Walker& Dunlop

November 6, 2019
8:00 am ET

Operator: Welcome to Walker & Dunlop 's third quarter, 2019 earnings conference call and webcast. Hosting the call today from Walker & Dunlop is Willy Walker, chairman and CEO. He is joined by Steve Theobald, chief financial officer, and Kelsey Duffy, vice president of investor relations. Today's call is being recorded and will be available via webcast on the company's website. At this time, all participants have been placed in a listen only mode and the floor will be open for your questions following the presentation. If you would like to ask a question at that time, please press star and one on your touch tone phone. If at any point your question has been answered, you may remove yourself from the queue by pressing the pound key. We ask that you pick up your handset to provide optimal sound quality. Lastly, if you should require operator assistance, please press star and zero. It is now my pleasure to turn the floor over to Kelsey Duffy. Please go ahead.

Kelsey Duffy: Thank you, Bre. Good morning everyone. Thank you for joining the Walker & Dunlop third quarter of 2019 earnings call. I have with me this morning our chairman and CEO, Willy Walker, and our CFO, Steve Theobald. This call is being webcast live on our website and a recording will be available later this morning. Both our earnings press release and website provide details on accessing the archive webcast. This morning we posted our earnings release in presentation to the investor relations section of our website, www.walkerdunlop.com These slides serve as a reference point for some of what Willy and Steve will touch on during the call.

Please also note that we will reference the non-GAAP financial metric adjusted EBITDA during the course of this call. Please refer to the earnings release posted on our website for a reconciliation of this non-GAAP financial metric. Investors are urged to carefully read the forward looking statements language in our earnings release. Statements made on this call which are not historical facts may be deemed forward looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 forward looking statements describe our current expectations and actual results may differ materially.

Walker & Dunlop is under no obligation to update or alter our forward looking statements whether as a result of new information, future events or otherwise, and we expressly disclaim any obligation to do so. More detailed information about risk factors can be that can be found in our annual and quarterly reports filed with the SEC. I'll now turn the call over to Willy.

Willy Walker: Thank you, Kelsey. Good morning, everyone, and thank you for joining us. The third quarter was one of the most successful quarters in Walker & Dunlop 's history, due to strong financial results, record numbers of bankers and brokers hired, positive regulatory decisions, the implementation of technology in new and innovative ways, and the continued progress towards our 2020 goal of generating $1 billion in annual revenues. As shown on slide three we generated $212 million of total revenues in Q3, a 15% increase from a year ago, which drove diluted earnings per share of $1.39, a 21% increase over last year's Q3. As Steve will discuss later during a quarter when we added a significant number of bankers and brokers to the platform, we still generated outstanding financial returns, due to the strength of our underlying business model. With over $1 million of revenue per employee, the $92 billion servicing portfolio, generating huge amounts of cash, and a debt to equity ratio of 0.3 times, we feel exceedingly well-positioned financially to continue growing our business.

On the first day of Q3, JLL closed on its acquisition of HFS. The combination of these two competitor firms created an unprecedented recruiting opportunity for W&D and we took advantage of it, growing our sales force by 13% during the quarter. There are three primary reasons for our recruiting success. First, we recruited a number of talented teams away from the large global real estate services firms in 2018, and those teams played a major role in establishing a reputation within the industry that W&D is a great place to work and succeed. Second, with HFF being acquired by JLL, and Eastdil Secured being spun out of Wells Fargo, Walker & Dunlop sits somewhat uniquely as the client-focused commercial real estate finance company with big company capabilities, yet the touch and feel of a family-owned business. The client focused-world of commercial real estate, finance and sales, that combination of big company capabilities, the small company touch and feel, is gold. And third, the culture W&D is very different from many of our competitor firms as we celebrate collaboration and reward exceptional sales performance. Those three cultural and market factors combined make Walker & Dunlop a fantastic place for highly talented professionals to join and be successful.

On the regulatory front, the Trump administration's white paper on housing finance reform, coupled with the release of FHFA's 2020 multifamily GSE scorecard, were welcome developments during the quarter. Ending the conservatorship of Fannie Mae and Freddie Mac, as outlined in the administration's white paper, would be a very positive development for the housing finance industry and Walker & Dunlop . The 2020 GSE multifamily scorecard, announced by the Federal Housing Finance Agency in September, provides Fannie and Freddie with $100 billion each of lending capacity over the next five quarters. So as you can see from slide four, it's up from past annual volumes. The scorecard sent a clear message that FHFA, under the new leadership of director Mark Calabria, views the capital provided to the multifamily market by the GSEs as vital, particularly as part of the solution to the current affordable housing crisis in America.

As you can see on slide five, the Mortgage Bankers Association's most recent forecasts the size of the multifamily finance market in 2020 is $390 billion. Combining Fannie and Freddie's combined market share will be around 41% they use all of their capacity. 41% market share in an expanding market provides for volume growth for both GSEs. It also pushes their market share down to levels where the regulator would like to see them. The clarity provided by the 2020 scorecard allows Walker & Dunlop to continue to benefit from our strong market position and scale with the GSEs, while also continuing to focus on building out other areas of our business that will complement our future growth.

I'll now turn the call over to Steve to discuss our Q three financial performance in more detail and then I'll come back to discuss our progress towards Vision 2020 and how technology is transforming our business. Steve?

Steve Theobald: Thank you, Willy, and good morning everyone. Once again, our unique market position and focused business model generated strong financial performance across the board. The third quarter results add to our exceptional year-to-date performance, positioning us well to meet our 2019 financial targets. Total transaction volume for the first nine months of the year was $22.2 billion the 19% year over year increase, led by growth in property sales, Fannie Mae, and brokered volumes. We continued to enjoy a macro economic backdrop that is constructive for US commercial real estate, particularly multifamily.

Turning now to slide six during the quarter, our overall transaction volumes increased by 16% from last year, including record quarters for brokered originations, at $3.1 billion up 29% from last year, and property sales of $1.6 billion, up 83% from last year. These are the two areas in which we have been heavily investing and you can see the success of those efforts coming through in our transaction volumes.

Our overall GSE volume of 3.8 billion in the quarter was down slightly year over year as an increase in Fannie Mae volumes was offset by declining in our Freddie Mac volumes. Our HUD volume picked up in the quarter to $281 million, up 42% from Q3 of 2018. The combination of higher volumes with Fannie and HUD, and the increase in the margin on our Fannie Mae business during the quarter, resulted in a gain on sale margin of 162 basis points, an increase from 150 basis points last year.

I wanted to spend a few moments talking about what we see as the potential impacts of the new GSE scorecard on our financials going forward. To begin with, the clarity over what the market opportunity is for Fannie and Freddie over the next five quarters is welcome. With $200 billion of combined lending capacity through the end of 2020, the GSEs will continue to be the dominant providers of capital to the multifamily industry and this will benefit W&D as one of their largest partners. You wouldn't know it from our strong Q3 financial results, but we did see a significant slowdown in Fannie and Freddie's lending volumes in September, as they waited to see what the new FHFA scorecard would bring. And it took them most of October to ramp their lending back up and start with winning business again. With both GSEs out of the market for September and October, we expect to only originate around $1.5 billion of loans with each GSE in Q4. While that is below our typical Q for lending volume for Fannie and Freddie, given the construct of the new scorecard, a slow Q4 will simply push more capacity into 2020. Both GSEs are fully back in the market today; given the robust pipelines we have across our entire lending platform, we are very optimistic about our outlook over the next five quarters. I would add that even with light GSE volumes in Q4, W&D should still finish 2019 with double digit growth in revenues and earnings, as we established at the beginning of the year.

Revenue for the quarter was up 15% from Q3 '18, to $212 million, bringing year-to-date total revenues to $600 million, up 18% from the same period in 2018, driven largely by the increase in transaction volumes year over year. Our year-to-date financial metrics are highlighted on slide seven. Diluted earnings per share was $1.39 for the quarter, up 21% from the same period last year, while year-to-date diluted EPS was $4.11, up 15% from last year as we remain on track to deliver double digit EPS growth in 2019. As you can see on slide eight, servicing portfolio, was at $91.8 billion as of September 30th and continues to fuel growth in servicing fees, which contributed $159 million in year-to-date revenues, an increase of 8% year over year. Our portfolio now includes over 7,000 loans and continues to exhibit strong credit fundamentals. During the quarter, the average LTV and debt service coverage ratio for new loans was 67% and 1.47 times, respectively, consistent with the historical healthy levels that have characterized this commercial real estate cycle.

Adjusted EBITDA remained strong in the third quarter at $55 million, down slightly from $58 million in Q3 '18, as growth in cash revenues was outpaced by growth in expenses, primarily the $15 million a year over year increase in personnel costs, which was driven largely increased commission expense. The $11 million increase in non-cash MSR revenues in Q3 did not benefit adjusted EBITDA in the quarter but will contribute to higher cash servicing fees and therefore adjusted EBITDA growth in future periods. Year to date adjusted EBITDA was 184 million, up 15% from the first nine months of 2018, driven by our strong growth in cash revenues.

We achieved a third quarter operating margin of 28%, bringing year-to-date operating margin to 29%, well within our annual target range of 27 to 30. As Willy mentioned, we had amazing success in recruiting new original origination teams into our company during the quarter. Expenses related to recruiting and onboarding our new recruits total of approximately $2.5 million. Q3 personnel as a percentage of revenue was 44%, up slightly from 43% in the third quarter of last year, even as we have added a 115 employees to the company over the past 12 months. Year-to-date 2019 personnel as a percentage of revenue was 42%, up from 40% in 2018 but within our historical range.

We ended the third quarter with $66 million of cash on the balance sheet and an additional $138 million being used to fund agency loans rather than borrowing on our warehouse lines, bringing our total available cash to $204 million. During the quarter, we use $2.7 million to buy back 50,000 shares, leaving us with $45.8 million of board-authorized repurchase capacity.

Our strong cash position and financial results continue to support our quarterly dividend payment. Yesterday, our board of directors authorized a dividend of 30 cents per share, payable to shareholders of record on November 22nd, 2019. We continue to grow our overall capital base while still generating strong returns, with a return on equity of 18% for the third quarter and 19% for the year-to-date period, right in the middle of our high teens to low 20% target range.

Our third quarter and year-to-date financial results are reflective of both our competitive advantage in the market today, as well as our profitable business model, which continues to generate the cash we are investing in future growth. The recruiting success achieved this quarter sets the stage for a fantastic 2020 and beyond and we aren't even close to done yet. With that, I will now turn the call back over to Willy.

Willy Walker: Okay, thank you Steve. The Q3 and year-to-date financial results that Steve just ran through illustrate the growth Walker & Dunlop has achieved by remaining focused on our long-term mission of creating the premier commercial real estate finance company in the United States. Vision 2020 was established in 2016 as a roadmap to generating $1 billion in annual revenues by the end of 2020. The hiring and investments we have made over the past several years, including the 22 talented bankers and brokers we hired in Q3 alone, will provide the human capital and sales growth to achieve Vision 2020.

Our revenues for the 12 months ended September 30th were $815 million. Adding $185 million of incremental revenues over the next five quarters will be challenging, but we have brought on the people and made the investments to have a real shot at achieving that goal. The cornerstone of Vision 2020, as outlined on slide nine, is continuing to scale our debt financing platform to originate $30 billion to $35 billion of annual loan volume. While we were already a market leader with the GSEs and HUD when we established Vision 2020, we knew there was a large opportunity to scale our debt brokerage business across the nation and we have done just that, growing our broker volume from $4.2 billion in 2016 the $9.3 billion over the last 12 months. Scaling our depth brokerage platform has helped to fuel growth in our overall mortgage banking volumes, which were $17 billion in 2016 and have grown to $27 billion on a trailing 12 month basis, a fantastic. 59% increase over 2016. Given the additions to our debt financing team this year in the overall macro-economic environment, we should reach our goal of $30 billion to $35 billion by the end of 2020.

The second component of Vision 2020 was launching and growing a multifamily property sales business annual volume of $8 billion to $10 billion. We entered this business in 2015 with the acquisition of Engler Financial and over the past four years we have added 28 property sales brokers across the country and grown our sales volume to $4.4 billion over the last 12 months. Our growth has been dramatic and impressive and with 50% of our current team having joined us just this year, we have visibility on brokering $8 billion to $10 billion worth of multifamily properties in 2020.

The third pillar of Vision 2020 and clearly the most lucrative is building $100 billion dollar loan servicing portfolio. For the past several years, we have added an average of $10 billion of net new loans to our servicing portfolio on an annual basis, and with the portfolio at $92 billion today, we are within striking distance of our $100 billion goal. W&D is now the seventh largest commercial loan servicer in the country, and with an average servicing fee of just over 23 basis points, an average loan duration of just under 10 years, we have an asset base and cash flows that make W&D look a more look a lot more like an asset management firm than a mortgage bank. Crossing the $100 billion dollar mark in 2020 will be an amazing milestone and provide us with long-term repayment protected cashflows that we can continue to reinvest in our business.

The final piece of Vision 2020 is to build an $8 billion to $10 billion fund management business. This is the one component of Vision 2020 that we are unlikely to achieve, but we have made great progress over the past 18 months in entering and scaling this business. The acquisition of JCR Capital in 2018 brought with it around $750 million in assets under management, as well as a registered investment advisory platform to raise new funds. We ended Q3 2019 with one $1.6 billion in assets under management at JCR and in the Walker & Dunlop Blackstone Mortgage Trust joint venture, and given the momentum we are seeing in raising JCR Fund Five, as well as a new separate account with a long standing Walker & Dunlop partner, we will have established a good sized fund management platform at Walker & Dunlop by the end of 2020, with the opportunity to reach our goal of $8 billion to $10 billion in AUM in the following years.

While we focused on achieving Vision 2020 we are already setting building blocks in place for our next five year strategic plan. We have had an amazing track record at Walker & Dunlop of establishing and achieving five-year BHAGs. BHAG stands for stands for "big, hairy audacious goals, " a term established by Jim Collins in his legendary book, "Built to Last." One component of W&D's BHAG will invariably be technology. Over the past 18 months, we've made significant strides in driving efficiencies in our business processes. As we've implemented technology to become more efficient, we have also aggregated large amounts of data to make us more informed in our credit underwriting and more insightful to our clients. We've also built a database that combines loan details with operating data from our servicing portfolio that allows us to accurately project property performance on a borrower's entire portfolio, even in cases where the borrower may have never done a loan with Walker & Dunlop . Since we started using this database a year ago, we have originated 65 loans for 39 different sponsors totaling over one $1.9 billion of new loan activity. We have just scratched the surface of what we can be achieved through our technology and data analytics investments, and we are very excited about how these initiatives will continue to change the way our clients view W&D and the insight our bankers and brokers can provide.

Before I close our prepared remarks, I'd like to loop back to what I said at the beginning of this call. Q3 2019 was one of the most successful quarters in Walker & Dunlop 's history, due to our financial performance, recruiting success, regulatory clarity, technological implementation, and continued progress towards our long-term strategic goals. We've had plenty of quarters with one or two those areas showing fantastic performance, but rarely all five and that is extremely exciting. Two weeks ago, for the first time ever, we brought together our entire company to hear from our executive team and outside speakers, participate in training sessions, and celebrate our collective success. We held the meeting in Dallas, Texas, and as our president of Howard Smith said, when we do things at W&D, we do them big. The all-company retreat was a wonderful way to welcome the new employees who joined us in Q3 and to underscore what makes Walker & Dunlop such a great place to work for our 811 employees.

One of our outside speakers was Bill Emerson, who for 15 years as CEO of Quicken Loans transformed Quicken into the largest single-family mortgage originator in the United States, while consistently being ranked a great place to work with exceptional customer service. Bill listened to a number of the W&D presentations before he spoke and encouraged W&D to think big and continue down the technological innovation path that we have started to implement. Bill didn't need to tell anyone in the audience to think big, but his insights, after having scaled Quicken, at what he described as "the intersection of culture and technology" were incredibly informative and appropriate given where W&D finds itself today in executing on our long-term growth plan and mission to become the premier commercial real estate finance company in the United States. We will continue to recruit exceptional bankers and brokers to Walker & Dunlop , leveraging off our position as a company with big company capabilities yet the touch and feel of a family-owned firm. We will continue to drive towards Vision 2020 to achieve our financial goals and grow the services we provide to our loyal and fantastic customers and we will continue to develop and deploy technology to make us smarter, more efficient, and more insightful in all we do.

I'd like to thank my Walker & Dunlop colleagues for all you do to make our company so great and congratulations on a fantastic Q3. With that, I'd like to ask the operator to open the line for questions.

Operator: The floor is now open for questions. At this time, if you have a question or a comment, please press star and one on your touch tone phone. If at any point your question is answered, you may remove yourself from the queue by pressing the pound key. Again, we do ask that while you pose your question, you pick up your handset to provide optimal sound quality, and we'll take our first question from Jade Rahmani with KBW. Please go ahead.

Jade Rahmani: Thanks very much for taking the question. Just in terms of the 2020 commentary you provided with respect to the MBA forecast of $390 billion, that implies about 9% growth. Is that what you're internally expecting for the overall market?

Willy Walker: You know, Jay, I mean we, you look at those numbers as you know, Freddie Mac also gives their estimate of market size as well. We-- we don't have an internal economist group to make our own projections as far as the overall market size. But given the velocity of the market today, without any external shocks from a macro economic standpoint, I think that's probably a pretty good calculation that the MBA has. No reason to not think it's a good number.

Jade Rahmani: And have you dug into the drivers of that increase? What would be driving the growth at this point in the cycle given, you know, cumulative multiple years of extremely strong production?

You know, is it new deliveries? Is it construction loans? Is it you know, refis? What-- what's driving that level of growth?

Willy Walker: So there were-- I believe the MBA had projected 320,000 new units delivered in 2019. So you have all that-- those deliveries, which by the way had been absorbed extremely well by the market. And then you also just have a lot of capital chasing deals and therefore transaction volumes, I think, are underpinning a lot of that number. Jade. So there's a core refinancing number in there, which by the way, we do not have a significant volume of refinancings in our portfolio for 2020. But there's a core refinancing volume and then there's a lot of new M&A activity of trades and investments, sales. And given the growth of our investment sales platform, we look to be a big beneficiary both on the investment sales side as well as on the lending side.

Jade Rahmani: In terms of the recruiting environment, you've stepped up recruiting, it seems, just based on press releases meaningfully in the quarter. And I believe this was in advance of the FHFA scorecard. So just want to get your-- some insight into your thinking about, you know, what gave you the confidence to ramp up a recruiting, carry those personnel costs, and thinking about the dynamic of potentially having to grow, you know, the brokered and potentially even a private label CMBS counterweight business, which could have lower margins than the agency business.

Willy Walker: If you look at the recruiting we did in the quarter, Jade, the majority of the, the bankers and brokers that joined us, we're in our investment sales business and in our capital markets business. So the-- we have been scaling those two platforms as both Steve and I mentioned during our prepared remarks. And the-- the growth of those two business lines has been outstanding. And yet at the same time, there's still a huge amount of growth for us to capture in both of those businesses. So the recruiting we did for instance, in the investment sales space, all of those hires are, are putting brokers in new geographies. So we added teams in the quarter in places like Southern Florida. We added another banking team in Houston. We added an investment sales team in Chicago. We added an investment sales team in Portland, Oregon. We added an investment sales team in San Diego. So we're adding talent to the platform in geographies where we have not had coverage in the past. And so all of that is not only great to expand into those geographies, but to some degree it's, you know, it's 100% of accretive cause we don't even have bankers and brokers in those markets prior to those hires. So all of that is just very net beneficial to the underlying platform, where we don't have an existing operation. and today we do.

Jade Rahmani: Thanks very much for taking the questions. I'll get back in the queue.

Operator: Our next question will come from Steve Delaney with JMP securities. Please go ahead.

Steve Delaney: Hi. Good morning. Thank you. Good morning and congratulations on the strong quarter. Going back for just a minute to the GSEs, back away in late August and September, Willy, in your mind, was that close to a hundred percent cap driven and, you know, the momentum in their volumes or could it have also possibly been due to the rate volatility we were seeing? I mean they, yes-- you know, caps are an issue but also they, when they're pricing loans, they need to know what the execution is going to be in the securitization market as well. So I'm-- I'm just curious if you have any thoughts on that or have talked to anybody at the GSEs? It kinda gave you some clarity on, on why they reacted so cautiously. Thank you.

Willy Walker: Good morning Steve. And thanks for being on the call. I would, I would put forth to you that it had very little to do with rates and everything you-- you annual volumes and two things. One, trying to make sure that as the regulator under new director Mark Calabria was defining the 2020

Scorecard, that they were not doing volumes that would make the FHFA and the regulator put a-- put a downward cap on their 2020 volumes. So, I think both of them were running at a pace up until August that was going to put them into a number well North of $75 billion of annual origination volumes each. And I think they both felt that if they continued at that pace, that there was a real chance that the regulator would put in a downward to the caps for 2020. So they both hit the brakes, basically saying, "we're not going to go over that number and we're going to stay at that number for 2019."

And I would say to you as well, once they'd put on the cap or the brakes, and then the regulator came out with the scorecard, what we have seen before is that neither GSE, no lender, can just snap their fingers and come right back into the market. And as Steve said, to (inaudible) both of them are right back in the market, and the business we're doing, we love and they're both playing their commensurate role, if you will, in the markets today. But it took them awhile to get back up and get going. But the clarity the new scorecard has provided has been fantastic because we know the role that they're going to play going forward. And I would also add that it is the first scorecard under director Calabria. So this was the moment where director Calabria would establish the role he wanted to see Fannie and Freddie play in the multifamily space, and it was a very, very positive scorecard.

Steven Delaney: Yeah, that's helpful and thanks-- thank you, you and Steve, for giving the clarity that you gave us on 4Q, because it was, it was unclear to us how much, how much of that impact would have been in 3Q and 4Q. And, and I think we have that answer now. But rolling out to 2020, you know, $100 billion, I mean, I think the market, we all took the new caps and the structure as being an improvement under the under the old structure and $100 billion, you know, over five quarters, sounds like sounds like a lot, but also we can't overlook the-- the requirement that 37.5% of that needs to be classified as affordable. So as you look at your mix of business, you know, now in terms of larger loans and newer projects that may not be deemed affordable, you know, could that be a potential barrier for you? And also, you know, in terms of borrower demand for larger loans that wouldn't be considered affordable, could we still get a little tight next year in that regard? Thanks.

Willy Walker: Yeah, on the affordable side, Steve, both Fannie and Freddie said both publicly and, well, personally that they should have no problem hitting the 37.5% affordable requirements, given their historic business mix. So it's great that the regulator has them focused on that market segment and that they will continue to provide capital to that market segment because it is very much needed. But as it relates to any challenges as it relates to their lending mix, we've heard no, if you will, concerns or warning signs from either of them that that's going to be overly challenging.

And then as it relates to larger loans as you, as you well know, we've had you in our history, we've done sort of mega portfolios. But our average loan size at W&D is somewhere around $18 million or $19 million bucks. So actually some of our large competitors such as JLL and CB, they-- they are sitting there doing $50 million and $60 million loans. I would say that there might be a moment where Fannie and Freddie do shy away from those larger loans a little bit and the, and the class A stuff, they'll still do them, but they might shy away from them a little bit. For us, which is more of a, you know, middle market firm that does institutional business, I don't see any issues as it relates to our overall deal flow and not finding a home for those-- for those (inaudible)

Steve Delaney: Thanks, Willy. Yeah, Steve?

Steve Theobald: Yes, perspective-- Yeah, sorry, with respect to a W&D we're, we're extremely active in the affordable space ourselves. We are, you know, one of the largest manufactured housing community lenders with the agencies and we'll continue to do that. So, you know, I think we'll, we will certainly be contributing our share of that 37.5% over time.

Steven Delaney: Got it. And Steve, one for you, on page three, you know, the trends obviously all look great. You know, year over year, up 15% to 20%, but and if you-- EBITDA surprisingly down 6%, I apologize if you explained that, but could you remind me what that is or is there one particular item in there that they caused that decline?

Steve Theobald: Yeah, I think Steve, we this particular quarter we obviously had a significant increase in MSR income, which doesn't count towards, you know, EBITDA, because we back out cash-- cash revenue. Yeah. And if you look at just the, the amount of hiring we did in the quarter, plus commission expense that we paid out this this quarter, given the success we had on the volume side, those cash expenses, you know, essentially exceeded our cash revenues this particular quarter.

Steven Delaney: Got it. Got it. Thank you both for the comments.

Operator: Our next question will come from Henry Coffey with Wedbush.

Henry Coffey: Good morning, and let me add my congratulations on a great quarter. When we look at at profitability metrics. I know you didn't mention, you know, that MS-- that your servicing fees are sort of coming down as, as some of the older product matures. Are we about where, where that gross number will be for the next few quarters around 23 basis points?

Willy Walker: Henry, it is super hard to predict. Obviously I'm not knowing what the future's gonna look like, but I, you know, we, we had seen in that average servicing fee rate over the last few quarters and that certainly slowed in Q3. I mentioned this in my remarks, that we did see an increase in our Fannie Mae servicing margins this past quarter. I think a function of, you know, a little bit less competitive dynamic in that space resulted us seeing an increase there. I think you're still seeing servicing fees from 10 years ago rolling out of the portfolio. And 10 years ago you know, we were still not long removed from the great financial crisis and that was a period of time when there wasn't much lending activity going on outside of the agencies. So, you know, that dynamic still exists.

I think the other thing that is still occurring is the mix- the overall mix of our servicing portfolio is changing as we're doing more broker business with life insurance companies. That servicing is, you know, being added to our portfolio in many cases. And those are, you know, coming on at lower than our average servicing fee rate.

Henry Coffey: Thank you. And then I know you sort of just went over this, but basically we're talking about in the fourth quarter, not a dramatic falloff in Fannie and Freddie volumes, but basically going to $3 billion-- is the brokered business turning out to be more robust going into year-end with rates where they are? Should we be altering our total origination estimates all that much? I know this could have a, you know, more brokered, less Fannie. Freddie could have an impact on GAAP earnings, but then be equally positive to EBITDA. So what, what should we be thinking about? Know you got the two, the $3 billion number, is there an offset from the brokerage side of the business? And then obviously, the expectation would be for a bigger than expected March. Am I thinking about all this the right way?

Steve Theobald: Yeah, Henry, I think without obviously giving guidance around origination volumes for Q4, I think, you know, we-- while those, well the Fannie/Freddie volumes that we discussed in the call for Q four are, you know, below what we would typically expect to see in a fourth quarter, we're obviously still pretty optimistic about the future here. The markets are still very good. You know, Jade asked specifically about the MBA forecast, so, you know, we clearly are still seeing strong financing volumes out in the marketplace.

Willy Walker: I just jumped in on that, just quick. First of all, we're one month into Q4, so we look at a pipeline and we're trying to tell the market about where Fannie and Freddie were for September and October, which has driven our pipeline to where it is today. And we're giving people some insight into what we think Q four is going to look like there. I think that the Q3 numbers, from a capital market standpoint, show the growth that we are experiencing that business line. And so broadly to your question, yes. Our capital markets business has been growing significantly and there's nothing in the market that would say that it should not continue to grow. And so just under a lot underscoring what Steve said, the overall financing market and property sales markets today are transacting, you know, at a great pace. It's a very healthy environment. We're not the only company in our industry that is reporting good earnings this quarter. And I think a lot of people see tremendous opportunity going forward. I would say that with the hiring we have done, we've positioned ourselves exceedingly well to have increased volumes across all of our lines in 2020 and 2021 and that - Steve pointed to in his prepared remarks - that's what really gets exciting is when you take the hiring we did in Q3 and you play it into the P and L for 2020 and 2021 we, we've hired a lot of growth in Q3 of this year and that's great.

Henry Coffey: Just on a bigger picture, you know, we, we went through the FHA white paper about other comments. I think he's talking about a $20 billion IPO or something with the GSEs. But as this business evolves, is there a 'tweener market developing something between the GSEs and the insurance companies? Are there people that, you know, picked up that white paper and said, "Hey, we could build a multifamily business inside of this," or is it just, you know, "that was nice, let's just go on with business the way it is."

Willy Walker: If you look at the $390 billion market size expectation from MBA for 2020 and you take that Fannie and Freddie should do, what, $160 billion combined between the two of them at $80 billion each that still leaves a 200-- $200 plus billion market for other capital to meet in the multifamily space. So there were 3,220 distinct lenders who provided capital to the multifamily industry last year, Henry, and Walker & Dunlop was the fifth-largest. And so I think the real question you're asking is, is there an opportunity for Walker & Dunlop to be providing capital to that other $230 billion that's going to go out to multifamily in 2020 and the very direct answer is, yes. So we've entered the small loan space with the agencies. We can broaden that out. We have our joint venture with Blackstone to be able to originate multifamily bridge loans. We have our capital markets group, which is sending loans across to life insurance companies, banks, and CMBS. We have our own CMBS group that is table funding CMBS loans, and we are consistently looking for opportunities to either find bankers and brokers who can deploy capital or raise capital at our new fund management business, that can be deployed into the market. So we see a lot of opportunity in providing capital to that other part of the market that Fannie and Freddie aren't covering currently.

Henry Coffey: And, but-- you think for Fannie and Freddie, it's "steady as she goes" and there's not going to be the emergence of either a third GSE or GSE-like structure or the merger of the Fannie Freddie business or-- I mean, it seems like GSE reform is kind of an urban myth right now, and the markets are just taking care of the business themselves.

Willy Walker: I would not under estimate director Calabria's desire to get Fannie and Freddie out of a conservatorship. And so there is a lot of focus and a lot of time being spent on achieving that mission. And the second thing I would say is, as it relates to merging Fannie and Freddie in the multifamily space, FHFA has been declaratory and saying that they greatly appreciate and want to maintain the two securitization models and distinct securitization models that Fannie and Freddie have for multifamily loans. So I see the merging of those two enterprises together into one common platform as exceedingly remote.

Henry Coffey: Great. Thank you very much.

Steve Theobald: Thanks Henry.

Operator: Our next question will come from Jason Weaver with Compass Point. Please go ahead.

Jason Weaver: Hi, good morning, and thanks for taking my question. I'm just trying to close in on the asset management outlook as it pertains to AUM goals. Can you tell us the targeted side for JCR Fund Five, and what other plans are in the pipeline for further funds?

Steve Theobald: Okay. Morning Jason. Thanks for joining us. We haven't-- we haven't-- we're out marketing JCR Fund Five, and can I tell what the cover is on that? [inaudible] with the target? Yeah. So we're looking to raise $250 million, Jason, into JCR Fund Five, and I'm looking at a first close quite soon and have some great commitments for that fund. And then as it relates to how we continue to grow the business, what comes on Fund Six and do we go out and acquire other either fund platforms or actual portfolios, that is still TBD. What we wanted to kind of give investors an update on is we established that goal back in 2016 with no fund management business. It took us '16 and '17 and a little bit of '18 to find a company to acquire. We're thrilled that we've acquired JCR and have a really solid platform, but achieving that $8 billion to $10 billion goal, barring some opportunity that we don't see right this moment, we probably don't achieve that goal by the end of 2020. But as I tried to say, we've got a great platform that we can start to build upon, and given the JCR had $750 million of AUM when we acquired them, and we're at $1.6 billion with the combination of our Blackstone business as well as what's at JCR, the growth is significant.

Jason Weaver: All right. Thank you. And, and on the same subject, regarding 2020 goals, do you have any expectations of the number of new brokers you're looking to add in investment sales near term?

Willy Walker: We haven't-- we haven't we haven't put that out there. I would just say that the, the market is in no way settled right now. So there is still a significant amount of opportunity for us to continue to build off of the Q3 momentum, in bringing on additional talent to our platform. As I tried to underscore in my comments, we really do have a very unique market positioning today and that is paying dividends with people who want to really be a part of the growth of a firm that has big company capabilities, but the touch and feel of a small company. And so I think that we will continue to benefit from our market positioning and also benefit from the recruiting we've done because every time we add someone to the platform and they joined W&D and they see how productive they can be on in a company, that is such a great place to work, that momentum just builds upon itself.

Jason Weaver: Okay. Thank you. I'd also say congratulations on another strong quarter.

Willy Walker: Thank you very much and thanks for being on.

Operator: Our next question is a follow-up from Jade Rahmani with KBW.

Jade Rahmani: Thank you for taking the follow up. In terms of the affordable component of WD's business, does it line up with the 37.5% target that the FHFA has put out?

Willy Walker: In what sense "line up?" We have, as Steve said, Jade, we-- you know, we're a very big originator of manufactured housing, which typically qualifies as affordable. We have our HUD business, which you saw some pretty significant growth in the quarter, and that-- that is all affordable business that we're doing on the HUD side and many opportunities there come both into HUD as well as into Fannie and Freddie. And we also have specific bankers in the affordable space who bank a lot of the affordable housing developers and owners. So I guess if you're saying do we have bankers and brokers who focus on that segment of the market? Yes, very much so. And so we see big opportunity there. I would also say that our small balance lending operation as well qualifies in the affordable space. And we've, as you know, brought on a team about a year ago now and they've hit the ground running in 20 20- 2019, and we see an opportunity for significant growth there as well.

Jade Rahmani: I guess the question is 37.5% WD's GSE origination volumes in the affordable category?

Willy Walker: I don't have that off top of my head. I'm looking, I'm looking, I'm looking across the table and don't have it. I don't know the answer to that question, Jade.

Jade Rahmani: OK. In terms of the 4Q outlook, do you expect a-- should we expect an increase in gain on sale margins as a result of the pullback that the GSEs had? You know, I think they widened their pricing and that could be a benefit to gain on sale margins, or it would gain on sale margin decline from 3Q levels because of the mix shift toward more brokered business?

Willy Walker: So, as you as you know, we don't-- what we've given is a range there and the range has been a 150 to 170 basis points. As you saw in Q3, we came in at one 62, which was up 12 basis points from Q3 of 2018. And I would not read anything more into it, in the sense that we didn't change the range. 162 on Q3 is a, is a very healthy number. And Steve didn't modify the range of 150 to 170. So if you're, if you're building a model, I wouldn't-- I wouldn't go outside of that range for Q4. But to exactly all the points you just put in there, there are a lot of moving parts here, as it relates to what percentage of our volume is agency, where is the pricing on specific agency loans, and then what's the volume on the non-agency brokered volume? So the range is 150 to 170, we haven't changed it, and so wherever you want to pick your point in that range you're-- you're probably somewhere within you know, very close to where we'll be.

Jade Rahmani: Okay. Just a technical question on the Fannie Mae risk sharing side, in terms of capital that you have to post that represents the first 5% of loss that you'd eventually have to absorb if there were losses, is it just the pledge securities that you post, which I believe is around $120 million?

Steve Theobald: That's, that's right, Jade. I mean there are minimum net worth requirements and minimum liquidity requirements associated with the business. But the specific set aside is that pledge security account, which is essentially Fannie's collateral against our guaranteed.

Jade Rahmani: And is there any risk of that requirement increasing in what the FHFA is considered?

Steve Theobald: This is a- there's a provision in the Fannie documents that they can look at it, you know, at least annually to assess. To my knowledge, there's no move to increase those requirements at this, at this point.

Jade Rahmani: Okay.

Steve Theobald: And if your is, is it a risk? It's always a risk, but there's nothing happening a right now to suggest that that risk is happening.

Willy Walker: And with the losses, or lack thereof, in this space, I'm hard-pressed to think that that's a hot button issue for either the regulator or Fannie at this point.

Jade Rahmani: Okay, fair enough.

Willy Walker: We talked about, just real quick, when Steve gave the data points, our average LTV in Q3 was 68%, and our average debt service covers 1.47 times in our Q3 lending book. We are not out over our skis, nor are any of our competitor firms as it relates to the loans that they're putting out with Fannie or Freddie at this time.

Steve Theobald: Yeah. If anything given the loss history, I would argue that we're way over collateralized at the moment.

Jade Rahmani: In terms of a M&A, I often get asked about you know, potential mergers, acquisitions for Walker Dunlop, and I was wondering if you think it could ever make sense to combine with a REIT or elect a REIT designation, which an Arbor Realty, one of your smaller competitors has?

Willy Walker: So I'd say a couple of things. First of all, as it relates to combinations, we clearly have been the net beneficiary of our size and scale in this marketplace, given the HOPEFULLY/JLL merger and what's happened after that. So the idea of, you know, we're very well-positioned in the market today, Jade, in our current form and size.

As it relates to a mortgage REIT, whether it be a public or private REIT, that would be a source of funding that, you know, we would be able to use very effectively. We have clearly in the past looked at that as something that we might do. So who knows? I mean in the sense that we're constantly looking for the ability to raise additional capital and given our success at creating a platform to deploy it--

Steve Theobald: But, but I think to be clear that says, you know, we would love to manage a REIT as opposed to transforming our company from a C corporation into a REIT, Jade. I think as, you know, we've looked at this on multiple occasions in the past and I think two things that don't really work that well for us. One, I think a not-insignificant amount of our revenue is not good REIT income. And so you wouldn't gain all of the tax efficiencies that you might as a REIT. And secondly, our success has been driven by the fact that we've been able to reinvest our capital into future growth of the company. And obviously in a REIT model, you're dividending out all that capital to shareholders and having to, you know, either borrow or raise new equity in order to continue to grow and- that's just not a model that we think is the right one for us over the long run.

Jade Rahmani: Would there ever be a consideration of carving out some portion of the MSR portfolio, which is very REIT-like in terms of consistency of cash flow and-- and contributing that to a REIT structure?

Willy Walker: We've looked at that in the past. I think given the requirements of the agencies, that it's not really feasible for us unless you become a REIT.

Jade Rahmani: And then just lastly, I guess a related question -- in terms of the platform, have you or would you consider property management or other landlords-centric services as a way to create a deeper touch points and potentially leverage off the network that you've built with those relationships, in order to also diversify the company's revenue streams?

Willy Walker: Yeah, I would say never say never, but that is clearly not in what our mission statement says today. We want to be a commercial real estate finance company. We are a commercial real estate finance company. We want to be the premier one. And those are real estate services and we have been very definitive in saying we are not a real estate services company. We are a real estate finance company. So all areas that we have looked at in the past, all you know, interesting as it relates to customer touch points. But we feel really good about the strategy and the people we've added to the platform and our growth opportunities in our given space now for the next several years. And so I'd reiterate, never say never, but that's clearly not the strategy today.

Jade Rahmani: Thank you very much for taking the questions.

Willy Walker? Thank you, Jade.

Operator: And there are no further questions at this time, so I'll turn it back to speakers for closing remarks.

Willy Walker: Great. Fantastic Q3, many thanks to all of you who joined us on the call this morning and hope you have a great day. Bye-bye.

Operator: This does conclude today's program. Thank you for your participation. You may now disconnect.