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CBRE Group, Inc. (CBRE)

Q4 2021 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Greetings and welcome to CBRE's Q4 2021 Earnings Conference Call. At this time, all participants are in listen-only mode. Our question-and-answer session will follow the formal presentation. [Operator Instructions] As a reminder, this conference is being recorded.

I'd now like to turn over the conference to your host, Kristyn Farahmand, Senior Vice President of Investor Relations and Strategic Finance, CBRE. Ma'am, please go ahead.

Kristyn Farahmand

Senior Vice President-Investor Relations & Strategic Finance, CBRE Group, Inc.

Good morning, everyone, and welcome to CBRE's fourth quarter 2021 earnings conference call. Earlier today, we issued a press release announcing our financial results which is posted on the Investor Relations page of our website, cbre.com, along with a presentation slide deck that you can use to follow along with our prepared remarks as well as an Excel file that contains additional supplemental materials.

Before we kick off today's call, I'll remind you that this presentation contains forward-looking statements that involve a number of risks and uncertainties. Examples of these statements include our expectations regarding CBRE's future growth prospects including our 2022 qualitative outlook and multi-year growth framework, operations, market share, capital deployment strategy and share repurchases, M&A and investment activity, the performance of existing investments, financial performance including cash flow, profitability, expenses, margins, adjusted EPS, core adjusted EPS and the effects of the COVID-19 pandemic, the integration and performance of acquisitions and other transactions and any other statements regarding matters that are not historical fact. We urge you to consider these factors and remind you that we undertake no obligation to update the information contained on this call to reflect subsequent events or circumstances. You should be aware that these statements should be considered estimates only and certain factors may affect us in the future and could cause actual results to differ materially from those expressed in these forward-looking statements. For a full discussion of the risks and other factors that may impact these forward-looking statements, please refer to this morning's earnings release and our most recent annual and quarterly reports filed on Form 10-K and Form 10-Q, respectively.

We have provided reconciliations of core adjusted EPS, adjusted EPS, adjusted EBITDA, net revenue, and certain other non-GAAP financial measures included in our remarks to the most directly comparable GAAP measures together with explanations of these measures in the appendix of the presentation slide deck.

Our agenda for this morning's call will be as follows: first, I'll provide an overview of our new financial metrics. Next, Bob Sulentic, our President and CEO, will discuss initiatives that support our four dimension diversification strategy. Then Emma Giamartino, our Chief Financial and Investment Officer, will discuss the quarter in detail, our capital deployment strategy, our initial qualitative 2022 outlook, and our updated multiyear growth framework. Then we'll open up the call for questions.

As you can see on slide 5, the fourth quarter completed a strong and transformative year for CBRE. We made strategic investments in Turner & Townsend and Industrious, and saw significant gains from strategic noncore investments made through our SPAC and in venture capital funds. Due to our controlling interest that results from our 60% ownership stake in Turner & Townsend, we fully consolidate Turner & Townsend's financials including their balance sheet. We will focus our commentary on consolidated performance inclusive of non-controlling interests and we will use consolidated adjusted EBITDA for our net leverage calculations.

To give more transparency to our investors, we are introducing a new earnings metric called core adjusted EPS this quarter. Core adjusted EPS excludes the impact of strategic non-controlling investments that are not attributable to a business segment. These had an immaterial impact prior to 2021. These investments are a small part of our portfolio, but there is likely to be considerable volatility in their fair values, particularly for Altus Power, the largest of our investments, now trading on the New York Stock Exchange. We believe this new metric will help investors better assess the underlying performance of our core business.

Starting in Q1, we will also present strategic non-core investments and corporate overhead separately, which today are combined. We believe this incremental transparency will help investors assess the level of corporate overhead and the performance of these non-core investments. We've also enhanced our presentation today to help provide greater insight into our performance. As a result, the slides accompanying our remarks are different from previous quarters and focused on the most significant drivers to our consolidated results for revenue, adjusted EBITDA, and earnings.

The segment-specific slides we've presented in previous quarters are included in an Appendix as are some slides from our research team detailing the long term historical relationship between real estate and inflation that we believe investors will find topical.

With that, please turn to slide 7 as Bob provides insight into our strategy. Bob?

Robert E. Sulentic

President, Chief Executive Officer & Director, CBRE Group, Inc.

Thank you, Kristyn, and good morning, everyone. As you've seen, we had a strong finish to 2021, significantly outperforming both Q4 2020 and the pre-pandemic peak in Q4 2019. This capped an outstanding year for CBRE with all key financial benchmarks reaching new all-time highs for the company.

We certainly benefited from a supportive macro environment in 2021. Beyond that, our strong financial performance is the product of our long-standing work to strengthen our balance sheet and improve the resiliency of our income statement, as well as our successful efforts over the past several years to diversify our business across four dimensions, asset types, lines of business, clients, and geographies. We have described our diversification efforts in detail in recent quarters, highlighting how it has positioned CBRE to benefit significantly from secular tailwinds.

Prime examples of this are our investments in Turner & Townsend, a project manager that enhances our green energy and infrastructure capabilities, and Industrious, a leading asset-light player in the growing flex space market. In our Real Estate Investment segment, we are now executing a strategy to realize positive synergies between our development and investment management businesses with support from our strong balance sheet.

So far, this effort has focused on industrial and logistics assets, which are benefiting from long-term secular trends. Our research team projects that global e-commerce sales will rise to approximately $3.9 trillion by 2025, requiring an additional 1.5 billion square feet of distribution space. Specifically, we are placing development projects into investment programs run by CBRE Investment Management, essentially converting portions of our more than $18 billion in-process development portfolio into investment management AUM. This strategy also capitalizes on our industrial investment sales and property management expertise.

At the same time, we are further building AUM in our industrial and logistics strategy by supporting CBRE Investment Management's acquisition of large portfolios of operating assets. The most recent example is the agreement to acquire a $4.9 billion portfolio of US and European logistics assets from Hillwood. Our balance sheet provided a backstop for proportions of this portfolio, which enabled our team to move quickly to secure a highly desirable set of assets. We plan to replicate this model for other secularly favored asset types, including multifamily and life sciences. And expect our integrated investor operator developer model will generate material, incremental recurring revenues and earnings for years to come.

Reflecting our strong 2021 performance, and the substantial opportunities we see in front of us, we are increasing our multiyear aspirational growth framework. For the period from 2020 to 2025, we now expect our average annual core adjusted EPS growth to exceed 20%, barring an economic disruption from geopolitical or other events, which we are watching closely. This is up from the low double-digit growth expectation we set a year ago. The average annual growth rate is expected to be in the low double digits for the prospective period from 2021 to 2025. We believe there is potential upside to our expected growth rates for both periods through incremental capital deployment.

Emma will walk you through this in detail after she reviews the quarter. Emma?

Emma Giamartino
Global Group President, Chief Financial Officer & Chief Investment Officer, CBRE Group, Inc.

Thanks, Bob, 2021 was an outstanding year for CBRE with strong growth across our key financial metrics and record free cash flow driven by operational discipline and our four dimension diversification strategy. We're also well-positioned for future growth, which I'll discuss shortly. Throughout my remarks today, I'll highlight how our results benefited from asset type diversification, and in future quarters, I will focus on the benefits of other diversification dimensions.

Now, please turn to slide 9 so we can dive into our results for the quarter. Like Q3, I'll include compares with Q4 2019 for the transactional business lines to provide insight into our performance from peak levels. On a consolidated basis, revenue grew 24% compared to Q4 2020 and 20% over Q4 2019, led by rebounding sales and lease revenue. Advisory Services added nearly $1 billion in net revenue, growing 43% over Q4 2020 and 23% over Q4 2019 to over $3.3 billion, a record for our largest segment. We continued to benefit from a supportive property sales backdrop. Globally, sales revenue jumped over 73% from Q4 2020 and 45% from Q4 2019. The US led the recovery among our major markets with 89% sales revenue growth compared to the prior year quarter.

We had the highest market share across all major asset types in 2021 while our overall US market share rose 100 basis points in the quarter according to independent data provider, Real Capital Analytics. Capital inflows into multifamily and industrial remain strong, allowing us to benefit from the very intentional work we have done to build leading sales platforms focused on these asset types.

US industrial sales revenue more than doubled from Q4 2019 while US multifamily sales nearly doubled over the same period. Office continues to gradually improve back toward pre-pandemic levels and our US office sales revenue was around 14% shy of Q4 2019, an improvement from steeper declines in the prior quarters.

Global leasing revenue rose 14% compared to the fourth quarter of 2019 with all three regions ahead of 2019 levels for the second consecutive quarter. EMEA leasing revenue grew 25% on Q4 2019 and the Americas was up 13% while APAC grew 7%.

Industrial leasing surged around 60% compared to the fourth quarter of 2019 as occupier demand for distribution space remained strong. Like in sales, office leasing also continued to recover with global office leasing nearly flat versus Q4 2019. EMEA and APAC office leasing rose around 7% and 11% respectively compared to Q4 2019. US office leasing revenue trends also continue to improve. While still below its 2019 level by around 4%, the year-over-year shortfall from prior peak levels has narrowed compared to previous quarters. Notably, while it's still early in the year, we are continuing to see strong momentum in both US sales and leasing thus far in 2022 with revenue trending significantly above prior peak first quarter levels.

Loan servicing was the primary growth driver within the rest of Advisory with revenue rising around 70% from Q4 2019 to nearly $93 million. Our loan servicing portfolio grew 23% versus the prior year and 10% sequentially to nearly $330 billion, primarily driven by private capital sources. Our multifamily portfolio comprising nearly half of the total grew about 14% versus Q4 2020. Our alternative asset-type portfolio, which includes agriculture, health care, hotels and others rose over 70% and now comprises approximately 19% of our total servicing portfolio. Growth was driven by a strong pace of third party servicing wins, which is a key focus area for growth in this business. OMSR gains faced a tough compare and were down about $47 million. These gains were elevated in last year's fourth quarter as the government agencies were extremely active in providing liquidities to a multifamily market burdened by COVID impact.

Turning to GWS. Net revenue grew 22%, increasing $330 million to nearly $1.9 billion. This includes about $175 million in net revenue from the Turner & Townsend transaction, which closed on November 1 and was in line with our previous expectation. We are extremely excited about the growth trajectory for this business. Project management is a fragmented market estimated to be over $100 billion with strong, secular growth tailwinds particularly within infrastructure. This transaction helps to bolster the nascent infrastructure capabilities within our existing businesses. We believe broadening our infrastructure offerings will help to accelerate future growth and deepen diversification, especially by helping to further insulate our business for more cyclical trends.

Our legacy GWS revenue grew nearly 8%, led by project management, which rose about 17%, excluding contributions from Turner & Townsend. Strong growth in project management was driven by continued recovery from the pandemic constrained environment. Facilities management revenue increased nearly 6%, and net revenue rose over 10%, supported by growth from local clients. We expect facilities management growth to benefit from continued progress in returning to a more normal business environment in 2022.

Looking at REI, revenue increased $125 million or 43% to over $413 million. This was driven by increasing activity in our UK multifamily development business, which is continuing to recover from COVID-related challenges. Investment management revenue was relatively flat for Q4 2020, at about $150 million due to lower carried interest revenue, which can be volatile. Excluding carried interest revenue, investment management revenue grew 19%, driven by strong asset management fee growth. AUM rose to a new record of nearly $142 billion, with more than 80% invested in assets other than office. Industrial comprises the largest component in line with our strategic vision to position the company to benefit from this sector's strong secular talent.

Flipping to slide 10, consolidated adjusted EBITDA grew to over $1.1 billion, excluding non-cash gains related to OMSRs, our Altus Power investment through our SPAC and venture capital investments, adjusted EBITDA grew over 37% compared to Q4 2020. On this basis, our underlying adjusted EBITDA margin on net revenue rose 6 basis points versus Q4 2020 to 16.5%, which is 1.7% above our Q4 2019 level. Advisory Services segment operating profit marginally exceeded our expectations increasing $219 million to over $740 million as sales and lease revenue rose more than expected. Advisory's net operating profit margin, excluding volatile noncash OMSR gains reached a new record of 21.5%, about 120 basis points better than Q4 2019. We achieved this despite record productivity pushing more producers into higher split tranches.

In GWS, legacy segment operating profit reflected higher-than-expected medical expenses as we saw a ramp up in year-end insurance claims compared with 2020's severely pandemic-constrained levels, as well as a $3 million impact of noncash deferred purchase consideration expense for Turner & Townsend. Turner & Townsend profitability performed in line with our expectations, contributing just over $23 million of profit from November 1 through year-end.

REI segment operating profit rose $39 million to $156 million and was roughly in line with expectations as outperformance in investment management offset a modest shortfall in development. Investment management benefited from higher-than-expected net promotes and co-investment returns driving operating profit to $41 million. Development operating profit of $122 million was affected by a $29 million increase in a reserve we had previously taken on a UK construction project that faced challenges that were exacerbated by the pandemic. We believe we have fully reserved for this project and don't expect it to result in further adverse financial impacts.

Putting aside this reserve increase, development operating profit would have been over $150 million for the quarter and about $380 million for the year surpassing our previous expectations. This was driven by the conversion of our average in-process portfolio to operating profit at a rate of over 2.1% over the trailing 12-month period, a level well above our historical norm of between 1% and 2% with most years around the midpoint.

We also saw increased corporate overhead in the quarter. This is largely driven by higher incentive compensation, as performance materially exceeded initial 2021 expectations and our investments in key corporate functions to help support our larger business. We do not expect incentive compensation to fluctuate as much in 2022 as business volatility continues to normalize.

Looking at slide 11. Adjusted earnings per share rose 51% to $2.19. This includes a benefit of $0.36 from a gain on our SPAC investment and another $0.03 from mark-to-market adjustments on our Altus Power and VC investments. Excluding these noncash gains, core adjusted EPS rose 24% to $1.80. Excluding only the SPAC's deconsolidation gain, which is consistent with how we've reported our results in previous quarters, adjusted EPS rose over 26% to $1.83.

Robust underlining earnings growth reflects the strong increase in adjusted EBITDA, as well as lower net interest expense. These are partially offset by higher depreciation and amortization, mainly related to elevated prepayments of government agency-related loans, which triggered higher OMSR amortization. Our results also include noncash interest expense related to deferred purchase consideration for our remaining Turner & Townsend payments, and an increase in our effective adjusted tax rate to 23.9%. The nonrecurring reserve increase in the UK multifamily development business lowered earnings by approximately $0.07. Going forward, as Kristyn noted earlier, we'll report both adjusted EPS and core adjusted EPS to give you transparency into how both our core operations and non-core investments are performing.

Now, we'll discuss our financial capacity on slide 12. Due to our strong profitability, we generated nearly $1.1 billion of free cash flow in the quarter, bringing our annual free cash flow total to almost $2.2 billion, which is a new record for our company. We ended the year with a net cash position of 0.2 turns while deploying nearly $1.8 billion of capital net of debt issuance proceeds during the year primarily for investments in future growth. We also repurchased around $370 million of stock, providing our shareholders a repurchase yield of over 1%.

We intend to continue this capital deployment strategy and believe there is ample opportunity to invest in future growth, while also programmatically returning cash to our shareholders. In support of this, we commenced our fifth consecutive quarter of repurchases in Q1 2022. We intend to continue repurchases throughout this year, assuming the return remains attractive and we have capacity given our evolving M&A pipeline. Additionally, as we move forward, strong free cash flow conversion will remain a priority for us. And our senior executive team will be evaluated on this metric as part of their 2022 goals.

Please turn to slide 13. We expect another year of strong growth in 2022. Market conditions remain generally favorable notwithstanding heightened geopolitical tensions and tailwinds are likely to persist across the four dimensions of our business in areas where we are proactively investing to drive growth. Advisory services is positioned for another year of strong revenue and segment operating profit growth with leasing revenue expected to rise at a high teen to low 20% rate and sales revenue expected to rise at a low to mid-teens rate. We expect incremental benefit from offices' gradual recovery and that industrial leasing should decelerate modestly due to a potential near-term shortage of available properties. As Bob highlighted earlier, we believe long term secular trends are bolstering demand for industrial space and expect strong performance for this asset class on a long run basis.

Outside of sales and leasing, we expect Advisory revenue to rise at a high single-digit to low double-digit compared to 2021. We also expect Advisory's operating margin to be roughly flat versus the prior year as the benefit of high-margin transactional revenue growth will be tempered by some operating expense investments designed to accelerate future growth. Advisory operating profit expectations also include increased strategic equity awards to help better align a broader leadership team with our enterprise strategy and to shareholders. We expect strong long-run margin performance in Advisory partially driven by these investments.

In GWS, we expect low to mid-double-digit organic top line growth and mid to high single-digit organic segment operating profit growth. This is being driven by continued strong growth in project management and accelerated growth in enterprise facilities management, partially driven by a return to normal contract cycle times. We expect this growth to be more weighted to the second half of the year. GWS legacy segment operating profit expectations also include the impact of $17 million of non-cash deferred purchase consideration expense for Turner & Townsend. This expense will continue through 2025 when we've made the last of our required payments. We will also record about $10 million in noncash interest expense associated with our deferred payment.

Like in Advisory, GWS operating profit expectations also include an impact from increased use of strategic equity awards. This is reducing expected legacy segment operating profit growth by around 1%. We expect Turner & Townsend to grow net revenue at a mid-teens rate in line with its historical average over the approximately $974 million it generated in calendar year 2021. Strong organic growth is expected to more than offset a small foreign exchange headwind at today's spot rate. Turner & Townsend's net operating profit margin is projected to tick up around 0.5% from the 13.4% generated in the fourth quarter. This reflects strong top line growth, the restoration of certain expenses cut during COVID, and about $10 million of non-cash expense for retention bonuses.

REI revenue is expected to grow around 20% and segment operating profit is expected to roughly match the elevated operating profit of $520 million generated in 2021 excluding the $24 million accounting change driven gain we recorded in last year's first quarter. Revenue growth is being driven by continued recovery of our UK development business. Our REI expectations also contemplate elevated hiring in investment management for new product development, a key strategic focus as well as more moderate appreciation in asset values. Finally, we expect our development in-process portfolio will convert to operating profit at a rate of under 2% in line with historical performance.

Our in-process portfolio is well positioned for the current environment with nearly 80% of the portfolio comprised of industrial, multifamily, healthcare, and life sciences assets. As you can see, we are consciously orienting the portfolio toward assets with strong long-term performance potential. Setting aside any effects of our strategic non-core investments, we expect corporate overhead to decline nearly 5% from 2021. We anticipate investments in further scaling key corporate functions to be more than offset by more favorable incentive compensation impacts.

Going forward core adjusted earnings, which excludes the impact of our small portfolio of strategic non-core investments will be the basis of our financial forecast. We are making these investments for their strategic value rather than near-term financial gains. However, there will likely be sharp volatility in their investment valuation, especially for our largest non-core investment in publicly traded Altus Power. Altus is poised to benefit from the transition to a low carbon economy, while enhancing capabilities to help our clients meet their clean energy and sustainability goals.

As always, for investments of this nature, short-term bouts of market volatility can cause the value of our investment to swing sharply on a quarter-to-quarter basis. For example, the majority of the non-cash gain we recognized in the fourth quarter would be reversed in the first quarter at Altus' share price as of February 15.

Now, looking at depreciation and amortization, we expect this to rise about 4%, and we project our effective adjusted tax rate to be in line with the 23.9% rate we saw in Q4 2021. We are also highly focused on monitoring how inflation could impact our business. Real estate provides a natural inflation hedge when held on a long-term basis, which somewhat cushions our transactional businesses. In fact, sales could potentially even benefit if inflation concerns draw more capitals real estate.

On the expense side, clients reimburse us for the salary and benefits of nearly half of our employee base who work primarily in the GWS and property management businesses. And inflation provisions are typically embedded in our multiyear GWS contracts. In light of this, we believe we are well-positioned to succeed in a higher inflation environment. It is also prudent to highlight that while the current operating environment remains favorable, there is heightened uncertainty given this higher inflationary environment, tighter monetary policy, and rising geopolitical tension.

Please turn to slide 14 for an update of our multiyear growth framework. As Bob noted, we've raised our base case annual core adjusted EPS growth expectations to more than 20% for the 2020 to 2025 period, and to low-double digits for the next four years. There's upside to both growth rates from additional capital deployment. We envision solid organic revenue and earnings growth across our three business segments. Our overall margin is expected to gradually increase over this period even with considerable growth from our lower margin GWS segment. The GWS margin itself should also improve over time as higher margin project management accounts for a larger share of our GWS revenue base.

We will continue to manage our balance sheet prudently. We are comfortable with increasing net leverage to around one turn as we deploy capital into M&A to accelerate growth. We can even go as high as two turns for a highly compelling strategic opportunity. We expect to focus our capital deployment strategy on secularly favored areas that will further diversify our business. We see significant opportunity to expand our investor, operator, developer model into multifamily, life sciences and infrastructure. Importantly, this model plays to our competitive advantages including cross-functional collaboration, business line diversification, and balance sheet strength, giving us the opportunity to further differentiate CBRE. Given our sizeable financial capacity, we expect shareholder capital returns will continue to figure prominently within our capital allocation plans over this multiyear horizon.

Ending with slide 15. Since 2016, core adjusted EPS has achieved average annual growth of 21% while revenue and free cash flow have also grown at double-digit annual rates over this period. This strong growth has been supported by the strategic steps we've taken to bolster our balance sheet while pursuing a disciplined capital allocation program and increasingly diversifying our business. We expect our multiyear growth framework will extend the successful track record of performance across our key financial metrics. We are extremely optimistic about our trajectory as we head into 2022 and look forward to delivering another year of strong performance.

And with that, operator, we'll open the line for questions.

QUESTION AND ANSWER SECTION

Operator: Thank you very much. At this time, we will be conducting a question-and-answer session. [Operator Instructions] We have a first question from the line of Anthony Paolone with JPMorgan. Please go ahead.

Anthony Paolone
Analyst, JPMorgan Securities LLC

Q

Great. Thank you. I guess my first question is just to understand if, I guess, the new EPS metric is going to be core adjusted, what's the EBITDA that ties to that metric? Because it doesn't seem like it's the [ph] $1,124 billion (33:48).

Kristyn Farahmand
Senior Vice President-Investor Relations & Strategic Finance, CBRE Group, Inc.

A

So, we haven't changed the adjusted EBITDA metric, but there are going to be two different segment operating profit metrics going forward for each segment. So, we will be reporting consolidated segment operating profit for each segment as well as operating profit attributable to CBRE common stockholders. And for purpose of consolidated adjusted EBITDA, we feel like that's the best measure for the company in terms of the EBITDA metric because we are fully consolidating all of Turner & Townsend's financials into our own. And so, that keeps the margins actually logical.

Emma Giamartino
Global Group President, Chief Financial Officer & Chief Investment Officer, CBRE Group, Inc.

A

And, Anthony, I'll just add, on core adjusted EPS, the comparable, we're not reporting a comparable core adjusted EBITDA. So, our adjusted EBITDA will include the gains from the SPAC and our venture capital gains. Does that answer your question?

Anthony Paolone
Analyst, JPMorgan Securities LLC

Q

Yeah. I think so. Okay. I'll jump back in the queue. Thanks.

Operator: Thank you. We have next question from the line of Alex Kramm with UBS. Please go ahead.

Alex Kramm
Analyst, UBS Securities LLC

Q

Yeah. Hey. Good morning, everyone. You make those comments on inflation and I didn't look at the slides that you had from your research group. But I think on balance, you think inflation is a positive. Does that include rate hikes as they are obviously forecasted now to happen? Maybe you can specifically talk about rates. You have a very diversified business, so kind of hard to think through where rate increases may hit you. So, maybe a little bit more detail on that would be helpful. Thank you.

Emma Giamartino
Global Group President, Chief Financial Officer & Chief Investment Officer, CBRE Group, Inc.

A

Yes. So, we've base our outlook based on what our in-house economist believes will happen in terms of inflation and rate hikes over the next year. And his view is that inflation will moderate through 2022 and 2023 and the Fed will do a similar number of hikes as the market is projecting to manage that inflation. And so we've incorporated that outlook into our guidance. As we said, we think we have – we know that we have a number of inflation hedges throughout our business, but there are areas where we know inflation will impact us. And so there are two main areas where we've incorporated that. For the half of our global employee base that is not reimbursed by clients, we have factored in wage inflation. And then for our relevant business lines that may be impacted by cap rates, we have assumed some moderation in cap rates throughout the year. And that may be a conservative assumption going forward. And then I do want to say that our outlook does not contemplate the uncertainty and impacts from the geopolitical tensions that are rising throughout the world.

Alex Kramm
Analyst, UBS Securities LLC

Q

Okay. Thanks for that. And then maybe shifting to margin quickly. Can you just flesh out the margin comments a little bit more? I guess on the Advisory side, what's the right base to use for that margin comment given that, you know, you present your margin sometimes with or without gains? And then on the GWS side, again, sounds like that's tied to, I think you mentioned a 1% impact from certain items. But like if you think about the core underlying GWS business organically, is that seeing benefits from operating leverage or are there also other investments that are countering that in 2022?

Emma Giamartino
Global Group President, Chief Financial Officer & Chief Investment Officer, CBRE Group, Inc.

A

So, throughout our businesses, throughout all three lines of business, we are investing more to drive incremental growth in future periods. So, across all three business lines, we're investing about $300 million in OpEx, and those investments are for areas like increasing our capabilities and to serve our clients and in GWS, for example, expanding into smart buildings, in Advisory we are increasing our consulting group to drive future growth. And in REI, we're launching new products in life sciences and infrastructure, which is requiring some investment in 2022.

And then you mentioned the 1%. Our margin expectations for this year also include strategic equity grants that we are putting in place to help align a broader set of our leadership team across Advisory and GWS, and that's about a $22 million SOP impact across those two segments.

Alex Kramm
Analyst, UBS Securities LLC

Q

Okay. And sorry, on the Advisory side, what's the right base to use for the margin – flat margin comment? Sorry, just – I don't know if you answered that?

Emma Giamartino
Global Group President, Chief Financial Officer & Chief Investment Officer, CBRE Group, Inc.

A

Excluding OMSRs.

Alex Kramm
Analyst, UBS Securities LLC

Q

Okay. Fantastic. Thank you very much. I'll jump back in the queue.

Operator: Thank you. [Operator Instructions] We have next question from the line of Jade Rahmani with KBW. Please go ahead.

Jade Rahmani
Analyst, Keefe, Bruyette & Woods, Inc.

Q

Thank you very much. I think on a recent markets call hosted by CBRE, your team mentioned that the company intermediated around $400 billion of transactions in 2021, of which around $80 billion was debt placement. So, I wanted to ask in the debt brokerage space, how big a priority is growing that business? Do you see that as meaningful? And I would have expected, you know, the mix between debt and equity to be closer to equal so, that $80 billion baseline seems like there's a big potential to grow.

Robert E. Sulentic
President, Chief Executive Officer & Director, CBRE Group, Inc.

A

Yeah. Jay, this is Bob. We have significant efforts underway to grow all of our lines of business in all three segments of the company and the debt business has grown nicely over the last several years. We expect it to continue to grow. Obviously, the sales numbers that you heard for 2021 and specifically the fourth quarter of the year were the subject of us taking market share in a market that was very strong and that's what you're seeing in those big numbers.

Jade Rahmani
Analyst, Keefe, Bruyette & Woods, Inc.

Q

In a normal market environment, leaving aside current geopolitical uncertainty, do you anticipate that the debt business would be closer to perhaps 30% to 40% of the total?

Robert E. Sulentic
President, Chief Executive Officer & Director, CBRE Group, Inc.

A

I don't think we've put those numbers out there.

Jade Rahmani
Analyst, Keefe, Bruyette & Woods, Inc.

Q

Thank you. As it relates to uncertainty, you know, prior to Ukraine, there was growing uncertainty with respect to the industry at outlook and inflation. Are you seeing or noticing any changes in sentiment or tone from customers, you mentioned, you know, the very strong first quarter results so far in leasing but just want to hear what you're hearing from clients, that they're getting, you know, more cautious, if there's any changes in appetite to transact.

Robert E. Sulentic
President, Chief Executive Officer & Director, CBRE Group, Inc.

A

Well, in fact, the matter is, Jade, some of the biggest news related to Russia and Ukraine has unfolded over the last 24 hours. And everybody's watching that and concerned about that and everybody is concerned about what the impact might be on the global economy. When I say everybody, everybody in our sector. But everybody pretty much in every sector.

The thing that shouldn't be lost in all of these though and we talked a lot about it here today, and we talked about it the last few quarters, we have built a business that is really well diversified across those four dimensions, asset type, client type, service type and geography. And there is a massive amount of commercial real estate around the world that is going to be used in various places depending on what's going on and in various types of assets and services. And because we have a broad footprint across all those dimensions, we're able to push our resources, our management time, our M&A focus, our capital into the areas that we think are most benefited secularly at any given point in time. That's come across in our results the last couple years. It clearly came across in our results for 2021.

So, irregardless of what happens geopolitically here, regardless of what happens in the economy, we are much better positioned than we have been historically and relatively well-positioned to other companies in our sector and other companies across business. And you saw what played out for CBRE relative to the S&P 500 in the wake of COVID-19. So, I think there's real risk out there geopolitically, but I think we're well-positioned to withstand whatever the economy brings in our direction.

Jade Rahmani
Analyst, Keefe, Bruyette & Woods, Inc.

Q

When you think about infrastructure as an opportunity for the company, is there any further dimension that you could put around that? Do you see it as, for example, core within real estate, but expanding the services that are offering or really moving beyond core real estate to areas such as perhaps chemicals, manufacturing, aviation, energy, government? Are you talking about really expanding CBRE's offering into those core infrastructure sectors?

Robert E. Sulentic
President, Chief Executive Officer & Director, CBRE Group, Inc.

A

Well, infrastructure is relevant as today into big areas. Number one, Turner & Townsend. Turner & Townsend does a lot of infrastructure work in a variety of industries and for governments around the world and so we expect that to grow over time. We expect that to grow with Turner & Townsend who is growing very, very nicely in that area.

The second place is we have a relatively small but growing infrastructure investment management business. As that business grows either organically or through acquisitions, we expect it'll touch those other client sources or those other investment opportunities beyond commercial real estate. In fact, it is a separate asset from commercial real estate. It's a real asset class but it's a separate asset class and the projected growth for it over the next decade is enormous as you know.

Jade Rahmani
Analyst, Keefe, Bruyette & Woods, Inc.

Q

So you envision CBRE eventually having infrastructure away from core commercial real estate as a key product offering or business line item?

Robert E. Sulentic
President, Chief Executive Officer & Director, CBRE Group, Inc.

A

We have that today with Turner & Townsend and investment management and we expect it to grow significantly. So, yes.

Jade Rahmani
Analyst, Keefe, Bruyette & Woods, Inc.

Q

Okay. And lastly, within Turner & Townsend, you know, what percentage of their business relates to climate, [ph] build for resiliency, (44:55) you know, energy-related situations?

Emma Giamartino
Global Group President, Chief Financial Officer & Chief Investment Officer, CBRE Group, Inc.

A

Energy-related work is about 10% of the revenue historically.

Robert E. Sulentic
President, Chief Executive Officer & Director, CBRE Group, Inc.

A

And growing. The other thing about that, Jade, and you know, we get that question with regard to our own business. And the answer is not as clean as we would all maybe like it to be when we're answering a question, right? So, we have products or services that are directly attentive to green energy, consulting work we do, project work we do. But our green energy work, our environmental work is embedded across our business. It's in our development business in the nature of the buildings we design and develop. It's in our property management business. It's in our project management business. It's in our facilities management business. It's hugely embedded in our, this massive supply chain we have. So, when you look at a company like Turner & Townsend or you look at the work we do, there's direct specific sustainability work. But then it's, we create advantages for our clients and growth momentum for ourselves due to sustainability-related work we do across all those services.

Jade Rahmani
Analyst, Keefe, Bruyette & Woods, Inc.

Q

Thank you for taking the questions.

Operator: Thank you. We have next question from the line of Steve Sakwa with Evercore ISI. Please go ahead.

Steve Sakwa
Analyst, Evercore Group LLC

Q

Yeah. Thanks. Good morning. I guess, Emma, I'm just trying to sort of piece together a bunch of the numbers that you've put out there and what you guys had on the slide deck. You sort of talk about this low doubles-digit sort of earnings growth from 2021 to 2025. I realize it's not going to be exactly linear by year. If you just sort of took that at face value, that would sort of suggest you'd be up in the kind of high $5 range, maybe pushing $6 a share. I realize you didn't give the exact EPS guidance, but then you also talked about this $300 million additional investment that you're making, and I realize that's within the margin. So, I'm just trying to make sure that when you talk about these additional investments, is that sort of inclusive of that sort of low double-digit growth and so, effectively, you'd be doing a lot more earnings power if you weren't making these investments, or is that kind of a drag in the short term on that 11% to 12% and you hockey stick a little bit more in, you know, say 2023, 2024, 2025?

Emma Giamartino
Global Group President, Chief Financial Officer & Chief Investment Officer, CBRE Group, Inc.

A

No. It's the former. It's that $300 million of investments is embedded in our outlook for this year. And without that investment, our EPS growth would be significantly higher, but we believe those investments are important to drive future growth.

Steve Sakwa
Analyst, Evercore Group LLC

Q

Great. And just as a follow up, as you look at that, do you look at that as sort of a one time or do you think those investments are sort of ongoing maybe not at those levels? Or I guess should we start to see margin improve more? And I can understand you've got to make the investments today, but should we see better margin improvement, you know, say, in 2003 and beyond?

Emma Giamartino
Global Group President, Chief Financial Officer & Chief Investment Officer, CBRE Group, Inc.

A

So, those are ongoing investments that we continue to execute in our business as we're trying to drive incremental growth in the future with new capabilities across our lines of business. I threw out a couple examples earlier. And one thing to note is that in 2021 we invested in our business and we set out to invest to drive growth at the beginning of the year based on the revenue that we anticipated hitting throughout 2021. If we had known revenue would have accelerated the way it did in the latter half of 2021, we would have invested more in OpEx in 2021 than we did. And so you're seeing some of the margin expansion in 2021 as a result of that. So, we weren't able to get our investments up to where we would have if we could have anticipated the growth.

Steve Sakwa
Analyst, Evercore Group LLC

Q

Okay. And then just last question. You know, I know you were pretty programmatic on the buyback. It sounds like, you know, that'll sort of stay in place, maybe accelerate a little bit if the stock, you know, sells off with the equity market pullback. But is that roughly $400 million, is that sort of embedded in, effectively, the guidance or would the buyback benefits all be additive to that kind of low double-digit earnings growth rate? Just trying to figure out how much of the buyback is sort of already in your expectations and how much would be additive?

Emma Giamartino
Global Group President, Chief Financial Officer & Chief Investment Officer, CBRE Group, Inc.

A

We have a modest level of repurchases embedded in our outlook, but not the entirety of it. And the way we look at our programmatic repurchase program is we use it as a balance to optimize our return to shareholders. So, if we see a really strong M&A pipeline, which we do, and we execute some of those larger deals, we'll pull back on our repurchases throughout the year. So, we're really using it as a lever. So, in that outlook, you're seeing a small level of repurchases, you're also seeing a very low level of M&A. And so, any of those uses of capital will be incremental to our growth.

Steve Sakwa
Analyst, Evercore Group LLC

Q

Great. And then, last question, just maybe on that M&A pipeline, I realize you won't name names, but could you maybe just talk about the types of businesses that you're seeing the most activity and where you're most interested?

Robert E. Sulentic
President, Chief Executive Officer & Director, CBRE Group, Inc.

A

Steve, we really look across all three of our segments for opportunities to expand our offering to our clients and grow the business. And of course, strategically, we have particular areas that we're more focused on than others. We don't talk about those publicly until we do a deal because we consider it proprietary information. But I will tell you that we have a very rigorous program that is run between the leadership of our three segments and Emma's corporate development team where we identify specific areas in each of the three segments of the business that we think are particularly well-suited to grow through M&A. And some of that M&A is infill M&A and some of that M&A is more transformational.

We also, we have our eye on a number of what we call sponsorship opportunities that would be consistent with what we did with Turner & Townsend or Industrious where we think we can buy a portion of a company, have them help us in the way we serve our clients and help them supercharge their growth in the way we bring them into our orbit, so to speak, to serve the clients we have.

So, all of those things are part of our M&A strategy. It's broad, it encompasses small deals and large deals, and you should expect to see significant use of capital going forward to further grow the business through M&A.

Steve Sakwa
Analyst, Evercore Group LLC

Q

Great. Thanks. That's it for me.

Operator: Thank you. We have next question from the line of [ph] Matthew Filek (52:02) with William Blair. Please go ahead.

Q

Good morning, everyone, this is [ph] Matt Filek on for Stephen Sheldon. (52:11) Thank you for taking my questions. Was wondering if you can provide some additional commentary on leasing, specifically how much of the strong leasing guidance is driven by a recovery in office versus continued strength in areas like industrial? And have you seen any changes in lease duration?

Emma Giamartino
Global Group President, Chief Financial Officer & Chief Investment Officer, CBRE Group, Inc.

A

So, throughout this year, we're seeing I think, as I mention in my remark, we're expecting recovery across of all asset types, industrials specifically, we're expecting that to slow somewhat as supply becomes somewhat constrained, we're expecting office to return similar to how it did throughout the latter half of 2021. And then what was the second part of your question? Oh, lease terms...

Q

Yeah. Just wondering about changes in lease durations? Those are coming along [indiscernible] (53:10)...

Emma Giamartino
Global Group President, Chief Financial Officer & Chief Investment Officer, CBRE Group, Inc.

A

Lease terms have picked up slightly and continuously throughout 2021. I think new lease terms are up 1% and renewals are up 4%. But they haven't materially moved. So, new lease terms are about six years and renewals terms are at about four years.

Q

Great. That's helpful. Thank you. And then one additional follow up. Can you also talk about the performance between small and large leasing deals? Think you had previously mentioned that large leasing deals were still below pre-pandemic levels in the prior quarter, just wondering if there's been any changes there.

Robert E. Sulentic
President, Chief Executive Officer & Director, CBRE Group, Inc.

A

[ph] Matt, (53:46) large leasing deals have picked up on the office side, but they haven't – we're not back to where we were pre-pandemic. Of course, large leasing deals in industrial have been unlike anything we've seen historically. And in the absence of some supply constraints, we would expect large leases and on the industrial side to continue.

Q

Great. Thank you for that.

Operator: Thank you. [Operator Instructions] Next question from the line of Alex Kramm with UBS. Please go ahead.

Alex Kramm
Analyst, UBS Securities LLC

Q

Yeah, hey. Hello again. Just figured I'd squeeze in a couple of follow ups. Should be quick. Just on your medium term outlook, I think you previously had caveated that with, does not include a return to office, and maybe that's a couple quarters ago. But is office embedded in that? What is embedded in terms of office in your updated guidance? So, yeah, any color there would be helpful. Thanks.

Robert E. Sulentic
President, Chief Executive Officer & Director, CBRE Group, Inc.

A

Alex, we've embedded assumptions about return to the office in our guidance, and they're slightly more conservative than they were in the prior couple quarters. There's just a lot of uncertainty and we see it all over the place with companies trying to figure out and employees trying to figure out the degree to which they'll go back to the office. So, we think that the return to the office is going to be slightly less than we would have thought 90 days ago or 180 days ago and that's embedded in our numbers. We also think though that there's other things that are going on as a result of the way people are looking at their office space usage that are going to help our business, significant opportunity in project management. We continue to believe there's going to be significant opportunity in the flex space arena where we've invested in Industrious and our big clients all over the world are telling us that. And all of those assumptions are embedded in what we've modeled for our business.

Alex Kramm
Analyst, UBS Securities LLC

Q

Fair enough. And then just last one for me, you mentioned the changes to the splits, I believe, I didn't fully catch the comment, was impacting, I think, the margin last year. Can you just remind me what exactly you've done there? And then, also what the reception has been from, I guess, various parts of your brokerage force?

Emma Giamartino
Global Group President, Chief Financial Officer & Chief Investment Officer, CBRE Group, Inc.

A

Yeah. This is an important clarification. It was not a change to splits. It's that as producers do more volume, they enter into a higher tranche of splits. And so, as they did more volume in Q4, they entered – more producers than usual entered into the higher tranche of splits. So, no change to what those tranches are and what the splits are.

Alex Kramm
Analyst, UBS Securities LLC

Q

Okay. Well, thanks for clarifying. That's it for me.

Operator: Thank you. Ladies and gentlemen, we have reached the end of the question-and-answer session. And I'd like to turn the call back to Bob Sulentic, CEO, for closing remarks. Over to you, sir.

Robert E. Sulentic
President, Chief Executive Officer & Director, CBRE Group, Inc.

Thanks everyone for joining us and we'll speak with you again at the end of the first quarter when we give the results for that period.

Operator: Thank you. Ladies and gentlemen, this concludes today's conference. You may disconnect your lines at this time. Thank you for your participation.