kind of 15 months, and I think it's been very successful, and you can see the agents growth that I described earlier. But we've, in the last kind of couple of months, been looking at the data in a different way and we actually think we can change how we do our targeted recruiting profile in a way that will help us on the agents split dynamics while still giving us the kind of GCI and agent growth that we're trying to get there. And so those are 3 different things that we can be and are going to be doing differently that will hopefully change our dynamic around this now that we've kind of done our market reset.

And again while still subject to competitive market forces here, we're not just going to let those forces carry us wherever they take us, we are going to use these kind of things plus other things we have in the hopper that aren't ready for prime time yet to actually take a different strategic approach to this part of the market.

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**Kevin Damien McVeigh Deutsche Bank AG, Research Division - Head of Business and Information Services Company Research**

That's super helpful. And then just one quick follow-up and again very helpful. The \$50 million in cost savings, do we get that all in '18? Or is that partially '18 and then somewhere into '19? And is there any sense on how that comes in over the course of the year?

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**Anthony E. Hull Realogy Holdings Corp. - Executive VP, CFO & Treasurer**

Many of the actions have been taken already so we should get the bulk of it during the year. But I think we'll see it more prominently I think in the second, third, fourth quarter, I guess if I have to guess. But I think we'll get the full \$50 million for the year.

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**Ryan M. Schneider Realogy Holdings Corp. - CEO, President & Director**

Yes. The important thing for me there, Kevin, is we move very quickly, we took the action, literally, in the first kind of 6 weeks of the year with a goal to get as much as we can in '18. I totally agree with Tony's answer, but I wanted you to focus on the pace as much as the numbers itself.

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**Operator**

Your next question comes from the line of Bose George with KBW.

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**Bose Thomas George Keefe, Bruyette, & Woods, Inc., Research Division - MD**

I just wanted to clarify on the split. So going into 2018, are the splits stabled and is just the increase really just reflecting what you've done towards year-end and that's kind of rolling over year-over-year? Or are you still expected some increases over the course of '18.

**Ryan M. Schneider Realogy Holdings Corp. - CEO, President & Director**

So as I said in my remarks, you're going to see a large year-over-year increase in Q1 when you look at the Q1 quarter numbers. It will be consistent with the what you've seen in the last couple of quarters, and so you're going to see that. There will still be upward pressure after that, so it's not like it's going to start going down or anything but that upward pressure will bluntly -- as the words I chose were substantially moderate. And there's always uncertainty because of the market forces, and this is kind of a hard business to forecast in the longer term. But you should expect a large increase in Q1 in split rates year-over-year and then substantial moderation from there.

**Bose Thomas George Keefe, Bruyette, & Woods, Inc., Research Division - MD**

Okay, great. And then actually just in terms of the competitive landscape, can you sort of characterize that is it being driven by multiple competitors, feuds? Just any color there would be great.

**Ryan M. Schneider Realogy Holdings Corp. - CEO, President & Director**

Look, I think the -- look, this is an intensely competitive business and there is no 1 competitor who is driving the intense competition, really it's everybody. It's an incredibly intense market. And whether you're talking about the big name kind of regional and national brokers or hyper-local brokers and only kind of 1 city, the competitive intensity is across the board and it comes from all of them.

People often ask us, "where do we lose our most agents to?" and the answer is, actually, we lose most of our agents when they leave to other, which is often those small kind of hyper local ones. That category is incredibly competitive part of the market. But I would say it's equal across all parts of the market and geographies.

**Bose Thomas George Keefe, Bruyette, & Woods, Inc., Research Division - MD**

Okay. And then just one more from me. The change in focus in terms of capital return over M&A, how much of that is sort of what's out there in the market versus an internal decision to sort of change the focus?

**Ryan M. Schneider Realogy Holdings Corp. - CEO, President & Director**

Look, these things are always a mix. And like I said, we'll still look at things but I do expect the run rate to be lower. I mean I think if I step back, we got a national scale position, we don't need acquisitions to kind of enter markets or bolster our share in a lot of the markets around the U.S. and so we got that kind of going for us.

Second, we're seeing that the returns, we think, are going to be better for us on the organic growth side with recruiting for, example, as opposed to acquisitions in some of that because some of the pricing we see out there in the market is a lot higher than it's been in the past when we get a sense of what the multiples of things are trading at compared to what they used to trade at. We like the old multiples a lot better than the current ones. So this is all on evolution but I would say while most are look at things you should expect that we focus more on the organic growth side, and we think that's the way to actually best use our capital along with returning it to shareholders.

**Operator**

Your next question comes from the line of Anthony Paolone with JPMorgan.

**Anthony Paolone JP Morgan Chase & Co, Research Division - Senior Analyst**

Can you give us a sense as to the \$200 million in technology spending whether you think that's enough, too little, just right or what's happening on that front? can you spend a lot of time talking about that as being the core to some of your initiatives?

**Ryan M. Schneider Realogy Holdings Corp. - CEO, President & Director**

Yes. So Realogy as I understand it, if I got that history right, disclosed the \$200 million technology spending at our Investor Day last year. And my view is that's an awesome asset for the company in the sense that it truly shows that technology scale that the place has and the potential it has. I personally think that will be enough. But as you probably expect, I think there'll be 2 different changes that'll happen. One



is where we spend that in the future is likely to be different than in the past both given how the world is changing and some of the strategic priorities I'm laying out. And so I think there will be opportunities for us to reallocate some of that money.

And then second as I mentioned when I talked about our cost reduction, I do think one trend happening in companies across America is how do you find ways to reduce costs in other parts of your business so you can invest more in technology. And so I think if there are incremental technology dollars that will come from us being more efficient in other places, I don't think we'll be taking just our free cash flow and diverting it to more technology spend in and of itself. I think it will be a reallocation of what we spent today with occasionally some efficiency plays to try to find more money to reinvest for the long term.

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**Anthony Paolone JP Morgan Chase & Co, Research Division - Senior Analyst**

Okay and then my second question is you spent some time talking about Realogy's positioning and being excited about that. Can you maybe give us a sense as you get into the real estate business here and what your initial views are on things like any other emerging technologies you see out there as being interesting, things like the commission rates on selling homes and where that goes over time? How teams of agents have become more robust some of those hot buttons are on the industry and where you think those might go over several years?

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**Ryan M. Schneider Realogy Holdings Corp. - CEO, President & Director**

That's both -- that could be a whole call by itself, and it also is part of the subject to some of the strategy work that we've kicked off and that we are working on here in the near term. Look, let me just say I think this is a phenomenally exciting industry. I do think it is an industry as a whole that has more opportunity for technology change than both the industry I came from financial services, which I think is further along in the technology change as well as some others. And so I think a lot of the trends that you see other industries go through on the technology side, there are still a lot of opportunities for the real estate industry to go through those. I think that's where a lot of my focus is going to be and my excitement. And so I've probably spent disproportionate time thinking about that and how we can change. As part of our goal is to be one of the players in the industry that leads that journey because we have the scale to do it. And if we do it, we have just tens of thousands and hundreds of thousands of agents in our franchise business, in our own brokerage business that can benefit from those things when we do it.

So of all the things you said that's the place I've been spending most of my strategic time thinking. While I have thoughts on the others, I think I should either defer those to a time when we have a longer time period one-on-one or another invent kind of presentation forum.

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**Operator**

Your next question comes from the line of Ryan McKeveny with Zelman & Associates.

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**Ryan McKeveny Zelman & Associates LLC - VP of Research**

On the tech and data focus side of things, as it relates to the brokerage industries, you have Zap on the franchise side and obviously, kind of more control over the NRT piece of the business. So any additional color on just kind of the initial emphasis around tech and data? And where that might show up in the brokerage segments of the business?

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**Ryan M. Schneider Realogy Holdings Corp. - CEO, President & Director**

Yes, thanks for your question, Ryan. Today, in our owner brokerage area, we support both a number of products and we deliver directly to our own brokerages, but we also use and enable a lot of third-party products and part of that is because we need to meet the agent wherever they are, and make sure they got what they need to be successful because we're only going to be successful if they're successful.

And so I don't think our future is necessarily going to be different than that, e.g. it's not going to be a Realogy-only technology solutions get provided. What I think we are going to have to do is make sure we are incredibly easy for agents to both use our technology, not just what we have today but new things that we develop to help make them successful, but also we're going to have an open environment where it's incredibly easy to plug in any of the third-party products that an agent wants to use. And that's really kind of that standard journey from building kind of close software to using APIs to build much more open and easily integratable software and things like that. That's an example of place where I think the industry hasn't done as much as some other industries and I think Realogy has room to change in that dimension. And so that's likely what we're going to be doing from a kind of a strategic standpoint in that dimension.

And then we've got to take on where can we build great products whether they're technology products are data products that we can then deliver to our agents and our franchisees are going to help them be successful. Those could spend a lot of different parts of the value chain. They don't have to be delivered in a massive, integrated system many can be delivered on kind of an individual basis and, again, just kind of plugged into the agents ecosystem. We got some of those started but we'll wait to talk about them when they actually hit the market.

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**Anthony E. Hull** *Realogy Holdings Corp. - Executive VP, CFO & Treasurer*

Ryan, the one thing I would just supplement to Ryan's answer with, because I think you raised a really good point in your question, which is it's one thing to do it with your own brokerage and really influence the agents' productivity and it's a whole another challenge when you're going through a franchise network to, a, get the franchisees to change and then affect that change with their agents. So I think that's something our competitors sort of do out there is, "We'll just do this, that and the other thing and it'll magically happen." It's not easy and we have like a 3-year head start on anybody on doing that through our Zap rollout, and we have so many learnings from that, that I just think we are just much better prepared to when you sort of -- when you're -- we're effectively a third party trying to influence our franchisees and then their agents, I think we're much better at that now than any of our competitors. So we have a lot of experience in that area.

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**Ryan McKeveny Zelman & Associates LLC - VP of Research**

That's really helpful. And one on the commission splits. So is the way to think about that in the sense of the recruiting effort that have been happening, is it that we should maybe be a step back in terms of some of the things like recruitment bonuses, and some of those 2- or 3-year agreements? Or is it kind of what you mentioned the shift in the recruiting where if I read kind of between the lines may be instead of going after for instance one super high producing agent that's extremely high split, maybe you get that same volume by recruiting 2 agents that are slightly lower volume but in aggregate the same and a lower average split? So any additional color on kind of how that trends to get the moderation and the splits going forward?

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**Ryan M. Schneider** *Realogy Holdings Corp. - CEO, President & Director*

Yes, Ryan, I don't want to say too much on that one partly just for competitive reasons, but your latter answer is closer to kind of what our thinking is likely to be in the future on that one. And I'll just leave it at that.

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**Operator**

Your next question comes from the line of Will Randow with Citigroup.

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**Will Randow** *Citigroup Inc, Research Division - Director*

I guess that the increased focus on capital returns, is that tied to your stock price, richness of M&A multiples? And while I definitely agree with a greater focus on returning capital to shareholders, looking forward, can you walk us through how you got to that thought process? And any underpinning precedent you might have or analytics?

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**Anthony E. Hull** *Realogy Holdings Corp. - Executive VP, CFO & Treasurer*

I think it's a combination of the 2, Will. Clearly, we believe and the board believes that our stock is significantly undervalued. So we can buy our stock at a much lower multiple than we can do acquisitions at in the current environment, so -- and without the risk attendant to doing acquisitions, so not to cause to disruptions and other things. So we just think it's the best -- it's the most accretive use of our capital if you compare it to M&A or even debt retirement and repurchasing shares is the best allocation right now.

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**Will Randow** *Citigroup Inc, Research Division - Director*

Understood. And Ryan, you compared real estate services to financial services, and I agree there is definitely room for efficiency gains. But I mean the one issue you're dealing with in the financial services is commissions overall have compressed. Can you talk us through that thought process. And if you believe that precedent is going to look like we're going to see in real estate services over the next 10 years.

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**Ryan M. Schneider** *Realogy Holdings Corp. - CEO, President & Director*

Yes. So, Will, thanks for the question. That was actually not the analogy I was trying to draw partly because my financial services background is more in the direct-to-consumer and some business-to-business credit card kind of stuff, not working with anything in kind of the brokerage or financial advisor side of the financial services. So I was not trying to draw that analogy at all, so please don't assume that, that was what I was thinking.



The analogy I was trying to draw was on the pace of utilization of new technologies and then the delivery of those to create great experiences, whether it's for agents or customers. And that I thought financial services may be a bit ahead of the real estate industry is one of my observations joining here, which is really exciting because then that means there's opportunity especially for a company with Realogy's scale and kind of throw weight in the technology and data area. So that was the analogy I was trying to draw. I was not at all trying to draw competitive analogy around commissions.

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**Anthony E. Hull** *Realogy Holdings Corp. - Executive VP, CFO & Treasurer*

And I would just add to that, that commission rates have remained very stable. They remained to be stable in 2017 on an industry-wide basis not just Realogy. So it requires speculation to think that's going to change in the future, and we don't like to speculate. And there's really no evidence of that.

In fact, our competitors who offer -- some more competitors who offer kind of teaser rates to build market share aren't getting any -- don't seem to be getting any traction on that. So I think it's really -- at the end of the day, it's the value provided by our great agents that justifies and maintains the pricing that they charge consumers. So we don't see any change to that. And as time goes on, we think the value of the agent grows and grows given just the complexity of the real estate transaction.

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**Operator**

Your next question comes from the line of David Ridley-Lane with Bank of America.

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**David Emerson Ridley-Lane** *BofA Merrill Lynch, Research Division - VP*

Sure. I'm wondering if you've seen any early signs of the impact of tax reform particularly in the higher state and local tax areas. I know you're over indexed in NRT to those areas, do you think there would be or have you seen signs of pressure on pricing or potentially sides.

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**Anthony E. Hull** *Realogy Holdings Corp. - Executive VP, CFO & Treasurer*

Hey, David, thanks for the question. So one thing I want to reiterate is that the change in the tax law is very beneficial to Realogy as I pointed in my prepared remarks. And just overall in the first 2 months of the year, I guess for 7 weeks of the year, we have not seen anything in our opens that would indicate it's having an impact. So, so far, it's really early. So it's too early to make any adjustments, but so far we don't see any impact from it.

But it's difficult to predict the impact of the new tax provisions and what impact it'll have on homesale transactions or home prices. Everyone looks at the negatives, potential negatives but they forget to look at the positives. And on the positive side, individual tax rates are now lower for most families and individuals. They have more take-home pay available, and we think customers will have greater funds to put towards the home purchase down payment, so those are the positives.

On the unknown side, it's the impact of caps on deductions on a sliver of mortgage principal and on property taxes and what impact that will have on transactions. If nothing else along with higher standard deductions, these could reduce the financial incentives to own a home but we don't believe this is a major driver for families to become or remain homeowners.

Since you brought it up as it relates to caps on state and local tax deduction, caps on state and local taxes, it's complicated by a number of factors. First and foremost the provision impacts all families living in high tax states, renters and homeowners alike, so it's not a thing that affects our business. It affects all families that live in high-tax states.

So I guess a family would have to uproot themselves from their jobs, their schools, their community to move to a lower tax rate in order to avoid that increase. We view that change as resulting -- the change in the tax law in state and local side to result in a trickle of activity rather than anything on the grand scale. And then the other thing that folks need to consider when they're thinking about this is alternative minimum taxes. Those were already in place under the old tax law and they were already capping a number -- for a number of families property tax deductions and tax -- state tax deductions. So if that doesn't change materially, preimpose the tax law, it lessens the impact of this cap on state and local tax deduction. So anyway it's early to tell we haven't seen anything yet but we think we'll keep watching it carefully.



**David Emerson Ridley-Lane** *BofA Merrill Lynch, Research Division - VP*

Great and then just click will follow up. On the NRT recruiting, I think in 2016, your recruited agents that had \$212 million in gross commission income. Do you have the comparable period for where you ended the year in 2017?

**Anthony E. Hull** *Realogy Holdings Corp. - Executive VP, CFO & Treasurer*

I think the total recruiting we've done is about just over \$400 million of revenue over the last 15 months.

**David Emerson Ridley-Lane** *BofA Merrill Lynch, Research Division - VP*

And those agents will become productive over the last 12 to 18 months, something in that time line?

**Anthony E. Hull** *Realogy Holdings Corp. - Executive VP, CFO & Treasurer*

We'd expect them to become productive as soon as they begin with us within -- it probably takes probably 3 months or so to get up and running. But we're definitely seeing in our results the positive impact of the recruiting we did last year and the recruiting we're doing currently.

**Operator**

Your next question comes from the line of John Campbell with Stephens.

**John Robert Campbell** *Stephens Inc., Research Division - VP and Research Analyst*

First, this is a two-part question. Ryan, back to the \$50 million cost saves. I guess first, it sounds like you've already taken a lot of actions you needed through the first 6 weeks of the year. But can you walk back through what you did and kind of where those savings came from?

And then secondly just curious, \$50 million is that a net expense run rate reduction? Or are you investing some of that back in the business and back to technology.

**Ryan M. Schneider** *Realogy Holdings Corp. - CEO, President & Director*

Yes. So let me start on the second thing and I tried to say this in the remarks. So 2 goals here, one is be more efficient; second goal is create some funds to kind of reinvest in technology in our agents and strategy initiatives. So it's a mix of those 2 things is the purpose. We move pretty -- try to move pretty quickly for the \$50 million, so we could capture as much of it within 2018. It really it hit every part of the company. The big 3 buckets were people reductions, real estate, primarily office closings for example, and then some things with different vendors and procurement. Those were the 3 big buckets. There's a reasonable tail of smaller things that's just not worth going into, but those are the 3 big things that I have you focused on.

**John Robert Campbell** *Stephens Inc., Research Division - VP and Research Analyst*

Okay. That's helpful and then as a follow-up to that maybe this is for Tony, but out of NRT cost, any idea how much of that is kind of location or facility costs? And then maybe if you could provide kind of what percent occupancy? Or what type of saturation you have across your NRT office footprint today?

**Anthony E. Hull** *Realogy Holdings Corp. - Executive VP, CFO & Treasurer*

Saturation in terms of utilization of the office space? Or saturation...

**John Robert Campbell** *Stephens Inc., Research Division - VP and Research Analyst*

That's right.

**Anthony E. Hull** *Realogy Holdings Corp. - Executive VP, CFO & Treasurer*

I don't think it's change materially. It's probably up 1 point or 2 but it's 65% capacity utilization. So I think it's -- obviously, with adding agents last year, that improved because we didn't have offices. So that's an area longer term not -- I don't think we'll see it short term, but longer term that's a source of operating leverage. But if we can place more agents in our current footprint, then obviously, is beneficial.

**Operator**

Our next question comes from the line of Jason Deleeuw with Piper Jaffray.

**Jason Scott Deleeuw Piper Jaffray Companies, Research Division - VP & Senior Research Analyst**

Just wondering on the market share trends that we should expect given the strategic shift with the agent recruitment and the commission splits, the guidance for the first quarter, NRT guidance volume looked a little soft. And so I'm just wondering what we should be expecting market share trends? Or is there just more of an overall industry market impact in terms of kind of the first quarter guidance.

**Anthony E. Hull Realogy Holdings Corp. - Executive VP, CFO & Treasurer**

Well, being much longer term than first quarter, I would say that we want to air on the side of gaining market share given the incredible demographics so they're coming down the line that are known. So we don't want air on the side of the more market share rather than less. And in terms of the NRT numbers in the first quarter, Ryan referenced some new development headwinds in the first quarter. And that's taking NRT's volume in the first quarter because it's such a small quarter, and the new developments are pretty high average sales price. It's about 3% offset to NRT. So without that headwind NRT, it would up 5% for the -- in the first quarter, so it's really that new development in which again, Jason, is very episodic and it really depends on when the projects are closing and we had a number close in '16, a good number close in '17, we have a great pipeline that'll start close within '19, so it's just a pause in '18.

**Jason Scott Deleeuw Piper Jaffray Companies, Research Division - VP & Senior Research Analyst**

Good. And then just other question is on the technology investments and thinking about agent recruitment and retention, I mean how important is technology for recruitment and retention, is it becoming more important? And is the technology going to be -- is it more important on the lead generation site? Or is it more on kind of managing the relationship in the transaction process?

**Ryan M. Schneider Realogy Holdings Corp. - CEO, President & Director**

So my view after a couple of months is it's amazingly important and it's only going to become more important both as kind of the world changes on technology but also as that, plus the data side of it that we have access to can be an increasing key to make people more successful. I think both technology and leads are important. I mean anything we can do to help an agent close one more deal a year, I think is incredibly powerful both the loyalty to us, the economics to us et cetera. And you can see past helping agents make that happen both through higher quality leads that only we can provide. You can also see past that's happening to technology and data products and hopefully with our scale. We are more uniquely also position to provide. So I think both are going to be I think the overall topics are incredibly important in the future even more than in the past, and both pasts that you laid out can and should be part of how we improve our value and keep enhancing our value proposition to our agents.

**Operator**

The last question comes from the line of Mike Dahl with Barclays.

**Michael Glaser Dahl Barclays Bank PLC, Research Division - Research Analyst**

I wanted to focus -- two-part question, just around some of the comments on the guide. So first part is if I think about the 1Q guide, and on the comments of balance of the year in line with or better, simple math is that's around \$700 million for the full year. And so I guess, a, is that really the ballpark that you want us all to be thinking about? And then, b, hoping you could give us a bit more of a bridge to get there because I understand and appreciate the comments around split rates starting to moderate a bit, but if I look at that number including the restructuring benefits as well, it seems to me that it still implies split rates for the year are up north of 100 bps. So any other puts and takes we should be thinking about in the balance of the year comments?

**Anthony E. Hull Realogy Holdings Corp. - Executive VP, CFO & Treasurer**

A couple of things. We said that we think the balance of the year will be equal to or greater than, and the reason was said that was because -- so you took that equal to as opposed to the greater-than approach. So the reason we say that is because it's early in the year in terms of what the spring selling season is going to be like and you have that wide range of forecast for the year of 3% to 8%, for the total volume. So I think that's one thing.



And yes, we said that the split increase are going to moderate, but we could to get expect them to be up year-over-year and it's kind of early to give you sort of a range on that but we still think it'll be a headwind for 2018 overall.

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**Michael Glaser Dahl Barclays Bank PLC, Research Division - Research Analyst**

And I guess just on the other buckets, fair enough on taking the equal versus the greater than, but you still have the equal as part of the commentary out there. So I guess still with the -- even if we take up more positive approach to greater than, are there additional buckets of spend? I know you talked about the tax spend, but it sounds like that's going to be flatter. I'm just trying to understand if there other -- even beyond the kind of core transaction or split side, if there's anything in kind of TRG or Cartus that we should be thinking about that are kind of headwinds in '18 relative to '17.

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**Anthony E. Hull Realogy Holdings Corp. - Executive VP, CFO & Treasurer**

Sure, sure. Well the first headwind is inflation, which is something we -- what we use cost savings to offset. The second one that Ryan, specifically, pointed to is new development, which is sort of \$10 million to \$11 million in each headwind in each of the first 2 quarters. So that one is obviously, a major headwind. And then we've benefited last year from taking our asset the PHH joint venture and liquidating it, so there was a gain of \$20 million on that. And then we're replacing it with a new joint venture, which is just in a ramp-up stage. So I think those are the major headwinds for the year, in addition to the one you brought u,p, which is splits.

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**Operator**

This concludes the Realogy 2017 Earnings Conference Call. We thank you all for your participation. You may now disconnect.

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