

30-Jul-2020

Realogy Holdings Corp. (RLGY)

Q2 2020 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good afternoon, and welcome to the Realogy Holdings Corp. Second Quarter 2020 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 tomorrow. 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 the Realogy's Senior Vice President, Alicia Swift. Please go ahead, Alicia.

Alicia Swift

Senior Vice President-Financial Planning & Analysis and Investor Relations, Realogy Holdings Corp.

Thank you, Chris. Good morning and welcome to Realogy's second quarter 2020 earnings conference call. On the call with me today are Realogy's CEO and President, Ryan Schneider; and Chief Financial Officer, Charlotte Simonelli.

As shown on slide 3 of the presentation, the company will be making statements about its future results and other forward-looking statements during this 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, including any statements we make related to expectations with respect to the ongoing COVID-19 crisis. 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, July 30, 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 on this call, and per SEC rules, important information regarding these non-GAAP financial measures is included in our earnings press release. Lastly, for the second quarter of 2020, the Relocation business continued to be reported as discontinued operation.

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

Ryan M. Schneider

Director, Chief Executive Officer & President, Realogy Holdings Corp.

Thank you for joining us this afternoon. I want to start by thanking Realogy employees, affiliated agents and franchisees for their dedication and hard work helping customers safely buy and sell houses during these challenging times.

I also want to thank our employees and agents for their openness sharing the different challenges COVID created in their local markets. That openness helped us move quicker as a company to implement solutions to better support agents and customers.

And finally, thanks to all of our employees for their thoughtful dialogue on diversity and inclusion, especially those who shared experiences that help all of us better understand the unique challenges people face today. And for all of you joining our call today, I hope you and your loved ones remain safe and healthy.

Today's discussion will be structured like last quarter. I will start with summary remarks and key takeaways, then turn over to Charlotte for a brief overview of the financials, and I will come back to talk about what we're seeing in the housing market, including early results from July.

So, I'm excited to share our Q2 results and our continued strategic progress during this incredibly turbulent time. We demonstrated strong performance delivering \$172 million of operating EBITDA from continuing operations in Q2 even in the depths of the COVID crisis.

Our operating EBITDA performance in the quarter was driven by three things. First, closed transaction volume across both our franchise and owned brokerage businesses fell dramatically in April and May, but improved markedly in June. We are seeing continued closed transaction volume improvement in July, and we are particularly excited by the very strong new open transaction volume we have seen in June and July, which I will share with you later in the call.

Second, we delivered substantial cost reduction in the quarter, both temporary reductions we shared with you on our last call and permanent savings we implemented in 2019. And third, our mortgage business had a very strong quarter. We made good strategic progress in this business in the past year, especially expanding our coverage in the market and greater integration with our brokerage business.

This strategic progress combined with the obviously strong refinancing trends helped drive the quarter's results. And along with our operating EBITDA delivery, we continued to invest and drive our strategic agenda in the second quarter.

So, first, our technology focused in innovations are delivering results. We had substantial adoption acceleration of our products in the quarter. We delivered real expansion of our virtual capabilities in the past four months; virtual staging, virtual open houses, virtual tours, virtual title closings, virtual mortgage closings.

We also continued to deliver marketing lead generation and other products to help agents do more deals. The combination of virtual capabilities, strong products and increased adoption helped agents drive volume successfully and safely during this crisis. And we are excited to virtualize and simplify the real estate transaction in the future.

Second, we grew brokerage agents 2% year-over-year and our top two quartile agent retention improved a bit. The Q2 competitive environment was overshadowed by COVID, but pretty much continued the trend from Q1 of 2020 of being more rational than a year ago.

Third, we continued to expand our other strategic growth initiatives. We are growing our Corcoran franchise. More broadly, we like the pace of franchise sales even during COVID. We've been able to do franchise sales and onboarding of new franchisees in a purely virtual manner, which will serve us well in the future. And, we are increasing our marketing for high quality lead generation efforts like our new AARP program.

And fourth, we seized the market opportunity to refinance \$550 million of debt at an attractive price. We retired our 2021 unsecured notes improving our debt maturity profile and lengthening the term of the debt on our balance sheet.

Putting this all together, we demonstrated resiliency in tough times. We feel good about our performance and trajectory and we really like our position for the future, especially given the improving volumes we are seeing in June and July.

But we are closely watching the COVID and macro uncertainty. I look forward to sharing more detail about what we are seeing in the housing market, what we're seeing in consumer behavior and our thoughts on the future later in the call.

So, I will now turn over to Charlotte to briefly discuss the financials.

Charlotte C. Simonelli

Executive Vice President & Chief Financial Officer, Realogy Holdings Corp.

Thank you, Ryan. Good afternoon, everyone. Before getting into our financial performance, I would like to say that I am very pleased by both the swift actions we took across Realogy as well as the progress delivering on our strategic priorities. We adapted new ways of working and remained focused on emerging stronger on the other side. Amid this uncertain time, Realogy has become more agile and efficient and has effectively managed the areas of our business under our control.

Now, on to the second quarter performance, Q2 revenue was \$1.2 billion, down 27% versus prior year due to lower closed transaction volume. While the year-over-year decline was expected, we have now seen new open transaction volume rebounding, especially later in Q2 and in July.

Operating EBITDA from continuing operations was a \$172 million. We were pleased with this delivery in the midst of a crisis and benefited from strong cost management, exceptional performance from our GRA mortgage JV and

improving closed transaction volume in the latter part of the quarter. Despite the volume decline, we held operating margins flat at the Realogy level in the quarter with a strong focus on cost management.

Q2 operating EBITDA was down \$63 million versus prior year, primarily driven by the closed transaction volume decline and by a 164 basis point year-over-year increase in agent commission split. The higher commission split year-over-year was primarily driven by upward pressure from retention efforts over the last 12 months and the mix shift to higher performing agents in the quarter. We expect this pressure to continue in the second half of 2020.

Our GRA mortgage JV contributed \$35 million in operating EBITDA. This strong result was the combination of the strategic progress we made expanding geographic coverage, growing loan officers and improving service quality over the past year, which enabled us to capture more business. We also benefited from a very attractive Q2 mortgage environment, which has been driving a refinance boom. This demonstrates the power of our ancillary businesses, which is a strategic advantage, and we really like the financials.

We've successfully reduced costs and reallocated spend. Collectively, operating, marketing and G&A expenses declined \$95 million in the quarter. The permanent cost reductions we worked hard to deliver continue to come to fruition and contributed to the quarter along with the temporary actions we executed and realized in Q2. Given the improved transaction volume we are seeing, we have pulled back many of the temporary cost actions. We anticipate that approximately \$30 million of the temporary cost savings will remain in the third quarter. We also expect nearly all temporary cost actions will be lifted by Q4.

Finally, on cost, we are using learnings from this crisis to identify ways we can permanently lower our cost base across Realogy. It's too early to give you the overall numbers for 2021, and we still have work to do, but we are encouraged by our early findings. Just to give you one example, we expect to reduce administrative facilities by \$10 million to \$15 million in annual lease expense.

We ended the quarter with \$686 million in cash inclusive of revolver borrowings we proactively drew down at the onset of COVID and generated free cash flow from continuing operations of \$106 million. Including discontinued operations, free cash flow was \$47 million as we saw a use of working capital driven by our securitization facilities.

We have been proactive with our balance sheet and remain committed to deleveraging. In early June, we executed an oversubscribed \$550 million Second Lien Notes offering maturing in 2025, thereby eliminating the 2021 notes overhang. The transaction lengthened our maturity profile, while also supporting our near-term liquidity.

Our total net leverage ratio was 5.6 times and the senior secured leverage ratio was 3.29 times as of June 30, 2020, well within compliance with our financial covenants in the second quarter.

Finally, last week we amended our credit agreement to ease the 4.75 times senior secured leverage ratio financial covenant to 6.5 times commencing in Q3, 2020 for four quarters, with a gradual return to the original level by mid-2022. This was accomplished for a minimal upfront cost with no change in pricing. As our Q2 results show, we are well in and expect to remain in compliance with our original covenants, but took this proactive measure as tail risk insurance for the next four to eight quarters.

Overall, I am very pleased with our performance in Q2. Despite COVID-related volume declines, we successfully managed cost to ensure operating EBITDA and free cash flow delivery in the quarter. We also continued delivering key strategic priorities during the quarter to ensure continued momentum.

I will now turn the call back to Ryan to discuss what we are seeing more broadly across the business.

Ryan M. Schneider

Director, Chief Executive Officer & President, Realogy Holdings Corp.

Thank you, Charlotte. What I want to do now is tell you what we're seeing in the world and what we expect in the future. So let me start with our numbers. So in Q2 Realogy's closed transaction volume was down 24%. Brokerage closed transaction volume is down 30% in the quarter, with June down 17%. Franchise closed transaction volume is down 20% in the quarter, with June only down 2%. And the main difference between our brokerage and franchise closed transaction volume numbers is the same geographic variation that we referenced last quarter. For example, in Q2, New York City closed transaction volume was down more than 50%.

Now, some of the delta is driven by price, since there were fewer Q2 transactions in the highest price ranges e.g. \$1 million-plus homes where our brokerage business is just more heavily represented. The closed volume trends continue to improve in July. Based on the preliminary data through most of July, franchise closed transaction volume is up about 10% versus 2019 and brokerage closed transaction volume is up about 5% versus 2019.

On the franchise side, the improving closed transaction volume is driven by price and on the brokerage side the improvement is from both units and price. More interesting for the future is what's happening with open transaction volume, which remember, is the new contracts getting signed.

Open volume is showing very strong growth. In June open volume was up 21% versus 2019, up 30% in franchise and up 9% in brokerage. And again, most of the delta was driven by geographic variation. And based on the preliminary data through most of July this trend continues to improve with both franchise and brokerage open volume up approximately 30% versus 2019.

So what's driving such strong open volume growth across both our brokerage and franchise businesses? So, look, first, there's definitely some pent-up demand from the massive drop-off we all saw in late March, April and May. And second, there's no doubt the incredibly low mortgage rates are helping more and more people buy homes.

The third, low inventory is really driving up price. Today we are seeing inventory down at least 15% or more in every price band compared to a year ago, when inventory was already at historic lows. And that depth of inventory decline and especially the fact that the inventory is down across all price bands is something our most tenured industry leaders here at Realogy say they have not seen before.

And then finally, we are seeing both incremental housing transactions and people willing to pay more for a house, because of the societal shift driven by the COVID crisis. We are seeing increased demand for suburban living in multiple geographies, driving more transactions in higher prices. We are seeing increased rotation in homes within the suburban markets, as people's needs are changing. e.g. greater home office needs, e.g. putting a premium on outdoor space, e.g. the ability to live in a different geography given virtual work. We're seeing well-off consumers accelerate second home purchases, and frankly, we're seeing the already ongoing flight to attractive tax and weather destinations accelerated.

And we see these four consumer shifts I just mentioned when we look across both the transaction data and the anecdotes we get when we survey large numbers of consumers and agents across our brands. So we're really excited by what we're seeing in June and July, right. The new open volume is incredibly strong, but we're not running away too much with our excitement, and you shouldn't either, right. The volume drop in March, April and

May was unprecedented. And the increase in open volume we're seeing here in June and July is also unprecedented. And how long this growth will continue is hard to predict, right. There's macro and COVID uncertainty, and we just don't know how long trends like pent-up demand and like the consumer behavior changes we are seeing will last. So because of that uncertainty, we're very focused on what is actually happening today and sharing that with you. But we are not actually extrapolating too far into the future.

So, look, wrapping up, Q2 began with unprecedented challenges and an unprecedented drop in volume in our industry. And even though there was a tremendous amount of uncertainty at the start of the quarter, we are excited to exit Q2 with \$170 million in operating EBITDA from continuing operations. We moved very rapidly in the crisis. We demonstrated strong results on cost. We continue to drive strategic success like technology delivery, agent growth, corporate expansion and mortgage. We strengthened our balance sheet and we've even launched efforts to reimagine our business and reimagine how we operate the company. Putting all this together, especially coupled with the very strong and improving open volumes we're seeing in June and July we really like our position for the future.

So Charlotte and I look forward to taking your questions today.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] And our first question comes from the line of Tommy McJoynt with KBW. Your line is now open.

Thomas McJoynt-Griffith

Analyst, Keefe, Bruyette & Woods, Inc.

Q

Yeah, good evening, guys. Thank you. Appreciate the metrics on June and July trends. Now squaring that all up, do you have expectations for what you think transaction volumes will look like in 3Q and how that would breakdown by sides versus price?

Ryan M. Schneider

Director, Chief Executive Officer & President, Realogy Holdings Corp.

A

Well, look, we're not giving guidance on 3Q transaction volumes, but I basically just gave you the actual closed volume for the month of July, most of the month. And I gave you our open volume in both June for the whole month and July month-to-date.

Now, open volume typically takes 45 to 50 days to turn into closed volume. And, look, there is a wide range around those numbers; some deals close in one day, some take six months. And there is a wide range around them. And then we've got a little bit extra uncertainty here because with COVID restrictions, you can – sometimes, they can delay closing. And if there is a big problem, we did see a cancellation spike back in March a bit, so that could always change things.

But, look, the opens are kind of up 30-plus-percent. And so, you can do your own math on those things and your own assumptions about the distributions. We don't think it's helpful to give you a prediction as much as to give you the actual numbers and let you decide how you think the world is going to go. And again, we really love the trends. We can't exactly say what'll happen with August and September because of COVID and macro, but boy, that we love the trends. And we thought giving you as much detail as we could effectively up through last week would be the most helpful thing of what we're seeing in the market and what it implies for our future.

Thomas McJoynt-Griffith

Analyst, Keefe, Bruyette & Woods, Inc.

Q

Okay. Got it. Thank you. And switching gears, there's a few moving pieces in your franchise business margin with less marketing spend. And you had announced the termination of the listing fee contracts. Could you just kind of walk through those moving pieces and how they should impact that segment's bottom line?

Charlotte C. Simonelli

Executive Vice President & Chief Financial Officer, Realogy Holdings Corp.

A

So, on the franchise side of things, we did have lower marketing expenses. We also had a lower contribution into the brand marketing fund. And so, those basically are more correlated, the absence of the revenue, but also the absence of the spend. We actually recognize that in the P&L as it gets spent. So that's more of an EBITDA-neutral.

There were some minor impacts in the P&L. And I think when we publish the Q, there will be more information available for you in that. But the bigger driver on the franchise side was the absence of the brand marketing fund and then the marketing expense and then the additional cost savings. The temporary cost savings that ploughed through the P&L on a pro rata basis sort of based on the number of the employees we have does impacts across our business.

Thomas McJoynt-Griffith

Analyst, Keefe, Bruyette & Woods, Inc.

Q

Got it. Thank you.

Operator: Thank you. And our next question comes from the line of Anthony Paolone with JPMorgan. Your line is now open.

Anthony Paolone

Analyst, JPMorgan Securities LLC

Q

Thank you and good afternoon. I guess my first question is, as you think about a stronger housing market which seems a little bit different than maybe what we were fearful of a few months ago. Now how do you think that ends up impacting the competitive landscape and things like splits? Does that bring back the heated competition compared to maybe what things were working like a few months ago or does that change that in some way, any color there'll be great.

Ryan M. Schneider

Director, Chief Executive Officer & President, Realogy Holdings Corp.

A

Yeah. I draw less – look, the competitive environment bluntly has not really been correlated with the housing market strength. 2018 and parts of 2019 were kind of flat and in some cases even down housing markets and the competitive environment at times was just incredible.

We're happy that Q2 like Q1 felt like a much more rational competitive environment the year before, still tough out there and we're part of that tough competition out there in the market. The bigger thing probably for splits is, remember the stronger the volume is out there, the more people can kind of work their way up to the tables. And so I think there may have been a hypothesis going into COVID that, weak housing years, maybe you won't have to pay as much in splits because people don't do as much volume. But the stronger volume comes back than the more volume business people do and especially the higher-end agents like Charlotte talked about, you get kind of

higher splits kind of coming from that as people move up the tables. But, look, we'd rather have the stronger volume and pay people to move up the tables than the reverse. So, we're okay with that. But the market strength in this -and the competitive environment have not been really correlated, and I don't think that is what's ever really driven the competitive environment. But there is the relationship which is pure volume and splits that we have talked about before.

Anthony Paolone

Analyst, JPMorgan Securities LLC

Q

Got it. And then in the title and in mortgage business, which did really well, any sense as to how much was just the sheer amount of refinancing is quite strong, but just also it sounded like maybe all gained market share. And so, I guess particularly something like the Guaranteed Rate joint venture doing \$35 million versus something else like \$7 million a year ago.

Ryan M. Schneider

Director, Chief Executive Officer & President, Realogy Holdings Corp.

A

Yeah.

Anthony Paolone

Analyst, JPMorgan Securities LLC

Q

If you had this level of market share, what would last year have been, just trying to dissect those as we think about the future revenues?

Ryan M. Schneider

Director, Chief Executive Officer & President, Realogy Holdings Corp.

A

It's funny because of all the refi stuff, it's a little bit harder to rip that apart, but, look, let me just tell you our story, right, which is, we started this new thing a couple of years ago and we lost money on it the first year as we were building it up. And we started off with not the greatest position as we were building off something that had been kind of falling apart before, but boy, over the last couple of years the team has worked really hard. We've expanded the number of loan officers substantially. The quality of loan officer has gotten better. We've expanded our geographic coverage and Guaranteed Rate, on the mortgage title side or on our brokerage business, has done a lot of work to better integrate this thing into the brokerage business to improve how much of our own business we capture effectively through our mortgage – or excuse me, through our brokerage business.

And that would have taken last year's number and definitely made it bigger all own its own. And then there was clearly a big chunk that comes from just the market here. So, we haven't actually ripped it apart to get to the decimal point you're talking about, but we really like the trajectory and we like the financials. And this shows the power of ancillary services and a lot of people talk about someday they'll make money from ancillary services, but we're doing it right now and this quarter was one of our better examples of it.

Anthony Paolone

Analyst, JPMorgan Securities LLC

Q

Okay. Can I sneak one more in?

Ryan M. Schneider

Director, Chief Executive Officer & President, Realogy Holdings Corp.

A

Sure.

Anthony Paolone

Analyst, JPMorgan Securities LLC

Q

So, again, one thing I am curious about is, see, you have lot of people in your organization that have been through pretty extreme ups and downs. Any thoughts on just how to bridge high unemployment rate and maybe a recovery that seems to be stalling a little bit here with just the housing market that's showing very strong trends and trying to think about how sustainable that might be?

Ryan M. Schneider

Director, Chief Executive Officer & President, Realogy Holdings Corp.

A

We don't know. We've talked about it and no. Look, this is unprecedented. No one has ever seen this peak. No one at Realogy that – I've only been here a few years, but I talked to all of the veterans, no one has ever seen - even if you go back to the Great Recession, the speed of the drop that happened in late March, April especially and no one has ever seen the speed of the comeback that's happened in June-July. Like, we were talking about it, we're going to have our busiest closing day we like ever had since I've been here tomorrow and we were literally talking about taking people from other parts of our company to help our title team get closings done.

And so it's just an unprecedented thing. And just like the GDP numbers today, we're way down – or yesterday whenever we're way down and the personal income numbers were like up, there's a bunch of things in the economy right now that as, you know, an economist by training but thankfully never practice seem very hard to square in this unique environment we're in.

You've just hit on another one. I don't have an answer for you, but what I do have is the actual data that we're seeing in the market. And then what we're worried about that could hurt that down the road, but also just what the momentum is as the housing market and our company has. But I don't think there is an answer that squares the circle on your question, just like three or four other kind of big macro contradictions out there in our economy right now.

Anthony Paolone

Analyst, JPMorgan Securities LLC

Q

Okay. Fair enough. Thank you.

Ryan M. Schneider

Director, Chief Executive Officer & President, Realogy Holdings Corp.

A

Thank you.

Operator: Thank you. Our next question comes from the line of Carter Trent with Stephens. Your line is now open.

Carter Trent

Analyst, Stephens, Inc.

Q

Oh, yeah. Thanks for taking my question. So banks are getting structured on who they lend to. So with credit kind of tightening the way it is, do you expect that to slow housing down any – anecdotally or you guys hear about any transactions that are fallen through because buyers can't get a mortgage?

Ryan M. Schneider

Director, Chief Executive Officer & President, Realogy Holdings Corp.

A

We are not seeing that yet. We've heard the same. There was a bit of noise in the jumbo market back in April-May. We maybe even mentioned it on our last call if we got the question I don't even remember, but it was – there was a bit of noise in the jumbo market about people tightening and a bit of a harder time getting mortgages. But we have not seen that playing out yet. Like the other factors that I listed, that could be one of the things that slows down the party at some point here. But when you've got macro uncertainty and COVID risk and some of the consumer trends and not knowing how long they're going to run, I would just put that in the list of things that could be a headwind to housing, but we're not seeing that be a headwind right now. And other than that, jumbo market anecdote from a few months ago, this topic has not come up for me, my team or our mortgage business in the last couple of months.

Carter Trent

Analyst, Stephens, Inc.

Q

Got it. Cool. Thanks, Ryan. And little more on the cost saves. Charlotte, can you remind me how much is expected in the back half of this year? And should we think about the cost saves as kind of a net reduction to the expense line item? So, basically, what I'm getting at is, are you guys planning to reinvest some of the – kind of the gross expected savings?

Charlotte C. Simonelli

Executive Vice President & Chief Financial Officer, Realogy Holdings Corp.

A

Yeah. So, how you should think about it is in the two buckets, the first is the \$70 million to \$90 million that we talked about, which is pretty evenly phased by quarter throughout the year. So those are the permanent cost reductions we had already announced. And then from a temporary cost saves, we have the \$80 million to \$100 million that we delivered in Q2, and then that drops down to \$30 million in Q3 and next nothing in Q4.

As far as reinvesting back, there's always other costs that hit the business. We do have slightly higher litigation right now. There's other things going on. But – so, it's not a direct correlation like there's some spend back in the business, but it's relatively minor.

Carter Trent

Analyst, Stephens, Inc.

Q

Okay. Got it. Thanks, guys. Appreciate you taking my questions.

Ryan M. Schneider

Director, Chief Executive Officer & President, Realogy Holdings Corp.

A

Thanks, Carter.

Charlotte C. Simonelli

Executive Vice President & Chief Financial Officer, Realogy Holdings Corp.

A

Thank you.

Operator: Thank you. Our next question comes from the line of Matthew Bouley with Barclays. Your line is now open.

Matthew Bouley

Analyst, Barclays Capital, Inc.

Q

Hey, good afternoon. Hope everyone's doing well. Thanks for taking the questions. So, with the brokerage business accelerating up 30% in July in open transactions, and as you mentioned, Ryan, we're all trying to figure out kind of what's sustainable versus what's pushed out or pent up. And maybe it'd be helpful, if you could talk through some of the geographies there. So, we're trying to figure that out a little. I know you mentioned New York City being down 50% at one point.

What's the recovery look like there and in some of the other markets that were hit hardest versus what if some of those markets that perhaps weren't under the same level of lockdowns et cetera, how did those trend versus to what degree have those markets accelerated? Thank you.

Ryan M. Schneider

Director, Chief Executive Officer & President, Realogy Holdings Corp.

A

Yeah, sure. That's a great question. Let me just give you some detail. I'm only going to focus on the brokerage business and let me talk about open volume, which was kind of plus 30% through July. So, look, New York City is still by far the toughest, just given the degree of lockdown and challenges there. It's still pretty substantially negative, it's not negative 50% anymore, but it's negative 30% to 40% still when you look at July.

The other one that was really tough, which is big for us was, California was negative in terms of open volume through May, June was kind of breakeven, July is up 30%, but that's the first month up from after a lot of decline.

Whereas places like Florida were up pretty good in June and are up very good in July, way about 30%; Texas and Arizona even with the COVID situations there, plus 25%, 30%; New Jersey is one of those destinations, suburbs is up more than 50%; New England is up more than 30%. And so, it's really the geography is that kind of did better through the April-May time like Florida and Texas and maybe a New England have continued to be stronger than the average.

The ones that were really tough like in California, like in New York are improving, but are still at or kind of below the average. And – but then the overall, obviously, is looking pretty good. But – so we're watching it pretty closely at those local levels. And, again, a lot of the things like New Jersey and New England is that suburban affect I talk about, Connecticut, is on fire, right, New Jersey is on fire. Florida, which also includes that vacation home and that, what would you call it, attractive tax, weather acceleration on the consumer side. So there's a lot of things coming together that lead to some of the regional strength and some of the regional challenges. But that's a little bit of local color what we're seeing on the brokerage side. And franchises in the same ballpark, the numbers are different, but the direction is often the same.

Matthew Bouley

Analyst, Barclays Capital, Inc.

Q

Got it. That's very helpful, exactly what I was looking for. And then I had a longer-term question on splits as well, obviously up over 74% or so for the second consecutive quarter and gave some color around the drivers of that. It sounded like that there's going to be a bit of mix in there which may or not, you know, may not normalize to some degree in the near-term here and then the retention side which seems a little more structural. The question is really if the market is normalized a year from now, however we want to define that, could splits actually step back a bit for the first time in a while or is 74% kind of the starting point and we're just going to go from here? Thank you.

Charlotte C. Simonelli

Executive Vice President & Chief Financial Officer, Realogy Holdings Corp.

A

Yeah. Thank you for the question. I think we're taking it day by day here. And as far as the drivers for Q2, we definitely think part of that is driven by COVID and part of that will continue throughout the rest of this year. As far as next year, we're not giving guidance for next year on commission splits. We need to wait to see how it evolves right now, as we sort of unwind from the crisis. As far as unwinding I think we'd all like to see that, but at this point that's not something that we would guide you to.

Matthew Bouley

Analyst, Barclays Capital, Inc.

Q

Okay, understand. Thank you, both.

Ryan M. Schneider

Director, Chief Executive Officer & President, Realogy Holdings Corp.

A

Thank you.

Operator: Thank you. And our next question comes from the line of Stephen Kim with Evercore ISI. Your line is now open.

Stephen Kim

Analyst, Evercore ISI

Q

Yeah. Thanks a lot guys. Yeah, exciting times. Wanted to ask a couple of clarifying questions if I could. Charlotte, you mentioned the temporary savings and a range for 2Q. What was the actual number in 2Q? And then the brokerage commissions were up year-over-year, which was encouraging. I was just wanting to make sure the lost USAA affinity business, we thought that that might push brokerage commissions down. Did that actually impact 2Q or not? Yeah, we can start with those.

Charlotte C. Simonelli

Executive Vice President & Chief Financial Officer, Realogy Holdings Corp.

A

Sure. Yeah, so we definitely were at the higher end of the range that we gave you. So, you can use the higher end of the range from a temporary cost savings perspective in 2Q. As far as USAA goes, it's actually a negative to commission splits, it's an increase year-over-year, because those transactions came at a lower commission split because...

[indiscernible] (36:53)

Stephen Kim

Analyst, Evercore ISI

Q

I'm sorry, Charlotte, I meant the actual commission rate?

Charlotte C. Simonelli

Executive Vice President & Chief Financial Officer, Realogy Holdings Corp.

A

Sorry. What were you saying?

Stephen Kim

Analyst, Evercore ISI

Q

I meant, the actual brokerage commission...?

Ryan M. Schneider

Director, Chief Executive Officer & President, Realogy Holdings Corp.

Oh, you mean the average broker commission rate?

A

Stephen Kim

Analyst, Evercore ISI

Correct. Correct.

Q

Charlotte C. Simonelli

Executive Vice President & Chief Financial Officer, Realogy Holdings Corp.

The ABCR was actually up in the quarter, a few...

A

Stephen Kim

Analyst, Evercore ISI

Right.

Q

Charlotte C. Simonelli

Executive Vice President & Chief Financial Officer, Realogy Holdings Corp.

...so – yeah, we were actually up. But you're asking if that drove it? No, that's...

A

Stephen Kim

Analyst, Evercore ISI

I'm asking whether the – I guess, I'm just asking whether or not the USAA – the loss of USAA affinity business had any impact, whether it had its impact in this quarter or whether some lingering business related to the USAA affinity relationships that actually...

Q

Charlotte C. Simonelli

Executive Vice President & Chief Financial Officer, Realogy Holdings Corp.

It did have an impact – yeah, it did have an impact in the quarter, but that was an increase in commission splits. That's where you're going to see the...

A

Stephen Kim

Analyst, Evercore ISI

Yes.

Q

Charlotte C. Simonelli

Executive Vice President & Chief Financial Officer, Realogy Holdings Corp.

...impact in the quarter because...

A

Stephen Kim

Analyst, Evercore ISI

Right.

Q

Charlotte C. Simonelli

Executive Vice President & Chief Financial Officer, Realogy Holdings Corp.

A

...the transactions that we did were weighted to higher commissions, not the lower ones that we would have paid on a USAA business, which was non-existent this quarter.

Stephen Kim

Analyst, Evercore ISI

Q

Okay. Got it. That's what I needed. Okay. And then, the franchise business, the margins there, I was thinking that you lost some – you had a listing fee relationship I think that was going to impact, like I think it got accelerated into Q2. Did that actually hit 2Q, like you were thinking it was going to? I know initially you thought it would be not until 2022. That's the one that I'm referring to. Did that actually have an impact in 2Q, because we really couldn't even see the impact of it?

Charlotte C. Simonelli

Executive Vice President & Chief Financial Officer, Realogy Holdings Corp.

A

Yeah, exactly. There was an impact in Q2 and it was – it has been terminated. So, it did get realized in the quarter.

Stephen Kim

Analyst, Evercore ISI

Q

Right. So, the margins we're looking at, include that.

Charlotte C. Simonelli

Executive Vice President & Chief Financial Officer, Realogy Holdings Corp.

A

Yeah.

Stephen Kim

Analyst, Evercore ISI

Q

Yeah. Great. And then, lastly, Ryan, this is key question, right, that everyone is trying to figure out. This is this – the pent-up demand or whatever or is this actually tied to secular forces, which we actually think it's the latter. But, when you survey your customers, I know you've done that, I'm curious as to whether or not you're asking them when they decided to start their home purchase process, because I might give you a sense for whether you're seeing some pent-up action or whether you're talking about people who have just, it's like sort of just the demand has been created when COVID hit and in the aftermath. So, have you asked that question? Are you getting any sense from that?

Ryan M. Schneider

Director, Chief Executive Officer & President, Realogy Holdings Corp.

A

The sense I get and I kind of ended with it [indiscernible] (39:22) biggest one is there is like pent-up demand kind is what it is, but that's going to run out someday and for all we know, it's already run out possibly, who knows. The pricing – the upward price benefit we're all getting in volume on inventory, that may run for a pretty long time because there's just not that much inventory out there. And even when you look at the July new listings, there's clearly a lot more demand than the new inventory coming to the market.

The real big question is how long these kind of secular consumer changes are going to kind of go on? And from the survey stuff and the agent anecdotes and franchisee anecdotes I get, I think a lot of that, the decision – it was

not pent-up demand, it's decision people have made in months like May and June, for example. Right? Hence, the – more June and July kind of open volume strength. And some of those have some natural ends to them. Right? If people are accelerating their second home purchases, which isn't that big in the scheme of things, in my view, there're still – you're only going to do one second home purchase probably. So, some of that's going to run out.

The more secular shift to suburban living and some of the rotation within the suburban markets, that's the one – those are the ones with both the big numbers associated with them, but also the big uncertainty of, is it a small group of people kind of rushing to the exits to do those things or is that a really big secular trend that could go on for a long time. And I just think we're too early, right, to actually know the answer to that yet because, again, we're kind of looking at seven weeks here a very interesting kind of unprecedented volume acceleration. And so, that's why we kind of focused on, look, here's what we're seeing and even telling you what we're seeing in different local geographies, per the previous question.

But, there is a real chance that this thing has got a lot of momentum – got a lot of legs to it, but there's also a real chance that whether it's COVID, macro or something else, you could – this thing could kind of, like, fall off a cliff pretty quickly and go back to kind of a normal housing market. I think the low rates parts probably here with us for a while and that's very favorable. So, those are my thoughts, but that's also why we've probably gone more detail in this call than we usually do and how we're thinking about the future.

Stephen Kim

Analyst, Evercore ISI

Q

If there's one thing that as you think about managing your business longer term that you would do differently if that – if the secular trends are real versus if they are not, what comes to mind?

Ryan M. Schneider

Director, Chief Executive Officer & President, Realogy Holdings Corp.

A

Well, look, the easiest answer, but probably not the most important is what you would do differently on your cost position. Right? If we're in just a kind of a volume bubble here, right, what you would do on the cost is different than if you're in a much stronger housing market for multiple years, in terms of kind of how you'd want to kind of manage the margin and make sure you're investing to support a much larger volume than you're kind of you've been used to dealing within this industry for many years. So, that's probably the easiest one.

I think there's some of the stuff on what we're doing virtualizing the transaction that will be increasingly helpful if this is an ongoing trend. And then, I like our position in business mix. People think we're like the urban real estate company, but like our – in every geography we're in, we're in like 50 of the biggest 100 metros in the US, our suburban business is bigger than our urban business. Right? Even like the New York City, we got – we love our business in Manhattan and Brooklyn, it's huge, but go add up our business between Sotheby's, Coldwell Banker and Corcoran on Long Island, Westchester, Connecticut and New Jersey, and wow, like we will be a beneficiary of this suburban thing if it continues. So, keeping that pretty high in people's minds is important too if these secular trends to the suburban thing really do continue.

Stephen Kim

Analyst, Evercore ISI

Q

Great. Thanks very much, Ryan.

Ryan M. Schneider

Director, Chief Executive Officer & President, Realogy Holdings Corp.

A

Thank you, Stephen.

Operator: Thank you. And our last question comes from the line of Jack Micenko with Susquehanna. Your line is now open.

Jack Micenko

Analyst, Susquehanna International Group, LLP

Q

Hi. Good afternoon. First one for Charlotte, clarification, you had said you learned some things from temporary cost savings and I think you had said potential facilities lease savings of \$10 million to \$15 million. Am I right on the number and is that – are you thinking of that as a 2021 time of reality, or how do we think about that?

Charlotte C. Simonelli

Executive Vice President & Chief Financial Officer, Realogy Holdings Corp.

A

Absolutely. You are right on the number. And that's just the early step that we've been able to identify and start to execute on. Some of that could start hitting later in the year, but yeah, I think the bigger piece of that will start hitting next year.

Ryan M. Schneider

Director, Chief Executive Officer & President, Realogy Holdings Corp.

A

And Jack, if I could just editorialize on that for a minute. Look, I think every good company is trying to reimagine themselves a bit with both what they've – we've learned from virtual work and the COVID crisis and where the world may be going. I'm really excited that we started doing that work. As we talked in our last call, that's kind of the next generation of the \$70 million to \$90 million of cost savings that we did last year and even some of the temporary stuff we did now.

And to already have kind of one very tangible example that we made decisions on to kind of put in the book feels good, but both on the transaction side and the company side, that's just a really important thing. And I was really glad Charlotte was able to share something with you about it today. And we're looking forward to what else we – we – we're finding on that. It's been an amazing learning experience. Most of the learnings aren't ready for public disclosure yet, but boy, are we excited about doing that work.

Jack Micenko

Analyst, Susquehanna International Group, LLP

Q

Yeah. And I think a lot of corporate America is coming to the realization that maybe the real estate picture for them has changed, maybe permanently.

[indiscernible] (45:36)

Ryan M. Schneider

Director, Chief Executive Officer & President, Realogy Holdings Corp.

A

[indiscernible] (45:38) it goes far beyond real estate. It gets into employee productivity in buildings versus at home. It gets into the employee satisfaction. It gets into where you can recruit. It gets into all the stuff. But again, I think tons of companies are doing all that same kind of work, but we're excited to be pushing pretty hard on it and the facilities one was a great tangible dollar one you can kind of go at pretty quickly. And so, we're a part of it.

Jack Micenko

Analyst, Susquehanna International Group, LLP



I'll let you wrap up with a big picture question, Ryan. What shakes the tree on inventory? On one side, we always hear price appreciation brings sellers to the market. On the other hand, you hear today, hey, I would like to sell my house, but I don't know where I'm going to go and I don't want to get caught in a situation where I sell my home in three days in a multiple bidding situation and I've got nowhere to go. So, does this environment actually create somewhat of a more vicious cycle? Just curious how you're thinking about that.

Ryan M. Schneider

Director, Chief Executive Officer & President, Realogy Holdings Corp.



Yeah. Well, we start with the worry that you've got. I mean, the inventory for the last whatever two and a half years has been pretty historically low when you look at how many months inventory are out there. Right? If six months is the historical average, it's been like four months inventory for a couple of years and it's even less right now. And all the things that have historically shaken a little bit of inventory, like the higher price thing have actually not done it, to your point. Look, I still believe there is a huge new construction thing going on here where, as a society, we're just not building enough homes, period, of any type. And you can see it in the new construction numbers on where they are relative to like even just the late 1990s and stuff like that. And there's all kinds of reasons for that. So, I think that's a piece.

The thing that may do a little more unlocking though, to me, if I was going to look for a positive, is that thing we're seeing a kind of rotation in the suburban market where people want and need different things. But when we survey thousands of customers and agents, what people want and need different aren't – isn't the same thing. Right? Some people are looking for more on the home office side or more on the external space side. Others have those things, but don't want or need them as much as before. And that might be able to actually unlock some inventory if that suburban rotation is not a temporary thing and is a longer thing.

But, the tight inventory thing is a big worry as an industry and I think even as a society that we don't talk about enough. I wish I had better answers on it, but I don't. I do think we're well-positioned to capture it, whether it comes in units or price. And because of that suburban massive presence we have I talked about, I think where the world is going is in our favor. But, we would love more inventory out there too.

Jack Micenko

Analyst, Susquehanna International Group, LLP



Got it. Appreciate the thoughts.

Ryan M. Schneider

Director, Chief Executive Officer & President, Realogy Holdings Corp.



Thank you.

Operator: Thank you. And our last question comes from the line of Ryan McKeveny with Zelman & Associates. Your line is now open.

Ryan McKeveny

Analyst, Zelman & Associates



Hey, thank you so much, guys, for squeezing me in. So, two quick ones. One, the commission rate, and I apologize if I missed this earlier, but the commission rate actually ticked up a bit in both the franchise and owned

side of the business. And I think that's the first time in a while we've actually seen that tick higher. I think in this industry, typically when inventory is very tight, you actually can see some compression on the commission rate, just given kind of the competition amongst agents. So, curious, if you can just comment on kind of what drove that this quarter?

And then, second question, on the Corcoran side of things, on the franchise, we've seen some of the announcements. I'm just curious, what you can say regarding kind of the pipeline and how things are going thus far relative to maybe how you expected things to go? Obviously, COVID throws a bit of a wrench into things. But just curious, big picture, how that's going versus you anticipated, and ultimately, what the pipeline is looking like in that side of things? Thank you.

Ryan M. Schneider

Director, Chief Executive Officer & President, Realogy Holdings Corp.

A

Well, thanks, Ryan. I'll take both of your questions. So, look, on the average broker commission rate, look, we were happy to see it tick up a little bit in franchise and brokerage. And that's great. We don't see a trend there or something. That number is kind of bounces around. But when you really look back at it over the last, not just couple of years, but multiple years, those numbers are pretty stable and a lot of times they move around because of mix. I don't think this quarter was because of mix. But, we'll take the fact that it was a little bit better, but I don't think there's yet a macro trend there.

But the part of the reason I think it didn't go down, you may want to keep in mind, is actually that the power of agents – I know you talked about agent competition, but there's – agents earn this commission, in my belief, because they actually provide real value. And agents, I think, provided even more value during this – during the COVID kind of quarter that we just finished. In terms of the work they were able to do to help customers set the right price, often a higher price, by the way, to the customer's benefit and to get deals done in a much more uncertain and much more health and safety kind of time.

So, the uses of agents in Q2, I bet, is actually up versus normal. That's a guess, I don't have the data, but that's my guess. And I think you should remember, all of the iBuyers shut down and agents powered on and agents got hundreds of thousands of deals done; Realogy agents and other agents. And so, you can see a little bit of a market dynamic there where somebody's other price or other option kind of went away. So, I don't think there's a lot of news in that other than it's kind of continues to be a relatively stable thing out there. But I do think that there's – people are using agents, and frankly, maybe even more during this crisis because agents are helping customers power through and get their homes bought and/or sold safely. So, I'm a big fan, and I think they're actually proved a lot of it in the quarter.

Look, on the Corcoran side, we're excited about the franchise launch, we're excited that we're building a portfolio, we added a couple more. Our first Corcoran franchisee just bought a great firm in Northern California to expand. That's great. We've got a pipeline. We can't publicly announce what's already been signed and what's going to be announced soon hopefully. But we've got a good pipeline. We feel good about it.

Just like our Sotheby's business that we launched, whatever it was, coming up on 15 years or more than 15 years ago or Better Homes and Gardens over a dozen years ago, you don't build these franchise businesses overnight. But boy, we're excited by the build we've had so far and what the pipeline looks and we really like obviously the economics of franchise real estate, especially at the high end where Corcoran plays.

So, thank you, Ryan, for both of those good questions.

Ryan McKeveny

Analyst, Zelman & Associates



Very helpful. Thank you.

Operator: And ladies and gentlemen, this does conclude today's question-and-answer session. And this does conclude today's conference call. Thank you for your participation and you may now disconnect.

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