

Realogy Holdings Corp.

Capitalization Summary (\$MM)

Price	\$25.45
Diluted Shares (MM)	145.1
Market Cap	\$3,693
Total Debt	\$3,725
Cash	(\$224)
Enterprise Value	\$7,194

Share Ownership and Trading Data

Average Daily Trading Volume (MM)	1.6
52-Week Price Range	\$37.85-\$22.22
Short % of Float	2.5%
Major Shareholders	Insiders 1.4%



Valuation and Misc. Stats (\$MM) 9/30/16

Book Value	\$2,464
Price/Book Value	1.5x
EPS (ttm)	\$1.14
Price/Earnings	22.3x
Adj. EBITDA (ttm)	\$771
EV/EBITDA	9.3x
Dividend Rate/Yield	\$0.36/1.4%

P&L Analysis (\$MM)

Fiscal Year Ending December 31,	2013	2014	2015
Revenues	\$5,289	\$5,328	\$5,706
Operating Income	\$525	\$537	\$558
Margin	10.3%	10.5%	10.3%
Adj. EBITDA	\$796	\$779	\$845
Margin	13.6%	13.6%	13.5%

Catalysts/Highlights

- Any stabilization of transaction volume trends or competitive activity at NRT should dramatically improve investor sentiment
- RLGY's high FCF yield (10.5%) should enable accelerated share repurchases
- More drastic action such as a sale or split-up of the Company is within the realm of possibilities

INVESTMENT RATIONALE

Realogy's Company-owned brokerage services (NRT) and franchise services (RFG; includes brands such as Century 21 and Coldwell Banker) make it the leading residential real estate broker in the U.S. Realogy's relocation and title and insurance services offer another captive revenue stream; additionally, its relocation services business is a useful lead generator. Brought public in 2012 at \$27/share by Apollo, following a 2006 LBO, Realogy shares have declined 50% from mid-2015 highs of ~\$50 and now trade below the IPO price. The recent declines reflect stalled earnings growth after a sharp post-recession rebound; following another cut to guidance in conjunction with the announcement of 3Q16 results, RLGY management now forecasts just \$750-\$770 million in operating EBITDA in 2016 versus \$723 million in 2013. The challenges have been most pronounced at NRT, which contributes ~57% of segment EBITDA (FY15) after backing out inter-company royalty payments to RFG. NRT's homesale transaction volume, the principal driver of its results, has markedly underperformed national trends since late 2014. NRT's average homesale prices have been roughly flat since 2015 and the number of closed transactions declined 4% Y/Y in 3Q16. This principally reflects market-level challenges in NRT's markets, which are concentrated in the high end of prime coastal metro/luxury markets. At the same time, NRT has experienced heightened competition for top broker/agent talent, leading to some loss of market share and operating margin erosion.

Without a doubt, Realogy's business model has proven to have less operating leverage than investors anticipated. However, we remain comfortable with the Company's competitive position. While market conditions are unlikely to improve in the near term for NRT, this appears to be a temporary slowdown in a larger post-recession recovery which still has plenty of room to run. Broker/agent competition appears to be driven more by the current macro environment and new entrants in key markets rather than any radical disruption of the business model, and this headwind should moderate somewhat over time. Meanwhile, Realogy's franchise business sports attractive ~65% EBITDA margins and has not faced the magnitude of headwinds that NRT has. Looking longer term, the brokerage business is driven by favorable underlying factors, with housing transaction volume growing at a 7% CAGR over many decades. The U.S. housing market has yet to fully recover from the crisis and affordability levels remain elevated, suggesting there could be a return to historical average transaction volume growth rates in the not-too-distant future. Realogy also recently expanded its cost savings initiative and now expects to generate \$60 million in run-rate annual cost savings by mid-2017.

At the current share price, investors appear to be improperly ascribing permanence to—or even a worsening of—current real estate market conditions. Realogy shares trade at just 8.6x EV/Adj. EBITDA (2016E) and offer a remarkable 11% 2016E FCF yield on a fully taxed basis, adjusted for the estimated present value of Realogy's tax assets. By comparison, RLGY has traded at a post-IPO average of ~12x EV/EBITDA. In estimating Realogy's intrinsic value, we conservatively project the Company does not return to ~5% EBITDA growth rates until 2019. Valuing the Company at 13x forward FCF (fully taxed) or 9.5x EV/EBITDA (TTM), we derive a 2019E intrinsic value of approximately \$41 per share—implying 18% IRR potential. If real estate market conditions improve sooner than we project, investors may not have to wait this long to see a marked recovery in RLGY shares.

In the interim, Realogy offers a compelling de-levering/FCF story, aided by its extensive tax assets (~\$500 million NPV of NOLs) which should shield cash taxes into 2020. RLGY expects to generate \$425-\$450 million in FCF (~\$3/share) in 2016, and we project FCF could reach ~\$540 million by 2019. RLGY has rapidly de-levered in recent years to 3.8x covenant-adjusted EBITDA as of 3Q16, opening the door for return of capital to shareholders. RLGY initiated a modest dividend (1.4% yield) in August 2016 and authorized an initial \$275 million share repurchase program in February 2016. RLGY repurchased \$134 million of shares (~3%) at ~\$30/share YTD 3Q16 and the pace of repurchases is likely to accelerate given the recent share price declines. We project RLGY could spend an incremental ~\$1.2B on repurchases beyond the current authorization over the next three years while maintaining its current leverage ratio—translating to incremental repurchase capacity of another ~35% of the current market cap. Finally, should shares continue to flounder, we would not dismiss the possibility that Realogy again becomes a private equity target, considering the highly attractive economics implied by our projections. Alternatively, Realogy could pursue a separation of the franchise business into a standalone company in order to highlight its more stable, higher-margin revenue stream, which would likely garner a premium valuation.