THOMSON REUTERS STREETEVENTS

EDITED TRANSCRIPT

RDFN.OQ - Q3 2018 Redfin Corp Earnings Call

EVENT DATE/TIME: NOVEMBER 08, 2018 / 9:30PM GMT

THOMSON REUTERS

CORPORATE PARTICIPANTS

Chris Nielsen *Redfin Corporation - CFO*

Elena Perron *Redfin Corporation - Head of IR*

Glenn Kelman *Redfin Corporation - President, CEO & Director*

CONFERENCE CALL PARTICIPANTS

Brent John Thill *Jefferies LLC, Research Division - Equity Analyst*

Heath Patrick Terry *Goldman Sachs Group Inc., Research Division - MD*

Jason Scott Deleeuw *Piper Jaffray Companies, Research Division - VP & Senior Research Analyst*

Jason Stuart Helfstein *Oppenheimer & Co. Inc., Research Division - MD and Senior Internet Analyst*

John Robert Campbell *Stephens Inc., Research Division - MD*

Mark Stephen F. Mahaney *RBC Capital Markets, LLC, Research Division - MD and Analyst*

Ryan McKeveny *Zelman & Associates LLC - VP of Research*

Stephen Hardy Sheldon *William Blair & Company L.L.C., Research Division - Analyst*

Thomas Steven Champion *Cowen and Company, LLC, Research Division - VP*

PRESENTATION

Operator

Good day, and welcome to the Redfin Corporation Q3 2018 Earnings Call. Today's conference is being recorded. At this time, I would like to turn the conference over to Elena Perron. Please go ahead.

Elena Perron - *Redfin Corporation - Head of IR*

Thank you, Nick. Good afternoon and welcome to Redfin's financial results conference call for the third quarter ended September 30, 2018. Joining me on the call today are Glenn Kelman, our CEO; and Chris Nielsen, our CFO. You can find the press release on our website at investors.redfin.com.

Before we start, note that some of our statements on today's call are forward-looking. We believe our assumptions and expectations related to these forward-looking statements are reasonable, but our actual results may turn out to be materially different. Please read and consider the risk factors in our SEC filings together with the content of today's call. Any forward-looking statements are based on our assumptions today, and we don't undertake to update these statements in light of new information or future events.

During this call, the financial metrics, unless otherwise noted, will be presented on a GAAP basis and include stock-based compensation as well as depreciation and amortization expenses. You will find reconciliations of non-GAAP measures discussed today to the most comparable GAAP measures in our earnings release. All comparisons made in the course of this call are against the same period in the prior year, unless otherwise stated.

With that, let me turn the call over to Glenn.

Glenn Kelman - *Redfin Corporation - President, CEO & Director*

Thanks, Elena, and hi, everyone. Redfin continued to gain share in the third quarter with revenue of $140.3 million, up from -- up 28% from the third quarter last year. In our core business of brokering home sales through Redfin agents and through other firms' agents working as our partners, revenues increased 22%.

Our net income was $3.5 million, down from $10.6 million in the same quarter last year. Our profits are seasonal, so we still expect to run at a loss for the year.

Our third quarter revenue was consistent with the guidance we gave you in August when we first reported that market-wide homebuying demand had begun to slow, especially in the expensive coastal markets where Redfin's presence is largest. Our earnings exceeded the range we set in August.

What's most important is that our share increased year-over-year by 0.14% in the third quarter, less than the second quarter's 0.19% gain, but similar to the first quarter's 0.15% gain. As we've emphasized in every earnings call, we've developed the discipline over a decade of ignoring market fluctuations in favor of a measure of how well we compete for the available buyers and sellers of homes. Our third quarter results support our thesis that offering better service at lower fees lets us take share at a steady rate.

Redfin's share gains were only slightly lower -- excuse me, slower in the third quarter than the second across all regions, though our national share gains were muted further still because we divide our own sales by total U.S. home sales, which shifted to regions outside the West. More than half our sales are concentrated in the West where volume market-wide declined 13% in September. We believe Americans' migration to affordable cities is a long-term trend, which complements Redfin's plans to grow most aggressively beyond our original coastal strongholds.

From the third quarter of 2017 to the third quarter of 2018, visitors to our website and mobile applications grew 19%, a slight acceleration from the second quarter's 18% year-over-year growth. Machine learning software personalized our site in new ways for each online visitor, leading to even faster growth and repeat visits and in a number of homebuyers contacting our agents for service.

The challenge has been in closing sales. We saw more data in the third quarter that our investment in personal service is increasing the level of engagement year-over-year between Redfin's homebuyers and our agents. Though offset by homebuyers' market-wide reluctance to bid on homes, these improvements in customers' contact and engagement rates will, we believe, make Redfin more efficient over time than any other brokerage, serving people from their first online listing search to a closed sale. We see this as the key to higher agent productivity, lower prices and higher gross margins. We measure engagement as the likelihood that a customer who meets a Redfin agent returns for a second meeting, usually to tour homes for sale. We lose more customers between the first and second tour than in any other step in the homebuying process. So the second tour has long been the point of attack for improving our customers' overall success rate.

In our last earnings call, we reported the first year-over-year engagement gain in 34 months, starting with the 1% gain for the customers we initially met in April. Those year-over-year gains increased in May, June and beyond, reaching a nearly 8% gain for the customers we first met in July and August. Even as homebuyers market-wide began balking at higher interest rates, our year-over-year gain in engagement was still 5% for September's customers.

Now we have to recognize that though Redfin has done the work to make our customers more committed to us, the market has made us commit -- customers less committed to buying a home, which is why we're being more careful about how many agents we hire for the 2019 homebuying season. We expect the average number of homebuying customers per agent to increase modestly next year, though the number of serious customers per agent may stay the same.

Our agents will be happy that these hiring limits give each one more opportunities in 2019 to make customers ready to buy a home. We'll still maintain the standards for personal service we set at the start of 2018, and new systems should help us execute even better: at connecting agents face to face with customers, at shifting more paperwork to our coordinators so agents can stand in front of customers, at managing the performance of agents with low customer success rates, and at rallying more customers to agents with high customer success rates.

Even as we let Redfin agents take on more demand, we also plan to increase demand through advertising. We believe online traffic will keep growing as will our base of repeat and referral customers, but there's an opportunity to grow faster. We expect mass media ads to increase growth rates modestly in 2019, assuming the housing market is more challenging than this year's but still relatively stable. Just as important, we believe that telling the world there's a modern way to buy or sell a home can increase customers' affinity for Redfin for years to come.

The basis for our plans to get the industry's highest return on advertising is the decade we've invested in differentiating our service. Other brokerages can advertise, but what can they promise potential customers when each agent at that brokerage sets their own service level and pricing? At Redfin, our listing agents charge about half the typical fee to sell a home. We set up additional marketing campaign for each listing and let each customer see the results online. We sell homes faster for more money. We use technology to get buyers into homes first and to make an offer first. We're the only major brokerage to employ our agents rather than relying on franchises and contractors, so we can organize the whole company around what's best for the customer. Our customer satisfaction scores are 50% higher than traditional brokerages. Our repeat rates are 69% higher.

But because home sales are infrequent, we can't just wait for one customer to tell another about our savings or our service. Compared to a 5% commission, our customers in 2018 will have saved more than $150 million in fees, an amount that will feel squandered if most people never find out about it. We know from our 2018 results that consumers respond to an ad about a 1% pricing for listing a home, but most just don't know about that pricing. In a May 2018 survey of thousands of homebuyers and sellers in the markets we serve, only 8% named Redfin as one of the first 3 brokerages that come to mind, up from 4% in December 2016. The highest awareness was where we've advertised the longest and have the highest listing share: in our hometown market of Seattle at 19% and in the Washington, D.C. area at 13%.

After 4 years of spending between $4 million and $13 million on mass media ads in 5 to 13 markets, we plan to spend $40 million to $60 million on mass media in 2019 across 20-plus markets. This will increase both the breadth and depth of our advertising. 8 to 10 of those markets will get mass media ads the first time. And the media in our 10 largest markets will have at least 25% more reach and frequency than in 2018.

Our big bet on mass media is the culmination of 4 years of experimentation with different ads, media, times of day and frequency, comparing sales between markets with advertising and similar markets without. We've now had time to compare the long-term sales growth of markets that got advertising back in 2015, to those markets that didn't get advertising until later or have yet to get it. The data is overwhelming. Mass media ads lift the market's long-term revenue trajectory over many years. What has been most reassuring to learn is that a craft that once seemed to involve branding voodoo and a Taco Bell-size budget, in fact, works best with the same data driven, cost-conscious approach we've taken with almost every other major investment. Our Chief Growth Officer over the past 4 years, Adam Wiener, is a former engineer who has built our marketing department to develop this approach into a competitive advantage.

Even as advertising accelerates Redfin's brokerage sales, we also expect growth from new businesses, starting with Redfin Now, our business of buying a home on our own account and then selling it. In the third quarter, this business grew 237% year-over-year. Demand has continued to exceed our expectations, but as a softening market has lowered the prices, we're willing to pay homeowners, offer acceptance rates have declined modestly. It's too soon to say how a buyer's market will affect consumer preferences for an instant offer or a brokerage sale. But we believe many homeowners who want to weight both choices, and that offering this choice will lead more owners to Redfin.

After our first quarter of investing in Redfin Now as a long-term business, we're still optimistic that we can expand now using much of the software and people already in place for our listing brokerage. Beyond our brokerage's network of agents, coordinators and contractors, our website reaches tens of millions of homeowners and homebuyers who could benefit from Redfin Now. And our software to help agents sell houses largely works the same when we own the home being sold. The ability to renovate homes is where we need to add major new systems and staff, which is what we're doing now.

Once we buy and renovate a home, we still bear the risk of selling it. Each of the 24 Redfin Now homes we sold in the third quarter got a price above what we paid for it. And we're now selling the 56 homes we owned at the end of the third quarter at a good pace. As Redfin Now grows and the market softens, we don't expect to sell every single home for a profit, as we have to manage a larger number of properties as a portfolio, where the goal is plenty more winners than losers rather than a perfect record. We'll keep running the portfolio in a disciplined way, balancing growth against risk and drawing on the lessons we slowly learned from the last 22 -- 21 months of buying, renovating, maintaining and selling houses.

Meanwhile, our title and mortgage businesses will, we believe, be another source of long-term growth. We account for these businesses along with licensing and advertising fees from the Walk Score site we got through an acquisition as revenue in the other category, which grew only 17% year-over-year in the third quarter. This growth has slowed because we've been less aggressive about building software for our title business, Title Forward, or expanding it beyond the mid-Atlantic states where Title Forward is based, even though Title Forward now accounts for nearly 5x the revenue of our mortgage business. As we release title software and benefit in 2019 from Title Forward's expansion westward towards Redfin's largest markets, we expect Title Forward's growth to accelerate next year, lifting growth for other revenues overall.

But we're still investing far more in our mortgage business. We're building our own loan origination system and planning over the next 5 years to reinvent how quickly and easily people can move from one home to another. This process now takes consumers 6 months and often costs them nearly 6% of their nest egg, but it should take 6 weeks. And when it does, people will be far less reluctant to move, to find better opportunities and a better life. Few real estate companies have embraced this entire problem with a website, a brokerage and businesses for mortgages, title and instant offers. And while the magnitude of this opportunity has created financial and operational strengths for Redfin today, it will, over time, let us compete in a level no other company can.

In the third quarter, the mortgage business grew more than 600% year-over-year, but this has largely been the result of expansion rather than increasing adoption within the market. Redfin Mortgage's challenges have been winning the confidence of Redfin's agents, who for years have recommended local lending partners to our homebuyers. We also need to increase revenue per loan through better pricing for jumbo mortgages. Already, the brokerage customers who use Redfin Mortgage are happier than the customers who work with other lenders. This may be one reason that without any marketing on our part, 1 in 5 of our September loans went to buyers who ended up working with an agent from another brokerage.

Now our mortgage advisers just need to make our agents happier, too. While our advisers may be more efficient working from Redfin Mortgage's Dallas headquarters, we believe they'll drive more adoption working side by side with our agents in the field. We are now hiring mortgage advisers in field offices, with a focus in one market on tripling adoption rate among our brokerage customers from its current level by the end of 2019.

Before turning the call over to Chris, let's assess the housing market. In our last call, we said that the market was weaker than most analysts realized, especially in high-priced coastal cities. Since then, rising rates and high home prices have caused buyers to become cautious industry-wide, a trend that we believe will continue, if not strengthen, at least through November. Our agents report that more customers are comparing their likely mortgage payments with rents, especially in markets like Seattle, Chicago and Denver, where many of the newly built properties have until recently been for rent, not for sale. September sales in Seattle, San Jose, Sacramento, Los Angeles and Orange County fell industry-wide 20% or more. Across the 88 markets that Redfin serves, the percentage of all listings that accepted an offer within 2 weeks of reaching the market was higher at this point last year than now. And the percentage of listings that dropped their price was lower last year, indicating that sales and prices are unlikely to strengthen.

Eventually, these price reductions, along with a wider selection of listings, will draw buyers back into the market. But buyers' immediate reaction has been to wait and see where housing lands. Real estate is one of the only markets where a store has a sale and shoppers run for the doors.

We'd be remiss not to tell our customers that running pell-mell for the door could be a mistake. It's possible that interest rates in the housing market would cause the economy to stagnate, leading to a year of lower sales and in some markets, lower prices. But if the economy stays strong to start 2019, buyers could come back to a market that still has relatively few homes for sale and face a new wave of bidding wars. In that event, some will wish they had been greedy when others were fearful. Regardless, Redfin will be ready.

This earnings call has told 2 stories, of a market at least in temporary retreat; and of a company with a widening competitive advantage. The discipline that lets us sell homes for more money at a lower fee is even more important now, and the true measure of that is our continued share gains. Take it away, Chris.

Chris Nielsen - *Redfin Corporation - CFO*

Thanks, Glenn. Third quarter results were mostly in line with our expectations. Our revenue came in near the top of our range, while net income was above the guidance we provided in August. Total revenue was $140 million, an increase of 28% from last year. Real estate services revenue, which includes our brokerage and partner businesses, grew 22% year-over-year. Brokerage revenue, or revenue from home sales closed by our own agents, was up 21% on 22% growth in brokerage transactions. Brokerage revenue per transaction was down 1%, as our transaction mix continues to shift from home buyers to home sellers. Revenue from our partner agents grew to 23% on a 7% growth in partner transactions. Revenue per partner transaction increased 14%, reflecting continued benefit from phasing out partner customer refunds at the end of last year.

For our properties segment, which consists of homes sold through our Redfin Now program, we record the entire value of a home sale as revenue. In the third quarter, our properties segment contributed $11.4 million in revenue, up from $3.4 million in the third quarter of 2017.

Our other segment, which includes mortgage, title and other services, generated revenue of $2.6 million, up from $2.3 million in the third quarter of 2017.

Gross profit was $42.3 million, up 8% year-over-year. Real estate services gross margin was 34.0%, down 410 basis points year-over-year and about double the percentage point decline we saw in the second quarter of 2018. As we indicated on our last call, this was largely due to relatively flat revenue in the third quarter compared to the second quarter, which puts additional pressure on our year-over-year gross margin.

The year-over-year decline was primarily driven by a 180 basis point increase in personnel costs, including stock-based compensation due to increased headcount, a 100 basis point increase in transaction bonuses, and an 80 basis point increase in tours and field events, each as a percentage of revenue.

For our properties segment, cost of revenue includes the purchase price, capitalized improvements, selling costs and commissions and home maintenance expenses. In the third quarter, properties gross margin of minus 2.7% was down from 1.1% in the third quarter of 2017, primarily due to a 140 basis point increase in personnel costs, including stock-based compensation due to increased headcount, a 120 basis point increase in our cost of properties and a 70 basis point increase in transaction bonuses, each as a percentage of revenue.

Our other segment had gross margin of minus 14.4%, up slightly from a minus 14.7% in the third quarter of 2017 as those businesses continue to scale.

Operating expenses increased 34% year-over-year and represented 28% of revenue, up from 27% 1 year ago. Our technology and development expenses grew slower than revenue, increasing 25% year-over-year as we continue to leverage our fixed costs.

Marketing and general and administrative expenses both grew faster than revenue. Our marketing expense increased 47% year-over-year on continued investments in advertising to drive greater brand awareness. General and administrative expenses increased 37% year-over-year, driven by increases in headcount and outside services related to public company operation and Sarbanes-Oxley compliance. Our stock-based compensation increased 103% year-over-year to 3.9% of revenue, up from 2.5% in the third quarter of 2017.

Our net income, including stock-based compensation and depreciation, was $3.5 million, down from $10.6 million in the third quarter of 2017. Diluted net income per common share was $0.04 compared with $0.50 diluted net loss per common share in the third quarter of 2017. The prior year loss was primarily driven by the fair market value feature of our redeemable convertible preferred stock, which converted to common stock in connection with our IPO. Excluding the impact of the redeemable convertible preferred stock, which is now converted to common stock, adjusted diluted net income per common share for the third quarter of 2017 was $0.12. Adjusted diluted net income per common share includes stock-based compensation.

Now turning to our financial expectations for the fourth quarter of 2018. Revenue is expected to be between $115.1 million and $118.3 million, representing year-over-year growth between 20% and 24%. We expect our properties segment to account for $15.0 million to $16.0 million of that revenue.

Net loss is expected to be between $18.7 million and $16.6 million compared with the $1.8 million net loss in the fourth quarter of 2017.

Our guidance includes approximately $5.9 million of stock-based compensation, $2.2 million of depreciation and amortization, $2.1 million of interest expense from the convertible note we issued in July, and $1.9 million of interest income. It assumes, among other things, that no additional business acquisitions, investments, restructuring or legal settlements are concluded, and that there are no further revisions to stock-based compensation estimates.

And with that, we'll open it up for your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from Heath Terry of Goldman Sachs.

Heath Patrick Terry - *Goldman Sachs Group Inc., Research Division - MD*

Wondering if you could sort of give us a little bit of a sense of where agent efficiency is at this point, and sort of if it's possible to disaggregate what you're seeing in agent efficiency in terms of the impact of the market versus the efforts that you have to improve agent efficiency through technology and training? And then particularly as you reflect on sort of the broader market, it's obviously being -- it's obviously a bit of a difficult environment for home sales in general. Do you have a sense here, especially given, Glenn, the history you've talked about of having in real estate and having been through markets, tough markets for housing before, sort of how you would characterize your outlook from here? Is this simply a function of higher rates and changes to the tax environment? Or is there maybe something more that we're seeing if you had to think about the factors behind all this?

Glenn Kelman - *Redfin Corporation - President, CEO & Director*

Sure. So first, agent efficiency. We try to disaggregate that in our comment about engagement rates. The sales cycle is going to lengthen in a softer market, and that is going to affect close rates, which is the most important factor in agent efficiency and gross margin. But if you look at engagement rates, which is just the likelihood that a customer who meets a Redfin agent is going to come back, that increased significantly. And we saw that increase continue even as the markets softened. And so that's why we said that customers are more committed to us even as they are less committed to buying a home. That tells us that if you were to exclude market factors, we would have increasing agent efficiency. And when you couple that with the fact that we are now going to step up customers per agent, we think there is some upside for us to become more efficient. It's just hard to account for how that will weigh against next year's sales cycle. And when you ask about whether this is just a temporary change driven by a rate shock, I think that is one plausible theory, but we also have to soberly account for affordability versus wages, even before rates went up, buyers were really struggling to figure out how they are going to buy a house in the expensive coastal cities. And since many of them were using stock and not their salary to do that, the stock market is fairly relevant to the housing market in those coastal cities. So once buyers adjust to interest rate increases and that becomes the new normal, I think it's quite possible that strong economy drives the real estate market forward. We come back to some level of normalcy and may be even bidding wars and all the rest. But it's just also possible that there is a more significant correction. And were ready for that. That's why we acted so quickly. I think we were early in saying that we see a problem in the market in our last call. Here in this call, we've already adjusted our hiring expectations for 2019. All that stuff we said in the IPO road show video and elsewhere about really being ready for hard times, being born in the dark, being tough, we're ready.

Operator

(Operator Instructions) Our next question comes from Brent Thill of Jefferies.

Brent John Thill - *Jefferies LLC, Research Division - Equity Analyst*

I guess when you think about the market now, do you think differently about the home buying market? Or does it give you more conviction that you actually need to go on more offense, given what's about to hit?

Glenn Kelman - *Redfin Corporation - President, CEO & Director*

We feel that our business model is built like a brick outhouse. It is solid. We have a significant cost advantage over our competitors. We can sell houses faster for more money at a lower fee, and that is going to become even more important over the next few years. So obviously, we want to be financially prudent. We have an employee model that is sensitive to changes in the cycle, but we're fundamentally confident about our ability to gain share. So the cycle is going to go with us and against us, but the competitive advantage, I think, will only widen. And I'm not trying to sound cocky, we have to take a change in the market really seriously, and we've tried to do that. But I do feel completely confident in the fundamental strength of our competitive advantage. We make our customers happier than other brokers, and that will serve us well in good times and bad. I think where you might see us a shift is we may shift some of the savings from sellers to buyers. In a really hot market, sellers naturally want a low price because they think any broker can sell the house. In a buyer's market, the buyers are the ones who may want more savings. We haven't made any commitments around that yet, but I think that's the first change you contemplate that affects how we actually price our service and serve our customers. It's just favoring the buyer instead of the seller as it becomes a buyer's market.

Brent John Thill - *Jefferies LLC, Research Division - Equity Analyst*

And maybe for Chris, just the comments Glenn's making on the doubling down of the branding. I know you're not giving guidance for '19, but it seems like next year's going to be a big investment year. And kind of how you think about the balance of trying to make money versus making the wrong -- or rather, the right long-term bets for the branding, can you just talk through the balance of that?

Chris Nielsen - *Redfin Corporation - CFO*

Sure. So as you said, we're not providing guidance on '19, but we did talk about the amount of mass media marketing spend that we want to make next year. And the way we think about that is we really do have a lot of conviction over what we've observed in the last few years from the long-term benefits of that kind of advertising. And so regardless of what are sort of slightly different market conditions we've been in the last few years, we believe that that's the right kind of investment to make to continue to build the business for the long run. And so that's what you see reflected there in our commentary there.

Glenn Kelman - *Redfin Corporation - President, CEO & Director*

And I apologize, I didn't directly answer that question to the extent that I should. I now realize what you're asking about. If we were only advertising for our result in 2019, I think we would be more careful about the timing. We certainly do want to see a result in 2019. And I think we'll be sensitive to which markets we advertise in, because there has been such shift away from some of the coastal markets. But we're advertising for long-term awareness gains. When I look back at how differentiated the product is, how much customer preference there is for it once customers have awareness, my main reaction is that we should have done this a long time ago. And I'm really glad that we're doing it now. So I think we will see modest improvements in 2019 growth rate over 2018 and longer-term significant benefits. So that's a good investment to make.

Operator

Our next question comes from John Campbell of Stephens.

John Robert Campbell - *Stephens Inc., Research Division - MD*

You talked -- in the past kind of managing the flattish brokerage revenue per transaction, but you guys clearly have some growing pressure from the slower trends in the top 10 markets. You guys battled against that pretty good this quarter. I think that was only down 1%. But just curious, can you hold that kind of flattish from here? Is there enough leverage you can pull to kind of keep that flattish?

Chris Nielsen - *Redfin Corporation - CFO*

Yes, we do believe that stays relatively consistent over time. It has bounced around from quarter to quarter based on mix by market. If you look at the average home prices we sold in the third quarter, for example, they were not up as much year-over-year as they were in the first and second quarter, so you can see that reflected there. But generally, that's the right expectation for you to have is that we hold those relatively consistent over the long run, with a little bit of variability quarter to quarter.

John Robert Campbell - *Stephens Inc., Research Division - MD*

Okay, that's helpful. And then, Glenn, you mentioned kind of slowdown in hiring pace next year. Can you first, I guess, talk to the degree of slowdown? You guys grew agents by 40% last year. So I'm guessing it's a good bit short of that. And then tacking onto that, I apologize if I missed this explanation, but what was the average lead agent count down sequentially?

Glenn Kelman - *Redfin Corporation - President, CEO & Director*

Well, we have some attrition, which is natural. And then we've been less aggressive about backfilling. Last year, we backfilled in the third quarter, because we were ramping up to deliver more personal service and we went beyond backfilling to increase the census. This year, we felt like we were already well staffed for personal service, and we have become concerned about whether there will be sales growth market-wide in the United States. So I can't give you a precise number, but it wouldn't have been 40% under any circumstances, even a strong bull market, because that was a onetime investment in changing the ratio between agents and customers. And then we're going to grow agent count slower than revenue would be our expectation for 2019, because we think that we can reap some returns on agent productivity, unless the sales cycle really goes haywire. There's always a chance that people stop buying houses almost entirely for a 2- or 3-month period, but those are really extreme markets. We saw that in 2008. We don't see anything like that on the horizon. So we think there is some upside in agent productivity, because our agents really have learned new habits around meeting customers, and we've built really good systems to drive performance and close rate. And we saw that in increased engagement in the back half of this year. And even though the sales cycle was lengthening because of these market-wide changes, we do think there's significant upside next year. So agent hiring is going to be fairly limited because of the market and because of our conviction that we can get more from our agents. It's also worth noting, they want to do more. They're ready for this.

Operator

Our next question comes from Jason DeLeeuw from Piper Jaffray.

Jason Scott Deleeuw - *Piper Jaffray Companies, Research Division - VP & Senior Research Analyst*

Just at the high level, can we just kind of think of the investments, the growth investments you're making in the business? Can we think of that as less investment in the agent count and more investment in the mass marketing? And the $40 million to $50 million next year, is -- I'm just trying to get a sense I mean, how much of that is incremental versus the marketing expense that you have this year?

Glenn Kelman - *Redfin Corporation - President, CEO & Director*

We spent $12 million this year. So the $40 million to $60 million next year is mostly incremental, and it's mostly to reach new markets. We've got a formula that we think works. It's fair to say that we're shifting dollars from an investment in agent hiring to the media expense. I view that as complementary, because every time we increase close rate, it lets us spend more to meet customers. When you pour water into a leaky bucket or a leaky funnel, you've really got to have the hose turned on high. But if we're better than anyone else at guiding a customer from an online visit to a closed sale, we can spend more on advertising than anyone else. So I think some of that engagement improvements that we've seen in the back half of the year have encouraged us that these improvements in personal service pair well with the investment in marketing.

Jason Scott Deleeuw - *Piper Jaffray Companies, Research Division - VP & Senior Research Analyst*

And then the fourth quarter net loss guidance, I guess is higher than I would have thought with the new -- but is there some marketing spend that's occurring this fourth quarter that's going to impact that number? Or is it gross margin? Just any help you can give us. I'm thinking about some of the expenses.

Chris Nielsen - *Redfin Corporation - CFO*

Sure. So typically, we don't run mass media in the fourth quarter and we're not planning to do that this year either. There is some marketing spend for online activity, but mostly you should think about that as being in proportion to what we've done in prior years. The biggest driver, I believe, of what you're seeing in terms of the net loss is just related to the top line volume. And there, what we reflected in the guidance is that the October numbers actually looked quite consistent with the revenue growth we had seen in the third quarter. But as we are now looking at bookings for November and December, the bookings growth is less than that. And so we wanted to make sure that we reflected to investors what we're seeing from a revenue book standpoint. And given that we've hired agents already and have staff in place, that puts pressure on the bottom line.

Glenn Kelman - *Redfin Corporation - President, CEO & Director*

Long term, we are going to limit expense growth outside of mass media to be consistent with revenue.

Operator

Our next question comes from Mark Mahaney of RBC.

Mark Stephen F. Mahaney - *RBC Capital Markets, LLC, Research Division - MD and Analyst*

I think I missed part of the call due to the technical problems. You talked about the size of the marketing commitment next year. Could you just repeat that? And how you came up with that size of kind of the brand, the mass marketing campaign, how you reached that level?

Glenn Kelman - *Redfin Corporation - President, CEO & Director*

Sure. It's going from $12 million this year to $40 million to $60 million next year. And the way we reached that number was by thinking about the markets where we could profitably execute a mass media campaign. So we have a template for what has been successful in the past. We've been fairly painstaking about experimenting with the right number of advertising points for TV, the right number of billboards and all the rest. And then we compared that to the profit that we get from different types of customers, which varies from market to market because houses are more expensive in California than they are in Nashville, Tennessee. So there's some cutoff where it just doesn't make as much sense, because all the customers we meet are just buying homes that don't yield much profit. And I think the other part of this calculation is we feel that this level of spending can remain relatively constant over time as revenue grows. So if we had a much larger revenue number 2 or 3 years hence, it's possible we have a larger mass media budget, but you wouldn't see the kind of increase that you just saw from '18 to '19.

Operator

Our next question comes from Ryan McKeveny from Zalman and Associates.

Ryan McKeveny - *Zelman & Associates LLC - VP of Research*

So one clarification, on the revenue growth for next year increasing, are you talking total revenue including properties? Or is that specific to just the real estate revenue line item?

Glenn Kelman - *Redfin Corporation - President, CEO & Director*

We weren't talking about properties, the Redfin Now revenue. That's sort of cheating, isn't it?

Ryan McKeveny - *Zelman & Associates LLC - VP of Research*

It is, which is why I asked. Thank you for that.

Glenn Kelman - *Redfin Corporation - President, CEO & Director*

I'm glad you asked. Just to be clear, we're doing this to increase the number of transactions we do year-over-year. And we've contemplated that we can do that even if the market's a bit soft. I think there's some markets where all bets are off, but we understand that it could be tough market next year, and we still think we can grow.

Ryan McKeveny - *Zelman & Associates LLC - VP of Research*

Yes, Glenn, that's helpful, and that kind of is my question. I guess the guidance for 4Q, I running some back of the napkin math, I think you're looking for something like 10% growth on the revenue, real estate revenue. So off of that base, certainly, meaningful acceleration to put the full year up in '19 versus '18. So maybe just a bit more on what gives you that confidence? I hear you on the marketing side of things, the mass media. But I guess on one hand, you're saying some of that is longer-term benefits for the investments. So can you help us think through that? What gives you confidence in that reacceleration in '19 versus '18?

Glenn Kelman - *Redfin Corporation - President, CEO & Director*

Sure. Just so we're both on the same page, we're not talking about accelerating from the Q4 rate. We're talking about accelerating from the overall 2018 rate. And it's just hard to spend that much money and not increase demand. We have been fairly conservative in our projections around how the business will respond to that increase in demand. And if we had 1 year of historical data, I'd feel much less confident, but we do have 4. And so it's a fool's errand to try to provide full year guidance in a cyclical business like real estate, especially when we make money from transactions and not subscriptions. So you're not going to get a high degree of precision here, but I do think there's a reasonable basis for concluding that we can accelerate this business, because we have seen consistent responses from consumers to our advertising, especially when we simplified the message to really be about our 1% listing fee. So not everything has to go perfectly next year for us to accelerate growth. Some things need to go well, a few things can go wrong, and we'll still make that, that number go through.

Ryan McKeveny - *Zelman & Associates LLC - VP of Research*

Got it. Very helpful. And the second question, you mentioned just the buyer's market and maybe shifting some of the savings from sellers to buyers, I guess the 1% listing fee, I sit here in Chicago. I see it on billboards, that time of year. I think it's a very powerful message. So I'm curious when you think about kind of shifting away from that, are there levers that you could pull outside of pulling the actual 1% listing fee, whether it's market minimums, et cetera? Just thinking how you balance that, because it's obviously a powerful message. I'm just curious if there's other levers to increase the seller fees without necessarily directly changing the 1%.

Glenn Kelman - *Redfin Corporation - President, CEO & Director*

Bundled pricing is the simplest lever where you can still give people 1% pricing, but it's based on buying other products. It's also possible that we will experiment with charging higher fee for our listings and more savings for buyers. Someone asked me to speculate on what, if anything, could change in our business if there's a really strong shift to a buyer's market. It's not as if I'm drumming my fingers on a pricing proposal that we just haven't told you about. By drawing on our experience from 2008 to 2011, we saw more savings shift to the buyer in that time frame, and it's possible that could happen again. So we're starting to get more speculative than we should for a Q3 earnings call.

Operator

And our next question comes from Jason Helfstein of Oppenheimer.

Jason Stuart Helfstein - *Oppenheimer & Co. Inc., Research Division - MD and Senior Internet Analyst*

So a bit more so, do you think would we see a lift in monthly average visitors as part of that marketing? Or visitors are captured in those numbers, and you'll see more in the conversion side? So just any thoughts there, what you've seen in the markets you've tested. Are there areas for investment in 2019? I mean, you talked about shifting money around. Are there any other areas where you're going to invest more? And then any thoughts about the outlook for Redfin Now for next year? I know that's hard, but any thoughts.

Glenn Kelman - *Redfin Corporation - President, CEO & Director*

So first of all, wait, what was the first question?

Jason Stuart Helfstein - *Oppenheimer & Co. Inc., Research Division - MD and Senior Internet Analyst*

The monthly average visitors.

Glenn Kelman - *Redfin Corporation - President, CEO & Director*

Yes, I knew the answer was no, but I couldn't remember the question. I'm so embarrassed. If we were advertising that our website had more listings, or that it was better in some other way, we would be focused on driving traffic gains. But we've been so focused on really advertising the brokerage that we don't see significant traffic gains. It's almost been surprising to industry experts who have tried to help us build a framework for evaluating advertising. They look at some traffic graph. They see when the ad ran. And it isn't a spike, it isn't a micro-spike. It's an anthill. So we don't see that traffic gain. Instead what we see is that people come to us and want to transact. Out of the millions of visitors that we have, getting an extra few thousand people who want to transact doesn't increase traffic, but it really makes a difference in revenue. The second question was about other investments besides mass media, mortgage would be the primary investment. That is a significant undertaking. Underwriting a loan involves a massive amount of paperwork. We're building our own loan origination system. We're obviously going to use some industry-standard components for pulling credit and assembling our financial documents. But we knew we were biting off a real chunk of work, but we think as we swallow it, the mortgage business is going to be significant. So we're going to continue to strain the P&L with that. Our goal has been to run fairly close to breakeven, excluding mass media, and still do mortgage, title and Redfin Now. And that's why people here work so dang hard, work so hard. What was the third question? Redfin Now. I just think consumers are really going to want the choice, but everyone's wondering how the merchant sales business, the instant offer business, whatever you want to call it, is going to perform in a different market. And if the market is down next year, one thesis is that I've met homeowners who are already angry when a listing agent says, "Your baby ain't that pretty. This house is going to sell for less than you think," and they're angry. And so presenting that in an offer as a check where we're the counterparty might increase their anger and we'd see offer acceptance rates decline. But there is another case to be made that they'll pay more for liquidity, that in anxious times, there will be a massive premium on that. And our first data on that was buried in the script. I don't know if you heard it but we saw offer acceptance rates modestly decline. I thought there was a possibility that they'd fall through the floor, that nobody would take our offer because we started pricing in significantly more risk into the offer in Q4. But people still pick us up on it, so it hasn't been a binary answer to your question.

Operator

Our next question comes from Tom Champion of Cowen.

Thomas Steven Champion - *Cowen and Company, LLC, Research Division - VP*

Question around the customer caps. It sounds like that's going a little higher next year. I guess I'm just curious if the housing market inventory is improving, does the cap still makes sense? I think that was part of the original rationale. And then, Glenn, I was wondering if you could talk about the progress with share of listings. You mentioned it a little bit last quarter. And maybe how to think about the timetable to be able to directly market to buyers on the website?

Glenn Kelman - *Redfin Corporation - President, CEO & Director*

Sure. So the cap still makes sense. It will seem like madness to us years from now, but there was a time at Redfin when an agent could have as many customers as he wanted. This is not an all-you-can-eat buffet. We have a brand to protect. We have customers to take care of. So even though we may be more generous with where the cap is, having the cap has actually just let us run this business better and balance productivity against close rate and growth. So that has been really good news. The other question was about listings share. Listings share has been good. You saw in Chris' commentary that we had a slight dip in revenue per transaction, because once again, listings were more popular than we thought compared to the number of buyers closing sales with us. I think there will be some pressure on listings growth next year, because we're going to start lapping the price drop to 1% in some of these markets. But in other markets, it's been there for a while and listings have still been growing. So I think the question is just going to be what kind of market we're going to be in and whether consumers are going to be as price-sensitive next year.

Operator

Our next question comes from Stephen Sheldon of William Blair.

Stephen Hardy Sheldon - *William Blair & Company L.L.C., Research Division - Analyst*

The first partner revenue held up better than brokerage revenue, both sequentially and year-over-year. I would have thought you'd maybe see a bigger slowdown in partner revenue in a period with some broader housing weakness, effectively keeping more business for yourself. So I guess how are you managing that mix, especially if you see kind of continued housing weakness over the next few quarters?

Chris Nielsen - *Redfin Corporation - CFO*

This is Chris. I think what you see reflected there is, as Glenn talked about earlier, we did have a set of measures in place to keep our agents from working with too many customers during the early part of the year and through the summer. And so that did have us introducing a set of customers to partner agents, and those deals closed in the third quarter. And so generally, I think your instinct is right about that change. And certainly over time, you can see that the percentage of transactions performed by partner agents has been headed down, just as we've continued to staff up on the brokerage side of the things.

Stephen Hardy Sheldon - *William Blair & Company L.L.C., Research Division - Analyst*

Got it. And then you've talked about this a little bit, but just as we're thinking about 2019 and the start of the next kind of key transaction season here in 4 to 5 months, I guess what are you watching for in regards to signs that headwinds are either getting worse or may be abating?

Glenn Kelman - *Redfin Corporation - President, CEO & Director*

I've been doing this for 13 years. You can't tell much about the next year at the end of the current year. You get a really strong signal in January and February. Starting after the Super Bowl, it should be on like Donkey Kong. We should start seeing early stages of demand. And if that doesn't happen, you know the markets in trouble. I will say that just listening to Chris, the market was significantly better in October than it seems to be going into November and December. We are not ending the year market-wide with a bang, but with a whimper.

Operator

And we have no additional questions at this time.

Glenn Kelman - *Redfin Corporation - President, CEO & Director*

All right, thanks, everybody. We'll see you next quarter.

Operator

Thank you all for your attention. This concludes today's call. All participants may now disconnect.
