
Real Estate Crowdfunding

The digital evolution of real estate funding and investment

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In brief

The digital disruption that has transformed numerous sectors of the economy over the years has begun in real estate funding and investment. Real estate crowdfunding (**RECF**) is the fastest growing category of the global crowdfunding industry and is forecast to continue to grow exponentially in the medium term. This growth represents a threat to traditional real estate business models, but an opportunity for innovative sector participants and investors to be part of the inevitable evolution of real estate finance.

In this article we consider the impending digital evolution of real estate funding and investment, and highlight the opportunities for the Australian market.

In detail

What is RECF?

RECF is the offering of traditional real estate assets or ventures, through differing types of financial product and distributed to investors through technology.

RECF allows a broader range of investors (the ‘crowd’) to make smaller investments in real estate assets and ventures in a more efficient manner. The aggregation of smaller amounts of capital from a broad group of investors results in the creation of a significantly larger pool of new capital, allowing the crowd to collectively buy properties, lend money to home owners and property developers, and potentially take equity stakes in new development projects as joint venture partners.

RECF is the evolution of traditional real estate syndication, with one subtle and important difference: the user experience, for which technology is the key.

User experience in real estate transactions

The addition of the ‘technology’ element allows RECF platforms to offer a user experience that traditional real estate syndication arguably cannot. For example:

- Information – The online investment experience can be enhanced by digital analytics and investment tools which provide investors with targeted and tailored information to help them make more informed decisions more quickly. Over time digital investor education

tools can help to educate the market, building confidence in the investment opportunity and trust in the platform provider.

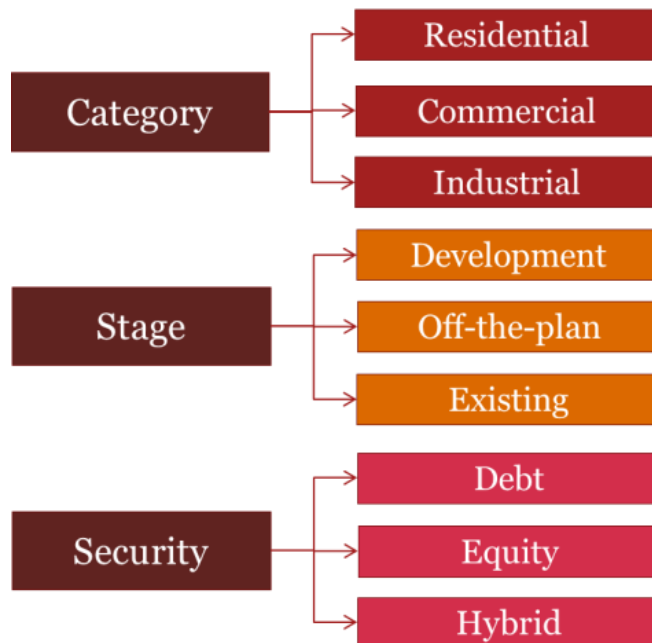
- Scale - Online platforms enable operators to connect with investors anywhere in the world quickly and inexpensively, facilitating the efficient, low-touch scaling of the investor base.
- Convenience – By optimising platforms for mobile devices and focusing on a creative user interface, RECF platforms can reduce the friction involved in traditional real estate investment processes making it easier to invest at volume.
- Trust – Integrating social media tools to connect users with their peer groups helps facilitate open and transparent dialogue about an offering or a RECF platform operator. As investors become more comfortable investing online, the advice and referrals of trusted peers should increase investment volumes.
- Entertainment – RECF platforms have the potential to overlap the experience of real estate investment with entertainment, through strategic platform design and by embedding elements of gamification, transitioning the user experience from one of pure investment to part entertainment.

The success of RECF platforms in Australia will turn in large part on the quality of the user experience. For many incumbents in industries that have been disrupted in the past, this subtlety had not been recognised until it was too late to take action.

RECF models

Global real estate participants and technology entrepreneurs have begun combining real estate with finance and technology¹ to create new businesses, tap new investor segments and change the way real estate is bought, sold and developed.

The 85 models operating globally¹ are varied. Broadly, establishing a RECF platform requires a consideration of the following elements:



Each of these elements can be combined to create specialised RECF models.

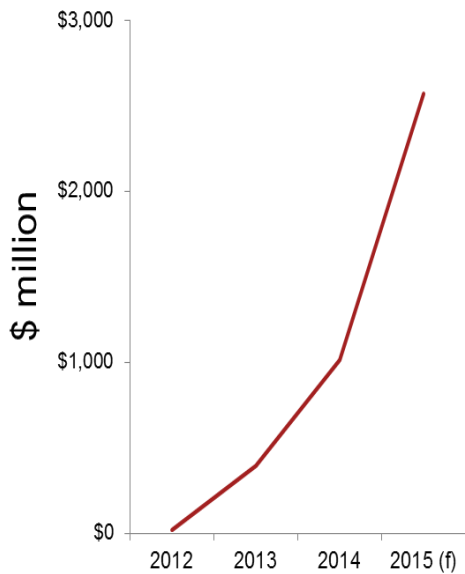
For example, one model may be to offer residential property (category) that is existing (stage) through pure equity instruments (security).

Another may be to facilitate investment in commercial projects (category) that are still in the development phase (stage) through mezzanine debt instruments (security).

Source: PwC

¹ Massolution, 2015 *CF-RE Crowdfunding For Real Estate*, page 64 (<http://www.crowdsourcing.org/research>)

Global growth of RECF



According to Massolution², real estate crowdfunding is one of the fastest growing segments of the global crowdfunding industry and is expected to continue to increase materially over the medium term.

The amount invested through RECF platforms has grown (or is forecast to grow) as follows:

- In 2012, a modest \$19.06 million was invested through RECF platforms.
- In 2013, that figure increased to \$396.4 million in 2013 (nearly 20 times growth)
- In 2014, just over \$1 billion in 2014 (156% year on year growth)³.
- Massolution forecasts volumes to reach \$2.57 billion in 2015 and continue to grow to a total of \$250 billion by 2020⁴.

Investment in RECF platforms

The rapid growth of RECF platforms has not gone unnoticed by global investors.

In the first 3 quarters of 2014, venture capital firms in the US invested \$118.5 million into 11 real estate related start-ups which is more money and more deals than any complete year since 2000, according to industry tracker Dow Jones VentureSource.

In the third quarter of 2014 alone, \$64.8 million was put into six companies. This is the largest amount and the highest number of deals in any quarter since the second quarter of 2000⁵.

In 2014, \$41 million was raised by 2 RECF platforms, RealtyShares⁶ (\$10 million) and Fundrise⁷ (\$31 million). Interestingly, the investors in those rounds were not just venture capital firms, but included global social networking firms and property developers. For some investors, exposure to these platforms represents both an investment opportunity and a hedging strategy.

RECF in Australia In Australia, RECF is embryonic. However, given Australia's solid financial services markets and passion for real estate, it is likely that over the medium term the Australian RECF sector will develop as follows:

1. **Increase in RECF** – There is likely to be an increase in the number of RECF platforms, initially focusing on pure residential opportunities. Since RECF is a new concept to

² 2015CF-RE Crowdfunding For Real Estate, (<http://www.crowdsourcing.org/research>)

³ 2015CF-RE Crowdfunding For Real Estate, page 58 (<http://www.crowdsourcing.org/research>)

⁴ 2015CF-RE Crowdfunding For Real Estate, page 55 (<http://www.crowdsourcing.org/research>)

⁵ Dow Jones VentureSource

⁶ <http://techcrunch.com/2015/04/07/realtyshares-gets-10m-from-menlo-to-grow-its-platform-for-crowdfunding-real-estate-projects/>

⁷ <http://dcinno.streetwise.co/2014/05/28/chinese-firm-leads-31-million-fundrise/>

Australian investors, it will be incumbent on the early platforms to educate the market in order to achieve market traction.

2. **Vendor engagement** – A broader range of vendors are likely to turn to RECF platforms to sell properties. For property developers, this will be driven primarily by competitive pricing and the perceived value of comparable project marketing services. In time, other vendors are likely to seek out RECF platforms to sell properties.
3. **Early investors** – Early adopters are likely to be self-managed superannuation funds (**SMSFs**) and those who are priced out of the property investment market but have some level of capital to invest. For SMSFs, RECF enables trustees to build a diversified portfolio of property assets for relatively modest investment amounts as well as the ability to leverage the investment. The long term nature of property investment also aligns with the purpose of superannuation investments.
4. **Differentiation** – As the sector matures, it is likely that variations in models and service offerings will begin to emerge. Offerings in commercial, industrial and retail categories should also become available. The more sophisticated platforms will seek to diversify their own revenue streams by building in adjacent and complementary services.

The takeaway

Real estate, finance and technology are converging. In the near future this convergence is likely to materially change the way Australians search, acquire, invest in, fund, develop, market and manage real estate assets.

For property developers, real estate agencies, property investors or financiers, it is important to understand these changing dynamics and consider the possible implications and opportunities for your business.

Let's talk

PwC's Venture Capital & Real Estate Advisory teams work together to help clients in the funds management and real estate sectors to understand the RECF opportunity and to execute projects designed to position those businesses for growth.

Our Venture Capital team uniquely comprises lawyers, tax advisers, deals and strategy consultants to provide a one-stop multi-disciplinary service to our clients. We have established and act for some of Australia's most prominent venture capital fund managers, equity crowdfunding platforms and angel groups.

For a deeper discussion of how these issues might affect your business, please contact:

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