

BROKERAGE FIRMS DEAD? WHY THE PREDICTIONS ARE **WRONG**

By Steve Murray, president

We read recently that Robert Reffkin, founder and CEO of Compass said that, essentially, brokerage firms as we know them would be dead and gone in ten years, that technology and agent teams will become the prevalent model at that time and that Compass will be a market leader. This comes on the heels of Reffkin saying last fall that Compass would have “a 20 percent market share in 20 large markets by 2020.” We weren’t at Inman recently where Reffkin supposedly commented on the future of brokerage, but we will accept the written words and recollections of an Inman writer on this issue.

I suggest that all leading brokerage firms call us and let us sell your firm quickly before all this happens and before there are no buyers.

Just kidding.

Some 40 years ago, in the fall of 1977, one of the largest financial services firms in the country gathered over 50 of the top firms in the brokerage industry to announce that they were going to buy them or attempt to buy them. In the ensuing years, that financial services firm threatened many of these firms with the statement that “if you don’t sell to us we will put you out of business.” True story.

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That firm was Merrill Lynch Realty. In less than 12 years, they left the industry after running through a few hundred million dollars. For the record, that is only slightly longer than the other big giant at the time—Sears—lasted in its ownership of Coldwell Banker.

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Why is This Happening?

Here are our views of why real estate makes such an inviting target for so many people with so much money.

1. The industry, in 2017, had gross revenues of \$72.4 billion.
2. The two largest national franchise organizations have about 10 percent national market share each.
3. The 10 largest national or regional brands have less than 50 percent market share which has not grown appreciably in 15 years.
4. The two largest owned-and-operated brokerage firms, NRT LLC and HomeServices of America, after spending billions buying brokerage firms over the last 20 years, together will handle about seven percent (7%) of all transactions in the country for 2017 (700,000 transactions divided by about 10.2 million brokerage-assisted transactions.)
5. The best 20 percent of brokerage firms, regardless of brand, business model or location, have average EBITDA margins of 4 to 6 percent. There are outliers above that, but they are few. There are many more who don’t do that well.
6. Depending on who you ask, 40 to 50 percent of all Realtors® did one deal or less last year and likely the most productive 20 percent of all Realtors did close to 75 to 80 percent of all sales.

“We have data on the top brokerage firms, agents and teams in the 20 largest markets in the country. We know which firms can be bought (although Compass executives say they are not buying large market-share brokerage firms now). We can also compile the 2017 lists of top teams and individual agents in the 20 largest markets and say with some certainty that even if Compass bought every one of them, they wouldn’t get to 20 percent market share in any of these markets.” —Steve Murray

Residential brokerage, therefore, is highly fragmented at the brokerage level, more concentrated at the agent level, with low margins (at the brokerage level), low productivity generally and somewhat inefficient.

New Competitors

We have new competitors—Compass, Open Door, Offer Pad, Purple Bricks, HomeSmart, Realty One Group and EXP. As Jamie Dimon, chairman and CEO of JP Morgan Chase said that new competitors are a fact of life, and they often will try to be lower cost, more efficient and more appealing. He said, “that is what capitalism is.” Incumbents must change and innovate to stay competitive. They have no other choice.

Compass has some advantages. One, they have a lot of capital. Two, they likely have no pressure to actually make money at what they are doing. Three, their investors think they are a technology firm, not a brokerage, and we all know how much the investing world loves technology companies—at any price.

Sooner or later, their money may run out. Sooner or later, their investors will likely want to get a return from their investment (not a sure thing at all). And, sooner or later, the world will find out that Compass is not a technology firm, but a realty firm like most of your companies. In the meantime, they are creating challenges for incumbents.

Change the Way You Do Business

I recall that once it became clear that RE/MAX wasn’t

going away, incumbent traditional brokerage firms had to change the way they did business. At the time, none thought there was any way they could survive with gross margins of less than 30 percent (the portion of total commissions retained by the brokerage firm). Then, they said they couldn’t survive if it declined under 25 percent. Then, no way under 20 percent gross margin.

Yet, today there are dozens of large brokerage firms with gross margins under 20 percent, or even 15 percent, that are profitable and growing firms. They adapted and moved forward.

As a leader, you can’t control what your competitors do. You can only do what you need to do to grow your business and your profit. A leader should anticipate that new competition will always appear, and for the most part, try to manage with lower costs, new technology and perhaps more efficiency than incumbents.

A leader’s key question is how to change to adapt to these new circumstances. Pining about yesterday doesn’t help, and it has never worked as a business strategy.

I don’t think Compass will get 20 percent in all 20 markets by 2020. We know those markets, know the top incumbents in most of them and know the top agents and teams in those markets. The numbers say it is not likely. Maybe they get there in one or two markets—maybe. But, it doesn’t mean they won’t be disruptive in the meantime.