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CBG - Q2 2016 CBRE Group Inc Earnings Call

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OVERVIEW:

Co. reported 2Q16 adjusted EPS of \$0.52. Expects calendar year 2016 adjusted EPS to be \$2.15-2.30.



CORPORATE PARTICIPANTS

Steve Iaco *CBRE Group, Inc. - IR*

Bob Sulentic *CBRE Group, Inc. - President & CEO*

Jim Groch *CBRE Group, Inc. - CFO*

Gil Borok *CBRE Group, Inc. - Deputy CFO & Chief Accounting Officer*

CONFERENCE CALL PARTICIPANTS

Brad Burke *Goldman Sachs - Analyst*

Anthony Paolone *JPMorgan - Analyst*

Jade Rahmani *Keefe, Bruyette & Woods - Analyst*

Brandon Dobell *William Blair & Company - Analyst*

David Ridley-Lane *BofA Merrill Lynch - Analyst*

Mitch Germain *JMP Securities - Analyst*

PRESENTATION

Operator

Greetings, and welcome to the CBRE second-quarter 2016 earnings conference call.

(Operator Instructions)

As a reminder, this conference is being recorded. It is now my pleasure to introduce your host, Steve Iaco, Investor Relations. Thank you. You may begin.

Steve Iaco - *CBRE Group, Inc. - IR*

Thank you, and welcome to CBRE's second-quarter 2016 earnings conference call. Earlier today, we issued a press release announcing our financial results for the quarter and first half of the year. This release is posted on the home page of our website CBRE.com.

This conference call is being webcast through the Investor Relations section of our website. There you can find a presentation and slide deck which you can use to follow along with our prepared remarks. An audio archive for the webcast will be posted to the website later today, and a transcript of our call will be posted tomorrow.

Now, please turn to slide labeled Forward-Looking Statements. This presentation contains statements that are forward looking within the meaning of the Private Securities Litigation Reform Act of 1995. 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.

Except for the extent required by securities laws, we undertake no obligation to update or publicly revise any forward-looking statements we may make today. For a full discussion of the risks and other factors that may impact any forward-looking statements, please refer to our second-quarter earnings report furnished on Form 8-K and our most recent Quarterly and Annual Reports on Form 10-Q and Form 10-K. These results are filed with the SEC and available at SEC.gov.



During this presentation, we may make certain statements that refer to non-GAAP financial measures as defined by SEC regulations. Where required by these regulations, we provided reconciliations of these measures to what we believe are the most directly comparable GAAP measures. Those reconciliations, together with explanations of these measures, can be found within the appendix of this presentation.

Please turn to slide 3. Participating on our call today are Bob Sulentic, our President and Chief Executive Officer; Jim Groch, our Chief Financial Officer; and Gil Borok, our Deputy Chief Financial Officer and Chief Accounting Officer.

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

Bob Sulentic - *CBRE Group, Inc. - President & CEO*

Thank you, Steve, and good morning, everyone. CBRE posted another quarter of strong growth on the top and bottom lines, with a 24% increase in adjusted EPS. This growth came amid an uncertain macro environment, and notably, a time when global property sales volumes market wide have pulled back from a robust 2015.

The diversity of CBRE's service offering is especially important in the current market environment. Our performance for the quarter was supported by strong growth in mortgage services, reflecting continued debt capital flows into commercial real estate and in occupier outsourcing, which again grew revenue strongly even before contributions from the acquired Global Workplace Solutions business.

Leasing was also up nicely in the Americas and Asia-Pacific, and our Investment Management and Development Services businesses produced solid EBITDA gains for the quarter. Jim will take you through all of this in detail shortly. Before he does, I want to address the UK's vote to leave the European Union.

Please turn to slide 5. CBRE, like the rest of the commercial real estate services industry, was affected by the high degree of uncertainty in the UK market leading up to the referendum on June 23. This can be seen in a nearly 40% drop in UK market-wide property sales volumes in Q2 according to CBRE research.

However, the effect on CBRE's UK revenue was materially less pronounced. In local currency, CBRE's total UK fee revenue increased 12%. Without the contributions from the acquired Global Workplace Solutions business, UK fee revenue in local currency was just 5% below Q2 2015, which had been up 32% over Q2 of the prior year. This performance highlights how significantly our UK business has evolved in recent years.

During the first half of 2016, occupier outsourcing and property management, which is sticky recurring revenue, accounted for 69% of UK fee revenue, versus just 19% in the first half of 2013. This shift in our UK revenue mix has been driven by our acquisitions of Norland in late 2013 and Global Workplace Solutions in September, 2015, and positions us well as the UK goes about resetting its relationship with the European Union.

Please turn to slide 6. CBRE expects continued near-term hesitancy among occupiers about space decisions in the UK, particularly London. We expect a modest increase in property yields reflecting the higher perceived risk of holding UK property. However, this increase may be temporary, especially for top-tier assets, due to the inherent attractiveness of the UK market.

In addition, the decline in the value of sterling against the US dollar should provide some incremental support for foreign investment into the UK over time. We also anticipate a delay in some office development activity, which should provide longer term support for property prices as well as rents, particularly in central London, where availability stands at just 3%.

We are monitoring Brexit-related developments closely. There is a long road ahead, but the swift resolution of the political leadership in Britain is an encouraging sign. Given our clear leadership position, CBRE is well positioned to capitalize on opportunities in the UK and across Europe. We are firmly focused on continuing to support our European business and clients.

Now, I'll turn the call over to Jim who will discuss our second-quarter results in detail.

Jim Groch - CBRE Group, Inc. - CFO

Thanks, Bob. Please turn to slide 7 for an overview of our financial results. Fee revenue rose 20% in local currency to \$2.1 billion, or 3% organic growth in fee revenue without the contributions from the acquired Global Workplace Solutions business and other M&A.

Adjusted EBITDA for the quarter totaled \$360 million, a 19% increase in US dollars from last year's Q2. Margin on fee revenue was 17%. Adjusted earnings per share increased 24%, to \$0.52 for the quarter.

Q2's results include \$4 million of net benefit to adjusted EBITDA from currency movement, including gains on hedges. This compares to a net unfavorable impact at \$14 million in the second quarter of 2015. Q2 2016 adjusted EBITDA of \$360 million includes adjustments for \$28 million of integration costs relating to the acquisition of Global Workplace Solutions and \$27 million incurred in connection with cost elimination program that we discussed in the prior two quarters.

Please turn to slide 8 regarding Q2 results for our three regional service segments, all in local currency. Fee revenue increased 18% in the Americas, 31% in EMEA, and 18% in Asia-Pacific. Without contributions from the acquisition of Global Workplace Solutions, fee revenue increased 6% in the Americas, but was essentially flat in both EMEA and Asia-Pacific.

Please turn to slide 9 for a review of our business mix. Our business mix continues to evolve towards greater contractual revenues. The Company as a whole contractual fee revenue was 44% of total fee revenue, up from 34% in Q2, 2015, and 19% in Q2, 2006.

Please turn to slide 10 for a review of our major global lines of business in Q2. All percentages increases are in local currency. Occupier outsourcing continued to exhibit strong growth. Global fee revenue was up 118%, aided by the acquisition of Global Workplace Solutions. Without contributions from this acquisition, fee revenue rose 10%.

Commercial mortgage services had a very good quarter, with revenue up 14%, led by private lenders, particularly banks, and continued growth with government-sponsored enterprises. Leasing achieved good growth in the Americas, which was up 8%, and Asia-Pacific, which rose 7%. We continue to benefit from the influx of producers choosing to join CBRE.

In the Americas, Canada, Mexico, and the US all turned in healthy performances, while Asia-Pac was led by greater China, India, and New Zealand. Leasing was down 11% in EMEA, as growth in Belgium, Germany, and the Netherlands and Spain partially offset a decline in the UK.

Property sales revenue rose 2% in the Americas, while EMEA and Asia-Pacific both declined 16%. This compares with an exceptionally strong Q2, 2015, when year-on-year growth rates were 25% in the America, 62% in EMEA, and 24% in Asia-Pacific. Q2 2016 property sales revenue in the UK declined by approximately one-third.

CBRE continued to make gains in property sales, as evidenced by our 150 basis point market share increase in the US during Q2 according to RCA. Fee revenue from property management services, which we call asset services, increased by 7%. Valuation revenue was essentially unchanged.

Please turn to slide 11 regarding our occupier outsourcing business, which we reported within the three regional service segments. Fine interest in our outsourcing remains high. This can be seen in the 96 total contracts we signed during Q2, including 37 with new clients. Notably, more than one-third of these new clients were in EMEA and Asia-Pacific, evidence that outsourcing is gaining more traction in overseas markets.

Our engagements often span multiple geographies and services. CBRE is well positioned to serve complex multi-market requirements for our clients with the acquired Global Workplace Solutions expertise firmly embedded in our outsourcing business.

Please turn to slide 12 regarding our Global Investment Management segment. Adjusted EBITDA for this business line increased to \$26 million. The business continues to attract significant capital commitments. We raised \$1.8 billion of new equity in Q2 and \$7.1 billion in the trailing 12 months.

Assets under management totaled \$88.6 billion, up \$3.9 billion from a year ago in local currency. However, all but \$200 million of this increase was offset by foreign currency movement over the past year.

Please turn to slide 13 regarding our Development Services segment. Strong performance in this business continued in Q2. Adjusted EBITDA totaled \$19 million for the quarter, while pro forma revenue, which includes gains on real estate sales, equity earnings, and non-controlling interest, increased to \$46 million.

These strong results in the quarter were helped [by] the timing of asset sales. We note that these development asset sales accounted for the vast majority of our equity earnings for the quarter. Due to the timing of project sales, we expect results for the remainder of the year to be heavily weighted to the fourth quarter, with a significantly lighter third quarter.

Development projects in process totaled \$7.1 billion, up \$1.1 billion from Q2, 2015. The pipeline of \$3 billion was down \$700 million from a year ago, as projects converted from pipeline to in-process.

Please turn to slide 14. Before I turn the call back to Bob, I'd like to briefly highlight our results for the first half of 2016. These results are strong, including growth rates of 24% in fee revenue in local currency, 17% in adjusted EBITDA, and 21% in adjusted earnings per share.

This growth is particularly notable coming at a time when average earnings of S&P 500 companies are expected to decline in Q2, 2016, for the fifth consecutive quarter.

Please turn to slide 15 for Bob's closing remarks.

Bob Sulentic - *CBRE Group, Inc. - President & CEO*

Thank you, Jim. As you have seen, our business has performed very well in the first half of 2016, even with a decline in market-wide property sales volumes compared to a year ago. It is important to note that market fundamentals in commercial real estate remain in good shape, with the impact of Brexit largely limited to property transactions activity in the UK, and we anticipate solid earnings growth for the year.

Looking ahead, we are adjusting our outlook for the remainder of the year. This is due principally to the impact of Brexit on UK property transaction volumes and less visibility around the timing of the realization of certain incentives in our Global Investment Management business and Development Services business. These factors have caused us to reduce our earnings guidance by 3% at the top end of our range and by 5% at the bottom end.

This results in expected adjusted EPS for the calendar year of \$2.15 to \$2.30, which represents solid growth of approximately 9% at the midpoint of the range. We see adjusted EPS in the second half of 2016 more weighted to Q4 rather than Q3 compared with our customary progression of earnings throughout the year.

As the clear market leader, CBRE is well positioned to further extend our competitive advantage in the marketplace. Our ongoing talent and technology initiatives, collaborative culture, market-leading service offering, and financial strength uniquely position us to satisfy clients' growing demand for our services.

With that, operator, we will open the lines for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)



Our first question comes from Brad Burke with Goldman Sachs.

Brad Burke - *Goldman Sachs - Analyst*

Hey, good morning, guys. I wanted to ask about the guidance. The initial guidance you gave us for the year indicated that leasing was going to grow high single digits; capital markets, mid to high single digits; outsourcing, low double digits; and your principal business EBITDA would be flat to slowly down. With the updated guidance that you're giving us today, can you give us an update on how those expectations have changed as they are reflected in the full-year guidance?

Jim Groch - *CBRE Group, Inc. - CFO*

Hey, Brad. It's Jim. Sure. We are not changing any of the specific guidance that we gave early in the year. Actually, I think that generally, we still anticipate all those ranges that we gave, that we'll perform within the ranges provided at the beginning of the year.

If you look at the update on our guidance at the midpoint, the range is a little wider, and at the midpoint, we are down 4%. I think as we referenced, a little more than half of that is really tied to Brexit impact on UK transactions. And then some of the widening and the bit that's left is in there around just some timing risk around the realization of incentives in our Global Investment Management and Development Services, and then just some very minor tweaks to our forecast internally.

Brad Burke - *Goldman Sachs - Analyst*

Okay. And staying with the UK, slide 5, I appreciate the detail on the UK business. Can you give us a sense of the exposure that you have within your principle businesses? While I assume there's not much for Development Services, but interested in Investment Management exposure.

Jim Groch - *CBRE Group, Inc. - CFO*

Yes. Very, very -- there is no Development Services really, and Investment Management is mostly core portfolio funds in separate accounts. So very, very little exposure there.

Brad Burke - *Goldman Sachs - Analyst*

Okay. And the headlines that we're seeing about the open-end fund businesses in the UK, the daily liquidity retail-oriented products, I realize that you guys are going after a different segment, but still wanted to check if you're expecting any spillover impact from the pressures that we see on those daily liquidity vehicles?

Jim Groch - *CBRE Group, Inc. - CFO*

We really haven't seen much on the -- outside of the retail, and we're really not exposed on the retail side.

Brad Burke - *Goldman Sachs - Analyst*

Okay. I appreciate it, guys. Thank you.

Jim Groch - CBRE Group, Inc. - CFO

Thank you, Brad.

Operator

Our next question comes from the line of Anthony Paolone with JPMorgan. Please proceed with your question.

Anthony Paolone - JPMorgan - Analyst

Thanks. Good morning. In terms of sales and leasing it, seems like you guys had another quarter of share gains, at least relative to the third-party data. Can you talk about whether you think that's happening from more wins, or is this headcount, or what do you think is driving that?

Bob Sulentic - CBRE Group, Inc. - President & CEO

Tony, this is Bob. Headcount is certainly part of it. We have talked over the last several quarters about the gains we have made over the last two or three years in recruiting. That has continued into this year, although at a slower pace, partially because some of the pricing we've seen out there for recruiting we don't think makes sense. So our recruiting is down by about one-third this year.

The other thing that's benefiting us is some of the strategic things we've done with those businesses. Notably, we have grown our small asset class materially on the sales side and on the advisory and transaction services side of our occupier client offering. We've integrated our outsourcing business with our local brokerage business and added a bunch of advisory capabilities that have really allowed us to take on a lot of account business beyond what we were ever able to do before and offer things to our clients that go beyond what we were able to offer before. And that's coming through in our numbers, and it's coming through in our numbers for outsourcing business and our local brokerage business or local leasing business, and we're taking market share as a result.

Anthony Paolone - JPMorgan - Analyst

Okay. And can you help us at all with thinking about just the incremental margins for sales and leasing as we look ahead?

Jim Groch - CBRE Group, Inc. - CFO

We really haven't been providing guidance around incremental margins. Part of that is just it depends on the trajectory of the business. So we haven't been that specific.

Anthony Paolone - JPMorgan - Analyst

Okay. Then if I look at your cost elimination program, you guys spent, I think, \$27 million on this in the second quarter, and that was from about \$8 million or \$9 million, I think, in the first quarter. How much do you think you are going to drive in terms of run rate savings from the initiative? Like how much is left here because it seems like it's been expanded since last quarter?

Jim Groch - CBRE Group, Inc. - CFO

We haven't given specific guidance on where that's going. I would say we mentioned that we started this program in late last year, and at the time, we noted that we have grown the business massively over the last three years, and when you do, you intermittently need to step back and look for pockets where you may have some inefficiency, and we thought it was a good time to work on that.



But I'd also highlight that all those savings don't drop to the bottom line because we do reinvest. While we are cutting costs in some areas, we are looking to reinvest in other areas where we think we can get real leverage from our investments.

Anthony Paolone - JPMorgan - Analyst

And if I think about that just to understand the numbers, like the \$27 million you spent in the quarter on that stuff, like would that be in the \$688 million of OpEx, or is it somewhere else? How do we think about that?

Gil Borok - CBRE Group, Inc. - Deputy CFO & Chief Accounting Officer

Tony, it's Gil. In the P&L with the press release, the GAAP P&L, it mostly would be an OpEx. In normalized EBITDA or adjusted EBITDA purposes, it's adjusted out. But that is where you would see it mostly in the GAAP P&L.

Anthony Paolone - JPMorgan - Analyst

Okay. Got it. And then on outsourcing, if we take GWS out of the mix, it looked like the organic growth may be slowed a bit from 1Q into 2Q. How do you think about that the rest of the year?

You have talked in the past about organically that's still running into the double digits. Is that still something we should expect, or could that slow a bit perhaps because of the EMEA exposure and Brexit and so forth? How do you feel about that?

Bob Sulentic - CBRE Group, Inc. - President & CEO

Tony, Brexit hasn't really impacted the growth of that business or the stability of that business. And we did achieve 13% organic growth in that business in the first half, very consistent with our expectations for the business, which are unchanged in terms of the ongoing organic growth. We are extremely pleased with the way that business has grown year to date.

By the way, it was double-digit growth in the second quarter, too, at 10%. There is a little inefficiency quarter to quarter. We're quite excited about what we think the profile for continued growth of that business is.

Anthony Paolone - JPMorgan - Analyst

Okay. Thank you.

Operator

Our next question is from Jade Rahmani with KBW.

Jade Rahmani - Keefe, Bruyette & Woods - Analyst

Regarding the guidance and your comments about waiting more toward 4Q than 3Q relative to historical performance, can you maybe put some color around what the drivers of that are? Is that due to increased uncertainty in 3Q around capital markets volumes that you expect to normalize in the fourth quarter, or is it those incentive fee realizations?



Jim Groch - CBRE Group, Inc. - CFO

Yes. There is nothing particular driving it really, just the timing of whether it's carried interest in the Investment Management business or individual sales within the Development Services business. It can differ from year to year, from quarter to quarter.

We are ahead on activity year-to-date versus last year. And as we just look at the timing on these when we see transactions coming in, Q3 looks like it will be light, and Q4 looks like it will be strong, although in comparison to last year, Q4 was exceptionally strong. So we don't -- Q4, that type of activity will likely be down from Q4 of last year still.

But Q3 will be light, and it's just timing. Some deals we thought were going to hit in Q3 happened in Q2 and looked like some others are actually going to hit in Q4 instead of 3.

Jade Rahmani - Keefe, Bruyette & Woods - Analyst

In terms of capital markets, what can you say about the level of visibility you currently have for 3Q and even 4Q given the timing and how long it takes transactions to close? Would you say you are assuming similar year-over-year revenue growth, ex-foreign currency impact, that you've experienced in this quarter?

Bob Sulentic - CBRE Group, Inc. - President & CEO

We expect to end up the year in the ranges that we gave at the beginning of the year. And the one place that we are seeing things meaningfully different is no big shocker. It's the UK, which is a sizable market with London.

But we've worked hard to get a handle on what our people around the world are working on, and we have done that again recently and feel pretty good about the ranges that we gave at the beginning of the year. So we are not changing anything in that regard.

Jade Rahmani - Keefe, Bruyette & Woods - Analyst

On the cash flow and capital management spend, can you quantify the amount of dollars you've spent on M&A this year or this quarter and what you expect going forward? And given your view of the cycle and perhaps recent stock performance, if you might contemplate some stock buyback or dividend as an alternative use of capital?

Jim Groch - CBRE Group, Inc. - CFO

Well, as far as use of capital, we are always looking carefully at how to apply our capital in the most favorable way possible for our shareholders, but we don't comment specifically on what we might do there. As far as dollars spent on M&A, those figures will be in the Q when that comes out.

Jade Rahmani - Keefe, Bruyette & Woods - Analyst

Finally just, on headcount, can you comment on what the perhaps year-over-year organic growth rate was overall or in transaction professionals?

Jim Groch - CBRE Group, Inc. - CFO

Yes, Jay. We don't give specific headcount on our transaction professionals. But what I can say is that we have continued to bring on new producers in the investment sales, mortgage brokerage, and leasing parts of our business at a very strong rate, although off the last couple of peak years we have had by about one-third. And we don't have any reason to believe that there'd be big variability in that pace for the balance of this year.

We are watching very closely what's going on in the market, and we're seeing some what we consider foolish deals in the market, the kind of things that just aren't sustainable. So we're staying clear of that activity. But again we're having good success. It's impacting our growth in a positive way, and we expect that to continue.

Jade Rahmani - *Keefe, Bruyette & Woods - Analyst*

Thanks very much for taking my questions.

Steve Iaco - *CBRE Group, Inc. - IR*

Thank you, Jade.

Operator

Our next question comes from the line of Brandon Dobell with William Blair. Please proceed with your question.

Brandon Dobell - *William Blair & Company - Analyst*

Thanks. Let me go on back to slide 11 for a second, the occupier outsourcing, a couple of questions there. The 37 new clients, are those just new occupier outsourcing clients, or are they new clients for CBRE as a whole?

Bob Sulentic - *CBRE Group, Inc. - President & CEO*

Well, yes. Let me -- I want to make sure I'm answering what you're asking, Brandon. So are you asking, are these clients that we have never done anything at all for before, or just that we have not done outsourcing work for before?

Brandon Dobell - *William Blair & Company - Analyst*

Asking another way would be helpful. Just trying to get a sense of when you talk about new, are these ones you're getting because you have already done business someplace else in the world or leasing with, et cetera, or just purely new guys that have done nothing else with you before.

Bob Sulentic - *CBRE Group, Inc. - President & CEO*

These are new to the outsourcing business. I think when you ask the broader question, are they new to CBRE, we have done business with almost every major company in the world at some point through our transactional activities over the years. So there's almost nobody that we would do a new outsourcing account for that we have done nothing for ever before. The count you're getting there is for new outsourcing accounts.

Brandon Dobell - *William Blair & Company - Analyst*

Okay. The expansion that you continue to sign at a pretty good clip, any sense of the order of magnitude of those contracts? I'm looking at a secondary perspective, we talking just more space, breadth of services? And is there any market difference between how those expansions may look in the US versus EMEA?

Bob Sulentic - *CBRE Group, Inc. - President & CEO*

To that last question, I can't give you an answer off the top of my head. I can tell you that expansions typically -- there is a very typical pattern. We usually add services when we expand. So we will start providing one service, and we'll typically add another service or two when we do good work for our clients. And it's also very typical that we will take on new geography, sometimes just within the United States, or sometimes in other parts of the world. But those are the two things.

And that's one of the beautiful things about this business. If you do good work for these clients, and we track the work we do for them very closely, there is almost always an opportunity to take on new services or new geography. And it's core to the strategy that Bill Concannon articulates for his people every day and drives with his people every day. As he would say it, win them, keep them, grow them. And that grow them is also about taking on new turf or adding new lines of business form.

Brandon Dobell - *William Blair & Company - Analyst*

And then final one for me, on the expense structure, given what's going on, in the UK in particular, but just around Brexit, any acceleration or change in trajectory on how aggressively you guys are going after the expenses that have built up over the years through M&A or just in recognition of what that market looks like for the next handful of quarters, particularly among transaction support people, but also just more broadly?

Jim Groch - *CBRE Group, Inc. - CFO*

No. No change there really. We haven't made any changes. Look, I think it's important to emphasize that fundamentals for the markets have generally, globally, outside of circumstances in the UK, remain quite strong. So we started with some cost efficiency work in Q4 of last year. We are making good progress on that. We are reinvesting some of those savings primarily in technology initiatives.

I would also highlight, our margin on fee revenue in Q2, which is a medium size quarter, obviously, for the year, nowhere near Q4, just for the three regional business was 16%. The margins are good, and the margin overall is higher when you include the principal businesses. So we feel pretty good about where we are, and no major program being accelerated.

Brandon Dobell - *William Blair & Company - Analyst*

Okay. And I'm sorry. I just lied. Got a final one. In the conversations with customers in investment sales, property sales, how much have you heard people talk about -- or source of capital talk about shifting away from UK and Europe for a while and focusing on the US given its market liquidity and transparency, those kinds of things? Or is it more we want to be in the UK and Europe. We are just going to take time to let things settle out, and we are not going to shift our focus on where the capital is going?

Bob Sulentic - *CBRE Group, Inc. - President & CEO*

Well, the UK and Europe are different for me. They are not one thing.

Brandon Dobell - *William Blair & Company - Analyst*

Right.

Bob Sulentic - *CBRE Group, Inc. - President & CEO*

So people are definitely pausing in the UK. There's a few anecdotes about pausing in Europe, but really not very much. I was over there a couple weeks ago, and in general, we are not seeing that on the continent.

Here in the US, when you talk to our people in local markets, there's a bit of wishful thinking that we will get incremental capital here as a result of what's happening in the UK, but there was already a lot of capital aimed at the US markets, and I would say that in aggregate, that's what it was before, and the net-net of all of it is, people that were going to invest in the UK are waiting to see. And in the other big markets around the world, we haven't seen a meaningful impact yet.

Brandon Dobell - *William Blair & Company - Analyst*

Perfect. Thanks, guys.

Operator

Our next question comes from the line of David Ridley-Lane with Bank of America Merrill Lynch. Please proceed with your question.

David Ridley-Lane - *BofA Merrill Lynch - Analyst*

Good morning. Could you give us some details of the pace at which you are approaching GWS clients around potentially cross selling in leasing. Are you targeting those pitches around contract renewal dates? Are you targeting existing GWS clients where you already have a large share of their leasing but not a company-wide contract? Just wondering about the pace there.

Bob Sulentic - *CBRE Group, Inc. - President & CEO*

David, we first and foremost have made a very, very visible commitment to the clients that came over through that GWS acquisition that we are going to be riveted on transition the work we do for them now. And we have made clear to them that we're not in there aggressively trying to do more for them in any different way than we have been historically.

Now, you know we have a very, very big leasing offering around the world, and we're talking to most companies in the world most of the time about doing leasing work for them. Nothing about that has changed. But with regard to the relationship people on those accounts, they have almost exclusively focused on transitioning the accounts and doing great work for them and measuring that work.

That's going well. We had a lot of work to do in that area. We have gotten most of that integration work done.

I will tell you that if you talk to Bill Concannon and his Team, they will tell you now that it's -- things are starting to feel very different with those clients. Those clients are becoming much more comfortable with him. We've had some very recent significant wins. The confidence that we can marry up all the pieces of that business and go to market as an integrated offering is growing pretty rapidly.

So we think those opportunities are very, very good. But through the first three quarters of that acquisition transition, the focus has been on transitioning those accounts and really crushing the work that we've already been given from those clients.

David Ridley-Lane - *BofA Merrill Lynch - Analyst*

Got it. Okay. And then on the -- here in the United States the issuance of commercial mortgage-backed securities has been weak so far in 2016. As you talk to your capital markets professionals, is that having a negative impact, or are there enough sources of debt financing that it's not really impacting the US capital markets volumes?



Jim Groch - CBRE Group, Inc. - CFO

The mortgage business is doing quite well. It's up 14% for the quarter. And we're seeing lots of liquidity. So I think there has been plenty of liquidity to fill that void. It's not been an issue.

David Ridley-Lane - BofA Merrill Lynch - Analyst

Great. And last one for me. If FX rates stayed the same as they are today, do you have a rough estimate of what the benefit from FX hedges would be in 2016?

Jim Groch - CBRE Group, Inc. - CFO

If the rates stay where they are now, then there should be no impact because we mark-to-market our hedge positions every quarter. So that's how it would play out.

David Ridley-Lane - BofA Merrill Lynch - Analyst

Okay. So the benefit you saw in the second quarter was as of rates on June 30?

Jim Groch - CBRE Group, Inc. - CFO

That's correct.

David Ridley-Lane - BofA Merrill Lynch - Analyst

Got it. Okay. Thank you.

Jim Groch - CBRE Group, Inc. - CFO

Yes.

Operator

Our next question comes from the line of Mitch Germain with JMP securities. Please proceed with your question.

Mitch Germain - JMP Securities - Analyst

Jim, you guys have been on this pace of, call it, around 12 or so talking acquisitions per year. Any change in your appetite? Or does that still seem to be somewhat aligned with the run rate that we should expect?

Jim Groch - CBRE Group, Inc. - CFO

Mitch, that's a good question. Our M&A pipeline is quite active. But we did start to pull back on infill last year when we saw pricing in the marketplace increasing. So we're, as always, we're very active in the market. We are looking for great companies, a great cultural fit, companies that are going to truly add capabilities to what we offer. But we will -- pricing matters. It does. And we will pull back from time to time and get back in when we see things be more in line with where we think they should be.



Mitch Germain - *JMP Securities - Analyst*

Got you. Okay. And then just curious. It seems like we have seen a couple of asset trades and some refinancings in the UK. That may be -- Bob, the discussions that you are having with your team, does this seem like the pause is maybe lifting a little in that market and things are moving slowly back to normal, or maybe just get a little sense about momentum there?

Bob Sulentic - *CBRE Group, Inc. - President & CEO*

I talked to Martin Samworth, the CEO of EMEA for our business, two days ago, and I asked him that question. And he said that in fact, there was a distinct clawing back of the momentum that had been lost due to Brexit up until about a week ago when, as he put it, everybody in Europe started going on vacation. And he thinks that legitimately, that there has been a turnaround, but the whole vacation season there is causing that turnaround to slow for a while. But he's encouraged that when September comes around that we'll see things -- the momentum reemerge.

Mitch Germain - *JMP Securities - Analyst*

That's it for me. Thank you.

Operator

Our next question is a follow-up question from Brad Burke with Goldman Sachs. Please proceed with your question.

Brad Burke - *Goldman Sachs - Analyst*

Just one follow-up for me with regards to the AUM in the investment Management business, realizing that there have been a lot of FX headwinds to AUM growth, but based on what you are seeing now in terms of capital raising and the capital that you have yet to deploy, how we ought to be thinking about AUM growth over the next year or so?

Jim Groch - *CBRE Group, Inc. - CFO*

I think we'll continue to be in line with what we have been doing over the last year or two. Unfortunately, that growth continues to be offset generally by changes in FX. The growth has been quite good, but as you highlighted, the FX has tended to offset most of it.

Brad Burke - *Goldman Sachs - Analyst*

Okay. That's it for me. Thank you.

Jim Groch - *CBRE Group, Inc. - CFO*

Thank you.

Operator

Thank you. Our next question comes from the line of Jade Rahmani with KBW. Please proceed with your question.

Jade Rahmani - Keefe, Bruyette & Woods - Analyst

Thank you for taking the followup. When you quantify the percent of revenues from contractual revenue sources, can you give some color on what percentage of leasing transactions, which are not contractual, but would be considered recurring, or historically, what percentage of leases, renewal, and -- if you guys win that business?

Jim Groch - CBRE Group, Inc. - CFO

Okay. When we refer to contractual revenues, and we had a slide in our deck that showed the change in the business and the degree to which contractual revenues have increased as a percentage of the total, there are no leasing revenues in those numbers. So they are -- you will hear us refer to leasing as being a largely recurring over time. But we don't include any of those revenues in the contractual section of what we refer to as contractual.

As far as a percentage of deals where we get renewals, I can't give you a figure, an exact figure, but it's extremely high. And if we didn't get a renewal -- on the margin, if we or others aren't getting the renewals on their assignments, then we are picking up the other competitors' piece and vice versa. But that tends to be quite rare.

Jade Rahmani - Keefe, Bruyette & Woods - Analyst

And in terms of EBITDA contribution from contractual revenue sources, is it similar to the percent of revenue, or lower than that given the high margins that capital markets generate historically?

Jim Groch - CBRE Group, Inc. - CFO

We haven't been -- the most we've said on that is that the contribution is closer than you would think because on a fee revenue basis, our contractual revenues include some of our lower-margin business in that (inaudible) management area and some of our higher in Investment Management. So it's not quite equal between revenue and EBITDA, but it's not as far off as you might think.

Jade Rahmani - Keefe, Bruyette & Woods - Analyst

Thank you very much.

Operator

Our next question is also a follow-up question from Anthony Paolone with JPMorgan. Please proceed with your question.

Anthony Paolone - JPMorgan - Analyst

Yes, thanks. So staying on the contractual business and the outsourcing since it's becoming so big and important for you all, can you take us inside a little bit and tell us, when you have a multi-year contract, you have a contractual revenue stream, but does it guarantee the level of that revenue stream, or does that vary and you just know you will be doing things and get paid for it? Like how does it work?

Bob Sulentic - CBRE Group, Inc. - President & CEO

There's parts of it that are fully guaranteed, Tony, and there's other parts of it that aren't. So we often will have incentives in these contracts that will allow us to earn incremental dollars if we meet certain performance thresholds. And we also will have some variable amount of work.



So for instance, we may take on a contractual relationship with a big corporate client to do project management work of a certain type for them, and the more projects they do, the more work we do. That's very typical of those accounts. So it's a mixed bag.

The way we generally view these big outsourcing accounts when we take them on, they tend -- they are getting larger and larger, so it's not uncommon any more for us to take on a client and grow it to be a multi-hundred-million-dollar revenue source for the Company. We almost view these incremental accounts as starting new little businesses within our Company. When you start them, there is something there, and then you do a good job, and you grow them. And with 90%-plus renewal rates and increasing customer satisfaction rates, we tend to keep them and grow them. So you end up with something at the core that is largely guaranteed, and you have the opportunity to grow it from there.

Anthony Paolone - JPMorgan - Analyst

Okay. And then so when you think about the double-digit organic growth in outsourcing, how much of that do you think is winning new contracts and just the expansion and adoption of outsourcing around the world versus, I don't know, like a same contract revenue concept?

Bob Sulentic - CBRE Group, Inc. - President & CEO

We've never publicly produced those numbers. I can tell you both are very meaningful. It's not one as dramatically larger than the other. Both are very meaningful, both the expansion of existing counts and the addition of new accounts.

Anthony Paolone - JPMorgan - Analyst

Okay. Thanks for the insight.

Bob Sulentic - CBRE Group, Inc. - President & CEO

Thank you.

Operator

Thank you. We have reached the end of the question-and-answer session. Mr. Sulentic, I would like to turn the floor back over to you for closing comments.

Bob Sulentic - CBRE Group, Inc. - President & CEO

Thanks everyone for being with us, and we will talk to you again at the end of the next quarter.

Operator

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



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