Zillow edges toward profitability in 2017's first quarter

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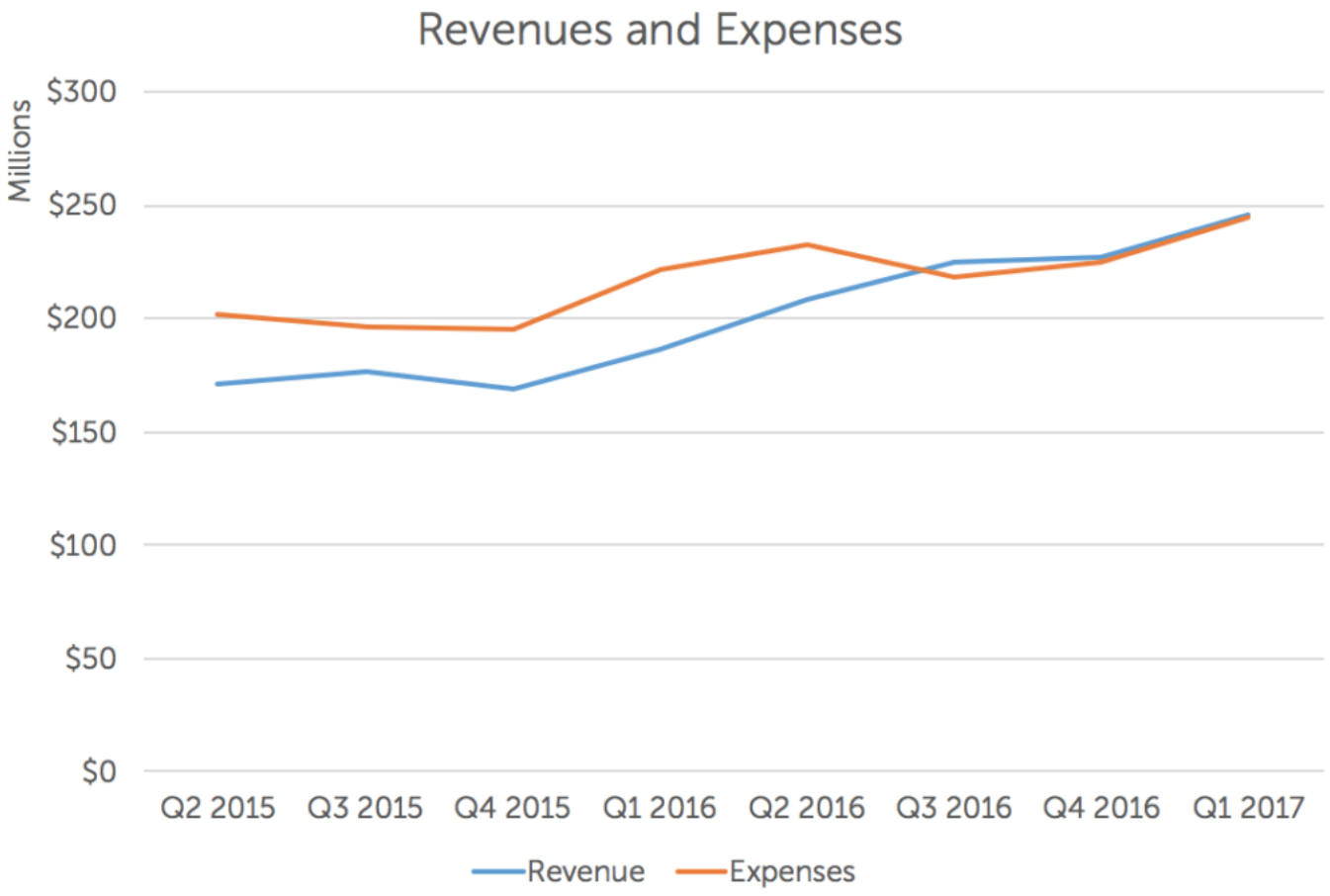
What's interesting in the Zillow Group results for Q1? Here are highlights, with charts and commentary. In a nutshell:

- Zillow continues to edge toward profitability, with overall expenses coming in line with revenue.
- Overall revenue growth is re-accelerating, matched by increased spending on sales and marketing.
- Technology-and-development spend has slowed considerably, contributing to slower overall expense growth.

First: The profitability chestnut. Cutting out all the noise for a moment (including stock-based compensation), let's focus simply on revenue and expenses.

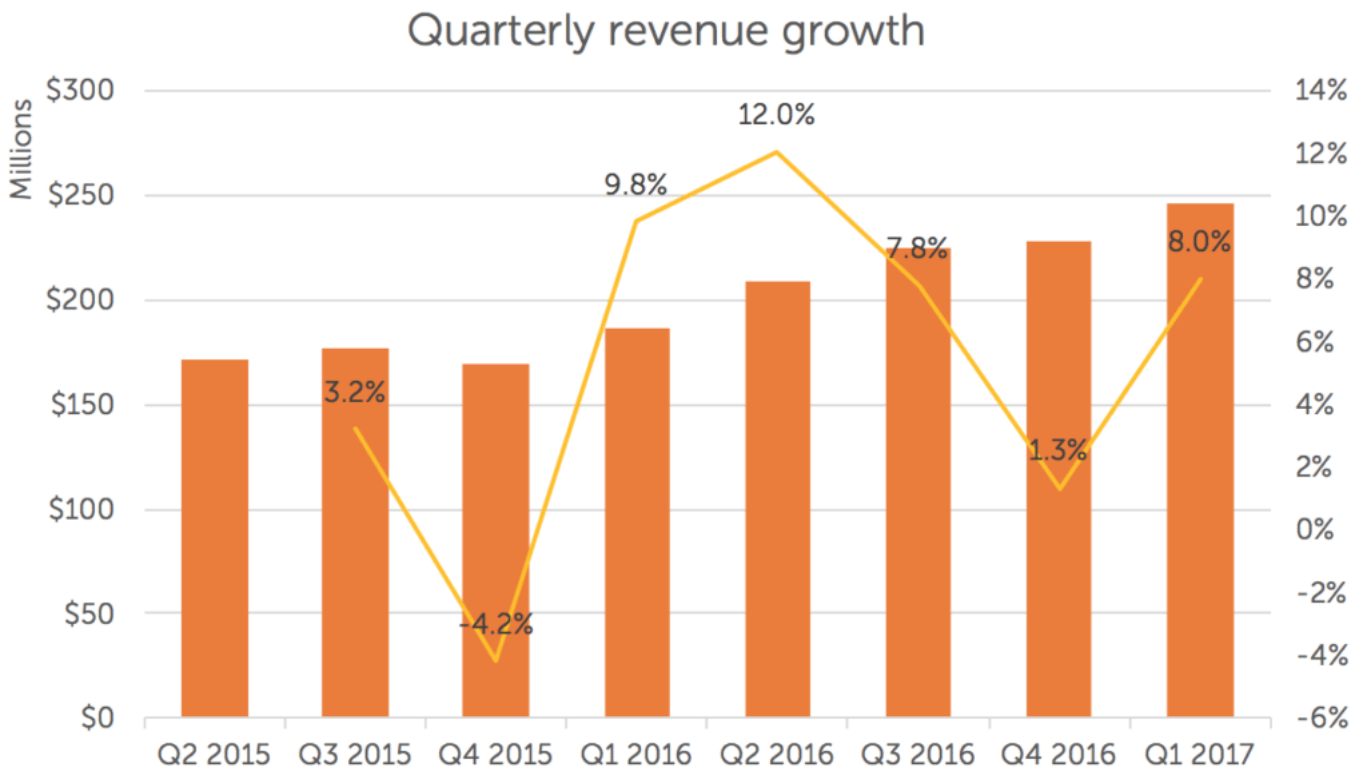
One of the biggest questions for Zillow is: Can it turn a profit?



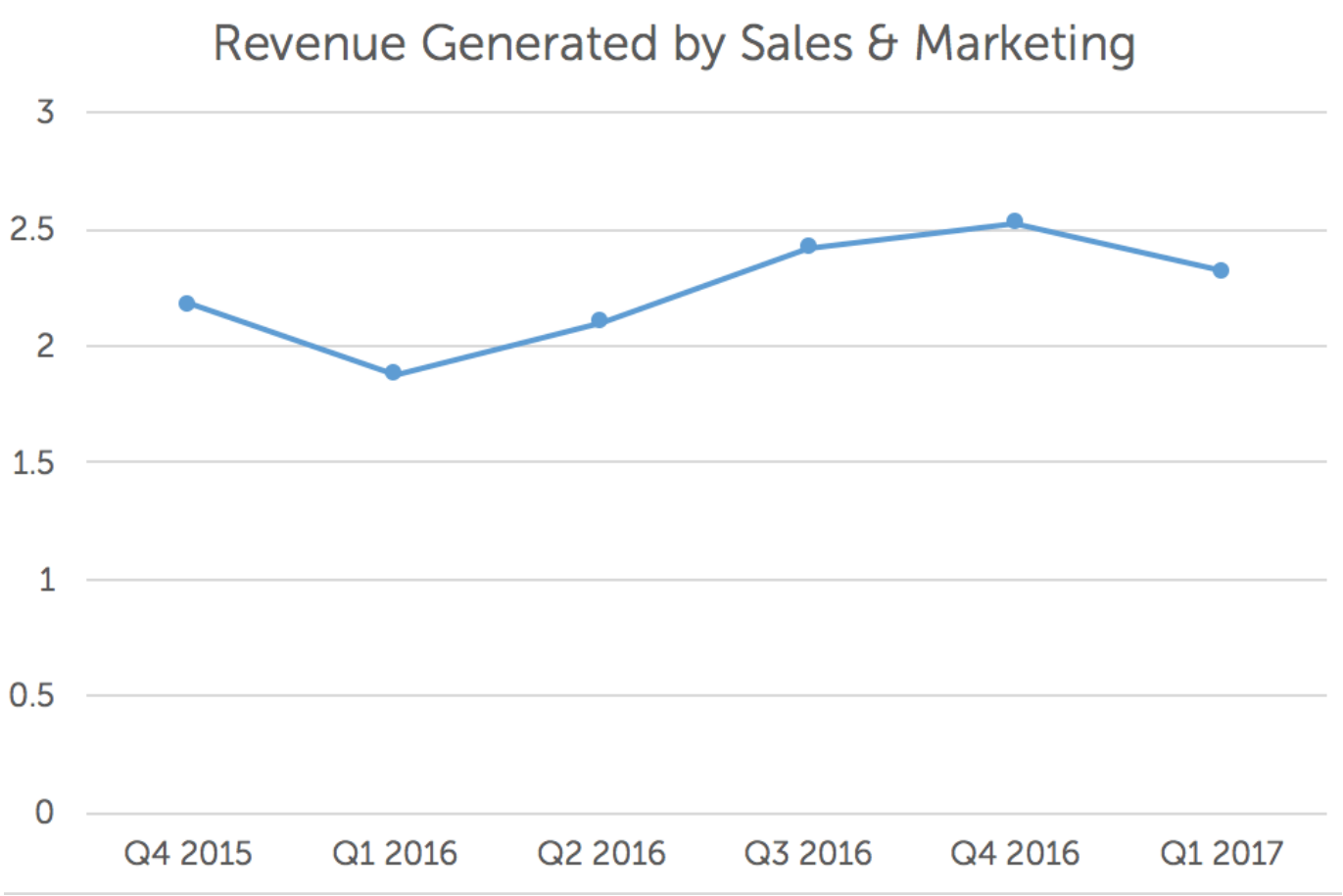
Zillow has lost millions of dollars during the past few years and has yet to turn a profit, even though it's on track to generate more than $1 billion U.S. in revenue this year.

So, any signs that give clues to whether Zillow can and will become profitable are quite relevant.

Zillow has done a good job over the past three quarters; expenses are finally matching revenue. Quarterly revenue growth has picked up steam as well, up from a relatively slow Q4. In Q1, revenue was up 8 percent from Q4, and 32 percent from Q1 in FY2016.



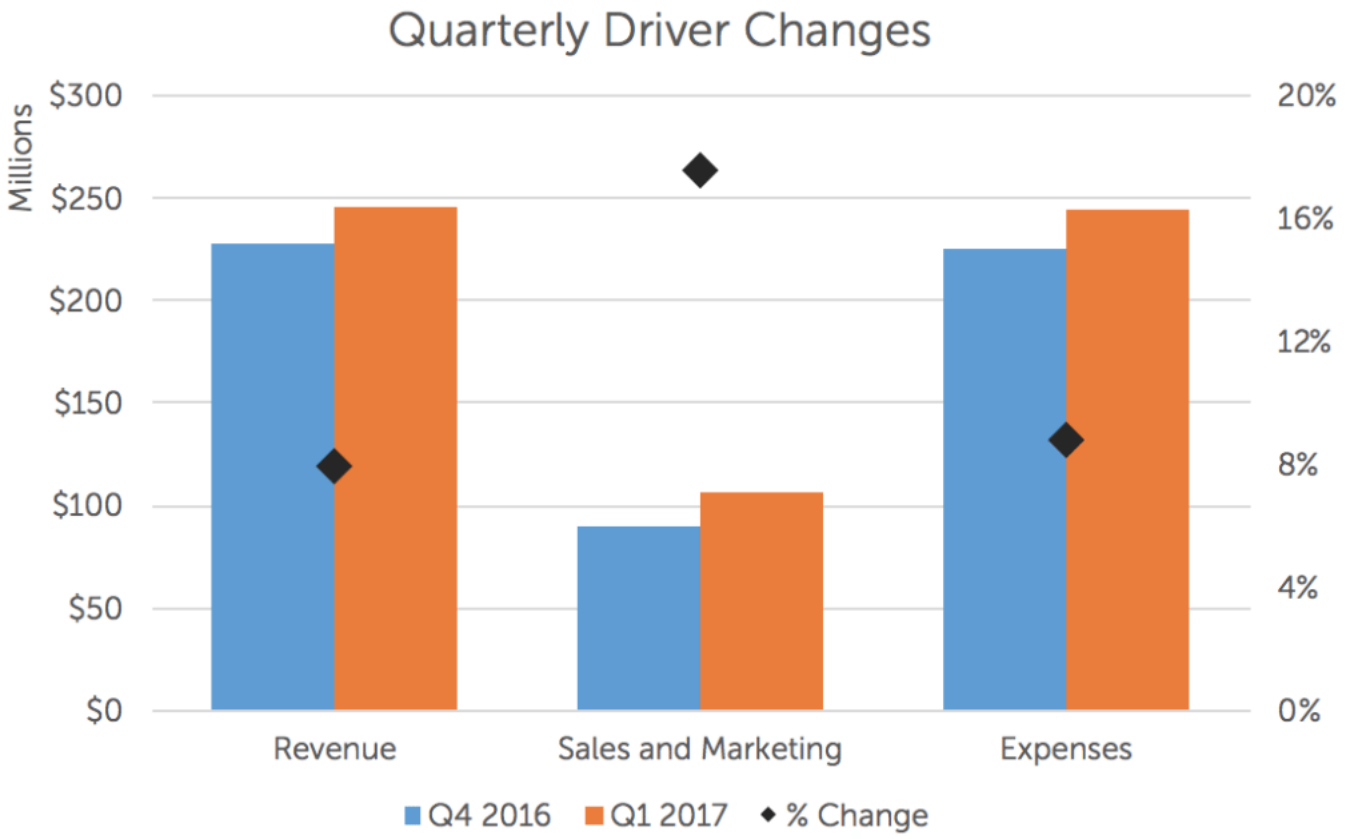
In particular, the sales and marketing expense is quite illuminating. While Q1 revenue was up 8 percent from the previous quarter, expenses were up 9 percent overall and the sales and marketing expense was up 18 percent.



In absolute terms, revenue was up $18 million U.S., expenses were up $19.7 million, and sales and marketing $15.8 million.

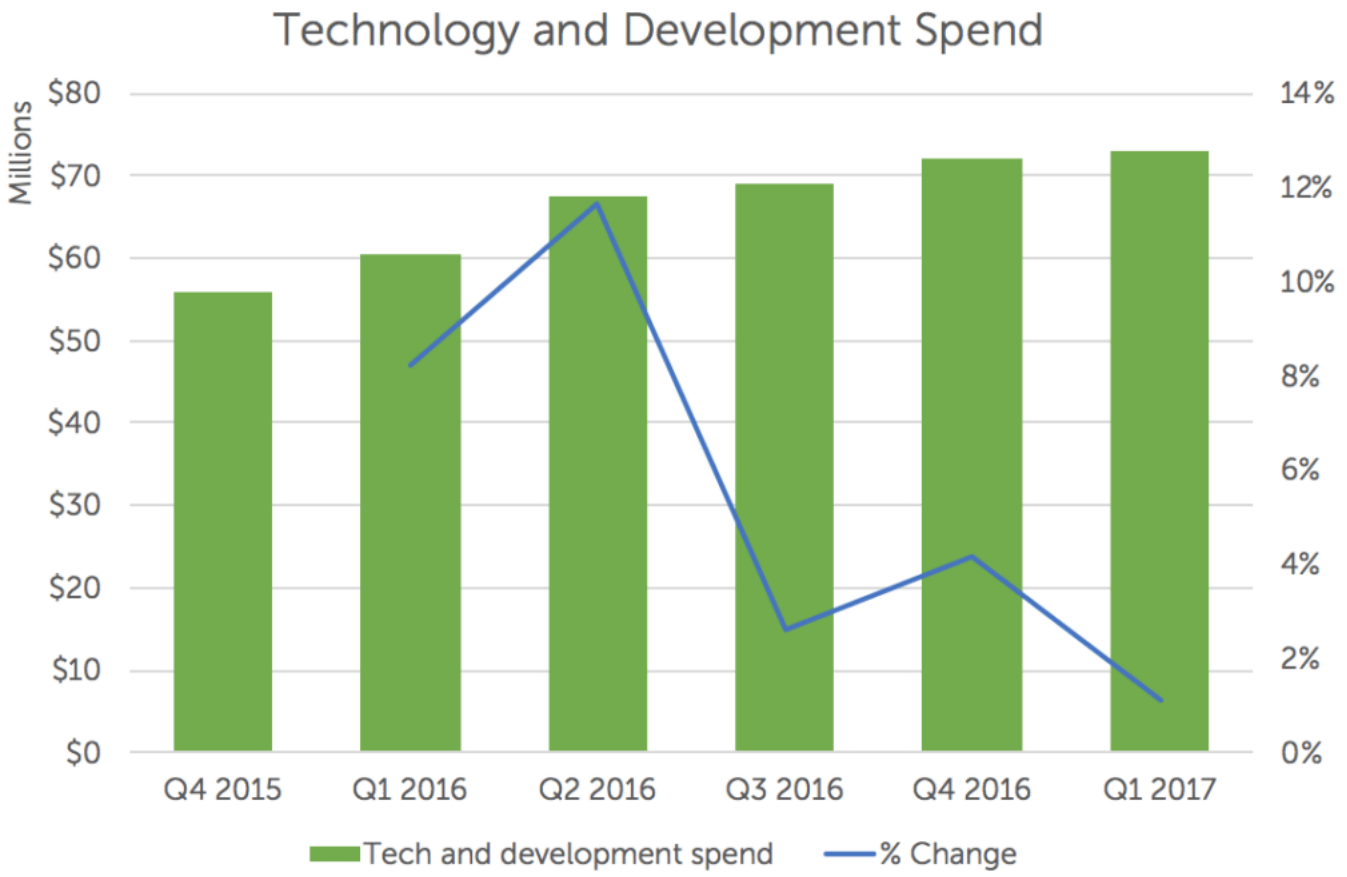
But, looked at over the past year, the story changes. Compared to the same quarter last year, revenue is up 32 percent, expenses up 10 percent and sales and marketing 7 percent.

Again, looking at year-over-year growth in absolute terms, revenue was up $60 million, expenses $22.6 million and sales and marketing up $6.8 million.



Looking further, we can see a rough proxy of how effective sales and marketing spend is in driving revenue. For the past several quarters, each dollar spent on sales and marketing generates from $2 to $2.50 in revenue. And it's slowly trending upwards.

There was a big increase in sales and marketing spend in Q1 of FY2017, so relative effectiveness has dropped slightly. But, overall it's a good direction to be heading in — upward, that is. Another interesting metric is technology and development spend. It's finally leveling off. In fact, it's flat when compared to the previous quarter.



Technology is surely a critical component of Zillow's consumer and customer proposition, so tech spend will always remain high.

But, if you're anxious for Zillow to turn a profit, the relatively flat growth is an important factor and a good signal.

Overall, it was a good quarter for Zillow. Not simply for the headline revenue growth, but for the drivers behind it, that signal a meaningful turn for the company towards sustained profitability.

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