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What's your house really worth?

How Zillow is turning online voyeurism into a real estate revolution. Fortune's Jeffrey M. O'Brien reports.

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(Fortune Magazine) -- This is what usually happens the first time you visit Zillow.com: You type in your address to check out the Zestimate, an approximation of your home's market value. It appears in a little pop-up superimposed on a photographic map of your neighborhood. The number might make you smile; it could make you angry.

Next, you realize that the information on your property is incomplete. What about the kitchen upgrade? Your new deck? The landscaping? All that work's gotta count for something. You've spared no effort to convince the assessor that your house is worth less than the official report, but now it's time to primp. So you tap in some modifications and watch your home's value rise.

Next, you check your neighbors' Zestimates. Then your childhood home, a best friend's place, your boss's house. Just as you open your address book in search of more targets, your spouse calls out from the bedroom, wanting to know what the hell you've been doing for the past two hours. "Nothing, honey," you say, shutting the laptop and trudging off to bed, caught red-handed in a loop of real estate yuppie porn.

If you haven't heard of Zillow by now, it's probably because you don't own a home. Or maybe you're just not as prurient and narcissistic as the rest of us. The national real estate market is in flux: Prices fell last autumn; new-home sales have risen for the past two months.

But what does that have to do with you? Zillow knows. With 52 million house valuations across the U.S., the site attracts as many as four million visitors a month. In less than a year since launch, the Seattle company has become one of the Internet's biggest real estate destinations. There are many listing sites on the Web, but Zillow is more of a media play. It makes money by selling ads to brokers, banks, contractors, appliance retailers and anyone else interested in reaching data-obsessed homeowners and -buyers.

And now the company is trying to create something even more ambitious: a perfect market for real estate. MixE*Trade, Craigslist and the Multiple Listing Service together, and you begin to get the idea.

A pair of disruptors

The two men behind Zillow, a pair of former Microsoft executives named Richard Barton and Lloyd Frink, don't exactly cut the image of moguls intent on upsetting a \$2.27 trillion industry. On the day of my visit to Zillow's headquarters, Frink, who's 42 and president of the operation, is wearing a Seahawks jersey and seems most interested in talking about football. And Barton, the company's 39-year-old chairman and CEO, couldn't look less threatening - put a pool cue in his hand and he'd be perfect in a Dockers ad.

But the two entrepreneurs know an industry in transition when they see it. They've placed \$5 million of their own money, \$1 million from early employees, and another \$51 million in venture capital on a bet that real estate is ripe for some good old-fashioned Internet



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Barton and Frink (not to be confused with "Barton Fink," the most excellent 1991 Coen brothers film) have had this feeling before. Thirteen years ago Barton convinced Bill Gates that consumers would benefit from a more transparent process of booking flights and hotel rooms. With his boss's backing, Barton launched Expedia, hired Frink, took the company public, and proceeded to massively disrupt the travel industry.

When Barry Diller bought the site for \$1.5 billion in 2003, the duo cashed out. They won't say how much they made, but let's just say it was enough to take some time off and figure out what to do next. (Nor will they say much about Zillow's finances, except that the company still has half of its VC money and that an IPO is probable, but not this year.)

Now they're taking on the wobbling, punch-drunk world of real estate. "When we were doing focus groups on Expedia, consumers would tell us they could hear the tap-tap-tap of the keyboard when talking to a travel agent, and they wanted to jump through the phone and look at the screen," says Barton, sitting in his office in the company's Seattle headquarters. "Expedia was about satisfying that impulse, and that's also what we're doing at Zillow. The hunger for information about real estate is infinite, at least among adults."

"There are a lot of parallels with Expedia and Zillow," adds Frink, who plays the technical guru to Barton's visionary. (Frink was hired by Bill Gates at 14 - not a typo - and his first big project was coding the DOS-based program Doodle.) "In the real estate industry you have tools and systems built for the professionals. We're trying to build something for consumers."

Until recently Zillow was read-only. But now Barton, Frink and their 133 employees are introducing new features to keep people coming back and, in the process, protect the site from downcycles in the real estate market. In September, Zillow opened the site to enable visitors to edit home records for everyone to see.

In December the site began accepting listings from homeowners and agents, and unveiled an intriguing feature called Make Me Move. Everyone has heard the heartwarming tale of the newlyweds who luck into a dream home while driving through an idyllic neighborhood. They get out of the car and slide a note under the door: "If you're ever interested in selling, we can offer you x. We promise to love your house. Please call." Two days later an elderly woman phones to tell the couple their timing was impeccable and the price is right. The couple buys the home, raises a family and lives happily ever after. Make Me Move - which, as it sounds, lets Zillow users post the figure that would cause them to pack up and go - is intended to make that fairy tale a lot more common.

We all have our price. Judging by some of the Make Me Move listings that have cropped up in a few months, that price is often ridiculous. But Zillow officials say the average Make Me Move figure is just 17 percent over the Zestimate. That's a relatively modest premium, so users are clearly taking the feature seriously. Which got me thinking. My wife and I have entertained thoughts of moving. We're not restless enough to go through the stress of interviewing agents, listing our home and opening it to visitors. But if someone made the right offer, sure.

I've paid attention to the market since we moved into our 101-year-old two-bedroom, two-bath Victorian in San Francisco, so I had an idea of what our house could sell for. I looked at the Zestimate, sized up my place against comparable homes, factored in the hassle of finding a new place to live and came up with my own Make Me Move figure. Sure enough, it was pretty close to 17 percent above the Zestimate. Not wanting to sell myself short, I nudged it up and put my house on the market in the most passive-aggressive way possible. All in the name of research. My price? A cool \$1 million.

A transparent market

The real estate industry is based on what economists call information asymmetry, which simply means that one party (typically the seller) knows more about a product than the other (the buyer). It's an opaque market that encourages obfuscation and leads to flawed pricing.

The big idea behind Zillow is to make real estate more like a stock exchange, a transparent market where all information about every property is readily available, and as a result pricing is perfect. The problem with building such a system, Barton explains, is that "the best information about the real estate market is locked up in people's heads. It's happening in conversations in backyard barbecues."

For a buyer, the best way to root out the true value of a property is to tap into that communal knowledge, interviewing neighbors about how well the home has been cared for, barking dogs, loud buses, crime, buzzing power lines. For a seller looking to price a home properly, the key is knowing how many people showed up at every nearby open house for the past six months, analyzing overbids and price reductions, knowing the average time on the market and walking through every comparable home that has sold recently.

Doing all that legwork is unrealistic, of course, which is why we use agents. If Zillow does what Barton and Frink say it will, however, all that information will be as readily available as the number on the mailbox.

numbers to Zillow.com, when they wouldn't even be willing to accept a cookie from my Web site."

The blogger, who claims to oversee interactive technology and marketing for a large unnamed commercial real estate agency, sees trouble ahead for his business. "He who holds the primary customer relationship controls the customer," he says. "From that perspective, Zillow is well poised to control the customer."

Both founders have heard this type of angst endlessly, and they swear they're not trying to obliterate the middleman. (They're much more intent on stealing one of the last great cash cows of newspaper advertising - like Craigslist with a profit motive.)

"At Expedia we were the agent," says Barton, whose mother was a real estate broker. "With Zillow we're not. There's speculation that we're going to charge commissions and sell houses. That is not what we're doing." He goes on to say that a broker is less like a travel agent than an attorney. You have access to every bit of legal information that a lawyer does, but none of the training - would you really choose to represent yourself?

It's clearly in the company's short-term interest to maintain the current power structure. Brokers, agents and developers spend upwards of \$8 billion in advertising a year. By 2010 a greater percentage of that money will go to the Internet than to newspapers, according to the media consultancy Borrell Associates.

So Frink spends his time convincing the professionals that their ads on Zillow will attract new clients. "If you have a good agent, they'll say, 'I know about the barking dogs,'" says Frink. "If we can get the agents to share that kind of information with the public and they get a benefit from it, they'll get more clients and gain more trust."

Agent outreach

For the most part, Frink's outreach seems to be working. The site is getting more ads from agents every day, and the National Association of Realtors is sold on the concept. "Zillow is lighting up the imagination of consumers, getting them engaged in the real estate process. If you're marketing anything, it's good to have an interested user base," says Mark Lesswing, a senior vice president at NAR. "Many realtors don't fear Zillow anymore. They use it as a way to show how their services are more valuable than something you can get for free on the Web."

If Christopher Guest ever films a mockumentary about real estate agents, he could do worse than to make the trip to Phoenix and get a load of Brett Barry. With a George Michael beard, bleach-white teeth, perma-tan and a smattering of gold jewelry, Barry darts around his office in a strip mall, his face lighting up whenever another human comes within shouting distance.

Specializing in a planned community near Scottsdale, Barry lords over his territory in a canary-yellow Porsche Boxster whose vanity plate reads SAYSOLD. "It's a realtor thing," he says, half apologizing for, half drawing attention to his chariot. Locals tell me today is the coldest day of the year in Phoenix, but that doesn't dampen Barry's enthusiasm. "Let's put the top down!" he calls out as we get in the sports car for a tour of his domain.

Barry is skeptical of Zillow's valuations, especially in a market like Phoenix, where so many properties are languishing. If the Zestimates are based on sales, then Zillow is missing a whole lot of data. He points at a stack of pages from the MLS (for Multiple Listing Service, the nationwide database of properties for sale). "Look, 213 days, 353 days, 529 days," he says, referring to how long each house has been available. "There's a lot of fat in the market. Prices are still too high."

For any homeowner looking to sell, it's a gloomy message: These are the worst of times. Not long ago, Phoenix was the nation's fastest-growing market. The median price rose 55 percent in 2005. Agents were closing deals on the hoods of cars; investors flipped homes without ever moving in.

Fast-forward to early 2007: Throw a rock in any direction, and it'll bounce off a FOR SALE sign. "There are 45,000 listings in the Phoenix MLS, and that number hasn't changed in six months," Barry says as we cruise among lookalike stucco homes. With every passing week, the number of houses on the market rises, increasing the downward pricing pressure. "It's like a freeway pileup."

But Barry's not glum. The way he sees it, his services are even more valuable in a down market. (He says he made \$100,000 more last year than in 2005, the height of the boom.) And he's taking me along on his rounds to show me why that's true. At each place he quickly identifies shortcomings, punching numbers into his cell phone calculator and revealing that a house is overpriced by \$25,000, \$40,000, \$90,000.

Scouting trips like this one give Barry valuable knowledge. Same for the kibitzing he does with fellow agents, telling stories, listening to

repeatedly ranked in the top 1 percent nationwide.

And yet even Barry has problems persuading clients to follow his advice. Homeowners too often become emotionally attached to the price they could have fetched at the top of the market - especially if they've taken home-equity loans.

"You look out on the street and see five to ten houses for sale, but many people still don't believe things have changed," he says, shaking his head at a dirty carpet. "The average seller says, 'I need to get this much out of our house to move up.' But the market doesn't care."

By giving consumers real-time updates on the value of their homes, Zillow intends to improve the dynamic between homeowners and agents like Barry. "We're going to change the nature of the communication," says Frink. "When real estate agents are talking to clients, it's going to be more of a two-way conversation."

Improving accuracy

The first step on that road is improving the accuracy of the Zestimates. Overall, Zillow has Zestimated the value of 57 percent of U.S. housing stock, but only 65 percent of that could be considered "accurate" - by its definition, within 10 percent of the actual selling price. And even that accuracy isn't equally distributed.

For example, 85 percent of homes in Los Angeles have Zestimates, and two-thirds have been accurate. But only 53 percent of homes in metropolitan New York have Zestimates, and only half of those are accurate. In Louisiana, where one in 50 homes is listed on Zillow, the site is just about worthless. (In at least one case, questions about Zillow's accuracy have taken on a political charge: A community activist group, the National Community Reinvestment Coalition, accused the site of discriminatory valuations in minority neighborhoods. "A lot of people have thrown rocks at us," Barton says. "Have we been sued yet? No, but I'm sure we will be.")

Squirreled away five floors below Barton's office, the company's VP of data and advanced analytics, Stan Humphries, is trying to improve those percentages. Each night his formulas churn through two terabytes of data, comparing every home with similar nearby properties and factoring in newly reported sales.

"When you want to see comparable homes - when you ask, 'What homes are like this house?' - realtors do that with intuition," Humphries says. "We do it with machine learning. You can infer information. If one house always sells for more than everything around it, we might be able to infer that it has a view. This is a really hard problem to solve, but at some point in the next year we are going to produce valuations that people are going to be completely stunned by."

Barry remains dubious. Zillow has Zestimates for 99 percent of all Phoenix homes and claims that 72 percent are accurate to within 10 percent. But Barry tells of a family who recently came to him believing their home was worth a lot more than it was. Zillow told them it would sell for \$505,000; Barry and another agent each independently put the figure at \$440,000. He doesn't discourage clients from looking at Zillow, but he definitely suggests they take the numbers with a grain of salt. "It's a tool," he says dismissively. "These folks said they looked at Zillow, but after seeing the Zestimate, they knew they wanted someone with knowledge of the area to see their house."

Finding the fairy tale

Back to my million-dollar pricetag. By now, it's early January, almost a month since I first visited Barton and Frink in Seattle. I haven't heard a peep about my Make Me Move price, and suddenly, just as I'm wrapping up this article, an e-mail hits my in-box. It reads, "Hello, we are neighbors of yours, looking to buy a home in Potrero Hill. In an effort to not waste your time, we are wondering if your million-dollar price quote is at all flexible. We are able to buy in a range close to there, but not quite there. Thank you very much in advance for your time."

Whoa. Now what? My wife and I discuss whether we have any wiggle room and decide that the first order of business is to call the woman and see if she's serious. The following morning, that's what I do. She is. As it turns out, the potential buyer and her husband are perfectly suited to play the role of the house-seeking couple in the fairy tale. They love the neighborhood and have been frustrated by their inability to buy. With the help of an agent, they've made three offers in three years, only to be outbid each time. Oh, yeah, and she's pregnant. They want a place to raise their family and are sick of going through the usual routine. "I've seriously considered putting a note up at Farley's," she says, referring to the local coffee shop, "or writing a form letter and putting it in mailboxes."

She's been a fan of Zillow since she found the site several months ago and immediately identified Make Me Move as a great way to draw a bead on houses before they go up for sale. Scouring the site, she found six pricetags in my neighborhood and inquired about mine and one other. As soon as she talked to the other guy, he decided it would actually take more to make him move after all, and he chickened out. I remain convinced that my number is fair. But she can't get there.

sure how much he's really worth. "We're doing 95 percent of the looking and all the legwork. He really just comes in when we're ready to make an offer," she says, adding that she'd be nervous about not having a pro to see the process through to the end.

Ultimately, the buyer and I decide to chill, think about how we could make the transaction happen, and pledge to strike up the conversation anew in the spring. Which is fine by me. With a buyer on hold, I'm able to begin scouting a dream property for my family. Just five years ago such a search would have started in a newspaper and ended in the office of an agent, where we would have probably competed with dozens of other bidders. Today I might be able to hop on Zillow and buy a house that's not even on the market - without dealing with open houses, bidding wars or buyer's remorse. Or even an agent.

In an opaque market, where the closest approximation of the value of a home lies in the head of a knowledgeable broker - say, Phoenix circa early 2007 - an agent can easily be worth the standard 6 percent commission. But in a perfect market, where the true value of a home is crystal clear to all parties and the fairy-tale note on a napkin comes in the form of an anonymized e-mail, 6 percent begins to look an awful lot like a luxury. Kind of like a canary-yellow Porsche.

Doris Burke contributed to this article.

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