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# EDITED TRANSCRIPT

CBG - Q4 2017 CBRE Group Inc Earnings Call

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## OVERVIEW:

Co. reported 2017 adjusted EPS of \$2.71. Expects 2018 adjusted EPS to be \$3.00-3.15.



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## CORPORATE PARTICIPANTS

**Bradley Kenneth Burke** *CBRE Group, Inc. - Head of IR*

**James R. Groch** *CBRE Group, Inc. - CFO and Global Director of Corporate Development*

**Robert E. Sulentic** *CBRE Group, Inc. - CEO, President and Director*

## CONFERENCE CALL PARTICIPANTS

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

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**Greg Michael McGinniss** *UBS Investment Bank, Research Division - Associate Analyst*

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## PRESENTATION

### Operator

Greetings, and welcome to the CBRE Fourth Quarter Earnings Call. (Operator Instructions) As a reminder, this conference is being recorded.

It is now my pleasure to introduce your host, Brad Burke, Investor Relations. Thank you. You may begin.

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### Bradley Kenneth Burke - *CBRE Group, Inc. - Head of IR*

Thank you, and welcome to CBRE's Fourth Quarter 2017 Earnings Conference Call. Earlier today, we issued a press release announcing our financial results and it is posted on our website, [cbre.com](http://cbre.com). On the Investor Relations page of our website, you will find a presentation slide deck that you can use to follow along with our prepared remarks. This presentation contains forward-looking statements. These include statements regarding CBRE's future growth momentum, operations, market share, business outlook and financial performance expectations. These statements should be considered estimates only, and actual results may ultimately differ from these estimates. For a full discussion of the risks and other factors that may impact these forward-looking statements, please refer to our fourth quarter 2017 earnings report furnished on Form 8-K and our most recent annual report on Form 10-K.

During our remarks, we may refer to certain non-GAAP financial measures, as defined by SEC regulations. Where required by these regulations, we have provided reconciliations to what, we believe, are the most directly comparable GAAP measures. These reconciliations, together with expectations of these measures, can be found within the appendix of this presentation. Additionally, all growth rate percentages cited in our remarks are in local currency, unless otherwise stated.

Please turn to Slide 3. Participating on our call today are Bob Sulentic, our President and Chief Executive Officer; and Jim Groch, our Chief Financial Officer and Head of Corporate Development.

Now please turn to Slide 4, as I turn the call over to Bob.



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### **Robert E. Sulentic** - *CBRE Group, Inc. - CEO, President and Director*

Thank you, Brad, and good morning, everyone. Our fourth quarter results capped another excellent year for CBRE, with fee revenue up 9% in local currency and adjusted EPS up 6%. Our performance significantly exceeded the expectations we discussed on our third quarter earnings call. Our fourth quarter growth was led by occupier outsourcing, which produced its strongest rate of fee revenue growth since we acquired Global Workplace Solutions over 2 years ago and leasing, which also posted a double-digit revenue increase.

For the year, revenue and earnings reached all-time highs. Our full year adjusted EPS of \$2.71 represented an 18% increase over 2016. This makes 2017 our eighth consecutive year of double-digit adjusted earnings growth. And as we'll discuss in a few minutes, we expect double-digit earnings growth again in 2018.

Please turn to Slide 5. We made important strategic gains across the company in 2017. I'll highlight a few. First, our Americas property sales and leasing businesses both meaningfully outperformed the broader market in 2017. These market share gains were driven by focused efforts to build the global capabilities of our capital markets business and to drive the connectivity between our outsourcing and leasing businesses.

On data and technology, we added significantly to our digital talent base through recruitment and M&A. We have developed and are executing digital roadmaps for each of our lines of business, allowing them to continue introducing commercially focused technologies that are enhancing client outcomes. One example is our recently announced workplace experience service, CBRE 360, which is supported by a variety of digital tools to meet the rapidly rising demand for occupancy strategies that boost employee morale and productivity.

Through our Client Care program, we quantify the quality of the outcomes we are delivering for clients. We are making a big investment in this effort across the globe, and it has resulted in measurably higher client satisfaction, most notably in our global occupier outsourcing and Americas leasing business and in our EMEA and Asia Pacific businesses. We believe these efforts are now clearly contributing to our financial results.

We also executed a highly targeted M&A strategy with a focus on adding capabilities rather than scale to drive client outcomes. Jim will provide some detail on these efforts.

Finally, we added significantly to our talent base, both market-facing producers and leaders who are responsible for driving the business. We had one of our best years ever for producer recruiting, adding hundreds of producers globally, net of departures. These gains and others would not be possible without the efforts of our more than 80,000 people around the world. Their determination to deliver great outcomes for our clients helps to drive the kind of robust performance you have seen from CBRE consistently over the past several years.

Now Jim will take you through some highlights of our financial performance for the year and the quarter.

### **James R. Groch** - *CBRE Group, Inc. - CFO and Global Director of Corporate Development*

Thanks, Bob. Please turn to Slide 6. I'd like to highlight a handful of takeaways from our results. Performance for the fourth quarter exceeded our expectations, led by occupier outsourcing and leasing. Our occupier outsourcing business achieved 17% growth. Our leasing business had an outstanding December, resulting in 11% revenue growth for the quarter.

We were pleased with our margins for the quarter and the year in our regional services businesses, with fee revenue margins increasing 28 basis points for the full year, despite a decline in Q4. The shift in our business mix to more contractual services accelerated in Q4, as we experienced 17% fee revenue growth in our occupier outsourcing business.

In Q4, our consolidated fee revenue margin was 19.7%. The margin in our regional services business stood at 18.7%, which, despite a decline from an exceptional Q4 2016, remained well above our historical average for the fourth quarter.



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As Bob mentioned, we increased our pace in M&A activity this year, as more rational deal terms returned to the market. We acquired 11 companies globally, including those operating in Investment Management, project management, retail advisory, tech-focused brokerage as well as 2 real estate Software-as-a-Service companies. These capabilities enhanced our strategic position and long-term organic growth rate. In 2017, organic fee revenue grew 7%.

CBRE ended the year in the strongest financial position in the company's history. With low leverage, high liquidity and considerable free cash flow, CBRE is well positioned to make opportunistic investments when available, while weathering any market turbulence.

Please turn to Slide 7, which summarizes our financial performance in Q4 by line of business. I'll highlight a few points about the quarter and the year.

First, outperformance in leasing in the quarter was driven by our occupier outsourcing clients. While our leasing business can fluctuate quarter to quarter, the combination of our traditional leasing advisory business with our occupier outsourcing business is a real differentiator for CBRE and is expected to support continued market share gains over the long term.

Second, as Bob noted, our Americas property sales business gained meaningful market share for the full year, despite an 8% revenue decline in the fourth quarter that was more in line with the broader market. In 2017, our market share increased by 80 basis points to 17%, almost double the market share of our closest competitor according to Real Capital Analytics.

Our EMEA business continued its strong growth with sales up 20%, supported by foreign capital inflows. In Asia Pacific, we posted a healthy quarter for property sales, as the 8% decline followed a 35% increase in the fourth quarter of the prior year.

Commercial mortgage origination revenue rose 5% for the quarter, on top of the 36% growth posted in Q4 of the prior year. Loan volume growth remained healthy in Q4 with conduit lenders leading the way on higher CMBS activity.

Finally, I'd highlight the 30% increase in Q4 revenue generated from our \$174 billion loan servicing portfolio. This business has annuity-like revenues and we have been focused on supporting its growth.

Slide 8 highlights our occupier outsourcing business, which saw fee revenue increased 17% for the quarter and 12% for the full year.

New business activity also remained robust in Q4 with a record number of new and expanded contracts. We were particularly active in the health care sector with 10 total contracts, and in Asia Pac and EMEA with 21 and 28 contracts, respectively. We also signed our largest full-service outsourcing contract in Europe since 2014. The client is a global financial services company, and we will be providing them integrated facility management, project management and transaction management services.

Our pipeline in the outsourcing business has never been larger, and we are expecting solid mid-teens growth in fee revenues in 2018.

Slide 9 summarizes our Global Investment Management segment. We saw excellent sequential growth in Assets Under Management, up over \$4.3 billion in the quarter in local currency to \$103 billion on strong inflows and positive adjustments in portfolio valuations. We are benefiting from our efforts launched 1 year ago to streamline our offerings with greater focus on fewer, more strategic investment strategies.

Capital-raising continues to be strong, reflecting the solid performance of our investment programs. Total new equity commitments rose 19% in USD in 2017 to \$9.9 billion, our most ever in a single year.

Adjusted EBITDA for the full year grew by 15%, and we expect continued growth in 2018. Carried interest contributed a modest \$15 million of revenue in 2017.

Slide 10 summarizes our Development Services segment. This business achieved \$120 million of EBITDA for the full year, up 5% over prior year. The \$13 million EBITDA decline in the quarter was due to the timing of asset sales, which were significantly higher in Q4 of 2016.



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Our in-process portfolio increased by almost \$1 billion, and our pipeline declined by \$1.6 billion sequentially, with both changes driven primarily by higher-than-normal level of transfers from our pipeline to in-process portfolio. This business is well positioned with an excellent portfolio of projects and an extremely strong team, and we expect additional growth in 2018.

Please turn to Slide 11. As I'm sure you're aware, our revenue recognition accounting will change beginning in the first quarter of 2018 due to our implementation of ASC Topic 606. We anticipate little effect on our annual fee revenue, EBITDA, fee revenue margins, EPS or related adjusted results. However, under the new rules, cost of certain services provided by third parties, primarily to our occupier outsourcing clients, will be included in our cost of services and reimbursement revenue. This change is expected to increase both gross revenues and cost of services by approximately \$5 billion in 2018. Beginning in Q1 2018, prior period results will be restated to conform to the new accounting rule, providing comparability in a year-over-year reporting.

I'm sure you're also aware that we stand to benefit from changes in the U.S. tax code, and we expect our adjusted tax rate for 2018 to be in the range of 23% to 24%, as compared with 28.3% for 2017. However, in the fourth quarter, we recorded a provisional net charge of \$143 million or \$0.42 per share. This charge includes the transition tax on accumulated foreign earnings and the remeasurement of certain deferred tax assets and liabilities. We have excluded this nonrecurring item from our adjusted tax rate and adjusted earnings per share.

Finally, we plan to call our \$800 million of 5% bonds due in 2023 in March of '18. This will be funded with a combination of cash and available credit.

Now please turn to Slide 12 for Bob's closing remarks.

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### **Robert E. Sulentic** - CBRE Group, Inc. - CEO, President and Director

Thanks, Jim. Before I address our business outlook for 2018, I want to take a moment to comment on the macro environment. The global economy looks to be in solid shape. U.S. tax reform and lighter financial regulation appear to be catalysts for business investment. Domestic job growth is expected to remain strong though tempered somewhat by the tightening labor market. In 2018, we expect global leasing and investment markets to remain relatively consistent with the levels seen in 2017.

An environment where rates are steadily increasing in response to improving economic conditions is a net positive scenario for our service business. However, if rates were to increase more quickly than expected, there may be some short-term dislocation in the sales market until price discovery becomes clear.

Overall, we regard this as a supportive backdrop for our business in 2018, and we continue to operate within an industry poised for long-term growth. This is due to the 3 enduring trends we have discussed previously: the growing acceptance of outsourced commercial real estate services; the increasing capital allocation to commercial real estate as an institutional asset class; and the continuing consolidation of activity within our industry to the highest-quality, globally-diversified firms.

For 2018, we expect our leasing revenue to increase by mid-single digits, reflecting modest increases in rents and gains in market share. Capital markets, which includes our sales and mortgage origination business, combined, should achieve revenue growth of low to mid-single digits, as we expect additional share gains.

Occupier outsourcing should realize solid mid-teens fee revenue growth. As Jim noted earlier, our pipeline in this business is stronger than it has ever been.

We expect low double-digit adjusted EBITDA growth from our real estate investment businesses in 2018 with positive contributions from both Development Services and Investment Management.

We also expect a reduction in our net interest expense of approximately \$27 million, more than offset by approximately \$35 million of additional expected depreciation and amortization expense.



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As Jim mentioned, CBRE will benefit from a lower effective tax rate in 2018. These tax savings have created a great opportunity for us to invest back into our business, and we intend to take advantage of that opportunity. We will make growth-oriented investments in commercially sound technology tools as well as sales initiatives aimed at our -- at areas of our business that are well suited to benefit from those efforts. We will also pursue a host of efficiency initiatives supported by technology to take advantage of our scale. And very importantly, we will make incremental investments to provide ongoing benefits for our people, such as an enhanced 401K match and paid parental leave.

We expect adjusted EBITDA margins for full year -- for the full year of approximately 17.5%. Our margins reflect the elevated level of investment noted above and a mix shift, reflecting stronger expected growth in our outsourcing in our non-U. S. businesses. At the same time, you can expect our intense focus on costs to continue in 2018.

We expect to achieve adjusted earnings per share for 2018 in the range of \$3 to \$3.15 per share, which represents a 13% increase from 2017 at the midpoint, with an 8% increase attributable to adjusted EBITDA growth and 5% to the combined effect of lower tax rate, interest savings and higher depreciation and amortization. Without the effect of tax reform and the incremental investments we discussed, we would have expected approximately 10% adjusted EBITDA growth and double-digit growth in adjusted EPS in 2018.

With that, operator, we'll open the lines for questions.

## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions) Our first question is coming from Anthony Paolone of JPMorgan.

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

My first question is on the EBITDA margin. You talked about the mix shift and then also investing in the business. Do you see that some of those investments continuing into '19 and acting as any sort of drag on margins on a multiyear basis? Or is this, say, kind of add this to the cost structure, step it up and then that's kind of the new level?

### James R. Groch - CBRE Group, Inc. - CFO and Global Director of Corporate Development

Anthony, this is Jim. I would say majority of those investments are more recurring in nature. We would still anticipate getting operating leverage by line of business hopefully in '19 over '18.

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

Okay. And then could you give us a little more color on the acceleration in outsourcing revenue growth and where you're seeing that, either by industry or geography or business function, like, which -- it seems to be a pretty notable pickup as you head into '18?

### Robert E. Sulentic - CBRE Group, Inc. - CEO, President and Director

Tony, this is Bob. Well, we're going to see a lot of that in Europe. We think we're really well positioned there to grow the business. And we've got the GWS work behind us next year, the integration work, which was long and hard, but very fruitful. And we're expecting to see it in various verticals that we work in. So we talked earlier about health care. We're seeing at additional work with some financial services firms, a lot of work with the technology firms that ask us to do multiple services around the globe. That's become a big driver on our growth. And then one of the things we're



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really starting to see now is a lot of leasing work for these clients. So we're very encouraged about the picture. It was -- it came through in our numbers for 2017. It's going to come through again in 2018.

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

And was that, like, some of this pickup, was that visible just given that it takes time from when you win the contract to when it really starts to kick in sort of a lot of what we're going to see in '18 you kind of -- you worked on in '17? Or -- I'm just trying to think about...

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**Robert E. Sulentic** - *CBRE Group, Inc. - CEO, President and Director*

Yes. Well, these are big, complicated contracts. And so there is a ramp-up of effort before you land and actually start to work. But another thing that's going on there is we have hundreds of contracts with big global companies now and where -- a lot of our growth -- Bill Concannon talks about this all the time -- we -- a bunch of our growth comes from new accounts, but an awful lot of it comes from adding services to the accounts we have. And we talked in our comments earlier about this Client Care effort we have underway within our outsourcing business -- or occupier outsourcing business. We call that our Dark Green initiative. When you're working with these large clients and you do great work for them on one line of business or on what they've already given you, the odds of expanding that account are really, really good. We are doing increasingly good work for these clients. It's very measurable and it's definitely coming through in our growth rates. That's an absolutely important part of what you're seeing.

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

Okay. Got it. And then just last question. It looks like you'll save money on interest in '18 net of cash. But then you get some offset with D&A. Like, what's the expectation for CapEx just kind of get to cash flow picture?

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**James R. Groch** - *CBRE Group, Inc. - CFO and Global Director of Corporate Development*

Anthony, I'm trying to think. Let's see. We've got -- we're going to put -- you'll see that for -- in our 10-K coming out shortly. But it will be up slightly from '17.

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**Operator**

Our next question is coming from Jason Green of Evercore ISI.

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**Jason Daniel Green** - *Evercore ISI, Research Division - Analyst*

Just a question on the leasing environment. Wondering -- obviously, a very strong quarter. If you're seeing any hesitation in terms of doing long-term leasing deals or if people are kind of aggressive in leasing environment and thinking about doing long deals versus short deals.

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**Robert E. Sulentic** - *CBRE Group, Inc. - CEO, President and Director*

Jason, we think the leasing environment is going to be pretty stable between '17 and '18. One of the factors that's just very real out there is that employment growth causes leasing growth. And we expect -- or we're seeing a circumstance where we're getting pretty close to full employment. So that's a factor in our outlook for the amount of leasing growth we see next year or one of the reasons because as we think it's flat. But the market kind of is approaching leasing going forward, in our view, the way it did this past year.



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**Jason Daniel Green** - *Evercore ISI, Research Division - Analyst*

Okay. And then just one more question in regards to the debt, the bonds you guys are calling. Is there any prepayment penalty associated with those? Anything we should be thinking about going forward?

**James R. Groch** - *CBRE Group, Inc. - CFO and Global Director of Corporate Development*

Jason, there's a \$20 million call premium.

**Operator**

Our next question is coming from Nick Yulico of UBS.

**Greg Michael McGinniss** - *UBS Investment Bank, Research Division - Associate Analyst*

This is Greg on for Nick Yulico. Just had a couple of questions on M&A. I'm curious what some of the specific capabilities that you guys added via M&A this year were.

**James R. Groch** - *CBRE Group, Inc. - CFO and Global Director of Corporate Development*

Greg, yes. This is Jim. I'm happy to run it through with you. So really, a mix of acquisitions, different parts of the world and different businesses, but our real focus was on bringing either new or enhanced capabilities to our clients and our people serving our clients. So Caledon is an example, and our Investment Management business is a really strong group that's been totally focused on infrastructure management. We have a fund on our public security side on the infrastructure -- in the infrastructure is space. This is on the private side, so that's one example. We acquired a business called Mainstream, which is a global work order, Software-as-a-Service platform, a business and a product that we're very familiar with, as the -- as we were their largest customer. They rolled out a product. It was globally capable. We liked it a lot and thought it have a great opportunity and acquired the business. In Australia, we acquired a company called Aurora. It's a health care-focused project management basis. In France, a retail consultancy firm called Convergences. So those are a few examples. But overall, we did 11 acquisitions and equity investments in 3 additional companies.

**Greg Michael McGinniss** - *UBS Investment Bank, Research Division - Associate Analyst*

I really appreciate the color there. And have you started to see any sort of rationalization in M&A pricing that may be a bigger deal with your liquidity and they make a bigger deal potentially possible in 2018, 2019?

**James R. Groch** - *CBRE Group, Inc. - CFO and Global Director of Corporate Development*

Yes. We don't give any real guidance or color around large deals when they may or may not occur. But you can see from our history, really selective on the large deals. So of the dozen or so large deals in the last dozen or so years or more than that, we've chased 5. We've won 5 we went after. We didn't bid on any of the others. So they kind of break lose when they do. And we're always prepared for the deals that we think are particularly strategic to achieving what we're trying to accomplish.

**Greg Michael McGinniss** - *UBS Investment Bank, Research Division - Associate Analyst*

All right. And just one more question for me. You spoke on additional market share gains in 2018. I'm just curious what you considered your market share gains in 2017 in the leasing and sales businesses to have been.



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**James R. Groch** - *CBRE Group, Inc. - CFO and Global Director of Corporate Development*

Well, I'll hit the capital markets business. If you look at Real Capital Analytics, they have a us up 80 basis points for the year at about a 17% market share, which is almost double our next closest competitor. On leasing, we think that it's a -- market share gains are evident. Getting more detailed data is pretty hard to do in the marketplace.

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**Operator**

Our next question is coming from Mitchell Germain of JMP Securities.

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**Mitchell Bradley Germain** - *JMP Securities LLC, Research Division - MD and Senior Research Analyst*

I want to ask Tony's question a different way with regards to tech. Obviously, it's constantly evolving. But if you were going to place a target of where you want to be versus where you are now, how much more progress has to be made to kind of hit those goals?

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**Robert E. Sulentic** - *CBRE Group, Inc. - CEO, President and Director*

Well, first of all, Mitch, I want to create some context for how we think about technology. We're investing in it really heavily, but we are extremely focused on doing things that are commercial and enabling our real estate services capability. We've studied this closely in 2016. We studied it closely, again, in 2017. We've got a very clear view across our lines of business as to what we need to do and the tools we need to bring on board, and we're implementing that. We've ramped up the capabilities of our digital and technology leadership team and the development teams that work for them. and we think that it's going to be important across all of our lines of business. But it's going to be important that we enable ourselves with technology. We aren't thinking that we're going to be disintermediated. We're watching that risk very closely as it relates to the small trades and some other parts of our business. But in general, it's about enabling ourselves with technology. And we expect to continue to ramp up our expenses. I will tell you that our -- if you were to dissect our income statement and our budget for 2018, you would find that one of the biggest areas of growth is in the whole digital and technology area.

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**Mitchell Bradley Germain** - *JMP Securities LLC, Research Division - MD and Senior Research Analyst*

Great. That's helpful. I know you are talking about low to single -- low to mid-single-digit growth capital markets. Obviously, there are 2 real big streams there, right? One is investment sales. One is your commercial financing side. How do -- how should we think about each one of those respective segments as you roll up into that guidance?

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**Robert E. Sulentic** - *CBRE Group, Inc. - CEO, President and Director*

Sales is going to grow a little more slowly than debt. There's some concern in the sales market, obviously, about the -- about what might happen with interest rates. The other thing is buyers are underwriting assets. They're having a little bit of trouble underwriting growth and values. So we think sales are -- will grow a little more slowly than debt. And as result of the slower growth in sales, some people will refinance, which will cause the debt side of things to grow more rapidly. But we look for that low to mid-single-digit type growth next year. Significant amount of it come from taking market share.

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**Mitchell Bradley Germain** - *JMP Securities LLC, Research Division - MD and Senior Research Analyst*

Got you. Smart move to pay down the debt. Is the thought to maybe refinance the portion that will sit on the line for kind of longer term? Or like we just kind of sit on the line for a little time now?

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**James R. Groch** - *CBRE Group, Inc. - CFO and Global Director of Corporate Development*

So in October, when we refinanced our line, we also refinanced \$750 million of term loans. What we did there is we actually -- we only drew \$250 million of the \$750 million of term loans. And we negotiated the delayed draw feature on the remaining \$550 million, actually, which will take down roughly simultaneous to when we call the bonds. And so it won't -- not -- a little, if any, will really sit on the line of credit. And the term loans are 5-year and pre-payable at any time with no penalties.

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**Operator**

Our next question is coming from Jade Rahmani of KBW.

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**Jade Joseph Rahmani** - *Keefe, Bruyette, & Woods, Inc., Research Division - Director*

Just a follow-up on the debt repurchase. How much would you say the allocation is between cash and the term loans? Should we assume that you'll draw down the entire capacity on the term loans?

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**James R. Groch** - *CBRE Group, Inc. - CFO and Global Director of Corporate Development*

Yes, we'll draw down the capacity at the time we take it down, but it's somewhat fungible. Our first 2 quarters are seasonal period where we use a little more cash. So we'll take down the full term loans. There's no -- like I said, there's no pre-penalty, so we may decide to pay that down a bit as early as the end of the year. We'll see how things evolve throughout the year.

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**Jade Joseph Rahmani** - *Keefe, Bruyette, & Woods, Inc., Research Division - Director*

Just on the -- you mentioned interest rates. I wanted to see if you could comment on any initial trends, so far, in 2018. Are you hearing any feedback from your sales force or clients about increased concern with respect to the interest rate outlook as some of the recent stock market volatility appears to reflect?

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**Robert E. Sulentic** - *CBRE Group, Inc. - CEO, President and Director*

Well, we stay very close to the buyers of institutional real estate assets. And what we're hearing from them is what we've seen in the stock market. We're hearing from them some level of concern. They're not overwhelmingly concerned, but they're watching it closely. And they think there's more reason to watch it now than there has been for several years. So that's on their mind. And that's -- as I commented earlier, that's one of the reasons why we don't think there'll be a real growth in sales volumes this year in an otherwise good economy, I might add.

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**Jade Joseph Rahmani** - *Keefe, Bruyette, & Woods, Inc., Research Division - Director*

And in terms of seasonality, as a follow-up, do you think that those types of conversations could cause initial deal closings to slip beyond 1Q? So could you see the softness in capital markets play out perhaps stronger in the earlier part of the year on heightened concern, but then people maybe adapt to that?

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**James R. Groch** - *CBRE Group, Inc. - CFO and Global Director of Corporate Development*

Yes. Jade, this is Jim. I would say you can look back in the last couple of years and see periods where the tenured treasuries have moved around a good bit between 2% and 3% and generally didn't have much impact on cap rates, generally didn't have much impact on volumes. If the rates



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move more quickly or kind of a surprise than expected, then you can get a little bit of messiness in a quarter where people kind of wait for price discovery to clear up a little bit. But overall, I think our guidance is based on what we've seen in the last month or 2, including the last few days.

### Operator

Our next question is coming from Stephen Sheldon of William Blair.

### Stephen Hardy Sheldon - William Blair & Company L.L.C., Research Division - Associate

First, just given the guidance for momentum to continue in occupier outsourcing in 2018, is that more weighted towards the first half of the year just given the tougher comps as you progress through the year? And does the mid-teens guidance only include contracts currently in the pipeline? Or does it factor in kind of additional growth in the pipeline?

### James R. Groch - CBRE Group, Inc. - CFO and Global Director of Corporate Development

It's our guidance just based on our expectation for the year. An awful lot of those revenues are reasonably well baked at this point. But some -- there is some timing that we're estimating based on contracts that we've landed or in process as to our estimate as to when they will actually come online. But we've got -- as I commended during the call, it's the strongest pipeline we've ever had. And we feel pretty confident about the mid-teens guidance. And we don't really expect that to be particularly weighted to the back half of the year, whereas in '17, we did give our guidance that it was going to be a little bit more weighted to the back half of the year. And we met that guidance obviously and exceeded it a little bit.

### Stephen Hardy Sheldon - William Blair & Company L.L.C., Research Division - Associate

Okay. And then I think you noted a large occupier outsourcing win in EMEA in the fourth quarter. Did you see any revenue flow in from that? Or is that going to be incremental as we look at EMEA occupier outsourcing in 2018?

### James R. Groch - CBRE Group, Inc. - CFO and Global Director of Corporate Development

Very little would have hit, so far, on that contract. There's usually a pretty good lead time to get these contracts up and running.

### Stephen Hardy Sheldon - William Blair & Company L.L.C., Research Division - Associate

Okay. And then, yes, I appreciate the color on the expected growth kind of by service line. I just wanted to make sure, are the revenue growth rates you give generally kind of constant currency? Or did they factor in a potential boost from FX trends this year?

### James R. Groch - CBRE Group, Inc. - CFO and Global Director of Corporate Development

Yes. We've got maybe a little over 1% boost in our -- that's baked into our budget for FX. But we'll -- typically, when we're setting the budget, we're looking -- when we set our budget, we're looking at forward curves on exchange rates. And so we've got some of that baked in already.

### Operator

Our next question is coming from David Ridley-Lane of Bank of America Merrill Lynch.



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

Wanted to ask about the impact of U.S. tax reform, not on you, but on your own clients. I mean, the 20% deduction on pass-through income would seem like a pretty meaningful benefit to CRE investments on through LLCs and the like. Has that factored into the psychology around buyers and potentially increase the activity levels or prospectively would?

**Robert E. Sulentic** - *CBRE Group, Inc. - CEO, President and Director*

Well, the -- as has been broadly publicized, the changes in the tax code were generally good for commercial real estate. As it relates to our clients, I think it's a good thing for them. I think other large corporates like ourselves are going to be more profitable as a result. They're going to have more dollars to invest as a result. I think their view of the economy and how long it's going to run in a positive way has been enhanced by the changes to the tax code. And as a result, they'll be more inclined to do positive things at employees and so forth to benefit our business. And when you look at the size of our business on both sides, the occupier side and the investor side, I think we'll get -- we should get positive benefit from both sides.

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

Understood. And then on the 2018 guidance, the double-digit EBITDA growth that you're guiding for the principal business of Investment Management and development, are you expecting an above-average year for asset sales and incentive fees? Or is this kind of driven by more core growth in the projects and Assets Under Management?

**James R. Groch** - *CBRE Group, Inc. - CFO and Global Director of Corporate Development*

I'd say kind of all the above, really. Both businesses are doing well. The Development Services business has a very strong set of projects in process, also a very strong pipeline. The Global Investment -- and I'd say not a particularly unusual year for asset sales in that business. The global investors business, our Investment Management business also doing quite well with a record year for capital rates, AUM at a record level as well. So they're both kind of solid fundamentals of both businesses. And we expect that both will be up in low double digits.

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

If I could sneak one more in. I know you have a -- don't have a formal net debt to EBITDA leverage target and understand that you are mindful of where we are in this cycle, but is there a level of which you would feel that you're potentially underlevered? I mean, you are under 1x now.

**Robert E. Sulentic** - *CBRE Group, Inc. - CEO, President and Director*

Yes. As we commented in the past, we try to be explicit that we are comfortable being what you might call underlevered, as you relayed there, in a business cycle. And we're comfortable with higher leverage earlier in a business cycle. And we're comfortable moving in a band that materially differentiates between later in the cycle and earlier in the cycle. We -- you won't see us go below 2.0 net leverage late in the cycle. But we -- yes, I guess, I'll just restate what I -- what we said in the past on that front.

**Operator**

Our next question is coming from Jason Weaver of Wedbush Securities.



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**Jason Price Weaver** - *Wedbush Securities Inc., Research Division - SVP and Senior Equity Research Analyst*

Just on the guidance for your EBITDA growth, generally -- sorry, guys. I was just asking about the EBITDA guidance figures. Does that include any impending or anticipated growth from acquisitions? Or is that all organic expectation?

**James R. Groch** - *CBRE Group, Inc. - CFO and Global Director of Corporate Development*

It's most -- it's really almost entirely inorganic. So any infill M&A that we do within a calendar year typically contributes very little, if any, incremental earnings in that year because we don't normalize the deal costs, startup costs, integration, et cetera, of the smaller deals. We consider that normal course activity for us. So yes, we'll get some revenue contribution, but not much earnings.

**Jason Price Weaver** - *Wedbush Securities Inc., Research Division - SVP and Senior Equity Research Analyst*

And one more. Bob touched on this in his remarks. But can you comment a little bit more granularly on the recruitment environment for producers, both in the regions and if you think competition is intensifying it all?

**Robert E. Sulentic** - *CBRE Group, Inc. - CEO, President and Director*

We don't think competition is intensifying. It's probably backed up a little bit in a positive sense over the last year. Well, let me rephrase that. It certainly has backed up a little bit in a positive sense. We are having meeting with a lot of success in recruiting around the world. And the reason we're meeting with a lot of success is because producers realize they can come to our company and through a combination of our footprint, the client base we have, the range of services we have that they can leverage to land transactional business. They can do more here than they can do elsewhere. And as a result, we ended up with a recruiting year in 2017 that was better than we expected going into the year. It was one of our better years. It's one of the things that's contributing to our assumptions about taking some market share next year. And that is -- that's become a continuing theme and opportunity for us, and we expect that to happen again in 2018.

**Operator**

Our next question is coming from Jade Rahmani of KBW.

**Jade Joseph Rahmani** - *Keefe, Bruyette, & Woods, Inc., Research Division - Director*

I was wondering if you could provide adjusted earnings and adjusted EBITDA excluding net MSR gains.

**James R. Groch** - *CBRE Group, Inc. - CFO and Global Director of Corporate Development*

Sure. Well, I'll just give you the net MSR impact. And for those that are not familiar to MSR, it's referred to kind of gains from mortgage servicing rights offset by amortization of those gains. The impact -- so these are all headwinds, net headwinds. The impact in Q4 was about \$6 million negative or roughly \$0.01. The impact for the full year was around \$33 million of headwinds, negative impact around \$0.07 for the year. And in our budget for '18, we expect about \$20 million of headwind where amortization exceeds the gains.

**Jade Joseph Rahmani** - *Keefe, Bruyette, & Woods, Inc., Research Division - Director*

Is the headwind a year-over-year comparison? Or is the headwind that...



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**James R. Groch** - *CBRE Group, Inc. - CFO and Global Director of Corporate Development*

Year-over-year.

**Jade Joseph Rahmani** - *Keefe, Bruyette, & Woods, Inc., Research Division - Director*

Okay. But on an absolute basis, mortgage servicing capitalization gains exceeds the amortization expense.

**James R. Groch** - *CBRE Group, Inc. - CFO and Global Director of Corporate Development*

That's correct.

**Jade Joseph Rahmani** - *Keefe, Bruyette, & Woods, Inc., Research Division - Director*

So do you happen to have what the impact -- what the gain on sale from mortgage servicing rights was and what the amortization expense was so that we could calculate cash earnings and adjusted EBITDA excluding that?

**James R. Groch** - *CBRE Group, Inc. - CFO and Global Director of Corporate Development*

Sure. We'll give the full detail on the K, but the net in '17 was about \$50 million.

**Jade Joseph Rahmani** - *Keefe, Bruyette, & Woods, Inc., Research Division - Director*

And do you know what it was in the fourth quarter?

**James R. Groch** - *CBRE Group, Inc. - CFO and Global Director of Corporate Development*

I don't have that off the top of my head, but...

**Operator**

Our next question is coming from Patrick O'Shaughnessy of Raymond James.

**Patrick Joseph O'Shaughnessy** - *Raymond James & Associates, Inc., Research Division - Research Analyst*

So when we see some sales dislocation because of a spike of rates, like, it sounds like we might be seeing in the very near term, do you typically see that leading to the permanent loss in that sales activity that might have otherwise taken place? Or does it just kind of push it back and then when rates normalize or the environment calms down, there's a little bit of a catch-up that takes place?

**Robert E. Sulentic** - *CBRE Group, Inc. - CEO, President and Director*

Yes. What happens -- I mean, it depends on how much it spikes. If it's -- if interest rates spike a little bit, we don't think it'll have much of an impact at all. If they spike more, then people will go to the sidelines to wait and see what happens. But there is an awful lot of debt and equity capital out there in the market for commercial real estate. And our belief is that with what's likely to happen with interest rates, it's not going to have a big impact on the market in 2018.

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**Patrick Joseph O'Shaughnessy** - *Raymond James & Associates, Inc., Research Division - Research Analyst*

All right. And I think you'd kind of lead in my next question, which is that there's a lot of private equity dry powder out there geared towards real estate investments. How patient is your sense of that dry powder can really be?

**Robert E. Sulentic** - *CBRE Group, Inc. - CEO, President and Director*

I think they can be very -- look, I think that the institutional investors in real estate are pretty darn disciplined now more than they have been in any cycle in my 30-plus year career. And they're inclined to hold the assets they have. If they don't think they can get good pricing and they're happy to sit on the capital they have, if they don't like the buys they can make, we have a big Investment Management business. That's exactly how our guys and gals are looking at it. I can tell you that.

**Operator**

At this time, I'd like to turn the floor back over to management for any closing comments.

**Robert E. Sulentic** - *CBRE Group, Inc. - CEO, President and Director*

Okay. Well, thanks, everyone, for your questions. We'll talk to you again in 90 days. And in the meantime, I want to remind everybody that we have our investor day here in New York on March 8.

**Operator**

Ladies and gentlemen, thank you for your participation. This concludes today's teleconference. You may disconnect your lines at this time, and have a wonderful day.

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