



The shift to crowdfunding portals to finance real estate projects

January 27, 2014 - Front Section

BBVA's research team examined the prospects of crowdfunding in the Economic Outlook report produced for the Second Quarter of 2013. They highlight that crowdfunding's value proposition is simplicity and efficiency. Building on this conclusion, they speculate that crowdfunding will cause conventional banks to eventually lose market share. Once crowdfunding portals have served early adopters and proven their value proposition, they will rapidly gain market share and achieve widespread adoption, at the expense of incumbents. The simplicity and efficiency of crowdfunding will result in lower transaction costs due to less involvement from financial intermediaries, more opportunities for direct risk assessment by investors, and, consequently, higher returns. Thus, while in the short run these financial products will only cater to a non-institutional and proactive subset of investors in the financial markets, they will eventually capture significant market share.

There is a broad spectrum of control among crowdfunding portals: from the fully hands-on and vertically integrated, such as Real Crowd (where the portal sponsors and manages each deal that gets listed), to the more hands-off, non-intermediated approach taken by GroundBreaker (where the portal provides a marketplace for investors and sponsors to interact but is otherwise not involved in the deal). The more restrictive portals manage risk by pre-vetting and co-sponsoring projects, at the cost of lower returns for investors and/or the operator, while the more liberal ones expect investors to manage risk by performing their own due diligence, maximizing their potential returns. It is this last breed of portals that will best realize the market efficiencies of crowdfunding by empowering individuals to invest based on their diligence and preferences.

While the liberalization of markets through crowdfunding will improve efficiencies, the more that is expected of the investor by a portal, the more the portal must ensure the involvement of competent developers and experienced investors. Despite these concerns, in the era of "big data," the crowd may be the most reliable source of analysis. On more open and active platforms, investors stand to benefit from crowdsourced investment analysis, something that has made companies like Estimote.com so successful.

Regardless of the winning approach to real estate crowdfunding, we should expect an increasing portion of the multi-billion dollar real estate market to shift to direct investments through crowdfunding portals. Both investors and real estate developers stand to gain from this disruptive technology as it brings higher deal flow and more efficient access to capital. It is only conventional investment firms that stand to lose.

Matt Steele is the advisor at GroundBreaker, New York, NY.

New York Real Estate Journal - 17 Accord Park Drive #207, Norwell MA 02061 - (781) 878-4540