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Walker & Dunlop, Inc. *(WD)*

Q3 2012 Earnings Call

CORPORATE PARTICIPANTS

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Deborah A. Wilson

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Bose George

Analyst, Keefe, Bruyette & Woods, Inc.

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MANAGEMENT DISCUSSION SECTION

Operator: Welcome to Walker & Dunlop's Third Quarter 2012 Earnings Conference Call and Webcast. Hosting the call today from Walker & Dunlop is Willy Walker, Chief Executive Officer. He is joined by Debbie Wilson, Chief Financial Officer, and Claire Harvey, Vice President of Investor Relations.

Today's call is being recorded and will be available for replay beginning at 11 a.m. Eastern Standard Time. Dial-in number for the replay is 800-695-2533.

At this time, all participants have been placed in a listen-only mode and the floor will be opened for your questions following the presentation. [Operator Instructions] It is now my pleasure to turn the floor over to Claire Harvey. Please go ahead.

Claire Harvey

Vice President-Investor Relations, Walker & Dunlop, Inc.

Thanks, Glenn. Good morning, everyone, and thank you for joining Walker & Dunlop's third quarter 2012 earnings conference call. Joining me this morning are Willy Walker, our Chairman, President and Chief Executive Officer, and Debbie Wilson, our Executive Vice President, Chief Financial Officer and Treasurer. This call is being webcast live on our website and a recording will be available later this morning. Both our earnings press release and website provide details on accessing the archived call.

This morning, we posted our earnings release and presentation to the Investor Relations section of our website, www.walkerdunlop.com. Both documents provide additional detail on certain topics that we will refer to during our prepared remarks.

Please also note that we may reference certain non-GAAP financial metrics such as adjusted net income, adjusted earnings per diluted share, adjusted operating margins, adjusted income from operations and adjusted total expenses during the course of this call this morning. Please refer to the earnings release and presentation posted on our website for reconciliations of the GAAP and non-GAAP financial metrics and related explanations.

Investors are urged to carefully read the forward-looking statements language in our earnings release. Statements made on this call which are not historical facts may be deemed forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements, including statements regarding future financial operating results, involve risks, uncertainties, and contingencies, many of which are beyond the control of Walker & Dunlop and which may cause actual results to differ materially from the anticipated results.

Walker & Dunlop is under no obligation to update or alter our forward-looking statements whether as a result of new information, future events, or otherwise. We expressly disclaim any obligation to do so. More detailed information about risk factors can be found in our reports on file with the SEC.

I'll now turn the call over to Willy.

Willy Walker

Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.

Thank you, Claire, and good morning and thank you all for joining us on this special day for Walker & Dunlop. Today marks the 75th anniversary of the day my grandfather and great uncle founded this company. My father has spent his entire career successfully leading and growing this enterprise, and today I have the honor of working with an outstanding group of professionals who are focused on where Walker & Dunlop goes from here to continue expanding upon this company's storied history and fantastic shareholder returns.

It is particularly pleasing to be announcing such impressive quarterly results on this anniversary. The successful acquisition of CWCcapital and resulting growth, both organic and due to the acquisition, of over 100% in origination volumes, revenues and adjusted net income is dramatic.

This company has never been stronger with regard to market position and financial strength and our investors should know that our management team is laser-focused on how to take advantage of where we stand today.

I want to take a moment to reflect on the history of Walker & Dunlop before we dive into specifics on the quarter and year-to-date finances. Debbie will provide additional color on our financial performance, and I will conclude by discussing where we go from here.

I won't spend much time on truly ancient history, but it is noteworthy that we have been in business for as long as the Golden Gate Bridge and Federal Reserve Building have existed. We have managed through many cycles always with a focus on meeting our clients' needs and realizing long-term capital appreciation for our shareholders.

My father made the wise decision in 1988 to enter the Fannie Mae DUS business, allowing a small thinly capitalized company to begin competing with the country's largest financial services firms. Walker & Dunlop and Fannie Mae have provided billions of dollars in capital to the multifamily industry over the past quarter-century with unquestionable success from a financial return and loan performance standpoint.

In November 2007, when Walker & Dunlop celebrated its 70th birthday, we established the Drive to 75, an ambitious goal of increasing revenues, operating income and net income 5X in five years. This plan was audacious

under normal circumstances, but considering the near complete meltdown of the financial markets that ensued, it would have been understandable if we had put the Drive to 75 on the back burner until the markets recovered, but we did not.

Instead, we expanded our agency lending by acquiring Freddie Mac and HUD origination and servicing businesses from Credit Suisse in 2009. That acquisition closed only four months after Fannie Mae and Freddie Mac were placed into conservatorship and when many people doubted the future of the agencies. We did not.

Our next move was to go public to raise capital at the beginning of the next economic cycle. Only 38 companies went public in 2009, one of the most depressed IPO markets of the last quarter-century. Here we knew raising capital was critical to our continued growth. So we put our heads down and drove towards an IPO when few thought a company of our size, much less than mortgage banking company, could go public, but we did. So when the opportunity to acquire CWCapital arose this year, we jumped.

CWCapital was a fantastic company with great people. The acquisition looked accretive right out of the blocks. The added scale of CW makes Walker & Dunlop one of the largest providers of capital to multifamily and commercial real estate markets in the country. Some have asked, why we decided to significantly expand our agency lending business at a time when the future of the GSEs is still not known. My response is why would we not.

Deal flow is the life blood of our business and it is accessed one of two ways; by people or by brand or by the combination of both. The acquisition of CWCapital dramatically enhances our access to deal flow by bringing on talented originators, underwriters and closers and it enhances the Walker & Dunlop brand by making us the second largest multifamily and eighth largest commercial real estate lender in the United States.

When we announce our full-year 2012 earnings, we believe Walker & Dunlop will have accomplished the Drive to 75 and grown revenues, operating income and net income 5X in five years. This growth has come from us zigging when others zigged. We have made bold strategic moves, but more than anything, it is the people of Walker & Dunlop who have made this noteworthy growth and profitability possible.

Walker & Dunlop was recently named one of the best companies to work for in the United States by the Great Places to Work Institute in their annual 2012 Best Small & Medium Workplaces list published last week in Fortune Magazine. We have won many awards throughout our company's 75-year history, but none has been as gratifying or important to our company's sustained growth and success as being named a Great Place to Work. If you are an investor in Walker & Dunlop today, you own shares in a company that is not only growing dramatically and putting up great numbers, but a company that is filled with talented professionals who enjoy their jobs and the company they work for.

The addition of CWCapital had an immediate and dramatic impact on our Q3 financial performance. CW added \$1 billion in loan originations and that was just for the month of September. Our average deal size also grew significantly in Q3 with almost two thirds of our deals being over \$20 million. Although larger deals typically have lower origination fees as a percentage of the loan size, larger deals require less resources to originate on a per loan dollar basis and they carry similar servicing fees to smaller deals, producing significantly higher aggregate servicing income over the life of the loan.

Along with the dramatic growth in our origination volumes, the acquisition of CWCapital adds \$14.5 billion in long-term largely prepayment protected servicing, increasing the average life of our combined portfolio to over 10 years and maintains the weighted average servicing fee of 23 basis points. The combined \$33.9 billion portfolio is a stable foundation for the company, mitigating volatility across market cycles and should continue to comprise 20% to 25% of our annual revenues, a wonderful annuity for our company and our investors.

CWCapital had fantastic underwriting and we are very comfortable assuming the risk from CW's Fannie Mae DUS portfolio. Our credit statistics continue to reflect exceptional performance in our at risk portfolio, but now is not the time when our portfolio will reflect poor underwriting. Multifamily is a hot asset class with low vacancy levels and exceptional operating results. It is only in times of stress when poor underwriting is exposed.

Walker & Dunlop weathered the financial crisis extremely well due to our rigorous underwriting and credit standards in the years leading up to the crisis. Although our loan origination volumes are up dramatically, the processes and procedures that ensure we are making great loans have not changed. It is when times are good, the credit discipline is most important.

Along with the CW acquisition, we've been hiring new talent to expand our various business lines throughout the year. Personnel expense as a percentage of revenues increased to 46% in Q3. Although higher than in previous quarters, this ratio is not concerning at this time for two reasons.

First, we have made significant investments in origination talent this year and those investments are already paying dividends with our increased origination volumes. Second, Q3 was a distinct quarter due to the acquisition of CWCapital and the mix of origination and servicing revenues and personnel expense.

Debbie will go into more detail on this point in a moment, but this ratio in Q3 is not indicative of our true personnel expense as a percentage of revenues. With all that said, we produced a very healthy 34% adjusted operating margin in Q3 after backing out deal-related expenses.

As I mentioned during our September call, CW was a lower-margin business than Walker & Dunlop and it will take us a few quarters to integrate CW and get back to Walker & Dunlop's historic operating margins. With deal costs, Q3 operating margin was 17%, and year-to-date operating margin was 24%. The integration of the two firms is moving along rapidly, but we still have plenty of work to do to gain the economies of scale we expect to derive from the combined platform.

I would like to turn the call over to Debbie to go through the financials and I will then finish the call by taking – talking about Onward to 80 and what to expect from Walker & Dunlop as we move forward. Debbie?

Deborah A. Wilson

Chief Financial Officer, Treasurer and Executive Vice President, Walker & Dunlop, Inc.

Thank you, Willy. Today we celebrate the company's 75th anniversary and report record Q3 performance; what an exciting and monumental time for the company. In the past, we've described our quarterly results using words such as exceptional, record-breaking and transformative. The third quarter of 2012 continued this trend.

Significant amounts of time and effort were invested during the quarter to ensure the key areas of our business, originations, underwriting, rate locks, closings, deliveries, servicing and asset management, could continue without interruption as we brought Walker & Dunlop and CWCapital together. And those efforts paid off. Employees rallied around the combined company and delivered strong results. I am very proud of our team, and I would like to thank them for all of their hard work this quarter.

I will focus my remarks today on the performance drivers for Q3 and how the CWCapital acquisition impacted the three months ended September 30. I will then provide an update on the integration of CW, including acquisition and integration related expenses and long-term savings.

The CWCcapital transaction generates both short-term and long-term changes to our financial statements. As you can see, we are providing both GAAP financial information and adjusted financial information that excludes the short-term impacts of purchase accounting and deal-related expenses.

We believe the adjusted financial information provides investors with meaningful data about the ongoing operating results of the company and allows investors to benchmark performance between periods. The majority of the deal-related expenses and short-term impacts of purchase accounting are collectively defined as selected expenses and are included in our GAAP financial statements.

Slide 17 and 18 of the presentation provide breakout of the selected expenses and reconciles GAAP and adjusted financial information for expenses, income from operations, operating margin, net income and diluted earnings per share. You may want to have these slides nearby as I speak to the Q3 results.

Adjusted net income for the third quarter was \$14.3 million or \$0.56 per diluted share, a 136% increase from \$6.1 million or \$0.28 per diluted share in Q3 of 2011. GAAP net income for the third quarter was \$7.1 million or \$0.28 per diluted share, a 17% increase over the third quarter of 2011.

Reporting adjusted diluted earnings per share of \$0.56 in Q3, 2012 is fantastic. While that reflects the dramatic growth in profitability of the quarter, please note our weighted average share count for Q3 includes only 3.3 million of the 11.6 million shares issued in conjunction with the CWCcapital acquisition.

Third quarter total revenues grew to \$70.1 million, a 110% increase over the same period last year, driven by the increase in originations and growth in our servicing portfolio.

During the third quarter, we originated \$2.2 billion of loans, a 141% increase over Q3 of 2011. It is important to note that although the CW acquisition added a great deal of the quarter's volumes and financial performance, Walker & Dunlop on a standalone basis grew loan originations 27% over Q3 2011 to \$1.2 billion. CWCcapital added another \$1 billion of loan originations in September, and while no small feat, September was not a typical month for CWCcapital.

Revenues remain strong as average gains from mortgage banking activities increased to 245 basis points, up from 238 basis points in Q3 2011. The two components of gains from mortgage banking activities, origination related fees and MSR, both increased by well over 100%.

Origination related fees increased 187% to \$27.7 million, significantly higher than the increase in loan originations due to the volume of Fannie Mae and HUD loans originated during the quarter. MSR, increased 116%, slightly less than the growth in overall loan originations, primarily due to the two large transactions that have short yield maintenance periods and therefore generated lower MSR values.

What should be noted with deals of this nature is that although we book a significantly smaller MSR upfront, should these two large transactions stay on our books through maturity, we will receive all the servicing income with very little offsetting amortization expense.

Servicing revenues were \$13.3 million in the quarter, a 52% increase over Q3 2011, of which 23% related to the growth in the legacy Walker & Dunlop portfolio and 29% related to the addition of CWCcapital portfolio. The servicing portfolio grew 113% over the past year and ended the quarter with a balance of \$33.9 billion.

Now let's turn to expenses. Our largest expenses are personnel and amortization. As expected, with a significant increase in Q3 loan originations and the acquisition of CWCcapital, we saw expenses increase as well. Total

expenses were \$58.3 million in the third quarter, a 146% increase over Q3 2011 and include the \$11.7 million of selected expenses related to the CWCcapital acquisition.

Total adjusted expenses, which excludes selected expenses, totaled \$46.6 million or a 97% increase over Q3 2011. The largest driver of the expense increase was personnel, which was 46% of revenues.

Although higher than past quarters, the level of personnel expense makes sense. Personnel expense increased 184% primarily due to the 187% increase in origination related fees where Walker & Dunlop paid commissions to our producers who, near the end of the year, are at the top end of their performance-based incentive pay structures.

Additionally, Q3 revenues did not include a full quarter of servicing fees. As I previously mentioned, in Q3 there were two large transactions where we did not book typical MSRs and only booked one month of CW's servicing revenues. Without these unique items, personnel expense as a percentage of revenue would have been 43%, which is closer to our historical performance in the high 30%.

Amortization and depreciation was \$17 million for Q3 2012, a 171% increase over Q3 of 2011. If we exclude the \$7.4 million of amortization related to the origination pipeline acquired with CW, the remaining amortization and depreciation expense would be \$9.6 million, which is reasonable given the current size of MSR portfolio.

I'd like to point out several changes to our balance sheet. Please turn to slide 21 of the presentation, while I review these numbers. Our balance sheet is exceptionally strong at quarter's end. As you can see, our net cash position is almost exactly where it was prior to the transaction. We have added approximately \$60 million in term debt and currently carry a debt-to-equity ratio of 0.24 to 1 and have plenty of room to use debt financing in the future.

As a result of the CWCcapital acquisition, we have added two lines to our balance sheet; goodwill and intangible assets. You will see \$53 million of goodwill on the balance sheet, which is less than the \$60 million to \$70 million we estimated on September 13. The reason for this downward adjustment is the fair value of the MSRs acquired was higher than our initial estimates. The goodwill from the CWCcapital acquisition will not be amortized, but will be tested for impairment at least annually.

At September 30, the intangible asset on the balance sheet was \$12.5 million and is comprised of the remaining pipeline intangible asset of \$11.3 million and \$1.2 million of licenses recognized in the 2009 Column transaction.

When we closed the CWCcapital acquisition, we booked an \$18.7 million intangible asset related to the CW origination pipeline that was just above the high end of the \$12 million to \$18 million range we provided on the September 13 call. We amortized \$7.4 million or 39% of the pipeline intangible asset in Q3 near the midpoint of the 30% to 50% guidance we provided previously. And we expect to amortize 20% to 30% in Q4 and the remainder in 2013.

In addition to the aforementioned pipeline intangible asset and associated amortization expense, we previously provided estimates of legal and banking costs, severance expense and the cost of transition services agreement for Q3 and Q4 of this year. In Q3, we incurred \$2.3 million of legal and banking fees, \$400,000 less than expected. Severance expense was \$1.1 million, approximately \$300,000 higher than expected. And finally, as expected, we paid CW Financial Services \$1 million for transition services in the third quarter.

For the fourth quarter of this year, we expect to continue to incur an additional \$1.2 million of severance expense and \$2 million of transition services expense. Q4 will also include additional expenses related to the servicing, as we have retained the CW servicing team through the end of the year as we transition the CW servicing portfolio to

our outsourced vendor. Beginning in 2013, we expect to save \$5 million to \$7 million per year from economies of scale and reduce the cost of servicing the CW portfolio by 40% to 50%.

We are extremely pleased with our quarterly performance and view the CWCapital acquisition as both strategic and highly valuable. The fourth quarter is typically our busiest quarter of the year and we now expect to originate between \$2.5 billion and \$3.2 billion, resulting an updated 2012 full year origination guidance of \$6.7 billion to \$7.4 billion. This guidance reflects year-on-year growth in origination volume of 66% to 84%.

And with that, I'll turn it back to Willy.

Willy Walker

Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.

Thank you, Debbie. Walker & Dunlop has gained significant market share through the acquisition of CWCapital and is extremely well-positioned for the anticipated growth in commercial mortgage originations over the next five years. We call our plan for the next five years Onward to 80, building off our successful Drive to 75. So what does Walker & Dunlop look like at 80 and how will it differ from Walker & Dunlop today?

First, Walker & Dunlop is a market leader in the multifamily finance space and we will work tirelessly to maintain and grow that position. Fannie Mae and Freddie Mac may or may not look exactly like they do today in 2017, but Walker & Dunlop will still be one of the very largest lenders to the multifamily sector regardless.

Second, Walker & Dunlop will continue to grow its capital markets business to originate loans on other commercial property types such as office, retail, hospitality, and industrial. We have spoken previously about our desire to expand this business in the Southwest and Western United States, and within the next few years, we expect to originate \$3 billion to \$5 billion annually in commercial mortgages through this channel.

Third, we will continue to build out our proprietary capital solutions, so we are underwriting and lending on all commercial real estate asset classes. Today, we are using our balance sheet and warehouse lines from commercial banks to lend on multifamily properties. We are exploring various capital solutions to lend on other asset classes such as a mortgage REIT, institutional funds and CMBS. Walker & Dunlop has the credit track record, client relationships and access to capital to be a significant lender to the entire commercial real estate industry going forward.

How big does Walker & Dunlop get? It's very hard to tell to be honest. Is it realistic to think Walker & Dunlop can grow revenues to over \$1 billion in the next five years? If we continue to scale our multifamily business and expand our lending operations to broader commercial real estate market, there is no reason why we cannot.

Will Walker & Dunlop continue to move up the commercial real estate lender lead tables? We moved from number 45 to number eight over the past five years. So there is no reason we shouldn't continue to gain market share, particularly as we expand our lending beyond multifamily. But it is important to remember the largest providers of capital to commercial real estate today are commercial banks and insurance companies that have huge balance sheets, extremely low cost of capital and significantly lower investor return expectations.

Walker & Dunlop clearly has the ability and desire to be one of the largest commercial real estate lenders in the country, and moving up the lead tables within this competitive landscape, while remaining highly profitable, is one of our main objectives over the next five years.

Walker & Dunlop has grown revenues at a compound annual growth rate of 32% over the past five years. We cannot predict what the macro environment will look like going forward, but we know that Walker & Dunlop, with CWCcapital and our current market position, should be able to grow dramatically over the coming few years.

As Debbie just mentioned, Walker & Dunlop will likely grow origination volumes 66% to 84% from 2011 to 2012. We are establishing 2013 origination guidance of \$8 billion to \$10 billion, which would produce origination growth year-on-year of 13% to 42% based on the midpoint of our updated 2012 guidance. We will continue to focus on origination and revenue growth as well as sustained profitability.

I'd like to conclude by going back to the very beginning, 1937. Oliver Walker and Laird Dunlop were looking out at a pretty bleak economy when they decided to go into business together, but they saw an opportunity, they were not daunted by the naysayers and they executed on a plan. My Father joined this company in 1962 and spent every day of his career sustaining and building upon the success of my grandfather and great uncle.

Today is a hugely significant day for our company. We celebrate 75 years of business, three generations of Walker leadership of this firm, generations of borrowers who've entrusted their real estate financing to Walker & Dunlop, the successful acquisition of CWCcapital and record operating results for the third quarter.

We have plenty to do as we move Onward to 80, but for today, I personally give thanks to this company's heritage and to the 430 Walker & Dunlop employees who make this company what it is today.

With that, I'd like to take – I'd like to open the line for questions.

QUESTION AND ANSWER SECTION

Operator: The floor is now open for questions. [Operator Instructions] We'll go first to the side of Bose George with KBW. Go ahead. Your line is open.

Bose George

Analyst, Keefe, Bruyette & Woods, Inc.

Q

Hey, good morning. Congratulations on hitting the ground running after that acquisition.

Willy Walker

Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.

A

Thanks, Bose.

Bose George

Analyst, Keefe, Bruyette & Woods, Inc.

Q

I have a couple of questions. First, in Debbie's prepared remarks, she noted that there was a large deal or two large deals where a traditional MSR wasn't booked. Could you just clarify that, just how the economics of that work?

Deborah A. Wilson

Chief Financial Officer, Treasurer and Executive Vice President, Walker & Dunlop, Inc.

A

Sure. That was – I was going to pull out the – let me pull the page on the slides as it relates to average mortgage banking, which if you look over time, has been 136 basis points, and in Q3 2012, it was 118 basis points. There

were the two large transactions. One of them has a very short yield maintenance period. And as you know, most of our loans have a nine and a half year yield maintenance period and a nine year estimated life. So when the large transactions have a very short life, effectively the MSR's have very little value.

Bose George

Analyst, Keefe, Bruyette & Woods, Inc.

Q

Okay. And in that particular transaction, is the – are the economics just a little lower or is there like more cash gains or is there some offset to that?

Deborah A. Wilson

Chief Financial Officer, Treasurer and Executive Vice President, Walker & Dunlop, Inc.

A

It depends, but in this particular instance, no. Large transactions vary deal-by-deal, but in this just the way the loan was structured, the MSR has a short yield maintenance period. It could last for a long period of time, but just given the components of yield maintenance, it's a little unnerving to put an MSR for a long period of time if the borrower can prepay in a short period of time.

Bose George

Analyst, Keefe, Bruyette & Woods, Inc.

Q

Okay, great. That makes sense. Thanks. And just in terms of the – you booked your MSR this quarter. It was 134 basis points versus 190 basis points last year. Is the difference there just the servicing fee?

Deborah A. Wilson

Chief Financial Officer, Treasurer and Executive Vice President, Walker & Dunlop, Inc.

A

MSR's are generally driven by servicing fee. The value of the MSR's are generally driven by servicing fees. Product mix can have an impact, but servicing fee is generally the biggest driver of that.

Bose George

Analyst, Keefe, Bruyette & Woods, Inc.

Q

Okay, great. And then just lastly on – sort of a political question. The FHFA is supposed to put out a report on the future of GSE multifamily in October. Was that expected?

Willy Walker

Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.

A

It was expected, Bose. I don't know what the status of them putting out the paper is, to be honest. I haven't done an update on that. I think the election, as we talked about in our earnings release this morning, sort of renews the discussion on the agencies with likely an entirely new Treasury Department in the Obama administration, some changes on the House Financial Services Committee et cetera. The – I think the debate begins anew, if you will.

And I would also add that with Fannie Mae and Freddie Mac, I think Freddie made a \$1.3 billion and Fannie made \$1.6 billion in the third quarter. So we've got about \$3 billion between the two agencies being made in the third quarter.

I find it – it will be very interesting to see how Congress looks now that they own them and are benefiting from that financial success at a time when everyone is focused on the fiscal cliff. It will be interesting to see how those revenues coming to the government change the government's outlook on what they want to do with Fannie and Freddie.

Bose George

Analyst, Keefe, Bruyette & Woods, Inc.

Q

That's great. Thanks. I definitely agree with you. Thanks again.

Willy Walker

Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.

A

Yeah. And Bose, just one quick thing on the point that Debbie made. Those two loans, one's a five-year loan, one's a seven-year loan and they're both adjustable rate mortgages. And so as a result of that, you're not booking a big MSR, but they're five and seven years. So they're not that short from a term standpoint, but as Debbie said, they aren't prepayment protected and as a result, we didn't book an MSR.

Operator: And we'll go next to the side of Will Marks with JMP Securities. Go ahead. Your line is open.

Will C. Marks

Analyst, JMP Securities LLC

Q

Thank you. Good morning, Willy, Debbie, Claire.

Deborah A. Wilson

Chief Financial Officer, Treasurer and Executive Vice President, Walker & Dunlop, Inc.

A

Good morning, Will.

Will C. Marks

Analyst, JMP Securities LLC

Q

Hello, I wanted to start with, I can't remember if you've given this in the past. I don't think you have, but what the combined number will look like for the full nine months for the two companies or the quarter or both?

Willy Walker

Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.

A

We haven't given that, Will. We did in our, what filing?

Deborah A. Wilson

Chief Financial Officer, Treasurer and Executive Vice President, Walker & Dunlop, Inc.

A

June 30.

Willy Walker

Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.

A

Our June 30 filing has CW first six months of the year, right?

Will C. Marks

Analyst, JMP Securities LLC

Q

Yes.

Deborah A. Wilson

Chief Financial Officer, Treasurer and Executive Vice President, Walker & Dunlop, Inc.

A

Which [indiscernible] (33:05) \$2 billion.

Willy Walker*Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.*

A

So are you talking about origination volumes, Will, or are you talking about...

Will C. Marks*Analyst, JMP Securities LLC*

Q

Right. Yes, origination volumes.

Willy Walker*Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.*

A

Yeah. CW had done, I believe, \$2 billion in the first six months of the year. I don't – I can't remember specifically what they've done in July and August, but the bulk of their Q3 originations were September. So I'll take a swag that they've done probably \$3.3 billion through the first nine months of the year on a standalone basis with \$1 billion being in September that comes into the consolidated, \$300 million in July and August and then \$2 billion before that.

Will C. Marks*Analyst, JMP Securities LLC*

Q

Perfect. Okay. Thanks.

Willy Walker*Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.*

A

We can get you actual for July and August as it relates to what their origination volumes were.

Will C. Marks*Analyst, JMP Securities LLC*

Q

Great. I'll follow up on that. Thank you. And then on – based on the guidance you're giving for next year, the – can you give some underlying assumptions, is there – does that include some hiring or is it pretty much just the same, where you are right now, obviously there is a benefit from owning CW for the full year.

Willy Walker*Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.*

A

Yeah, the 2013 guidance is based upon the origination platform we have in place today. That doesn't mean that we won't continue to look to hire talented originators and continue to grow. As I said in our comments, we're still looking to grow our capital markets business in the Southwest and in the Western United States and we're very focused on adding origination talent there.

But I think one of the challenges for us right now, Will, to be very blunt about it is that we've brought these two companies together, I think, exceedingly well. We have brought across the vast majority of origination talent at CWCapital and everybody seems to be enjoying the W&D platform, the added scale we have and clearly the numbers in Q3 are reflective of a great success on a combined basis, but we're quite honestly getting our arms around the scale we have today and the market presence we have and quite honestly how fast we can grow in 2013. So we feel very good with that range. And at the same time, as we noted, if you look at how we've grown origination volumes over the past five years, we've grown dramatically. And so we're quite honestly looking at our new scale, looking at the marketplace.

I would add one other comment, which is just that the demand for capital only seems to be increasing and with our new market position, we have a wonderful market to sell into and we have a much more significant market presence than we've ever had.

Will C. Marks

Analyst, JMP Securities LLC

Q

Okay. Thanks. And one more question. One the guidance, what kind of servicing fees should we assume next year? I mean, is the current run rate pretty close to where you should be?

Willy Walker

Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.

A

Well, you know we don't give guidance on servicing fee as well. So we're not going to give you an exact number, but I think that one of the things that Q3 did show is that in doing some of these larger transactions, sometimes they will be structured adjustable rate mortgages where there are some borrowers today who are looking not to lock and taking adjustable rate mortgages that they can prepay. And as a result of that, you're putting on some pretty big volume, but you're not booking the full MSR's upfront. But as Debbie noted, if those loans stick around for their full term and many of them have swaps related to them, which make it so it's unlikely that people will prepay, it's wonderful servicing income over the life of a loan. So to be honest, we're right now working through the type of deal flow that the CW origination network brings in, the type of deal flow that Walker & Dunlop has gotten historically and we're doing our own modeling, but we can't give you an exact number on that right now.

But Debbie – I think Bose just pointed out the Q3 last year was at 190 basis points, something and we're at 136 basis points this quarter. Your comment was should we just take the middle of that. I'm not sure whether you ought to go right down the middle, but I think the additional volume that we bring in and the presence that we have with Fannie and Freddie, I think, should say that agency lending will be a very significant component of our 2013 origination volumes even as we grow out our non-agency lending operations.

Will C. Marks

Analyst, JMP Securities LLC

Q

Okay. Makes sense. Thank you very much.

Willy Walker

Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.

A

Yep.

Operator: And we'll go next to the side of Brandon Dobell with William Blair. Go ahead. Your line is open.

Brandon B. Dobell

Analyst, William Blair & Co. LLC

Q

Thanks. Good morning, everybody.

Willy Walker

Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.

A

Good morning.

Brandon B. Dobell*Analyst, William Blair & Co. LLC*

Q

Couple of things on the forward-look. Within that origination guidance you provided, what's your underlying assumption for -let's call it an organic Walker & Dunlop, kind of excluding CWCcapital origination number or I've got to say a growth rate for just the Walker & Dunlop producers you've got on board?

Willy Walker*Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.*

A

Brandon, we're not breaking that out, but as you saw in Q3, W&D on a standalone grew over -originations over 20% quarter-on-quarter.

Brandon B. Dobell*Analyst, William Blair & Co. LLC*

Q

Right.

Willy Walker*Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.*

A

We feel very good about the W&D origination platform as well as the addition of the CW, but we're not breaking out what W&D, if you will, historic versus CW historic are going to do going forward.

Brandon B. Dobell*Analyst, William Blair & Co. LLC*

Q

Okay. And then from a, I guess, logistics perspective on the CWCcapital integration, it sounds you guys are still on track for the same kind of timeframe around getting the servicing businesses or servicing business transferred to your outsourcing platform, office closings, things like that. Any changes from what you guys talked about on the last conference call?

Willy Walker*Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.*

A

Fortunately, no. Anytime you do a deal of this scale for a company of our size, you sort of think that something might present more of a challenge or not happen to plan, but big credit to our management team, things are moving along very nicely and on plan. And as Debbie outlined, many of the estimates that we gave to you all on September 13 have come in pretty much right on the top of the estimate that we had at that time. So we feel pretty good about what we projected out as well as the timeline for getting integrated.

Brandon B. Dobell*Analyst, William Blair & Co. LLC*

Q

Okay. And then final one from me. As you look at the escort average deal size trends both in the Walker production [indiscernible] (40:04) as well as the CWCcapital production or producers, how do we think about the influence of those trends on the average fees for you guys? And is there any difference in what the servicing fee would look like on a large deal, let's say, a CWCcapital deal going forward as opposed to the traditional Walker deal? Just trying to get a sense of the direction on the average basis points of fees even though those deals size may be getting a lot bigger for you. Thanks.

Willy Walker*Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.*

A

It really, Brandon, depends on the borrower.

Brandon B. Dobell

Analyst, William Blair & Co. LLC

Okay.

Q

Willy Walker

Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.

One of the big issues here is that there are some borrowers today, so apart that the asset is a large asset, \$200 million of financing, whatever, the real driver right now is who the borrower is and what the – what's motivating the borrower. If it happens to be a real estate investment fund, so a private equity firm that is in the real estate investment business that has a fund life, they might be more steered towards doing an adjustable rate mortgage because they're going to pick up the additional – the lower interest rate and they're also going to have some more flexibility on the prepayment side.

A

If the owner of the asset is somebody who is in the real estate business and is a long-term holder of the asset, given where rates are right now, they're more likely to go for a fixed rate 10-year mortgage where your – the rate is a little bit higher than floating rate today, but you've taken any of the interest rate risk out of the loan as it goes forward. And in that case, obviously we're booking a full MSR when we originate the deal.

And so it's not so much -- I mean, it's very difficult to tell because our origination platform today has access to some clients that quite honestly Walker & Dunlop had worked at for years to try and break into. And...

Brandon B. Dobell

Analyst, William Blair & Co. LLC

Okay.

Q

Willy Walker

Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.

And vice versa. There are some historic Walker & Dunlop clients that CW would have loved to have had access to. So I think the bottom line is that we're blessed to have some trade originators. That's just a very, very big client. It really is dependent on where the client's motivation is at this time in the cycle and then also where rates are. I mean, if rates are to move and people see rates moving, people are going to go to fixed much quicker than they are to a – to an adjustable rate mortgage, but today given where rates have stayed, there are a lot of people looking at those two and some people are opting like those two deals that Debbie mentioned in Q3, they're opting for adjustable rate mortgages.

A

Brandon B. Dobell

Analyst, William Blair & Co. LLC

Okay. And then final one, maybe a quick one for Debbie. Any sense on kind of where capital spending and/or operating cash flow with those two should look like for 2013 at this point?

Q

Deborah A. Wilson

Chief Financial Officer, Treasurer and Executive Vice President, Walker & Dunlop, Inc.

We have not yet – we've not done our cash flow analysis completely for 2013. So we don't know that yet. We don't expect to have huge capital expenditures though.

A

Brandon B. Dobell*Analyst, William Blair & Co. LLC*

Q

All right. Okay. Appreciate it. Thanks a lot.

Deborah A. Wilson*Chief Financial Officer, Treasurer and Executive Vice President, Walker & Dunlop, Inc.*

A

You bet.

Operator: And we'll go next to the side of Cheryl Pate with Morgan Stanley. Go ahead. Your line is open.

Cheryl M. Pate*Analyst, Morgan Stanley & Co. LLC*

Q

Hi, good morning. I just wanted to touch on the servicing margin, and looking at the legacy Walker & Dunlop portfolio, obviously has remained very steady. And then I guess my question is more, when I'm looking at the CWCcapital, when we had the presentation back in September, it was, I think, 18 basis points as of June 30 and then 21 basis points on August 31. Was there anything really different that sort of shifts the mix there? And I guess, how should we think about the sustainability of that increase going forward?

Deborah A. Wilson*Chief Financial Officer, Treasurer and Executive Vice President, Walker & Dunlop, Inc.*

A

Cheryl, it's Debbie. Good question. What you'll notice between the two presentations are two things. One is the balances in the earlier presentation were higher and the servicing fee was lower. So the portfolio required was actually smaller, but it had a higher servicing fee. And the reason is is because CWCcapital sold about \$3 billion plus of CMBS servicing with a very low servicing fee, which decreased the balance, but increased the servicing fee rate. So it's started to look much more like the servicing fees associated with our historic portfolio.

Cheryl M. Pate*Analyst, Morgan Stanley & Co. LLC*

Q

Okay. Great. That's helpful. Thank you.

Deborah A. Wilson*Chief Financial Officer, Treasurer and Executive Vice President, Walker & Dunlop, Inc.*

A

You bet.

Operator: [Operator Instructions]

Deborah A. Wilson*Chief Financial Officer, Treasurer and Executive Vice President, Walker & Dunlop, Inc.*

A

[indiscernible] (44:31)

Operator: We'll go next to the side of Mike Widner with Stifel Nicolaus. Go ahead. Your line is open.

Michael R. Widner*Analyst, Stifel, Nicolaus & Co., Inc.*

Q

Hey, good morning, guys. I guess two questions, thinking more broadly and looking really at slide four of the slide presentation. You mentioned down at the bottom in the strategic outlook \$3 billion to \$5 billion annually through other capital markets channels. I guess the first simple question is, is that in addition to the \$8 billion to \$10 billion you kind of referenced for 2013 above or is that – I know it's kind of just rough guidance, but I mean, is that included in that number or would that be potentially in addition to that number? And how are you thinking about kind of what the biggest opportunities there are?

Willy Walker

Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.

A

Yeah, it's in the number, Mike. Good morning by the way.

Deborah A. Wilson

Chief Financial Officer, Treasurer and Executive Vice President, Walker & Dunlop, Inc.

A

Hi, Mike.

Willy Walker

Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.

A

It's in the number. And as I said, we're looking to originate \$3 billion to \$5 billion over the next couple of years. So we're still executing on our plan to build that up. As you know, we added teams in Wisconsin and Florida in Q2 of this year. They've hit the ground running and are doing fantastic origination work right now, but the capital markets growth is built into 2013, \$8 billion to \$10 billion guidance.

Michael R. Widner

Analyst, Stifel, Nicolaus & Co., Inc.

Q

Got you. And so when you say other commercial property types, the other geographic locations, I guess, but the other property types, I mean what – hey, just so we can get a sense of kind of what markets you might be expanding into, I mean, where do you see the greatest opportunity and where do you just see the greatest traction kind of in the near term?

Willy Walker

Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.

A

So to try and lend on a low leverage Class A office building in Washington D.C. or New York is not a space that Walker & Dunlop will be able to lend on because that is dominated by life insurance companies and CMBS, and in some instances, banks where it's either a short-term loan or it's a construction loan. And so just given our cost to capital and the competitive set, those are not assets that likely you'll see us lending on.

What you will – the opportunity for us is on assets that are either transitional where they are in lease-up, whether it'd be a suburban office building, whether it'd be a retail center. The other opportunities will be potentially in hospitality. The hotel market has been one that banks and life insurance companies have steered away from because it's really more of an operating business than it is a real estate lending operation, if you will. And if you can underwrite it and understand the asset and understand the operator, hospitality is a great space to put money out.

And then finally in the multifamily space, there are plenty of places in the capital stack, if you will, where Walker & Dunlop presently does not lend. And so we are typically doing, as you know, first trust mortgages, generally speaking, low leverage deals and on very stabilized properties. And so as we've discussed before and what we are doing with our interim loan fund is taking deals that are either in lease-up or are on acquisition and then a

rehabilitation to then go and lease them up again, we're making loans there. And then as well we can also move up the capital stack and potentially look at either higher leverage or mezzanine opportunities. So given the access to deal flow, given our relationships with borrowers particularly in the multifamily space, we feel very good heading in that direction in the future.

Michael R. Widner

Analyst, Stifel, Nicolaus & Co., Inc.

Q

Great. Appreciate that. I'm going to come back to that in a second. Let me ask, sure, the second broad one though. Last bullet point on that page, you mentioned identifying capital solutions, mortgage REITs institutional funds et cetera. Just wondering if you can elaborate a little bit on sort of what you mean by that and how that would potentially fit in with Walker & Dunlop from an earning standpoint or structure standpoint or how should we think about the opportunities there?

Willy Walker

Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.

A

So Mike, we've talked previously about the fact that we are out marketing to raise a debt fund, and that's what I call sticky capital, going out to institutional investors, investing large slugs, if you will, \$10 million, \$20 million into a \$100 million fund, which will have moderate leverage on it and you use that fund to lend on commercial properties. That, as you know, takes a lot of time to raise that capital, but once you've raised it, it's around for the fund life, which may be seven years to ten years and the nice part about it is that it's sticky capital. It stays.

The next that we've discussed before is a mortgage REIT, and that would be a remotely managed mortgage REIT where Walker & Dunlop would be the manager of the REIT. We would raise probably \$100 million to \$200 million out of the gate, likely by securities with that and then potentially have the ability to put whole loans into the mortgage REIT at the – at anytime we want to. We could then potentially securitize loans out of the REIT, if we see the opportunity to do so.

As you know very well because you cover a number of them, mortgage REITs recently have not exactly been investors' top choice. The bottom line there is that regardless of what the market conditions are, I think from a strategic standpoint, it might be very valuable to Walker & Dunlop to have a remotely managed mortgage REIT.

The other thing though is that mortgage REITs, when you really want the capital to be able to do great deals, the capital isn't there. So it's not, if you will, sticky money. And so it has obviously pros and cons to going down that path.

The final is CMBS. The CMBS market is coming back. There is no doubt about it. I would take a guess that we'll do somewhere between \$40 billion and \$50 billion of CMBS this year in the market overall. When I say we, I'm saying the market, not Walker & Dunlop. And the opportunity for us, given our access to a huge amount of multifamily, but also access to other asset classes as we grow at our capital markets business, to pool \$100 million, \$200 million dollars of commercial mortgages and then contribute those mortgages to larger securitizations run by either the big Wall Street investment banks or commercial banks is something that we've looked at and we've started discussions along those lines.

And as you well know, CMBS is a business where you need to be able to make big bets and have a big balance sheet to be able to both make big profits and also potentially big losses, if you're on the wrong side of where the market moves. Walker & Dunlop has no intention of taking those types of big bets. We don't have the balance sheet to do it. So the only way for us to play in that space today is to take significantly smaller bets, which would

be pooling \$100 million, \$200 million, not the billions of dollars that you need to be able to do full issuances and then contributing those loans to somebody else's issuances.

Michael R. Widner

Analyst, Stifel, Nicolaus & Co., Inc.

Q

I appreciate all those comments and it sounds like you've got a lot of options out there. Let me ask one more, if I could. Just sort of super big picture level, you step back and look at Walker & Dunlop post IPO, one of the allures to investors for forgetting your stock was the growth opportunity, and historically they can look back at kind of 15% to 20% growth in originations, earnings et cetera. And you know the allure was there is not a whole lot of places in financial services these days to get growth company that had a runway for a lot of that type of growth ahead as well as a track record of that behind.

With the CW acquisition, you substantially grew and then once you've got a much greater – much larger base, obviously it's hard to grow the core business and sustain a 15% to 20% kind of growth rate on top of that. So from the standpoint of a shareholder thinking about where the growth opportunity is here, particularly from an earnings perspective, on the one hand, doubling your size makes it a lot harder; on the other hand, you're a much larger platform and now you're talking about a lot of things that were – sort of seemed very distant possibilities in the future, but now seem like they might be closer.

So with that sort of thing in mind, how do you feel about the 15% to 20% kind of growth or the overall ability to grow the company now relative to when you IPO-ed and before you did CW? I mean, you're more excited today – I mean, obviously you're more excited today, that's – right. I mean, in terms of the growth, I mean, should investors still consider you guys to be, obviously, still a growth company, but with the 15% to 20% kind of threshold in mind, I think a question a lot of people wrestle with is, is that a more difficult hurdle now or is that actually an easier hurdle now, and because of the possibilities this opens up to you versus just being hard to grow on a larger base?

Willy Walker

Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.

A

Mike, I think it gets easier, but given that I haven't run this company from, if you will, \$250 million of revenues to \$1 billion of revenues, but have run it from \$50 million of revenues to \$250 million of revenues, the – I think that as we gain scale, it actually becomes easier. And the reason is that you sort of get to a tipping point where originators want to join a fast-growing platform and as we pick up more and more market share, they understand the benefits of that; the brand gets far more widely understood and known.

As you know, if I showed – if you went home and showed someone in your household list of the top 20 commercial real estate lenders in the United States, I'm pretty sure that 15 to 19 of the names on that list are sort of household brand names and then there is Walker & Dunlop, which unless you are in our space, you probably don't know the brand. And so I think as we continue to grow our geographic footprint, as we continue to grow as it relates to our market presence and as we expand in other real estate asset classes, that the growth can actually accelerate upon itself.

I think the other thing is that now that we are the number one Fannie Mae DUS lender and the number three Freddie Mac Seller/Servicer, to be sort of 1A at Fannie Mae, we clearly want to continue to grow that business, but what we have looked at as a management team is that if you just take what we do today and sort of grow it exactly as it looks today over the next five years, our market share with Fannie and Freddie and HUD is so huge that there is no way you'd have over a 50% share of Fannie Mae's business or a Freddie Mac's business or a HUD's business.

And so one of the things that I think is very insightful to our management team is that our diversification is key to our future growth. And that doesn't in anyway mean that we don't love our core business in the multifamily space and want to remain as one of the dominant providers of capital to multifamily. And I would also reiterate my points about the agencies that I'm feeling better about the agencies today than I have in a while, and as you know, Mike, as we've talked about it, I felt pretty good about the agencies for quite some time or the future of them.

But with all that said, I do believe that things can accelerate from here and not actually slow down. I think at the end of the day, it's really the management team. It's having great people. And as we have continued to grow, we've been able to attract great people and keep great people at this company. And given that the only thing that differentiates our money from someone's else – someone else's money is the people at the company. That's really the key to our success.

And so I'd just make one final point, which is that winning the – one of the – we were the number seven on the list of Great Places to Work by the Great Places to Work Institute this year. I think that says a lot about Walker & Dunlop and where we are at this space because we are a people business and so winning that award really says a lot about what this company is like, what the culture is like and how talented our people are.

Michael R. Widner

Analyst, Stifel, Nicolaus & Co., Inc.

Q

Well, as always, appreciate all that. And I guess I'd say congratulations on getting the acquisition done, congratulations on your 75th birthday and congrats on a solid quarter. Thanks, guys

Willy Walker

Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.

A

Thanks, Mike.

Deborah A. Wilson

Chief Financial Officer, Treasurer and Executive Vice President, Walker & Dunlop, Inc.

A

Thanks, Mike.

Operator: There are no further questions at this time. I'll turn the floor back over to Mr. Walker for any closing remarks.

Deborah A. Wilson

Chief Financial Officer, Treasurer and Executive Vice President, Walker & Dunlop, Inc.

A

Yeah. Will Marks asked earlier about the CWCcapital volumes through August and that number is \$2.3 billion. Willy?

Willy Walker

Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.

A

I love it when I'm right. So thank you for that clarification, Debbie.

Deborah A. Wilson

Chief Financial Officer, Treasurer and Executive Vice President, Walker & Dunlop, Inc.

A

Yeah.

Willy Walker

Chairman, President and Chief Executive Officer, Walker & Dunlop, Inc.

As I said at the top, it is a special day for our company. There aren't too many firms that have been around for 75 years and we are thrilled to be one of them. And I would just say that it's an honor to work with the team that we have at W&D today and it's also been true pleasure to welcome everyone from CWCcapital into Walker & Dunlop and have these two firms come together as, I guess seamlessly is probably the proper term, or as quickly as they have. And so to all of you on the call this morning, thank you for your interest in Walker & Dunlop and your coverage of us. And have a great day.

Operator: Thank you. This does conclude today's conference call. Please disconnect your lines at this time. And have a wonderful day.

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