DoubleClick and Clear Channel: Google's One-Two Punch to Increase Ad Reach

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Summary: After weeks of rumors that Microsoft was in discussions to buy DoubleClick, and subsequent talk that Google had swept in to start its own negotiations, Google came away with the display ad network for US$3.1 billion. This could mean a great deal for Google and its ongoing efforts to diversify its ad offerings beyond paid search and contextually placed text ads throughout its AdSense publisher network. Like its offline advertising forays (print newspaper ads, radio, television, etc.), this will diversify Google's ad mix by appealing to a broader range of advertisers. It could also serve as a better bridge to offline ad media efforts by bringing in this new segment of advertisers, to which it can serve display ads online and off. To further advance its offline efforts, Google on Monday announced it will begin to sell 5 percent of Clear Channel Communications' radio ad inventory in 100 top U.S. markets, covering roughly 675 stations.

Seeing Value in DoubleClick

Last Friday, Google reached an agreement to buy display ad network DoubleClick for US$3.1 billion in cash — its largest acquisition to date.

Though estimates of DoubleClick's revenues differ (The New York Times reports US$300 million while The Wall Street Journal claims US$150 million), the purchase price nonetheless represents a substantial premium over revenues and earnings. A bidding war with Microsoft in the weeks leading up to the deal could have driven up the price, giving DoubleClick's private equity owners a nice return on the US$1.1 billion they spent on the company in 2005.

A clearer indication of value can be extrapolated from DoubleClick's historical highlights and a comparison of its competitors' metrics (see table below).

Assuming DoubleClick's divestitures in 2005 were roughly equivalent to the percentage of revenues the two businesses represented (about US$150 million), and considering that its growth has been equivalent to that of the overall industry, TKG estimates its annual revenues are about US$270 million. Given private equity companies' propensity to manage cash effectively, TKG also estimates that its operating margin is equal to or greater than that of competitors aQuantive (17.2 percent) and ValueClick (18.7 percent).

Whether or not the purchase price was too high, the acquisition fills a gaping hole in Google's advertising offerings by providing the capability to sell display and rich media — segments in which it has vowed in the past to play an increasing role.

Both are sizable ad markets that represent considerable growth opportunity for Google, as well as synergies with paid search assets and initiatives in various offline media. According to eMarketer, the display ad

DoubleClick: Timeline and Highlights

2003	DoubleClick reports US$271 million in revenues and net income of US$16.9 million.
2004	Revenues total US$301.6 million and net income is US$37.5 million.
2005	The company is taken private by private equity firms Hellman & Friedman and JMI Equity for US$1.1 billion then sells two data and e-mail advertising businesses for a reported US$525 million
2006	DoubleClick purchases online video provider Klipmart for an undisclosed amount.
2007	Google purchases DoubleClick for US$3.1 billion in cash.

SOURCES: COMPANY AND NEWS REPORTS (2007)

DoubleClick: Sizing Up the Competition

	24/7 Real Media	aQuantive	ValueClick	Industry*
Ticker Symbol	TFSM	AQNT	VCLK	–
Market Cap	US$437.6 million	US$2.23 billion	US$2.94 billion	US$331.4 million
Total No. of Employees	390	2,106	1,072	378
Quarterly Revenue Growth (year over year)	44%	53%	38%	16%
Full-Year 2006 Revenues	US$200.2 million	US$442.2 million	US$545.6 million	US$98.2 million
Gross Margin	36%	41%	69%	58%
Full-Year 2006 EBITDA	US$18.2 million	US$124.2 million	US$145.1 million	US$8.4 million
Operating Margin	(4.1%)	17.2%	18.7%	0.2%
Full-Year 2006 Net Income	(US$8.6 million)	US$54.0 million	US$63.1 million	(US$185,070)

SOURCES: COMPANY REPORTS, HOOVER'S, CAPITAL IQ (2007) *INDUSTRY = INTERNET SOFTWARE AND SERVICES

market generated US$3.4 billion in 2006, and the rich media/video market generated US$1.5 billion.

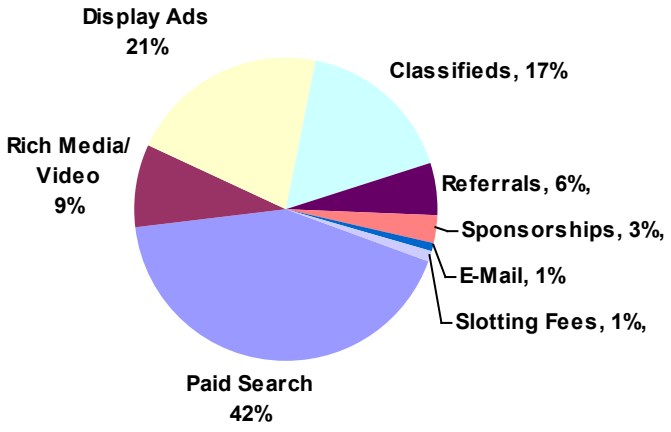
The growth potential in these media is important to Google given the flattening growth in its flagship paid search segment. It is also becoming increasingly important that Google diversify its revenue model, given the threats brought by new search engine marketing platforms from Microsoft and Yahoo! (see May 18, 2006, TKG Advisory, "Search Wars: Microsoft and Yahoo! Strike at Google's Leading SEM Position").

In Microsoft's case, its newly launched adCenter SEM platform features better ad targeting abilities for search marketers. Indeed, DoubleClick could have been a considerable threat to Google if applied toward broadening the capabilities of AdCenter, and keeping it out of Microsoft's hands can't be ignored as a partial driver for the acquisition.

AOL's position in all this is also important, as Google owns 5 percent of AOL and DoubleClick is one of AOL's largest partners. TKG has learned recently from credible sources that AOL is pushing hard against its quarterly advertising goals in an effort to make the company more attractive to potential buyers. It's likely Microsoft will take a close look at exactly what strings are attached to the AOL-Google investment and the AOL-DoubleClick deal and try to get Google/DoubleClick out of the AOL camp and into a friendlier orbit.

Online Advertising: 2006 Market Share by Format

SOURCE: EMARKETER (2007)



The Real Threat: Yahoo!

Yahoo!'s newly launched Panama SEM platform could also give Google AdWords a run for its money. TKG expects Panama to show financial results by the end of the first quarter of 2008. With this in mind, Google's acquisition of DoubleClick can also be viewed as a strategic counter shot to Panama by entering Yahoo!'s flagship display advertising territory. DoubleClick will indeed bring this capability to Google in order to challenge Yahoo!'s dominance in the space.

It's also interesting to note the advertising exchange DoubleClick recently launched. This is similar to the open ad exchange provided by RightMedia, which is 20 percent owned by Yahoo!. These exchanges are meant to bring transparency to online ad marketplaces through auction-based systems in which publishers set reserve prices for targeted ad inventory, against which advertisers can bid directly. DoubleClick's exchange hasn't had time to prove itself but could be valuable given the company's relationships with publishers, advertisers, agencies and ad networks. Google's even larger base of relationships could further position the tool to not only match Yahoo!'s capability with RightMedia, but also to be the center of an online and offline ad sales network.

Yahoo! will still be a formidable incumbent for display advertising,

however, and its power will grow as the relatively young Panama evolves. Yahoo!'s position in the search market is further emboldened by an array of strong content verticals, including Finance, Autos, Personals, Real Estate, Shopping and Sports. Combining positive ad metrics, momentum in paid search and a massive audience puts Yahoo! in the vaunted position to form deeper relationships with large advertisers.

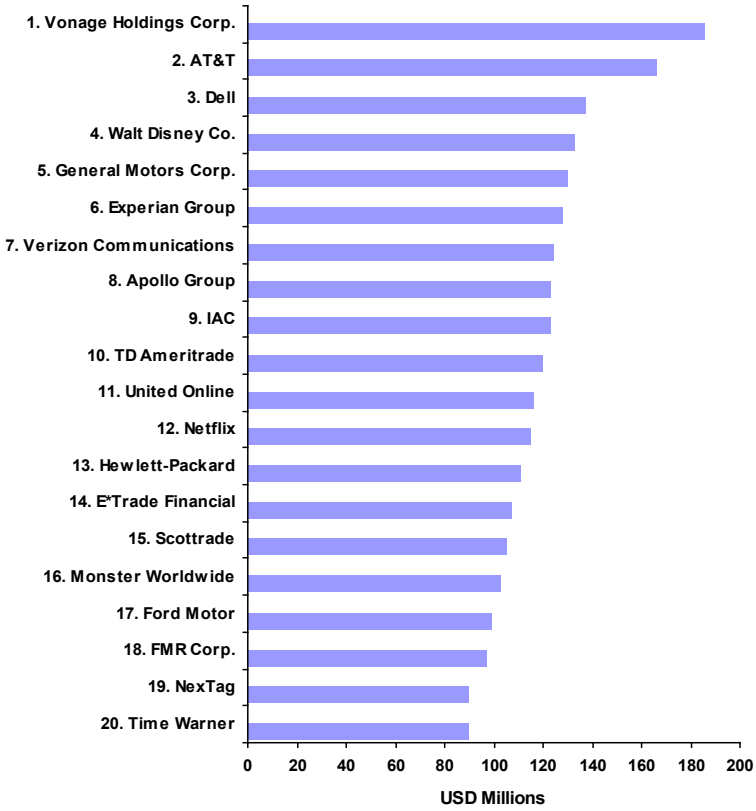
For Google, bringing display ads into the picture will be essential to compete with Yahoo!, and buying into the display market (via DoubleClick) was the fastest and most prudent countervailing strategy. The top Internet display advertisers in the chart at right represent the opportunity for Google to address the growing need to easily buy a geotargeted display ad solution across all local markets and content verticals.

Many of these advertisers could also represent adoption leaders in pushing new formats such as video advertising — a critical area for Google as shown by its other recent massive investment, YouTube.

The bottom line is that developing a tool for advertisers to easily buy ads across many formats will become vital for search giants (this, however, can come with a certain degree of antitrust scrutiny, as Google now faces possible U.S. Department of Justice investigations for the amount of control it will have over the online advertising market). Yahoo!'s "Amigos" newspaper consortium is a good example, as it will share advertising and editorial content — in addition to Yahoo! online tools and functionality — across a growing network of 264 newspapers. In fact, just days after Google's acquisition of DoubleClick, Yahoo! announced some of the official terms and operating procedures of the Amigos network, which appears likely to be a strong ad distribution channel for Yahoo!.

Top 20 Internet Display Advertisers, 2006

SOURCE: EMARKETER (2006)



Google's Offline Strategy

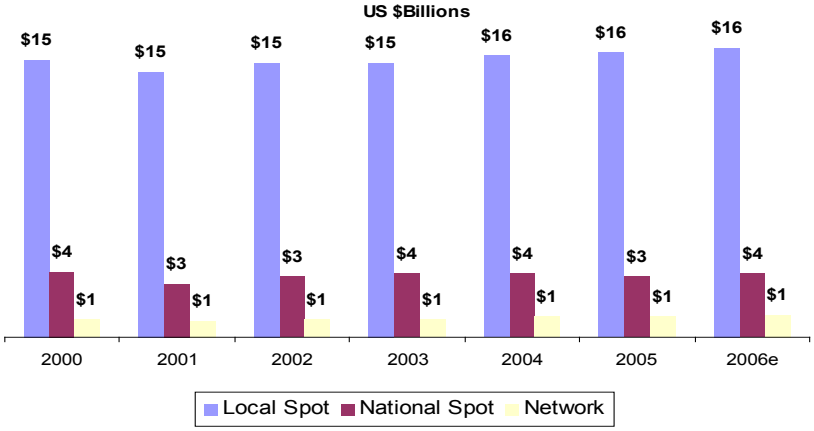
Like Yahoo!, Google has initiated its own forays into the newspaper industry, although its terms are much different from those of the Amigos consortium. For example, newspapers will offer content across Yahoo!'s network in exchange for its search functionality and content distribution (HotJobs listings, for example) across newspapers' own Web sites.

The content in Google's newspaper arrangement will instead flow from online to off. It gives advertisers the ability to purchase ads across 50 major U.S. newspapers through an online auction-like format. This brings traditionally cost prohibitive newspaper advertising within the grasp of many smaller advertisers and allows newspapers to more efficiently sell remnant or non-premium inventory that is otherwise backfilled with house ads. After a trial period, The Washington Post reported in late December that the newspaper partnership was deemed a considerable success and will be expanded.

Google's newly developed display advertising capability from DoubleClick could have implications for this offline newspaper ad distribution program. The newspaper inventory Google currently

Radio Industry Revenues by Spot Type

SOURCE: NATIONAL ASSOCIATION OF BROADCASTERS (2007)



resells is text only, but there are clear opportunities to enhance this to include display advertising, which we expect to happen in the future. The DoubleClick acquisition will likewise help Google to bring in new advertisers that are interested in a variety of offline ad media including, importantly, radio.

Clear Channel: A Clear Opportunity

Google and Clear Channel Communications announced a partnership on Monday in which the search giant will sell 5 percent of the radio group's inventory in 100 top U.S. markets. The agreement covers roughly 675 Clear Channel stations. Terms of the deal, including any potential cash or revenue share agreements, weren't disclosed.

Clear Channel is the largest U.S. radio broadcaster in revenues and stations, and it currently books roughly 20 percent of all U.S. radio industry revenues. The company is the result of an aggressive roll-up of regional stations into a national radio powerhouse.

Clear Channel revenues grew 6 percent last year (faster than those of the industry overall), mostly because of price increases. The National Association of Broadcasters forecasts industry revenues slightly above US$20 billion. After years of consolidation, the industry shows the flat growth that is characteristic of a mature market. And like any mature market, growth can come from few places. Increasing the number of advertisers is one possibility and, TKG believes, a primary driver for this partnership.

The deal is structured so Google will be responsible for selling new advertisers while existing station accounts will be handled by current radio reps. Over time, TKG expects these lines to blur as sales territories and radio accounts are carved up at the station cluster level.

Implications for Google and dMarc

The deal overall is a boon for Google and its wholly owned subsidiary dMarc. Google purchased dMarc last year for US$100 million, with the potential for a US$900 million earn out. DMarc provides radio stations with the equipment to schedule and play airtime, commercials and other on-air tasks. Typically, the radio industry offers what are known as "trade-outs," or exchanges of airtime instead of cash payment. These spots are then resold or bartered for cash and services.

Google's acquisition of dMarc prompted some nervousness among radio owners. The company's massive market cap and robust performance-based ad serving platform caused station owners to pull back slightly and reevaluate their existing deals. In the end, if Google can deliver advertisers and revenues, stations will likely opt to hand over more spot inventory.

Radio is a logical industry for Google to enter, and its aggressive purchase of dMarc shows it is serious about making inroads. Yahoo! has also reportedly been in talks with CBS Radio about various types of advertising partnerships. The key driver to Google's and Yahoo!'s entrance to the radio market is that radio advertising is essentially local in nature as shown above: Local spot inventory constitutes nearly 80 percent of radio revenues.

Furthermore, the configuration of radio has several important characteristics for Google:

- The largest vertical segments of radio spot advertising are automotive, entertainment and retail. These segments, generally speaking, are strong search advertisers.
- Radio spots are among the most expensive local advertising inventory.
- A mix of direct response advertisers (search advertisers) and

display advertisers (DoubleClick advertisers) can conceivably increase Google's chances of creating meaningful revenues.

- Radio spot flights are somewhat similar to Internet display advertising in that they are sold on reach. Google has previously rolled out day-part targeting.
- An audio ad format can be used across multiple platforms — most notably at the front end of the increasingly popular wireless voice search and free directory assistance offerings. Google's free DA product, 1-800-GOOG-411, announced last week, has clear synergies with radio ad sales in this respect. Internet radio can also join terrestrial radio as a formidable ad venue for such audio ads, once an ad creation and distribution network is built by the likes of Google.
- An AdWords dashboard will be appealing for many non-radio advertisers that are interested in testing new advertising methods but find the radio sales process out of step with performance-based advertising.
- Finally, where local sales are concerned, Google has been aggressively hiring radio reps well ahead of this announcement. It is conceivable that these reps could, over time, sell multiple ad products mentioned earlier. This could be similar to Google's AdSense network where advertisers can opt out of campaigns and focus only on search.

Format Over Function

Typically, different forms of traditional media sell products unique to their respective industries — newspapers sell print display ads, and television stations sell 30-second commercials. However, traditional media ad models will transition to a focus on the ad format. In such a format-centric model an audio ad, for example, could be initially purchased and recorded for use on radio but could live on to reach larger and more diverse audiences through other media (as submitted in the Google DA example above).

While this is potentially unnerving for traditional media, over time it could increase their revenues. Simply, it offers advertisers an opportunity to distribute ads to markets and audiences in which they could not have easily done so before. As more advertisers are exposed to cross-media ad purchasing, an increasing number will decide to broaden their advertising portfolio.

These new leads will be upsold by the traditional reps into core non-shared products like DJ mentions, promotions and other radio revenue products. Control over this inventory won't transition into the hands of a search company but will rather become an important part of a traditional media revenue mix. In other words, a certain amount of inventory will be allocated, and traditional media will maintain pricing power.

One company that has begun to show the value in this type of relationship is Bid4Spots. Along with Google, Bid4Spots will be a company to watch for its efforts in combining online sales with offline traditional media placement.

Final Thoughts: More Ad Dollars From New Advertisers

In any maturing industry, revenue growth will mostly come from shifting market share within an increasingly zero-sum game. In trying to prevent this game from weighing down its overall performance (given the slowing growth of its flagship paid search market), Google continues to diversify by entering new playing fields. As it breaks new ground in offline ad media while adding to its arsenal of online ad formats, the primary driver will be to address new advertiser segments.

Its offline newspaper partnerships are the clearest example of this. Newspapers benefit by gaining smaller advertisers to which Google can provide a more efficient exchange of remnant inventory at reduced price points through low-overhead self provisioning. Google meanwhile establishes new ground on which to sell ad inventory and brings in a new segment of the local ad marketplace interested in traditionally cost-prohibitive print newspaper advertising. DoubleClick could add the dimension of display ads to this text-based ad platform.

Furthermore, this will be a small piece of the puzzle that will provide a wide range of advertising options including text and display ads both online and off. Google's new path toward display advertising will bring in new forms of advertisers that most notably include large and national brand advertisers — a segment traditionally "owned" by Yahoo!. The competitive dynamics in this segment will be interesting to watch as these heavyweights exchange blows.

For Google, covering the gamut of advertising formats and media will help the company continue to grow its addressable market of advertisers and see top-line revenue growth. Google is saddled with the burden of sustaining steep revenue growth in order to both maintain and justify its valuation, and we expect no foreseeable end to its aggressive push to reach into all forms of advertisers across all media.

Bringing more small businesses online by offering free Web site hosting, development and landing page tools (i.e., Google's Local Business Center and AdWords Hosted Business Pages) will be part of this goal for Google and other online ad networks. But more than anything, building one-stop shops for ad sales across all media and formats, will represent the top strategic imperative for Google and other search giants in the coming months. **ILM**

