REFINITIV STREETEVENTS

EDITED TRANSCRIPT

JLL.N - Q2 2022 Jones Lang LaSalle Inc Earnings Call

EVENT DATE/TIME: AUGUST 03, 2022 / 1:00PM GMT

OVERVIEW:

JLL reported 2Q22 revenue of $5.3b, adjusted net income of $222m and adjusted diluted EPS of $4.48.

CORPORATE PARTICIPANTS

Christian Ulbrich *Jones Lang LaSalle Incorporated - Chairman of Global Executive Board, President, CEO & Director*

Karen G. Brennan *Jones Lang LaSalle Incorporated - CFO & Member of the Global Executive Board*

Scott Einberger

CONFERENCE CALL PARTICIPANTS

Anthony Paolone *JPMorgan Chase & Co, Research Division - Senior Analyst*

Chandni Luthra *Goldman Sachs Group, Inc., Research Division - Associate*

Jade Joseph Rahmani *Keefe, Bruyette, & Woods, Inc., Research Division - Director*

Matthew R. Filek *William Blair & Company L.L.C., Research Division - Research Analyst*

Patrick Joseph O'Shaughnessy *Raymond James & Associates, Inc., Research Division - Research Analyst*

PRESENTATION

Operator

Good morning or good afternoon, all, and welcome to the Q2 2022 JLL Earnings Conference Call. My name is Adam, and I'll be your operator today. (Operator Instructions)

I will now hand the call over to Scott Einberger to begin. Scott, please go ahead when you are ready.

Scott Einberger

Thank you, and good morning. Welcome to the second quarter 2022 Conference Call for Jones Lang LaSalle Incorporated. Earlier this morning, we issued our earnings release which is available on the Investor Relations section of our website, along with the slide presentation intended to supplement our prepared remarks. Please visit ir.jll.com.

During the call and in our slide presentation, we will reference certain non-GAAP financial measures, which we believe provide useful information for investors. We include reconciliations of non-GAAP financial measures to GAAP in our earnings release and slide presentation.

As a reminder, today's call is being webcast live and recorded. A transcript of this conference call will also be posted on our website.

Any statements made about future results and performance, plans, expectations and objectives are forward-looking statements. Actual results and performance may differ from those forward-looking statements as a result of factors discussed in the annual report on Form 10-K for the fiscal year ended December 31, 2021, and in other reports filed with the SEC. The company disclaims any undertaking to publicly update or revise any forward-looking statements.

I will now turn the call over to Christian Ulbrich, our President and Chief Executive Officer, for opening remarks.

Christian Ulbrich - *Jones Lang LaSalle Incorporated - Chairman of Global Executive Board, President, CEO & Director*

Thank you, Scott. Hello, and thank you all for joining our second quarter earnings call. This morning, JLL reported financial results for the second quarter that highlight the strength and resiliency of our business. Double-digit fee revenue growth was led by our markets advisory, capital markets and work dynamic business segments.

Our One JLL philosophy continues to drive strong growth across our business lines and is central to how we deliver best-in-class service to our clients. I would like to thank the over 100,000 JLL employees for their dedication in a complex operating environment, relentlessly impressing our clients with outstanding services.

Turning to the current market environment. Capital markets activity in the second quarter proved resilient in the face of rising interest rates and inflationary pressures. Global investment totaled $281 million, up 2% for the quarter and 19% year-to-date.

The Americas outperformed with volumes up 23% for the quarter. Performance across Europe and Asia Pacific has been mixed as geopolitical challenges and COVID lockdowns impact different parts of the world. Debt markets remain liquid and our JLL research team estimates there's approximately USD 380 billion of available capital yet to be deployed globally in the commercial real estate space.

Price discovery and in some cases, extending the time line to close deals. This presents the greatest risk to the second half of the year as the timing of deal closures can fluctuate.

Taking a look at different asset classes. Industrial and multifamily have slowed slightly from what were historically elevated levels. In multifamily, investors are factoring in lower rental growth rate as the outlook for future inflation moderates. In addition, underwriting standards are becoming more restrictive as lenders adjust to a higher interest rate environment.

Retail and hotels performed well in the second quarter as these asset classes continue their recovery from pandemic level loss. As restrictions ease, consumers are spending more on services and travel, which has supported the growth of both the retail and hotel sectors.

On the leasing side, global volumes across all asset types was up 20% year-over-year in the second quarter. U.S. office leasing activity for the second quarter was in line with the first quarter as occupiers become more cautious amid the macroeconomic uncertainty. The flight to quality is unabated as companies look to upgrade their space in an effort to attract employees back to the office. This has resulted in the average lease term remaining flat at just over 8 years.

In the industrial market, demand continues to outpace supply, causing rents to remain elevated and vacancy rates to stay under 2% in many markets around the globe. In some markets, the lack of available quality space has led to a softening in demand as companies are forced to evaluate their longer-term industrial needs.

In Asia Pacific, leasing volumes vary by geography. Activity in Australia and Singapore showed strength while lockdowns in China limited transaction volumes. On average, office reentry in Asia Pacific is ahead of other regions, boding well for future leasing activity in the region.

In Europe, sentiment is mixed, with geopolitical and economic growth concerns weighing on the number of leasing inquiries in certain markets. Best-in-class assets continue to perform well with rising rental rates and increased levels of competition for space.

Let's now shift our attention to JLL's performance for the quarter. Second quarter revenue rose 21% to USD 5.3 billion, and fee revenue increased 23% to USD 2.1 billion in local currency, nearly all of which was organic. Fee revenue growth was led by our markets advisory and capital markets businesses.

Adjusted EBITDA for the quarter was USD 359 million, an increase of 10% from the prior year and our adjusted EBITDA margin was 16.5% in local currency. Adjusted net income totaled USD 222 million for the quarter. Adjusted diluted earnings per share were USD 4.48, an increase of 9% from the prior year.

Our capital allocation strategy remains unchanged. We will first reinvest in the business to drive future growth, both organically and through select M&A while also returning capital to shareholders. During the second quarter, we were opportunistic with our share repurchase program, returning close to USD 300 million to shareholders. This represents an increase in repurchase activity versus prior quarters as we weigh all investment opportunities against our return hurdles.

We will continue to be disciplined in our approach to capital allocation, utilizing the strength of our balance sheet and the meaningful amount of cash that our business generates to balance investing in the business and returning cash to shareholders.

I will now turn the call over to Karen, who will provide further detail on our results for the quarter.

Karen G. Brennan - *Jones Lang LaSalle Incorporated - CFO & Member of the Global Executive Board*

Thank you, Christian. The double-digit top line growth across nearly all business lines in the second quarter despite a less constructive macro backdrop is reflective of our increasingly resilient and diversified global platform as well as the quality of our people and the strength of our client relationships.

The 18.5% adjusted EBITDA margin, we reported a year ago was well above our pre-pandemic margin and not reflective of a fully normalized cost basis. As a professional services firm with a focus on long-term growth and value creation, investing in our people, products and initiatives to improve efficiency, remains one of our most important priorities. These investments represented a key driver of the 200 basis point decline in our adjusted EBITDA margin from a year ago to 16.5%.

The expected return of T&E and marketing expenses and headwinds from the portfolio valuation reversal benefit a year ago were other primary drivers of the margin decline. Despite the decline, our adjusted EBITDA margin is still comfortably above pre-pandemic levels for the quarter and on a year-to-date basis.

Not withstanding the current macroeconomic environment and geopolitical backdrop, we have conviction in our ability to capitalize on the many growth opportunities we see ahead and expect to operate within our 16% to 19% adjusted EBITDA margin target range for the full year. In line with our capital allocation priorities, we used our healthy cash flow generation over the trailing 12 months and investment-grade balance sheet to repurchase nearly $300 million of shares during the quarter.

Moving to a detailed review of operating performance. I'll remind everyone that variances are against the prior year period in local currency, unless otherwise noted. Beginning with market advisory, leasing led the segment with fee revenue growth of 26%. The growth was broad-based across regions and concentrated in the office and industrial sectors. Office sector fee revenue growth outpaced the global office market volume by approximately 500 basis points.

Industrial factor fee revenue growth remained strong, up 37%. So the growth rate continues to moderate from peak levels as anticipated given tight supply. Global industrial market activity declined from a year ago.

With macro conditions and COVID restrictions bearing across regions, leasing fee revenue growth was most notable in the Americas, up 26% and EMEA, up 42%, while Asia Pacific grew 8% despite a greater pandemic impact. We saw a significant increase in transaction volume and size globally, including an approximate 30% increase in the average transaction size in the U.S. versus a year ago.

Property management fee revenue growth accelerated to 10% from single digits in the first quarter, in part due to inorganic contributions from our 2021 strategic joint venture in the U.S. The leasing market overall remains active, though supply and demand vary by asset class and geography. As an example, our U.S. leasing pipeline continues to increase with the growth in the industrial and retail sector pipeline, partially offset by a modest decline in the office sector pipeline.

Employers continue to evaluate their workplace strategies and real estate footprint as well as the potential impact on the macroeconomic environment, creating demand for our advisory services. As indicated by occupancy rate and rental rate growth disparities, we continue to see a flight to quality as occupier shift to new and/or Class A space with the amenities and sustainability profile needed to attract employees back to the office. This plays to JLL's strength given our specialization in Class A space, which has the best long-term prospects and comprises the majority of our leasing fee revenue.

Markets Advisory adjusted EBITDA margin declined 40 basis points from a year ago to 15.6% as higher commission expense, continued investment in talent to meet increased business demand and expected return of T&E expense more than offset higher fee revenue and changes in our incentive compensation programs to better align with business performance. The increase in commission expense was in part due to regional business mix and brokers achieving higher commission tiers earlier than last year.

Moving now to our Capital Markets segment. Despite the shifting macro environment and central bank actions globally, which have caused some policy transaction activity, fee revenue growth was strong, up 28%. The growth was broad-based led by debt advisory and investment sales.

Nearly all major asset classes exhibited growth, notably in the retail, land and residential sectors. Growth in the industrial sector moderated but remained in the double digits.

After 3 quarters of growth in the office sector, fee revenue related to office declined slightly from a year earlier. Investment sales, debt and equity advisory fee revenue grew 31% driven primarily by higher average deal volume and average fees.

Fee revenue from U.S. investment advisory sales grew about 45% and U.S. debt and equity advisory increased approximately 50%. Notably, EMEA investment sales, debt and equity advisory fee revenue grew 13%, while Asia Pacific declined 25% on a tough comparison quarter and softness in the industrial sector.

Our loan servicing business maintained a strong momentum with fee revenue up 32% driven by gains in our servicing portfolio, particularly from Fannie Mae originations as well as incremental prepayment fees.

As we look towards the rest of this year, the global capital markets investment sales, debt and equity advisory pipeline is up 30% compared with this time last year. Though liquidity remains solid and dry powder is at near record levels, the combination of interest rates, inflation and a changing geopolitical environment will influence closing rates and transaction timing.

Capital Markets adjusted EBITDA margin declined 350 basis points from a year ago to 19.1%. Higher commission expense and the continued return of T&E and marketing expenses more than offset the strong revenue growth, productivity gains and a reduction in other variable compensation plans.

Moving now to Work Dynamics. Fee revenue grew 19% with double-digit growth across business lines. Both our annuity and transactional revenue streams within the segment had strong momentum globally.

Project management fee revenue growth accelerated to 22% from 11% in the prior quarter as clients are resuming project-related work across all regions. Client wins and global contract expansions, particularly in the Americas, drove 15% fee revenue growth in workplace management.

The Work Dynamics adjusted EBITDA margin declined 60 basis points from a year ago driven primarily by investments in our people as well as products and services development, including the sustainability.

Moving next to JLL Technologies. Fee revenue inclusive of M&A grew 48%. Our large enterprise clients were the primary driver of 22% organic growth. It is important to note that JLL Technologies also influences the fee revenue growth across JLL through the differentiated capabilities that delivers.

We continue to invest in our technology team and platform, which we believe will further differentiate our suite of services, scale of recurring revenue business lines and create long-term value. The JLL Technologies adjusted EBITDA margin improved from a year earlier and higher equity earnings, which more than offset continued investment in people and platform both organically and through acquisitions.

Turning to LaSalle. A change in the market sentiment through the quarter led to a slowing in capital raising and asset deployment as the month progressed during the quarter. Still, capital deployment and valuation markup over the past 12 months drove a 12% increase in assets under management and translated to 23% advisory fee revenue growth, mostly within our core open-end funds.

Lower equity earnings were primarily due to the absence of the valuation reversal benefit a year ago, an approximate $11 million adverse swing in the fair value mark of our publicly traded J-REIT, which more than offset modest gains on the remainder of the co-investment portfolio. The increase in advisory fee revenue and incremental platform scale were more than offset by the lower equity earnings and lower incentive fees, resulting in a decline in the sale of adjusted EBITDA margin.

Shifting now to an update on our balance sheet and capital allocation. As of June 30, liquidity stood at $1.9 billion and reported net leverage was 1.0x, providing a strong foundation to execute on our strategic priorities. Our net leverage is just above the midpoint of our target leverage range and up from 0.6x a year earlier, primarily on incremental investments in our business and share repurchases.

We continue to invest in our business to further differentiate our capabilities and better serve our clients while also repurchasing our shares, all centered on driving long-term growth and value creation. Our nearly $300 million of share repurchases in the quarter brought our trailing 12-month repurchases to approximately $750 million and drove a 6% reduction in our quarter end share count from a year earlier and a 3% decline from the first quarter.

We expect to continue repurchasing shares on both a programmatic and opportunistic basis over the remainder of the year, with the amount dependent on a host of factors, including other potential investment opportunities. Approximately $1.3 billion remained on our share repurchase authorization as of June 30.

Looking ahead, we anticipate revenue growth rate to moderate from the pace of the second quarter due to the combination of the strong growth seen in the back half of 2021 as well as a somewhat less constructive macroeconomic backdrop. We continue to enhance the resiliency of our organization and are constantly refining and investing in our operating model to position us for long-term profitable growth.

Echoing Christian's comments, I'd like to thank my JLL colleagues for their relentless effort that combined with our differentiated operating platform and corporate culture are paramount to our client success and generating long-term value for all stakeholders.

Christian, back to you.

Christian Ulbrich - *Jones Lang LaSalle Incorporated - Chairman of Global Executive Board, President, CEO & Director*

Thank you, Karen. Since we spoke last quarter, global economic prospects have softened amid rising interest rates and inflationary pressures. Within our industry, the economic environment has caused investors to become more cautious and certain instances have delayed the closing time line for transactions.

Still, the tailwinds supporting our industry remain intact, labor markets continue to perform well and unemployment rates are low. There's sufficient liquidity in the market and a significant amount of capital yet to be deployed in the commercial real estate space. Once investors gain comfort with the future path of interest rates, we expect this capital to drive an acceleration in capital markets activities.

In addition, a record number of lease expirations will occur in the coming years, supporting future leasing activity. These factors combined with the resiliency of our industry bodes well for long-term growth prospects. I'm confident that JLL is well positioned to take advantage of these growth opportunities.

Operator, please explain the Q&A process.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from Patrick O'Shaughnessy from Raymond James. Patrick, Please go ahead.

Patrick Joseph O'Shaughnessy - *Raymond James & Associates, Inc., Research Division - Research Analyst*

So to follow up on some of your commentary on the pipeline, it sounds like in both leasing as well as capital markets, the pipelines are good. It's just a matter of timing. And some of the market turbulence might lead to deals getting pushed into 2023 that otherwise would have gotten done in the back half of 2022. Am I kind of interpreting your comments correctly there?

Christian Ulbrich - *Jones Lang LaSalle Incorporated - Chairman of Global Executive Board, President, CEO & Director*

Yes. It's Christian here. Yes, directly yes. I think we should be more focused with regards to that question, deals being pushed out on the capital markets side because, obviously, there's much more flexibility for deals to be pushed out.

On the leasing side, if there's a maturity on your lease agreement, you have to make a call. You can kick the can down the road and only try to extend the lease for another short period of time before you take the major decision, but you have to take a decision.

So we are very focused on watching our capital markets pipeline, whether deals are being delayed. And does that mean delayed by a quarter? Or does it mean that they are really being pushed out?

Patrick Joseph O'Shaughnessy - *Raymond James & Associates, Inc., Research Division - Research Analyst*

That's helpful. On JLL Technologies, obviously, you have a pretty sizable equity earnings gain in the second quarter. Can you characterize that with a little bit more detail? And then what's your outlook in terms of equity earnings for that segment for the duration of the year? And I think in particular, given that it seems like investment in the property tech space has quieted down a little bit.

Karen G. Brennan - *Jones Lang LaSalle Incorporated - CFO & Member of the Global Executive Board*

Sure. This is Karen. I can provide more color on that. So within the quarter, we saw both valuation increases and decreases across the portfolio. So it is a diversified portfolio. And we saw both directions happening.

Looking out for the remainder of the year, we're not going to put a specific forecast on valuations but have been carefully monitoring the portfolio of companies and feel reasonably good about where they stand right now in terms of cash on hand and ability to continue to move forward and grow their businesses in this environment.

Patrick Joseph O'Shaughnessy - *Raymond James & Associates, Inc., Research Division - Research Analyst*

Great. And then last one for me. Your tax rate was a little bit lower this quarter. What do you guys currently expect for the full year effective tax rate?

Karen G. Brennan - *Jones Lang LaSalle Incorporated - CFO & Member of the Global Executive Board*

Yes. So it was a bit lower this quarter at around 17.8% and year-to-date, it brings it to 19.1%. That was really due to a noncontrolling interest transaction and a benefit of a loss carryover we utilized in the second quarter. So it doesn't reflect what we expect for the full year. If you look out for full year 2022 at this stage, we're anticipating around 22% for the full year or thereabouts kind of in that range.

Operator

The next question is from Anthony Paolone from JPMorgan.

Anthony Paolone - *JPMorgan Chase & Co, Research Division - Senior Analyst*

Great. My first question relates to your comments about hiring and compensation and commissions and some of the costs in the system. Just wondering if you could talk more about your decision to hire and do these things into a slowing environment and what that specifically mean to margins as we think about the second half of the year?

Karen G. Brennan - *Jones Lang LaSalle Incorporated - CFO & Member of the Global Executive Board*

Yes. So we did mention a number of different things that relates to compensation and benefits overall in terms of movements in the quarter. Largely, the primary comment was around investments in people, right, and hiring. And so as we thought about lapping a year ago to today, we did not have a stabilized cost basis to support the level of growth that we saw and on a sequential basis, we can kind of rolling out of the pandemic in the second quarter of 2021.

So we were hiring both to meet a demand that we saw coming at us -- over the last 12 months from our clients and that we anticipate for the future. Looking ahead, we'll definitely be focused on keeping our close eye in terms of the macroeconomic environment, looking at our pipelines more broadly and hiring in accordance with what we see in terms of the outlook and the long-term prospects.

We certainly are taking a more prudent look in certain areas of our business. But there's other areas where now is a good time to hire talent in a market environment where there's a little bit more uncertainty. So we'll be taking a balanced view and looking forward, as I mentioned, working to operate our business within our margin range of 16% to 19%, taking into account more fluid macro environment.

Anthony Paolone - *JPMorgan Chase & Co, Research Division - Senior Analyst*

Got it. And on the commission side, you had mentioned, for instance, in capital markets, some of the year-over-year margin declines being brokers hitting just certain business levels that gave them higher splits, it seems. If we go into the back half of this year and you see capital markets negative or revenue down year-over-year, does -- I mean do those splits go back down? Or how does that work on the commission side? Like do we see margins improve in the fourth quarter if it's a tough comp year-over-year?

Karen G. Brennan - *Jones Lang LaSalle Incorporated - CFO & Member of the Global Executive Board*

Yes. So the impact we're talking about specifically called out within our markets business in leasing, where we had higher level volumes and larger average deal sizes in the second quarter as compared to a year ago in that quarter.

And so once -- these are calculated by individual brokers. So it really has to do with the mix of different markets and then transaction sizes that happen and the types of transaction sizes in parts of the market that brokers cover. They cover different -- specialize typically in different areas of the market.

And so as the second half of the year unfolds, if a broker has already achieved their certainty or that, yes, that will continue, but we're looking at what the mix is. And so as I mentioned before, it's really -- we had larger deal volumes in particular in the second quarter. So we'll be watching how that unfolds from here.

Anthony Paolone - *JPMorgan Chase & Co, Research Division - Senior Analyst*

Okay. And then just last one for me. On the capital markets side, the comment about the pipeline being 30% larger than it was a year ago. I mean how good a predictor has that been in the past for, say, capital markets revenue in the next quarter? Like can we see a 3Q positive capital markets comp on revenue -- or because of that stat? Or like how do we dial that into our thinking?

Christian Ulbrich - *Jones Lang LaSalle Incorporated - Chairman of Global Executive Board, President, CEO & Director*

I wouldn't narrow it down so -- the way you just described it. The pipeline describes the pipeline, and it gives an indication around the rough timing but not quarter-over-quarter. As I said earlier, what we are watching at the moment carefully is to what degree are deals being pushed out because of the current uncertainty.

The pipeline indicates that people are still highly committed to invest further money into real estate. But that may be that they are pushing it out a couple of quarters or it may be that they will only push it out maybe into the fourth quarter.

So don't take it that if we have a 30% higher pipeline, that you can see a significant increase in our capital markets revenue in the third quarter. That is not what this pipeline is indicating. But what it is indicating is that there is a very significant amount of fresh money waiting at the sideline to be invested into real estate.

And I think one important point to consider is that this very high inflation rate, which we have around the globe is expensive for money, which is waiting to be invested. And so there's a very strong motivational aspect to make the extra effort to find the right assets to invest that money rather than having it uninvested at the sideline.

Operator

The next question is from Chandni Luthra from Goldman Sachs.

Chandni Luthra - *Goldman Sachs Group, Inc., Research Division - Associate*

This is going to be a continuation of some of the themes that have been touched with previous questions here. As we think about the reality of a potentially tougher economic backdrop ahead, could you please talk about what levers do you have to pull on costs given you just made these incremental investments in headcount and other buckets?

Karen G. Brennan - *Jones Lang LaSalle Incorporated - CFO & Member of the Global Executive Board*

Sure. So in terms of the levers we can pull, we've already started to pull some of them as it relates to looking at more limitations on future growth and investment in certain areas of our business. Certainly, we demonstrated during the COVID environment that we can pull levers and pull back significantly on spending. And so they can start with specific variable expenses such as T&E and marketing and then go into more constraint on hiring.

I would also just remind everybody that a significant portion of our compensation structure is really tied to variable compensation expense. And so there is a natural fluctuation that will happen there as it relates to our performance over the course of the year based on how things manifest in the second half.

Chandni Luthra - *Goldman Sachs Group, Inc., Research Division - Associate*

My second question would be on LaSalle. So AUM obviously grew nicely. I think it was 5.5% Q-on-Q growth. You've talked about continued interest from investors. How should we think about the back half of the year and any mark-to-market risk within that? And if you could also give any color on transaction fees and incentives within LaSalle.

Karen G. Brennan - *Jones Lang LaSalle Incorporated - CFO & Member of the Global Executive Board*

Yes. So just taking a step back on LaSalle broadly, one thing I just want to highlight is there were a lot of movements going on within LaSalle. And so I just want to reiterate the point that we had 23% growth year-over-year for the quarter in our advisory fee business. And so the more modest growth that we saw in LaSalle overall compared to other business lines was really related to a decline in incentive fees.

And the incentive fees, as I've mentioned on previous calls really can vary from year-to-year. They range anywhere from $40 million to $240 million over, let's say, an 8- to 10-year period. We do expect that this year will be closer to the lower end of the spectrum and range for our incentive fees.

As it relates to equity earnings, there, the important call out is that we had some nice valuation increases broadly across the portfolio. We were lapping a quarter where we had the reversal of COVID valuation decline in 2020 in the second quarter of 2021. So on a comparative basis, it doesn't look as strong. And we also had fluctuations in our J-REIT, which I mentioned, right, where we had a big increase in 2Q and then a smaller change in 2Q of this year.

Chandni Luthra - *Goldman Sachs Group, Inc., Research Division - Associate*

Understood. And just -- if you could perhaps, Karen, give us any insight into individual markets across Europe. You gave this color on Germany and U.K. last quarter. Wondering what are you seeing in those markets right now.

Christian Ulbrich - *Jones Lang LaSalle Incorporated - Chairman of Global Executive Board, President, CEO & Director*

You mean color with regards to the capital markets environment? Or are you still focusing on LaSalle?

Chandni Luthra - *Goldman Sachs Group, Inc., Research Division - Associate*

No, I'm talking about capital markets.

Christian Ulbrich - *Jones Lang LaSalle Incorporated - Chairman of Global Executive Board, President, CEO & Director*

Okay. Sorry. Listen, if you look at the state of the world, it is a situation where probably the whole world is currently in not the best situation from a geopolitical environment. But there are some relative winners in that -- in those circumstances and there are some relative losers. And it's probably fair to say that Europe and especially Continental Europe are more in the bucket of the relative losers.

And therefore, if we were to kind of pick our debt where we will see the strongest capital market activity, that will certainly be the U.S. and some Asian markets and the European markets will be more muted in the next couple of months. I don't know whether that is what you were trying to get out here.

Operator

The next question comes from Jade Rahmani from KBW.

Jade Joseph Rahmani - *Keefe, Bruyette, & Woods, Inc., Research Division - Director*

The comment on the pipeline is somewhat in contrast to what some other contacts and public companies have mentioned. So just to put a finer point on expectations so that we're not projecting anything overly optimistic or at least were realistic, do you expect positive year-on-year growth in capital markets?

The comps are pretty challenging with revenues up 87% year-on-year in the third quarter of '21 and 51% year-on-year in the fourth quarter of '21. So reasonable to be modeling something in the way of perhaps 7.5% to 15% year-on-year declines. I know you might not specify the number but just on that expectation.

Christian Ulbrich - *Jones Lang LaSalle Incorporated - Chairman of Global Executive Board, President, CEO & Director*

We are servicing our clients. And so, we will -- we are currently spending a lot of time to talk to our clients to understand what their plans are for the third and the fourth quarter. I think it's fair to say that especially for the U.S. market, I just stated that we -- I believe that the U.S. market will perform the strongest of all our markets.

But even for the U.S. market, we expect slightly muted activity until after Labor Day. And then the big question is how is the market returning especially for the fourth quarter. And that is highly dependent on what our clients will do in the fourth quarter.

And so I won't make a clear prediction whether we will beat last year or not, on that question. But overall, the 30% pipeline is demonstrating a very strong interest to invest money into real estate. And as I said earlier, that may shift by some time, a quarter or 2. But it doesn't go away from our clear conviction. People want to get their money into real estate.

Karen G. Brennan - *Jones Lang LaSalle Incorporated - CFO & Member of the Global Executive Board*

Yes. And Jade, that might -- and I know you're looking for something more specific in terms of the percentage, which is -- we're not going to quantify at this stage. But what I can do is to provide some more color just on what we're seeing in the market and our clients' behavior, which was hopefully a whole frame how you think about the forecasting.

So broadly speaking, and these are from recent conversations with clients across the U.S. market, the investors are trying to price then the impact of 2 different risks, inflation risk and risk of recession, trying to think about the level of risk premium that they need for those different risks on the horizon.

And there has been some pricing reductions that have come in so far largely due to negative leverage and then the moderating rent growth through the recession years. And so people are pricing things in or working through what are my expectations and then working through the bid-ask spread out there as different groups of investors take a different approach.

Broadly, we're seeing investors shake out into 2 different buckets. There's a group that is still remaining active saying, actually, I finished my modeling and my assessment. And relative to where we were and -- I was trying to transact before and wasn't able to because of certain asset classes such as multifamily, industrial were really priced to perfection. This feels okay to me, and I'm going to continue to invest in certain areas. And then we're also seeing increased capital looking to get into the credit market, broadly speaking.

Then there's another group of investors that are really waiting and saying I want to see a bit more out there in terms of what's going to happen. I really want to look at how some of these bid-ask spreads shake out by geography, by property type, by asset type.

And so -- those are the 2 different groups. And so it's not as if we're seeing some decline in volumes but it's not completely coming to a screeching halt. So I think that's the important thing is it's difficult to see, but we're seeing the pipeline growth and Christian mentioned, at that longer term, medium term, we think is a positive. So hopefully, a little bit more of that color is helpful as you think about what to put in for the second half of the year.

Jade Joseph Rahmani - *Keefe, Bruyette, & Woods, Inc., Research Division - Director*

And on the leasing side, are you seeing occupiers increasingly hesitant to commit to obligations and make decisions right now? And so is there a behavior in which they're signing short-term extensions and waiting to have some more macro uncertainty?

Karen G. Brennan - *Jones Lang LaSalle Incorporated - CFO & Member of the Global Executive Board*

So within leasing, there are 2 different groups. So there's the office leasing and the industrial leasing. I'll start with the office leasing and then remind me if I forget to talk about Industrial.

So on the office side, right, we still saw growth in volumes year-over-year of around 20% globally. And if you think about what types of transactions are happening, it's really across 3 different buckets. You have the lease expirations that are happening, right? So a decision needs to be taken, a transaction needs to occur.

The second bucket would be people for good reasons, looking to expand and take action on our portfolio and our footprint to do something differently for growth reasons.

And then the third would be for bad reasons that they need to downsize now, put more space on the market and make some changes for more negative outlook.

And as I was saying the second bucket is the one where we're definitely seeing some more pullback in hesitation and people taking wait and see. But the first and the third bucket, right, something typically needs to happen there. And so it's just a matter of time line and expectations there.

One interesting thing also to call out in our pipeline as we look at overall leasing, if you think about the build-out required for spaces and some of the supply chain issues that are happening around the world. We're encouraging our clients to get out there sooner, take decisions sooner, because there is a longer period of time before you can actually build out your space and move in than there might have been historically. So that's a little color on the office side.

On the industrial side, we have seen slowing globally in terms of the volume. There is largely still a desire by many clients to continue to look at their distribution logistics facilities, in the context of supply chain risks that are now front of mind for people. But there's definitely a lack of supply.

There's certain -- we've mentioned this before that we expected the growth to moderate in industrial. But there's been like certain markets that are sub 2% vacancy. And so rents are still going up but there's just not as many transactions that can happen. So there's great, 2 different stories depending on which property type you're looking at here.

Jade Joseph Rahmani - *Keefe, Bruyette, & Woods, Inc., Research Division - Director*

On the JLL technology side, it is a bit of a black box for investors to understand. So any further clarity or resources in terms of understanding what drives that would be helpful. I believe that the carrying value is now in excess of $500 million, you said, which is up from $300 million. So clearly, all of that was not an income statement valuation change. But in terms of the adjusted EBITDA, is that all -- should we assume primarily noncash? And do we expect breakeven adjusted EBITDA going forward?

Karen G. Brennan - *Jones Lang LaSalle Incorporated - CFO & Member of the Global Executive Board*

Yes. So there's 2 different things I'd say if you think about that JLLT segment, JLL Technologies segment. And we will repeat the point I said earlier, which is there are elements within our technology team and effort within the business line, where we're driving growth in other business lines as a result of those activities.

But within this segment, what we're specifically reporting are 2 things. One is the investment side of it within the proptech space, which you referenced and which flow through in terms of our equity earnings and then the team that's responsible for overseeing that is in the segment.

And then there's other side where we have both software as a service that we're selling to our clients and then technology consulting and advisory within that space. And so a small segment today but growing and very good demand from clients for advice and services as it relates to the rapidly changing world in our industry as it relates to prospect.

And so you're asking for what should we expect going forward. You'll have equity earnings which will fluctuate quarter-to-quarter based on valuations. As we said in the quarter, it was up overall despite some write-downs for certain companies in the portfolio.

And then on the other side of the business where we're really -- the revenue-generating side of the business, we're going to continue to invest in talent and products and people there. We see a significant opportunity going forward. And that takes investment in order to scale the ability to deliver to the client more broadly.

And so we see good demand, and we don't expect that to moderate, we will continue -- to continue to invest in talent. We'll certainly be looking at overall, again, in the context of this segment, the overall context of the business, what does that do to our profitability and margin within the target that we're working towards on a full year basis.

Jade Joseph Rahmani - *Keefe, Bruyette, & Woods, Inc., Research Division - Director*

Okay. So it sounds like absent valuation gains, which we, from our vantage point, are unable to forecast, there still is some cash burn in that space due to the investment, which would make sense at this stage of scale.

Karen G. Brennan - *Jones Lang LaSalle Incorporated - CFO & Member of the Global Executive Board*

Yes. At this stage for where we are in the maturity and growth cycle, yes, we'll continue to have some cash drag down.

Operator

The next question comes from Stephen Sheldon of William Blair.

Matthew R. Filek - *William Blair & Company L.L.C., Research Division - Research Analyst*

This is actually Matt Filek on for Stephen. I was wondering if you can expand on some of the demand trends you're seeing across Class A, B and C office space and the expectation for those trends over time.

And as a second part to that question, do you think some of the less popular office space may be repurposed for alternative uses? And could that potentially create some opportunities within your project management service line?

Karen G. Brennan - *Jones Lang LaSalle Incorporated - CFO & Member of the Global Executive Board*

Yes. Thanks for the question. Certainly, we're seeing some really interesting trends there. So let me speak specifically to the statistics that we have in the U.S. market, which will give some good direction.

So in the second quarter, the vacancy rate for office overall increased by 30 basis points to 18.9%. Within that, we saw the vacancy holding firm for Class A buildings. And actually, we tried to cut it even by age of some of these buildings, so anything delivered before 2015. The vacancy withholding firm at 16.5%. But it's continuing to increase for older stock, so it was 19% for the older stock. So that's one sort of aged building.

And then if we look at just broadly Class A space versus Class B and C space and what happened in terms of the negative absorption and occupancy loss in the quarter, it was predominantly in the Class B and C stock because Class B and C, they contributed almost 70% of the negative net absorption despite comprising just over 40% of the overall inventory.

So we certainly see it come through the numbers and our conversations with clients. We're seeing that as well. In terms of their intentions, in terms of the quality of the space that they're looking to take, they may be looking to take a lot of space overall if they're going to make some changes in their portfolio. But they're looking for higher quality space, which we're seeing strength in, kind of rental rates holding there and good momentum. We expect to see that continue -- by trying to continue in the future based on conversations with our clients and what we're seeing in our data so far.

Matthew R. Filek - *William Blair & Company L.L.C., Research Division - Research Analyst*

Okay. Got it. That's helpful. And then just to clarify, do you think considering that there's that flight to quality that over time, some of the less desirable Class B and C office property could potentially be repurposed for another use beyond office? And is that something the project management service line could benefit from the redesign of that office space to something else?

Christian Ulbrich - *Jones Lang LaSalle Incorporated - Chairman of Global Executive Board, President, CEO & Director*

The short answer is yes and yes. Those buildings will eventually be either repurposed or taken down and you will be seeing new developments maybe in completely different asset classes. And yes, we will believe that this is a key driver of future demand for other service lines of us.

But I think you should put it into context of the whole need to be aware of climate change and the investments being needed to reduce the carbon footprint of buildings. We have pretty strict regulation especially in New York but also in many other places around the world. And that will also drive very significant investment into the refurbishment of buildings.

Operator

(Operator Instructions) As we have no further questions, I hand back to the management team for any closing remarks.

Christian Ulbrich - *Jones Lang LaSalle Incorporated - Chairman of Global Executive Board, President, CEO & Director*

Thank you, operator. With no further questions, we will close today's call. On behalf of the entire JLL team, we thank you all for participating on the call today. Karen and I look forward to speaking with you again following the third quarter. Thank you.

Operator

This concludes today's call. Thank you very much for your attendance. You may now disconnect your lines.
