

The Real Reason Google Paid \$3.2 Billion For Nest

The potential market for its products could be big, like really big

By [Verne Kopytoff](#) Jan. 14, 2014

- o [Facebook](#)[Twitter](#)[Tumblr](#)[LinkedIn](#)[StumbleUpon](#)[Reddit](#)[Digg](#)[Mixx](#)[Delicious](#)[Google+](#)[Google](#)'s ambitions are almost limitless, as it has proven time and again over the years. The company has pushed far beyond its roots in web search into [smartphones](#), [self-driving cars](#) and [robots](#). Even more is in the works.

On Monday, Google said it would [pay \\$3.2 billion to acquire Nest Labs](#), a maker of sleek Internet-connected devices for the home that are controlled with a smartphone. Nest's first two offerings, a thermostat and a smoke alarm, put a sci-fi twist on products that have barely evolved in decades. With the acquisition, Google gets a toehold in connecting all kinds of household devices to the Internet. The connected home, as its known, is shaping up as the next critical battleground in the technology industry, much like smartphones and tablets have been for several years.

"Google wants to be the connective tissue for all the devices and all the services in our lives," said Jan Dawson, an analyst for Jackdaw Research.

The vision is to turn homes into something not entirely unlike "The Jetsons." Ovens, refrigerators, crock-pots, door locks and light switches would all be tied to the Internet. Homeowners would be able to control everything using an app, no matter where they are. Imagine turning on the oven from work so that dinner is waiting when you get home or letting the maid in the front door while on relaxing at the beach. [Connected homes](#) are expected to make for a huge market. Sales of the technology are expected to pass \$40 billion in the next five to seven years, according a Gene Munster, an analyst for Piper Jaffray.

Technology companies including Google, Intel and Cisco Systems are serious about capturing a piece of the market. So are telecommunications giants like AT&T, appliance manufacturers Honeywell and GE along with firms that install home security systems like ADT.

But the race is not just about selling fancy appliances. It's also a fight for which company coordinates smart homes and collects data about the habits of those who live inside. Internet companies like Google are trying to learn as much as they can about [consumers](#) to better target them with

advertising. Knowing what people do at home—whether they cook a lot or when they leave for their job—could add a new dimension to personalized ads beyond what can be learned from their use of desktop computers and smartphones.

Tony Fadell and Matt Rogers, two former [Apple](#) engineers, founded Nest in 2010 as a company focused on reinventing “unloved” household products. Their start-up had gained a strong following among Silicon Valley insiders, although it had yet to crack the mainstream market. With Google’s deep pockets, Nest will be able to more quickly expand product development and its international business. After Google takes over, Fadell will continue to run the business under the Nest brand. “With their support, Nest will be even better placed to build simple, thoughtful devices that make life easier at home, and that have a positive impact on the world,” Fadell said in a statement.

Nest, which is privately held, hasn’t disclosed its revenue or product roadmap. But its sales are suspected to be relatively small, and at least for now, insignificant to a company of Google’s size.

Privacy is a big concern with Google’s acquisition, especially with the breadth of information that Nest devices can collect. Nest’s thermostat uses sensors, historical settings and algorithms to infer when people come and go. To address privacy concerns, Nest said that its privacy policy limits the kind of personal information it will share with Google. But the past has shown that privacy policies can be tweaked and that customers can be asked to share information voluntarily so that it can be combined with data from other products.

Nest is not Google’s first foray into the connected home. But those efforts have failed to catch on. Google tried to recruit developers to use its Android software for controlling connected devices without much luck. It also announced plans to build a connected light bulb with a partner company, but nothing has so far been made public.

Google has left a bigger mark in hardware through its \$13 billion acquisition of Motorola Mobility and the still experimental Google Glass, the Internet connected eyewear. Google also has also had some success with Chromecast, a device for connecting televisions to the Internet. Although companies have big hopes for the connected home, consumers are largely oblivious, analysts said. Relatively few know such devices exist and even fewer are willing to pay more to buy one.

“The largest barrier for the connected home is consumer awareness,” said Tom Kerber, a research director with Parks Associates. “The second barrier is the lack of a value proposition. Take a connected oven. You think, ‘What in the world do I need with that?’”

Complexity is another major hurdle. Setting up connected appliances and then operating them can be complicated. Companies are trying to create easy-to-use apps that serve as universal remote controls for all one's appliances, but they still have a long way to go. For now, most devices are operated using individual apps, which is cumbersome.

Ross Rubin, an analyst with Reticle Research, said that Google makes a good home for Nest, which has focused on making its technology easy to use and more affordable. Full home automation systems by the major integrators can cost tens of thousands of dollars, plus monthly service fees. Nest's smoke alarm, in contrast, costs \$129 while its thermostat is \$249. The challenge, he said, will be to make Nest more mainstream. "Today, Nest's products appeal to tech savvy buyers who appreciate the functionality," Rubin said. "They will have to work on more affordable products and new kinds of devices to reach more consumers."