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RKT.N - Q3 2020 Rocket Companies Inc Earnings Call

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OVERVIEW:

Co. reported 3Q20 quarterly adjusted revenue of $4.7b and adjusted net income of $2.4b.

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by and welcome to the Rocket Companies, Inc. Third Quarter 2020 Earnings Call. (Operator Instructions) Please be advised that today's conference is being recorded. (Operator Instructions)

I will now turn the call over to the company. You may begin your conference.

Jason A. McGruder - *Rocket Companies, Inc. - VP of Investor Relation*

Good afternoon, everyone. I'm Jason McGruder, Vice President of Investor Relations. Thank you for joining us for Rocket Companies' earnings call covering the third quarter of 2020. We are excited to share the results of another very strong quarter with you.

Before I turn things over to Jay Farner, I will read our disclaimers. Today's call is to provide you with information regarding our third quarter 2020 performance in addition to our financial outlook.

This conference call includes forward-looking statements. For more information about factors that may cause actual results to differ materially from forward-looking statements, please refer to the earnings release that we issued today as well as risks described in filings with the SEC, particularly in the section of these documents titled Risk Factors.

Our commentary today will also include non-GAAP financial measures. Reconciliations between GAAP and non-GAAP metrics for our reported results can also be found in our earnings release issued today as well as in our filings with the SEC.

And with that, I'll turn things over to Jay Farner to get us started. Jay?

Jay D. Farner - *Rocket Companies, Inc. - CEO & Director*

Good afternoon, everyone, and welcome to our third quarter earnings call. I'm pleased to report Rocket Companies' sixth consecutive quarter of record-breaking volume, highlighting the power of our platform and the strength of the Rocket brand. We are demonstrating true leadership at a critical time for our industry and our clients.

I'm extremely proud of our 22,000-plus team members whose dedication and drive have helped deliver the results we will share with you today. First, I want to congratulate our team on being named the #1 company for client satisfaction in mortgage origination by J.D. Power yesterday. This marks our 11th straight year being named to the top of the list. And when you add in our 7 consecutive #1 rankings for mortgage servicing, we've taken home 18 J.D. Power awards in the last 11 years.

This one in particular is special to us, however. It's proof that our platform is so powerful, that we can more than double loan originations year-over-year and still deliver on our commitment to servicing our clients at the highest levels. Again team, congratulations.

Our industry has reached an important moment. The COVID-19 pandemic has fundamentally changed the way Americans think of their homes. For decades, many have viewed their house as their most important investment. Today, home means so much more. It is now where we work, where we teach our children and where we gather with friends, bringing new meaning and significance to the place where we live, our home.

This enthusiasm around the value of home is clear in the numbers. For instance, the National Association of Realtors' existing home sales report showed that September sales of previously owned homes were more than 20% higher than the same month in 2019. Also, recent reports in the New York Times and San Francisco Chronicle tell of residents moving from the city centers to buy homes in the surrounding suburbs, in search of more space. Homeownership is on the rise across the country, led by a new generation of first time homebuyers.

As a result of shifting demographics and the ongoing pandemic, we are seeing a rapid acceleration in the long-term shift from physical to digital transactions across the industries where we participate. Consumers today don't just prefer, they demand a completely digital experience.

At the same time, the digital transformation of the lending process has become more important than ever as an unprecedented number of consumers look to leverage today's favorable interest rates. We are seeing the strongest growth among our most digitally engaged clients. Application volume through our self-serve digital experience has grown significantly faster than overall volume year-to-date. This trend accelerated earlier this year and continued through the third quarter.

The Rocket Mortgage platform is particularly powerful for first-time homebuyers who can receive loan approvals within minutes. In the third quarter, we delivered more purchase approval letters through our digital experience than in any quarter in our company's history. In addition to becoming the overwhelming choice for millennial homebuyers, Rocket Mortgage has continued to serve a large number of clients looking to take cash out of their homes, reduce their loan terms or refinance due to changes in life situations such as divorce. These clients, who are not rate-sensitive, remain an important population when you consider Rocket Companies' incredible footprint, serving all 50 states and more than 3,100 counties in the United States and a growing presence in Canada. Our marketplace has reached a significant inflection point due to consumers demanding a simple digital experience, and I'm proud to say Rocket Mortgage is executing at enormous scale.

In the third quarter, we delivered a record performance with $89 billion of closed loan volume, representing a 122% increase year-over-year. The growth we're achieving is unmatched. In Q3, we added nearly $50 billion of year-over-year closed loan volume. Consider this: our incremental volume in the third quarter is so large, that it alone would have made us the second largest retail mortgage lender in the nation.

To further illustrate the scale of this growth, Rocket Mortgage closed nearly $1 billion of origination volume each day in the third quarter. The scale and efficiency of our platform continues to drive substantial earnings power. We achieved a 69% adjusted EBITDA margin in the quarter and have generated $5.9 billion of adjusted net income in just the first 9 months of 2020.

The guidance that Julie will share with you today cements us among the most profitable fintech companies in the world, and we're not stopping there. Our mission is simple. We will continue to lead from the front as the most admired brand and technology platform in our industry.

Recently, we hosted Tech Con, our in-house technology conference for all Rocket Companies technologists, drawing more than 4,000 of the brightest minds in the industry. One of the most important topics covered was ethical artificial intelligence and its ever-increasing role in business. We crossed an important milestone in Q3 by generating more than $60 billion in application volume over the last 2 years using data science and AI. Our data science teams are now generating organic lead flow at higher conversion rates than paid marketing channels.

We are also using automation to improve the efficiency of our operations and are now making more than 1 million decisions per day using machine learning. All of these processes get better with scale, strengthening our competitive lead and reinforcing the Rocket Companies' flywheel. In addition to leveraging our rich data insights, we continue to expand the ways we are reaching consumers through innovations, partnerships and marketing.

In the last 30 days alone, we have announced enhancements to our Rocket Pro platform that grant real estate professionals never-before-available insights into their clients' mortgages. Now they can help guide homebuyers through the mortgage process from approval to closing using the Rocket Pro mobile app or website. Rather than calling one of our mortgage bankers or asking the client, real estate agents can now use Rocket Pro Insight to check in on a loan status. That leaves more time for mortgage bankers to help other homebuyers, and the agent can focus on showing and closing houses with their clients.

The reaction from those in the real estate community has been overwhelming. In fact in the first day, more than 1,100 agents joined Rocket Pro Insight, and the momentum has only increased. We anticipate nearly 15,000 real estate professionals will sign up to use the platform by the end of the year, providing a significant touch point with one of the largest influencers in the home purchase life cycle.

Another program to help both homebuyers and their agents was launched in early October. We kicked off a new relationship with realtor.com that allows the tens of millions of homebuyers visiting their website to seamlessly apply for a Rocket mortgage. The new venture was quickly followed by an announcement highlighting Rocket Mortgage's partnership with Intuit's Mint Personal Finance tool. Now Mint users can easily import their personal financial information into a Rocket Mortgage loan application with a tap of a finger, allowing them to lock in a mortgage rate in as little as 8 minutes, all while staying in the Mint app.

Quicken Loans Mortgage Services, which serves the needs of our mortgage broker partners, recently rebranded to Rocket Pro TPO. This transition allows our partners to continue to meet the needs of their clients while also providing them with the ability to leverage the best-known brand in consumer lending with Rocket Mortgage. To celebrate, we provided 10,000 fresh purchase leads to our Rocket Pro TPO partners, something that's never been done before in the industry.

As part of the rebranding, we've also announced new AI and machine learning innovations in partnership with Google technology for additional tech-focused enhancements to our platform and new ways to align with and support our brokers. Overall, the feedback we've received about the rebrand and technology rollouts has been extremely positive.

In addition to all the fantastic partnerships we've already shared with you, we are proud to announce that as of last week, we have forged a relationship with one of the largest financial services companies in the world. This collaboration, similar to the program we created with Charles Schwab, will allow us to originate mortgages for a new base of clients. We anticipate that we'll share more information in the new year.

Our exceptional brand marketing also continues to be a true differentiator in the industry. Our Rocket Can campaign has been incredibly successful. And we're proud to soon be rolling out a new slate of ads, including our first exclusively targeting the growing Latinx community. We continue to also leverage well-known talent like Jason Momoa, star of our Super Bowl ad, and future NFL Hall of Fame wide receiver Larry Fitzgerald in our marketing to appeal to a broad consumer base. The fact is Rocket Companies is leveraging the scale and flexibility of our platform to deliver first-to-market innovations with the best partnerships in real estate, technology and finance, all while reinforcing our brand with best-in-class marketing.

Outside of mortgage, innovation is taking place throughout our entire ecosystem. In the last several months, Nexsys, our title and closing technology company, announced it had partnered with insurance leaders Farmers and Lemonade to simplify homeowners' insurance verifications using its Clear HOI platform. These companies join others, including Allstate and Liberty Mutual, in helping provide a digital solution to lenders looking to confirm the presence of an insurance policy in real time, eliminating the need to manually call to confirm, a process that is deceptively tedious.

At Amrock, our title company, we closed more than 100,000 mortgage transactions in September, a record that proves the scalability of our platform. In addition, Amrock continues to be a trailblazer, digitizing the title industry much like Rocket Mortgage did for loan originations. In the first 3 quarters of 2020, the company is responsible for 90% of all eClosings in the industry, providing safety and convenience to our clients amid the ongoing pandemic. Additionally, Amrock is implementing machine learning and ethical AI into its workflow through its proprietary title decision engine or TDE. This tool, which is currently being used on more than 30% of Amrock's title work, automates the traditionally manual process of reviewing documents, maps and records of sale, cutting down the time our team members work on files by nearly 70%. This frees us up to work on other more specialized items, significantly increasing our productivity.

Finally, I'd like to take a moment to talk about our approach to client retention, an increasingly important driver of our business. After we originate a loan, we maintain monthly touch points with our clients and generate recurring revenue by processing their payments and servicing their loan over its lifetime. Julie will give more detail in a moment, but we are sharing today that Rocket Mortgage consistently retains over 90% of our total servicing clients on an annual basis. Retention at these levels has never been seen in the mortgage business and rivals any subscription-based model across industries including cable, streaming and wireless services.

Before I turn things over to Julie, I wanted to announce an addition to our Board of Directors. Our Board has voted unanimously to make Jonathan Mariner, the Founder and President of TaxDay, an independent Board member and new Chair of our Audit Committee. Prior to TaxDay, Jonathan spent 23 years in professional sport serving as the Chief Financial Officer for Major League Baseball, the Florida Marlins, the Florida Panthers and Dolphins Stadium. In addition to our Board, he also serves as an independent board member for Tyson Foods, McGraw-Hill Education, Little League Baseball and several others. We are very excited to have him join us.

And with that, I'll ask Julie to share with you the details of our financial performance in this quarter. Julie?

Julie R. Booth - *Rocket Companies, Inc. - CFO & Treasurer*

Thank you, Jay, and good afternoon, everyone.

Thanks to the hard work of the entire Rocket Companies team, we achieved another quarter of incredible results. In the third quarter, we achieved year-over-year quarterly adjusted revenue growth of 163% to $4.7 billion and adjusted net income growth of 365% to $2.4 billion.

We also produced another quarterly record in closed loan volume, which was up 122% year-over-year to $89 billion. Based on what banks and mortgage lenders have publicly reported, we believe that our closed loan volume growth was substantially higher than the overall industry in the 3 and 9 months ended September 2020 compared to a year earlier.

We generated record quarterly net rate lock volume of $94.7 billion, which represented a gain of 101% year-over-year. As a reminder, we recognize revenue at the time when we lock the interest rate with our clients. Rate lock typically occurs approximately 30 to 45 days prior to the closing of a loan.

We produced robust growth in both of our segments. Funded loan volume in our Direct to Consumer channel was up by 131% to $53.5 billion and increased in our Partner Network by 127% to $29.6 billion, both compared with the year-earlier quarter. We consider a loan funded when it is sold to investors on the secondary market.

While we continue to benefit from the low interest rate environment, we also produced strong year-over-year growth in the quarter from less rate-sensitive products. Demand for these products are driven by factors including clients wanting to purchase a home, take cash out of their homes, reduce the terms on their mortgages, changes in their life situations and the demand for investment properties. Although rate and term refinancing activity has been very high in 2020, we have historically had a balanced mix of originations. For example, from the first quarter of 2017 through the third quarter of 2020, more than half our overall volume was from our less rate-sensitive products.

Our gain on sale margins of 4.52% increased substantially from 3.29% in the prior year period and remained strong by historical standards. The sequential change from record gain on sale margins of 5.19% in the second quarter was driven primarily by changes in channel and product mix. As a reminder, record gain on sale margins in the second quarter reflected our ability to rapidly scale our Direct to Consumer volume during a period of pandemic-related market disruption, particularly during April and May.

Breaking down the 67 basis point variance in gain on sale margins sequentially, changes in loan pricing represented less than 10 basis points of the quarter-over-quarter difference in our gain on sale margins. Approximately 40 basis points of the change resulted from differences in channel and product mix, particularly the strong growth of our Partner Network volume during the quarter. Overall, our margins exceeded the high end of our expectations and remained at historically elevated levels throughout the third quarter.

In the past, we have typically seen primary secondary spreads normalize within a month or 2. However since March, these spreads have remained well above historical averages. We believe this speaks to the strength of demand in the current environment, as you heard from Jay.

Managing gain on sale margins is an important advantage of the Rocket Mortgage business model. Our centralized technology-driven operating model allows us to dynamically price our products on a real-time basis. As the largest mortgage lender in the country, we also benefit from the scale and sophistication of our capital markets capabilities including superior hedging, pooling and secondary market execution.

Client retention is another key differentiator of the Rocket Companies' ecosystem. We've spoken to many of you about our ability to recapture clients who pay off out of our servicing portfolio. Because of our unique business model, our recapture rate is more than 4x the industry average based on the latest figures from Black Knight.

Today, we are also introducing a new metric called our net client retention rate. This metric is intended to be comparable with retention figures across multiple industries, including cable and wireless service providers. Our new metric is calculated based on the clients who remain active with Rocket as a percentage of the total starting client base.

As we show in today's press release, our net client retention rate has consistently been above 90% over the past few years. Retention at these levels drive substantial lifetime value advantages for the company. Our high net retention rate allows us to benefit from the continued cash flow from our servicing portfolio and also have the opportunity to interact with our clients in the businesses throughout our ecosystem. This metric reflects the high lifetime value of our portfolio.

The unique strength of our business is that when the net client retention rate falls, it is generally the result of lower interest rates, leading to higher refinance activity. Because our recapture rate is 4.6x the industry average, we generate even more revenue from increased loan origination volume. Our high recapture rate serves as a natural hedge to our retention rate.

In the current environment, we are driving strong repeat transaction activity, which represented 42% of overall mortgage volume in the third quarter. We are also adding hundreds of thousands of new clients into our ecosystem, creating an expanding foundation for future growth.

Our total Q3 expenses increased by 46% year-over-year, primarily driven by higher variable compensation and an increase in team members and production roles to support our growth.

Turning to our balance sheet. We remain in a strong liquidity position with total liquidity of $6.9 billion, which included $3.5 billion of cash as of quarter end. We define total liquidity as cash and cash equivalents plus undrawn MSR lines, undrawn unsecured lines of credit and self-funded mortgages that can be transferred to our funding facilities at our option.

These figures reflect the strong underlying cash generation of the company and our recent issuance of $2 billion in senior notes at substantially lower interest rates than the notes they refinanced. After the end of the quarter, we repaid the $1.25 billion of senior notes due 2025.

Overall we are extremely proud of our long-term track record of delivering profitable growth at scale and our record performance in the quarter and year-to-date. To illustrate just how massive our scale is, the company has been consistently profitable on an annual basis, having generated double-digit GAAP pretax income margins every year from 2015 through 2019. Over just the first 9 months of 2020, we produced approximately $6.6 billion in GAAP pretax income, which represented a dramatic improvement compared with a year earlier.

Our strategic objective remains to achieve 25% market share of the mortgage market by 2030, while continuing to generate industry-leading profitability over the long run. To achieve these long-term objectives, we are investing in our brand and technology so that we can profitably grow through all market environments. For example, over the 12 months ended September 30, 2020, we leveraged more than $500 million invested in technology and our approximately 2,900 technology team members to further increase monthly loan production capacity and enhanced efficiency, including some of the enhancements Jay discussed. We also invested approximately $900 million in marketing over the same time frame.

Moving on to our outlook. We currently expect closed loan volume of between $88 billion and $93 billion, or an increase of 73% to 83% compared to $50.8 billion in the fourth quarter of 2019. We expect net rate lock volume of between $80 billion and $87 billion, which would represent an increase of 82% to 98% compared to $43.9 billion in the fourth quarter of 2019. And we expect gain on sale margins of 3.8% to 4.1%, which would be an improvement of 11% to 20% compared to 3.41% in the fourth quarter of 2019.

Lastly, the company's Board of Directors approved a $1 billion share repurchase program effective today. The authorization reflects the Board and senior leadership's confidence in Rocket Companies' long-term prospects. The program gives us the flexibility to take advantage of opportunities if we believe the market is undervaluing our business. We are committed to using our substantial cash generation to create long-term value for our shareholders.

With that, we are ready to turn it back to the operator for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Your first question comes from the line of James Faucette from Morgan Stanley.

James Eugene Faucette - *Morgan Stanley, Research Division - Executive Director*

I'm wondering if we could start with the new retention metric that you highlighted. And maybe you can just spend a minute or 2 helping us understand how you look at that and how that's different than the other retention metrics you've used in the past. And maybe Jay in particular, when you look at that 92%, kind of how did -- what goes through your mind in terms of the different ways that you can look to take advantage of that and increase the lifetime value of those customers?

Jay D. Farner - *Rocket Companies, Inc. - CEO & Director*

Yes. Thanks for the question. I know we talked a lot about this during the IPO process, and Bob Walters in particular, about our recapture capabilities, which are now I think Julie referenced north of 4.5x the industry average. So if someone's going to be paying off on our portfolio, we are recapturing that client, which is great because it generates very good revenue for us.

And that recapture rate is one of the reasons we were able to have this very high retention rate. And you just touched on it. When the retention rate is high, of course that means longer client lifetimes. And when you think about the lifetime value of the client, more opportunity to help them with a refinance, more opportunity to help them with a purchase, more opportunity to help them with other products such as auto or personal loans. And here's I think something different for us that we benefit from out of a lot of other retention-type businesses is that we're profitable on the first transaction, as you saw today, very profitable.

But this is actually even more unique for us because in our business, when the retention rate rises, you're probably looking at increased interest rates. And so as a servicer, we're collecting those monthly payments. We're also having the ability to market to those clients for other services. But if rates are falling and we might see the retention rate drop a bit, the rate today here in the low 90s which is still incredible, we're still benefiting because that recapture rate allows us to generate significant revenue on the refinance of their mortgage.

So the retention rate and the recapture rate work together, but also like are a natural hedge, I think Julie referenced, that really allows us to win regardless of whether interest rates are rising or interest rates are falling. And that really supports that broader ecosystem that we're building, as I touched on before, keeping the client in our ecosystem to be able to offer additional products and services to them. That's how I think about it.

James Eugene Faucette - *Morgan Stanley, Research Division - Executive Director*

That's really helpful. And then I guess to build on that, one of the key things that we look at is how quickly can you get people into the Rocket ecosystem. And can you do that at kind of the beginning of their professional and working careers as -- and when they're buying their first homes? I think you made some comments that you're seeing some success there. But maybe you can talk a little bit about where you are seeing success, and how we should think about the trajectory on that initial purchase volume and how that can contribute to the lifetime value, particularly if you're able to maintain those high retention rates.

Jay D. Farner - *Rocket Companies, Inc. - CEO & Director*

Yes. And thanks again for the question. As I referenced in the comments on the call here, the demand for the digital experience is stronger than ever. And we're seeing significant growth there, and in particular for us on the purchase side. So we're talking about millennials. We're talking about folks who've been thinking about buying a home. And as I touched on, COVID has really driven these clients or accelerated their desire to be homeowners, moving from urban centers into suburban places and looking for home purchase. In fact, I think Q3 was the strongest -- one of our strongest purchase quarters. And we issued more verified approval letters to clients in Q3 than any other quarter in our company's history. So that's one way that we engage that client early on in their life cycle.

And then I'd like you to think about the Rocket Auto business that we are excited about, because that also tends to skew to a younger demographic. And so if mortgage or home isn't the initial purchase, a loan or auto may be. And so all of those initiatives in our ecosystem that we're working on allow us to start that relationship building with a younger client base that then we'll retain for 20, 30, 40 years to come.

Operator

Our next question comes from the line of Timothy Chiodo from Credit Suisse.

Timothy Edward Chiodo - *Crédit Suisse AG, Research Division - Director*

I wanted to bring up a topic that comes up often in investor discussions. It's around some of the technology advantages that you have that have taken clearly years and lots of investment to build up. The question is really around can you bring to life some of these advantages that might be behind the scenes, that are maybe tougher for the consumer to see by looking at the user interface? Some aspects that might be more challenging to replicate, could take years to do, whether it be some of your direct connections that you've built out on a proprietary basis or some of the partners you work with like Finicity. Anything into sort of local or municipal systems, anything along those lines would be much appreciated.

Jay D. Farner - *Rocket Companies, Inc. - CEO & Director*

Yes. Thanks for the question. And I believe Julie referenced this as we think about the investments that we've made here in the last 12 months, $500 million when it comes to our now nearly 3,000 technologists and the platform that we've been building.

I think the best example that I can give you is the growth year-over-year. If we look at the first 9 months of '19, I think 94 billion closed. Now we look at 213 billion in the same 9-month period in 2020. 94 billion is a huge base, the largest lender in the country. And now more than doubling that demonstrates the power of that platform and those investments that we've made in technology across the board.

So we've talked about some of the more recent rollouts. One I'll draw your attention to is the Rocket Pro Insight platform. That's giving real estate agents real-time updates on the status of their clients' mortgage. And that's important to them of course because they feel in control. It's very important that, that loan closes. But it also frees up time for our team members to now to focus on the next loan, making us more efficient versus taking those calls. It also allows the realization to drive referral business into our platform.

Another one that I believe Julie referenced is the Mint partnership. We've been partners with Intuit for a long period of time, but really been working hand in hand to have a fully integrate the Rocket Mortgage experience in the Mint experience for their clients so they don't have to leave that app. And we've launched that now. And not only does that allow us to provide that experience to Mint users, but the APIs that were built, we can leverage across additional partnerships.

I know another one that we referenced that's been a tech investment for us is the partnership with realtor.com where we're reaching now tens of millions of prospective home buyers. And again, that takes good strong work from our technology team to be able to do that.

On the internal side, maybe the other things that are less evident, a significant portion of our underwriting process has been leveraging ethical AI, as we talked about, machine learning. A lot of our decisions around verifications of assets or verification of employment, verification of insurance is now done using automated systems. In fact, I think we referenced that there are over 1 million decisions each day that are now automated, all bringing great efficiency to our platform, which is what makes it so scalable.

Timothy Edward Chiodo - *Crédit Suisse AG, Research Division - Director*

That's extremely helpful. And then a quick follow-up, you actually -- you are one step ahead of me there and mentioned the realtor.com. Which I know you mentioned in your prepared remarks as well, but it does seem to have a tilt towards the purchase market obviously. And I was wondering if you could just expand on that partnership in terms of the potential relative to some of your other large brand name partners like State Farm?

Jay D. Farner - *Rocket Companies, Inc. - CEO & Director*

Well, the realtor.com partnership represents yet another example of us integrating our platform into their experience. And so we've started that process, but the sky is the limit on what that integration can look like, when you think of the data and information we have about home values in markets, the real estate connections, the real estate agent connections that they have, the equity information that we have about the 2 million-plus folks in our servicing book.

And so what we're really trying to create there is a seamless process from the very moment that you think about purchasing a home until closing the home. And so the real estate agent, the mortgage approval, Amrock's title business, Nexsys and the closing, the eClosing platforms that we've built, this is just a great way for us to wrap that all together and create a very unique and best-in-class experience for our clients and for realtor.com clients.

Operator

Our next question comes from the line of Ryan Nash from Goldman Sachs.

Ryan Matthew Nash - *Goldman Sachs Group, Inc., Research Division - MD*

So Jay, maybe to bring together a handful of things that you touched upon. I think a big part of the narrative was the ability to take market share. And I guess based on where you're running, I think you're above 7.5% year-to-date, maybe closer to 8% in the quarter, although I know you don't manage to any one individual quarter.

So with that as a backdrop, can you maybe just talk about the sustainability of volumes at these levels? And second, we're obviously seeing rates moving up a bit, and I think market expectations are for them to continue to increase. So can you maybe just talk about how you expect to drive market share in a more purchase-oriented market? Will you be leaning more heavily into the broker channel? Can you maybe just talk about -- you talked a little bit about cash out refis as part of originations. Is that a big part of the volume? And can that help serve as an offset in a smaller refi market?

Jay D. Farner - *Rocket Companies, Inc. - CEO & Director*

Yes, great question. Julie touched on over the last 2.5-plus years when we look at the volume breakdown or the kind of the reason for a refinance or a loan between purchase and cash out and term changes and life changes like divorce, north of 50% of our production is really non-interest rate-sensitive. So that's a critical component. We've demonstrated that for years, and that will continue to happen. Also, when we look at the clients that could save a substantial amount of money here in this environment, and we're still in a situation I believe where 70% of the folks out there, it makes sense to refinance.

So we feel very good about the continued strength and demand not only on the refinance side, but on the home purchase side. Homeownership is back to kind of pre-crisis levels. And as I referenced before, millennials are very focused on homeownership, moving from urban areas.

It was great, welcome news that the vaccine or a vaccine may be on its way, but we don't believe this will alter the course that has been set now for more work from home. Leveraging the home for family and work and all of those things, all things bode very well for homeownership. And so we imagine that will continue.

And I think as Julie gave her guidance for Q4, really what you're looking at if you back out a little bit of pressure we saw in October due to marketing spend for the election, which of course makes it a little bit more challenging for us from a marketing perspective; and the fact that Q4 has 4 or 5 fewer what I'll call actionable business days, the day before Thanksgiving or the day before Christmas Eve which can be a bit more challenging. If you back that out and look at what we're forecasting for production in Q4, it's very, very similar to what we accomplished in Q3. And as you touched on, this is where our ability to reach into the market, leveraging whether it's our partners at Schwab, realtor.com, Mint, or our broker partners along with leaning into our Direct to Consumer advertising, it really positions us to grow market share when others are pulling that because of slight changes in interest rate.

Ryan Matthew Nash - *Goldman Sachs Group, Inc., Research Division - MD*

Got it. And maybe one for Julie, I don't want her to feel left out here.

So Julie, can you maybe just talk about how gain on sale spreads trended across the quarter, given that they came in well above the guidance? And can you maybe just talk about what you're seeing that will drive the compression into the fourth quarter? How much of that is being driven by channel mix expectations versus competition? And as you look out over the next few quarters based on what you're seeing today, just any sense for how long you think we can continue to operate with these elevated spreads?

Julie R. Booth - *Rocket Companies, Inc. - CFO & Treasurer*

Yes, sure. Thanks for the question. And in Q3, our gain on sale margins exceeded our expectations and remained elevated by historical standards. So our margins have remained elevated for longer than expected.

If you look at that change as I mentioned, from Q2 to Q3, change in the loan pricing represented less than 10 basis points of that variance. Channel and product mix were the biggest drivers of this variance, about 40 basis points of this. And that resulted from our strong Partner Network growth that we saw during Q3.

So -- and as we look ahead into Q4, margins are still strong by historical standards, and they're continuing to stay elevated. We think that demand that we're going to continue to see with 70% of folks able to refinance and the amount of refinance volumes you take that into the next couple of years, if there's 6 trillion or 7 trillion out there ready to be refinanced, that is something that's going to take years to work through, which will continue to elevate that demand, we believe, going into the upcoming years. And so we feel really good about where our gain on sale margins and volumes are heading here into the fourth quarter.

Operator

Your next question comes from the line of Rick Shane from JPMorgan.

Richard Barry Shane - *JPMorgan Chase & Co, Research Division - Senior Equity Analyst*

One sort of business related and then one stock related. As we look forward to the implementation of the GSE adverse market fees coming into place, I'm curious whether or not you think the primary markets will reprice, or whether or not you think originators will start to absorb some of this and that will adversely impact gain on sale.

Robert Dean Walters - *Rocket Companies, Inc. - President & COO*

This is Bob Walters. Thanks for the question. Largely, most of that pricing has been absorbed. And we got a test run at it before the changes that were made a month or so ago. So they've largely been absorbed at this point and are fully priced into the margins.

Richard Barry Shane - *JPMorgan Chase & Co, Research Division - Senior Equity Analyst*

Great. Okay. And then when -- unique situation. You guys have announced $1 billion potential buyback. I am curious how that works with the combination of the A and D shares? Are D shares eligible for repurchase as well?

Jay D. Farner - *Rocket Companies, Inc. - CEO & Director*

Yes, that's probably a question, Julie, you want to field that? Or you want to push that to a different time?

Julie R. Booth - *Rocket Companies, Inc. - CFO & Treasurer*

Yes, I can just answer I know that the D shares are not eligible for repurchase. This would be a Class A share repurchase program that we have announced.

Operator

Your next question comes from the line of Ryan McKeveny from Zelman & Associates.

Ryan McKeveny - *Zelman & Associates LLC - Director of Research*

Congratulations on the results and guidance. So first question on gain on sale margins, Julie, taking some of your commentary on 4Q maybe a step further. I think one of the debates out there is really thinking about that outlook into 2021, 2022 and sort of theoretically how much compression there could be on gain of sale margins, especially if the environment is such where rates do back up at some point and then industry volumes begin to fade.

So definitely not looking for specific guidance on volumes or gain on sale margins for next year, but just hoping you can maybe elaborate on the puts and takes to the gain on sale margins. I appreciate all the color that you did provide around the differentiation with your recapture and dynamic pricing. But so maybe if you can share some color on what you've seen historically in periods that might be somewhat analogous to today where you have 2020 as a pretty massive year? But effectively what happens after that? And why? What are those primary factors that we should think about for the puts and takes?

Julie R. Booth - *Rocket Companies, Inc. - CFO & Treasurer*

Yes, sure. If we look back and we kind of look at maybe more normalized gain on sale margins, you'll see our Direct to Consumer margins have ranged between 400 and 450 basis points. And then on the Partner Network side of things, probably between 100 and 150 basis points if you look back over time.

So I think as I mentioned that the demand that we're seeing now will continue to probably have a nice upward impact on those margins, relative to the sort of historical levels that we have seen into the upcoming years. How long that will last? It's to be seen, but like I said, there's quite a lot of demand still out there into the upcoming years.

Ryan McKeveny - *Zelman & Associates LLC - Director of Research*

Got it. That's very helpful.

And on the partner segment, exciting to hear about that new partnership that was struck last week, but curious on the Rocket Pro TPO changes this quarter. I was hoping you could address just how you think about your positioning in the wholesale channel, how you think about your differentiation from others maybe in terms of execution, speed, pricing, platform, you kind of you name it, and how that benefits your mortgage partners. And along those lines, how does that positioning and some of the advantages you're bringing into that market influence the gain on sale margin in that segment, kind of above and beyond the overall mortgage market influences on the margin?

Jay D. Farner - *Rocket Companies, Inc. - CEO & Director*

Well, I would say as we think about our Partner Network, which is large and growing, both branded partnerships that we've accomplished with Charles Schwab, State Farm, Intuit, another partnership we referenced today that we'll be talking more about as we get into 2021, they're incredibly important. They reflect margin that is between maybe your traditional third-party and direct to consumer, which is certainly beneficial and they leverage our brand. And that's the unique thing also about the third-party channel that you're talking about brokers. And I think the unique thing that we bring to the table not only our process and our technology, but now as we've rebranded to Rocket Pro TPO, we are giving a brand that is so highly regarded in the industry and allowing these brokers to leverage that.

I think I also referenced something that really sets us apart. Whatever is best for our clients, we want to help them achieve that. And so we were able to offer 10,000 purchase leads to our TPO partners here as we rolled out the new Rocket Pro platform. And we'll be able to continue to do that.

And so those brokers have the advantage of using great technology, allowing their clients to access the process that has won the 11th J.D. Power award in a row for loan origination, and now leverage the brand that people know and trust, and receive lead flow to allow them to grow their businesses as well. So when we think about that space, we're really focusing on all of those things that we can do to continue to grow it and also differentiate ourselves from kind of the traditional players in that space.

Operator

Your next question comes from the line of Matt Roswell from RBC.

Matthew Van Roswell - *RBC Capital Markets, Research Division - Assistant VP*

I was wondering if we could think about the expense side going into the fourth quarter. Is there any sort of seasonality we should be aware of? Is there anything as we kind of think about adjusted EBITDA?

Julie R. Booth - *Rocket Companies, Inc. - CFO & Treasurer*

Yes. While we don't give guidance on our expenses going into the fourth quarter, certainly we will see the variable expenses vary every quarter with production. But there's nothing in particular that we're looking at in Q4 that is, I think, of note as we think ahead here. So nothing really special to comment on as we look ahead.

Matthew Van Roswell - *RBC Capital Markets, Research Division - Assistant VP*

Okay. And then a bigger picture question, how are the efforts going into sort of the nonmortgage loans going? Or are you so busy in the mortgage space, that you're not really focused that much going into auto and personal?

Jay D. Farner - *Rocket Companies, Inc. - CEO & Director*

Well, no, we're very focused on that. And one of the key strengths of our platform, not only is the technology, the client base, the brand, but also the leadership. And so our ability to leverage our leadership across those areas, both real estate Rocket Homes, Rocket Auto and Rocket Loans is going very well. I know we're not providing the guidance right now on those businesses, but when we think about 2021, we're looking at businesses that will see substantial growth.

Operator

(Operator Instructions) Our next question comes from the line of Arren Cyganovich from Citi.

Arren Saul Cyganovich - *Citigroup Inc., Research Division - VP & Senior Analyst*

Maybe you can just touch a little bit on your expansion plans into Canada and how that's progressing, and I guess what your thoughts are in terms of the proportion of mortgage production you would expect to get out of it over the next couple of years.

Jay D. Farner - *Rocket Companies, Inc. - CEO & Director*

Yes. We're very excited about the work that we're doing in Canada. I know we released here in the last week or 2 that we've made an acquisition of a company called Finmo to partner with Lendesk. And so that really allows a deeper direct access to the mortgage brokers in Canada. And our focus today is really developing the best tech process between the broker and the lender. And so that Finmo acquisition was critical.

I've seen a lot of positive response from both the broker community in Canada. And so just things are going as planned, and we continue to develop out that technology. It's -- the area's ripe for disruption. Between Lendesk and Finmo, we believe we're bringing an experience that no one else has to the table.

Arren Saul Cyganovich - *Citigroup Inc., Research Division - VP & Senior Analyst*

And then on the -- back on the share repurchase authorization, is this something that you intend to use on a regular basis? Or is this more kind of episodic whenever you see opportunities in your stock or a bit too much excess capital?

Jay D. Farner - *Rocket Companies, Inc. - CEO & Director*

Yes. So I think this is -- goes back to the broader concept of is just how we're going to handle capital allocation. And so remember, we've got a 35-year track record here, I think, of allocating capital in a pretty strategic manner.

As Julie touched on, our first priority is always ensuring we've got a very strong balance sheet, our business is well capitalized, and then making sure we're investing in our business. For us, there's never been a better return than investing those dollars back into our business, whether it's spending the dollars on marketing to grow that brand, spending the dollars on technology to continue to grow out that platform that we've been able to leverage.

Clearly, we're always considering different M&A activities. And then finally as we go through that waterfall, as profitable as we are, there are times when returning capital to shareholders is the right thing to do. And so that could come in the form of a special dividend that we've talked about. We did that as a privately held organization from time to time. But now that we're public, another way for us to help of course shareholders is to repurchase our shares.

And I think that was an important move that the Board made. We're going to be thoughtful and disciplined, but as always, opportunistic. We have a strong feeling about the value of our organization. And if there's an opportunity to buy back shares that we think are undervalued, then we'll do so.

Operator

Your next question comes from the line of Mark DeVries from Barclays.

Mark C. DeVries - *Barclays Bank PLC, Research Division - Director & Senior Research Analyst*

Is there any color you can provide us today on the percentage of lots you're getting from refi versus purchase, and also kind of broken down by your 2 channels?

Julie R. Booth - *Rocket Companies, Inc. - CFO & Treasurer*

Yes. That is not something that we have disclosed in the past. I think we disclosed our mix in our S-1 kind of 2019 and what that looks like. But that is something where we're still seeing very strong purchase demand here and something that we're very focused on. So we're just not disclosing right now the mix between that and the channels.

Mark C. DeVries - *Barclays Bank PLC, Research Division - Director & Senior Research Analyst*

Okay. The second question, maybe a similar response. But what percentage of your title business are you capturing from your originations? And how high do you think that can ultimately go? And are you generating a third-party business there?

Jay D. Farner - *Rocket Companies, Inc. - CEO & Director*

Yes. I don't think we disclosed the percentages. But as I referenced before, title -- or Amrock had its record quarter as well. And so a significant portion of the title that we do here is we leverage through Amrock. And they also have a robust third-party title business that is not based on Rocket Mortgage or Quicken Loans. But we don't give specific percentages.

Operator

Your next question comes from the line of Jack Micenko from SIG.

John Gregory Micenko - *Susquehanna Financial Group, LLLP, Research Division - Deputy Director of Research*

I wanted to revisit the buyback versus the special dividend. Pretty thin float, the buyback's maybe half of the shares that are kind of currently trading. What was the thought process between maybe a buyback or a special dividend at this point?

Jay D. Farner - *Rocket Companies, Inc. - CEO & Director*

I mean really, just what's the best opportunity for us. If we see the stock price drop to a place that we think is advantageous, the better use of our capital would be to buy those shares back.

John Gregory Micenko - *Susquehanna Financial Group, LLLP, Research Division - Deputy Director of Research*

Okay. And then looking at the marketing spend, it grew as a percent of revenue. And I know you guys are pretty consistent with your marketing spend. Was there anything this quarter as you think about the spend there and the timing maybe into spring selling '21? Or was it just you just kind of match the spend versus the revenue? Or are you making a conscious effort to really deploy more of this elevated revenue into marketing while it's available to you?

Jay D. Farner - *Rocket Companies, Inc. - CEO & Director*

Well, as we've talked about for a long period of time, if there's a marketing dollar that can be spent that is profitable, especially on the first transaction, we will spend it. Because the lifetime value of that client is multiples more than the initial revenue that we -- and profit that we generate in the first transaction.

We also of course saw increased media costs as we went into this quarter with the election. I'm sure you were watching the television, listening to radio and going online as much as I was. And it was hard to see an ad that wasn't related to the election. So that brought costs up a bit for us as well.

Operator

Our next question comes from the line of Bose George from KBW.

Bose Thomas George - *Keefe, Bruyette, & Woods, Inc., Research Division - MD*

Actually, do you guys give the recapture rate on borrowers who are paying off loans to make a purchase transaction? And I was just wondering, does that work into the retention metric?

Jay D. Farner - *Rocket Companies, Inc. - CEO & Director*

No, I don't think we give the specific number for that. But I will share with you as we think about the broader ecosystem, Rocket Homes plays a critical role in providing to our mortgage clients the homes that can afford the equity that they have in their home, and even getting them what we call Rocket ready or verified approval. And so someone in our servicing portfolio who's been demonstrating behavior, looking at homes in their area, wanting that verified approval, gives us a heads up or trigger to be able to work with that client, to ensure we bring them back from a purchase perspective as well. And so that's why this robust ecosystem is still important to us.

Bose Thomas George - *Keefe, Bruyette, & Woods, Inc., Research Division - MD*

Okay. Great. And then if I can, in terms of -- I wanted to ask about Ginnie Mae buyouts. Is that contributing much to earnings? Or is there any way to kind size that as a potential benefit?

Julie R. Booth - *Rocket Companies, Inc. - CFO & Treasurer*

Yes. We have done some Ginnie Mae buyouts. And you can see that we have borrowed on our line of credit on our balance sheet, but it is an opportunity that we're continuing to evaluate. And for right now, that is the amount that we're going to do is kind of what you see on our balance sheet there, about $250 million so far.

Operator

Our next question comes from the line of Don Fandetti from Wells Fargo.

Donald James Fandetti - *Wells Fargo Securities, LLC, Research Division - Senior Analyst*

I was just wondering there's been a lot of activity with the nonbank stocks, et cetera. Just curious -- and they all seem to want to take market share. Just curious if you thought the competitive dynamic would -- if that would change the competition, and then also what you're seeing from some of the large banks?

Jay D. Farner - *Rocket Companies, Inc. - CEO & Director*

Well, we do see other folks who participate in the mortgage and real estate space, thinking about going public. I think when we think of Rocket Companies and our focus on helping consumers with some of the most exciting experiences they have in their life, whether it's buying home or refinancing their home or buying a car, we think we're uniquely positioned. Obviously, we've talked a lot about brands here today. We've become the household name when it comes to thinking about a great high-quality mortgage or now real estate experience, spending nearly, what, $900 million, close to $1 billion in marketing. Also, when we think about the client service we're providing, and I referenced J.D. Power awards a few times here, but we think that really separates us from others that may be in a similar situation.

And then of course, the dollars that we're able to invest in the technology to grow this platform and separate us from others, with now 2 million clients on our servicing book, with a retention rate north of 90%, with a recapture rate that's 4.5x the industry according to Black Knight, and watching this base grow, how we think about this fintech platform that we built, the growth that we're seeing, we think that's quite a bit different than some other folks that may be in the space doing mortgages.

Operator

Your final question comes from the line of Henry Coffey from Wedbush.

Henry Joseph Coffey - *Wedbush Securities Inc., Research Division - MD of Equities Research*

Yes. I know on the last call, you talked about your objectives in terms of building capacity for next year. Maybe you could talk about that a little bit more. And depending on where the refi and the purchase money market falls out, how do you see that affecting your channel mix between the independent -- between the brokers, the partner network and your direct retail originations?

Jay D. Farner - *Rocket Companies, Inc. - CEO & Director*

Well, the progress is going very well. As you look at the closed volume that we were able to achieve in Q3 and our projections for Q4, the technology to allow us to -- and our target goal was the 25% of the normalized mortgage market. So that's 2 trillion, give or take, which would be 500 billion, north of just about 40-or-so billion a month. And so from a technology perspective, from an operations perspective, the platform is performing incredibly well.

When we think about the future, and we talk about this a lot, we touched on the realtor.com partnership. We talked about another very large partnership that we'll be announcing with more detail in 2021. We talked about the new rollout of Rocket Pro TPO, giving brokers that brand and that technology.

All of these things will allow us to continue to lean into the market and grow share regardless of interest rate conditions. And so we continue on our path, building all of the right long-term strategies to allow the company to achieve that long-term goal of 25% market share by 2030.

Henry Joseph Coffey - *Wedbush Securities Inc., Research Division - MD of Equities Research*

Just kind of a second question, it's not really related, but what about the "other areas?" How is that playing? Auto and direct lending, just the whole other ball of wax that you've talked about so much.

Jay D. Farner - *Rocket Companies, Inc. - CEO & Director*

Well, as I touched on before, I know we're not providing guidance, but I can state that much like the mortgage platform, building out the different channels in our real estate from Rocket Homes, which now has millions of visitors a month, For Sale By Owner platform, the Rocket Auto platform, all of those things are going as planned. And we are very excited about the growth we've seen here in Q3 and even more excited about the growth that we believe we will experience in the future.

With that, ...

Julie R. Booth - *Rocket Companies, Inc. - CFO & Treasurer*

I just have one -- one -- oh sorry.

Jay D. Farner - *Rocket Companies, Inc. - CEO & Director*

Go ahead, Julie. Want to clarify...

Julie R. Booth - *Rocket Companies, Inc. - CFO & Treasurer*

One thing I wanted to make sure that I did clarify here, I wasn't sure earlier the question regarding the share repurchase plan, if the question was regarding the or D shares. So I just want to clarify that the share repurchase plan applies to both A and D shares.

Jay D. Farner - *Rocket Companies, Inc. - CEO & Director*

Thank you. Thank you, Julie.

Well, great. We appreciate everyone joining today, and I think that's going to wrap up the questions. But thank you so much for taking the time.

Operator

That concludes today's conference call. Thank you, everybody, for joining. You may now disconnect.
