ZILLOW GROUP, INC. Q3 2016 EARNINGS – PREPARED REMARKS
November 1, 2016

RJ Jones, VP of Investor Relations:

Thank you. Good afternoon, and welcome to Zillow Group's third quarter 2016 earnings conference call. Joining me today to talk about our results are Spencer Rascoff, Chief Executive Officer, and Kathleen Philips, Chief Financial Officer.

During the call, we will make forward-looking statements regarding future financial performance and events. Although we believe the expectations reflected in the forward-looking statements are reasonable, we can't guarantee these results. We caution you to consider the risk factors described in our SEC filings, which could cause actual results to differ materially from those in the forward-looking statements made on this call.

The date of this call is November 1, 2016, and forward-looking statements made today are based on assumptions as of this date. We undertake no obligation to update these statements as a result of new information or future events.

During the call, we will discuss GAAP and non-GAAP measures. We encourage you to read our earnings press release, as it contains important information about our reported and non-GAAP results, including reconciliation of non-GAAP financial measures.

In our remarks, the non-GAAP financial measure Adjusted EBITDA is referred to as EBITDA, which excludes other income, depreciation and amortization expense, share-based compensation expense, acquisition-related costs, restructuring costs, the gain or loss on divestiture of businesses, interest expense and income tax benefits.

This call is being broadcast on the Internet and is available on the Investor Relations section of the Zillow Group website, along with our earnings press release. A copy of management's prepared remarks has already been posted to the Quarterly Results section of our Investor Relations website. A recording of the call will be available later today.

Today, we will open the call with prepared remarks. We will follow prepared remarks with live Q&A. In addition to taking questions from those dialed into the call, we will answer questions asked via Twitter. Individuals may submit questions by tweeting @ZillowGroup using the #ZEarnings. I will now turn the call over to Spencer.

Spencer Rascoff, CEO

Thank you for joining the call today to discuss our third quarter 2016 financial results.

Zillow Group delivered strong third-quarter results that exceeded our expectations, and that demonstrated progress in executing our strategic priorities. Total revenue for the quarter grew 35 percent year-over-year to a record of approximately $225 million and exceeded the high end of our guidance range. The increase in revenue was driven by strong contributions from each of our marketplaces, but primarily from the Premier Agent business, which grew revenue 33 percent year-over-year to more than $158 million, also ahead of our outlook. On the bottom line, GAAP net income was $6.8 million, or 3 percent of revenue, and third-quarter EBITDA was $59.5 million, or 26 percent of revenue. Our profitability this quarter was well ahead of our expectations and an exception to our typical cadence of steady year-over-year margin expansion. The outperformance in profitability was primarily driven by strong revenue results and operating expense savings, which Kathleen will discuss in a moment.

As we entered the second half of 2016, we continued to gain momentum from the first two quarters. Total revenue growth has accelerated across our business throughout the year, and all our marketplaces are performing strongly. With just one quarter left in 2016, we are on track to deliver full-year revenue growth of better than 30 percent year-over-year. We are excited to finish 2016 strong, with a continued focus on our four strategic priorities.

1. Growing our audience size,
2. Growing our Premier Agent business,
3. Growing our emerging marketplaces, and
4. Attracting and retaining the best talent in the technology, media and real estate industries.

We are making great progress against each of those strategic priorities. Our audience across all of Zillow Group's mobile applications and websites continues to grow in an expanding category. Zillow Group's market share remained substantial as our traffic lead persisted. According to comScore, all five of Zillow Group's consumer brands combined represented nearly two thirds of the total online real estate category in September and nearly three quarters of the category on mobile only.[1]

Average monthly unique users for the quarter grew 16 percent year-over-year to more than 164 million, reaching a seasonal high point in July with nearly 170 million unique users. Traffic to the Zillow mobile apps and website hit a new record high, while traffic to the Trulia mobile apps and website grew steadily year-over-year and contributed meaningfully to Zillow Group's overall audience leadership. We are able to achieve these impressive audience numbers by building great products that consumers love, and then effectively marketing our brands through earned and paid media. This growth is a testament to our product, engineering and marketing teams' excellence.

[1] comScore Media Metrix Multi-Platform, September 2016, U.S.

Turning to our Premier Agent marketplace, revenue grew 33 percent year-over-year. The nation's best real estate agents – those who convert leads at high rates – are gaining transaction share in their respective markets as a result of advertising on Zillow Group's platform. Our Premier Agent program provides our advertisers with a tremendous opportunity to grow their business in the form of high-quality leads connected with software. During the third quarter, we delivered 4.6 million leads to Premier Agent advertisers across our brands' mobile apps and websites. This was an increase of nearly 40 percent year-over-year. As a reminder, the growth rate of leads is expected to normalize in 2017 when we begin comparisons to greater lead volume resulting from Trulia's traffic improvement in early 2016. That said, we expect the growth rate in leads will continue to be greater than the growth rate of unique users in the near term.

We recently announced the launch of exciting new features to our Premier Agent platform that will drive even more leads to our advertisers. In October, we launched our Seller Boost program, which is an ad product that connects Premier Agents with prospective home-sellers from Zillow and Trulia. Additionally, we launched the Premier Agent Direct program, which promotes our Premier Agent advertisers on Facebook. Buying ads on Facebook using Zillow Group's precision targeting allows real estate agents, teams or brokerages to expand the audience to whom they advertise through our simple platform.

Meanwhile, we continue to invest heavily in our Premier Agent app, adding important functionality for our advertisers with the goal of improving their lead conversion. Recent features include better lead routing and lead ingestion from other lead sources. The free Premier Agent app is rapidly becoming a full-featured business management platform which can handle all of an agent's, team's, or broker's workflow.

We have also started to roll out our self-serve account interface to Premier Agents nationally, with a goal of completing the rollout by the end of the year. After testing, and based on feedback and data from our advertisers, we now provide account management tools that enable our advertisers to independently control their budgets and impression buys. This flexibility and control strengthens our partnership with Premier Agents and facilitates their growth on our platform. This transition introduces some uncertainty in the near-term in regard to Premier Agent revenue, and we have incorporated sensitivity for this into our outlook for Q4.

We recently modified and extended our Premier Agent program to accommodate brokers' needs. The Premier Broker program allows brokers to purchase impressions and route leads to agents at their firms. We provide brokers with a tool to monitor performance of their agents through our Premier Agent app platform to ensure that leads are responded to within a reasonable timeframe. Including brokerages as Premier advertisers brings additional advertiser liquidity into our marketplace, provides consumers with better service, and improves our overall partnership with the brokerage community.

Turning now to our third strategic priority -- growing our emerging marketplaces including rentals, mortgages and New York City. We've been very successful here, and each of these emerging marketplaces is growing even faster than our core Premier Agent business. These newer marketplaces together will bring in annual revenue this year that's nearly three times larger than all of Zillow at our IPO five years ago.

Our Mortgages marketplace once again performed very well in the third quarter. Revenue grew 57 percent year-over-year and we are on track to exceed $70 million for the full year. In the third quarter, we completely overhauled the lender directory and the Mortgages ratings and reviews platform. Enterprises and individual loan officers now have more flexibility in managing the presentation of their profiles with consumer feedback on our mobile apps and websites, which is a big win for consumers and our lender partners.

Our Rentals marketplace once again experienced year-over-year revenue growth that exceeded 100 percent for the third quarter. According to comScore, the Zillow Group brands of Zillow, Trulia and Hotpads are now three of the top four brands in the rental category.[2] In addition to Premier Agent Direct, we launched a similar partnership with Facebook for rentals, which enables our multi-family advertisers to buy Facebook ads through us using our precision targeting.

Our New York City marketplace continues to grow rapidly across both of our New York brands -- StreetEasy and Naked Apartments. These platforms provide New York home shoppers and their real estate agents with accurate for-sale and for-rent listings from thousands of landlords and real estate brokerages throughout New York City. StreetEasy is testing a new lead product for open rentals, which are apartments marketed by multiple agents. Representing the first integration between the StreetEasy and Naked Apartments teams, this product brings new inventory to StreetEasy, creating a more comprehensive search experience of available New York apartments. It also helps agents connect with StreetEasy's unparalleled audience of New York renters. Both brands continue to generate significant PR in New York City, with StreetEasy positioned as the media's primary resource for New York real estate information.

Our fourth strategic priority – which is crucial to the success of everything we do here at Zillow Group – is attracting and retaining the best talent while maintaining our unique company culture focused on innovation. Our people and culture are key competitive advantages. We strongly believe that great people build great products, which in turn attract audience.

We dedicate significant resources and focus at Zillow Group toward creating an environment in which our more than 2,600 employees can do their best work. I am thrilled to say that Zillow Group employees continue to positively rate their experience working here in our regular anonymous surveys. In addition, I'm proud to report that Trulia employee reviews on Glassdoor are now at their highest level since the merger with Zillow, highlighting a successful integration. This positive feedback supports our efforts in attracting the best talent to Zillow Group so we can continue innovating in the online real estate media space. I'd like to extend my sincere thanks to all of Zillow Group's hard working employees for contributing to our ongoing success.

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[2] Zillow's custom-defined Rental Sites category ranking based on US Media Metrix comScore data, Unique Visitors, September 2016; Zillow Rental Network is the unduplicated reach of Zillow.com Rentals, Trulia.com rentals, HotPads.com, and MyNewPlace.com, Media Metrix Audience Duplication report, September 2016.

Now, turning to our outlook for the year:

We are raising our full-year 2016 revenue outlook range to $837 to $842 million and our EBITDA outlook range to $136 to $141 million, excluding the litigation settlement charge from last quarter. We are in growth mode and focused on our long-term strategy to drive audience and revenue growth along with steady margin expansion. Our long-term target of more than 40 percent EBITDA margin at scale remains intact.

As we approach 2017, we remain focused on growing our audience across all Zillow Group brands and delivering more high-quality leads to advertisers. To do this, we are investing heavily in our products – tools like dotloop and our Premier Agent app – to improve lead conversion and improve the efficiency of Premier Agents. As part of our disciplined approach to grow through investment, we will continue to deliver steady margin expansion over time. We will discuss our 2017 outlook further when we finalize our annual plan and report our full year 2016 results next year.

Agents and homebuilders are spending nearly $11 billion annually on advertising[3], and the portion of that dedicated to online and mobile advertising increases each year. In addition, our emerging marketplaces – Mortgages, Rentals and New York City – represent several billion more in online advertising spending that we've just begun to address. With that in mind, we are very excited about the future for Zillow Group.

I will now turn it over to Kathleen.

Kathleen Philips, CFO

Thank you, Spencer, and hello to everyone joining us on today's call. Let's dive into our financial results.

Total revenue for the third quarter increased 27 percent year-over-year to a record of $224.6 million from $176.8 million in the same period last year. Excluding Market Leader from last year's results, which was divested in the third quarter of 2015, total revenue increased 35 percent year-over-year.

Looking at our primary revenue category, Marketplace revenue was $206.9 million for the third quarter, an increase of 35 percent year-over-year. Excluding Market Leader from last year's results, Marketplace revenue increased 45 percent year-over-year. Marketplace revenue now accounts for 92 percent of our total revenue as compared to 87 percent during the same period last year. As a reminder, our Marketplace category includes Premier Agent, Other Real Estate and Mortgages revenue.

Zillow Group Premier Agent revenue increased 33 percent year-over-year to a record $158.3 million in the third quarter. The annualized run rate for our agent advertising marketplace reached $626 million at the end of the quarter, compared to $468 million at the same time last year.

[3] Borrell Associates 2016

We ended the quarter with 89,147 agent advertisers, a modest and expected decline from the end of the second quarter of 2016. For the third quarter of 2016, average revenue per advertiser, or ARPA, was $585, increasing 46 percent year-over-year. As a reminder, we will no longer report on the number of agent advertisers and ARPA beginning in 2017.

Revenue from same agent advertisers, or those who have been on our platform for more than one year, grew by more than 59 percent compared to the prior year. New sales to existing advertisers made up 71 percent of total bookings in the third quarter. Year-over-year growth of the agent advertiser cohort that spends more than $5,000 per month was 80 percent on a total dollar basis, and 79 percent in advertiser count. Churn in this cohort continues to be minimal.

We continue to support more agent teams and independent brokers who buy advertising at much higher levels than the average. We are accelerating the broader trend across the real estate agent population of higher-producing agents gaining market share from those who are less productive.

Third quarter revenue for our Other Real Estate subcategory grew 182 percent year-over-year to $28.8 million. Other Real Estate Revenue includes agent services, dotloop, StreetEasy, Naked Apartments, rentals and other offerings to our endemic advertisers that are not traditional display advertising.

Moving now to our Mortgages marketplace, our revenue reached $19.8 million in the quarter, which represents a 57 percent increase year-over-year. Average revenue per loan information request increased 191 percent year-over-year. Our strategic decision to improve the quality of loan information requests during the first quarter of 2016 by asking consumers to provide more details before a request is sent to a lender resulted in a 46 percent decrease of such requests year-over-year. We view this as a continuing positive trend, and these changes have increased consumer and advertiser adoption of mortgage advertising products that yield higher revenue.

In our Display category, revenue was $17.7 million, a decrease of approximately 25 percent over the same period last year, and within our expectations. Our intentional shift from traditional display advertising revenue continues, as we focus on providing consumers with personalized experiences that lead to valuable connections for our marketplace advertisers.

Moving now from revenue to our expenses. Total operating expenses were $216.8 million in the third quarter.

Taking a closer look at our operating expenses by line item:

Our cost of revenue during the quarter was $18.3 million, or 8 percent of revenue.

Sales and marketing expense was $92.8 million, or 41 percent of revenue. We continue to make strategic and opportunistic investments in advertising, which support the expansion of our audience leadership in the online real estate category.

Technology and development costs in the third quarter were $69.2 million, or 31 percent of revenue.

General and administrative costs in the third quarter were $37.7 million, or 17 percent of revenue, and lower than we had planned.

Moving on to our bottom line, GAAP net income reached a record $6.8 million, or 3 percent of revenue. GAAP basic and diluted earnings per share was 4 cents.

Our EBITDA for the quarter was $59.5 million, or 26 percent of revenue, well above guidance due to revenue outperformance and operating expense savings throughout the company.

Zillow Group ended the third quarter with more than 2,600 employees and approximately $445 million in cash and investments.

Now turning to our outlook for the fourth quarter and full year 2016. I encourage you to review our press release that was issued this afternoon. It is available on our investor relations website and includes detailed fourth quarter and full year 2016 guidance and related GAAP reconciliations.

Fourth quarter 2016 total revenue is expected to be in the range of $218 to $223 million. Premier Agent revenue in the fourth quarter is expected to be in the range of $161 to $163 million. Display revenue is expected to be in the range of $14 to $15 million.

EBITDA in the fourth quarter is expected to be in the range of $46 to $51 million.

For the full year 2016, we are raising our total revenue outlook to a range of $837 to $842 million and our Premier Agent revenue outlook to a range of $601 to $603 million. We also are raising our display revenue outlook to a range of $66 to $67 million.

EBITDA for the full year 2016 is expected in the range of $136 to $141 million. For illustrative purposes, this EBITDA outlook range excludes the impact of our $130 million June litigation settlement.

Our third-quarter performance was excellent and we beat all expectations for the quarter, including our own. We expect to end the year strong and will enter 2017 in an outstanding position to continue growing our business and audience share. Even with all of the progress we have made establishing Zillow Group as the leader in the online real estate category, there is still much opportunity ahead.

With that, we will now open up the call for questions.

After Question & Answer Session

Spencer Rascoff, CEO

Thank you very much for joining our call today. We wish you all a happy and healthy holiday season and look forward to giving you an update on our progress in February.

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Zillow Group's third quarter 2016 earnings press release is available on the Investor Relations section of the Zillow Group website at http://investors.zillowgroup.com/releases.cfm. It is also included as Exhibit 99.1 to its Current Report on Form 8-K as furnished to the SEC on November 1, 2016, which is available on the Investor Relations section of the Zillow Group website at http://investors.zillowgroup.com/sec.cfm and the SEC's website at www.sec.gov.

Forward-Looking Statements

These prepared remarks contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934 which involve risks and uncertainties, including, without limitation, statements regarding our business outlook, strategic priorities, and operational plans for 2016. Statements containing words such as "may," "believe," "anticipate," "expect," "intend," "plan," "project," "will," "projections," "continue," "business outlook," "estimate," "outlook," and similar expressions constitute forward-looking statements. Differences in Zillow Group's actual results from those described in these forward-looking statements may result from actions taken by Zillow Group, as well as from risks and uncertainties beyond Zillow Group's control. Factors that may contribute to such differences include, but are not limited to, Zillow Group's ability to successfully integrate and realize the benefits of its past or future strategic acquisitions or investments; Zillow Group's ability to innovate and provide products and services that are attractive to its users and advertisers; Zillow Group's ability to attract consumers to Zillow Group's mobile applications and websites; Zillow Group's ability to maintain and effectively manage an adequate rate of growth; the impact of the real estate industry on Zillow Group's business; Zillow Group's ability to maintain or establish relationships with listings and data providers; the impact of pending litigation described in Zillow Group's filings with the Securities and Exchange Commission, or SEC; Zillow Group's ability to compete successfully against existing or future competitors; the reliable performance of Zillow Group's network infrastructure and content delivery processes; and Zillow Group's ability to protect its intellectual property. The foregoing list of risks and uncertainties is illustrative but not exhaustive. For more information about potential factors that could affect Zillow Group's business and financial results, please review the "Risk Factors" described in Zillow Group's Annual Report on Form 10-K for the year ended December 31, 2015 as filed with the SEC on February 12, 2016, and in Zillow Group's other filings with the SEC. Except as may be required by law, Zillow Group does not intend, and undertakes no duty, to update this information to reflect future events or circumstances.

Use of Non-GAAP Financial Measures

These prepared remarks include references to Adjusted EBITDA, which is a non-GAAP financial measure not prepared in conformity with accounting principles generally accepted in the United States ("GAAP"). This non-GAAP financial measure is not prepared under a comprehensive set of accounting rules and, therefore, should only be reviewed alongside results reported under GAAP.

We urge you to review our earnings press release as it contains important information about our financial results, including reconciliation tables and related information about this non-GAAP financial measure. The earning press release is available on the Investor Relations section of the Zillow Group website at http://investors.zillowgroup.com/releases.cfm. It is also included as Exhibit 99.1 to our Current Report on Form 8-K as furnished to the SEC on November 1, 2016, which is available on the Investor Relations section of the Zillow Group website at http://investors.zillowgroup.com/sec.cfm and the SEC's website at www.sec.gov.

Adjusted EBITDA is a key metric used by our management and board of directors to measure operating performance and trends, and to prepare and approve our annual budget. Our use of Adjusted EBITDA has limitations as an analytical tool, which limitations are described in our earnings press release. You should not consider Adjusted EBITDA in isolation or as a substitute for analysis of our results as reported under GAAP.