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10 TAKEAWAYS FROM THE FIRST 10 YEARS OF REAL ESTATE FINTECH

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Real estate crowdfunding came into existence after the Global Financial Crisis, with several companies launching from 2010-2012, spurred in part by the JOBS Acts, which streamlined the process of raising capital from individual investors. As the Internet transformed one industry after another, the real estate investment space appeared stodgy and overdue for disruption. This article outlines lessons so far, and a few predictions for the future.

1. Real estate crowdfunding is creating new and valuable options for investors. Today there are many companies that will allow investors to participate in real estate with as little as $5,000. These crowdfunding companies have indeed begun to democratize real estate investing. Also, they have created alternatives to some questionable practices such as an earlier generation of non-traded REITs that often charged their investors high upfront loans to invest.

2. Nobody has a proven, profitable business model—yet. The hallmarks of a great start-up investment are a disruptive product or service that can yield a large-scale, profitable business. It's been over five years since many companies in this space got their first venture capital funding, and it still isn't clear that any of them have figured out how to make money. Of course Amazon went from its founding in 1994 to 2001 without ever recording a profitable quarter. However, while there are some interesting companies in the real estate crowdfunding group, none of them can yet claim to have Amazon or Uber-like potential.

3. The industry is segmenting along two axes. All of these companies, and the entire real estate investment industry, breaks down based on a few distinctions: debt (lending) focus or equity (ownership) focus; and brokerage model or investment manager model. Beyond these distinctions, industry players based on typical project size, asset type, or geographic focus.

4. There have been many pivots. Realty Mogul and Fundrise both appear to be focused on launching and managing small non-traded REITs that invest in real estate—which is different from where both companies started out. LendingHome has continued their original strategy of originating fix-and-flip loans, and is not offering loans for owner-occupants. RealtyShares serves as a mortgage broker in many cases, and has exited the single-family residential financing space to focus exclusively on commercial real estate. The shift in strategies is to be expected in a nascent industry,

but it also speaks to the difficulty of finding a sustainable business model in this industry so far.

5. Lines between fintech and traditional players are blurring. LoanDepot has built a sizable business providing some mortgages by hiring hundreds of loan originators and opening offices around the U.S. At the same time, they are investing heavily in technology to optimize the customer experience and streamline operations internally. Are they a fintech company or a conventional mortgage lender? The answer is both. Like Charles Schwab, they are simply a successful company seeking to provide value to their customers in any way they can, across every available channel that makes financial sense.

6. There is no dominant marketplace for real estate among today's players. One of Silicon Valley's favorite types of start-up success is to establish a dominant platform where there was none before. Think about eBay, LinkedIn or even Google, each of which amassed dominant market share through a positive feedback loop of one kind or another. The more people used their services, the harder it became to displace these industry leaders. In real estate crowdfunding—as in the larger real estate investment industry—there are no dominant players. CBRE is the most prominent commercial real estate brokerage firm, but even this impressive global company has low market share as compared with the entire brokerage industry. Likewise, Blackstone Group is considered the largest real estate private equity firm with $120 billion of real estate assets under management. Meanwhile experts estimate the value of global real estate at $217 trillion (Source: Fortune). Even after stripping out all owner-occupied homes, this puts Blackstone's market share well below 1 percent.

7. There is no Adobe for the real estate industry either. With their PDF file format and other innovations, Adobe became an industry standard used by virtually everyone— both in business and for personal applications. Who hasn't sent or received a PDF file in the recent past? In the real estate investment world, having industry standards might be helpful in many ways. For example, a standardized way of handling escrows, loan transactions or even comparing one investment to another on an apples-to-apples basis would be very valuable. Sadly, no such innovation has arrived in the past 10 years. Having funded more than 800 investments in that time, the author's company has been eager to adopt new approaches that would streamline operations. However, I can report that we are conducting business largely the same way we have since inception— by meeting borrowers and seeing their projects in person; assessing property values through comparable sales; and then closing their transactions as smoothly as possible, still using title and escrow infrastructures that are largely unchanged in decades.

8. Curating investments remains as important as ever. Blackstone has grown into an industry leader in large part because they have chosen investments that made money for Blackstone's clients. Most real estate fintech companies are also curating or selecting investments, in one way or another. They must identify sponsors (individuals) who are competent and honest, who have projects that make sense. This may sound simple but as any experienced real estate investor will tell you, it is easier said than done, particularly with the vagaries of the market cycle. Choosing the right investments or opportunities to share with the investors they have aggregated will prove to be the single most important factor in the success or failure of these companies, as with any real estate investment business.

9. Few top real estate investors have staked their career on Fintech. Most real estate crowdfunding companies started by focusing on the opportunity to use technology in novel ways, and/or the regulatory changes brought by the JOBS act (namely, the relative ease of raising capital from individuals after the JOBS act passed). The most seasoned investment managers with the best track records did not join—and still have not joined—into the fintech fray, because they had no need to gamble on how this novel area would work out.

10. Blockchain technology is intriguing but no killer app has appeared—yet. Blockchain should be valuable for real estate transactions. The role of recording and title are both critical and also painfully outdated. However, without county recorders in the U.S. deciding to adopt some form of blockchain, the rest of us will continue to conduct business as before. Companies like the author's business are eager to embrace blockchain in ways that make sense but only once there is some momentum—which hasn't happened yet.

In summary, the real estate investment and mortgage industries are likely to follow a similar path to the larger investment industry. The future will not be defined by "old" and "new" companies that either ignore or embrace technology. Rather, there will be successful companies that take good care of their clients—some of which are new, and others well-established—and all the other companies, who will go out of business eventually. In retrospect, we should not be surprised that no new entrant has yet disrupted the entire business. Facebook exploded because young users with few entrenched ideas adopted it, and it spread from their as a new way for us to socialize. In contrast, real estate investment and mortgage decisions are largely the domain of relatively older people, who are unlikely to embrace new things for very important decisions, until they have proven themselves to be reliable over time.