

REALTORS & Red Herrings

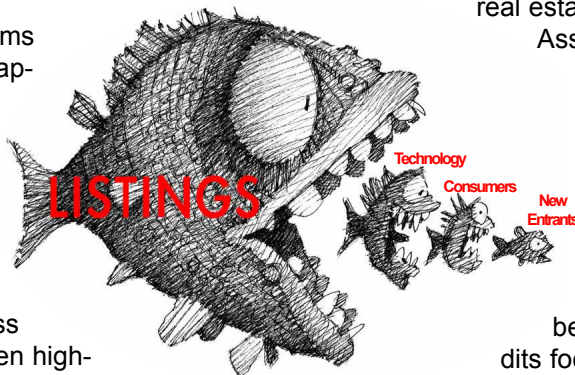
red herring (noun). Something that draws attention away from the central issue.

By Steve Kropper, Founder Domania • April 2003 • kropper@domania.com • 617-306-9312

I have been watching the residential brokerage industry for over ten years. In this time, I have seen many speakers pound the table and warn Realtors of one enemy after another, all red herrings. So, why are Realtors afraid of this mythical fish? The fish has many names: technology, consumers and new entrants. These are not the real problems facing the industry. These are red herrings that won't die, that persist for years stifling innovation meanwhile, the real estate side of major brokerages is barely profitable.

There are two real industry problems that desperately need creativity, capital and new entrants:

First, building broker value (and power) in the eyes of the agent through central sourcing and management of sales leads. Second, making the Internet a valuable channel for business through new software and business models that bridge the gap between high-volume, low-value Web leads, and the relocation department's requirement for low volume, high yield leads. Everything else is a red herring. So first let's know the enemy, the red herrings that persist.



Technology is the Enemy

What happened when Daniel Ellsberg, the Pentagon Papers and a copy machine were all in the same room? Leaks. Put technology near information and that information will always leak out all over. The same is true with MLS listings. The

introduction of the IBM Selectric typewriter was the first crack in the dam. As soon as listings were stored on a computer, *listings were sliding fast down the slippery slope to public accessibility.*

Today's debates over IDX and VOW are way too late. The horse is not only out of the barn, it has been out for a few years. The listing horse has been sold twice, re-branded and it is grazing in retirement in Kentucky. Control of listings is gone and that's a good thing for real estate brokers. At the recent Houston Association of Realtors SUCCESS conference, one speaker said, "I wish we could go back to the MLS books". In the back of the room, a prominent local broker said "Amen"! The red herring strikes again. Technology IS the enemy. It DOES erode control of information, but this erosion is inevitable and beyond your control. Don't let the pundits focus your spotlight on technology. It might be the problem, but you can't stop it. It is bigger than you. And me. And NAR. Have you looked outside our industry? You will see the same trends.

The Consumer is the Enemy

The Realtor IS still at the center of the transaction, but control is slipping and the "center" is on the move. The consumer is winning. Assertive, information-hungry consumers demand control in the form of direct, unfiltered access to all property details. If you deny that control and withhold information, then they will surf to another more cooperative broker as soon as

they can type in another URL. At a certain point, when the consumer is ready, the consumer will initiate an engagement with an agent. Then the Realtor takes over and begins the time-honored cycle of posing legitimate, reasonable questions to the consumer that raise their anxiety, and then sweeping in with answers to calm the worried home buyer or seller. Thus begins the highly evolved *cycle of dependency that makes real estate agents truly essential* in the home buying process. We consumers stumble through this transaction, too infrequently to be competent.

There are just enough years between transactions to forget the steps of the dance. That is why we welcome help.

Assertive consumers might be the enemy, but just like the advance of technology, aggressive consumers are here to stay. It is only the second inning of the consumer revolution in real estate, and brokers who provide the information tools that consumers demand will own that consumer. Why? Because everyone else wastes the consumers' time! Until they get seriously engaged with an agent, consumers have no loyalty and will surf across brokerage sites until they are satisfied (or exhausted). Growth-oriented brokers will give consumers access to rich information. But there is good news...and bad news.

Realtors are still in control of the END of the transaction. Mortgage brokers, mortgage lenders, title companies and ultimately every downstream vendor (flood, title, MI, inspection, appraisal) are dependent on the broker. FNIS is right on this target with their focus on the agent desktop, and tools that help manage the transaction. Each of these downstream players is dependent on the goodwill of the agent. Imagine if RESPA reform were to really happen. Imagine if Realtors could mine all the value from the lead they slaved to produce. Realtors could get rich on referrals to lenders (and a host of other vendors) without having to be in the lending business. However, it is just a dream. RESPA and assertive consumers are here to stay. The consumer may be the enemy, but you can't alter history, so get over it.

Let me introduce the last red herring, then I'll move on to some solutions to the industry's problems.

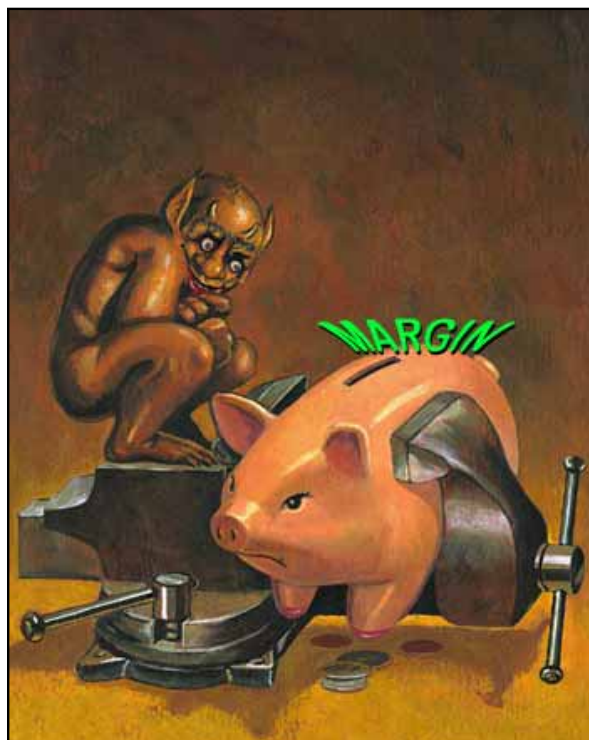
New Entrants are the Enemy

Do you remember HomeView? That was IBM's entry into real estate. Do you remember SureFind? That was Microsoft co-founder Paul Allen's entry into real estate. Both ventures are long forgotten. In a year, HomeAdvisor will also be history. Most new entrants thought conquering real estate would be easy. Where are they now? Long gone. Do you remember the "Lion over the Hill (Microsoft)?" This was the Red Herring of Red Herrings. It probably arrested progress in the brokerage industry more than the recession of the early 90s.



Did Microsoft HomeAdvisor change the structure of our industry? No! Sure HomeAdvisor's payments to your local MLS probably tempered dues increases a bit, but the much feared entry of HomeAdvisor barely impacted the industry and did not meet the success of Expedia travel, Microsoft's other disintermediation venture. One win, one loss.

Expedia's success and HomeAdvisor's floundering are not a bad investing score for new media. Yes, Microsoft DID disingenuously believe that better information technology would make agents obsolete and put HomeAdvisor at the center of the transaction. But it did not happen. *New entrants have had little or no impact on the real estate market.* Mainly Microsoft's entry proved beyond a reasonable doubt that control of the listings is NOT the key to agent job security.



While a common property repository controlled by the industry like Realtor.com might be important, hiding the listing data does not protect Realtors (see epilogue at the end of this paper, **Exposure Good, Monopoly**

Bad: The Story of Realtor.com). Control of the MLS is NOT the key industry franchise. The key asset is the ability to sell homes. Until Microsoft or eBay figures out how to sell homes on the Web (in fifty years, perhaps) the Realtor's position in facilitating a sale will be secure.

Like technology and the consumer, a focus on new entrants as the enemy diverts attention from the key industry concerns. Beware the alarmist who points to new entrants as the threat to watch.

The Bank Red Herring

The current “new entrant” red herring is the mortgage industry’s “threat” to enter brokerage. Real estate broker opposition baffles me. First, are there no brokers who want to sell their companies to a bank? Bank entry could mean liquidity, as it increases the number of prospective buyers for brokerages. Wouldn’t bank entry mean more buyers for brokerages when it is time to sell? Also, real estate is a hard business. If lenders want to buy their way in to this revelation, let’s let them. It will be harder than they think.

Now that we have identified who the enemies are NOT, let’s address the most pressing problem in residential brokerage today

Broker Agent Instability

I see only one critical problem (besides E&O insurance and mold) that warrants attention by the residential brokerage community. That is the *failure of brokers and agents to develop a stable relationship*, based on a mutual sense of value. Brokers’ biggest challenge is to recruit, retain, and be valuable to the independent-minded agents who occupy their desks. Brokers struggle to create and deliver value to their agents that will bind them to the office. Agents look for reasons to be loyal, and to invest in the broker. Dissatisfied, they instead focus on building their own personal brand. Amid a sea of red herrings, the broker agent relationship reminds me of the admonition from the cartoon Pogo: “We have met the enemy and he is us”.

Not surprisingly, I see the Internet as the salvation of the industry, and the brokers’ position in particular. The Internet generates leads of prospective buyers and sellers. These leads are best handled in a centralized, carefully managed “manufacturing machine” by salaried staff members. Sounds like the relocation department to me. The decentralized agent is a poor starting point for Web leads. The agent is effective at the local level doing one-to-one networking that drives most transaction sides today. But the new media of Yahoo Real Estate, HomeAdvisor, Realtor.com, Realestate.com etc. are centralized lead generators. They need a broker-like structure to flow leads

through. If leads are properly managed, the broker is in the power seat, and the agents will be grateful to get a flow of qualified leads from the broker. “But wait,” you say. I have tried Internet leads, and they are garbage.

You are right. The “product” called Web based real estate lead generation was released to the market before it was ready. I’ll get to “garbage” leads in a moment.



Relocation Department: Salvation of the Web

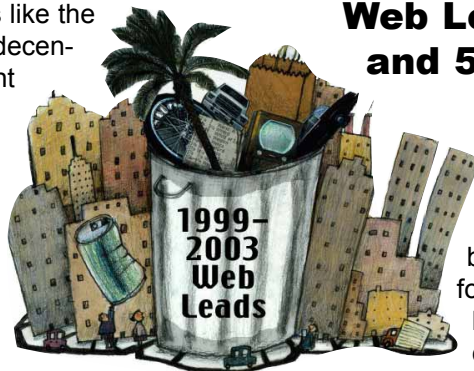
Today, the real estate business model depends on mostly a “hot” referral flow. By “hot”, I mean that most prospects are real customers...eventually. The Internet typically generates a high volume of low yield, “cold” leads that have to be incubated like an egg in a hen house. The egg (and the lead) must be kept warm, turned occasionally, and protected until it is ready to mature. And proper scrutiny of some eggs (and Web leads) reveals that most are duds - they will never mature. They are destined for the breakfast table, not the hen house.

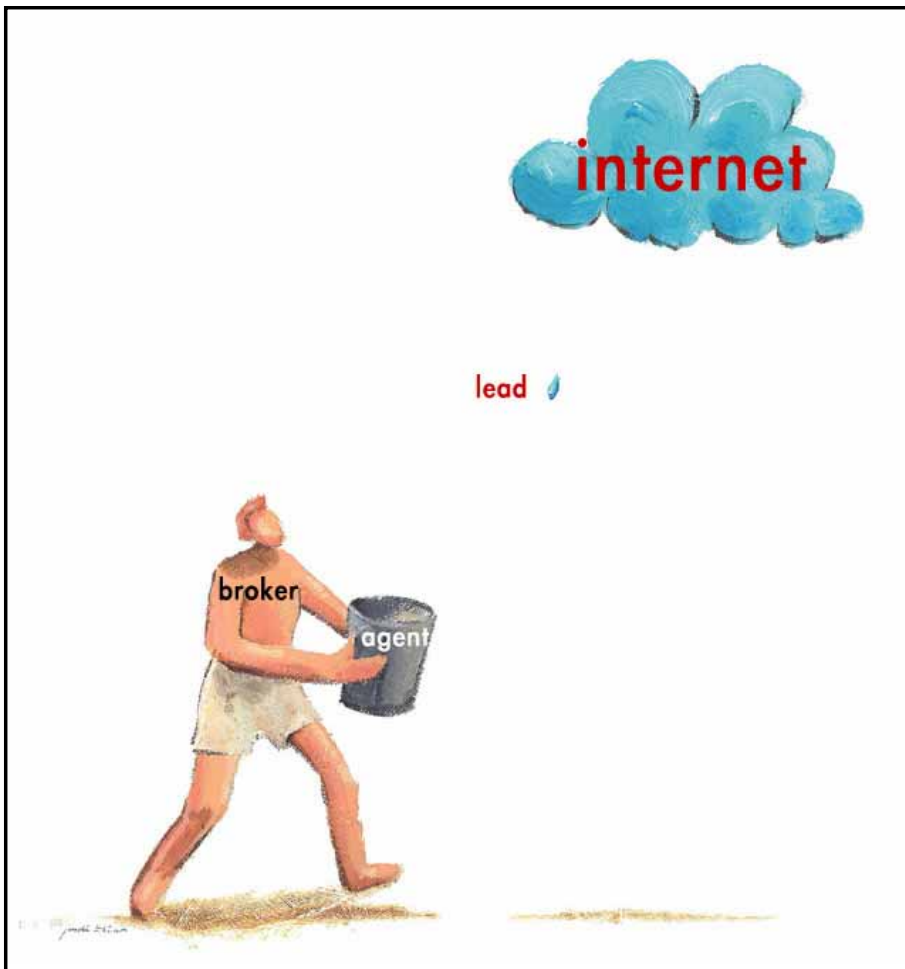
The only place in the residential brokerage industry that is even close to having these lead management capabilities is the relocation department. The *relocation department most closely resembles what I call the new well-oiled “machines”* of the real estate business such as ZipRealty and eRealty. The elements for success are salaried staff, good contact management software, and facilities for incubating and filtering leads BEFORE placing them in the hands of the right kind of agent.

If brokers (and Web sites) can make Internet lead generation a success, it can *restore broker control* and get us back to the symbiotic relationship that used to bind brokers and agents. But let’s get back to the critical 5% goal.

Web Leads and 5% Business Models

Remember years ago if you wanted to buy granola, organic milk or free-range chickens and you had to go to a natural foods store? You don’t remember? Well, take my word for it. Today, the food coops and natural foods stores are mostly out of business. They did their job introducing us to a more healthy palate. Now the





Sales leads that come right off the Web are of little value to brokers or agents. They are too dilute to be useful, like maple sap before it is boiled down to syrup. The reason is that most Web surfers are in the early stage of their home search. Those early prospects require months of incubation and hand-holding before they convert to a real “warm” prospect. The quality of leads from Yahoo, HomeAdvisor or Realtor.com has been so poor as to sour most of the real estate profession on the notion of Web-based leads. Do you buy leads off the Internet today? Probably not. Each of these on-line players brought out lead generation products too early, without understanding how the real estate business works, and most important without understanding what yield or conversion rate was required by the industry. The answer is 5% - let me explain.

Care and Feeding of Internet Leads

The Web has failed as a real estate lead generating tool thus far because one in a thousand users from a Web site like Yahoo real estate becomes a closed sale. One in a thousand! Agents will die of exhaustion before they make a sale at that rate. Agents need one in twenty (5%) leads to turn into a sale for the entrepreneurial agent model to work. So suppose that there were marketing software tools upstream of the agent that could *take a “raw” lead, do triage* to see if the lead was a) “hot” enough to warrant immediate live call back by an agent to a “hot prospect” or b) required outreach and incubation by a telesales rep in the relocation call center, or c) was a tire kicker who might never become a customer, but might warrant a low cost retention campaign (such as a maintenance dose of monthly comps via email in your brokerage’s brand name...available from my firm, Domania - pardon the sales pitch).

Suppose the leads could be triaged into hot and cold. And segmented further, by first time buyer or move-up homebuyer. And even further segmented by the target home price, location and personality of the buyer or seller. Suppose there were tools that made it so Internet leads converted to real closed sales at the same 5% rate as “off-line” referral leads. *Developing these filtering tools, integrating them with the relocation department and fine tuning how agents handle these leads is critical to making the Internet useful to the industry and to saving the broker-agent relationship.*

mainstream grocery stores carry a full line of hippie food. Food coops became superfluous when the mainstream grocers poached their best features.

Likewise, the innovations pioneered by the four current challengers to the mainstream are likely to be absorbed into the brokerage mainstream. ZipRealty, eRealty, LendingTree real estate and Homegain are developing models that can make Web sourced leads valuable. Some of the innovators will be bought, some will go bust, but mostly all the new ideas that they refine into sound profitable, consumer-pleasing business practices will be *adopted by the big brokers.* Where will these practices be integrated at the big brokers? Watch the relocation department for the first signs.

Years ago, Steve Murray and I pitched Long and Foster on delivering leads into their relocation department. The discussion went nowhere. Management understandably felt that agents would revolt if the relocation department started sourcing leads that were mostly local moves, rather than just true long-distance “relocation” prospects. Agents (and some large brokerages) felt that local leads would end up in their hands anyway without our help, and agents felt that any involvement by the relocation group was simply adding a tax to their commission. Fortunately for both brokers and agents, that concern has passed. The relocation department is best suited to handle Internet leads. Here’s why.

Domania has developed these triage, segmentation and incubation tools for the mortgage business, and our clients include top players like Chase and CitiMortgage. The same knowledge base is used for the services we provide to ZipRealty. Integrating Domania's technology into brokerage will not be easy. No venture has succeeded at generating real estate leads. No one, not Realtor.com, HomeAdvisor, Yahoo or the others has developed a model that is profitable, and delivers real value to brokers. The key is to develop business practices, marketing strategies and software tools that restore the broker's position with accountable lead generation tools for the residential brokerage community

In Closing

Those who are wary of consumers, new entrants and technology are looking for the wrong threats. The real threats are how to tie agents to brokers. And the solution may lie in the sales leads

that the Web can deliver to a central relocation department. Some real estate players view the Internet as a threat to the industry, and one that has passed like a storm. It may be the salvation of the industry.

Most social and business change happens slower than expected, but in the end, the impact is much greater than anticipated.

When you are surrounded by change it is hard to see it. After all, the Earth that we stand on moves at a bit less than 1,000 miles per hour, but it feels like we are standing still.

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Exposure Good, Monopoly Bad: The Story of Realtor.com

I started watching the residential brokerage sector in 1992. My real trial by fire was being involved with Microsoft's designated third party vendor in the listing market, called RealDirect. Over the course of the NAR annual convention in Atlanta in November of 1995, this threat of competition forced RIN (the Realtor Information Network, Realtor.com's predecessor) to drop its fees from \$15 per month per listing, to \$1 and finally to 50¢.

At the time, I was new to real estate, but the experience persuaded me that on-line ventures that used listings as "bait" to attract buyers and sellers were simply not viable. They were too vulnerable to internal dissension in the professional real estate community. The listings were so encumbered with display restric-

tions that the sites could not deliver value to Realtors (prospective customers, especially for listings) never mind make a profit selling leads to lenders, title companies, utilities and the score of downstream vendors hungry for pre-mover and new homeowner leads. The agents' perspective that they "owned" the listings, while true seemed likely to torpedo any solution to the industry's problem of high print advertising costs, especially for brokers who suffered under the ad rates in one-newspaper towns. I wonder if the circumstances have changed today?

And what was the critics' solution to the lack of effective competition to newspapers? It was to foster another monopoly, Realtor.com, that "neutered monopoly media" of the real estate business. With respect to the display of for sale listings on the Web, it always seemed pecu-

liar to me that that while brokers would jump at a newspaper's offer of free open house listings for example, somehow they expected to get paid to release their listings to the Internet.

Brokers suffering under the burden of high ad rates in one-newspaper towns were persuaded to circle the wagons, and tried to position Realtor.com similarly as a monopoly on the Internet. The industry would jump at free open house listings, but go to court to prevent free display of their listings on the Web. This still seems odd to me, and it is playing itself out again in the current IDX and VOW debates. Until these issues get resolved, the listing space seems like a minefield that is dangerous to all players, insiders and new entrants. And who is hurt by the lack of media choices? Brokers and agents. □