

Operator

Good day, and welcome, everyone to the Google Inc. Second Quarter 2011 Earnings Conference Call. This call is being recorded. At this time, I'd like to turn the call over to Jane Penner, Senior Manager, Investor Relations. Please go ahead, ma'am.

Jane Penner

Good afternoon, everyone and welcome to today's Second Quarter 2011 Earnings Conference Call. With us are Larry Page, Chief Executive Officer; Patrick Pichette, Senior Vice President and Chief Financial Officer; Susan Wojcicki, Senior Vice President, Advertising; Nikesh Arora, Senior Vice President and Chief Business Officer.

First, Larry, Patrick, Nikesh and Susan will provide us with results on the quarter. Also, as you know, we now distribute our earnings release through our Investor Relations website located at investor.google.com. So please refer to our IR website for our earnings releases, as well as supplementary slides that accompany the call. This call is also being webcast from investor.google.com. A replay of the call will be available on our website in a few hours.

So let me quickly cover the Safe Harbor. Some of the statements that we make today may be considered forward-looking, including statements regarding Google's future investments in our long-term growth and innovation, the expected performance of our business and our expected level of capital expenditures. These statements involve a number of risks and uncertainties that could cause actual results to differ materially. Please note that these forward-looking statements reflect our opinions only as of the date of this presentation, and we undertake no obligation to revise or publicly release the results of any revisions to these forward-looking statements in light of new information or future events. Please refer to our SEC filings for a more detailed description of the risk factors that may affect our results.

Please note that certain financial measures that we use on this call such as operating income and operating margin, are also expressed on a non-GAAP basis, and have been adjusted to exclude charges related to stock-based compensation. We have also adjusted our net cash provided by operating activities to remove capital expenditures, which we refer to as free cash flow. Our GAAP results and reconciliations of non-GAAP to GAAP measures can be found in our earnings press release.

With that, I will now turn the call over to the Larry.

Larry Page

Well, thank you, and good afternoon, everyone. Thanks for joining us today. It's really exciting to be with you today and share directly with you the progress we have made in my first quarter as CEO.

As you will see from our press release, we had a great quarter, with revenue up by 32% year-on-year and a new record for quarterly revenue at over \$9 billion. We've substantially increased our velocity and execution this quarter, which is a key goal of mine since taking over as CEO. So I created a new product focus management structure, with clear leaders responsible for each area.

The new management team is working together fabulously and has already achieved a lot in just these 3 months. First of all, I want to talk about Google+, which we launched a field trial invitation only. Our goal at Google+ is to make sharing on the web like sharing in real-life, as well as improve the overall Google experience.

Circles lets you choose with precision who you're sharing with, not surprisingly this has been very well received, because in real life, we share different things with different people. Hangouts allows for serendipitous interactions. Like in real life, when you run into a few friends, gives you seamless and fun multiuser video, and it's really amazing.

Last quarter, we launched the +1 button in search results and ads, enabling users to recommend stuff they like and to have those recommendations show up in the search results of people they know. This quarter, we released the +1 buttons to the entire web and many sites like Huffington Post, The Washington Post, and Best Buy has added +1 buttons. Google+ is still in field trial with limited access as we scale the system. Users have to be invited and sign up with a profile in order to use it. However, the growth on Google+ has been great, and I'm excited to release some new metrics for you today.

Over 10 million people have joined Google+. That's a great achievement for the team. There's also a ton of activity, and we are seeing over 1 billion items shared and received in a single day. Our +1 button is already all over the web, and it's being served 2.3 billion times a day. So while we still have a lot of work still to do, we are really excited about our progress with Google+.

Google+ is also a great example of another focus of mine, beautiful products that are simple and intuitive to use, and actually was one of the first products to contain our new visual redesign. We also launched that beautiful, consistent and simpler design on our homepage, Gmail and

calendar, with many more products soon to come. Reader focus has also been another big feature for me this quarter. More wood behind fewer arrows and last month, we announced that we'll be closing Google Health and Google PowerMeter. We've also done substantial internal work, simplifying and streamlining our product line.

While much of that work has not yet become visible externally, I'm very happy with our progress here. Focus and prioritization are crucial given our amazing opportunities. Indeed, I see more opportunities for Google today than ever before, because believe it or not, we are still in the very early stages of what we want to do. Even in Search, which we've been working on for 12 years, there's never been more important changes to make.

For example, this quarter, we launched a pilot that shows an author's name and picture in search results, making it easier for users to find things from authors they trust. Of course, when we started doing Search, people thought we were crazy. They said there was no money to be made in search over and above a bit of banner advertising. Most new Internet businesses have had that same criticism. Fast-forward to today, it feels like we're watching the same movie again in slow motion. We have tremendous new businesses being viewed as crazy. Android, I actually have a new metric to report in Android of 550,000 phones activated a day. And that's a huge number, even by Google standards.

Chrome is the fastest-growing browser. We have over 160 million users. Now people rightly ask, "How will we monetize these businesses?" Of course, I understand the need to balance the short-term with the longer-term needs because our revenues in growth serve as the engine that funds our innovation. But our emerging high usage products can generate huge new businesses for Google in the long run, just like Search. And we have tons of experience monetizing successful products over time. Well run technology businesses with tremendous consumer usage make a lot of money over the long term.

And I think about our products in 3 separate categories. First, there is Search in our Ads products, the core driver of revenue for the company. And Nikesh and Susan are going to talk more about Ads later in the call. Next, we have products that are employing high consumer success: YouTube, Android and Chrome. We are investing in these in order to optimize their long-term success. Then we have our new products, Google+ in commerce and local. We are investing in them to drive innovation and adoption. Overall, we are focused on long-term, absolute profit and growth, as we have always been, and I will continue to have tight financial management we have had in the last two years, even as we were making significant investments in our future.

I'd like to finish on our people. Great companies are no greater than the efforts and ingenuity of their people. We're continuing to hire the best. Keeping them happy and well-rewarded is crucial to our future. Many of you will be interested in hiring whether we hired a few hundred more or less than you expected this quarter. But we will optimize headcount for the long-term in the opportunities we see.

I'm happy with the investments we've made in people, but we're probably even a little ahead of where we need to be with headcount growth at the edge of what's manageable now. Easy to focus on things we do that are speculative, e.g. driverless cars. But we spend the vast majority of our resources on the core products. We may have a few small speculative projects happening at any given time but we're very careful stewards of shareholder money. We're not betting the farm on this stuff.

All of us at Google will want to create services that people in the world use twice a day just like toothbrush. And we strive to make those services beautiful, simple and easy to use. That way we can provide huge benefit to the world. We've made a good start, but we're only at 1% of what's possible. Google is just getting started, and that's why I'm here, working hard to lead the company in the next level.

Thank you. And again, we had a great quarter. Now over to Patrick for the financial results.

Patrick Pichette

Thank you, Larry. Thank you, everybody. Thanks for joining us. And Larry is going to stay with us for the Q&A. So I just wanted to make sure that everybody knows he's not going anywhere.

Okay, so let's go through the number. We had obviously an excellent quarter with 32% year-over-year revenue growth in Q2, and it clearly demonstrate the continuing power of Google's product innovation, but also the relentless momentum of the digital economy. The strength continues to be driven by our core desktop search ads, but also increasingly, by new emerging areas just like the Mobile, Display, including YouTube and Enterprise that we regularly talk about.

So let's turn to the specifics of our performance in the quarter. Growth revenue grew 32% year-over-year and we've reached \$9 billion in revenue, 5% quarter-over-quarter growth as well. Note that while currency fluctuation boosted our revenue somewhat, even in constant FX terms, our growth rates remain strong, particularly in what tends to be a seasonally slower quarter.

Google website revenue was up 39% year-over-year to \$6.2 billion and 6% quarter-over-quarter, with strength across most major geographies and verticals. Google Network revenue was also up 20% year-over-year to \$2.5 billion, 2% quarter-over-quarter. Network revenue was again negatively impacted by the Search quality improvements made during the latter part of Q1, as you will remember, and know that Q2 reflects a full quarter of this impact. This impact is to be expected in the short-term, given that it is now different publishers that are receiving traffic and may not have yet optimized their sites for our advertising programs.

Other revenue was also up 20% year-over-year, just \$310 million and 15% quarter-over-quarter. Our global aggregate paid click growth was strong, up 18% and down 2% quarter-over-quarter. Our UI changes to search ads such as BizURL drove year-over-year click growth in Q2, along with the ongoing and accelerating shift from offline to online. The slight decline quarter-over-quarter is just typically consistent with our summer seasonality.

Aggregate cost-per-click growth was also very healthy, up 12% year-over-year and up 6% quarter-over-quarter. Note that FX also had a positive impact on CPC, and remember too that this is an aggregate number that includes both Google.com and our AdSense properties.

Turning to our geographic performance, the U.S. and Rest of the World are growing both at very good pace, and our results reflect that. While the U.K. still continues to lag slightly in the global recovery, year-over-year and quarter-over-quarter growth in Q2 continues to show signs of acceleration in the U.K. as well. So revenue from the U.S. was up 26% year-over-year to \$4.2 billion, and in our earnings slides, which you can find on our Investor Relations website, you'll see that we've broken down our revenue by U.S., U.K. and Rest of the World to show the impact of FX and the benefits of our hedging programs. So please refer to those slides for the exact calculations.

Non-U.S. revenue accounted for 54% of our total revenue or \$4.9 billion, up 38% year-over-year, which includes only \$4 million of benefits from hedging programs, compared to last year where we had \$79 million of benefits for Q2. Year-over-year growth in fixed FX would have been 29% versus the 30% I just mentioned. Japan's future revenue was again negatively impacted by the aftermath of the disaster there, but there again we see signs of faster recovery, faster than expected at first. The U.K. was up 27% year-over-year to \$976 million, and year-over-year growth and fixed FX was still a healthy 19% for the U.K.

Let me turn to expenses. Traffic Acquisition Costs were \$2.1 billion or 24.2% of total advertising revenue. Our other cost of revenue was \$1.1 billion dollars, including stock-based compensation of \$51 million and finally, our

operating expenses, which exclude stock based compensation totaled \$2.6 billion. The stock-based compensation totaled \$384 million in Q2.

The increase in year-over-year in OpEx was primarily due to payroll, increased advertising and promotional spend and also professional services. So as a result, our non-GAAP operating profit was \$3.3 billion in Q2 which excludes the stock-based compensation, resulting in a non-GAAP operating margin of 36.7%.

Headcount was up approximately 2,450 versus Q1 ending the quarter with 28,768 full-time employees. When we exclude ITA adds of roughly 450, the net headcount growth is roughly similar to Q1.

Our effective tax rate was 19% in Q2, and the effective tax rate is down due to the mix of earnings between domestic and international subsidiaries, as well as our hedges.

Let me turn now to cash management. In Other Income and Expense, our result was \$204 million for Q2, a solid portfolio management performance from our team, which, like every quarter, is offset by the impact of our hedging expenses associated with FAS 133, which in itself was also significantly lower in Q2 gave us these great results. For more detail in OI&E, again, please refer to the slides that accompany this call on our IR website.

Operating cash flow, very strong, \$3.5 billion for Q2. CapEx for the quarter was \$970 million versus last quarter of \$890 million. So pretty much in line. The majority of our CapEx spend in Q2 was related to facilities, expenses, and production equipment. And regarding specifically these facility expenses, like last quarter, we just happened to have a great opportunity in Q2 to purchase buildings in Dublin and in Mountain View, and we took opportunity. As a reminder, we'll continue to make significant CapEx investments, and these have shown to be lumpy from quarter to quarter depending on when we're able to actually make these investments. But overall, we can be nothing but pleased with our free cash flow which was \$2.6 billion for Q2.

As Larry mentioned earlier, we continue to deliver growth with a disciplined agenda. This means investing and making sure that our resources are deployed wisely with focus and a balance between that short and long-term that Larry covered.

So with those financial highlights covered, I'm going to turn it over to Nikesh who will actually cover now our sales performance in the quarter. Here you go Nikesh.

Nikesh Arora

Thank you, Patrick. I'm going to give you a quick update on our business activities, which spans sales, partnership marketing, and customer service around the world in support of our product and revenue.

Let me start by focusing on the first priority of our sales team, the need to continue to drive revenue growth in core and new businesses. This quarter we continue to drive revenues in our corner areas like Search, as well as new areas like Display, Mobile, and Enterprise. Core Search and Desktop has done very well this quarter, with Google.com accelerating and our large advertisers continuing to spend more as they see more value in Search. We've also have been able to drive tremendous focus on small advertisers around the world, with programs like GXPO, which I will talk about slightly later.

Broadly, however, our sales teams are getting better at tailoring Integrated Solutions for clients, using the full area of our advertising products. These solutions create better opportunities to improve our customers marketing ROI. Clients have used Search to focus their targeting capabilities, such as audience and topic targeting, to help improve the marketing effectiveness. Some of our most successful Search clients include people like GM and EgyptAir.

On the other hand, in addition to our core desktop Search business, we continue to be very excited about our investments in Display and Mobile. Let me first focus on Display. We've seen continued healthy growth in our Display product space across all fronts: Advertiser, publisher and technology solutions. 98 of the top AdAge 100 advertisers have bought Display across YouTube and the Google Display Network this quarter. Customers continue to use our DoubleClick products and we are happy with the increased use for the DoubleClick Ad Exchange and Invite Media for ad buying. With our announcements to acquire Admeld, we hope to deliver even better solutions to our publishers and buyers.

Continuing on Display -- on YouTube, where we have over 3 billion daily views, we have had great success bringing popular content to our users, further increasing audience engagement. Take for example, our April broadcast of the Royal Wedding which generated 100 million YouTube views. Our range of platform and content means that advertisers are beginning to use them for superior branding solutions. A great example of our branding products in action was T-Mobile's launch of the Samsung S4G on YouTube. In this campaign T-Mobile took over YouTube running ads in their home page, watch page, Mobile. That particular campaign helped them reach 46 million unique users.

Continuing to talk about revenues, our Mobile business continues to be another area of robust growth. The number which Larry just shared of 550,000 Android, that and the success of smartphones in and general Mobile Data devices around the world is acting as an accelerator for our Mobile advertising effort.

Let me just take one quick example. One format which was launched by Susan's team called Click-to-Call or Click-to-Share has been particularly successful. Unilever is a great use case of these formats. They integrated our AdMob product into a very large campaign of launching a new product to use the banner to drive traffic to a campaign Mobile site and achieve unprecedented results with almost 700,000 unique visitors accessing their content.

Another leg of our revenues is the Enterprise Business. We've seen great results in enterprise as well, in particular apps for business continues to grow as organizations move to the cloud. We've had key wins at Intercontinental Hotels, [indiscernible] State of Wyoming. In addition to that, some small simple changes in our product side have allowed us to tremendously accelerate Google Apps for small businesses.

Looking at our revenues from a slightly different perspective, geographies and customer segments, we've seen strong growth in regions and across customers of all sizes. First let's take a look at geographies, we maintained our strength in large, mature countries while we accelerated in emerging ones.

Now a large majority of countries which are countries even though some of our facing economic challenges, this secular trend of online advertising and the effectiveness of the teams to continue to drive healthy revenue growth is showing great results. Several countries are worth noting as Patrick mentioned. The U.K. has accelerated this quarter with strong growth by small advertisers. In Japan, we've seen recovery, driven primarily by Display and Mobile spending by large advertisers. Our focused execution in Canada and Spain has led to these markets beginning to show recovery. Finally, we saw tremendous growth in emerging countries especially Brazil and Russia, where our Display products are getting strong adoption from advertisers.

Across each country, we focus to improving the product knowledge and selling capability of our sales force, our frontline teams can now sell Search, Display, and Mobile to the needs of our customers, which is a great trend we're seeing of integrated products selling across multiple Mobile ad formats. As a result we're becoming better advisors in the digital space for our large advertisers. For example, Nike, Sony Ericsson, Telefonica, all of

them partnered with us to create integrated solutions down there, sponsorship of Copa América.

Outside of revenue, one key area of responsibility is marketing. And if we continue to use marketing as a strategic blipper. We use marketing to both drive customer acquisitions as well as usage of our key consumer products. I'm very proud of my team's work on getting business online GXPO as I mentioned in Q2 we successfully launched Brazil, Canada, Australia Thailand. To objective is to try and bring another million small, medium businesses across 20 countries online for the first time. As you know, more advertisers gets more queries, has more adservices against it. There's nothing in a more robust option for us.

In addition, also we saw strong results from our own advertising campaigns, including the most recent one around Google Chrome. The web is what you make of it. I'm sure many of you might have seen Justin Bieber and Lady Gaga in these campaigns. These campaigns have shown tremendous effectiveness and have also convince more users to switch to the Chrome browser.

Last but not the least, I want to spend a quick minute on talking about something we're more and more passionate about, which is continuing to drive better customer satisfaction on an advertiser front. We continue to improve service and support across all customer segments. We've started providing large sets of advertisers proactive full support and on boarding help, which includes signing up for campaign building, signing up and getting assistance, as well as free full support after they become a customer of ours. As a result of these initiatives and others, spending by our small businesses continue to accelerate.

Overall as Patrick and Larry have mentioned, it was a great quarter. I'm very proud of the wok of our teams across the world in various countries. We have done a tremendous amount of effort to serve our customers, partners and users.

Now I'm going to turn over to my business partner, Susan, who is going to talk about all the positive impact that our products will have this quarter.

Susan Wojcicki

Thanks, Nikesh. Larry started the call by talking about a few of the quarters product highlights and I'd like to cover some more of them. So let me begin with Search. We're always looking for new ways to help our users find answers to their questions. This quarter, we brought 2 of the most popular mobile search innovations to the desktop, Voice Search and Search by Image.

Voice Search traffic for Mobile devices is up 6x in the past year. So we thought this would be a useful feature for our desktop users as well. It's especially useful for searches that you know how to say but don't how to spell like Bolognese sauce or Schenectady, New York, neither of which I could easily spell.

With Search by Image you can draw pictures of places, art, or even mischievous creatures like the Loch Ness Monster right into the Google search box and Google can identify and tell you about those pictures.

In addition to these changes, we released about 100 other quality improvements to the Search algorithm. More and more people are searching and using apps from Mobile phones, where Android has had terrific momentum. There are now 135 million Android devices that have been activated in total, up from 100 million just 2 months ago. There are also now over 400 different Android devices available globally.

Android market is also picking up momentum. It has over 250,000 different apps, and users have downloaded apps over 6 billion times, which is double the downloads from just a few months ago. We're expanding beyond apps too. This week, we started renting movies and selling books on phones from Android market and earlier in Q2, we launched Music Beta, which lets users upload their personal music collections and playlist to the cloud. All this media, movies, music, books and apps, are instantly available on their Android devices, no cable required.

Smartphones are also becoming key to the shopping experience. Making shopping mobile and local is a vision behind Google Wallet and Google Offers. We announced the Google Wallet mobile app in May in partnership with Citi, MasterCard, Sprint, and First Data, and we are now testing it in field trials. And as of this week, Google Offers are available in San Francisco, Oakland, New York, and Portland.

But now on to Ads, which is the product area that I manage. On the Search Ads side, we had a great quarter for quality with over 50 ads quality improvements and a big upgrade to the ads relevancy system. We launched the latest in a series of small tweaks for a search add format. This format, this quarter, we added the landing URL to the headline so that users know where click will take them. This may seem like a small thing, but we launched several of these small tweaks over the past year and cumulatively, they have had a big impact.

There were also a lot of quality improvements across our Display Network. Over 20 launches, making it one of our strongest quarters from a quality perspective. In general, Display advertising is moving to a scientific model

based on technologies like real-time bidding. But this technology when you land on a web page, advertisers decide what they want to pay for the ad space, and then auction is held. And the best ad is matched with the publisher's ad space. It's a lot more efficient. It provides better performance for both advertisers and publishers, and more relevant ads for users. Real-time bidding is an important technology shift that we are investing heavily in.

Invite Media, which is the buying platform for advertisers and agencies that we bought last year, has doubled its client list in the last year, with over 5x growth outside of the U.S. Mobile Display is starting to take-off too with traffic on the AdMob network up more than 3.5x in the past year. More and more of that traffic is coming from tablets, so we launched a new set of formats designed specifically for tablets. These formats are web-based. They use HTML, and brand advertisers don't need to make different versions of their ads for different models.

Nikesh also mentioned our great momentum with YouTube, where we're getting strong performance from the YouTube skippable ads. Because users can choose to skip these in-stream ads, the people who choose to watch them are much more engaged. More and more advertisers are choosing to make their ads skippable and now, over 1/3 of in-stream ads on YouTube are in a skippable format, which is a pretty remarkable stat given that we launched this format in December.

Finally, I'd like to update our progress on Chrome. Larry mentioned how we passed 160 million users which is more than double year-on-year. This quarter, our partner Samsung and Acer Search using Phonebooks in 7 countries. Phonebook are designed to be fast, to just work, and to get better over time, thanks to our automatic updates. And they're now available through Amazon and Best Buy. Phonebooks are also available to schools and businesses via subscription model. The subscription includes Phonebooks, of course, administration, warranty, and support, starting at \$20 a month.

So overall it was a very busy quarter for us. But maybe the coolest thing we did was the Les Paul doodle we ran last month. It was a guitar you could actually play, and users recorded over 40 million songs while it was up. That's about 5 years of music.

I'm looking forward to hearing your questions and comments. And for now, back to Patrick.

Patrick Pichette

Thank you, Susan. So Jamie, our operator, is going to help us through this. Jamie, you can just set up the call for Q&A. And as I said, we'll have Susan, Nikesh, Larry, and myself to answer any questions you may have.

Question-and-Answer Session

Operator

[Operator Instructions] And we'll take our first question from Spencer Wang with Credit Suisse.

Spencer Wang - Crédit Suisse AG

Two quick questions, if I could. First for Patrick or perhaps Nikesh, International revenue growth as you mentioned was really strong. I was wondering if you could just provide a little bit more color on perhaps that's driving that? If you could give us a sense of how much of that is core Search versus some of the newer initiatives like Mobile, YouTube, and Display. And then the second question is for Larry. I was wondering if you can just talk a little bit, Larry, about the patent strategy. Our understanding is you guys have about 650 patents. So just given the Oracle situation, I was wondering if you could talk about the patent strategy to ensure that you guys can continue to innovate going forward.

Patrick Pichette

I'll let Nikesh answer the first part of the question, and then Larry will talk about the patent issues.

Nikesh Arora

As I mentioned in my prepared remarks, that we've seen tremendous growth across pretty much all product areas. So the growth you're seeing in international is driven by Mobile, by Display, by Search. Clearly international is not one market there are many different countries. So we have seen different effects in different markets. Places like Japan, as I said, have been driven more by Display and Mobile. Various parts of Asia are just getting up the curve for us in Display and are strong contributors in Mobile. Having said that, Russia has been very strong for us. Brazil has been very strong for us. Brazil in the back of Mobile and Display as well, and as well as core Search. So if you think about what we're seeing, we're seeing more and more a pickup of Display and Mobile because we have established sales team are pretty much on almost every major market around the world to help sell Display. And the Mobile tick up based on tick up of smartphones and Android et cetera is helping that trend as well. In addition to that, a lot of effort has gone in to bringing small business online and that increases a number of

advertisers in many international markets. As you get more advertisers in international markets. It has a very positive impact on our RPMs in those markets. So we're seeing that effect as well.

Larry Page

To your question on Android and patents and so on. Obviously we have a number of intellectual property patents in progress not just already issued. I must just say, Android's really on a tear. I mentioned there were over 550,000 new Android daily activations previously. And there's over 400 such devices, 39 OEMs, 231 carriers in 123 countries, and over 78 open handset alliance partners. And that velocity is only increasing. And of course despite the efforts of some of our competitors, there hasn't been any slowdown in any of those things. And partners and developers are continuing to expand the Android ecosystem. Of course we're really committed to Android and continued to support that platform and ecosystem, and do it in a cost effective manner.

Operator

And we'll take our next question from Mark Mahaney with Citi.

Mark Mahaney - Citigroup Inc

Two questions Larry. Could you talk about what you have maybe put in to improve the velocity of decision-making? And as you step back and think about the management improvements you could see over the next year or 2, how significant do you think -- how much better -- how much more efficiently do you think Google could be run, than what we've seen maybe over the last 2 or 3 years? And then Susan, real quickly, social search signals, how important do you think they are now? How key are they -- how much of that is Google+'s strategy for trying to make the core search results more relevant?

Larry Page

This is Larry. I'm super excited about the changes we've made and I think as companies scale, we always change how we're running the company over time. So I think we have a much more of a product focused structure now, which I'm very excited about and talked about it. And I think that maintaining and improving our velocity and execution is a really noble goal for us. And it requires always a lot of work in companies. And I think that's super important direction for us, and I'm really excited about it.

Patrick Pichette

Susan, on social?

Susan Wojcicki

Yes, so I think the first thing I would say about social is that we're very early right now. And really our focus with Google+ will be to focus on making sure that we have a wonderful consumer and user experience. From a targeting perspective, there are a number of signals that we use right now. Obviously keyword on Search, contextual, interspaced advertising, demographics, and social signals overtime can be an important part of that. But it would be one of multiple ways that we actually do targeting. When we did rollout Google+, we do have pluses on all the ads this is what we do in search results. So if the user does click on it, and someone on their circle has actually does a query and triggers that, then there will be social annotations, which will be useful information for the user to see that their friend has +1-ed that ad.

Operator

And we'll go next to Ben Schachter with Macquarie.

Benjamin Schachter - Macquarie Research

Congratulations on the execution and the launch of Google+. Larry, at a high-level what, if any, are some of the key differences on how you think about managing specifically the economic model of the company today versus when Eric was CEO? Specifically any changes to target margins, revenue growth targets, et cetera? And then separately, on Mobile Search specifically, it's clearly been successful in terms of search share. But when we're trying to figure out the overall impact to net revenue in kind of balancing out some of the positives like incremental searches and share gains and higher click-through rates, but also having the headwinds of TAC payments to partners and lower CPCs, how should we think about the overall net impact of Mobile to the business?

Patrick Pichette

Why don't I'd take the second part of that question, and then Larry can talk about the economic model versus in the context of what you said. But for Mobile search, you have to go back and focus on what we focused on. Build businesses that are going to be billion-dollar businesses and that actually contribute significant operating dollar margins. These are businesses that scale to a humongous scale as they grow. So for us, that is the focus that we have. And the second piece in the specifics of Mobile is we really see Mobile a bit like Search was in 2001, 2002, 2003. All these formats are so new that you know that there's so much more room for optimization on top of it. So it is in fact a bit of a mistake to kind of say okay, today whatever we have is a

good proxy for what the future will look like. And that's why we're excited about it. And that's why we focus so much on Mobile. For the economic model and how we run the company, maybe Larry, your thoughts on that?

Larry Page

Absolutely, thanks for the question. I think certainly Eric is a great partner and leader for me and for Google for the last 10 years, and continues to play a big part in the company. So I don't think there's, like we said before, there's no major changes in what we're doing. And I'll reiterate maybe a little bit and add a little detail to what I already said. I think about really in our products in 3 separate categories. First, through Search and our Ads business, which is the core driver of revenue for the company. We really invest in that, we work hard on it. Next we have businesses that are enjoying really high consumer success. For example, YouTube, Android, and Chrome. And we invest in those in order to top them for long-term success. And we have some new businesses on Google+, Commerce, and Local that we're really excited about and are at pretty early stage and those things we invest in as well. And we don't do things that we don't think will generate really big returns over time. So we're optimizing for our long-term economic success. But we do have these very different buckets of things that we work on.

Operator

And we'll go next to Ross Sandler with RBC.

Ross Sandler - RBC Capital Markets, LLC

Two questions. First on Google+ and then second on Google Offers. So on plus, we haven't seen real integration. We know it's only a couple of weeks old but with Google's kind of core competencies around search and other things that you've been very successful at in the past. So can you talk about plans on integrating some of Google's core strength into Google+ to further, I guess, differentiate the products from other services that are out there? And then on Google Offers, can you just talk about your overall strategy in terms of rolling out offers? You're in 4 cities today. How fast do you think you're going to accelerate into these newer cities, and is international territories also on the roadmap and the near-term for Offers?

Larry Page

I'll answer the first part, this is Larry. Google+ actually has a lot of interesting product integration. The black Google bar that you see is an entry point and notification point for Plus across basically all of our properties. And we're really excited about that, and think it's a big deal.

Suffice to say there are many things that you would do with Plus and with +1 that affect what you would see in search results. Like I mentioned, when you +1 something, your friends will see it in search. So absolutely, and I hope it was clear that was our strategy, but we're very focused on improving all of Google, improving the sharing and identity across all of Google.

Patrick Pichette

Maybe Nikesh can give a comment on the rollout of Google Offers.

Nikesh Arora

Thanks, Patrick. We won't give out details on how we rollout our offer strategy. I think Susan said it very well in our overall strategy, because Offers for us is not just an isolated event. It is a combined, a bit of a commerce offering, which includes their Mobile phone and other things we talked about. We were very happy with the rollout we've had in the one city where we've been for a while, which is Portland, and we just rolled out 2 more cities earlier this week. So from our perspective, you can expect us to roll out other cities, but we're going to be testing and looking at the models see what's working and what's not working because we want to build the next version of how we rollout an Offers product. So stay tuned.

Operator

We'll go next to Brian Pitz with UBS.

Brian Pitz - UBS Investment Bank

Two quick questions. As we note the proliferation of the newer, richer ad formats like product image ads that we're seeing more and more of on your site, can you help us better understand the impact on paid click growth specifically? And then separately, can you also give us a little more color on some of the [indiscernible] quality changes you're doing on the network? Any commentary on how much impact to growth of AdSense that had this quarter and how long should we expect to see more than expected impact from continued quality changes?

Patrick Pichette

Why don't I let, actually, Susan tackle those questions? Susan?

Susan Wojcicki

On the richer ad formats, we see a few important opportunities for us, and what we feel about them is it gives us the opportunity to make those ads better for the users. And as we can create better experiences for our users,

they're more likely to have the information that a user wants. And so what we'd hope to see is a click-through increase over time. And hopefully, for the advertiser on the back end, a better conversion. So in terms of click growth, and what's actually driving the click growth that we see, it's a matter of factors. One of them is always going to be query growth that we have. Second thing would be on improvements that we have to our back end quality models. So the better the quality model is, the more likely we are to actually match the right advertisement to the right user. And we had a number of good ads, as I mentioned, not just good, we had great ads quality launches this quarter, and a number of ad formats that made the ads more readable. And by making them more readable, the users are more likely to click on them. And that turns into click growth. And then on the last question that you had, which was Panda, Panda was a change made by the search team with the goal of improving overall search experience. There was, as we talked about last time, some negative effects from the AdSense partners. However, Panda does -- or any search quality that we make, does have a change of ranking, which means that there are different sites that wind up getting traffic. And that those sites may adjust their monetization strategy over time. And so it may just take some time for that to actually balance out. And also, in terms of the last question, we don't really comment about future changes that we're going to make, but we're always thinking about the right way to continue to improve the search results for our users.

Patrick Pichette

Panda, once again a great example of putting the user first ends up benefiting everybody in the end, the publishers, the advertisers, and the users.

Operator

And we'll go next to Justin Post with Bank of America Merrill Lynch.

Justin Post - BofA Merrill Lynch

Larry, thanks for joining the call. And while we have you, I'm just going to ask you a question I get all the time. How focused is senior management on the stock either as an employee retention tool or a measure of management's performance over, say a 3 to 5 year period? And then secondly, if I could just ask about the local opportunity, it looks like a lot of launches happening for Google. Do you see it as a different ad market than your current search ad market? And how might your model be different than some of the larger players in that market currently?

Larry Page

We have a lot of stuff to do here at Google, and unfortunately one of the things we don't get to decide is our stock price. So you all are in charge of that. I think we're really focused on our long-term success as a business and the kind of things I mentioned already are absolute, overall profitability over the long-term and our revenue growth. And so, we tend to focus much more on that, with a much more long-term view than we do on our stock price.

Patrick Pichette

Susan, views on the difference and the similarities between the local and our traditional ads market.

Susan Wojcicki

Yes, Local can be thought about 2 different ways. Local can be the large retailers who have many different points of presence. So, for example, Starbucks or Pizza Hut or any retailer which is a large holding company or one large retailer, but then has many different local points of presence and then there's a separate bucket which are the small Joe's coffee shop example. And both of them need different things from a product perspective in order to be able to advertise more broadly. And we are working in both buckets to solve and make them advertisers on AdWords with solutions that will work for them. The large ones need functionality of how do I run a campaign in all of these different locations with different keywords, different pricing. And so we're working to enable location in our AdWords campaigns where you're managing a large account to make that much easier. The Joe's Coffee Shop example, what we're working on is enabling signing up for AdWords to be a much easier experience. So we actually have a product that we released this quarter called Google Boost. And Boost, a product is a 1 page, 5 minute sign-up for advertisers. It's very easy to sign-up. We haven't marketed it a lot right now but we have seen good success with our advertisers. And we're hoping to make that more known to our advertisers.

Patrick Pichette

The last piece in the puzzle is, obviously Susan, Mobile, which is completely integrated from an ads perspective and targeting as well.

Susan Wojcicki

Yes, the other thing too is we would like to make all of our products be accessible from a Mobile perspective. Click-to-Call would be an example. Click-to-Call is really nice so that as someone, for example, is local walking down the street, they can actually call. But it's also really nice from the small retailer perspective, because they can understand that they're getting a call and they're getting a lead, which for them would be much more tangible

than actually a click to their page. So we're investing very heavily in that in terms of Click-to-Call technology and the good tracking for the local advertisers.

Operator

And we'll go next to Jeetil Patel with Deutsche Bank Securities.

Jeetil Patel - Deutsche Bank AG

Two questions. I guess first of all, you've got obviously quite a few products and applications that have had success over the years. Kind of that are out there obviously Search, Gmail, Chrome, Android et cetera. I guess as you think about next generation of consumer relationship and stickiness, how do you think about like integrating a lot of these core assets together in terms of building a consumer relationship, which kind of moves seamlessly from all these different solutions and formats out there, as well as devices? And then second, maybe around Google+, obviously it's only been 2 weeks now. But maybe can you talk about the overall trend in terms of 10 million users? How does that compare against maybe the early days of how Android or Chrome or maybe even search or mail ramped? What kind of trajectory or what kind of trend schedule does it look like right now if you were to pinpoint it against another product in the business?

Larry Page

We are -- on the integration point, we obviously have a lot of different products that do different things for different people. And we know one effort that I mentioned, I've been really excited about, is this visual redesign. And I also mentioned the bar that goes across the black bar that goes across with Google+, that gives you a notification on sharing and so on. We're definitely working hard to integrate our products better to make the user experience simpler, intuitive and beautiful and consistent. And I'm really excited about our progress just in one quarter on that and I think you'll -- we're certainly working hard on that. And we have to continue to over time. On the Plus growth question, we've been very, very excited about the growth we've seen and the engagement we've seen. Over 1 billion items shared and received in a single day. And I think that for us, there's a lot of barriers to use Plus right now. One thing, you have to be invited and so on and it's still in field trial. So I think given all that, were just extremely excited about that. But it's very early days. It's been less than 2 weeks since we released it into field trial.

Operator

And we'll go next to Jason Maynard with Wells Fargo.

Jason Maynard - Wells Fargo Securities, LLC

First on Local. You've got a lot of interesting services and capabilities. But they're still fairly disparate and in some instances there's some overlapping features. I'm just curious, from an end-user perspective, how are you thinking about bringing together your various local commerce products? And then maybe to follow up on the Google+ question, since it is so early, what are your longer-term goals for Plus? I mean measured by their users or number of items shared. How are you thinking about this over say, a 2 year timeframe?

Larry Page

I'll take the second question first, on the Plus, how would we think about success of it. I think we are really, obviously, like I said we want people to make products that everybody uses 2x a day, like their toothbrush. We'd certainly think about plus that way, and also just generally having really great sharing experience and identity experience across Google and all of its products. And so that's kind of how we think about the success there I think it's pretty straightforward. On the first question, integration? Patrick, do you want to take that?

Patrick Pichette

Let me say just that what's been really cool about local for us, in the addition to what Susan has mentioned a few minutes ago is, you have to think of it as we are in fact assembling all the pieces of the puzzle. Local is actually a quite complex experience, but when you have Maps, you have Mobile, you have Wallet, you have all the ads serving, you basically have the pieces of the puzzle to succeed, and it's not as much what was yesterday's tools that we had, and how do we evolve only yesterday's tools, it's about taking those pieces of the puzzle and really creating true innovative services. And that's how we have to think about local. And that's why it's not obvious. But if you look at the arsenal we're building, it's actually quite formidable. So that's why we're excited by that. Thanks Jason for your question.

Operator

And we'll go next to Doug Anmuth with JPMorgan.

Douglas Anmuth - JP Morgan Chase & Co

I wanted to ask 2 things. First, Patrick, can you give us some color on the mix as headcount additions? And in particular, if you look at R&D it looks like it was flat sequentially, but yet you added more than 2,000 people during the quarter. So I'm hoping you can provide some color there. And then

secondly can you give us some context just in terms of how you think about the Display business and whether you need more O and O inventory.

Patrick Pichette

I'll answer the first one, and then I'll let Susan answer the second. On headcount, again, as we said on the call, roughly, we have IT for 450 so roughly about 2000 for the quarter, and Larry comment on that. And we -- there's still a huge amount of engineers in that. It just happens that R&D is actually in every line item. So you'll find in many other areas of our P&L. And so you should not worry. We have a complete focus to make sure that we actually have a majority of our hiring that is focused on Engineering, which is really the core of the business and then we continue to kind of -- then you have the mix of sales and then just general overhead. It's really engineering and sales that have been the focus in that sequence. For Display, I'll let Susan talk about it.

Larry Page

I'll just add too in the headcount question. None of the focus there has changed substantially from our past.

Susan Wojcicki

On Display, our biggest O and O property is obviously YouTube. And given the numbers that we saw, we've seen tremendous growth there and a huge opportunity to monetize video as more users come online, and more content lines are being uploaded on YouTube. But the strategy, and our Display strategy overall is dependent not just on O and O. It also has many other components. The first of being to be a platform to enable advertisers and publishers to much more easily buy and sell Display advertising. And then second, to enable all of the sites out there, of which there are of course many, many millions, hundreds of millions of them, for them to be able to monetize and sell display advertising and for us to be able to help them as part of that process and via our network, where we have a lot of different targeting techniques to try to serve the right ad to those users. So really our strategy is part O and O with our sites like YouTube, but then also to continue to build a great network and platform products to that advertisers and publishers across the industry can serve Display advertising.

Operator

And we'll go next to the line of Anthony DiClemente from Barclay's Capital.

Anthony DiClemente - Barclays Capital

I have one for Patrick and one for Larry. Patrick if you just isolate the 6% sequential growth in cost-per-click versus last quarter, wondering if you could help us understand the driver of that acceleration, and moving forward, should we expect that to continue or moderate, given that as Mobile queries start to take up more of the query mix? And then question for Larry, it would appear that in social media that switching costs for users are high perhaps years of photos on a social network platform. And as you look at Google+ and the growth there, what are the most compelling offsets to those switching costs you think or do you perhaps see a future where folks can simultaneously be a part of multiple social networking platforms?

Patrick Pichette

So why don't I let Susan actually give you a bit of color on our CPC and evolution, and then Larry will take on the latter, the social one.

Susan Wojcicki

The drivers of CPC, there are few of them. One of them in this quarter was FX, certainly. But we've been really focused on our ads quality improvements, and how do we continue to obviously make our ads better for our users and for our advertisers. And in doing so, we've actually -- we done a lot of optimization of our ads that appear above the search results like site links, some of the ad changes in the formats that we made this quarter, and a lot of the ads that appear above the top search results tend to be higher CPC because they're the first 3 ads. So as we continue to optimize and really drive a lot of the increased click-through and visibility for the ads that appear above the search results, you will see -- since those tend to be higher CPC because they're at the top of the results, you will see some of that increasing.

Patrick Pichette

Larry on sell-through and switching costs?

Larry Page

I think we've been really excited about Google+ really improving the overall social experience and making it more like how you would share in real-life. And that's really a different product than is out there now. And we're getting just rave reviews for that. People really like being able to share with more discrete groups in an easy way, intuitive way, and there's a lot of magic built into the product that causes that. And as you say, you asked about the photos, we actually have a really great photo experience on the Android. Like if you take a picture on Android and you have Google+ client, which you would have, if you're using it. It uploads your photos automatically, and it's

super easy to share them and post-them to your friends, or your family or whatever. It's a really, really great experience. So there is legacy in Google, as a company, believes in users owning their own data and being able to easily move it out of Google. As some of our competitors don't believe in that. We think the users will eventually move to services that are in their best interest and that work really well for them.

Operator

We'll take our final question from Jim Friedland with Cowen and Company.

James Friedland - Cowen and Company, LLC

I wanted to ask a question on -- or follow-up on where you guys said that you're a little ahead of where you expected to be on hiring. Should we think about the hiring and particularly in R&D sort of coming in waves where you hire a bunch of people, get them integrated, it sort of slows down and picks up again? And then the second question and just on the P&L, other cost surviving users of percentage of [indiscernible] TAC seems to be a little high. Is that coming from increased Data Center depreciation or is it may be coming from YouTube and content related costs?

Patrick Pichette

I'll answer the first one, the latter one, and then I'll let Larry talk about hiring in general. The P&L, yes, it is a combination of factors this quarter. So in that cost is also included headcount. And so headcount is actually increased. Power is increased because of seasonality. It's summer now, so our power is a little higher. And we've also had kind of catch up on expenses on some of the equipment. So there's been a bit of a between Q1 and Q2, there's been a bit of a cleanup in some of the areas of equipment that have actually slightly deflated Q1 and inflated Q2 as we finish the clean up, so that was a bit of a catch up there. So I wouldn't read the data point between Q1 and Q2. Don't create a graph with that, with that line. But it's a bit of everything, including a bit of cleanup and some of the equipment accounts. For the issue of hiring, I'll let Larry actually talk about general where we stand right now.

Larry Page

That's a great question. I think just a couple of factors that affected that and I think you know we implemented compensation changes in Q1. We increased our employee compensation. And they've had even more positive effect on hiring and retention than when we expected. It's been a super successful change. And I think in general this has more excited people who want to work at Google and who want to stay working at Google than we

expected. And so that's had some impact on those numbers. Of course there's a limit on how many we can -- and how fast we can productively hire, and I said this in my remark, I think kind of my judgments where at the edge of that piece being reasonable. We're just adding a lot of people. And I'd say that we're always looking for good people, and we're always -- the exact rate is going to depend on success and where we really want to invest in the company. We have a really strong management team. I said that's working together fabulously, and we can absorb those hires and put them to use well. But like I said, we're definitely -- we're surprised that the success of our previous changes around compensation as well.

Patrick Pichette

With that, I just want to thank Larry for joining us today, and Nikesh, and Susan for the comments as well as the Q&A. I want to thank, once again as I always do, all the Googlers out there. Our fantastic Googlers that have made this quarter possible. And all of the innovation, especially I think it's worth mentioning, our Google+ team that has done a phenomenal job in this launch. So 2 thumbs up.