Realogy Corporation
Second Quarter 2008 Earnings Call Transcript
August 14, 2008

Note: ***The following is a verbatim transcription of the Realogy Corporation second quarter 2008 earnings conference call. It has been edited from its original version for transcription errors.***

OPERATOR: Good morning and welcome to the Realogy Corporation Second Quarter 2008 earnings conference call via Webcast. Today's conference is being recorded, and a written transcript will be made available in the Investor Information section of the Company's Web site by close of business today. A webcast replay will also be made available on the Company's Web site. At this time, I would like to turn the conference over to Alicia Swift, Vice President of Financial Planning. Please go ahead, Alicia.

SWIFT:
Thank you, Diane. Good morning and welcome to Realogy's second quarter 2008 earnings conference call. On the call with me today are Realogy's President & CEO, Richard Smith; and Chief Financial Officer, Tony Hull.

Before we discuss the Company's Second Quarter 2008 financial results, I would like to call your attention to three items.

First, you should have all reviewed a copy of our financial results press release issued on August 12, 2008, and our second quarter 2008 Quarterly Report on Form 10-Q filed with the Securities and Exchange Commission that same day. As we stated in the Form 10-Q, the 2007 results for the three and six months ended June 30, 2007 have been reported on a pro forma combined basis. They have been prepared to give effect to the Company's April 10, 2007 acquisition by Apollo Management, L.P. and the related financing transactions as if they had occurred on January 1, 2007 and combine the Company's financial results for the predecessor period from the beginning of the period -- January 1, 2007 or April 1, 2007 -- through April 9, 2007, and the successor period, from April 10, 2007 through June 30, 2007.

Second, the Company will be making statements about its future results and other forward-looking statements during this call. Statements about future results made during the call constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These statements are based on current expectations and the current economic environment. Forward-looking statements and projections are inherently subject to significant economic, competitive and other uncertainties and contingencies, many of which are beyond the control of management. The Company cautions that these statements are not guarantees of future performance. Actual results may differ materially from those expressed or implied in the forward-looking statements.

Important assumptions and other important factors that could cause actual results to differ materially from those in the forward-looking statements and projections are specified in our 2007 Form 10-K and Form 10-Qs for the quarters ended March 31, 2008 and June 30, 2008 under the sections "Forward-Looking Statements" and "Risk Factors" and other periodic reports that we file.

Third, we will be referring to certain non-GAAP financial measures during the call. Our August 12 press release, which is posted on the investor information section of our Web site, contains definitions of these terms, a reconciliation of these terms to their most comparable GAAP measure, and a discussion of why we believe these non-GAAP financial measures are useful to our investors.

Let me briefly review the headlines from our release issued on August 12 regarding Realogy's second quarter 2008 results. Specifically for the second quarter, we reported …

- Revenue of $1.4 billion,

- EBITDA of $161 million, and
- A Net Loss of $27 million – which is after $153 million of interest expense and $55 million of depreciation and amortization.
- Our revolver balance as of June 30, 2008 was $205 million.
- Our Senior Secured Net Debt to Adjusted EBITDA Leverage Ratio for the trailing 12 months ended June 30, 2008 was 4.9 to 1, in compliance with the terms of our credit facility.

Now, I'd like to turn the call over to Realogy's President and CEO, Richard Smith.

SMITH:
Thank you, Alicia.

Good morning and thank you for attending our Second Quarter 2008 earnings call.

Before I get into our operating performance and business unit accomplishments, I'd like to briefly review our operating philosophy as well as the overall housing market and some of the broader economic factors that are impacting our business.

Although cyclical patterns are a normal part of the residential real estate industry, it is fair to say that the depth and length of the current housing downturn has proven exceedingly difficult to predict. We are now entering the fourth year of a housing downturn. Since the downturn in residential real estate began in August 2005, this is the 37th consecutive month in which our industry and our business have been under considerable downward pressure.

Throughout this downturn, we have held steadfast in taking a long-term view of what we know to be a dynamic and cyclical industry. At the same time, we have been proactive and effective in increasing productivity and reducing our operating costs. This is a trademark operating characteristic for Realogy, one that is important to helping us meet the challenges of a cyclical industry and a challenging economic environment.

In addition to our focus on productivity and costs, we have continued to implement strategic growth initiatives that we believe will pay future dividends. Our launch of the Better Homes and Gardens Real Estate brand less than a month ago certainly speaks to our long-term commitment to growth. Although we are building from the ground up, we are excited about building a new real estate franchise network around an iconic American brand name that is recognized and trusted around the world.

Cyclical industries require focused, cost-conscious and forward-thinking management. I am proud of the fact that we have such a management team, and I am equally proud of the efforts that have been made by our employees to maintain a disciplined approach to spending in today's challenging economic environment.

When the housing market turns – and it will turn, the only question is as to the timing – but when it occurs, I remain confident that Realogy will be far better positioned to capitalize on the market than our competitors, most of whom we believe have not been as disciplined in taking out costs or increasing productivity during this down cycle.

Clearly, the timing of a housing recovery remains the greatest variable and challenge facing the industry today.

At this juncture, the National Association of Realtors, or NAR, is still forecasting improving year-over-year trends in the housing market in the second half of 2008, assuming increased affordability of housing, pent-up demand and improved mortgage availability due to government initiatives. NAR has taken down its 2008 forecast from being flat on sides and price to down 9% and 6%, respectively. Fannie Mae remains more conservative than NAR, calling for a gradual recovery to begin in the first half of 2009.

In terms of unit sales, NAR is projecting 5.1 million existing home sales in 2008, which would be a decrease of 9% over the prior year. Fannie Mae has continued to upwardly adjust its full-year 2008 forecast on unit sales and is currently forecasting 4.9 million existing home sales, which would be a 14% decline over 2007. So there's your likely range on units – down somewhere between 9% and 14% nationally for the year.

In terms of price, NAR and Fannie Mae have a variance of 3% in their year over year price forecasts, with NAR forecasting a median 2008 price of approximately $207,000 and Fannie at approximately $200,000. Averaging them together, their forecast on home price declines in 2008 is somewhere between a 7% and 8% decline year over year. We believe this reflects the significant influence that foreclosures and short sales have on pricing.

We are encouraged by the recent passage of the Housing and Economic Recovery Act as a positive development for both the real estate industry and consumers. We believe that the greatest near-term impact of the bill will be to increase the availability of credit for first-time and mid-market homebuyers.

Although it's too early to know the success lenders will have in implementing the recovery act provisions, we believe the refundable first-time homebuyer credit; higher permanent loan limits and the foreclosure rescue package – will help chip away at inventory levels, stabilize prices and spur activity assuming that the overall health of the U.S. economy and consumer confidence don't deteriorate further. As you know, each of those factors is under significant pressure.

Although we continue to see improved affordability levels and good activity at the lower to middle segments of the market, we cannot be certain as to when the credit markets will start to return to a more normal state or when the general economy will start to improve. Consequently, we cannot accurately forecast the timing of a housing recovery.

We are frequently asked, "Has the housing market hit bottom?" and/or, "When will it hit a bottom?" The best answer to that question is discussed in two parts – in the context of sides and price.

With regard to transaction sides, we believe that unit volume has settled into a relatively narrow range that could be termed a "sloppy bottom." As evidence, NAR's seasonally adjusted annualized home sale unit number has remained between 4.9 to 5.0 million units dating back to last Fall. Absent a further tightening of an already challenged credit market, we expect that trading range to continue throughout the end of this year. We also expect year-over-year comparisons for transactions to strengthen in the fourth quarter because NAR's seasonally adjusted annualized sales figure first started stabilizing around 5 million homes in the Fall of 2007.

Unfortunately, the same cannot be said for home prices which continue to be negatively impacted by high inventory levels, foreclosures, a challenging financing environment at the higher home price levels and other market pressures. The uncertainty about price declines seems to be driving the headlines and that has definitely had an affect on consumer confidence as well. Interestingly enough, NAR's chief economist recently pointed out a downward distortion in the existing price

data which he attributed to an increase in short sales and foreclosure activity. The mix of business issue is certainly impacting the national home sales price reports.

Following the rules of supply and demand, it is reasonable to expect that as prices decline, the number of transactions will increase. We are seeing this trend occur in a few of our markets both in our franchise segment and owned brokerage operations.

Here are several additional notable – and conflicting – real estate market trends to highlight:

- The NAR Housing Affordability Index fell seven points from May to June to 119. However, the June index is still 7% to 12% higher than it was at the year's end for 2005, 2006 and 2007.
- Mortgage purchase application volume decreased 2% during the week ending August 8, and is at or near its lowest level of the year, according to the Mortgage Bankers Association weekly application survey.
- In late July, RealtyTrac released its foreclosure data, reporting that the number of homes entering some stage of the foreclosure filing process increased by 14% in second quarter of 2008 compared to the previous quarter, and by 121% on a year-over-year basis. Of the approximately 740,000 homes that were in some stage of the foreclosure filing process, 220,000 were actually lost to a foreclosure during the second quarter.
- NAR reported that housing inventory levels rose a fraction of a percent from May to June to a total of 4.5 million homes for sale. That represents an 11.1-month supply at the current sales pace, and that's up from a 10.8-month supply in May.
- NAR's Pending Home Sales Index released last week showed an increase in sales contract activity in June across all four regions of the country.
- According to the Census Bureau, the U.S. homeownership rate held steady at 68% from the first to the second quarter, which is also the same as in the second quarter a year ago.
- The most recent S&P Case-Shiller Home Price Index released in July reported a 16% decline in home prices from May 2007 to May 2008.
- And looking at Case-Shiller against three other leading home sale price reports for the same time period yields interesting contrasts:
    - The REAL Trends Market Report, which is a compilation of actual transaction activity covering more than one-third of all U.S. home sales, showed approximately an 8% year-over-year drop in average sales prices for the month of May.
    - NAR reported that the national median existing home price for all housing types was down approximately 6% from a year ago in May.
    - The Office of Federal Housing Enterprise Oversight ---which like Case-Shiller tracks 'same house' sales price activity but looks at the data on an equal-weighted basis across a wider geographic region -- reported that U.S. home sales prices fell 5% for the 12 months ending in May 2008.
    - Thus, the variance looks like this: Case-Shiller down 16%, and Real Trends, NAR and OFHEO down in the range of 5% to 8% for the same May 2007 to May 2008 period.
    - As we have pointed out in the past, the Case-Shiller Home Price Index is not the standard by which we measure or forecast price.
- Lastly, since we often point to demographics as the main driver of demand for housing, I thought I'd share this population milestone that was just reported in July by the National Center for Health Statistics. More than 4.3 million babies were born to U.S. families in 2007. And what makes this particularly interesting is that this figure is higher than any year during the height of the Baby Boom. A lot of households increased their size last year, and history supports that their housing needs will grow as well.

  - Also relevant to the current housing situation, the Harvard Joint Center for Housing studies reported that changes in the number and age distribution of the adult population should lift household growth to 14.4 million from 2010 to 2020, and that's a 14% increase from 12.6 million from 1995 to 2005.
  - The demographics clearly continue to be supportive of the long- term health of the housing industry.

Now, let's discuss our operating performance and business unit accomplishments.

The Realogy Franchise Group has been very busy under the leadership of CEO Alex Perriello:

- The licensing agreement between Realogy and Meredith Corporation became operational last month. We officially launched the Better Homes and Gardens Real Estate brand on July 23 at a prominent industry conference in San Francisco where we introduced our first franchisee, Better Homes and Gardens Real Estate Wilkins & Associates, a prominent established broker located in northeast Pennsylvania. We have been pleased with the response from within the industry to the launch of this new franchise system, and we are in ongoing conversations with a strong pipeline of prospects interested in franchise opportunities with this new brand both in the U.S. and internationally.
- RFG had domestic franchise sales in the second quarter of $171 million in gross commission income or GCI, and that's a year-over-year increase of 24%.
  - In our new franchise sales, we continue to see the average company GCI increase which reflects our focus on conversions of larger, established brokerages rather than start-ups and smaller operations.
- The total GCI retained and added in the last 12 months as a result of new franchise sales and renewals was $1.1 billion dollars, compared with only $288 million that was either terminated by Realogy or not renewed by the broker.
  - As we have discussed previously, RFG created a strategic development team last year to proactively identify and assist brokers who have been adversely affected by the housing downturn. This team assists individual franchisees who are having difficulty managing through the downturn with solutions that are unique to our multi-brand strategy. Through mergers, acquisitions, group walk-overs and other creative solutions, this team has retained approximately $108 million in GCI for our Realogy brands since its inception in mid-2007.
- One other item of particular note for the Franchise Group is that our Sotheby's International Realty brand was recently rated as the No. 1 most prestigious real estate company in the 2008 Luxury Brand Status Index survey of high-net worth consumers.

Now, on to NRT, our Company-Owned Brokerage Services segment. During the second quarter of 2008, Bruce Zipf, NRT's CEO, and his team have continued to reduce their operating costs while improving their operating efficiency and retaining their productivity. NRT has been well ahead of the rest of the residential real estate brokerage industry in terms of proactively managing through this downturn and leading by example.

As we mentioned on our last call, NRT was working toward a target of consolidating approximately 70 brokerage office locations. This goal was accomplished, which will reduce storefront costs by $15 million dollars on an annualized basis.

We measure our success in consolidations by looking at the agent revenue retention rate. During the second quarter, NRT management retained approximately 92% of the GCI from its top two quartiles of productive sales associates. As we have noted in the past, the top two quartiles of productive agents at NRT generate approximately 88% of our company-owned store revenue.

NRT's cancellation rate in June was 13%. This was consistent with prior year levels for NRT. In the first six months of 2008, cancellation rates ranged from 11% to 15%.

In a continuation of its efforts to increase efficiency and reduce its operating overhead, NRT recently consolidated a number of back-office support functions from nine of its local operating companies into two regional support centers. This regional model has already been successfully implemented elsewhere within NRT.

On the acquisition front, NRT closed one transaction in the second quarter and continues to look for accretive acquisitions. Given market conditions, NRT management is focused on walkovers, or the group recruitment of experienced, productive sales associates. Thus far this strategy has proven to be very successful, financially and operationally which allows us to grow in a very capital efficient manner.

NRT's REO division is the largest independent Real Estate Owned asset management company in the United States. This division's transaction volume of foreclosed properties nearly doubled in the second quarter of 2008 as compared to the second quarter of the prior year to approximately 10,000 units.

CARTUS, our relocation services firm, led by CEO Kevin Kelleher and his team, continues to attract new clients, and for the first half of 2008 established a record in new client signings. Cartus' second quarter was highlighted by an impressive new signing with Procter & Gamble – for both its domestic and international relocation needs. Halliburton and Adidas were among the other very noteworthy additions to our client list. Overall for the quarter, Cartus signed 43 new clients, which is helping offset some softness it is seeing with its existing client base.

Looking ahead, we believe that the current challenging economic environment may create additional opportunities to expand Cartus' client pipeline as more companies consider outsourcing relocation services rather than keeping that function in-house. As the market leader, Cartus is well positioned to capitalize on that trend.

At TITLE RESOURCE GROUP, CEO Don Casey and his team have addressed the challenges of declining unit volume from NRT by expanding other facets of the business. TRG continues to work with very prominent national lenders to grow its lender channel volume.

Management has continued its focus on its underwriter channel, generating increasing levels of net premiums driven by TRG direct title operation volume in newly licensed states, notably Florida and New Jersey. According to a title industry report published in June, TRG ranked third among the Top 10 national underwriters based on net operating increases for the first quarter of 2008.

TRG continues to improve its capture rate for NRT's REO Division in Florida, which was primarily driven by lender controlled business. And in total, TRG opened more than 1,000 REO title orders, which accounted for about 3% of its purchase title and closing unit volume during the second quarter.

As we mentioned last quarter, TRG is spearheading the development of a Web-based transaction management software platform called Home Base. This innovative system currently is being piloted in approximately 20% of NRT's brokerage offices. Within the next three years, NRT will manage its sales transactions via this internally developed, Web-based paperless system.

Now, I'd like to discuss specific regional trends we are seeing, and provide some color from certain local markets.

At NRT, Florida continues to show signs of reaching a bottom with unit sales up 1% for the three months ended June 30 of this year versus same period last year. For the month of June 2008, unit sales were 4% greater than June 2007, further highlighting an improving market in Florida. Also, the California real estate markets where we operate that have been hardest hit over the last three years, namely San Diego and Sacramento, are showing signs of rebound and have had an increase in unit sales over the last three months. For the three months ended June 30 of this year versus same period last year, unit sales increased 9% and 29% in San Diego and Sacramento, respectively. Most of this unit sale increase is from increased foreclosed home sales activity, and as a result, the year-over-year average sales price decreased by 21% and 30%, respectively, for the quarter. This activity is corroborated by the California Association of Realtors' increase in units during each of the past three months.

Other markets that are showing signs of improvement are Dallas, San Francisco, Minneapolis, and Washington, D.C.

Now as for New York City, our Corcoran operations were down from record levels in the second quarter of 2007. The super-luxury market -- those over $10 million -- remains resilient. Where we are seeing impact from the sagging financial services sector is in the lower price points in Manhattan as well as Connecticut, Westchester and New Jersey. The Hamptons are also showing weakness, although the rental market over the summer remained buoyant.

As for some of NRT's most-challenged markets, Arizona, Utah and Atlanta, they continue to suffer the most in terms of year-over-year comparisons in transaction volume among all the NRT markets. Recently added to this list are Baltimore and Boston which both performed fairly well for most of 2008, but in the last two months have weakened considerably.

In our Franchise Group, our Western region franchisees performed the best in the second quarter with unit declines of 16%. California had unit increases of 2% offset by price declines of about 19%. In contrast, Washington state experienced unit declines of 35% and price declines of 8%. The Northeast region was hardest hit in the second quarter with volume declines of 28%. New York, New Jersey and Pennsylvania had volume declines between 27% and 30%. As you can see, the dynamics vary greatly from market to market, illustrating once again that all real estate is local.

With that, I have just a few closing comments:

- Clearly the housing downturn did not abate in the second quarter, and it has now entered its fourth year.
- That said, a number of factors, not the least of which is the U.S. government's direct involvement, point to improving conditions.
- We believe there are very early signs of a developing bottom. The issue, of course, is exactly when. We do think it is sooner rather than later, but of course we can't know for certain.
- In the interim, management has worked very hard in taking every precaution. We continue to manage our costs down, only commit capital when absolutely necessary, and, simultaneously, we have made prudent investments in the long-term growth of our company.

With that, I will turn the call over to Tony.

HULL: Thank you, Richard. I am going to discuss the details of our second quarter financial results as well as address certain capitalization issues. I will be referring to the tables in the press release as well as several pages of the 10-Q.

Looking at Table 1 of the press release, total net revenue was $1.4 billion as compared with $1.8 billion on a pro forma combined basis in the second quarter of 2007. This is a 22% decrease and was mainly a result of lower transaction volume at RFG and NRT. The breakdown by revenue category is as follows:

- Gross commission income totaled $1.04 billion at NRT.
- Service revenues totaled $208 million, primarily from Cartus activities, and the remainder is TRG revenue relating to purchase and refinancing closing activity as well as title underwriting revenue.
- Franchise fees totaled $91 million and consist of both upfront and on-going RFG domestic and international franchise fees.
- Other revenue of $51 million includes marketing fees that RFG collects from its franchisees, revenue from NRT's REO business and net interest income from Cartus' relocation services.

Total commission expense of $685 million decreased $232 million quarter over quarter mostly as a result of lower transaction volume. Looking at NRT's gross margin as calculated by dividing commission costs by commission income, you will note that the margin improved from 33% in Q2 2007 to 34% in Q2 2008.

Table 2 of the press release compares 2007 results as if the Apollo transaction had occurred on January 1, 2007 to 2008 reported numbers, which are in the right-hand column of the table. As you can see, 2008 operating expenses of $422 million were $35 million or 8% lower year over year as we continue to see the impact of storefront and other cost reduction initiatives.

Marketing expenses of $60 million were down 14% or $10 million in the second quarter of 2008 versus the second quarter of 2007 as a result of our continued efforts to migrate toward more affordable and effective media solutions.

Finally, second quarter 2008 general and administrative expenses of $55 million decreased 25% as a result of lower IT, finance and legal expenses across the company.

Looking on Table 4 of the press release at those same categories for the six months ended June 30th:

- Operating expenses of $851 million were $49 million, or 5% lower year to date
- Marketing expenses of $115 million were down $29 million, or 20% lower year to date
- General and administrative expenses of $118 million decreased $30 million, or 20% year to date

Next I would like to discuss our key business drivers for the second quarter. Feel free to follow along on Table 5 of the press release.

RFG home sale sides decreased 21% in the second quarter of 2008 compared to the second quarter of 2007. NRT home sale sides decreased 19%. Results at both RFG and NRT were directionally in line with NAR and Fannie Mae, which have reported existing home sale unit declines for the second quarter of 16 and 17 percent, respectively.

Average home sale price decreased 5% at RFG and 8% NRT in the second quarter of 2008. RFG's numbers were slightly better than those reported by NAR and Fannie Mae. At NRT, the mix of business and the impact of foreclosure activity put downward pressure on its average price. NRT's year-on-year average price decline went from minus 1% in the first quarter to minus 8% in the second. We are seeing a relative shift in mix of property transactions from the high range to lower- and middle-range homes due to constrained availability of jumbo mortgages and

relative strength in our middle and lower market segments as mortgage availability, especially FHA loans, remains okay. Remember that in 2007, the activity at the higher end of the market was relatively stronger than other market segments and this bolstered NRT's average sales price. The number of foreclosure sales brokered by NRT offices represented about 8% of NRT's units in the second quarter of 2008. This also affected the average sales price at NRT.

Royalty rate at RFG was up 9 basis points to 5.10% in second quarter, and the average broker commission rate was up 3 basis points at RFG to 2.52%. Average broker commission rate for NRT held steady at 2.48% year over year.

Taking a look at the drivers for our other two business segments, at Cartus we experienced a 16% decrease in referral volume from brokers. This tracks similarly to industry-wide volume declines during the second quarter.

At TRG, purchase title and closing units declined 18% which goes hand-in-hand with the sales volume declines experienced at NRT. Refinance units were flat year over year due to the overall level of mortgage rates. It should be noted that incremental title units related to foreclosed home activity that NRT is brokering are directed by the mortgage lender or servicer and is not a controllable opportunity at TRG.

I will now discuss revenue and EBITDA by business unit for the second quarter ended June 30, 2008 as reflected on page 57 of the 10-Q.

Total revenue at RFG was $185 million compared with $241 million in 2007. The 23% revenue decline is in line with the change in home sale sides and average home sale price shown on the driver table along with lower intercompany royalties from our company-owned segment, NRT. Offsetting these declines was the 9 basis point increase in royalty rate mentioned earlier. Total EBITDA at RFG was down 34% for the second quarter 2008 versus 2007. This was a result of the revenue decreases discussed above. Lower costs realized from initiatives put in place over the last three quarters were offset by increases in non-cash bad debt reserves and higher development advance note amortization.

At NRT, total EBITDA was down $39 million. Revenue declined $333 million due to lower home sale volume. This was mostly offset by lower commission and royalty expense along with $53 million of marketing and other operating expense reductions positively impacting the quarter.

At TRG, EBITDA declined as a result of lower home sale unit volume. This was offset to a degree by increased volume from the lender channel.

Revenue at Cartus shown on page 57 of the 10-Q for 2008 versus 2007 decreased 10% and EBITDA was $23 million, down $10 million on a pro forma combined basis from the prior year comparable quarter. The declines were due to lower referral revenue which is being affected in three ways:

1. First, on the origination side of our relocation transactions, the time it takes transactions to close has increased from last year so referral revenue and unit volumes are delayed.
2. Also on the origination side, decreased home values are lowering referral revenues from closed home sales
3. Finally, on the destination side of the transaction, more relocating employees are electing to rent versus buy, thereby reducing referral units in their destination location.

Benefitting EBITDA in the quarter, on the expense side was a $5 million reduction in insurance accruals as a result of lower loss rates.

I would like to take a moment to update you on Cartus' exit from our government relocation business. As of June 30, 2008, we had approximately $218 million of assets (that's homes and other receivables) in the Kenosia facility down from $272 million at end of March. At the beginning of August, there were 268 unsold inventory homes remaining under this facility, down from just under 500 at December 31, 2007. Our intent is to sell these homes as quickly and as close to their acquired values as possible. Remember that we took an incremental reserve of $14 million at the end of 2007 to reflect the updated values of the 500 at risk homes that were in inventory at that point in time. We currently anticipate that the reserve will be adequate. The disposition effort will be most prominent in the third and fourth quarters. As of today, we still expect a cash benefit of $50 million from the exit from the government business in 2008.

Turning to the balance sheet on page 6 of the 10-Q, we ended the second quarter with a $205 million balance on our revolving credit facility. This represents about $35 million in favorability from the $240 million quarter-end forecast that we provided in the mid-May conference call. The improvement is mostly due to timing differences between the second and third quarters. The reported balance sheet cash as of June 30 was $124 million, this total includes $29 million of available cash, $38 million of statutory cash required for our title business and $57 million which represents a negative cash reclassification of cash balances held in certain bank accounts. This reclassification effectively increases cash and accounts payable equally.

Also on the balance sheet you can see that relocation properties held for sale that include our government fixed fee business dropped 32% to $125 million and that overall securitization debt on the right side of the balance sheet fell by over $100 million to $898 million.

Capital expenditure spending is shown on the cash flow statement on page 7 of the 10-Q. As you can see, it was $24 million year to date versus $53 million for the same period in 2007 as a result of our ongoing effort to be conservative with cash spending. Similarly, M&A spending dropped from $42 million during the first six months of last year to $11 million this year. Of the $11 million spent in 2008 so far, $4 million related to earn-out payments on prior-year deals.

As Richard mentioned, our focus in the second quarter was more on organic growth via recruiting and walkovers than traditional M&A activity. This enables us to acquire gross commission income with minimal upfront cash.

As shown on page 70 of the 10-Q, Adjusted EBITDA for the 12 months ended June 30th was $679 million. Adjusted EBITDA is calculated based on EBITDA of negative $318 million for the 12 months ended June 30, 2008. That's shown about 7 lines down on the table. The first two major adjustments to the reported 12-month trailing number are merger, restructuring, separation and former parent legacy costs and the 2007 Impairment charge, which together total $766 million. With those items adjusted out, the starting point for the 12-month period is $448 million. To that we add a total of $231 million of adjustments that are prescribed in our credit agreement. These include:

- The pro forma impact of fourth quarter 2007 costs savings of $20 million. This factors in the total Q4 2007 completed restructuring actions of $58 million to reflect what their impact would have been had they been in place on July 1, 2007
- The pro forma impact of 2008 cost savings of $20 million. This includes completed actions taken in both the first and second quarters of this year and reflects what their impact would have been had they been in place on July 1, 2007
- The next item is the removal of $82 million of losses or expenses incurred in the last 12 months relating to business optimization initiatives. This figure includes the impact of a number of completed actions including the movement of $17 million in certain employee-related fixed costs to variable, $17 million related to certain material NRT contract

renegotiations, and $29 million related to the exit from the government fixed fee at-risk home sale business.

- The next add-back is $45 million of non-cash charges. These include $36 million for the change in allowance for doubtful accounts and reserves for development advance notes and also $7 million for stock based compensation
- Purchase accounting adjustments of $15 million are added back
- The pro forma effect of NRT and RFG acquisitions for franchise sales of $15 million are added back and reflect the contributions as if they occurred as of the beginning of the 12-month period
- Apollo Management fees of $14 million are added back
- Wright Express proceeds of $11 million are included
- Incremental securitization costs of $5 million are included
- And finally start-up costs relating to BH&G Real Estate franchise brand of $4 million are added back.

At June 30, 2008, total Senior Secured Debt plus capitalized lease obligations less readily available cash totaled $3.3 billion. That divided by Adjusted EBITDA of $679 million for the 12 months ended June 30,results in the senior secured net debt to Adjusted EBITDA ratio of 4.9 to 1.

The pro forma adjustment provision in our Credit Agreement is designed to encourage management to maximize productivity gains and cost reductions. These pro forma adjustments are based upon actual actions taken by management, for example, completed headcount reductions, completed office closures, completed contract renegotiations and completed business exits during the trailing 12-month period. These are not adjustments we take lightly, and we are proud of the efficiencies our team has achieved. We will continue to take actions as warranted by market conditions.

While we are not giving guidance for the third quarter or the year, we continue to point to NAR and Fannie Mae's forecast for the balance of 2008. NAR currently expects 2008 existing home sale units of 5.1 million, a 9% decrease from 2007. On the other end of the spectrum, Fannie Mae currently expects existing home sale units of 4.9 million in 2008, a 14% decrease from last year. If you look at the quarterly detail of their forecasts, both entities continue to forecast a reduction of year-over year unit sales declines as the year progresses. We are seeing this same trend at RFG and NRT. In July, RFG and NRT unit declines were 16% and 12%, respectively, versus declines of 21% and 19% in the second quarter. Looking ahead, this September we lap NAR's drop in annualized unit activity to the 5 million run rate level that we've been seeing for the past 10 months. Assuming that 5 million number holds, we would expect to see RFG and NRT's sides declines to drop from the teens to single digits accordingly.

As Richard indicated, the price side of the equation is of concern to us for the balance of the year. NAR expects a 6% full-year price decline while Fannie Mae expects a 9% price decline. To update you on our actual results, price declines in July held at minus 7% at RFG and minus 9% at NRT. To put the NRT numbers in perspective, in the third quarter of 2007, NRT's average sales price was approximately $540,000. In July of this year its average was $495,000. That's due to a mix of business, and is a fairly dramatic change.

Just like every other cycle, once prices come down enough, we expect that units will start to increase, and prices will follow. We are seeing the cycle progress as expected in several markets, including big unit improvements in many markets in Florida, California and elsewhere. I would like to draw your attention to statewide data reported by the California Association of Realtors and Florida Association of Realtors.

While CAR reported unit declines in the first quarter of 28%, it reported second quarter unit increases of 13%. It took price declines of 32% in California in April to make units start to increase. Also, California inventory levels decreased to 8 months supply in June down from 10 months a year earlier. This should help stabilize prices going forward. FAR reported unit declines in the first quarter of 26% but only a 6% decline in the second quarter. Prices are down 16% in the first half of the year in Florida. Although it is too early to predict, the cycle seems to be taking its course in these two states that were the first two to see the housing slowdown. These are two extreme examples and we would expect to see nationwide price and unit movement to be significantly less dramatic.

Our cash flow expectations have changed since our first quarter conference call due to a number of factors.

- The first of two significant developments that I will highlight is our election to roll the $2.4 billion of floating term loan balance to a monthly rather than quarterly interest payment schedule. This election saves us approximately $700,000 a month in interest expense but will increase our revolver draw during the third quarter by about $30 million.
- The second development relates to Cartus' UK Relocation securitization. As noted in our second quarter 10-Q, the UK securitization is at its maximum capacity of 100 million pounds sterling due to the deteriorating state of the UK housing market. As a result, homes in the securitization are selling slowly, very slowly, and any new home sale advances are now being funded entirely with Realogy's revolver rather than funding them from the Cartus UK securitization. Fortunately, this is a timing issue as the UK government is looking at ways to address its housing issues, and historically UK housing cycles are typically much shorter than those in the US. Until the recovery, this situation could raise our anticipated revolver draw. Also as a reminder, the value of the assets secured in this facility are not a Realogy risk as our UK clients (which are mostly UK government agencies) reimburse us for the float until the homes are sold and are responsible for any loss incurred in the ultimate sale of the home. We are working on a number of possible solutions to mitigate the adverse cash-flow impact of the UK securitization situation.

For 2008, we currently expect to pay approximately $570 million in cash interest expense. This number could increase modestly if we continue to decide to roll our floating rate debt monthly rather than quarterly, but this would be offset by interest savings in 2009. The other cash items remain within the ranges we mentioned on our year-end conference call in March.

We continue to prudently and proactively manage expenses as the housing downturn enters its fourth year. While we cannot predict the macro impact the economy at large will have on our business, we are committed to maximizing operating efficiencies as warranted by market conditions wherever possible for as long as necessary. We know that housing is a cyclical business – the market will turn, it is just a question of when….and when it turns we believe that Realogy will be poised to take full advantage of the rebound.

With that, I'll turn it over to Alicia to review the questions that were submitted in advance of our call that we have not already addressed in our prepared remarks.

SWIFT: Thank you, Tony. As we move into Q&A, our prepared remarks have addressed many of your questions and we have tried to consolidate similar questions and provide a single response.

1. Do you see any issue meeting covenant compliance?
SMITH: As stated in the 10-Q, based on a forward four-quarter forecast, we expect to remain in compliance with our senior secured net debt leverage ratio covenant . This forecast does not contemplate additional debt or equity financing.

2. Can you provide an update on the contingent liabilities?
HULL: There have been no significant changes on the contingent liabilities since our call last quarter. In terms of the bulk of the contingent tax liabilities, we continue to expect that this will be resolved in late 2009 to 2010.

3. Since your revolver balance was favorable in the second quarter, can we expect this favorability to continue through the remainder of 2008?
HULL: No, the favorability of cash was due to timing between the second quarter and third quarter.

4. As a percentage of non-seasonally adjusted existing home sales sides, why does RFG's market share appear to have declined for 2 consecutive quarters?
SMITH: Well, we believe our market share has remained relatively stable. We believe NAR's survey data has inherent sampling errors of somewhere between 3% to 5%. So we're comfortable with our current position.

5. Why did the Letter of Credit use go up from $41 million to $131 million?
HULL: The main driver of the increase is a $67 million letter of credit issued to secure the surety bond we posted in connection with our appeal of the Credentials litigation.

6. Consisting mostly of international royalties and upfront international fees, why did RFG other revenue decline year-on-year in the past two quarters?
SMITH: The timing of new international deals is highly variable and comparisons against prior year are not necessarily indicative of the current environment. International royalties increased at RFG year over year in the second quarter. And in the second quarter of 2007, there were several international deals closed which generated upfront fees resulting in unfavorable comparisons quarter over quarter. This is a timing issue.

7. What is your current revolver balance?
HULL: We are not providing an inter-quarter update on our revolver balance. We disclosed the balance in our May release because the balance was materially higher than the March 31st reported balance.

8. Are you planning on consolidating additional NRT offices?
SMITH: The majority of our office consolidations are behind us. That said, we are very focused on maximizing the efficiency and profitability of our offices and will adjust as warranted by market conditions.

9. Please help us understand what drove the increase in payables and the decrease in accrued expenses in the quarter?
HULL: The increase in accounts payable is due to the cash classification issue discussed previously. The decrease in accrued expenses is primarily due to normal seasonal reductions in accrued manager variable compensation and franchise royalty rebate payments as well as a decrease in accrued interest. As discussed earlier, we have been paying the floating rate interest

on the Term Loan monthly rather than quarterly thereby decreasing the accrual at the end of the quarter.

10. Are you investigating a second lien financing that would help you get around a potential third quarter 2008 covenant violation? What is the permitted indebtedness currently permissible under the credit agreement?
HULL: As Richard stated earlier, based on our current forecast which is completed on a forward four-quarter look, we currently expect to remain in compliance with our senior secured net debt leverage covenant. The Credit Agreement contains restrictions on the incurrence of indebtedness, but it does permit certain debt incurrences. As you know, the Credit Agreement and Indentures are publicly available.

11. The add back for 2008 pro forma cost savings increased from $15 million at the end of Q1 to $20 million at the end of Q2. Similarly the business optimization initiative savings increased from $70 million at the end of the first quarter to $82 million. What led to the increased savings here? Please provide detail on the additional cost savings and on the expected timing to realize these savings.
HULL: The additional cost savings in Q2 reflect the completion of 70 NRT office consolidations in 2008, the consolidation of a number of back-office support functions at NRT that Richard discussed earlier and some reductions in force.

The business optimization expenses are detailed on page 71 of the 10-Q.

The cost savings are expected to be realized over a 12-month period depending on when the actions were initiated. For example, the 2007 cost savings should be realized by year end. The 2008 Q1 actions should be fully realized by the end of first quarter 2009 and similarly the Q2 actions will be fully realized by the end of Q2 2009.

12. After all of the cost reductions, how much investment will be required to return to previous levels of profitability when the cycle turns?
SMITH: Throughout this downturn we have continued to invest in our business and create efficiencies, which we believe will improve our margins and profitability in an improving market. But to be very specific, the majority of the cost reductions are expected to survive even after the market turns.

13. What is the current health of the franchisees? Has the Company re-negotiated any franchise contracts in order to aid the franchisee?
SMITH: All things considered we believe our franchisees are managing through this downturn as well as can be expected. And as we mentioned, in those instances involving troubled franchisees, we offer services to assist them. There may be isolated cases in which we have taken a franchisee's financial health into consideration when renewing a franchise agreement but that's the exception, not the rule.

14. What were REO sales as percentage of RFG during the second quarter?
SMITH: We do not specifically track REO sales at the affiliate level for a variety of reasons. Anecdotally, there are markets where franchisees believe REO sales represent up to 30% of their business. But again, that is in isolated markets. The good news is that where the REO business exists, we are capitalizing on that dynamic.

15. Is revolver availability affected by amount drawn on synthetic LCs? What happens in a scenario in which the Company's liquidity is not enough to cover required contingent payments? If the synthetic LCs is drawn does the amount due become payable soon thereafter or does the synthetic LC facility convert to a term loan.

HULL: The Synthetic Letter of Credit is currently undrawn and Company expects to satisfy any potential payments of its contingent liabilities through either cash from operations or drawing on its main source of liquidity, our $750 million revolver. In the unlikely event any portion of the $500 million LC is drawn by our former sister companies to satisfy a specific contingent obligation, we would immediately repay the LC using our revolver. Funds drawn on the LC are immediately repayable and cannot be converted into term loan borrowings.

16. Please disclose the changes in offices since year end at RFG and NRT?
SMITH: At June 30, 2008, we had approximately 16,000 franchised and company owned offices which included approximately 900 of our company owned and operated brokerage offices. At December 31, 2007, we had approximately 15,700 offices which included approximately 940 of our company owned and operated brokerage offices.

17. You attributed the price decline at NRT to a change in sales mix. Is it the case that the high-end homes are not selling or are they simply selling at a lower price?
SMITH: No, the high-end homes have certainly not escaped pressure on pricing. The good news is they are selling but at lower prices. The pricing and availability of Jumbo financing is also a significant factor in this market. It is definitely a mix of business issue.

18. If the downturn continues into 2010, what are some of Apollo's plans to cure the potential violation of covenants?
SMITH: Well, we and Apollo are very focused on covenant compliance and are well aware of the options available to us, if they are necessary. We have demonstrated our ability to proactively take the steps that are necessary to maintain covenant compliance.

19. Did Apollo buy any of the debt during this quarter?
HULL: Any questions about Apollo's actions should be directed to Apollo.

20. How does your current market outlook compare with your outlook at the time of the first quarter earnings call in May?
HULL: The trends we expected back in May seem to be materializing on the sides part of the equation, however, price has and will continue to be more difficult to predict.

21. Do you expect to continue paying interest on the senior toggle notes in kind?
HULL: Until we indicate otherwise, we will continue to pay in kind.

22. Has Realogy repurchased any of its debt to date?
HULL: As reflected on the balance sheet, Realogy has not repurchased any of its debt.

23. The relocation receivables and relocation properties held for sale declined by a combined $64 million yet the net change in securitized obligations declined by $116 million. Where is the cash derived for the remainder of the payment? Can revolving credit usage and general corporate cash be utilized to reduce the receivable facilities?
HULL: The securitization balances increase and decrease based on asset movements. The first half of the year required us to fund approximately $50 million from our revolver in terms of working capital. Please recall that the waiver received to exit from the government business required a step down in the level of borrowing under the Kenosia facility of approximately $40 million. So that accounts for the bulk of the $50 million in the first half of the year.

24. Please give more color on your REO asset management business? Volumes? Total revenues and EBITDA?

SMITH: As we mentioned in our prepared remarks, we are one of the largest independent REO asset management companies in the US. We have seen substantial increases in our volume but we do not disclose the specific revenue and EBITDA related to this business.

25. Can you provide an update of NRT revenue by region and average home sale price as you did in your 2006 reports (i.e. Midwest, Southern California, Tri-state, etc.)?
HULL: We disclosed geographic concentrations of NRT data in the 10-K annual report.

26. What were some of the factors contributing to higher home sale commission rates? Would we expect higher commission rates going forward?
SMITH: We believe higher commission rates are a function of lower average sales price. And to the extent that average price continues to fall, we would expect the average broker commission rate to remain steady or slightly improve.

27. Has the environment for mortgage financing worsened since the Freddie/Fannie problems became very public?
SMITH: Well, what remains important to us in this environment is that FHA and VA financing remain available and is a growing part of how consumers are financing their home purchases. Clearly, Freddie and Fannie having explicit rather than implicit government support, and that is viewed by us and the industry as a positive development.

SWIFT: That concludes the Q&A portion of our call. Thank you, Richard and Tony. I have two quick points of information to add, and then we will conclude today's call:

- First, we will make a transcript of this call available on the Investor Information section of the Realogy.com Web site by the close of business today.
- Second, we anticipate announcing our Third Quarter 2008 results in mid-November, with the exact date still to be determined.

We thank you again for taking the time to join us on the call, and we look forward to speaking with you next quarter. Thank you.

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