

MARKET TRACKER MAY 2016

# Proptech business models: is the real estate sector facing a paradigm shift?

The theory of evolution maintains that changes occur abruptly instead of being part of a smooth, constant process. Could the same theory apply to the real estate sector? With its hallmarks of segmentation, regional peculiarities and a plethora of different construction and legal standards, the industry is now facing the arrival of a new kind of company: proptechs. Their aim is to make a disruptive change within the sector and thus trigger a digitalised transformation similar to the one happening in the financial sector as a result of fintechs.

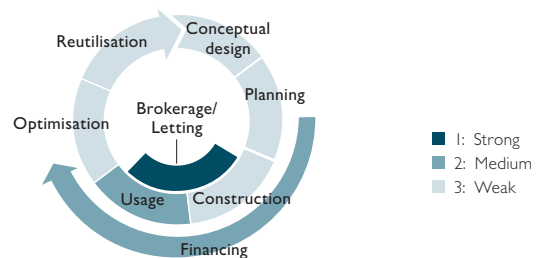
## The conditions for a fundamental innovation boost seem unfavourable

Proptech is a term formed from the words **property** and **technology**, and it is used to describe new companies whose business models link innovative technological possibilities with the real estate sector. Digitalisation is a growing force within the real estate industry, and in recent years, it has brought forth a number of interesting business models, some of which have reached the expansion phase. However, we have not seen a revolution in terms of innovation. Neither the new proptech arrivals nor the real estate sector's own evolutionary processes have been able to release a tidal wave of change. The reasons: the underlying structure of the sector seems to be too "analogue", the data generated is too fragmented, and, as a product, real estate itself is too closely connected with personal choices.

## All the same, it is possible to discern the first footholds for proptech companies in the value chain

If you look at the real estate industry's value chain, stretching from project development to conceptual design, planning, construction, usage/operation, optimisation, reutilisation and then on further to the intersectional services of financing and brokerage, some of these activities seem to attract more attention than others from proptech business models. For example, classic brokerage activities (marketing platforms) use planning tools such as BIM (building information modelling). Then there are also crowdfunding models and the software-supported mapping of interiors. What these all have in common is that they use IT to produce highly efficient solutions for real estate activities.

FIG. 1: INTENSITY OF PROPTech COMPANIES' ACTIVITIES



Basis: Quantitative analysis – number of proptech companies

## Global proptech market: highly developed in the USA and UK, but only in its infancy in continental Europe

Just like their fintech peers, proptechs have their origins in the English-speaking world, but they are now also well represented in Asian countries such as China, Singapore and India. In Europe, the UK is home to the largest concentration of proptech start-ups.

Though only a few exceptional cases have so far developed solid, i.e. profitable, business models, investors are currently channelling a lot of money towards the sector: on an international scale, total funding for proptechs and proptech start-ups came to \$1.7 billion in 2015. The USA accounts for the bulk of this money (49%), followed by China (26%). Looking at Europe (4%), some three-quarters of the total investment volume comes from the UK, and above all from London, where a proptech ecosystem with numerous "accelerators" has taken root. Accelerators are institutions which provide start-ups with short-term support, generally for 1–4 months, by giving them access to expertise and resources.

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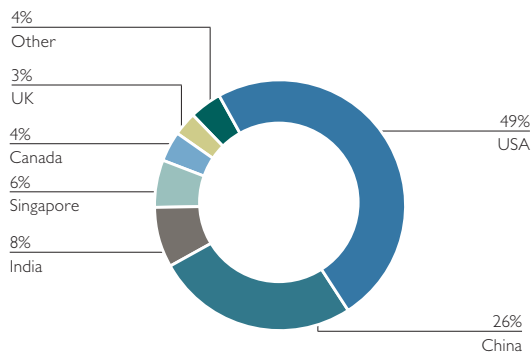
### Your contacts:

Dr. Thomas Beyerle  
thomas.beyerle@catella.de  
+49 (0)69 31 01 930-220

Riccardo Bazzoli  
riccardo.bazzoli@catella.de  
+49 (0)69 31 01 930-276



FIG. 2: BREAKDOWN OF TOTAL INTERNATIONAL INVESTMENT VOLUME IN PROPTECH (2010–2015) IN %;

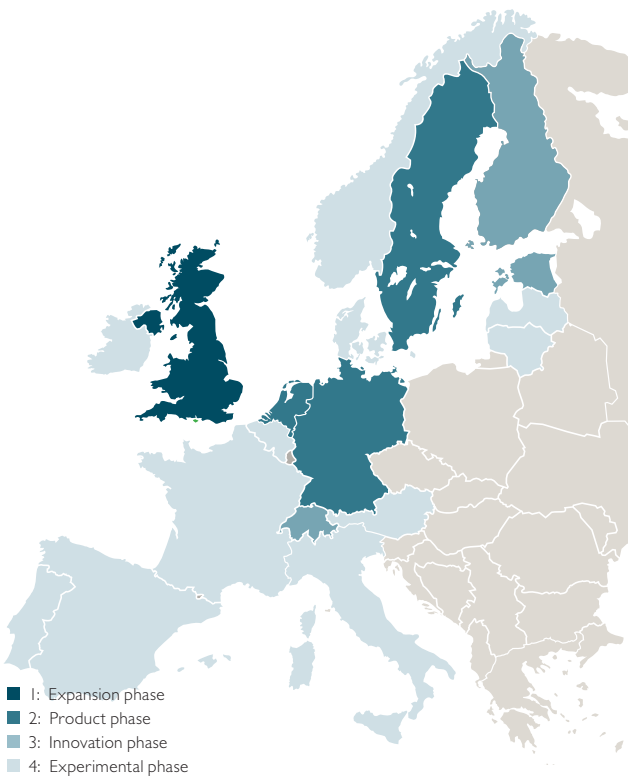


Source: Catella Research 2016, CB Insights

Compared to other European countries, the UK has been focusing attention for longer on proptech issues. For example, they are not just covered at trade fairs and in presentations dedicated to the start-up scene, but they also appear in scores of articles in the real estate press.

Until recently, proptech seemed to be a very foreign word in continental Europe, but it appears to now be making more of an appearance across the continent, while accelerators focusing on the proptech field have started appearing in Germany.

FIG. 3: PROPTECH'S MARKET PENETRATION ACROSS EUROPE



Basis: Quantitative analysis – number of proptech companies

Source: Catella Research 2016

### Digitalisation is rudimentary in Europe

Digital innovations have not really taken off in the real estate sector. If you look at the software in general use, little has changed since the 2000s. Process thinking is making slow progress, and problematic interface points as well as data availability still pose significant difficulties.

FIG. 4: RELATIVE RATE OF DIGITALISATION ADVANCES IN SELECTED INDUSTRY SECTORS ACROSS EUROPE

Economic branch	1	2	3	4
Information and communication				■
Financial and insurance activities			■	
Manufacturing			■	
Real estate activities		■		
Public administration, compulsory social security	■			
Human health and social work activities	■			
Agriculture, forestry and fishing	■			

■ 1: Advanced  
 ■ 2: Relatively advanced  
 ■ 3: Relatively basic  
 ■ 4: Very basic

Source: Catella Research 2016

When it comes to innovation and the use of IT in the workplace, the USA left the European market far behind in the late 1990s in almost every economic sector. Nowhere in Europe are there high-tech clusters such as Silicon Valley and the Boston metropolitan region. Only the financial hub of London in the UK can even begin to compare with these sites, and even then, it lags far behind them.

### In summary, proptech still has a long way to go

The proptech sector has its work cut out for it if it wants to have a disruptive effect on the real estate sector. Its current models feature fascinating solutions and display high levels of technological affinity, but they require too much capital and struggle with regulatory impediments. The data they require to successfully undertake their mission is another reason why they ultimately fail.

It is this latter factor in particular that is crucial for their ability to make a real impact. The real innovation will be the reorganisation and optimisation of process chains and procedures while establishing a set of uniform data standards.

In Europe, proptech, to a large extent, is still in its experimental phase, and it has yet to be “born” in certain countries. Nevertheless, the real estate sector needs to pay more attention to the issue of digitalisation. There is still a long way to go before we see a substantive change to the market: most proptech firms simply do not have access to the industry. They are also hampered by a structural drawback, as the data they need to fill their business models with life is not forthcoming. And then there is the property sector’s own internal capacity for development to be considered.