

Change Is Relentless

An Examination of Key Trends Shaping the
Real Estate Industry in 2003

**Strategic Issues Work Group
Association Executives Committee
National Association of Realtors®**



INTRODUCTION

What lies ahead for the U.S. real estate industry in the next few years?

The Strategic Issues Work Group of the National Association of Realtors®' Association Executives Committee was charged with identifying emerging trends and issues that are likely to impact the real estate industry in the near future. The goal was to prepare a document that will assist real estate associations, brokers, agents and affiliated professionals in their strategic planning.

The work group held a series of structured discussions in February 2003 with brokers from a variety of business models, top real estate agents and consultants familiar with industry trends. For reasons of confidentiality, the names of those participants are not included in this report; however, their comments are cited as direct quotations.

The result of those discussions is this report, which covers:

- **Industry Trends:** A Shifting Kaleidoscope
- **Brokerage Trends:** A New Definition of the Business
- **Agent Trends:** Gaining Control of the Business
- **The 'New' Consumer:** A Force for Change
- **Technology Trends:** A Voracious Appetite for Data
- **Conclusion:** Change Is Relentless

In keeping with the group's mission, this report draws no conclusions and makes no recommendations. There was consensus on many areas but strong opposing opinions in others. Rather than try to decide which point will succeed we report on all making the report seem contradictory in some areas. Time will resolve these debates. Any action you take as a Realtor®, association executive or other affiliated professional must be your own decision, based on your own unique market and skills.

Jerry Matthews, Chairman
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INDUSTRY TRENDS:

A SHIFTING KALEIDOSCOPE

The real estate industry is a shifting kaleidoscope of local, regional and national players who come together to assist the consumer in a real estate transaction. The broker, agent and firm are rapidly evolving in different directions. The very definition of the “business” is changing. Innovative thinking and evolutionary changes in the marketplace create both new challenges and opportunities for real estate professionals.

Here are some of today’s key trends:

- **The agent is the brokerage business.** Through increasing control of the core real estate brokerage activity, the agent has literally become the real estate brokerage business. There is no doubt that the agent controls all aspects of the transaction, including the relationship with the

consumer, and that is the key to the business. “This shift to the agent control of brokerage has tremendous impact on the power structure in the real estate business and organizations that serve it,” says a consultant.

- **Ancillary services are now core.** Many successful brokerages have expanded into mortgage, title, insurance and other homeownership services. With declining revenue from brokerage activities, these services provide new streams of revenue. In fact, these services are now a central part of the business and no longer seen as ancillary and can extend the relationship with the consumer far beyond the current real estate transaction. “We don’t consider ourselves as a real estate company any more; we consider ourselves as a home services company,” says a major broker. Firms now depend on these services to drive bottom-

line profits. “In the future, brokerage will become less important as a source of our profits,” says a consultant. “Earnings from other business units will bolster the profitability of the brokerage business.”

- **Brokers play a supportive role.** With agents playing the central role in the sales process, brokers are now playing a supportive role. Agents see the value of their broker as a provider of marketing, technology, training and risk management services, so that they can focus on selling homes and serving their clients. “I don’t have to pay attention to training my staff, getting the hours to renew my license, or paying attention to the new state regulations,” says one agent. “My broker makes sure I’m compliant.”

- **Agents are becoming shareholders.** Many brokers are inviting agents — especially their top

“The real estate process is no longer just a local transaction. We need to understand what parts are shifting to a national level and what are not.”
— A major broker

producers — to own an equity share in the company. That gives these agents a voice into brokerage decisions that affect their livelihood, and a stake in the success of the firm that goes beyond their own productivity. In other cases, top agents are asked to participate in the company's strategic and financial planning sessions, another step that blurs the traditional lines between brokers and agents.

• **Consolidation of firms.**

National companies are absorbing independent and mid-size local and regional firms, while entrepreneurs and “super-agents” spin off their own niche firms. Most professionals interviewed by the work group believe that consolidation will continue and reach the pivot point of driving local practices. “The national brands now have half the associates across the country,” says a consultant. “That means national companies can now make decisions that affect the local marketplace – for instance whether to opt out of IDX (Internet data exchange) systems.”

• **Control of the transaction process.** It is by no means clear that traditional brokers will control the “packaging” of real estate transactions, if and when that integration occurs. Lenders and title companies are well positioned to control the process – especially if it becomes extremely costly to develop an effective national transaction management platform. “Ultimately there has to be an easier, more efficient way

to do the homebuying process,” says a consultant. “The process today is still too difficult, cumbersome and uncertain for the buyer and seller. Whoever can solve that problem can make a lot of money.”

• **Loss of industry leaders.**

Many of the creative brokers who built successful local and regional firms have sold their businesses and retired. This “brain drain” of leaders who built the industry and supported its various organizations has accelerated a developing trend. “The leaders of the associations that make decisions that affect our business often are not market leaders. This is a mistake and a real danger,” says a large national broker. However, other participants disagree with that assessment, and point to instances of broker leadership in some places. “There are times when brokers have not staked out a leadership position due to a number of factors,” adds one participant.

• **Multiple-brand ownership.**

Consolidation is creating interesting situations. When one company owns multiple brands in the same market, the level of actual competition declines. The different brands could all be operating the same real estate model, just different names and nuances. “It could happen that one company could own all four corners on Main Street with four different stores,” says a broker, “and that would really change the market.”

• **Low-cost “freedom shops.”**

New brokerage companies structured so agents work from home are rapidly growing in some markets. These “freedom shops”

provide technology support and a brand name to home-based agents in return for a modest fee or commission split. This is not the same as referral offices. “RE/MAX is the high producing agent model, but now we’re seeing a low producing, low-cost, stripped-down offering,” says a consultant.

• **Value disconnect.** There is much concern about the real value of traditional relationships and transactions between brokers, agents, consumers, vendors, franchises, associations, and MLS services. Emerging models, technology and consumer demand have raised questions about the true economic value of every aspect of the transaction and every transaction player. The exercise of property data and other ownership rights of components that now have transaction value – or economic value – could change the distribution of revenues. “It’s time I got some of the revenue that my collection of listing data has created for the MLS”, says one broker.



BROKERAGE TRENDS:

A NEW DEFINITION OF THE BUSINESS

High agent splits, continuing downward pressure on commission structures, the cost of technology and demand for support services have eroded operating margins at many brokerage companies. As noted above, there is also a significant shift in the definition of the “business” of the firm as ancillary services become central to the company’s success. Here are some of the other steps brokers are taking to improve their short-term profitability, long-term viability and the business definition of their firms.

- **Imposing transaction fees.**

Many brokers are now charging a transaction fee of hundreds of dollars to buyers and sellers – income that goes straight to their bottom line. “For the first time in more than a decade, the pretax margin from the realty part of the brokerage business has edged up,” says

a consultant, “and this consumer fee had a great deal to do with that.”

- **Lowering agent commissions.**

Some brokerage companies are reducing agent commissions by using call center and online services, such as virtual office websites (VOWs) to produce prospective buyers. They do the “prospecting,” then turn over qualified leads to their agents for a fee or pay a smaller commission on that sale.

- **New limited-service subsidiaries.** To improve their revenue, some brokerages are offering limited-service subsidiaries in the same market as their full-service offices. “If agents are fully informed, they are okay with this concept,” says one such broker. “We’re trying to protect their full-service interests and full-service fee by giving the consumer an alternative. We tell the

client: ‘Here’s what you get for X and what you get for Y.’ We can’t give full service for a limited service fee.”

There are also looming challenges to real estate brokerage:

- **Aging of the brokerage owners.** Many firms today are run by owners in their 50s and 60s. Without a succession plan, they are likely candidates for acquisition in the next decade. “My big challenge is bringing new and younger talent into the business,” says one mid-sized broker. “The

“The traditional agent-broker model is almost economically unviable for the broker. The risk reward formula is out of kilter, since the broker gets too small a piece of the brokerage transaction.” — A broker

aging of ownership, management and key sales associates is really the unrecognized issue of our decade.” However, overall statistics indicate that younger agents continue to enter the profession, as the average age of agents and brokers appears to be stable.

• **Managing potential liability.**

As agents expand into related lines of business – from mortgage services to property management to residential development – brokers may be facing greater liability risks.

“If they don’t meet a broker’s high standards, they become a walking liability,” says one broker. “We have created policies on these types of issues to try to protect all of us, but it is a real concern.”

There is evidence that brokers will stiffen demands on performance that is related to risk management. In addition, a number of new risks

— such as mold litigation, terrorism attacks and changing insurance company policies — are putting increasing pressure on brokers’ errors and omissions (E & O) policy costs.

• **Company branding.** An important issue for many brokers is the increasing presence of agent branding. They hold to making the firm the brand name for consumers. “If we produce an image of the company with the consumer that is positive and supports the agent’s role, the firm can lead the brand without agent concern,” offers a large national broker. But other firms allow their agents to lead the branding.

• **Building intranets.** Brokers of all sizes are now delivering their internal support services via company intranets. This is cheaper and faster than paper documents, and leaves an audit trail.

“This is the major internal communication resource in our company,” says one broker. “We put contracts and forms, schedules, newsletters – almost everything – on our intranet.” The intranets also are moving extensive property data information within the company.

• **New sales training.** A changing business is driving the need for a different type of training. “Most people in the real estate business are order takers who need more sales training,” according to a Midwest broker. “They wait for the phone to ring, and then process that customer. We are looking at other changing industries and taking their basic sales courses and incorporating that into our training.”

• **Community partnerships.**

One of the newer services that brokers provide is building service-oriented or “fun” partnerships with community organizations. “We have a relationship with a professional sports team,” says one regional broker, “and we want to leverage that relationship with our associates – both on the business side and the personal side.”



AGENT TRENDS:

GAINING CONTROL OF THE BUSINESS

Real estate agents are tightening their grip on the basic real estate brokerage process. Successful agents are boosting their revenue by forming teams, using online technology, and creating additional revenue streams. They are continually striving for more and more control of their sales business, as well as the entire transaction.

Here are some of the big issues for agents:

- **Growth of agent teams.** One of the biggest changes on the agent side of the business is the tremendous growth of teams. Hiring personal assistants, marketing and technology specialists and licensed buyer agents can increase the productivity of top agents. If the firm does not support or accommodate the team concept, top agents will move.

- **Pricing pressures.** A growing percentage of consumers are asking agents to reduce their commissions. This has been sparked by awareness of discounted online and limited-service models, and remains a challenge for full-service agents. “So far I have been able to explain to customers why my commission rate is fair – so far,” says a top agent.

- **Agent branding.** The growth of agent teams is spurring a trend toward agent branding. For instance, many agents now want their names to be given the most prominent display on a newspaper ad or a for-sale sign. “I’ve never been one to hold back my agents from letting their entrepreneurial spirit shine through,” says a regional broker. “If you, as a company, do a good job in selling the agent on the benefits of your brand, they will see the benefit of

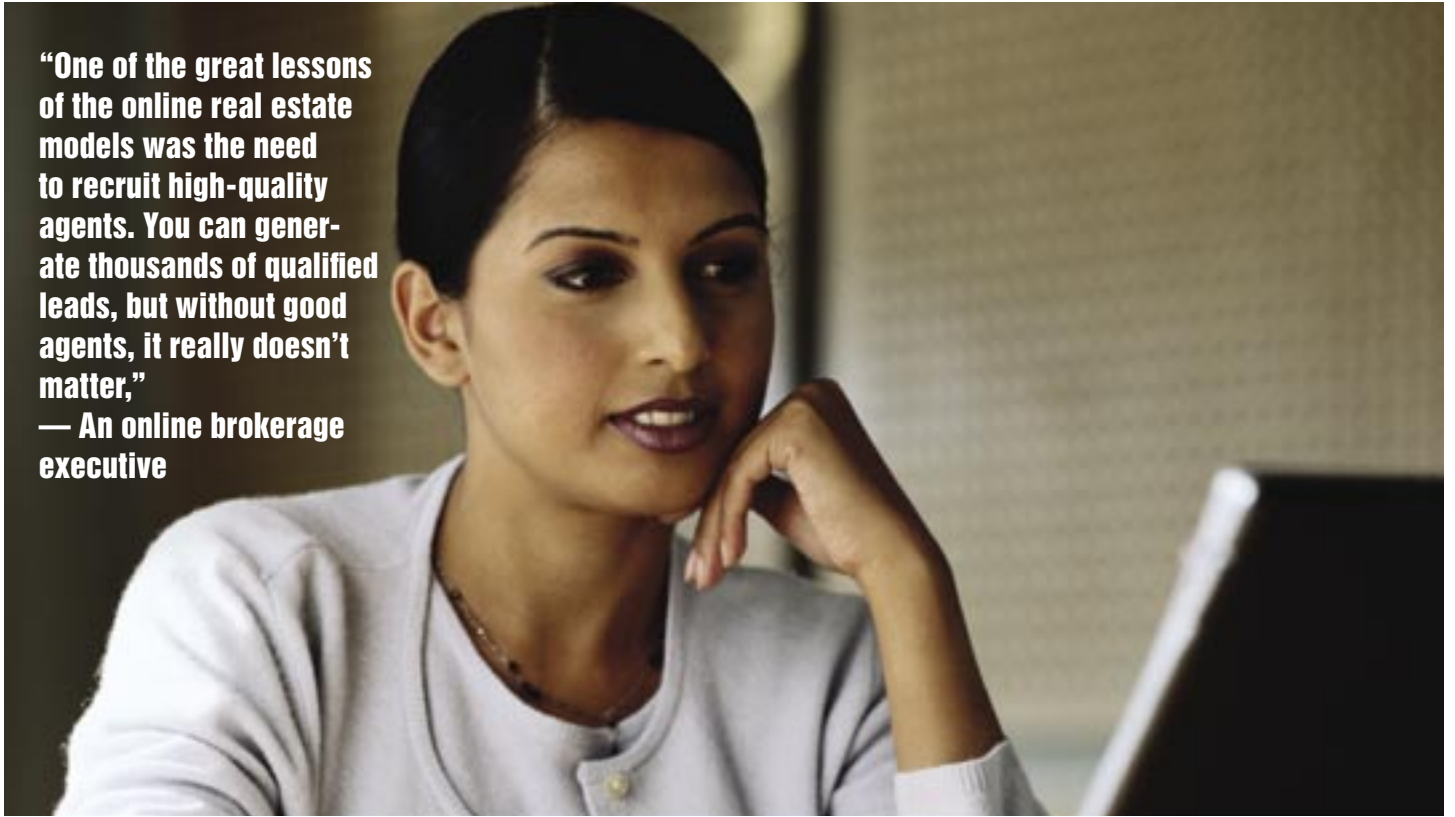
using that brand in their marketing and promotion.”

Many agents disagree, as they see their own name and reputation as the key to future business.

- **Related lines of business.** Agents, like brokerage firms, are looking at offering related services to buyers. “I want to offer everything under one roof to my buyers,” says one agent. “If they trust you, they’re happy to have you guide them through the whole process.”

“Nothing will take the place of actually looking at the homes.”
— A top agent

“One of the great lessons of the online real estate models was the need to recruit high-quality agents. You can generate thousands of qualified leads, but without good agents, it really doesn’t matter,”
— An online brokerage executive



• **Technology skill levels.** Real estate agents need to continually improve their online technology skills to keep up with clients. In some cases brokers or local and state associations have offered programs. “Even if you’re great at relationships, you have to be comfortable with technology because the consumer expects it,” says one agent.

• **Direct access to MLS data.** Some agents want direct access to MLS listings, rather than going through their brokers. As one agent says, “I’m doing more than my company is doing electronically, but I can’t access information unless it’s through my broker. That will have to change; I want to control the information going and coming, and I need to know the response to my technology investment.”

• **Controlling the “book of business.”** Veteran agents who are considering retirement are looking for ways to value their list of clients. At the appropriate time

and price, they may choose to sell that “book of business” to the broker in exchange for a continued annuity. In many cases, the agent will continue to keep the relationships and make referrals to the company.



THE 'NEW' CONSUMER:

A FORCE FOR CHANGE

Many of today's consumers are far more knowledgeable about the real estate market than in the past. They are comfortable using the Internet and other communications technology, and far less wedded to traditional brokerage customs and traditions. Low-cost Internet-based models and "blended" approaches that combine online and personal service have the potential to appeal to a growing segment of the market.

Other marketplace changes in the next few years are likely to be driven by the "new" consumer, who wants:

- **Convenience.** Buyers are looking for one Web site to search for comprehensive, accurate, up-to-date listings for the entire market. Brokerage firms, MLS services, national aggregators – whoever can deliver complete data to

a consumer – will have a clear advantage in the market. "As a consumer who has bought or sold homes, I want to see everything," says one consultant. "I'll still use an agent, but I want the information."

- **One-stop shop.** The drive for convenience also naturally leads to growing demand for an integrated transaction process with 'one-stop' providers delivering brokerage, mortgage, insurance and title services as well as non-transaction items relating to home ownership. This fits nicely with new areas of diversification from brokers.

"As agents and managers, we have to give the consumer what they're looking for," says one broker. "We have our own mortgage and title companies, and the revenue stream from them is moving to 50 percent or more of our total profitability. But it's

almost like wearing three hats and our challenge is melding it into one business."

- **Low-cost service.** Online brokerage models or low-service market discounters will put continuing pressure on broker and agent commissions. While fee-for-service models have not caught on, many sellers like the option of a flat-fee for online marketing services, and a reduced commission for in-person showings and other agent services.

"We're seeing more requests for reduction in commission from consumers, especially when they see flat-fee programs from online sources," says one consultant.

However, despite the pressure, many brokers have been able to maintain their current pricing structure and market share.

- **Technology, technology and more technology.** "You can either get into the game and

"It's the consumer who's really driving change in the real estate industry."

— An independent broker

use technology or it will be your demise,” says one broker. Brokers and agents must be able to deliver information to consumers, and respond quickly to their e-mail inquiries. The Internet puts a premium on speed in communication, which may be difficult for agents in the field. It also means that brokers must continue to invest in technology, adding services and features that meet the evolving needs of sellers and buyers.

- **High-level performance.**

Consumer demands for comprehensive information, immediate communication, and personal service are increasing rapidly – not just in real estate, but in all aspects of daily life. Several real estate consultants and other professionals say the industry is not keeping up with this demand for better performance. “Today’s consumers want you to anticipate their needs – that’s the only time they’re impressed,” says a top-producing agent.

- **Consistent brand experience.**

Consumers are also seeking a consistent high-quality brand experience in their personal lives. They want to know what to expect in terms of product, quality, effectiveness and cost — and that expected brand experience must be delivered every time.

The challenge for the real estate industry is creating and enforcing standards that promote a consistent brand experience with a work force that is predominately self-employed contractors. It appears that whoever delivers this brand experience – firm, agent or franchise is responsible to the consumer.

What’s changing in this equation?

- **Trust.** Will the ‘new’ consumer trust the agent, the broker or a national brand ‘one-stop’ service? The answer, to date, is far from clear. For instance, some consultants say agents’ personal relationships with clients will be more important than ever before. Others suggest national providers using advanced technology may challenge that agents’ traditional trust-building role. “The consumer today is as likely to trust technology as their real estate agent,” says an Internet-based broker. “That is a huge shift. To the extent that the transaction can be made more efficient, buyers will use technology, whether it comes from a local or national source.”

- **Internet presence.** A viable business site on the Internet has become a necessity for real estate professionals. A sophisticated Internet presence and the ability to understand ‘techno-speak’ is far more important to agents and firms now than even a few years ago. As one agent says, “The percentage of buyers bringing the home they found on the Internet to me has increased dramatically – especially with move-up buyers in the same community. They know where they want to live, but they still want my input on the rest of the transaction.” It is important to note that customer leads from the Internet are now second only to personal referrals.

- **Evolving Internet-based models.** Just because some of the new business models have failed is no reason to downplay the

potential challenge to traditional brokerage business. Second-generation models – such as Lending Tree and eBay – may need to be monitored for consumer acceptance and impact. One of the Internet’s success stories is eBay, which created a market for buyers and sellers within virtually any type of tangible product. “Auctions benefit sellers who want to create buzz and excitement about their property,” says an executive for an online company whose real estate auction services are currently structured as a marketing venue. But with success, the new generation Internet models could impact traditional brokerage services.

- **Community.** With the threat of terrorism, international turmoil and an uncertain economy, people are spending more time with family and friends, and focusing more on their local communities.

“Home” has increased in importance, along with factors like a shorter drive to work or a second home. Neighbors and the nature of a community are becoming more significant to buyers. Marketing themes may need to reflect this change in attitude. “The way society looks at home and community is changing, and we as an industry need to look at that,” says a broker.



TECHNOLOGY TRENDS:

A VORACIOUS APPETITE FOR DATA

Consumers, agents and brokers alike are demanding more and more data to make their personal and business decisions. To a large degree, technology is the force in satisfying the industry's overwhelming appetite for information at all levels.

For consumers, one of the real estate industry's greatest assets is the multiple listing service as a source of accurate, up-to-date information on local real estate markets. The ready availability of MLS data in a variety of forms of distribution provides a high level of comfort for buyers and sellers in terms of pricing a transaction.

However, it has not been easy to translate local MLS systems into effective online sources of data, especially on a regional or national level. Questions like who "owns" the data, who can display

that data, and how to display the data to consumers continue to be discussed throughout the industry. And the long-term impact of consumer technologies like Internet data exchange (IDX) and virtual office web sites (VOWs) remain uncertain.

The key issues:

- **Maturing of the Internet.** Originally just an information medium, the Internet in its high-growth years sparked a number of new online brokerage models. Today, consumer acceptance of those models has been limited to a smaller segment, largely "for sale by owner" sellers. However sites with listing and community information are growing in consumer acceptance. For full-service brokers and agents, the next challenge will be to integrate voice, text and data in an effective multi-media form of communication with clients. "It's really changing

from a one-dimensional service," says a consultant. "We will be able to send messages that go from speech to text and text to speech without anyone noticing the difference."

- **"Parochial" MLS attitudes.** As national players become more active in the real estate industry, the higher costs, duplication of services, and incompatible technologies associated with local MLS systems are becoming bigger points of contention. "When each association has its own MLS and data storage system, you have redundant costs

**"The modern buyer is ravenous for data. We need to keep giving them a better picture than they have today or someone else will."
— A consultant**

and inefficiencies throughout the system,” says an executive for a national real estate company. “MLS boards will have to take a stronger look at what will really serve the brokers in the marketplace.”

• **Enforcement of data policies.**

As MLS data becomes distributed to MLS participants, online aggregators and other companies, it becomes increasingly difficult to enforce data accuracy and integrity. This in turn could “water down” the traditional value of the MLS “brand” in the market. Policing data misuse and assuring accuracy will increase costs. And so we anticipate a potential struggle between data integrity, speed and cost.

• **Impact of VOWs.** The ability to register clients and begin a transaction process on-line through a VOW offers both opportunities and challenges for brokers. The release and subsequent use of the data can create unintended businesses that may actually harm the transaction or brokerage business. “We need to look closely at our policies on VOWs especially those that enable fee-based third parties that do not add value,” say several brokers.

• **Value of property data.** Brokers and agents are increasingly aware of the inherent economic value of the property data collected in the normal course of business. Data aggregators such as MLS and Internet portals will find new attitudes on any revenue created from data collected. This will change traditional relationships and economic use of the data.



CONCLUSION:

CHANGE IS RELENTLESS

Over the past few years, the nation’s brokerage community has done an admirable job of adapting to change. Many brokers have been able to recognize and respond to the evolving needs of agents and consumers, maintaining their share of the real estate market and expanding into new lines of business.

In addition, the fear of the unknown appears to have diminished for traditional brokers and agents. Perhaps it is the demise of some new Internet models or the continuing robust nature of the real estate business, but participants in the Strategic Issues Work Group expressed far less apprehension about the future than they did at the group’s previous session in spring 2001.

There is one primary conclusion from this report: Change is relentless and the velocity of change continues to increase. The brokerage community as it exists today, will be increasingly

pressed to keep pace. This is undoubtedly the biggest challenge facing traditional brokers and agents.

But change is not a force to be feared – or ignored. Change creates new opportunities for brokers and agents every day. Their ability to capitalize on those changes — as individuals, as teams and as companies — will determine the future of today’s real estate industry.