Transcript of
The Real Brokerage, Inc.
The Real Brokerage Second Quarter Earnings Call
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Participants

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Michelle Ressler - Chief Financial Officer, The Real Brokerage, Inc.

Analysts

Darren Aftahi - Roth Capital Partners
Tom White - D.A. Davidson

Presentation

Operator

Good morning, ladies and gentlemen, and welcome to The Real Brokerage Second Quarter Earnings Call. At this time all participants have been placed on a listen-only mode. And we will open the floor for your questions and comments after the presentation.

It is now my pleasure to turn the floor over to your host, Jason Lee. Sir, the floor is yours.

Jason Lee - Vice President, Capital Markets & Investor Relations

Good morning, everyone, and thank you for joining us today for Real's second quarter 2022 earnings call. With me on the call today are Tamir Poleg, our Chairman and Chief Executive Officer; and Michelle Ressler, our Chief Financial Officer. This morning, Real filed its financial results as well as its management discussion and analysis for the second quarter ended in June 30, 2022, on SEDAR and EDGAR. These documents along with the accompanying press release can be found on both SEDAR and EDGAR.

Before I turn the call over to Tamir, I would like to remind everyone that the company may make statements about its future results and other forward-looking statements during this call. Our actual results may differ materially from these forward-looking statements and the risk factors that could cause these differences are detailed in our Canadian continuous disclosure documents and SEC reports. Real disclaims any intent or obligation to update these forward-looking statements except as expressly required by law.

Now with that, I would like to turn the call over to Chairman and Chief Executive Officer, Tamir Poleg. Tamir, please proceed.

Tamir Poleg - CEO & Co-Founder, The Real Brokerage, Inc.

Thanks, Jason, and thank you to everyone joining the call today, including many listeners from our community of agents. We are excited by the progress we have made over the quarter, which is highlighted by continued rapid agent growth. We consider this a testament to the strong value proposition that we offer, which we believe is particularly attractive in more challenging macroeconomic environment as agents look for platforms that will allow them to be more productive.

With 129% agent growth year-over-year in Q2 to just over 5,600 agents, we believe we are still continuing to see incredibly strong market share penetration despite current economic headwinds. However, we remain alert and cautious and are continuing to monitor movements in the mortgage rates, among other key economic factors, which have resulted in a recent sharp decline in home sale transaction volumes in the market. Given the economic uncertainty, we are focused on strategic execution while navigating the current environment.

Firstly, we are focused on capturing market share. As I previously mentioned, we witnessed phenomenal agent growth over the quarter. In addition, subsequent to the end of the quarter, we announced that we have exceeded the 6,000 agent milestone. Importantly, as we continue to navigate the shift in the industry, we remain focused on the quality of our existing agent base and closely monitor our agent productivity. As such, we have been identifying and filtering out nonproducing agents from our platform. This is an important piece of managing costs and expenses as we continue to pave the way for a successful path ahead.

Additionally, we have witnessed voluntary self-churn at a higher rate than at the end of last year, which has been common across the industry. Similar to other trends we have witnessed across the space, the agents that have left our platform tend to be nonproducing or low productivity agents. We expect this trend to continue given the current market dynamics and aggregate transaction volume weighing in the regions where we operate. Again, despite the shift in the market, we continue to expand our net agent count growth at a tremendous rate, which leaves us optimistic about the agent proposition and the ability of our business model to perform through cycle.

As part of our growth strategy, we recently brought a new VP of Sales, Rob Kim, who, in addition to being a 20-year real estate veteran, comes from Knock, a B2C real estate startup where he managed strategic business partnerships. Rob has already made strong headway in building our agent and team pipeline, and we are excited for him to help further our expanding footprint.

On the expansion front, we expanded to Mississippi over the quarter. This brings our total footprint to 44 states, D.C. and two Canadian provinces. We are also focused on new ways of monetizing our existing platform. In Q4 of 2021, we launched our instant payment program, which gives agents the option to be paid at the time a transaction is executed rather than at closing. While revenue from the program currently remains a small contributor overall, it grew 172% on a dollar basis from Q1 as adoption continues to increase.

Additionally, we renegotiated our partnership with Chime, a real estate CRM tool that assists agent productivity while allowing for future revenue opportunity for Real. We were able to capture upgraded features at a steep discount off the retail price to offer a compelling package to Real agents. We appreciate the partnership and believe this will add significant value to agents' production goals. In addition, we are excited to announce that we are officially expanding our 'Real Launch' early career mentoring program to 12 additional states. In addition to the initial successful pilot program in Texas and California, which was also launched during the quarter. This program is geared towards our agents that are new to the field as well as those looking to reboot their existing careers to coaching. It represents an incredible opportunity for Real to help develop a pipeline of high-producing agents in a quicker fashion, while receiving a 50% commission split on transactions completed during the eight month program.

The bottom line is that it represents an important new revenue stream for the company while elevating our top-producing agent force. This is only Phase I in a holistic overhaul of our existing agent training programs. We have a number of exciting new revenue-generating opportunities in development, including a mid-career coaching program to help agents take their business to the next level. More information on our coaching program to come at our upcoming inaugural One Real Conference.

In October of this year, we plan to host an agent-focused conference in San Antonio, Texas. The event will be attended by both current and prospective agents and will feature world-renowned real estate expert, Ryan Serhant as our keynote speaker. The conference allows agents to learn from industry experts and showcase new ways to maximize real estate potential through interactive training sessions. It is also an opportunity for us to build a sense of community amongst existing agents and strengthen their affinity for the Real brand.

At Real, we continue to invest in our agents, giving them the resources needed to build and weatherproof their business. In June, we launched our Agent Success program, which is an early life cycle management program that creates communication touch points with recently onboarded agents to connect with all of our resources to help them establish a path of success. We believe this program will not only help integrate agents onto our platform and help them become productive more quickly, but it will also improve retention and reduce agent support tickets, which ultimately results in greater agent and platform efficiency.

In June, we also launched Knowledge Base, grow self-service support portal that enables agents to get their questions answered around the clock. Since implementing this tool, our support ticket per agent dropped significantly and enabled our support team to address support tickets faster and more effectively. That's the benefit of leveraging technology to do more with less. We also implemented Real Design Center, a platform of customizable marketing assets that will enable agents to increase their production. These Real-branded assets are integrated with MLS data, including property photos and descriptions, so agents can automatically create social media and print assets. Agents can even print and ship to prospects directly to the tool. This is a game changer for agents looking to increase brand awareness in their respective areas.

In late June, we launched onereal.com, a consumer-focused website that showcases real estate listings and provides agent and brokerage information directly to consumers. The site features in-depth search functionality that allows users to find properties to buy, sell or rent based on the following criteria: location, price, home types, number of bedrooms, number of bathroom and amenities. This website acts as our corporate site and is part of our consumer facing efforts. I want to clarify that this is not the consumer portal strategy that we have previously been discussing. We are on track to touch more on the strategy at The One Real Conference in October.

On the technology front, we are excited to have launched a new addition to our tech stack, which represented transformational enhancements to our agent software. We think about this sea change in innovation as a 'Real App 2.0' moment, as it affects how we are able to operate on the back end, replacing our need for industry standard third-party vendor SkySlope for documentation management. Our new proprietary software enables the ability to have more control over our processes, to enhance agent productivity and allows for further customization.

Real's software is an all-in-one app for transaction entry, document storage, brokerage review, compliance approval, communication, transaction document generation, payment processing and account reconciliation. Real agents now have enhanced visibility into the progress of their transactions through status updates, a sleek commenting system and the road to success program bar that tracks the journey of the transaction from entry to settlement. Agents can upload their documentation directly into the Real app, enabling not only a more streamlined process but also complete visibility into and control over agent transactions. The software is intuitive and easy to use, allowing agents to enter a deal start to finish in under 10 minutes.

As a test run I was personally able to input a deal in just a few minutes and without instructions as our development team created an experience that is incredibly user-friendly and intuitive. To emphasize what we have created, this proprietary technology is a game changer in our industry. No other brokerage has anything close. We have received extremely positive feedback from our Canadian agents, and we will be rolling it out in individual states throughout August and September, leading us to a company-wide launch at our One Real Conference in October.

As we look ahead to the remainder of 2022 and beyond, we remain focused on assessing key building blocks to fulfill our vision of a one-stop shop company to better elevate the home buying experience. As we have previously mentioned, the next important step on the build-out road map is owning mortgage capabilities. We are still in the process of searching for a business that best fits the criteria, and mortgage company valuations continue to look increasingly attractive. Separately, with regards to progress at Real Title, we continue to make inroads, having formed a JV in Texas in Q2 and one in Florida subsequent to the end of the quarter, which partnered with top Real agents. We believe that through enhancements to our app as well as rolling out the consumer-facing strategy, we will be able to drive higher attach rates in the future.

And before I conclude my remarks, I would like to note that in July, we graduated to the Toronto Stock Exchange from the TSX Venture Exchange. This marks an important next step in increasing our global visibility and expanding our investor base. According to the exchange, only 32% of TSXV-listed companies successfully graduate to the Toronto Stock Exchange, and those that do, on average, take four years to uplist. We are proud of having been able to achieve the stricter listing requirements to graduate and for accomplishing this goal in half the average time.

At this point, I will now turn it to Michelle for a more in-depth view of our financial results. Michelle?

Michelle Ressler - Chief Financial Officer, The Real Brokerage, Inc.

Thank you, Tamir, and thank you, everyone, for joining us. I will start by assessing some of our key financial results for the quarter. Revenue during the second quarter was $112.4 million, which represents a 386% increase from the same period in 2021 and an 82% increase from the first quarter. This was once again primarily driven by the strong agent growth we outlined at the top of the call.

Additionally, revenue growth was spurred by agent productivity. When reviewing the productivity per agent using the population that closed a transaction over the quarter and dividing this by revenue from commissions, the productivity per agent is slightly over $41,000 for the quarter. These agents closed on average 3.8 transactions during the quarter. We are also excited to have onboarded roughly 1,300 new agents in Q2 and are even more excited to have them participate in our new agent success program and the Real Launch mentorship coaching program as we continue to roll it out. We believe these initiatives will drive quicker revenue recognition to our business model by empowering faster times to initial transaction closings for new agents.

Notably, our elite agents represent only 1.6% of the total agent base, but generated $22 million in commissions, which represents 19% of total commission revenues for the quarter. Of agents that were Elite as of June 30, productivity during the quarter per agent reached over $242,000. We believe Real continues to be the winning solution for productive agents looking to be as efficient as possible even during the market downshifts. Furthermore, our agents completed over 10,000 transactions during the quarter, up 63% from the first quarter. The total volume of homes sold in Q2 alone was $4.1 billion or 71% increase from the prior consecutive quarter and a 357% increase from Q2 2021. As a point of comparison, it is nearly the $4.4 billion total we reported for the fiscal year 2021. The number of teams on our platform grew to over 300 at the end of Q2, which is a 33% increase since Q1 of this year.

Additionally, our platinum group teams, which are defined as teams that generate over $100 million in sales volume and the minimum of 200 transactions per year, grew in the low 70% range by count quarter-over-quarter. More than just focusing on top line growth, we remain committed to continuing to make improvements to our highly efficient operating model. Our operating expense per transaction, excluding revenue share, which is a core component of our agent incentives declined to 892 in Q2 from 1,180 in Q1. This is a 24% decline quarter-over-quarter. Our efficiency ratio, which we define as full-time employees, excluding Real Title employees, divided by the number of agents that are currently on our platform remains high and grew to around 1:62 from 1:55 at the end of Q1. The ratio of the number of employees on our transaction processing team to transactions processed over the quarter was 1:1,136.

In May, we recorded our highest single day of transaction processing, reaching 269. These metrics highlight the efficiency of our platform software and have translated to enhanced payment speeds and processing times for our agents. We believe that this is a big competitive advantage for our business. Our gross profit increased 283% year-over-year and 59% quarter-over-quarter to $9.3 million, which follows directly from our high revenue growth rate. Our gross margin declined to 8.3% from 9.5% in Q1, as our agents are increasingly productive and as a result are exceeding their commission caps.

As of June 30, approximately 10% of our agents have reached their respective commission caps. We remain focused on offsetting downward gross margin pressure with the adoption of the new monetization centers Tamir previously mentioned on the call, as well as the future rollout of higher-margin ancillary services. Our net operating loss for the quarter was $4.2 million compared to $2.8 million in Q2 of 2021, translating to a loss per share of $0.02 compared to $0.03 for the same period last year. However, we are operating cash flow positive and free cash flow positive. Our operating cash flow increased 86% year-over-year to $1.3 million, while our free cash flow increased 49% year-over-year to just over $1 million. Adjusted EBITDA loss for the quarter was recorded at $2 million, a slight increase from a loss of $1.9 million in Q1 when compared to a loss of $0.5 million in Q2 of 2021. We believe that adjusted EBITDA provides useful information about our financial performance, most importantly by excluding non-cash stock-based compensation that we offer to our agents and employees.

Turning to our financial position. We also ended the quarter the way that we began with a strong balance sheet that we continue to fortify by running a cost-conscious organization. Real ended the second quarter with a cash balance of $32.5 million and an additional $4.4 million held in investments in securities compared to $29 million and $8.5 million at the end of Q1. We have no debt and no need to raise that in the near term. Although others in the industry and more broadly have announced headcount reductions as a result of tough market conditions and overinvestment in recent quarters, our efficient and technology-driven operating model puts us in a position where we are quite comfortable with our current headcount. We plan to be strategic and hiring in the current environment, but we have no plans for layoffs.

In conclusion, we continue to cautiously monitor economic shifts while running a cost-conscious company. We remain confident that our business model is one that will continue to attract agents in a market downturn and should greatly outweigh any potential sharp reductions in market transactions.

This concludes my financial remarks. I will now ask the operator to open up the line for Q&A. Operator, can you please poll for questions?

Operator

Certainly. Ladies and gentlemen the floor is now open for questions. [Operator Instructions]. Your first question is coming from Darren Aftahi from Roth Capital Partners. Your line is live.

Q: Hey guys, good morning. Nice work on the quarter. The numbers are impressive. Curious if you can kind of maybe talk about what's going on with interest rates and housing prices, just the cadence of growth throughout the second quarter, maybe, April, May, June? And then maybe what you've kind of seen quarter-to-date in the third quarter.

Tamir Poleg - CEO & Co-Founder, The Real Brokerage, Inc.

Sure. Hi, Darren, good morning. So yes, I think that's -- everybody knows the situation in the market what we've seen overall that what that pending home sales in June were down about 20%.

We've seen some -- I mean, very often, we're seeing price decreases on asking prices on MLS. So this is becoming more and more popular. We are seeing some price reductions in markets like San Jose, California and Seattle, Washington. Some markets are doing much better than others. I think that as I mentioned previously, even though there is a decline in sales volume in the market, we are growing agent count rapidly. So this trend is kind of offsetting.

If we're talking about Q2, I think that we really showed the change in the second half of the quarter, so mid-May and June, that was affected by rising interest rates. I think that what happened was that many buyers were kind of shocked by the steep increase in interest rates, so they were kind of sitting on the fence. But in the past few weeks, as rates started declining, we are seeing buyers coming back into the market. So in the past, four, five weeks, we've actually seen a sharp increase in transaction volume.

So I think that what we will see at the beginning of Q3 is a little bit -- and I'm talking generally in the market, probably a decline in closed transactions, and those are transactions that are a result of transactions being put on contract in the second half of Q2. I think that the second half of Q3 is going to be stronger. But again, when it comes to Real, I think that we are doing a great job at attracting more agents. And when we grow a count by 120%, 130% year-over-year, even if there is a decline of 20% in market volume, we -- it gets offset by the addition of new agents.

Q: Great. And I'm just kind of curious your agent growth has been really strong. So two questions there. One, where are you taking agents from? And then two, you talked about some churn, which with the growth you've had is expected. I'm just kind of curious kind of the puts and takes of how we should think about agent growth going forward given the kind of churn and then kind of the ramp in new gross adds?

Tamir Poleg - CEO & Co-Founder, The Real Brokerage, Inc.

Sure. So a couple of weeks ago, we actually announced hitting the 6,000 agent milestone, and we keep seeing strong agent growth continuing right now. If you're asking where are we taking agents from, it's pretty much all across the board, as it was previously. So we cannot point out to one specific brokerage. I think that most of the agents that are coming over are from traditional brokerages. So we're seeing them increasingly looking for alternatives, especially now when they're a little bit uncertain about their income. They're looking for alternatives like ours that allow them to keep more money in their pocket out of every transaction.

So we think that this trend will continue, might even intensify as the market -- if the market cools down even further. When we talk about churn, it's pretty common when the market downturns for lower-producing agents or nonproducing agents to just go out of the industry, some agents are coming to the end of their license period and they need to renew and some of them are not renewing. So what we've seen in Q2 is two things: one, we proactively looked at our roster and examined who are the agents that have not produced in past three, four quarters, and we just terminated a few hundred of them. So we just off-boarded them. That makes our agents growth even more impressive, growing at 129% even though we terminated about 400 nonproducing agents. It means that the actual growth was higher. So we proactively terminated agents, and at the same time, we also saw agents that are nonproducing or very low producing just for forgiving their licenses and leaving the industry, and this is very typical. It's very cyclical. It happens every time that the market downturns.

Q: Got it. One last one for me. Could you give the exact number of agents at the end of the quarter as well as the number of completed transactions in 2Q? Thanks.

Tamir Poleg - CEO & Co-Founder, The Real Brokerage, Inc.

Sure. Michelle, do you have the number of -- the exact number of transactions handy?

Michelle Ressler - Chief Financial Officer, The Real Brokerage, Inc.

Yes, it was around 10,224, I believe.

Tamir Poleg - CEO & Co-Founder, The Real Brokerage, Inc.

And the number of agents, I believe, Darren the number was 5,650.

Michelle Ressler - Chief Financial Officer, The Real Brokerage, Inc.

Correct.

Q: That is helpful. Thanks guys. Congrats again.

Tamir Poleg - CEO & Co-Founder, The Real Brokerage, Inc.

Thank you very much.

Operator

Thank you. Your next question is coming from Tom White from D.A. Davidson. Your line is live.

Q: Great. Thanks guys for taking my questions. I guess a follow-up on the questions about agent growth. And Tamir, I guess what I'm trying to kind of understand. And then maybe this requires a bit of crystal ball forecasting on your part. But if indeed, we're sort of in for several quarters of a slowing market and a softer housing market, how quickly do you think agents who are at kind of incumbent for brokerages, legacy kind of incumbent brokerage models might look to migrate to a platform like yours. I'm just curious like just the type of market where they will make a move quickly or might there be some lag and curious how you're thinking about all the independent brokerages out there that might be suffering or increasingly start to suffer, how maybe you guys go after those?

Tamir Poleg - CEO & Co-Founder, The Real Brokerage, Inc.

Yes, it is a good question. Agents are looking at alternatives all the time. When the market is hot and they're closing deals and they're serving clients, they don't have too much time to think about it, and they definitely don't have, I don't know, the mental capacity or again, the time to actually make the switch. I think that what will probably happen now is that a lot of people that have been weighing their options for a long period of time will be ready to push the button and switch over.

At the same time, we have to acknowledge that high-producing agents and high-producing teams are not making this type of decision overnight. So it's a process. They have to get very comfortable. They have to choose the right timing in terms of their existing transactions, their existing listings. So it's not something that happens over days or a couple of weeks. I think that if the market continues to be softer over the next couple of quarters, we will see significant change. And when I refer to change, I mean, people going from traditional brokerages to models like ours. But again, it's a process and it's not happening overnight.

Q: Okay. And then maybe on operating expenses, Michelle, kind of, I guess, excluding revenue share. It doesn't sound like you guys are -- I think you said you're not making any headcount reductions or anything like that. But just curious whether you're slowing any kind of OpEx growth maybe relative to what you thought you might spend entering the year on things like marketing or just general headcount. Curious whether you guys are maybe looking at the market kind of softening and maybe not having to build up as much kind of headcount capacity as much as you thought? Just kind of any color there on expense growth over the next few quarters?

Michelle Ressler - Chief Financial Officer, The Real Brokerage, Inc.

Yes, sure. I mean we remain cost conscious. We aren't really making -- we haven't made any additional investments in headcount in terms of just like support staff. And we don't plan to either. What we are investing in is top talent to sort of help us through this next phase. We're making strategic hires. But aside from that, we don't really plan to increase costs in any significant way.

Q: Okay. And then maybe just one last one on instant payments, Tamir. I was hoping maybe you could share an update on, I don't know, maybe what percent of the agents have either enrolled or have kind of raised their hand to participate? And then I think you mentioned a revenue number related to instant payments. Is that just the dollar value of commissions that would have been paid out to the agent if they hadn't been enrolled, but that you guys are now retaining as a function of them getting their checks a little bit faster? Just I wanted to clarify what you meant there.

Tamir Poleg - CEO & Co-Founder, The Real Brokerage, Inc.

Yes, I think that the number that I mentioned was the -- I mean if you look at instant payments as a, let's say, a commission advance, so the total amount of advances that we advanced to agents grew by 170-something percent. That's what I meant. Instant payment is still not open to all agents. On the dev team, we were -- we have a plan to open it up for teams and team leaders.

So team leaders can actually use this tool to provide advances to their agents or instant payments to their agents. We didn't get to that in the time that we wanted to get to that, that got pushed a little bit to Q3. I think that once we open instant payments to teams and team leaders, we will see a sharp jump in the usage. So it's growing. It's growing nicely. It's not open to all agents, but I do forecast that we're going to see a nice jump in the second half of the year.

Q: Okay, appreciate it. Thanks guys. Nice quarter.

Tamir Poleg - CEO & Co-Founder, The Real Brokerage, Inc.

Thanks.

Operator

Thank you. [Operator Instructions]. Thank you, ladies and gentlemen. This concludes today's event. You may disconnect at this time, and have a wonderful day. Thank you for your participation.