Operator

Good day, ladies and gentlemen, and welcome to the Google Inc Second Quarter 2015 Earnings Conference Call. At this time, all participants are in a listen-only mode. Later we will conduct a question-and-answer session, and instructions will follow at that time. [Operator Instructions] As a reminder, this conference call may be recorded.

I would now like to introduce your host for today's conference Ellen West, Vice President-Investor Relations. Please go ahead, Ma'am.

Ellen West

Thank you. Good afternoon everyone and welcome to Google's second quarter 2015 earnings conference call. With us today are Ruth Porat and Omid Kordestani. As you know, we distribute our earnings release through our Investor Relations website located at investor.google.com. Please refer to our IR website for our earnings releases as well as the 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 later today.

Now 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, our long-term growth and innovations, the expected performance of our businesses, and our expected level of capital expenditures. These statements involve a number risks and uncertainties that could cause actual results to differ materially. For more information, please refer to the risk factors discussed in our Form 10-K for 2014 filed with the SEC. Any forward-looking statements that we make are based on assumptions as of today, and we undertake no obligation to update these statements as a result of new information or future events.

During this call, we will present both GAAP and non-GAAP financial measures. A reconciliation of GAAP to non-GAAP measures is included in today's earnings press release. The press release and an accompanying investor presentation are available on our website at investor.google.com.

I'll now turn the call over to Ruth.

Ruth Porat

Thanks. We had strong performance in the second quarter, notwithstanding the continuation of substantial currency headwinds. Key highlights this quarter include ongoing momentum in our core search business particularly mobile, complemented by significant growth in YouTube revenues.

In addition, we are increasingly benefiting from the shift towards programmatic advertising, particularly among brand advertisers. These strong top-line results were complemented by ongoing operating expense discipline in the quarter as reflected in 31% year-over-year growth in GAAP operating income and 16% year-over-year growth in non-GAAP operating income. I will first go over a summary of the quarter followed by specific financial details and conclude with things for the near-term. Omid will then cover the business and products highlights of the quarter after which we will take your questions.

Beginning with the summary of our financial performance, total revenue was $17.7 billion, up an 11% year-over-year, and up 3% sequentially. As a result of the ongoing strengthening of the U.S. dollar, we realized a negative currency impact on our revenues of $1.6 billion, or $1.1 billion after the benefit of our hedging program. Holding currency constant to prior periods, our total revenue grew 18% year-over-year and 4% sequentially.

On a GAAP basis, operating profit was $4.8 billion and the operating margin was 27%. On a non-GAAP basis, that is excluding stock-based compensation, operating profit was $6 billion and the operating margin was 34%. GAAP net income was $3.9 billion, up 17% year-over-year, and up 12% versus Q1. Non-GAAP net income was $4.8 billion, up 18% year-over-year, and up 8% versus Q1.

GAAP earnings per diluted share for Class A and B shares were $4.93, and for Class C were $6.43. Higher EPS for Class C reflects the impact of the adjustment payment made in Q2. Non-GAAP earnings per diluted share were $6.99. As detailed in the earnings slides on our IR website, stock-based compensation totaled $1.1 billion, up 29% year-over-year and down 6% sequentially.

Let me now turn to key elements of our financial statements. Starting with our primary revenue sources, Google sites revenue was $12.4 billion, up 13% year-over-year, and up 4% sequentially, notwithstanding currency headwinds. Year-on-year and quarter-on-quarter growth reflect continued strength in search, particularly mobile search. We continue to close the gap between mobile and desktop search monetization.

Specifically on mobile, we’re pleased with our ongoing progress resulting from our focus on user experience, ads quality and online to offline commerce initiatives. The combination of these efforts improves the effectiveness and value of mobile for users and marketers alike. Desktop search delivered solid revenue growth again this quarter. YouTube again delivered substantial growth in user engagement globally, particularly on mobile, which translated into strong adoption of our TrueView ad format.

Growth in watch time on YouTube has accelerated and is now up over 60% year-over-year, the fastest growth rate we've seen in two years. Mobile watch time has more than doubled from a year ago. Network revenue was $3.6 billion, up 2% year-on-year and up 1% sequentially, continuing to reflect the diversion performance of programatic on the one hand and our legacy network businesses on the other.

Our programatic business including AdExchange and DoubleClick Bid Manager continue to deliver strong year-over-year and sequential performance then more than offset lower results in AdSense for Search. We remain committed to policy changes that improve the user experience notwithstanding the fact that these policies have a negative impact on AdSense for Search revenue. Other revenue was $1.7 billion, up 17% year-over-year and down 3% sequentially. Given the geographic mix of our Play business, FX also had an impact on other revenue. Year-over-year and sequential movements were driven by substantial growth in Play offset by decline in the hardware sales.

Next revenues by geography. U.S. revenue was up 16% year-over-year to $8 billion and up 4% versus Q1. UK revenue was up 4% year-over-year to $1.7 billion and flat sequentially. In fixed FX terms, the U.K. grew 11% year-over-year and was flat quarter-over-quarter, rest of world revenue was up 8% versus last year to $8 billion and up 2% versus Q1. In fixed FX terms, revenues were up 22% year-over-year, and up 4% sequentially highlighting both the strength of our global business as well as the impact of FX.

Finally revenue monetization; as a reminder, these metrics similarly reflect currency movements. Aggregate paid clicks grew 18% year-over-year and 7% sequentially. Aggregate CPCs were down 11% year-over-year and 4% sequentially. In terms of the drivers within Google sites paid clicks were up 30% year-over-year, and up 10% sequentially in particular reflecting growth in YouTube TrueView as well as in mobile.

Google sites CPCs were down 16% year-over-year and down 5% sequentially. Mobile CPCs continue to strengthen and the gap to desktop continues to grow as I previously noted. The decline in CPCs reflects the impact of YouTube TrueView, which is a growing percentage of overall sites clicks mix and where CPCs remain lower than on our other platforms.

Network paid clicks were down 9% year-over-year and down 2% sequentially reflecting the impact of our ongoing policy changes designed to reduce the lower quality inventory on AdSense for Search consistent with our focus on improving user experience. Network CPCs were down 3% both year-over-year and sequentially.

Let me turn now to expenses. Traffic acquisition costs were $3.4 billion, or 21% of total advertising revenue, which was down slightly sequentially. Trends within sites and network TAC remains flat, due to mix shifts in partners, products and devices. As a reminder, the sites TAC line includes the TAC that we pay to search distribution partners for distributing Google Search as distinct from their own branded search.

Non-GAAP other cost of revenues was $3 billion in Q2, up 12% year-over-year, and up 7% versus Q1. Year-on-year and sequential growth were driven by costs associated with operating our data centers including deprecation as well as content acquisition cost primarily for YouTube and Play. Non-GAAP operating expenses were $5.4 billion, or 30% of revenue, up 11% year-over-year and down 1% versus Q1.

The increase in operating expense versus 2Q 2014 primarily reflects R&D expense attributable to increased hiring of engineers and product managers. Headcount increased 18% versus last year and 3% versus 1Q 2015 with total headcount at quarter-end of approximately 57,100. The deceleration in year-over-year growth and decline in quarter-over-quarter operating expenses reflects in part discipline in expense management and in part lower legal expenses than in comparable periods; a breakout of individual operating expense lines is available on our earnings slides.

Other income and expense was $131 million with interest income offset by higher expenses from our FX hedging program. The effective tax rate was 21% for the second quarter. As noted in our press release, in Q2, we identified an incorrect classification of certain revenues between legal entities. We revised our income tax expense for the relevant periods beginning in 2008 through the first quarter of 2015 in the cumulative amount of $711 million. The income tax adjustments were not material to the effected periods; more detail is available on our earnings slides.

Turning now to CapEx and cash. CapEx for the quarter was $2.5 billion, primarily for production equipment and data center construction. CapEx spend was lower versus last year and last quarter reflecting a bit of a digestion period after an extended period of investments in both data centers and the requisite machine deployment. We continue to view our computing infrastructure as one of our most strategic assets. Operating cash flow was $7 billion with free cash flow of $4.5 billion resulting in a cash balance of approximately $70 billion at the end of the quarter of which approximately $40 billion or 58% is held overseas.

Let me close with five topics of focus for the near-term, first on revenue growth and drivers. Our strong revenue growth in the second quarter, notwithstanding the adverse effects of the strong U.S. dollar evidences the health of our core search business most notably mobile, complemented by growth in YouTube and programmatic advertising. Our earlier stage products such as Fiber, Google Life Sciences, and Nest service longer-term sources of revenue. Regarding these areas, we are focused on tight governance to ensure that the resourcing for them is appropriate and we'll talk more about these products in greater detail as I get settled in.

Second, the sequential deceleration in expense growth achieved in the second quarter reflects in part the benefit of expense discipline discussed in prior calls. A key focus is on the levers within our control to manage the pace of expenses while still ensuring and supporting our growth. We will do this while we continue to invest in engineering talent to keep us preeminent in innovation globally.

Third, the pace of growth in capital expenditures over the last several years has been significant. Although the vast majority of CapEx to date have been to support our core business, growing requirements for newer products underscore the increasing importance of optimization across the many opportunities ahead of us. Fourth, our cash balance grew again this quarter, which of course gives us more strategic flexibility. We remain focused on judiciously capitalizing on the strategic opportunities that we have, which are many. And the key issue is how we prioritize our capital allocation, given the breadth of opportunities.

Finally, as Larry has frequently noted, Google's goal is to develop great new services that significantly improves the lives of as many people as possible. Solving problems for users at scale ultimately results in monetization opportunities. How we prioritize and focus on these opportunities remains paramount, both for our employees, who remain inspired by the opportunity to work on the most cutting edge developments with maximum global impact and for our shareholders. I look forward to working with you.

I will now turn the call over to Omid, who will cover the business details of the quarter.

Omid Kordestani

Thanks Ruth. It's great to be here to talk with everyone again. Since we last spoke, Google has been very busy hosting our customers and developers from across the globe at events ranging from I/O to the DoubleClick Leadership Summit to BrandCast. We're seeing great momentum and results across the company.

As you all saw at IO, we continue to invest in innovation across our core products. To call out just one, the new Photos app is a great example of how we're combining the power of a machine learning, search and beautiful design, something that Google is proud to bring together in such a great package for our users. Our investments in machine learning have applications across the company and have real potential to improve our business. For instance, machine learning helps us to improve and adds visual design to maximize its performance. There's enormous opportunity here.

I want to quickly share a few highlights of the past quarter and then spend more time talking about our progress in what continues to be our two biggest focus areas and growth drivers: mobile and video. First, our core products continue to do well and users love them. In fact, Google Search, YouTube, Android, Chrome and Google Maps, each have over one billion users. We also continue to see great partner momentum across the Android platform. The Android phone ecosystem started with one device, one carrier and one OEM, the T-Mobile G1 in 2008 and has grown now to over 400 OEMs and over 500 carriers, who make over 4,000 distinct devices. This is a testament to our great progress on both the tech and partnering fronts.

Google Play continues to grow at an impressive clip. Google Play games has added more than 180 million new users in the past six months and continues to be one of the fastest growing mobile gaming platforms in history. In addition, we're seeing strong momentum around Google Cloud platform, with a range of great new features, new major customer announcements like HTC and JDA software and our collaboration with Broad Institute.

And on the advertising side as a trend towards programatic ad buying continues, we're helping clients succeed in a multi-screen world with our DoubleClick platform. We recently expanded cross device measurement to all of our DoubleClick advertiser products, so marketers can measure these conversions for all of their campaigns. And to help publishers, we've recently announced full DoubleClick support for native ad formats.

Now I'll spend a few minutes diving more into the big areas of opportunity for us, the shift to mobile and the continued growth of online video. I talked last quarter about the shift we see in consumer behavior as people turned to their phones throughout the day to decide what to buy or do. Google's role has always been to meet people's needs in the exact moment they are looking and those moments are increasingly happening on mobile devices.

More Google searches now take place on mobile devices than on computers in ten countries, including the U.S. and Japan, two of our largest markets. And we know that when people search on their mobile phones, they're looking for immediacy and action. In fact, 30% of mobile queries are related to location and our efforts around local search are helping consumers to find relevant information fast.

We’re investing in creating great mobile experiences for people across Google products. As Sundar and his teams showed at I/O this year, there is a lot to be excited about from now on Tab to Android Pay and much more. As I mentioned, one of my favorites is the new photos app, where you can keep and organize all of your memories and easily share and save what matters to you. If you’re like me and have an overwhelming number of photos on your phone, the photos app makes taking, organizing and finding pictures much more manageable and enjoyable and it’s getting better every day.

In addition, our teams have made great strides to help users find what they need within third-party apps through indexing. We now have 50 billion links within apps index and 25% of signed in Google searches on Android now return deep links, taking users right to content within an app or to a link so they can install it. We also recently started showing such links in search results on iOS, developers like [indiscernible] are really seeing a boost in traffic as a result of deep linking. We also added now cards for more than 100 apps like OpenTable and Spotify and we have extended Google Voice actions to third party developers, so we can say things like, okay Google listen to MPR.

Alongside our efforts to make mobile better for users, we’re continuing to help marketers succeed in today’s mobile world. For instance at I/O we recently announced universal app campaigns, which will let developers easily reach users across Google search, the add mob network, mobile sites, YouTube and Google Play. Marketers just tell us what their ad will say, the audience they want to reach, and how much they want to spend and our ad systems will do the rest to help them maximize performance.

We introduced new mobile ad formats like automobile ads, which take you directly to a carousel of vehicle images important details like estimated MPG, and links to nearby dealer listings. And just yesterday, we announced purchases on Google, which makes it easier for people searching on Google to buy things right from their mobile phones.

I want to turn now to YouTube, which is showing strong momentum with users and advertisers as we reinvent the television experience for the digital age. On mobile alone, YouTube reaches more 18 to 49 year old in the U.S. than any U.S. cable network. And the number of users coming to YouTube, who start at the Youtube homepage similar to the way they might turn on their TV is up over three times year-on-year plus once users are in YouTube, they are spending more time per session watching videos, on mobile the average viewing session is now more than 40 minutes up more than 50% year-over-year.

As consumers continue to shift their content consumption from television to digital, brand dollars are flowing – I am sorry following, which we're seeing an upfront buying through our Google preferred model. Compared to the same period after BrandCast as last year, Google preferred commitments in the U.S. were three times higher. We're also seeing great adoption of our video ad formats like TrueView and continue to help marketers engage and connect the consumers in new ways. The number of advertisers running video ad on YouTube is up more than 40% year-over-year and for our top 100 advertisers, the average spend per advertiser is up over 60% year-over-year. We recently introduced a new feature for TrueView that allows brands to automatically insert product information, images and pricing into their video ads.

And as advertising increasingly shifts towards programatic buying brands can now easily buy TrueView ads programatically through DoubleClick Bid Manager. All this is helping our content creators build the next generation of media companies doing what they love making great videos. The number of channels earning six figures per year on YouTube is up 50% year-over-year.

One of the key reasons for this success is our Content ID initiative which is used by more than 8,000 partners who have claimed over 400 million videos helping them control their content on YouTube and make money on videos containing copyrighted material. So as you can see it's been a very busy and successful quarter, we are super focus on our key goals of delivering amazing mobile and video experiences and there is lot more coming in the next few months including the Android M release, now on tap Android Pay, and YouTube gaming.

Thank you to all the Googlers around the world for their great work everyday. And now back to Ruth.

Ruth Porat

Thank you. In my comments, I meant to note that the gap between mobile and desktop continues to [Technical Difficulty]. And with that I'll turn it back to Ellen.

Ellen West

Great, thank you [Technical Difficulty]

Question-and-Answer Session

Q - Unidentified Analyst

Really had build up headcount and data center capabilities. Just where are you on capacity and really what was the purpose of this big build up, what kind of capabilities does that give Google today? Thank you.

Ruth Porat

Thank you for that question. First I do want to clarify one thing in my comments on CPCs, I meant to note that the gap between mobile and desktop continues to narrow obviously an important trend wanted to clarify that. So look in terms of headcount in data center capabilities and what that does for us. As I said in our view, our infrastructure is one of the most strategic assets that we have and as we talk about what happened in the second quarter it reflects the fact that there can be some variability in the cadence of spend and so while overall capital intensity was lower in Q2 than in prior year and prior quarter, that's a more an issue of how spend is faced during the year but the main point as we do computing capacity as a strategic asset it provides us with the flexibility necessary for growth.

And as I try to convey as well obviously it's a priority to achieve efficiencies were possible and particular given some of the newer opportunities that we have. And so we are just beginning the 2016 budgeting process quarter that is prioritization but it really has been about strategic flexibility and the underlying strength of all that we do.

Unidentified Analyst

Thank you.

Ruth Porat

Great. Operator, we'll go to our next question, please.

Operator

And our next question comes from Ross Sandler from Duetsche Bank. Your line is now open. Please go ahead.

Ross Sandler

Great, I just had two questions. Omid, the U.S. reaccelerated looks like from 12% to 16% in the quarter, can you just give us a little color of what drove that was it more a function of core search and mobile picking up or – for YouTube? And then, Ruth did you mentioned in you prepared remarks that a lot of the expense deceleration was put in place before you got to Google. So now that you've been in the seat for a couple of months, can you talk about what you're seeing and what potentially you could do in addition to what was in place in 2015 before you got there? Thank you.

Omid Kordestani

Thank you, Ross. Our performance really reflects the fact that we have a diverse set of products that are doing well. We have strength in core search obviously and in particularly mobile, YouTube and programmatic we're seeing a lot of strength. We saw a nice pick up in a number of verticals in Q2 coming off weather-related weakness in Q1. And this quarter we're seeing retail and travel being stronger verticals in search. As to the second part of the question, I have Ruth to address that.

Ruth Porat

And so with respect to expense management obviously a lot has been done on expense discipline has been discussed on calls for a number of quarters in. And I think it's fair to say proper resource allocation stretches across OpEx and CapEx and it's about prioritizing our investments and ensuring that we're being efficient and effective with our spend. To be clear, the priority is revenue growth and we have a breadth of opportunity, but pursuing revenue growth is obviously not inconsistent with expense management.

And so as I noted we're just starting the 2016 budgeting process, in my experience the best way to slow the rate of growth in expenses is to work closely with business leaders really anchored in data, so together we can identify ways to prioritize resources and really continue to extend the discipline that we've talked about. And given my early conversations with our business leaders, I look forward to this exercise over the next couple of months and we're very engaged with it. Great, operator we'll take our next question.

Ross Sandler

Thank you.

Operator

Thank you. And our next question comes from Carlos Kirjner from Bernstein. Your line is now open. Please go ahead.

Carlos Kirjner

Thank you. I have two questions. Ruth can you help us understand Google's position vis-à-vis debt. It's probably not controversial that your debt level is much below your capacity. Are there any reasons why Google would not want to raise debt, if you had to finance a large acquisition and if yes, could you help us understand what these reasons are? And secondly, how do we reconcile the strength in mobile search with the fact that distribution pack grew only 6% year-on-year? Thank you.

Ruth Porat

So starting with your question about cash which – and whether we would issue debt, I think, the way I look at that is you're talking about overall efficiency of balance sheet and how are we using the balance sheet and I've slightly broadened the question more than what you did, but at the end of the day, our focus – my focus is maximizing shareholder value over the medium to long-term and that is about how effectively are we using our balance sheet where we investing and that could theoretically be a part of that. But if you step back as I've looked at it and the key issue is what do we need for working capital?

What do we need for CapEx? What do we need for M&A? What do we need potentially for capital return? How does one think about financing the various opportunities that we have and I would say it's early days, it would be premature to be more specific than that. But given this profitability of our business we have many opportunities given the growing mix of our business, we have opportunities, I would say allocation decisions are mutually exclusive, allocation can obviously change as opportunities evolve. But as we look at it, we have a breadth of opportunities, again I think it's premature to be more specific on that at this point.

Carlos Kirjner

How about the distribution TAC on growing 6% given the strength of mobile?

Ruth Porat

So as it relates to distribution TAC, sites TAC dollars are up modestly year-over-year and quarter-over-quarter and that's what I would really focus you on its the dollar change and obviously you know the 12%, but that's a good thing, because with those TAC dollars comes revenue. As a remainder TAC includes payments made to search distribution partners is distinct from YouTube and Play content acquisition costs, which are in other cost of revenue. So looking at this on a percentage of revenue basis, what you are seeing is the impact of YouTube revenue growth, sites revenue was up. But the associated content acquisition costs are reflected in higher other cost of revenue not in sites TAC.

Carlos Kirjner

Thank you.

Ruth Porat

Thank you. Operator, we'll take our next question.

Operator

Our next question comes from Stephen Ju from Credit Suisse. Your line is now open. Please go ahead.

Stephen Ju

Okay, thanks. So, Omid big picture in the outperformance of programatic in YouTube is interesting as it seems to beg the next question as you – your current list of advertising products now seems to touch all parts of the consumer purchasing funnel. So I'm wondering where you are in uniting all of the different pieces so that you can walk into a large advertiser and lay out the data, so that the 15 second TrueView spot that they ran turn into a list in the sales of X percent. Okay, thanks.

Omid Kordestani

Sure. It's a good question and in fact that's one of the areas that I really focused on after I came back and, it is a suite of products that's we are very proud of and working well for advertisers and what we like to say internally, as we like to have one Google represented to the customers so that in these conversations with them we really understand their objectives and really in the classic sense of the funnel you know we can start from the brand journey from the beginning to purchase across, search display video and then as you know we recently brought cross-device measurement to DoubleClick.

So, the focus is really on all aspect of this journey online to store we're showing how mobile ads are driving actual store visits for advertisers and your Brand Lift studies we're showing brands in real-time how their ads are performing, we done over 10,000 Brand Lift studies on YouTube campaigns alone. So its we really just excited about having this full suite now and being able to have the full coverage of this customer acquisition journey from branding all the way to conclusion of a transaction.

Stephen Ju

Thank you.

Omid Kordestani

Thank you.

Ruth Porat

Operator, we'll take our next question.

Operator

And our next question comes from Mark Mahaney from RBC Capital Markets. Your line is now open. Please go ahead.

Mark Mahaney

Great, thanks. Omid, you gave a lot of great data points on the growth in YouTube and stuff that's accelerated could you spend little bit more time on the why has YouTube seen this kind of reacceleration resurgence in growth. Do you think its part of a broader industry trend, the weakness in the upfront, offline is now coming online or is what else specifically, what specifically is YouTube doing to kind of better capture those dollars and then Ruth I know somebody ask you about that, logical follow-on question is the cash returns and share repurchases and dividends and just I know its early days but your thoughts on and your collective thoughts, Google how you think about that over the next few years when if ever it make logical sense to do that? Thank you.

Omid Kordestani

I'll start and hand it to Ruth. So its – I think it's really combination of all of the strength of YouTube coming together it starts with having over a billion users nearly almost one-third of all people on the internet everyday watching hundreds of millions of hours on the services and that creates billions of views and as Ruth mentioned the growth in watch time on YouTube accelerated in this now up over 60% year-over-year the fastest we've seen in couple of years.

And I think we are doing it also much better job with our products in our sales force to not only deliver for the creators on YouTube and do a better job of helping them monetize their contents and at the same time, then highlighting that success to programs like Brandcast where advertisers, agencies see that dynamic audience and service and then with the advertising products be able to then show them the real benefits of advertising and the ways that they can measure its effectiveness. So it's really all the pieces coming together for us and obviously we have a lot of work to do and we see still a lot of opportunity to enhance the service. So, I think you will see a lot of innovation coming from us both on the service front as well as on the advertising products.

Ruth Porat

Hey, Mark. As you noted, it is early days but the way I view any assessment of a return on capital for my prior answer regarding balance sheet efficiency is really in the context of maximizing stakeholder value over the medium to long-term.

And with return of capital it gets into the context of, how do you prioritize and allocate cash after an appropriate reserve for working capital amongst the CapEx, M&A and then potentially that capital return. And as I said, the allocation decisions are mutually exclusive, the profitability of our business gives us many opportunities, but the main point is to date the weakest return on investment here has been in our core search business including mobile search as a result of both smart M&A and CapEx. Here M&A, we built a lot of the growth engines today, YouTube and DoubleClick are great examples. Again this underscores the power of smart targeted acquisitions.

We also have a strong track record of investment in new products as you know well and the infrastructure to support explosive growth, our tech infrastructure I've already commented on is really unparalleled and we do view it as a great strategic asset and we've invested in it substantially over many years. So trying to gauge whether or how capital returns fits in, it's premature to do that and it's really looking across these various potential uses.

Mark Mahaney

Thank you, Ruth. Thank you, Omid.

Ruth Porat

Thanks Mark.

Omid Kordestani

Thank you.

Ruth Porat

Okay, operator, we will take our next question, please.

Operator

Thank you. Our next question comes from Eric Sheridan from UBS. Your line is now open. Please go ahead.

Eric Sheridan

Thanks for taking the question. Omid, you mentioned retail travel is through the stronger verticals advertising front and in the recent past, you guys have made a number of announcements around products that align your interest or more closely with suppliers, people who try closing the economic loop and you might be even moving down the funnel. How do you think about the opportunities for Google to sort of move down respective finals and industries where you do you already have a fair bit of expertise? Thanks.

Omid Kordestani

Sure. Thanks, Eric for the question. We're really focused on connecting retailers to consumers across screens and also reducing this friction involved in finding and purchasing products. All including local products and stores. So that entire journey and all the aspects of commerce is a great area of focus for us. And as users begin to – as they search, start their searches on mobile phones, we are continuously trying to find ways to improve their mobile shopping experience.

And as shopping experiences on these smart phones become easier and we focus on improving mobile conversion for advertisers. We are seeing great benefits from that, we just announced purchases on Google, for example, the smartphone only feature of the product listing ads an example. And again all of these are really for us the building blocks to help in reduction of that friction and bring the expertise we have and that understanding the immediacy, the local nature of these searches and understanding conversion and how to kind of put it all together for users, and for advertisers and machines.

Ruth Porat

Okay, operator we'll take our next question please.

Operator

Our next question comes from Douglas Anmuth from JP Morgan. Your line is now open, please go ahead.

Douglas Anmuth

Great thanks. Just to follow-up a little bit on the last one, Omid can you talk more specifically about the cross-platform efforts and estimated conversions in particular and whether you're seeing that prove more of the value across the platform.

And then secondly, you commented several times that the gap is tightening on pricing between mobile and desktop, can you quantify that by any chance and can you just talk about what you think drives that to tighten further, go forward? Thanks.

Omid Kordestani

Sure, I'll have Ruth take that second part. On the first part on this online to offline conversion efforts, we obviously know that mobile activities are influencing offline behavior and we're very busy investing in new dynamic products that help bring mobile users to stores. We're seeing strong results from clients using our tools to bridge this digital and physical world. And great adoption of local inventory ads, which help advertisers promote their store items to nearby shoppers. So again that's how the whole cycle of usage of smartphones and the immediacy come together.

And then we've created way for advertisers to measure the impact of these ads on store visits. So just to give you a couple of examples, Target, one of our advertisers found that mobile search ads greatly influence in-store store sales and using our store visit data they found that a third of their paid search ads resulted in a user visiting a target store during 2014 holiday season. So we love to continue working with them and other advertisers to show the results and then build on that.

Florida department store working with us found that 63% of their mobile influenced sales take place off-line. And so more and more we're doing these studies, we're putting the tools together for these advertisers and our partners, the merchants and finding ways for them to really quantify these benefits and just scale these programs for everyone.

Ruth Porat

And then as it relates to the second part of your question there are really two good stories here given the importance of search. Mobile CPCs up and desktop CPCs not declining so the gap is narrowing. On the mobile side as Larry said before with respect to desktop it took time to fully develop the pricing model and we remain focused on building the mobile ecosystem to have the right ad formats and measurement to take advantage of all the platform ads to offer features like estimated store visits, app install, the rengagement ads, cross device conversions are all part of this strategy.

And then on desktop, the business continues to grow. It remains a good contributor to overall results as we announced that the AdWords performance Summit in May ongoing developments in rich and useful ads that work across all screams including desktop, enable us to deliver the right answers for our users in the right moment in other words, ads format that accelerate time to conversion on both mobile and desktop and that's what's really narrowing this gap here.

Douglas Anmuth

Great, thank you.

Ruth Porat

Thank you. Operator, we'll take our next question.

Operator

Our next question comes from Anthony DiClemente from Nomura. Your line is now open. Please go ahead.

Anthony DiClemente

Hi, thanks a lot for taking my question. Ruth given your background, I just want to ask if you thought the regulatory backdrop for Google is in anyway analogous to the financial services industry and sort of what is your outlook for a larger player like Google in an environment of increasing regulatory pressure, particularly outside the U.S. and of course specifically for Google with the EC demanding changes to the search results, just wondering should we be concerned that that these regulatory pressures can ultimately have an impact on your business. Thanks.

Ruth Porat

Let's see, the industries are different, but as it comes to our business Google operates in a very competitive environment, there are many windows on to the web, choice, competition, investment are all going up, not down and we do look forward to continuing to work constructively with the EC to address any concerns they may have and regulators generally.

Anthony DiClemente

Okay, thank you very much.

Ruth Porat

Thank you. Operator, we'll take our next question please.

Operator

Our next question comes from Brian Nowak from Morgan Stanley. Your line is now open. Please go ahead.

Brian Nowak

I have two. The first one, Ruth, is going back to your comments on some of the earlier stage projects fiber life science that [indiscernible] focused on tight governance. Is there anyway you can kind of help us to think about OpEx or CapEx related to those projects at this point and how we should think about maintenance versus investment in OpEx and CapEx going forward? And then the second one just going back to the accelerating U.S. revenue growth, it sounds like mobile and YouTube are both doing pretty well. Can you just help us understand or are you seeing both accelerate – is U.S. search accelerating at this point or is it more so being driven by YouTube? Thanks.

Ruth Porat

Sure, so let me take your first question – first part of your question first. In terms of overall kind of the framework for thinking about our businesses broadly, I think a valuable framework to use is one that Eric and Larry have referred to for many years, namely the 70/20/10, 70% resources on the core 20% on adjacent areas, one point that included Chrome and Android and they are now in the core but it would include things like cloud and then 10% in additional new exciting opportunities in really sizable markets like Viber or what we're doing with Google Life Sciences.

And so in discussing this with Larry its clearest objective has been to instill within the culture this mission to drive not just important innovation associated with our core business but also to look for as he call them revolutionary ideas, big solutions that can meaningfully contribute both to making peoples life better into the next big revenue and earnings growth opportunity for Google.

And my take is that Larry gives the 70/20/10 as an instructive framework he is also noted how hard is it to reach that 10% on these big new revolutionary ideas, because it's tough to get people to tackle big difficult new problems and start pursuing incremental change. So human nature sort of provides a limit on how big that final bucket would be the new opportunities and I think the other point to consider is the Google's core business continues to deliver strong growth. So to achieve 10% in the big new areas means continually trying to reach 10% of an even larger number.

And the framework keeps us focused on big ambitions across the company but given the success of the core business I think its fair to say the 10% is a stretch goal for now and it's a way to think about resources which hopefully helps you fill in a bit there. And then the second part of your question if you could repeat that.

Brian Nowak

Yes. We just going back to the accelerating overall U.S. revenue. Just curious about a little more color on the drivers there were, its sounds like both YouTube and mobile search are doing pretty well. Is it safe to say that U.S. search and YouTube are both accelerating or you seeing YouTube driver is proportionate how should we think about the drivers of the U.S. revenue acceleration?

Ruth Porat

Well, you've covered a lot of it, the U.S. growth really reflects the fact we have diverse set of products that are doing well, we had strengthen core search particularly mobile, we had strengthen YouTube and programatic as Omid talked about. So it's really the breadth across a number of different products that deliver the results that you are talking about, that we are talking about here today.

Brian Nowak

Thanks.

Ruth Porat

Thank you.

Ellen West

Operator, we'll take our next question please.

Operator

Our next question comes from Heather Bellini from Goldman Sachs. Your line is now open. Please go ahead.

Heather Bellini

Great. Thank you so much. I just had two quick questions. I was just wondering you talked a lot about desktop and mobile CPCs. I was wondering if you could share with us if the narrowing of the gap between the two was actually starting to accelerate. And then the other thing I wanted to ask is just thinking about the CapEx spending made that companies go through and clearly Google been on one on an accelerated spending way for the last few years, should we then suggest – get from your comments are you were in a digestion period that the digestion period could also be a multi-year trend as well, if there is any thoughts you could share there. Thank you.

Ruth Porat

You know I think with respect to the first part of your question, we thought it was important to be clear that this gap is narrowing and to give you a sense of some of the mix issues within CPCs. So mobile, CPCs strengthening desktop not declining, YouTube remains lower, but we're seeing real strong growth in TrueView. And so it's just really to try in dimension that if you think about what's going on with the mix change.

And then as it relates to expenses, what I was trying to convey there is that we – in the second quarter had a bit of a digestion period here on the back of the substantial investment spend that we've had and I would say in terms of – if you kind of think about the second quarter in that context, there can be some variability in the cadences spend.

And so a part of it as we're talking about the CapEx here is how spend has phased during the year, I wouldn't suggest that we're talking about – as the way you frame the question, this multi-period given the sheer scope of opportunities that we have. So as I said again with the front-ends with respect to both CapEx and OpEx, we're just beginning the 2016 budgeting process. We're very focused on prioritization, but I was trying to give you some context for what was going on in the second quarter.

And then as it relates to OpEx in terms of the back half of the year, there are seasonal fluctuations that do typically impact operating expense as well. For example, headcount usually picks up in the third quarter with new grad hire starting and our marketing expense also tends to be weighted towards the second half of the year. So again I was trying to give you a sense of what's the cadence as you're thinking about the year.

Heather Bellini

Great, thank you.

Ruth Porat

Thank you. We'll take our next question please, operator.

Operator

Our next question comes from Robert Peck from Suntrust. Your line is now open. Please go ahead.

Robert Peck

I had two questions if you don't mind. The first is around possibility of working more directly with Yahoo on search and search results. Could you tell us about any progress there, work you've done there? And then number two, Ruth, could you talk about the future possibly breaking out more information around your businesses to a point where maybe we'd breakout YouTube or DoubleClick or some of these other businesses that could give investors a little more clarity on the size and growth of them? Thank you.

Omid Kordestani

I'll take the first part. So Yahoo is currently testing search results and adds some number of partners including Google as one of their options. And they have options to use search services and search ads across your properties and you may see our ads. And so it's a standard agreement and many other publishers use our Web search and AdSense for search. We look forward to working with them and hopefully having a good performance for them.

Ruth Porat

And then in terms of the second part of your question, I think, it's important to help our stakeholders understand how we think about key drivers of the business and how we manage the business, providing what I call a framework for understanding the momentum in the business, our investment choices, our capital allocation decision making. I'm committed to being direct with you. I won't give you competitively sensitive information, but my goal is to help you understand the business as well as possible.

And in my view it's our obligation to pursue activities that maximize value over the long-term and doing it in a disciplined fashion. And the point I'm really trying to drive here is I aim to create a framework that helps you understand where we're going. So you're asking what we think about breaking out any particular business, I'm trying to understand how best to provide more insight into the drivers of the business and beyond what is currently provided and it's really too early to be more specific than that.

Robert Peck

Thank you.

Ruth Porat

Operator, we'll take our last question please.

Operator

And our last question comes from Paul Vogel from Barclays. Your line is now open. Please go ahead.

Paul Vogel

Great, thank you. Two questions on YouTube. One, there's been a lot of speculation in the past about the profitability of YouTube. So I'm just sort of curious how you think about the revenue growth versus kind of the forward spend on forward demand and if YouTube in a position where it's starting to see leverage on the upside with the strong revenue growth. And then on the revenue side, in particular where you talk about how YouTube has been sort of – it's one of the things that's drag the optics of CPC down. When mobile was doing that I think the company believe that over time mobile would be additive and we're starting to see, but it took some time. How do you think about YouTube in the context of is there a point in time you think YouTube will actually be additive to sort of the optics of CPC versus where it is right now? Thank you.

Ruth Porat

So I think there was three parts to that question. In terms of the revenue growth in YouTube, Omid hit a number of them, but we continue to have strong growth there and it really does reflect as he said the sheer volume of users we have over a billion users. And those users are spending more time watching and watch time growth continues to accelerate now up over 60% year-over-year, the fastest rate we've seen in two years and we do view watch time as most valuable measure of engagement. And it does reflect the ongoing improvement in ads quality with more users also choosing to watch more TrueView ads not only do we have a huge user base that's highly engaged, but data points like the fact there are more 18 to 49 year olds on mobile YouTubes and watching cable TV today really underscores the opportunity here. And our focus is the opportunity to get larger budgets, move to YouTube.

And then in terms of the profitability question, as you know we don't breakout profit by product and we view our technical infrastructure as a core strategic asset that supports products across the company, I have already said that on this call that is an important point. It is fair to say that much of the network expenses that supporting YouTube, it's a large user of capacity and our ability to serve high quality HD video on demand around the world is unparalleled. From the users' perspective, YouTube is a great example of a multi-device platform with high usage on both desktop and mobile. We have one ad team that works across our various products and when we work with the largest ad partners globally, we're selling a total package.

Omid's comment on some of that, not surprisingly if you take our top advertisers, they all advertise across all our products, not necessarily the same rate, but we have a single team working with them to close the differential. We do view that as a great opportunity. And the goal, to give just a bit more color on how some of our assets and technical infrastructure and ad sales team benefit a number of our different products across the company. And then I think you slipped a third part in there on the status of – that kind of the CPC trends and YouTube TrueView pricing, so I will disclose out on that.

CPC pricing on YouTube for TrueView ads, ads that users choose not to skip is lower than on CPC pricing on desktop and mobile, but YouTube TrueView ads represented a larger percentage of our overall clicks, so had a greater impact on CPCs. And this is really about the tremendous growth in YouTube views. And not – you know again, when we see the real uptake here and the extent to which users are choosing to watch more ads given our effort around ad relevance and quality, advertisers want to reach these audiences. And our focus is on the opportunity to get larger budgets move to YouTube.

Paul Vogel

Okay, thank you.

Ruth Porat

Thank you. Okay, and with that, I want to thank everyone for joining us today. We look forward to speaking with you again next quarter.