

REAL ESTATE CROWDFUNDING

ALTERNATIVE FINANCE SECTOR REPORT

PUBLISHED

October 2014

AUTHOR

Samantha Goins

COMMISSIONED BY



Rationale for the Report

Real estate is one of the largest and best understood asset classes in existence. The global real estate market is worth over \$19 trillion and investors are familiar with the concept of buying, owning and letting property. From an investment point of view it has been one asset class that has been dominated by wealthy investors. High minimum investments, high transaction costs, restrictive regulatory regimes and ongoing operating costs all make it difficult for ordinary retail investors to directly access real estate investment opportunities.

However, crowdfunding could open up the real estate market to a much wider range of investors. Crowdfunding simply involves the pooling of funds from a number of investors (the "crowd") to fund a single project – a project could be a new business, a new product or a new real estate development.

With low entry levels, easy to use on-line functionality and its status as an alternative to mainstream financial institutions, crowdfunding has proven to be accessible and popular with early adopter investors. The market is expanding quickly, with over \$5.1bn raised through crowdfunding sites globally in 2013¹. The idea has already begun to spread into the real estate sector, allowing access to property in ways never seen before.

This report will be of interest to sophisticated investors, financial advisers, agents and intermediaries who invest in or are active in real estate. The content is balanced and impartial and the intention is to educate the reader on the risks and benefits of investing in real estate via crowdfunding platforms.

The contents will give readers background on real estate investment and how it works in the context of crowdfunding, take a look at the established platforms and review some of the more popular investment locations. The risks that investors must be conscious of in the market are looked at in context together with the different ways they can be mitigated and there is also primary analysis on the latest activity in the market, the type of opportunities available and the different options investors have if they want to participate.

The overall aim is to provide readers with the knowledge they need to make an informed decision about investing in real estate via crowdfunding platforms. This includes how to access the market, the level of returns they can expect, the risks they need to consider; the pitfalls they should avoid and where to go for more information.

1 - <http://research.crowdsourcing.org/2013cf-crowdfunding-industry-report>

CONTACT US:

+44 (0) 203 375 1700
enquiries@intelligent-partnership.com
www.intelligent-partnership.com

INTERACT WITH US:



REAL ESTATE CROWDFUNDING

ALTERNATIVE FINANCE SECTOR REPORT

Introduction to Alternative Finance and Crowdfunding

Alternative Finance is an umbrella term for various new on-line platforms that act as intermediaries between retail investors and borrowers/fundraisers. Alternative Finance activities include peer-to-peer lending, peer-to-business lending, invoice financing and equity crowdfunding. In the UK, the alternative finance market is predicted to raise £1.6bn² in 2014.

Equity crowdfunding consists of raising funds by collecting small contributions from a large pool of investors in exchange for a share of the ownership of the business or a share of the profits of the proposed project.

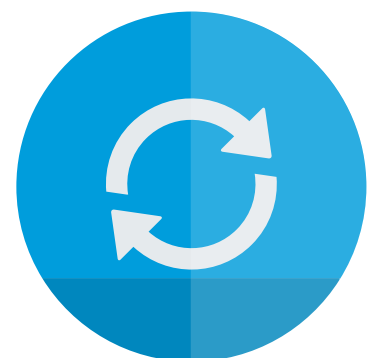
The platforms fulfil the role of an intermediary by matching borrowers and investors. This work would traditionally have been done by a long chain of intermediaries - investors would be recommended to purchase shares in a

venture capital fund which would invest in these kinds of opportunities. By reducing the number of intermediaries involved and utilising online technology the platforms can provide the same service at a much lower cost to both parties - borrowers and investors. In addition, the lower costs mean that entry levels can be set much lower - some are as low as £5.

Interestingly, although modern day crowdfunding is very much hi-tech, the concept of crowdfunding has a long history. A number of medieval cathedrals were built using many small donations collected from local populations; and the plinth that the Statue of Liberty stands on was built using funds raised by Joseph Pulitzer following a successful newspaper campaign. The first successful online crowdfunding project launched in 1997 when British rock group, Marillion, funded a tour by raising US\$60,000 in donations from fans³. The concept is not new, but

the global reach and social nature of the online community has brought it to prominence.

Since the early days, the crowdfunding market has changed drastically. The 2008 financial crisis coupled with the growth of the internet really kick-started demand for crowdfunding. On the one hand, businesses and entrepreneurs were suddenly unable to access traditional sources of funding as banks stopped lending. On the other hand savers and investors disappointed with stock market volatility and low interest rates were looking for new, additional and diverse sources of return. Both groups were brought together by crowdfunding platforms. This led to exponential growth - in 2011 \$1.5bn was raised globally on crowdfunding platforms, \$2.7 billion in 2012 and an estimated \$5.1bn in 2013⁴.

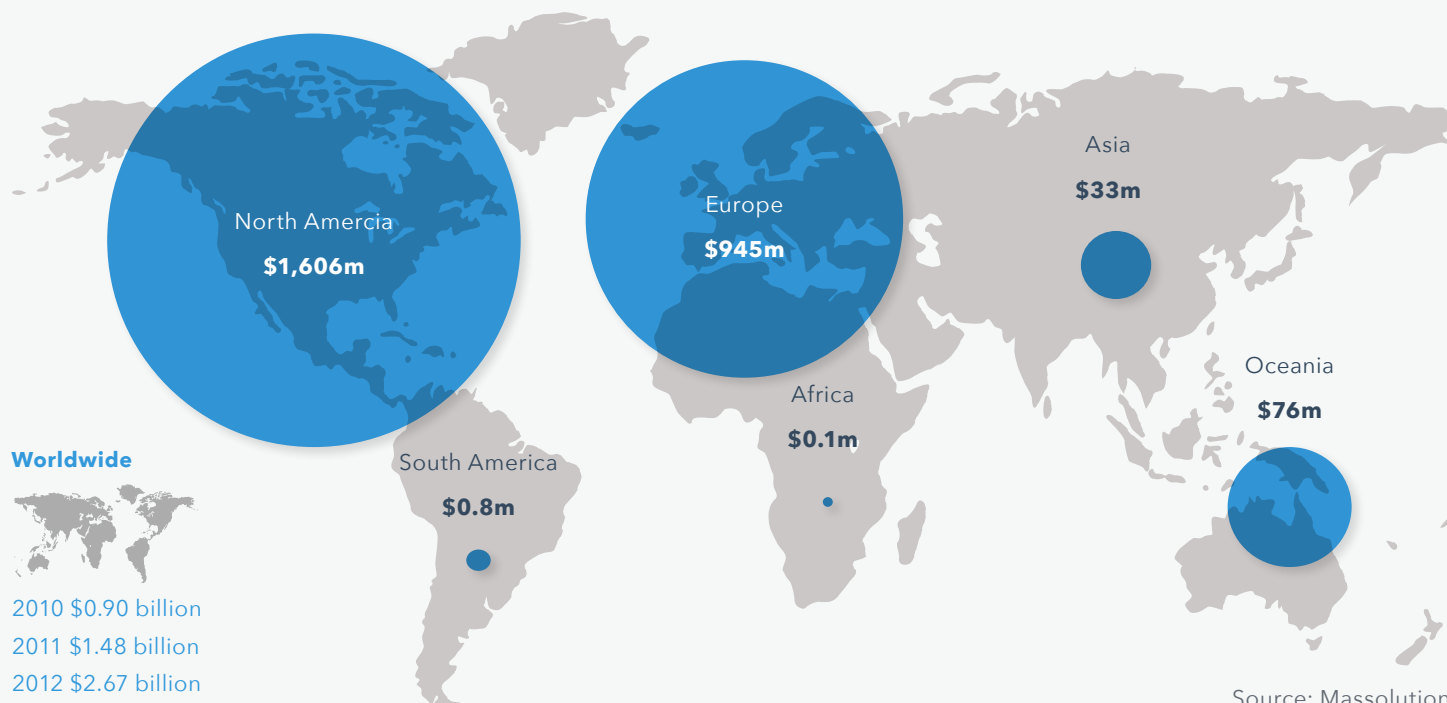


2 - The UK Alternative Finance Benchmarking Report

3 - <http://www.fundable.com/crowdfunding101/history-of-crowdfunding>

4 - <http://research.crowdsourcing.org/2013cf-crowdfunding-industry-report>

Global Crowdfunding Volume (2012)



Real Estate

Real estate is one of the largest, most established and best understood asset classes. An allocation to real estate as part of a well-diversified investment portfolio has many benefits: capital preservation; capital growth; regular rental income; diversification and a hedge against inflation.

There are two main conventional options for ordinary retail investors considering real estate. Direct property investments

give pure exposure to a specific project and investing directly should provide investors with the highest levels of control and transparency. Successful direct investments also have the potential for the highest returns. However, direct investments often require a large amount of capital to invest; transaction and operating costs can be high; there is no diversification to mitigate risks and some developments (particularly those that are off plan) are often high risk.

Real Estate Investment Trusts (REITs) offer a more accessible way to invest in property, with lower minimum investment amounts and risk spread across multiple properties. But investors will have little control over what properties are bought and sold, there can be a lack of transparency about underlying assets, fund management costs can be high and potential returns are much lower.

Direct Real Estate Investment Options

	Low Minimum Investment	Low Transactions Costs	Ability to Easily Diversify	Transparent Investment	Control of Investment
Directly Held Real Estate				X	X
REITS	X	X	X		
Real Estate Crowdfunding	X	X	X	X	X

REAL ESTATE CROWDFUNDING

ALTERNATIVE FINANCE SECTOR REPORT

Benefits of Real Estate Crowdfunding for Investors

Real estate crowdfunding provides investors with some of the benefits of both direct and REIT investments. The first platform dedicated to real estate was launched in 2010 and many new sites have entered the market each year since.

The concept is quite simple: platform members can browse through real estate investment offerings online to find opportunities where the location, property type, entry level, estimated returns and structure (debt, equity or co-invest) meet their investment criteria. They then invest an amount they are comfortable with, which is then held by the platform until the fundraising target is achieved. At this point, legal documents are drawn up and their investment, along with everyone else who has invested, is made available to the borrower.

Investors can either purchase equity, debt (through the funding of a loan) or syndicate (co-investment) style investments. Whether the investment is in debt, equity or direct ownership, these platforms allow investors to directly access to the performance of underlying real estate assets.

In short, this means that investors can take advantage of the low entry levels and easy investment process to achieve a high level of diversification and minimise their risk, whilst at the same time retaining control and visibility of their money and investing directly without incurring the charges associated with fund based investing. REITs typically hold 40 to 60

properties but often only invest in one sector (residential, commercial etc.), and are often criticised for having a lack of transparency when it comes to their activities. Crowdfunding gives investors far more control and the ability to pick and choose investments across various locations and sectors. Combined with lower minimum investment and transaction costs, this makes it easy to create a balanced and diversified real estate portfolio.

Real estate crowdfunding also offers some interesting short-term investment opportunities. Each investment is different and timing can range from one month to several years. Investors can choose a mixture of long and short-term opportunities to meet their needs – providing short-term income and longer-term capital growth

Benefits of Crowdfunding for Real Estate Developers

Traditional funding for developers can be costly, time consuming and limited to lending institutions such as banks or hedge funds. These lenders impose tight restrictions on borrowers, such as strict scrutiny of plans and tight deadlines to adhere to. Once they are able to access the funds, there are expensive transaction, legal and administration fees as well as time consuming paper work and regulations to follow. Since the 2008 financial crisis these institutions have tightened their lending criteria, restricting this source of funding. Crowdfunding offers developers cheaper, faster and easier access to capital.

A wider audience of investors allows developers to easily raise financing for projects. One of the largest platforms in the US, Fundrise, has 22,721 members⁵. Even non-real estate dedicated platforms are realising the opportunities for developers and investors. For example Angels Den, who are already an established equity crowdfunding platform have entered the property market utilising their platform and database of over registered investors at the time of writing this report (June 2014). 6,000 investors⁶.

The internet gives investors access to their investments 24 hours a day with everything happening live. Equity-based crowdfunding opportunities take on average 8.2 weeks from the investment first being launched on the platform to completion, and loan-based crowdfunding takes just 4.8 weeks on average⁷. Some platforms even boast funding projects in under a day!

The cost of raising money through a platform can also be significantly lower. The typical crowdfunding platform charges an initial fee for listing the project and possible administration fees to conduct their own due diligence. One platform, Real Crowd, charges borrowers a flat fee to gain access to investors and their 'Transactions Management Solution' as well as a monthly fee for their 'Investor Management Solution'⁸. As platforms already have an established investor base, there is less work spent on investor management which saves borrowers time and money.

Platform Locations

To date the majority of real estate crowdfunding investment has occurred in the US and UK where there are several established platforms operating such as Fundrise, Realty Mogul, Assetz Capital and iFunding. Other crowdfunding platforms in the UK are expanding their investment offerings to include real estate.

"There is a missing link as banks have pulled out of mezzanine funding and now leaves the door open for HNW individuals to fill the gap. We are speaking to a number of UK property developers who are very keen to open up this form of equity crowdfunding system."
Gary Stern, Angels Den

These platforms focus on investments located in specific areas in order to capture regional benefits leveraging their previous experience in the region and their relationships with local developers and investment providers. The Asian market is well suited to this new avenue for investment as the real estate market is buoyant, entry levels are high and investors are looking for new ways to access the sector.

5 - <https://fundrise.com/>

6 - <http://www.angelsden.com/>

7 - <http://www.crowdfunding.nl/wp-content/uploads/2012/05/92834651-Massolution-abridged-Crowd-Funding-Industry-Report1.pdf>

8 - <https://www.realcrowd.com/operator/landing>

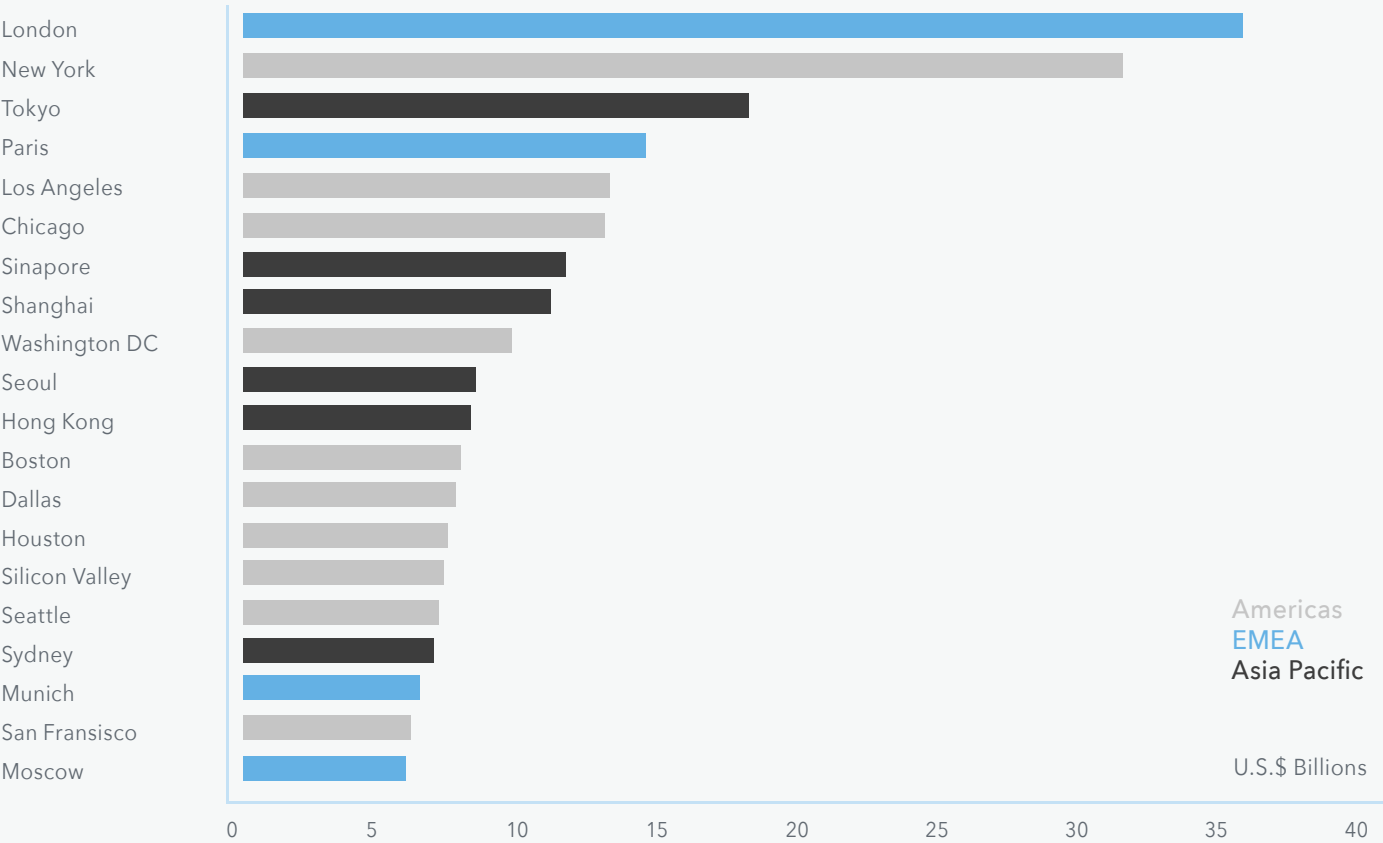
Investment Case & Risks of Real Estate

The real estate market offers a very wide range of options. Properties are located all over the world covering mainstream commercial and residential sectors and more esoteric opportunities such as car parks, care homes and student accommodation. Of course, the location, property type and the stage of development all impact the risks and returns for investors. This section looks at the investment case for real estate, considers the different types of opportunities available and the advantages that crowdfunding has for both investors and developers.

Commercial Property

Commercial property includes retail, office and industrial space. The sector took a big hit during the 2008 financial crisis but confidence is beginning to grow in several cities across the world. The chart below shows the top 20 cities for direct commercial property investment during 2013.

Direct Commercial Real Estate Investment - Top 20 Cities in 2013



Source: Jones LAng LaSalle, January 2014

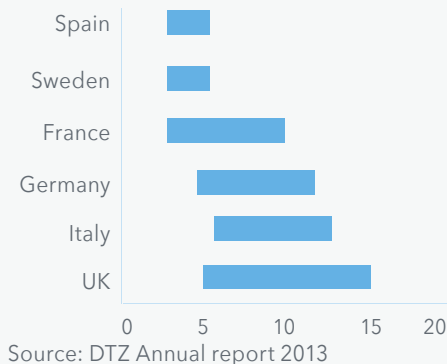
Commercial property has a wide range of investment benefits. It can provide steady annual returns from rental income secured on long-term contracts and capital growth at least in line with,

and often above inflation. Commercial property is also a source of portfolio diversification as it is less volatile than mainstream assets such as equities and bonds. Returns from commercial property

are relatively strong and investment interest is now improving across the globe. Management fees are a big consideration, it is important to have an experienced

management team in place to handle the day-to-day operations and this can come at a high cost. The right management company can be central to the success of a property. Commercial properties are large investments and are often valued according to their rental yield. Therefore it is important to have secure long-term tenants in place, particularly when looking to sell. Long-term rental contracts often include break clauses and upward only rent rises linked to inflation, which can help to provide inflation proof returns. In comparison to other European countries, the UK has some of the most attractive lease terms available, typically ranging from 5 to 15 years ⁹.

Typical Lease Lengths by Country

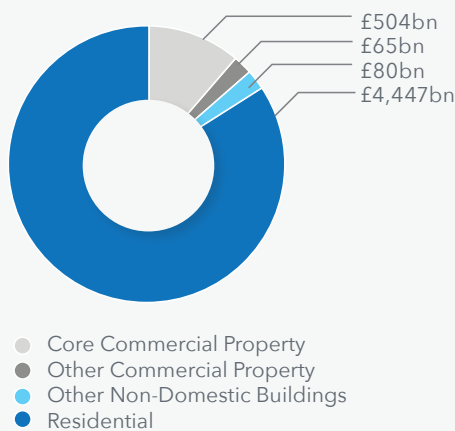


Residential Property

Residential property primarily covers buy-to-let style investments and now more commonly city centre apartment blocks and holiday lettings. Long-term buy-to-let investments can provide stable returns as rents historically keep pace with wage increases and inflation rates, as long as the property remains tenanted. In 2013, UK real estate was worth over £5,096 billion, with residential property comprising over 85% of that total.¹⁰ Residential property is uncorrelated to mainstream investments as rents tend to hold up during periods of economic distress, so again this can provide diversification within a balanced investment portfolio.

Residential property is less exposed to the business cycle than commercial property but has higher management requirements including regular rent collection, health and safety requirements, general maintenance and often a higher turnover of tenants. An experienced management company can take care of these duties for a percentage of rental income, which will impact profits.

UK Property Values (2013)



Overseas residential property investments can be higher risk as investors will typically have less understanding of the local market, so proper due diligence here is crucial. Companies such as Savills and Knight Frank operate on a global scale and can provide research, market updates and assistance for key locations all over.

Off-Plan Investments

Off-plan refers to buying a property before it is built. Properties are often sold at a pre-development stage as this helps developers to secure the funding needed to start the project. Prices are usually greatly reduced but for obvious reasons the risks are much higher - investors are exposed to all of the potential delays and risks that go with a new build - and it is often seen as highly speculative. However there is the possibility of much higher returns. Once the property is built investors can sell or lease it out for a higher profit. In certain locations returns can reach 25-30% per year.¹¹

Off-plan is the riskiest way to invest in real estate and can include a large amount of speculation. Several problems can arise before the building is completed. Delays can occur from the outset: building permission may not have been granted or environmental issues could halt the build and push up costs and result in delays. The developer could run out of funds and be unable to finish the property, or they could run over time which again will result in further costs. This could make it very hard for the investor to exit and mean they have to hold on to their investment for much longer than originally anticipated.

If the project fails completely investors could lose all of their investment, depending on what assets or property the developer owns as recourse.

Another consideration is the supply of properties in the local market. It may take several years to complete a property and the market could change dramatically over this timeframe.

Liquidity is very important, as it is very hard to find buyers for a property which isn't complete or which has run into trouble. Investors have little control over the building works or completion date - they are often solely reliant on the developer. Funds are released to the developer once specific build stages have been met, but if the project is over budget, they may require more capital to move to the next stage.

Redeveloping Built Property

A property that is already built and only in need of refurbishing or re-purposing is usually a much lower risk proposition. Some investment properties will already have sitting occupants producing a steady income. Returns will often be easier to forecast and more predictable, but are likely to be lower than off plan properties. However the initial capital outlay is much higher, especially for established properties with a predictable revenue stream, reducing the opportunity for stellar returns.

Properties that have already been built are likely to be the least risky as regards to building stage, although this can vary dramatically depending on the extent of the work required. Redevelopment projects could require a large capital input, planning permission and specialist skills, particularly if structural work is required. This will be inherently more risky than a property that already has sitting tenants or that only needs basic general maintenance. Of course the scale of redevelopment will impact the potential increase in value. Liquidity must still be considered, alongside the timeframe for any maintenance or development, the performance of the local market and transaction costs.

Redevelopment properties are often shorter term investments which look to add a large amount of value to the property in order to sell it on at a profit. Examples include splitting a large property into flats or modernising a property in order to add value.

⁹ - http://www.henderson.com/sites/henderson/uk_property/getdoc.aspx?ID=20150

¹⁰ - http://www.bpf.org.uk/en/files/reita_files/property_data/BPF_Property_Data_booklet_2013_spreads_web.pdf

¹¹ - <http://www.propertyshowrooms.com/guide/buying-off-plan-guide.asp>

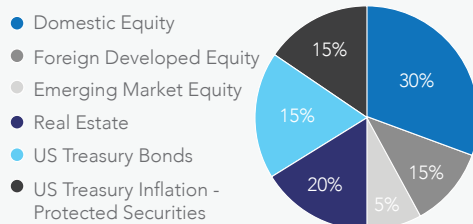
REAL ESTATE CROWDFUNDING

ALTERNATIVE FINANCE SECTOR REPORT

Diversification Benefits of Real Estate

Modern portfolio theory tells us that to decrease risk investment should spread across several uncorrelated assets. Global mainstream financial markets are becoming increasingly correlated and effective diversification is difficult to achieve. Real estate is not entirely removed from the financial markets, especially in periods of austerity or recession, but can provide a number of diversification qualities. Prices and occupancy rates do fall and experience periods of volatility, however property is a physical asset and a long-term store of wealth. The recommended allocation to real estate for an equity-oriented portfolio is 20%¹².

David Swensen Asset Allocation Model



In addition, real estate has also traditionally been a very good hedge against inflation. It can benefit from capital growth and regular income with returns often outperforming inflation, providing a real return on investment.

Risks Unique to Crowdfunding

The risks to consider with crowdfunding include the total loss of investment, lack of regulation and liquidity.

Many countries are struggling to create regulation and policy changes fast enough to accommodate the evolving world of alternative finance. The US and UK have both created new regulation with the objectives of better protecting consumers without hindering deal flow and have both restricted investment for

ordinary retail investors who do not have a high capacity for loss. Where there are no regulations in place, consumers should be wary of poorly structured platforms that do not segregate client money, do not have any capital adequacy requirements or do not have business continuity plans in place if the platform goes out of business.

Although some platforms offer a provision fund if the borrower defaults and doesn't repay their loan, many still do not. In the unfortunate event of a complete company failure the possibility of zero returns is very real. Some investments are asset backed and if a failure unfortunately occurs, selling the underlying asset may recoup some of the initial capital, but there is no guarantee that the assets will be sufficient to recoup the initial investment.

In addition, the lower levels of scrutiny in the crowdfunding model mean that there is an increased risk of fraud or failure as scams or poor quality projects find an easy route to market.

Finally liquidity will always be a risk, particularly as there is currently no established secondary market for real estate crowdfunding investments. However, this situation is likely to improve over time as wider and deeper secondary markets are established.

Mitigating the Risks

There are several ways to mitigate the risks when investing in real estate through a crowdfunding platform. The first would be to choose a reputable platform, which is preferably regulated and carry out due diligence on the underlying investments. The stricter the rules and criteria imposed by platforms the better the investments listed there are likely to be. It is not enough to trust the platform alone, investors should undertake their own research and due diligence and only invest in projects that they are

comfortable with and fully understand.

Platforms will have certain processes in place to further protect consumers, particularly in the UK and US where crowdfunding is covered by new regulation. If the platform fails they must have a process in place to pass on equity investments to experienced managers, and to ensure the ongoing administration of debt based investments. Many platforms will hold the investment in trust or beneficially on behalf of the investor, and to ensure it is kept separate from the assets of the platform.

Crowdfunding platforms do not offer any recourse (to financial services protection schemes) for investors if the investment fails, but asset-backed investments can mitigate the risk of a total loss as underlying assets will be sold to repay investors. Some platforms even have a provision fund to protect investors if the borrower defaults, but this is not mandatory.

Diversification across several properties can enable investors to create a well-balanced portfolio which is suitable and meets their needs. They can mitigate the risk of a total loss by offsetting riskier investments against solid asset-backed opportunities. The minimum investment seen with crowdfunding means investors can diversify across several properties which wouldn't be possible with traditional real estate investment opportunities.

¹² - <https://www.realtymogul.com/blog/asset-allocation-in-real-estate>

UK Crowdfunding Regulation

On 1 April 2014, the Financial Conduct Authority's (FCA) policy statement, PS14/4, on the regulatory approach to crowdfunding came into effect. The policy covered two broad categories of crowdfunding – investment-based and loan-based crowdfunding.

Loan-based (debt) Crowdfunding

- Platforms must meet a minimum prudential requirement to ensure ongoing viability
- Platforms must have a process in place to ensure existing loans continue to be managed if the platform fails
- Platforms holding client money will be brought into the existing CASS regime of client money rules
- Implementing cancellation rights for consumers
- Enforcing improved disclosure of information by platforms to consumers
- Enforcing the current FCA dispute resolution and giving consumers access to the Financial Ombudsman Service (FOS)
- Platforms will have to report their financial position, client money holdings, complaints and loans arranged to the FCA

Investment-based (equity) Crowdfunding

The FCA restricts investment to four categories of investors.

- Certified sophisticated investors (including self-certified)
- Certified High Net Worth investors
- Retail investors that confirm that they will receive regulated investment advice or investment management services from an authorised person, regarding the promoted investment
- Retail investors who certify that they will not invest more than 10% of their net investible portfolio in unlisted shares or unlisted debt securities (excluding their primary residence, pensions and life cover)

The full policy statement can be found on the FCA website¹³

Real Estate Market Update

The real estate market has a number of different investment opportunities providing a choice of locations, build types and sectors. It has historically been a strong performing asset class. This section provides an update on the global real estate market and the emergence of crowdfunding as an alternative form of finance.

Real Estate Returns

Historical returns from real estate in key locations across the globe have been strong. In 2013 IPD tracked a 10 year annualised total return of 8.4% in the US¹⁴ and 6.3% in the UK¹⁵.

Prime UK commercial property values are forecast to increase by over 8% per year from 2014 to 2018, and residential property is expected to grow by 5.5% per year around the UK and 6% in London by 2018¹⁶

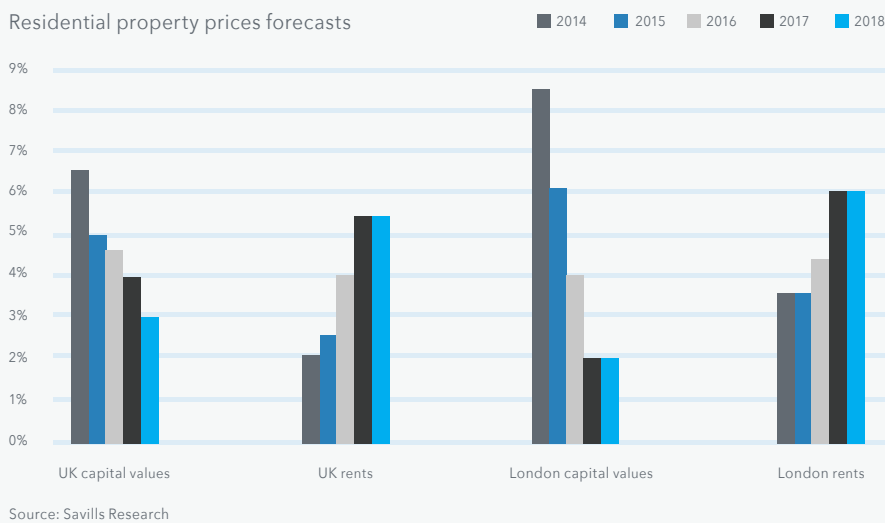
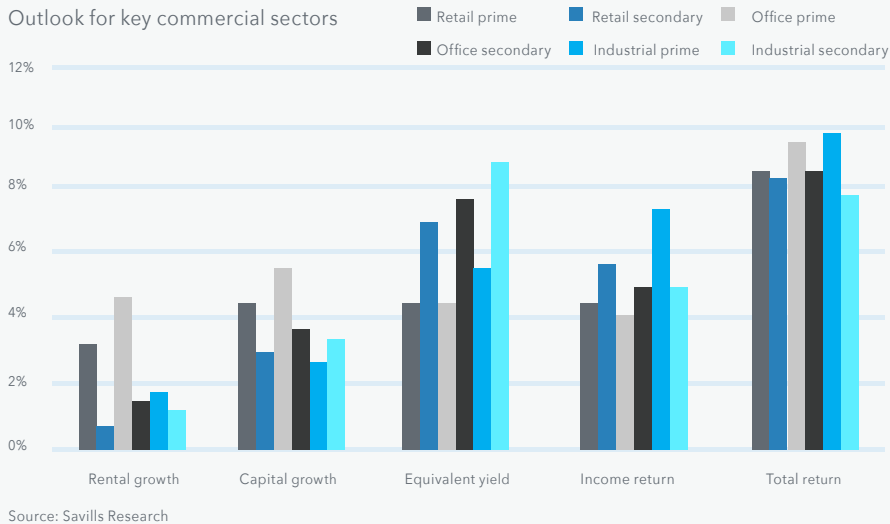
13 - <http://www.fca.org.uk/your-fca/documents/policy-statements/ps14-04>

14 - <http://www.ipd.com/indexes/index.html?country=USA>

15 - <http://www.ipd.com/indexes/index.html?country=UK&col=2>

16 - <http://pdf.euro.savills.co.uk/uk/residential---other/cross-sector-web.pdf>

UK Property Forecasts 2014-2018



Real Estate Crowdfunding Platforms

The Role of the Platform

The main role of a crowdfunding platform is to provide deal flow. Online platforms allow investors easy access to investment opportunities which can be added, updated and subscribed to any time of the day.

Some platforms have chosen to ensure a higher quality of deal flow by undertaking their own due diligence on investment opportunities. Many set requirements that developers must meet such as proven track records, credit and background checks. Once a project has been fully funded the majority of the platforms will require frequent, usually quarterly, progress updates.

Some platforms have a provision fund (or similar) to protect investors' should the borrower default. Others choose to take a charge over the property as security for investors. Many also have a system in place to manage investments should the platform fail, such as appointing a new manager or trustee to oversee administration.

For developers, platforms provide an effective way to market their projects to potential investors. Many follow a uniform template for how to list information so it is easily understood by investors. Investment providers can assess the benefits and costs of each platform and decide where is best to list their investment.

Platforms provide a straightforward investment process. Everything can be done online, from reviewing and signing legal documents to transferring funds, saving time and costs for both providers and investors.

Platform Successes

iFunding, a US based platform, was one of the top fund raisers with over US\$25.6m raised since its launch in Angels Den hosts monthly Speedfunding events, which have a success rate of 90% of fund seekers able to find at least one investor willing to invest in their business. 2013 from a pool of 3,000 investors¹⁸.

Platform Failures

There has only been one platform failure identified to date, Collaperty. Launched in 2013 as a commercial real estate crowdfunding site they are no longer in operation. Their website states "not being able to provide what the market is looking for" as the reason for their closure.

REAL ESTATE CROWDFUNDING

ALTERNATIVE FINANCE SECTOR REPORT

Platform Models

Real estate crowdfunding platforms can follow several different models. Many include both equity and debt opportunities, while some use a co-investment model. Lead-generation is also becoming a popular way for platforms to drive large numbers of investors towards investment opportunities, without transacting deals through the platform. These all fall under the real estate crowdfunding umbrella.

Equity

Equity is the fastest growing platform model. Investments usually include unlisted shares or membership interest in a limited liability company which is set up as a special purpose vehicle (SPV) for the specific project.

This is common practice in property development as it allows established businesses to operate individual construction projects within each SPV, keeping profits, costs and administration as simple as possible. Returns come from any profits on rental income or capital growth in the underlying development. Investors may be locked in for a defined term and find it hard to exit early, unless they can sell their equity interest privately to another investor. The secondary market for equity based crowdfunding is still in its infancy but is likely to develop as the crowdfunding market grows and matures. Platforms are likely to aid this development by incorporating marketplaces into their offering, allowing investors to list their investments for sale to other users.

Debt

Debt based platforms are centred on traditional lending methods and are one of the most well-established and fastest growing forms of crowdfunding, particularly in the UK. Companies, often profitable small or medium -sized enterprises (SMEs), will issue a certain amount of debt to fund expansion plans,

new ideas or research and development. Real estate debt crowdfunding lends money to developers to take on a specific project or a series of projects. As with any loan, the developer would then pay a fixed rate of interest to service the loan over a fixed term, with the return of principal at the end of the term. Loans can be interest-only or capital and interest and range from 6 months to 25 years.

Innovations in the Debt Market

Bridging loans may be more attractive to investors as they are usually short term, less than one year, pay a higher rate of interest and are secured against the property. Developers use bridging loans as a quick and short term of finance until longer term financing can be arranged. For example, a developer may want to ensure that they have the capital ready to purchase a property at an auction.

Bridging loans are risky as there is no guarantee that the proposed exit plan will be carried out to repay the loan.

Angels Den is one platform that is enabling its investor to expose themselves to bridging loans while mitigating the risk. They offer bridging deals that are already in place, with the valuation and due diligence process already completed. The original bridging company will keep a proportion of the loan so that its investors are only exposed to 60% of the loan-to-value.

Co-Investment

Co-investment involves a group of investors collectively investing in a property, by forming a syndicate. Each investor will own a portion of the physical property and the rental income and capital growth attributed to their share. Investments tend to be longer term providing regular income and capital growth over several years.

Co-investment strategies are the same

as syndicate properties which are very popular in the UK. They can require a large amount of legal structuring to put together and need ongoing administration, but they can allow investors access to established properties at a fraction of the overall cost.

Lead Generation

As there is no global standard for crowdfunding regulation many countries restrict investors from investing through platforms. For example in South East Asia, regulation on how real estate can be funded is quite strict, and therefore lead generation has become a popular alternative. Platforms allow developers to list investment opportunities online and gauge investors' interest. Platforms do not collect any investors' funds but instead put interested investors in touch with the developers seeking finance. These platforms may conduct some due diligence but offer no recourse if investments go wrong. They purely allow developers to access a large pool of willing investors. These platforms charge developers to list on the platform and may also charge investors to access the listings.



Investment Platforms

Here is a sample of the various successful crowdfunding platforms globally.

Name Varies	Platform Model	Location	Launched	Funds Raised	Minimum Investment
CoAssets	Lead Generation	Singapore	2013	S\$8.6m	S\$4,000
CrowdBaronAngels Den	Co-Invest (Equity) Mezzanine	UK and Hong Kong	2013 2012	\$2.06m £16m	Varies
Fundrise	Debt/Equity	US	2011	Unknown	\$100
Realty Mogul	Equity	US	2013	\$21.96m	\$5,000
iFunding	Debt/Equity	US	2013	\$25.7m	Varies
Open Avenue	Equity	Canada	2014	Unknown	\$10,000
Humming Crowd Realty	Debt/Equity	UAE	2014	Unknown	AED 1,000
Casa Grupo	Debt/Equity	Nigeria	2014	₦134.7m	₦100,000

Real Estate Crowdfunding Market Analysis

Data was compiled from several popular real estate crowdfunding platforms to build an accurate picture of the current market. Data included investment offerings listed on various platforms at the time of writing (June 2014). The following analysis is based on information gathered through extensive online research. Over 30 platforms were identified in the market, although it is believed that there are many more real estate crowdfunding websites operating on a local scale (particularly in the US) which are difficult to identify. Information was collected where available as many crowdfunding websites restrict users based on net worth requirements.

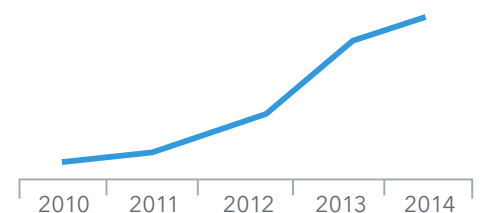
Several investment opportunities were analysed in order to gauge current trends within the market.

Platform Growth

The first dedicated real estate crowdfunding website identified was launched in 2010. The market has developed rapidly and we have identified over 30 dedicated real estate crowdfunding platforms worldwide, although we believe the actual number may be much larger.

Real Estate Crowdfunding Platform Growth (2010 - 2014)

Growth in Number of Platforms



Source: Intelligent Partnership (2014)

REAL ESTATE CROWDFUNDING

ALTERNATIVE FINANCE SECTOR REPORT

Due Diligence

71% of platforms identified undertake some degree of due diligence before allowing an investment to be listed. Although we do not know the exact criteria each platform requires of the developers, providing some form of due diligence will ensure that only qualifying opportunities are available to investors. Just because the platform undertakes some due diligence it doesn't mean that the investment is safe, or that it is suitable for the investor. Investors should always perform their own due diligence to verify any checks undertaken by the platform.

Locations

The crowdfunding concept is spreading rapidly and covers a number of countries around the globe. The majority of platforms are based in the US, followed by the UK and Canada. There is a lot of potential for growth into new markets over the coming years, particularly Asia and South America.

Platform Locations (2014)

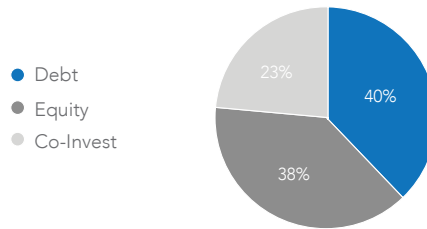


Source: Intelligent Partnership

Investment Structure

The ratio of equity and debt structured investments was relatively evenly distributed across our sample with 38% and 40% respectively. Restrictions on debt based investments are less stringent and there are a number of opportunities available. Co-investment accounted for 22% of our sample, with every investment coming from one platform that specialise in this investment model.

Investment Structure (2014)

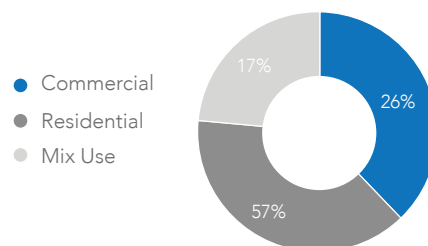


Source: Intelligent Partnership

Property Type

Real estate investment opportunities were found across residential, commercial and mixed use (commercial and residential) properties. Residential accounted for the highest proportion on investments with 57%. These range from single family homes to large scale apartment complexes. Commercial property, including mainly retail and office space, accounted for 26% of investment offerings. The remaining 17% consisted of mixed use developments.

Property Type (2014)



Source: Intelligent Partnership

Minimum Investment Levels

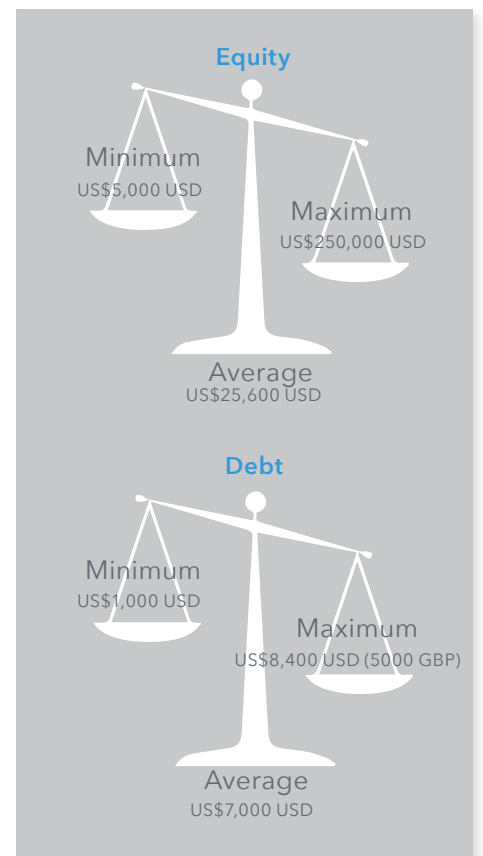
The minimum investment (capital required to invest) shows how accessible the real estate crowdfunding market is. Data was collected from several platforms from across the world in local currencies and have been converted to USD [x1.70 for GBP] for analysis purposes.

Equity crowdfunding is generally higher

risk and therefore minimum investment levels should reflect this. The lowest equity investment was US\$5,000 and the average was much higher at US\$25,600.

As debt based investments are often offered by relatively established companies they are seen as lower risk. The minimum investment is as low as US\$1,000 with the average at just US\$7,000. The lower capital requirement and less stringent regulation means debt based investments are more widely accessible to investors.

Minimum Investment Equity vs Debt Offerings (2014)



Source: Intelligent Partnership

REAL ESTATE CROWDFUNDING

ALTERNATIVE FINANCE SECTOR REPORT

Investment Terms

Real estate is considered to be medium to long-term investment, with annual rental income and capital growth over the longer term. Short term options such as off-plan and redevelopment projects also exist.

Equity investments are commonly into unlisted companies with no established secondary market. These tend to be longer term investments ranging from 1 to 8.5 years. The average term is 4 years. Investors should note that although the aim will be to sell the underlying assets after a fixed term there is no guarantee that a sale will happen and investors should be prepared to be flexible. Established companies are more likely to use debt based investments to fund individual projects or expansion of their activities. For this reason the average investment term is lower at 1.5 years. Investment terms range from only 5 month to up to 3 years. These are much shorter than traditional real estate investments and means investors do not have to tie up their capital over a long timeframe.

Investment Terms Equity vs Debt (2014)



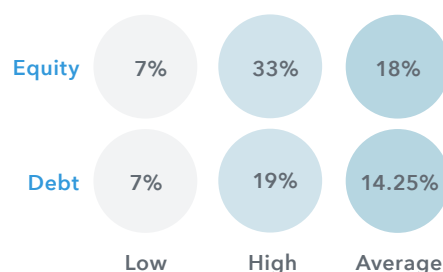
Source: Intelligent Partnership

Returns

The search for higher returns is one of the main drivers for investors to consider crowdfunding, particularly as bank interest rates on savings are so low. Returns are usually predicted for equity based investments and fixed for debt based. Note that returns will be influenced by location, type of property, build stage and local market demand.

In return for taking on higher risk with equity based investments you expect higher returns. Forecast returns range from 7% to 33% per year, with an average of 18% per year. Debt investments advertise strong fixed returns of between 7% and 19% per year. The average is 14.25% per year. These returns remain consistent with the IDP UK Commercial Property total return index, showing that these returns are realistic.

Returns Equity vs Debt (2014)



Source: Intelligent Partnership

Exits

The exit for equity and co-investment models relies on the sale of the underlying property. Each investment states when the developer hopes to sell the property to achieve the targeted return. Some equity models allow investors to sell their shares to other shareholders with permission from the investment provider. As mentioned previously there is currently no established secondary market for equity based crowdfunding investments although some platforms are likely to implement online marketplaces in the near future.

Debt investments typically have a defined exit on maturity of the loan, when it must be repaid in full. It is difficult for investors to exit before this date as yet there is not an established secondary market, although some platforms will look to implement marketplaces to facilitate this, as has been seen in the P2P markets in the UK and US. Investors may also be allowed to sell their investments privately before maturity with permission from the

investment provider.

Conclusions

The real estate crowdfunding concept is growing rapidly and in locations all over the world, giving investors the benefit of an asset backed real estate investment and the opportunity to achieve stellar returns at a much lower investment level. Crowdfunding provides more options to the investors around the investment timing, type and location of the property.

- 71% of platforms undertake some form of due diligence before listing an investment
- 38% of investments were structured as equity and 40% debt
- Average annual returns from equity based real estate crowdfunding are 18%
- Average annual returns from debt based real estate crowdfunding investments are 14.25%
- Residential property based investments were the most popular with 57% of the market

Additional Information

[Angels Den](#) hosts free Business Funding Clinic to educate fund seekers before pitching to potential investors and Speedfunding events for investors to hear fund pitches and ask business owners questions before deciding to invest.

[Massolution](#) provides crowdfunding and crowdsourcing market research, data and updates across all sectors of crowdfunding.

[Alt Fi](#) provides data and news for the alternative finance sector.

[UK Crowdfunding](#) provides background information and self-regulation for UK platforms.

[Times Realty News](#) provides market updates and commentary on the real estate crowdfunding sector.

REAL ESTATE CROWDFUNDING

ALTERNATIVE FINANCE SECTOR REPORT

Real Estate Investment SWOT

Strengths

- Provides diversification from mainstream financial assets
- Portfolio benefits such as hedge against inflation and steady regular income

Weaknesses

- Lack of liquidity in the sector
- High minimum investment costs
- High transaction costs
- Regulatory barriers in some countries
- REITs are unclear about the underlying properties
- Possibility of under or overvaluing the underlying property



Opportunities

- Emerging countries and economies may provide stellar returns
- High rate of competition to drive out bad investment opportunities
- Alternative finance to bridge the weakness and give more investors access to this asset class

Threats

- The economic health in parts of the world
- Changes in supply and demand
- Market 'bubbles'

Alt Fi Sector SWOT

Strengths

- The availability of capital
- Large amounts of deal flow
- The ability to 'test' the market with an idea
- Increased investor engagement
- Usually cheaper transaction costs
- Open data for clear investing environment
- Strong investment returns possible
- Monitoring investments live online

Weaknesses

- No secondary market at present
- Higher risk
- Possibility of bad investment offers as companies want to capitalise on the crowdfunding hype



Opportunities

- Vast amounts of possible applications for alt fi concept
- Possibility of secondary market
- New investment locations

Threats

- Regulatory scrutiny
- Banks are of a much larger size
- New lending institutions taking over the sector
- Lack of regulation

Conclusions

Real estate is a well-understood and established asset class providing a range of investment benefits. The diversity of the sector enables investors to capture a variety of investment benefits to suit their needs and overall portfolio strategy.

Crowdfunding is an alternative to traditional financing where savers and borrowers come together on an online platform. Investments can be donations or reward based, but the investment crowdfunding strategies (debt and equity) are an extremely effective way for businesses to raise capital for various projects and activities. In recent years the big major lending institution and banks offered disappointing interest rates and been reluctant to lend, so the popularity and use of the crowdfunding model has soared.

Before the development of crowdfunding, real estate investors were stuck with high minimum investment and transaction costs or completely unable to invest. Since the application of crowdfunding to real estate investing the dynamic has changed, more investors can access this asset for a lower cost and while enjoying the same portfolio benefits as a direct investment. Minimum investments can be found as low as \$100 in the market.

Commercial and residential properties are well-established investment products that can provide strong returns in key locations. Real estate crowdfunding platforms exist in several of these areas

and are enabling investors to achieve above average returns on all types of investment structures.

Crowdfunding comes with a number of unique risks that investors should be mindful of and consider when assessing potential investment opportunities. Due diligence is essential and should be carried out when considering any real estate investment opportunity, as risk and return varies depending on the risks and returns can vary dramatically by location and project.

- Real estate can have several roles in a portfolio – growth, income, aggressive or defensive diversification and a hedge against inflation
- The crowdfunding model can benefit real estate developers by saving on cost and time as well as reaching a large investor audience
- Investors can also benefit from crowdfunding, saving on transaction costs and the ability to easily diversify
- Returns from real estate crowdfunding projects are often forecasted much higher than the market averages in key locations

Disclaimer

This article is provided for general information purposes and for use only by Investment professionals and not by retail investors.

Reliance should not be placed on the information, forecasts and opinion set out herein for any investment purposes and Intelligent Partnership will not accept any liability arising from such use.

Intelligent Partnership is not authorised and regulated by the Financial Conduct Authority and does not give advice, information or promote itself to individual retail investors.

Publication

The information has been compiled from credible sources believed to be reliable, however it has not been verified and its accuracy and completeness are not guaranteed.

The opinions expressed are those of Intelligent Partnership at the date of publication and are subject to change without notice.

No part of this publication may be reproduced in whole or in part without the written permission of Intelligent Partnership.

© 2014 - Intelligent Partnership Limited

**TO FIND OUT MORE ABOUT OUR
LATEST ARTICLES, BLOGPOSTS AND
REPORTS, VISIT OUR WEBSITE:**

www.intelligent-partnership.com

OR INTERACT WITH US HERE:



CONTACT US:

+44 (0) 203 375 1700
enquiries@intelligent-partnership.com
www.intelligent-partnership.com