The Performance Advertising Imperative

Performance advertising is the fastest growing online advertising model. Yet many media companies outsource performance advertising to a third party, losing revenue, control, and independence in the process. There is a new alternative: sell your own performance advertising and control your online revenue.

A FAST white paper

Introduction

In an era when traditional advertising revenues are flat or declining, media companies are adapting their business models to capitalize on the double-digit growth of online advertising. All media companies – newspapers, magazines, broadcasters, service providers, yellow pages, and pure-plays that operate exclusively online – are looking to monetize their digital information with both display advertising and performance advertising. Yet the manner in which media companies make money from these two online advertising models is quite different.

> Forward-thinking online publishers are taking action by implementing their own branded performance advertising portals that allow them to sell and display their own keyword ads. As a result, they have the independence to keep 100% of their performance advertising revenue, the control to improve ad performance and better satisfy their advertisers, and the flexibility to syndicate and expand to other channels.

While media companies typically sell their own display advertising to maximize revenue from the large advertisers seeking to reach their valuable audiences, they often outsource performance-based advertising -- both search and contextual ads -- to a third-party ad network. Outsourcing has become so widespread that nearly all online publishers and content aggregators list sponsored ads from Google, Yahoo or other third party networks whenever a visitor conducts a search or clicks on a relevant page. Yet for every click on a sponsored link, the media company receives only a share of the revenue – often less than half – even though it created or aggregated the content and attracted the audience.

Outsourcing may appear to be the right decision for some media companies. To sell performance ads in-house, a media company needs a large base of advertisers willing to purchase keyword ads, a sufficient amount of search traffic and page views to match to the ads, and the investment capital and search expertise to implement an in-house solution. Until recently, only the major search engines met these requirements, which is why they have come to dominate performance advertising.

Today, however, the landscape has changed. As Google further extends its footprint into traditional media territory (news, classifieds, and online video), and as performance advertising lengthens its lead as the dominant form of online advertising, media companies have the competitive and strategic motivation to take control over both display AND performance advertising.

Forward-thinking online publishers are taking action by implementing their own branded performance advertising solutions that allow them to sell and display their own keyword ads. As a result, they have the independence to keep 100% of their performance advertising revenue, the control to improve ad performance and better satisfy their advertisers, and the flexibility to syndicate and expand to other channels.

This paper examines the strategic, lucrative opportunity media companies have to decouple themselves from third-party performance ad networks and sell their own performance advertising. First, we will define performance advertising and explore why it has become the dominant form of online advertising. Next we will examine the risks of outsourcing performance advertising and qualify the benefits of selling performance advertising in house. Finally, we will identify the types of media companies that have the resources to profit immediately by selling their own performance advertising.

A New Model: Pay for Performance

For the first few years of the Internet, online advertising was synonymous with display advertising. Born as basic banner ads and growing into new rich media formats, display ads represent the traditional “cost per impression” advertising model shifted online.

Performance advertising – developed by a small company called GoTo.com in 1998 and refined by Overture, Google, and others – is based on a fundamentally different model than display advertising. Instead of purchasing ad impressions up front, advertisers pay only when an ad generates some action by a user, typically a click.

To increase the likelihood of a click, performance ads are displayed only when they match some user action or intent, either a search related to the ad (known as paid search advertising) or a click on a Web page with related content or concepts (known as contextual advertising). Complex algorithms determine which ads are displayed and rank them based on the price paid, average click through rates, and other factors.

Performance ads are also purchased under a different model than display ads. As opposed to the typical fixed price of display ads, performance advertising prices are determined in an online auction where advertisers bid against one another for keywords relevant to their businesses. Keyword prices are determined dynamically based on the number of advertisers bidding for the keyword at any given time. Prices are fluid, changing every second based on the demand for the keyword.

What is Performance Advertising?

Many Names: Paid search and contextual advertising, keyword advertising, pay-per-click (PPC), “Sponsored Listings”

Format: Text and hypertext; emerging text and multi-media formats

Business Model: Cost-per-click (CPC); cost-per-action (CPA); paid-inclusion; hybrid models

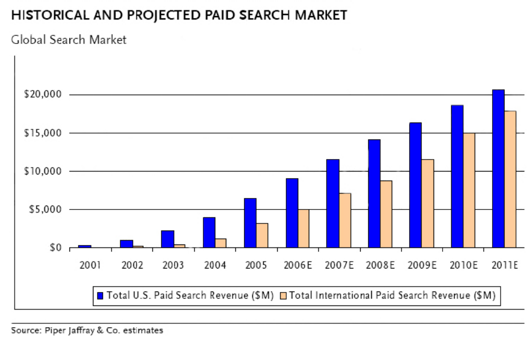
Price Set By: Typically auction-based model, dynamic pricing

Typical Advertiser: E-commerce and other Web-sites, large and small (long tail)

How Delivered: Atop or alongside search engine results pages (paid search advertising) or alongside any Web page with text that matches the keyword (contextual advertising)

Measured By: Number of clicks or number of actions

Targeting: Determined by the content of the user’s query or the page they are viewing



Historical and Projected Paid Search Market (source: Piper Jaffray & Co.)

Finally, the format of performance ads is very different than display ads. Unlike flashy, graphically-rich display ads which are placed prominently on the page, often interrupting the visitor’s viewing experience, performance ads are small text descriptions with hyperlinks that are placed along the top, side or bottom of search results or page content. This simple, consistent format gives equal weight to all advertisers for a certain keyword, and is less disruptive to a visitor’s search or content viewing experience.

The Benefits: Cost, Targeting, Performance & ROI

While display advertising remains the tool of choice for brand advertisers, performance advertising offers several major improvements for advertisers looking for direct responses – or actions – from their ads:

- **More Affordable**: Performance advertisers only pay when users click on their ads, allowing even the smallest company to run a pay-per-click campaign. While some keyword prices are very high, most average less than a dollar per click.
- **More Targeted:** Search-driven ads – the main type of performance advertising – are inherently more targeted than most forms of display advertising because they are presented to users during the act of searching for information related to the ad. Contextual ads, while not as highly targeted as search ads, generally are more targeted than display ads.
- **Higher Performing**: Because search and contextual ads are highly targeted to the advertiser's audience, click through rates are typically much higher than display ads.
- **True ROI**: Because advertisers only pay per click, they can effectively measure and manage their ad campaigns and calculate a true return on investment.

Thanks to its improved targeting, performance, and measurement, as well as its accessibility to the "long tail" of advertisers, performance advertising has grown to become the dominant form of online advertising. Today, the combination of paid search and contextual advertising represents 40% of all online advertising according to a recent report from the Interactive Advertising Bureau and PricewaterhouseCoopers. Data from many analysts shows that large and small marketers are continuing to shift a majority of their online budget to performance-based models, which explains why display advertising has lost share each year since 2001.

Why Search Dominates

There are two types of performance advertising inventory:

1) **Search Engine Results Pages (SERPS)** -- dynamic pages created based on users' keyword searches.

2) **Contextual Pages** -- any Web page with contextually-relevant content.

While contextual ad inventory is divided up among hundreds of thousands of online content sites, the majority of search inventory is owned by one company: Google.

Search: The Most Commonly Used Application Online

- Internet users conduct nearly 600 million searches daily.
- 45% of all searches are directly or indirectly related to commercial goods and services.
- Local search was ranked the second most used online service.

Source: Piper Jaffray & Co.

While Google did not invent performance advertising, it refined the PPC business model and generated the search traffic required to attract an enormous base of large and small advertisers. With the traffic and the advertisers in place, Google built an efficient ad network that enables marketers of all sizes to generate direct sales leads through paid search advertising. Today, Google owns more than 50% of all web searches and 75% of all paid search revenue worldwide according to Piper Jaffray's analysis.

The Outsourcing Dilemma

In today's highly fragmented media landscape, traditional and new media companies are looking to tap the explosive growth of performance advertising, both paid search and contextual advertising. As publishers increase traffic to their sites and build inventory, they stand to generate significant revenue from performance advertising. But, to date, nearly all sites have adopted the same strategy: outsource performance advertising to a third party network.

Google's AdSense is the largest performance-based ad network for online publishers. Each publisher who joins AdSense agrees to list relevant ads from Google's inventory in exchange for a share of the revenue generated by users who click on the ads. Publishers typically list ads on their content pages, their search engine results pages, or both. AdSense has been a boon for Google, contributing 1.35 billion or 37% of its total revenue in the first quarter of 2007. It has also been a cost-free, top-line revenue driver for publishers who have joined the program.

But is outsourcing the right decision? Are media companies leaving money on the table by splitting revenue with Google or another third party? Is it possible to drive more revenue by selling performance advertising in-house? Are publishers strengthening Google's grip on advertising by feeding the "new media" giant more traffic, searches and page views? Is cost-free revenue worth the trade-off of losing direct relationships with advertisers and control over an increasingly critical monetization model? These are all relevant questions to media companies who must transform their business models and maximize the online opportunity.

The Five Risks of Outsourcing Performance Advertising

The tantalizing top-line revenue potential of joining a program like AdSense often blinds media companies to the consequences of losing control and independence. While Google, Yahoo and other smaller performance ad networks tout the profitable returns they provide for their content partners, media companies must carefully weigh the inherent risks of putting a third party's hands on such a strategic revenue driver. Let's examine the five major risks of outsourcing performance advertising.

Loss of Revenue

Regardless of the ad network, outsourcing performance advertising always involves a revenue split between network and the online publisher. The split depends on the value of the publisher to the network, which is often determined by the publisher's traffic and average click through rate. In most cases the search engine takes the larger share despite the fact that the media company attracted the users and generated the clicks. As ad networks sign up more and more publishers, they become less dependent on any one site and gain even more leverage in negotiating revenue splits.

> **The Five Risks of Outsourcing Performance Advertising:**
>
> - Loss of Revenue
> - Loss of Advertiser Relationships
> - Loss of Audience Data
> - Poor Ad Performance
> - Eroding Audience Satisfaction

Loss of Advertiser Relationships

In nearly every form of advertising, media companies – particularly established outlets – use a direct sales force to sell and place ads. Even in the online world, most highly trafficked sites sell their own display ads. Yet, when an online publisher chooses to outsource performance advertising, it loses a key opportunity to attract new advertisers and strengthen relationships with existing advertisers by offering them a new performance-based advertising vehicle. Advertisers are instead forced to go to a third-party performance network or directly to a competitor who offers a performance product.

> Media companies could be in a situation where they lack relationships with the majority of advertisers that seek to reach their audiences.

Remember that performance advertising makes up more than 50% of all online advertising. Also consider that marketers are beginning to use performance advertising for purposes other than just customer acquisition, such as brand awareness. Analysts believe that branding will be one of the biggest growth drivers for performance advertising over the next few years. Media companies could be in a situation where they lack relationships with the majority of advertisers that seek to reach their audiences.

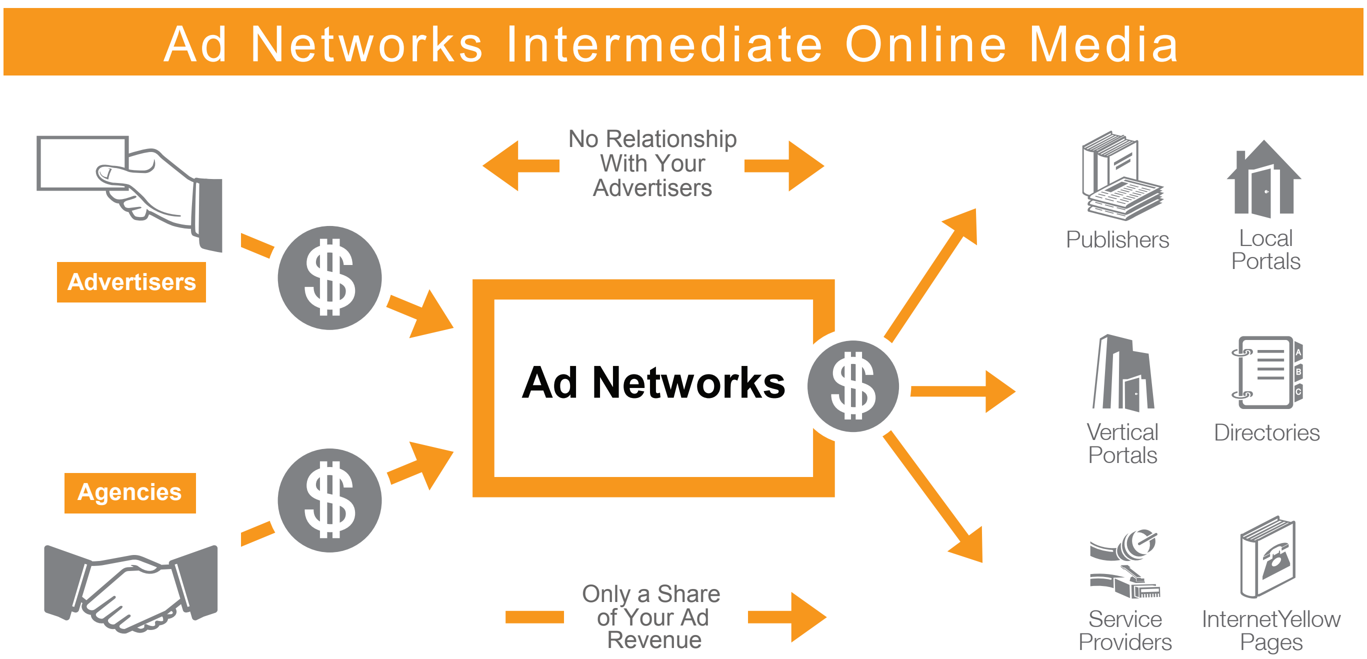
Loss of Audience Data

It is well known that consumers are increasingly turning to the Web as their primary media consumption channel. Every search and page view from a consumer is valuable data that, when viewed and analyzed in aggregate, helps media companies improve their sites and attract advertisers seeking to reach their online audiences.

When a publisher chooses to outsource performance advertising, it directly or indirectly releases key audience data including what content and advertising is most attractive and profitable and what users are searching for on any given day. Can media companies afford to be so transparent with their critical online audience data?

Poor Ad Performance

Performance ads are highly targeted because they match the content of users' search queries or the Web pages they are viewing. The problem with third-party networks, however, is that they use a "one-size-fits-all" ad relevancy model when matching ads to search queries or Web pages. As



Ad Networks Intermediate Media from Advertisers Online a result, they cannot possibly provide an ideal match in every case because the relevancy is not tuned to each media property's content.

Let's take a common example. If a visitor enters a search on a financial news site for "bond," the third-party ad network will deliver ads that match the keyword alongside the search results. If an ad for the new James Bond DVD is delivered – a clear mismatch – one can assume that the ad network's relevancy model was to blame because it was not tuned for financial news content. Publishers who rely on the rigid ad relevancy models of third party networks will suffer from mismatched ads, poor performance, wasted inventory, and lost revenue because they have no ability to tune the relevancy for their own properties.

The Untapped Search Opportunity

"More than 70% of search queries do not originate on search engines. Instead, people are choosing to bypass search engines and are going directly to their preferred information sources, retailers, and other websites and searching there."

-Sue Feldman, IDC

Eroding Audience Satisfaction

Many Internet users do not know or care about the difference between natural and paid search results. They simply want to find what they are looking for, whether the answer comes in the search results or from an advertiser. Publishers who rely on a third party to deliver ads in the search results on their sites may suffer from declining audience satisfaction if mismatched ads are continually showing up on the site. Visitors may jump to competitor's site where they can get more accurate results.

Another issue that negatively affects audience satisfaction can be characterized as the "Google Glaze." Due to the uniform, static manner in which Google's "sponsored listings" are displayed on publishers' sites, readers may ignore them. Because of the restrictive display policies enforced by third party networks like AdSense, media companies have little room to customize the display of ads to improve performance and satisfaction for audiences and advertisers.

The Time is Right to Bring Performance Advertising In-House

A recent independent study by IDC about search on the Internet unearthed a telling statistic: "…More than 70% of search queries do not originate on search engines. Instead, people are choosing to bypass search engines and are going directly to their preferred information sources, retailers, and other websites and searching there."

This finding reveals the profound and largely untapped monetization opportunity that keyword-driven, performance-based advertising presents for media companies. While the major search engines grabbed an early lead in performance advertising, media companies today have the search traffic and the page views to begin to sell their own paid search and contextual advertising.

White-labeled performance advertising software is now available to online publishers, enabling them to quickly implement their own branded advertising portals. By doing so, they can regain the control and independence necessary to compete and survive in today's hyper-competitive world of online advertising. IDC's Sue Feldman summarizes the opportunity: "Monetizing...search traffic requires sophisticated ad matching platforms that can analyze user behavior, match queries to ads, handle ad auctions, and track advertising transactions. Media companies that want to take back their leaking ad revenue have a unique opportunity to do so by implementing what we call a 'digital marketplace in a box'."

In the final section of the paper, we explore the major benefits to selling performance advertising in-house, and identify the types of media companies that have the resources and the motivation to seize this opportunity today.

Grow Revenue

Following industry best practices, media companies can easily understand the operating procedures and investments required to implement an in-house performance advertising solution. Once the solution is in place, the publisher can reduce or eliminate its reliance on a third-party network and its revenue sharing model, leading to direct revenue gains.

FAST AdMomentum™

FAST AdMomentum is a performance advertising and search monetization application that helps media companies protect and extend their search and contextual advertising revenue.

As a white-labeled application installed behind the firewall, FAST AdMomentum can be customized and branded by the online publisher and integrated with its existing systems and processes.

FAST AdMomentum includes the following core capabilities:

- **Paid Search & Contextual Ads**
  Support for both query-based ('structure or unstructured search') and contextual ('content-based') advertisements
- **Fully Configurable Ad Ranking**
  Support for multiple bid models (Auction, CPC, CPM, fixed price, paid inclusion)
- **Flexible Ad Targeting**
  Keywords, geo location, profiling triggers, sites and scheduling, content
- **Advertiser Control**
  Self-service ad center for small advertisers, account managed for larger advertisers, agency and starter packs
- **Multi-format and Multi-Channel Support**
  Ad delivery in multiple channels (e.g. web, mobile) and formats (e.g. text, banner, video)

Once they get their feet on the ground, media companies can customize the system to increase performance (and revenue) by adjusting ad models, improving targeting methods, tuning relevancy models and optimizing ad display. Sites with major affiliate or partner networks can grow revenue even further by syndicating their ad feeds. A local paper, for instance, can syndicate its sponsored links to affiliate sites such as local radio stations or smaller papers, aggregating traffic and advertisers to deliver the most compelling local search marketplace. And Media companies need no longer think of the Web as the end game. As mobile advertising becomes the "third screen," media companies with their own performance advertising portals can offer marketers a one-stop-shop for a true multi-channel search and contextual advertising campaign.

Gain Control & Flexibility

By outsourcing performance advertising, media companies lose control over critical assets including audience data and advertiser relationships. A branded performance advertising solution allows media companies to take back control of these assets.

Publishers that sell their own performance ads can keep all data behind their own firewall and use it to improve ad performance to gain competitive advantage in their markets. In addition, by bringing performance advertising in-house, media companies can eliminate the middle man and gain control over their relationships with advertisers seeking to reach their audiences.

An in-house solution also allows media companies to give more control to advertisers. Self-service ad portals present a low-cost way for media companies to attract even the smallest marketers, who can bid for, purchase and place their own ads without any support. For larger marketers, a publisher can employ a dedicated sales force to provide premium service. And for large advertising agencies, media companies can provide open APIs that allow agencies to integrate their ad buying software to streamline purchasing and reporting.

Media companies need not turn off the third-party faucet entirely, however. In-house solutions provide the flexibility to sell performance ads on the highest value inventory, while using a third-party network to back-fill lower value inventory. When a publisher has built up a large advertiser base, it can eliminate the third-party network completely.

Grow Advertiser Base

Because performance advertising allows lower-priced entry points, it enables a publisher to target a much wider range of advertisers. By selling their own performance ads, media companies can form relationships with a large number of new advertisers to help solidify future business models.

Exploit Your Content

Third-party performance ad networks are inherently limited by the fact that they must deliver ads to a wide-range of media sites, each with their own unique content. With their own branded performance advertising solutions, media companies can tune the ad relevancy based on a true understanding of their content. As a result, ad performance will improve, increasing advertiser satisfaction and revenue for the media company.

Mini case study

Major Portal Bests Google In Local Market With Branded Performance Ad Center

A major portal was facing a significant threat from Google. It needed to quickly migrate online its offline yellow pages business model and supplement paid-inclusion listings with performance advertisements.

Instead of partnering with a third party, this portal created its own branded paid search network using FAST AdMomentum. With the control and flexibility of a white-labeled solution, the company was able to:

- Generate a 7X increase in advertising revenue with no increase in traffic
- Blend national and local auction models
- Meet the needs of small local and large national advertisers

Am I Right for This Opportunity

Selling performance advertising may not be the right decision for every media company. But for online publishers that have an established advertiser base, a large amount of traffic, and the competitive and strategic motivation, a branded performance advertising solution can provide top-line and bottom-line benefits and help strengthen future online business models. Let's examine some of the best candidates that meet these requirements.

Yellow Pages, Local Search & Classifieds

Analysts predict that up to 70% of the traditional local advertising market will move online over the next 5-10 years. According to the Kelsey Group's Global Directories Forecast 2007, global ad revenues from Internet Yellow Pages and local search advertising is expected to grow from $4.1B in 2006 to $11.1B in 2011. Many innovative yellow pages companies have established online businesses to capitalize on this shift, while a new crop of successful local portals, local search and classified sites have shown that consumers are hungry for relevant local and vertical directory listings.

The key challenge for online yellow pages, local search, and online directories, however, is the intense competition coming from the major search engines and free sites such as Craig's List. By implementing an in-house performance ad network, these directory-oriented businesses can compete with the search giants by providing superior, targeted advertising opportunities for local and category-specific marketers. Because these sites often derive 100% of their revenue from advertising, they can leverage their deep advertiser bases and ad sales forces to ramp up quickly and see near immediate returns.

Newspapers & Magazines

Print publishers have been hit the hardest by the fragmentation of media, stung by shrinking circulations and newsstand revenue as readers move much of their print media consumption online. According to data from IDC, newspaper advertising market share will decline from 17.8% in 2006 to 16.9% in 2011, while consumer magazines will see their share shrink from 4.4% in 2006 to 4.2% in 2011.

Newspapers are ideal candidates for in-house performance advertising. They often have a large base of classified advertisers, many of whom are moving their print budgets online where they can achieve greater ROI. Newspapers can supplement their online paid-inclusion classified listings with high-performing sponsored listings that provide classified advertisers another way to target local readers online. Secondly, many newspapers have turned their online sites into local portals, adding rich, local search capabilities to attract traffic. With an in-house performance ad solution, a newspaper can reach out to the thousands of local businesses in its area and sign them up as performance advertisers.

Magazines also have a great opportunity to sell performance advertising because their online sites typically attract a highly targeted audience. A golf magazine, for example, mainly attracts golf enthusiasts. A performance advertising solution allows a golf magazine to target the major golf retailers and the thousands of "long tail" retailers that are looking to tap its qualified audience. Furthermore, many magazines are adding new community, social networking and user-generated content features to their websites to create stickiness and build loyalty. These features significantly increase inventory, a key requirement for performance advertising to be successful.

Vertical Search & Portals

Vertical search engines and portals can greatly benefit from in-house performance advertising because they attract a highly targeted audience. According to research from the Kelsey Group, over the last year, small and medium-sized advertisers doubled their spending on vertical or specialized sites and publications to reach more targeted audiences.

As an example, a health information portal with millions of health-conscious visitors each month presents an ideal ad buy for the thousands of small businesses that sell health-related products and services. If the health portal can provide greater ad performance at lower prices than the broad-based search engines, these marketers will be more likely to sign on directly with the portal to purchase keyword ads.

Mini case study

Vertical Search Engine Supplements Paid-Inclusion With New Performance Ad Portal

A U.S. $200M vertical search engine was looking to supplement its paid-inclusion ad revenue. Although it was generating some performance-based revenue via a third-party network, click-through rates were lower than average, ad response time was slow and ad relevancy was inconsistent. The site also had no ability to create custom rankings and custom ad-packages for its advertisers to boost revenue.

After evaluating several other ASP-based performance advertising options, this vertical search engine decided to deploy its own branded performance advertising portal using FAST AdMomentum. By integrating its new performance-based solution with its existing advertiser portal, the site can:

- Offer advertisers a single log-in for purchasing both paid inclusion and keyword advertising on its site
- Automatically place ads on several of its owned sites
- Integrate its CRM and ad sales tools to optimize workflow

With a customized ad ranking algorithm tuned precisely for its vertical content, this vertical search engine is confident that more relevant ads will lead to greater performance, satisfied advertisers and increased revenue.

Vertical portals are also under attack from the major search engines. There is a short time window for vertical search engines and portals to build the traffic and the advertiser bases to gain an early performance advertising lead in their respective markets.

Service Providers

As traditional subscription models come under pressure from new competitors in the broadband, mobile and fixed-line businesses, service providers must embrace advertising as the primary driver of new revenue. While cable operators are investing millions in their broadband portals to drive traffic, increase inventory, and enable advertising growth beyond their existing levels, traditional fixed-line and mobile operators are looking to advertising as a new revenue category. The emerging IPTV platform will also provide everyone in the content delivery market with a new targeted, interactive medium that is ideal for performance-based advertising models.

To maximize advertising profitability, service providers must consider the requirements of not only the major media planners and buyers but also the smaller, local advertising markets that will represent billions of dollars in future ad buys. It is simply sound strategy for service providers to create their own performance advertising marketplaces so they can stay independent from branded, third-party search engines and create customized solutions that highlight their unique advantages to advertisers. Advertisers will benefit from a premium alternative for running ads across providers' platforms, while providers will retain a greater portion of performance-driven ad revenue and increase negotiating strength against third-party search engines.

Conclusion

In the world of online media – on the Web and increasingly on the mobile phone – search has become the way consumers "turn the page" and "change the channel." The broad-based Web search engines were the first to capitalize on this phenomenon, building billion-dollar performance advertising machines by matching the presumed intent of users' searches with relevant advertisements. Programs like Google AdSense have provided media companies some top-line revenue from performance advertising. But as search engines steadily intrude upon media's turf, are these revenue handouts simply fool's gold?

Today, media companies have all the requirements to return to their roots and control all of their online advertising revenue, both display and performance-based. They have the advertisers at the head and at the long tail as marketers shift an increasing percentage of ad dollars online. They have the search traffic and the page views as their sites have grown from digitized versions of offline media to rich destinations for content, contribution, conversation, and community. And now they have the search-driven, performance advertising software that levels the playing field so they can fight back and reclaim control and independence.

About FAST

FAST is the leading developer of enterprise search technologies and solutions that are behind the scenes at the world's best known companies with the most demanding search problems. FAST's solutions are installed in more than 3500 locations.

FAST is headquartered in Oslo, Norway and Needham, Massachusetts and is publicly traded under the ticker symbol 'FAST' on the Oslo Stock Exchange. The FAST Group operates globally with presence in Europe, North America, the Asia/Pacific region, South America, the Middle East and Africa. For further information about FAST, please visit www.fastsearch.com.

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