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Industry Commentary

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PropTech Sector Sees Growing M&A Interest as Macro Trends Reshape Real Estate Market

The U.S. housing market has experienced a prolonged boom. Fueled by low interest rates, favorable lending standards, below-average new home construction volumes, and continued population growth, home prices have reached new highs while demand has exceeded supply by a wide margin. The COVID-19 pandemic disrupted the market as people began house hunting in the suburbs and the commercial real estate industry grappled with the implications of work-from-home arrangements. Despite a rising interest rate environment, COVID-19's impact on the real estate technology sector will leave a lasting impact for years to come.

Amid this macroeconomic backdrop, technological innovation is shaping the real estate sector as investors and innovative companies seek to address all parts of the home-buying value chain and improve the experience of real estate agents, consumers and every other constituent in the massive ecosystem (e.g., lenders, insurers, brokers, appraisers, title). William Blair has completed 12 M&A deals in the property technology ("PropTech") sector in the past two years, totaling over $10 billion of deal volume. We highlight some of the key macro trends influencing the housing market and discuss what is driving M&A activity and value in the PropTech space.

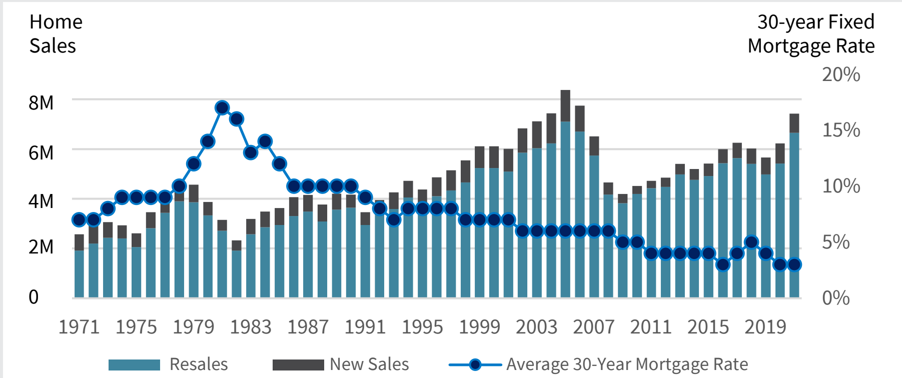
Key macro factors shaping the real estate sector today

During the Global Financial Crisis of 2007–2008, a sharp economic contraction adversely affected new housing starts in the years to follow. The subsequent recovery and growth were fueled in part by historically low interest rates, favorable lending standards, and new home formations that generated housing market demand with minimal new supply. The COVID-19 pandemic introduced a new era of growth in the housing market as interest rates dropped to historical lows and more people searched for new homes, particularly once work-from-home arrangements became more common. From 2020–2022, home prices soared and demand substantially exceeded supply. In fact, some industry commentators have referred to today's residential real estate market as the most under-supplied market in history.[1]

Driven by concerns about inflation, the Fed began to increase interest rates substantially in the first half of 2022. It opted to tighten rates again by 75 basis points on September 21 and expects to increase them by an additional 125 basis points by the end of 2022. The Fed signaled an intent to reach a terminal rate of 4.6% in 2023. This, among other indicators, suggests

1. InvestorPlace, "Fears of a housing market crash are creating huge opportunities," July 21, 2022.

Secular growth in transaction volume and decline in mortgage rates[2]

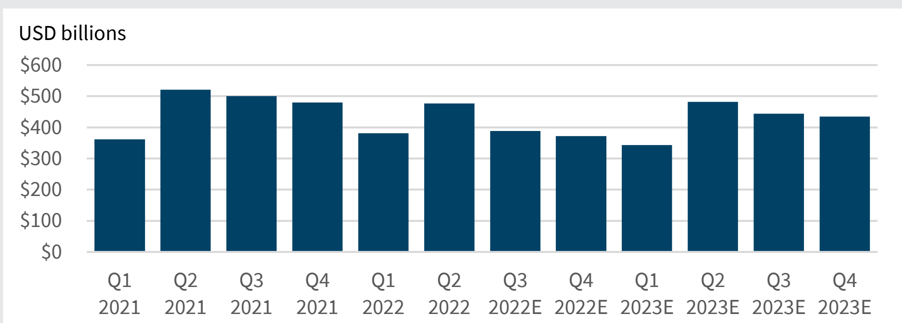


that the housing market's ascent may be nearing an end. Total mortgage origination was down from the first quarter to the second quarter of 2022 and is projected to continue declining in the near term due to rising rates, but consumer demand for housing remains strong.[3]

"This time is different"

Looking closely at buyer demographics, particularly the millennial generation (those born between 1981 and 1997), the struggle to get into a starter home remains a significant barrier. While existing home sales are largely competitive (homes selling at or above asking price), there is a shortage of approximately 3.8 million housing units according to Freddie Mac, and builders are not yet responding to the appetite for new housing stock.[5] In addition to the housing shortage, U.S. homebuilder sentiment dropped in July 2022 to its lowest level since the start of the COVID-19 pandemic, as high inflation and the steepest borrowing costs in more than a decade brought customer traffic to a near standstill.[6] At the same time, home listings have increased significantly; as of June 2022, inventory of available homes was 19% higher than it was in June 2021.[7] Even so, home inventory is lingering at about half of the level seen prior to 2020, and the rental market, alongside inflation, has skyrocketed, with the median monthly rent rising 14% year-over-year as of July 2022.[8]

Purchase originations expected to maintain steady seasonal volumes[4]



In addition to challenges with housing inventory, demographic trends are shaping the housing industry. As the pandemic took hold, many young people moved back in with their families. They are now looking to move back to the cities, driving up the rental market that already is experiencing tight supply in major metropolitan areas across the country. Caught between high rents and huge down payments for first homes, millennials are running far behind previous generations in terms of home ownership. Less than 50% of millennials in the United States owned homes in 2020, according to an Apartment List analysis of census data.[9] Comparing homeownership across generations, at age 30, millennial home ownership was 42% compared with 48% for Generation X and 51% for baby boomers.[10] Despite the current gap, however, millennials are expected to provide strong demand for homes in the years to come.

At the same time, the baby boomer generation is retiring in large numbers today. Demand for second homes and vacation homes is an influential factor in the housing market, particularly in popular retirement regions including Phoenix, Las Vegas, and Florida. For these and other wealthy homebuyers, the desire to limit debt burdens is apparent; all-cash purchases are 24% of all U.S. home sales as of July 2022, up from 15% in April 2021.[11 12] Alternative forms of financing are also gaining traction as private credit markets extend their reach into residential housing. While affordability has notably declined over the past several quarters, the growing range of available capital sources for borrowers and buyers has and will remain an important driver of the housing market.

With change comes opportunity: M&A activity in the PropTech sector

In response to these influential macro trends, the real estate industry is experiencing a wave of technological innovation across all areas of the ecosystem, from buyers and sellers to appraisers, lenders, closing attorneys, and loan maintenance providers.

Several factors drive the vibrant innovation taking place in the PropTech

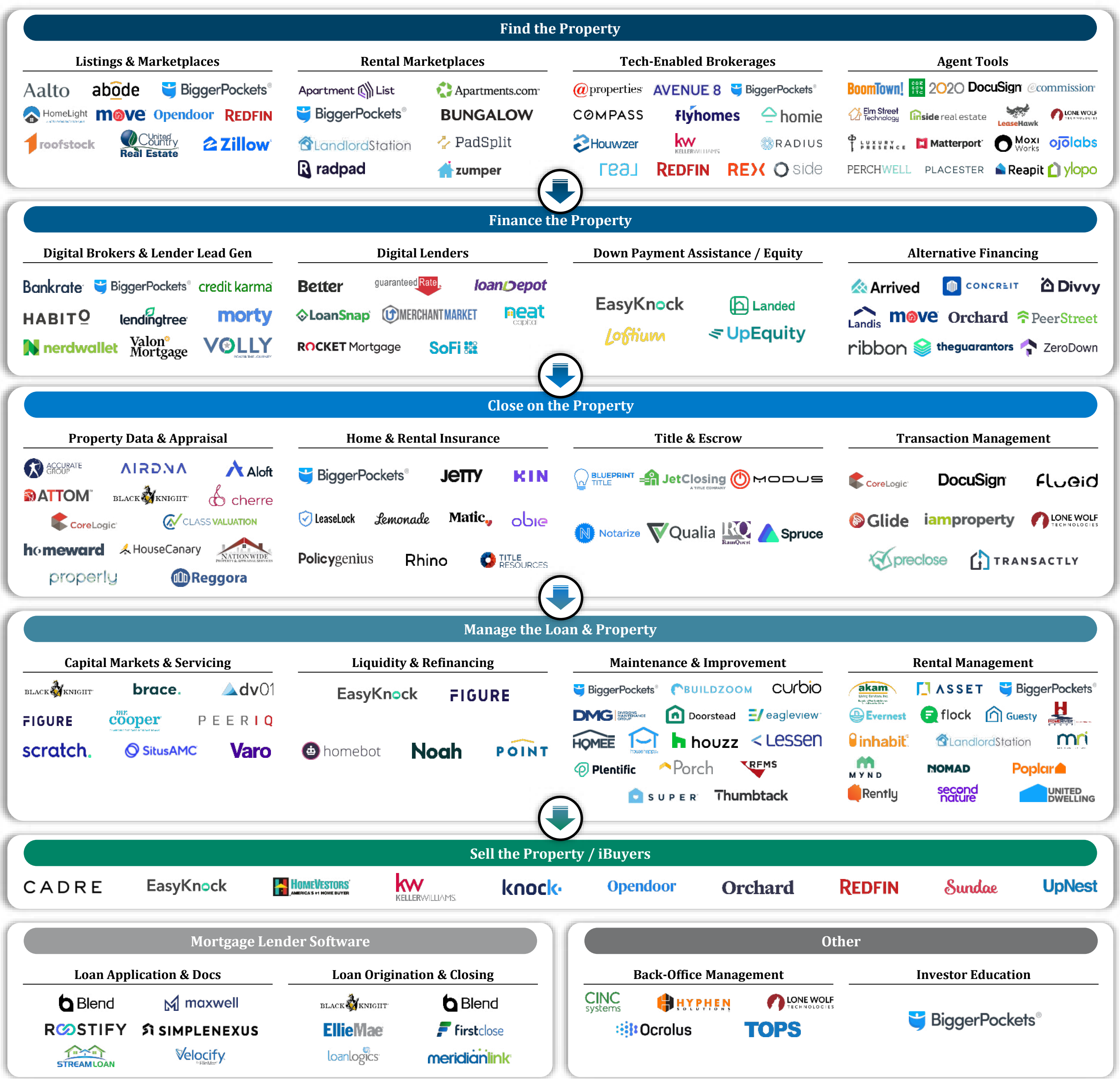
2. National Association of Realtors, "Existing Home Sales," August 2022. United States Census Bureau, "New Residential Sales," August 2022. Freddie Mac, "Mortgage Rates Increase," August 25, 2022.
3. Mortgage Bankers Association, "MBA Economic Forecast," September 19, 2022. Chart shows the dollar value of 1-to-4 family purchase originations in USD billions.
4. Ibid.
5. Freddie Mac, "One of the Most Important Challenges our Industry will Face: The Significant Shortage of Starter Homes," April 15, 2021.
6. National Association of Home Builders, "Builder Confidence Underwater After Falling for Eighth Consecutive Month," August 15, 2022.
7. Realtor.com, "June 2022 Monthly Housing Market Trends Report," June 30, 2022.
8. Redfin, "Rental Market Tracker: Growth in U.S. Asking Rents Slows for Second-Straight Month," August 19, 2022.
9. Apartment List, "Apartment List's 2021 Millennial Homeownership Report," February 9, 2021.
10. Ibid.
11. National Association of Realtors, "July 2022 Realtors Confidence Index Survey," August 18, 2022.
12. National Association of Realtors, "April 2021 Realtors Confidence Index Survey," May 20, 2021.

sector today. First, there is an obvious need for structural and process improvements. The U.S. real estate market has always been fragmented and focused on local and regional solutions rather than a broader, national approach. For both buyers and sellers, this means that too much time and effort are spent on process and logistics, a major source of complaints from all constituents. Looking at the real estate industry as a whole, this geographic fragmentation comprises the biggest difference from other large consumer markets, which do not have to confront such costly inefficiencies. In addition, when considering today's economic outlook—including inflation, interest rates, and the business cycle—it is often the case that more assets become available during economic downturns, offering value to home buyers who can afford to wait and to investors who have been watching from the sidelines waiting for opportunities like these.

Considering these factors, the real estate market is ripe for consolidation. The market needs a one-stop shop platform that addresses all critical customer pain points and feature requirements within a single integrated technology platform. Data science is also a corollary to this platform and to the broader innovation needs of the real estate industry; many start-ups today have focused on harnessing data to solve key problems around finding, buying, and managing properties.

Residential Real Estate Technology – Market Map[13]

The PropTech sector features a multitude of point solutions addressing various parts of the residential real estate value chain. Looking ahead, we believe value lies in combining disparate platforms into one cohesive customer experience.



13. William Blair. For illustrative purposes only.

Where will capital flow in residential real estate?

When considering where capital will likely flow in the PropTech sector, we identify two major trends that are emerging:

Real estate agents require better leads and supporting technologies: Within brokerages and agencies, agents need ways to acquire leads with high likelihood to transact. They need to then nurture these leads with superior supporting technologies. Given that agents typically spend a substantial percentage of their time on lead generation, there is strong demand for improved ways to generate high-quality leads and manage buyer and seller prospects. With the housing boom, almost 200,000 agents have entered the industry over the past two to three years.[14] When a downturn eventually arrives, there likely will be an outflow of lower-producing agents and new players, while high producers will gain market share. Technologies that drive efficiencies for the top producers, including better marketing, lead generation, and CRM, will be especially valuable in the years to come. Examples of companies creating technologies for better agent/brokerage performance include Boomtown, Elm Street Technology, Inside Real Estate, Lone Wolf, MoxiWorks, Perchwell, Reapit, and Ylopo. A substantial amount of private equity investment is flowing into this area as efficiencies within the top of the funnel will drive more sales and profits to agents and brokerages. Similarly, agents and downstream constituents also require accurate, real-time property-level data to drive differentiated insights and streamlined transaction experiences. Several firms providing this level of granular data include Attom Data, AirDNA, CoreLogic, and Placer.ai.

Need for a broader consumer experience with a streamlined, all-in-one platform: On the consumer side, the space is currently dominated by online services including Zillow, Redfin, and realtor.com, in addition to the regional real estate boards accessible to agents only. But each platform has serious pain points. There is strong demand for homebuyer-focused offerings, which can provide a broad consumer experience with a streamlined, all-in-one platform. The so-called "power buyers"—such as Orchard, Homeward, and Fly Homes—are well positioned because they are streamlining the consumer experience and getting very high attach rates (20%-30% or more) as a result. Such firms have proliferated to some extent, with a tremendous amount of venture capital invested in this space, and we believe there will be consolidation among these buyers, especially as some players like Reali leave the system. The real disruption and opportunity to create outsized value will come from combining disparate platforms into one cohesive customer experience.

Evaluating the investment landscape, venture capital and private equity firms have invested significant capital in the real estate sector since 2018. As these firms develop their portfolio companies over typical investment horizons, we expect a flurry of activity between 2023–2025 as private equity and venture capital firms seek follow-on financings, mergers, and exits. Many firms are focused on creating efficiencies and reducing frictions in the real estate market, which should lead to tremendous opportunities for those with differentiated insights and comprehensive solution sets.

Recent transactions highlight PropTech M&A trends

William Blair has led a number of influential transactions in the PropTech sector in the last two years. These transactions demonstrate some of the innovative ways investors are accessing the sector today.

- **RealManage receives growth investment from American Securities:** William Blair acted as exclusive financial advisor to RealManage in connection with its growth investment from American Securities. RealManage is the largest homeowner association and condominium management company in the United States, serving over 3,000 communities across 19 states using a technology-first approach. RealManage has acquired five highly successful community management companies, expanding its operations in Southeast Florida, Colorado, and Arizona. Communities and community association managers are supported by CiraConnect, RealManage's central services group that includes all of its software, resident service center, financial management, collections, and disclosure functions.
- **HomeVestors acquired by Bayview Asset Management:** William Blair served as lead financial advisor to HomeVestors, a portfolio company of Levine Leichtman Capital Partners, in its sale to Bayview Asset Management. HomeVestors is a leading real estate investment franchisor, providing services and education to franchisees seeking to operate their own independent, residential real estate investment businesses. The company generates proprietary real estate investment opportunities through advertising campaigns that utilize the "We Buy Ugly Houses®" national brand. HomeVestors was founded in 1996 and is based in Dallas, Texas.
- **Building Engines acquired by JLL:** William Blair acted as exclusive financial advisor to Building Engines, a portfolio company of Wavecrest Growth Partners, in connection with its sale to JLL (NYSE: JLL). Building Engines seeks to improve net operating income for commercial real estate portfolios. Building Engines helps its customers increase revenue, improve the occupant experience, and reduce operating costs with an innovative building operations platform. Today, more than 1,000 customers rely on Building Engines to manage critical operational needs across more than 3 billion square feet and 35,000 properties worldwide.
- **Zego acquired by Global Payments:** William Blair acted as lead financial advisor to Zego, a portfolio company of Vista Equity Partners, in connection with its acquisition by Global Payments (NYSE: GPN). Zego (Powered by PayLease) is a property technology company that frees management companies and community associations to better serve residents through resident experience management solutions. Zego enables operators in the residential real estate industry to modernize their resident experience, seeking to boost satisfaction and operational efficiency. The company offers an integrated property management back-end system covering payments and utilities to communications and smart devices.

14. National Association of Realtors, "Membership Count by Month - 1910 to Current," July 2022.

- **Grace Hill acquired by Aurora Capital Partners:** William Blair acted as exclusive financial advisor to Grace Hill, a portfolio company of Stone Point Capital, in connection with its sale to Aurora Capital Partners. Grace Hill provides technology-enabled talent performance solutions that help owners and operators of real estate properties increase property performance, reduce operating risk, and grow talent. Its solutions cover policy, training, assessment, and data-driven insights. Today, more than 500,000 real estate professionals from more than 1,700 companies rely on talent performance solutions from Grace Hill.
- **Storable receives majority investment from EQT:** William Blair acted as exclusive financial advisor to Storable, a portfolio company of Cove Hill Partners, in connection with a majority investment from EQT alongside existing investors, Cove Hill Partners, and the Storable management team. Based in Austin, Texas, Storable delivers management software, marketing websites, tenant insurance, payments, and the industry's largest storage marketplace through one integrated solution that is designed to help storage operators increase efficiency, enhance occupancy, and improve profitability.
- **Airbnb goes public via initial public offering:** William Blair acted as an advisor to Airbnb (NasdaqGS: ABNB) on its IPO, which raised $3,830,000,108 in December 2020. The deal priced at $68, well above the initial range of $44-$50. Airbnb operates a platform that enables hosts to offer stays and experiences to guests worldwide. The marketplace model connects hosts and guests online and through mobile devices to book spaces and experiences. Airbnb was founded in 2007 and is based in San Francisco, California.
- **Hyphen Solutions receives significant equity investment from GreyLion Capital and Stone Point Capital:** William Blair acted as exclusive financial advisor to Hyphen Solutions in connection with its investment from GreyLion Capital and Stone Point Capital. Hyphen Solutions is the leading provider of cloud-based residential construction management software, providing over 70,000 builders, installers, and manufacturers with industry-leading supply chain scheduling, procurement, and collaboration solutions for North America's top homebuilders and their suppliers. The company's SaaS applications deliver greater operational control, better communications, and increased productivity. The Hyphen Network services over 500 builder divisions, which built approximately 300,000 new homes in 2019.
- **Buildium acquired by RealPage:** William Blair acted as exclusive financial advisor to Buildium in connection with its sale to RealPage. Buildium's platform serves association management, student housing, residential properties, tenants, and vendors by providing solutions for leasing, advertising, tenant screening, document storage, collecting deposits, accounting, rental portals, and signing leases. Buildium services over 15,000 customers in 46 countries, totaling over 1 million residential units. Buildium was founded in 2004 and is based in Boston, Massachusetts.

To learn more about trends and opportunities in the PropTech sector, reach out to William Blair's technology investment banking team.

Select William Blair Transactions

Not Disclosed
RealManage
has received a growth investment from
American Securities

Not Disclosed
HomeVestors — America's #1 Home Buyer
has been acquired by
Bayview Asset Management

$315,000,000
BuildingEngines
has been acquired by
JLL

$925,000,000
Zego — Powered by PayLease
has been acquired by
globalpayments

Not Disclosed
Grace Hill
has been acquired by
Aurora Capital Partners

Not Disclosed
Storable
has received a majority investment from
EQT

$3,830,000,108
airbnb
Initial Public Offering

Not Disclosed
Hyphen Solutions
has received an investment from
GreyLion Capital
Stone Point Capital

$580,000,000
Buildium
has been acquired by
RealPage