

efficient frontier

US SEARCH ENGINE PERFORMANCE REPORT

Q2
2010

An Efficient Frontier Research Paper

July 2010

Contents

Q2 2010 Executive Summary	1
Spend Growth Accelerates, Exceeding Expectations	1
Retail Sector Leads the Recovery	1
Seasonal Strength Bolsters Travel. Auto Improves While Finance Continues to Lag	1
Bing Continues to Gain Market Share	1
Outlook for 3Q10	2
After a Strong First Half, Q3 is a Critical Quarter	2
Microhoo! Expectations	2
Retail to Continue its Growth	2
Spend and ROI Trends	3
Search Engine Landscape	3
Metrics	4
Impressions	4
Clicks	5
Cost Per Clicks (CPC)	5
Click Through Rate (CTR)	6
Return on Investment (ROI)	6
Google Content	7
Sector Data	7
Sectorwise	8
Auto	8
Retail	9
Travel	10
Finance	10
Definitions	11
Methodology	11
About Efficient Frontier	11

Q2 2010 Executive Summary

Spend Growth Accelerates, Exceeding Expectations

In Q2 2010, the search marketing sector continued to bounce back, shrugging off a still uncertain economic environment. Year on Year (YoY) spend was up 24%, with a 9.7% increase in spend Quarter on Quarter (QoQ), partly due to a recovery in Cost Per Click (CPC) prices which rose across all of the major search engines. Overall, return on investment (ROI) in search was up 4% YoY and 10.6% higher than last quarter (Q1 2010). Search marketing growth continues to exceed the 2010 outlook of 10-15% due to increased consumer demand, which results in higher pricing as indicated by higher CPCs.

Retail Sector Leads the Recovery

In the first half of 2009, search felt the adverse affects of a sputtering global economy. In sharp contrast to a year ago, search marketing in Q2 2010 is showing a strong recovery. Marketers shook off the continued economic uncertainty and capitalized on improving return on investment from search advertising to grow sales volume.

The retail sector leads the recovery with 38% growth in spend YoY and 16% growth QoQ, a pace that far exceeds the typical modest quarterly rise in Q2. Building on the momentum of Q1's strong growth, retail CPCs continue to grow at 18% YoY and 17% QoQ, indicating a growing aggressiveness on the part of advertisers in this sector. Consumers are also playing their part in driving the recovery. Impression volume in the retail sector was up 65% YoY, signaling continued consumer interest in online shopping.

Seasonal Strength Bolsters Travel. Auto Improves While Finance Continues to Lag

The travel sector also enjoyed a recovery in this seasonally strong quarter with a 10% YoY increase in spend due to a 13% YoY increase in CPCs. The auto sector continued its growth with a 6% YoY increase in spend. The Finance sector only took a 2% dip in growth despite a 22% YoY decrease in CPCs. This is because click volume grew 24% YoY and offset almost all of the losses from the drop in CPCs. Although advertisers were not able to monetize leads as well, interest remains high for financial products.

- **Retail:** Spend was up 38% YoY due on strong consumer and advertiser demand
- **Travel:** Spend was up 10% YoY on CPC gains
- **Finance:** Spend was down 2% YoY due to a decrease in CPCs that was largely offset by volume growth
- **Auto:** Spend was up 6% YoY on CTR and CPC gains

Bing Continues to Gain Market Share

Bing continues to grow its market share at Yahoo!'s expense. Taking quarterly fluctuations into account, Bing's spend share has grown from 6.1% in Q1 to 6.4% in Q2 2010. Bing click share has remained stable QoQ. The YoY gain for Bing is 56% in spend share and YoY gain in click share is 36%. Capitalizing on last quarter's growth in the Travel Sector, Bing continues to show strength in travel as it has more than doubled its market share YoY.

Meanwhile, Yahoo! continues to lose market share as spend fell to 18% from 18.7% in Q1 2010 and click share fell to 19.4% from 20.1% in Q1 2010. Yahoo!'s Q2 2010 numbers represent a 12% YoY spend share loss and a 9% YoY click share loss.

Google's market share has grown slightly in Q2, with both spend share and click share up to 75.6%. Despite a 13% YoY increase in Google CPCs, ROI is up 8% YoY, indicating much improved conversion rates. When baselining ROI performance against Google, however, Bing still shows a stronger return, resulting in 21% higher ROI than Google, while Yahoo returns 25% less than Google.

Outlook for 3Q10

After a Strong First Half, Q3 is a Critical Quarter

The last two quarters have shown strong growth in terms of SEM spend (20% YoY in Q1 and 24% YoY in Q2) and we expect the positive trends to continue for the second half of the year. CPCs continue to make a strong recovery, indicating growing demand and larger advertising budgets which should continue to contribute to the expected growth in the coming quarters. However, weakness in the European economy might negatively affect Q3, so we remain cautious as we keep our SEM growth expectations in the 15-20% range. Should we continue to see strength in Q3, and taking into account typical strength in Q4, the year could surpass our already upwardly revised expectations.

Microhoo! Expectations

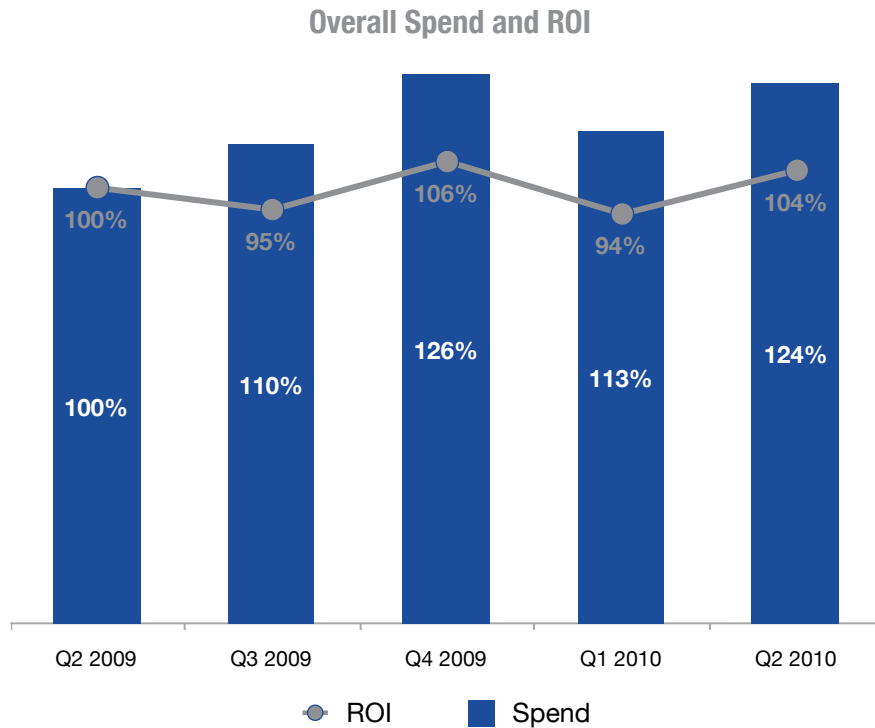
Given the diverse performances of Bing and Yahoo!, we remain cautiously optimistic about the Yahoo!/Microsoft partnership. In the long run, we believe that the integration will bring small advertisers on board the unified platform increasing marketplace demand and lift CPCs. Yet we are uncertain of the short term effects. Currently, the unified Microsoft and Yahoo! stance is that advertisers will only be allowed to place the same bids across both search engines. However, due to the very different ROIs across Yahoo! and Bing, we feel that this will be detrimental to advertisers because it will mean that the high ROI on Bing would subsidize the lower ROI on Yahoo!. The net effect could be suppressed CPCs, dampening the impact of greater demand.

Retail to Continue its Growth

Out of the four sectors, we expect retail to continue showing strong growth in search engine spend in the range of 30+%. We have found retailers increasingly willing to experiment and explore new ways of online marketing, using all available channels such as search and display, and using cross channel marketing to help them attribute offline revenues to online efforts. In addition, retailers are capitalizing on opportunities to dynamically leverage their complete product catalog and promotions calendar, thus increasing campaign coverage, CTRs, return on investment, and spend. After a long period of depressed search metrics, travel has started to make a recovery. It is still too early to tell if the strength in travel will continue but current signs are very positive. Finance remains the weakest of the sectors we cover, and we are uncertain about its recovery given the poor economic conditions in Europe.

Spend and ROI Trends

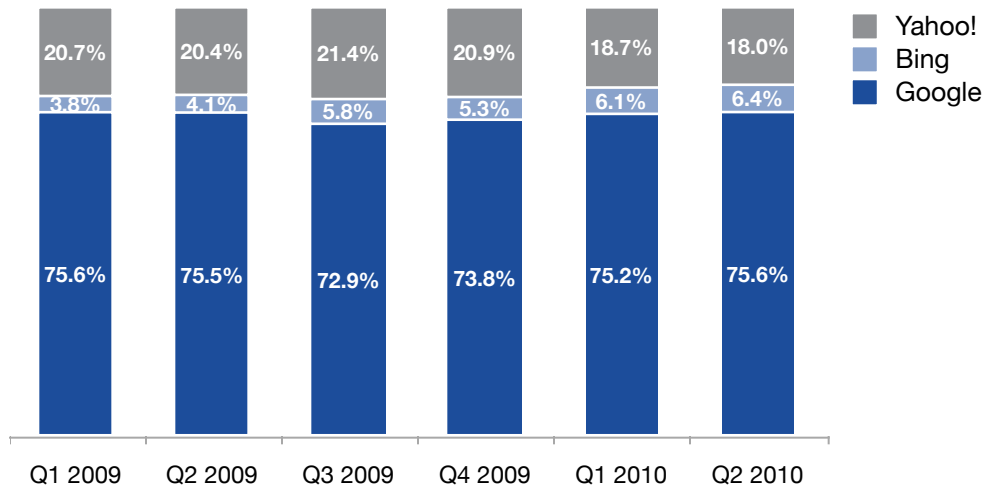
YoY spend has grown 24% while ROI has increased 4%. This is a very positive sign continuing from last quarter where we reported similar numbers. Positive ROI indicates there is still room for higher spend. The increase in spend is due to increase in pricing as clicks have dropped YoY for Google and Yahoo! (excluding Bing) while CPCs have increased on all the major search engines.



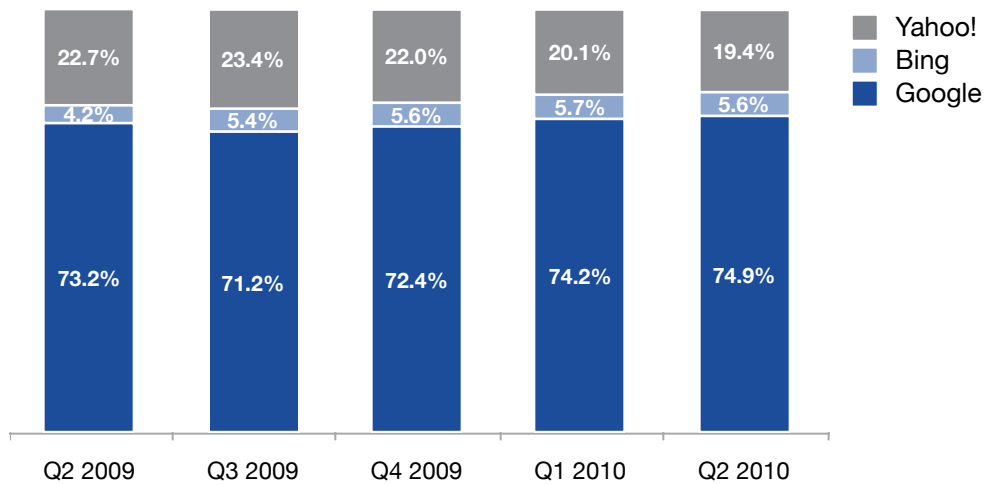
Search Engine Landscape

Google maintains its market share while Bing has inched up its share at the expense of Yahoo!. YoY Bing's market share has grown from 4.1% to 6.4%, a 54% increase.

Spend Share



Click Share by SE

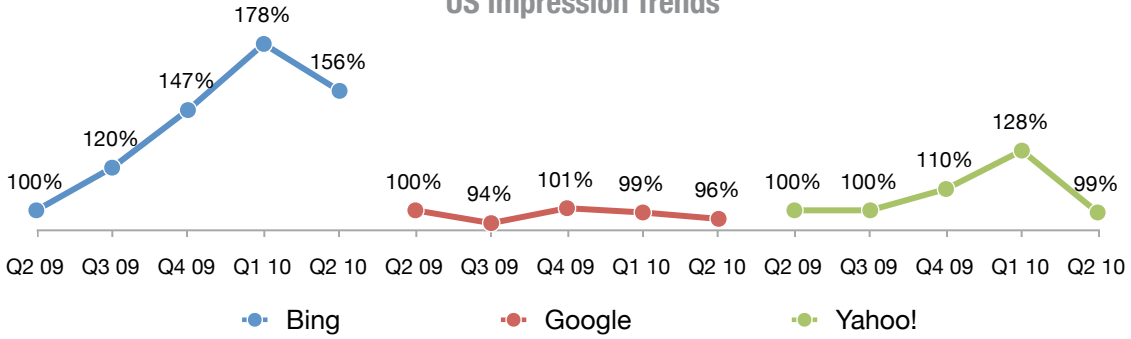


Metrics

Impressions

Impressions on Bing have grown substantially year over year increasing by 56%, indicating greater consumer interest in Bing. The increase is in line with Bing's increase in click share. Impressions on Yahoo! and Google have remained flat.

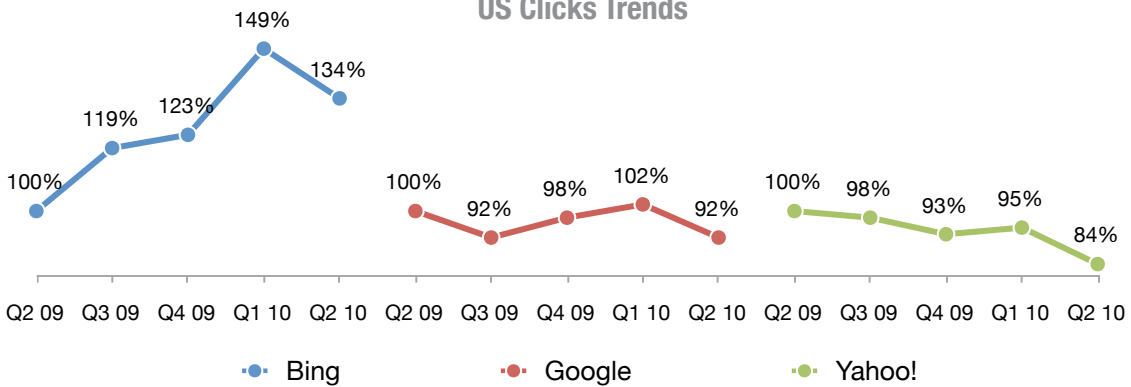
US Impression Trends



Clicks

Clicks on Bing have increased YoY by 34%, while clicks on Google and Yahoo! have declined.

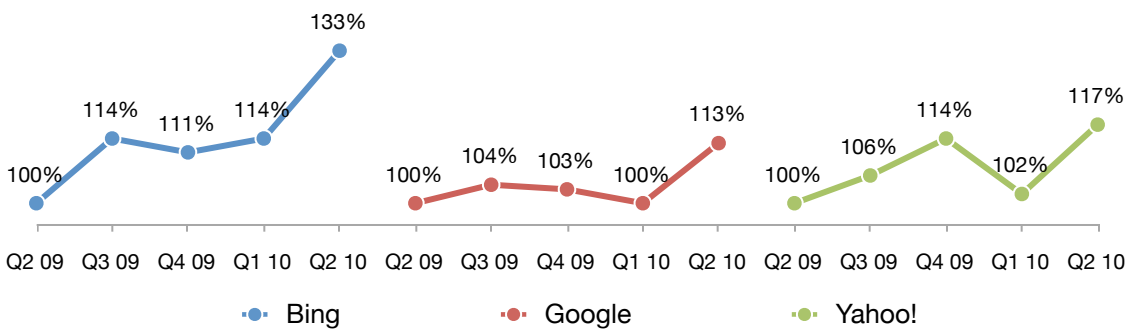
US Clicks Trends



Cost Per Clicks (CPC)

CPCs indicate the state of the market. Increased CPCs indicate a stronger market as advertisers are willing to pay more for a consumer click. Results of Q2 show that CPCs on all engines are up YoY with Bing leading the charge at 33% YoY increase in CPC.

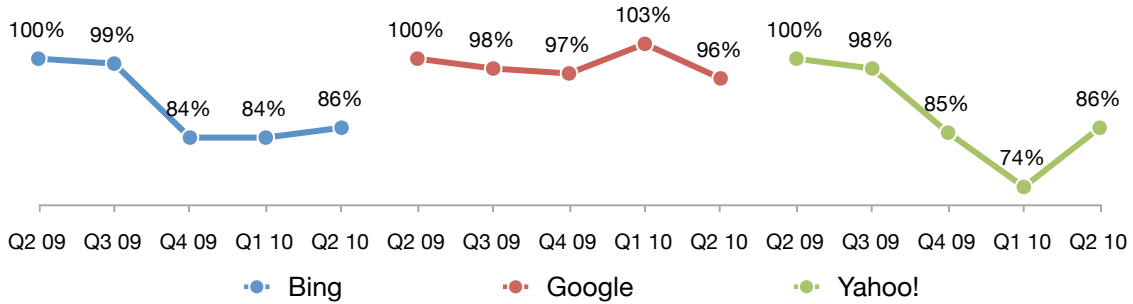
US CPC Trends



Click Through Rate (CTR)

CTRs have declined on all search engines. This is fairly typical as CTRs usually decrease when more users search online causing the percentage of qualified traffic to decrease naturally

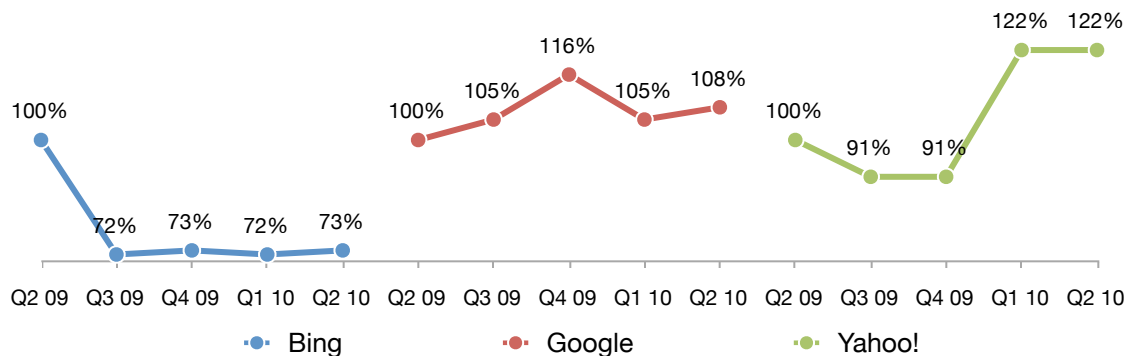
US CTR Trends



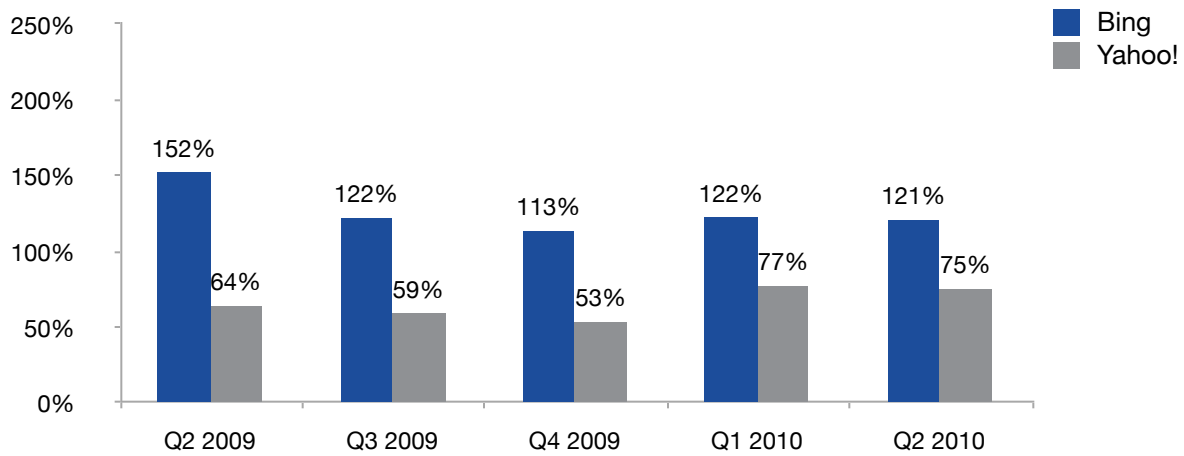
Return on Investment (ROI)

ROI on all SEs remained stable QoQ. However YoY, Yahoo!'s ROI improved 22%, Google's ROI improved 8% and Bing's fell 27%. Despite the fall in Bing's ROI, it still has a 21% better ROI than Google. In contrast, Yahoo!'s ROI is 25% worse than Google.

US ROI Trends



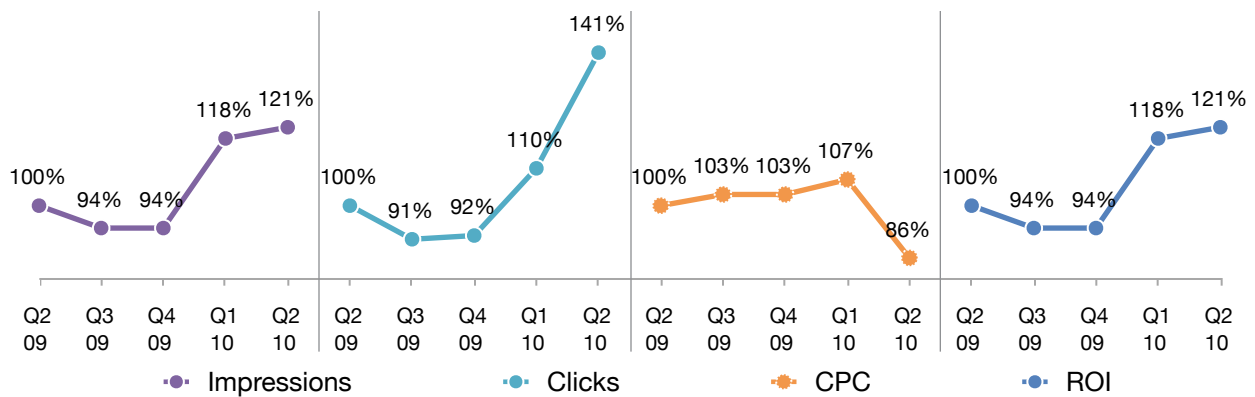
ROI vs Google



Google Content

We saw a sharp increase in clicks in the Google content network despite a flat impression change. This indicates that the content network has much higher CTRs than a year ago. Google's effort in refining the content network by showing more relevant ads appears to be paying off as advertisers are seeing a higher ROI.

Google Content Trends



Sector Data

Google continues to dominate retail and will be the biggest beneficiary of the growth in the retail sector. Bing has made big advances in the travel sector and we expect to see market share gains for Bing in Q3

if current travel trends continue. Out of the four sectors, Yahoo! is strongest in finance but unfortunately, finance has made the weakest recovery this year.

Sector Trends

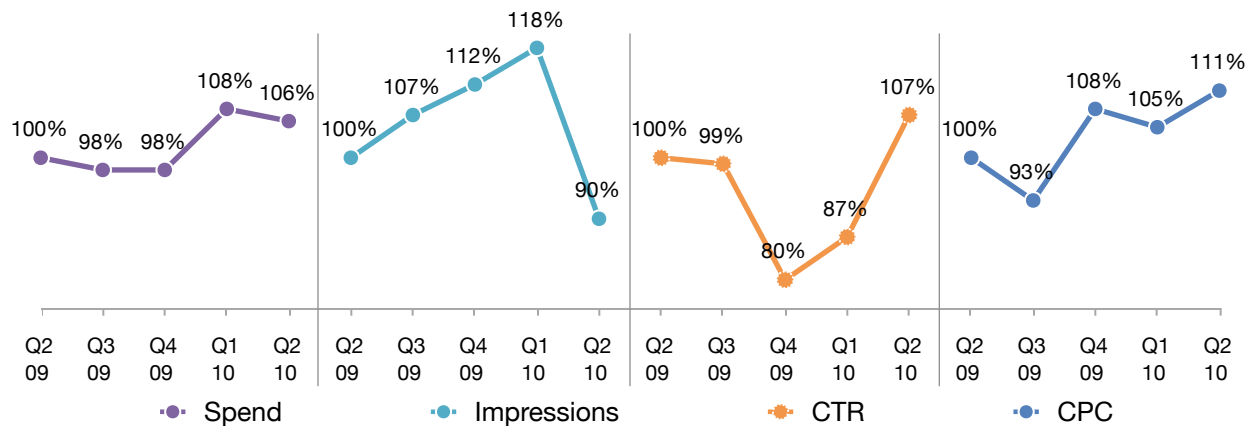
Auto	Q2 2009	Q3 2009	Q4 2009	Q1 2010	Q2 2010
Google	77.3%	77.3%	77.4%	77.4%	76.7%
Bing	4.9%	5.3%	5.6%	5.7%	6.6%
Yahoo!	17.8%	17.4%	17.0%	16.9%	16.7%
Finance	Q2 2009	Q3 2009	Q4 2009	Q1 2010	Q2 2010
Google	70.1%	66.2%	64.4%	71.6%	72.2%
Bing	4.8%	6.2%	4.8%	5.5%	6.5%
Yahoo!	25.1%	27.7%	30.8%	22.9%	21.3%
Retail	Q2 2009	Q3 2009	Q4 2009	Q1 2010	Q2 2010
Google	85.9%	84.7%	84.1%	82.4%	83.2%
Bing	3.0%	3.8%	4.2%	5.5%	5.3%
Yahoo!	11.2%	11.6%	11.7%	12.2%	11.6%
Travel	Q2 2009	Q3 2009	Q4 2009	Q1 2010	Q2 2010
Google	79.8%	76.5%	76.6%	74.9%	72.7%
Bing	4.4%	6.3%	6.8%	8.8%	9.0%
Yahoo!	15.8%	17.3%	16.7%	16.3%	18.3%

Sectorwise

Auto

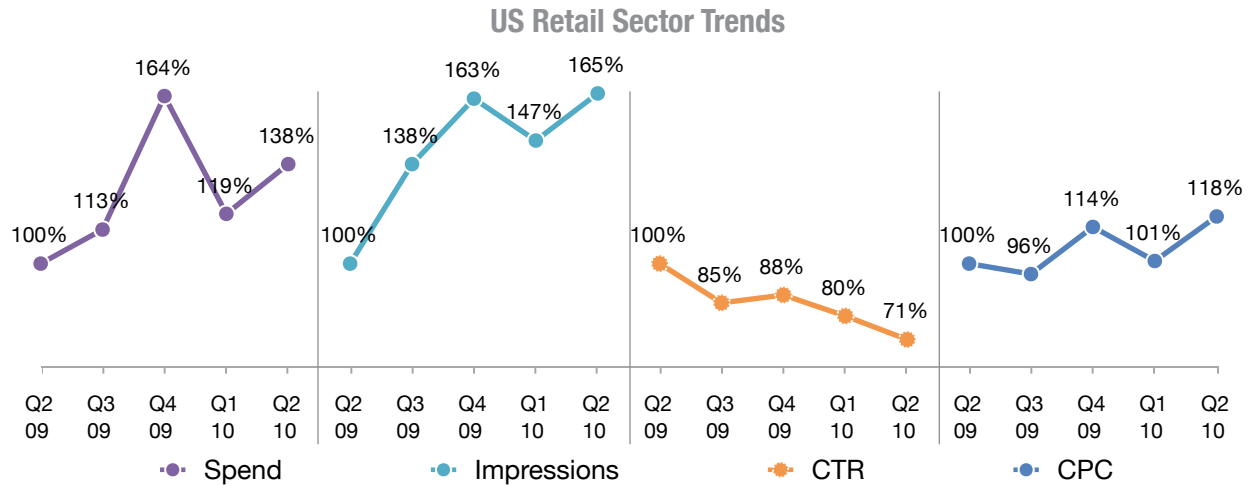
Spend has gone up 6% YoY while CPCs have gone up 11%. While these numbers look modest, they must be considered in light of the Cash for Clunkers program that started in 2009. We had reported a concern that the Cash for Clunkers program would deplete 2010 inventory. However, based on the numbers so far, we are not seeing that this has happened.

US Automobile Sector Trends

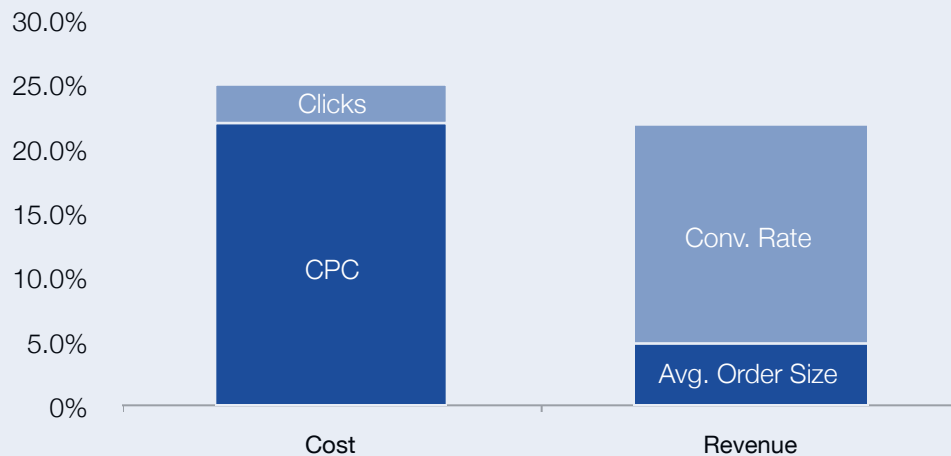


Retail

Retail continues to be the sector with the strongest growth, driven by strong consumer interest as seen from the 65% YoY increase in impression volume. Spend went up 38% YoY and CPCs went up 18% YoY. This bodes well for Google which is over indexed in retail.



Retail Study: YoY Comparison of Key Metrics



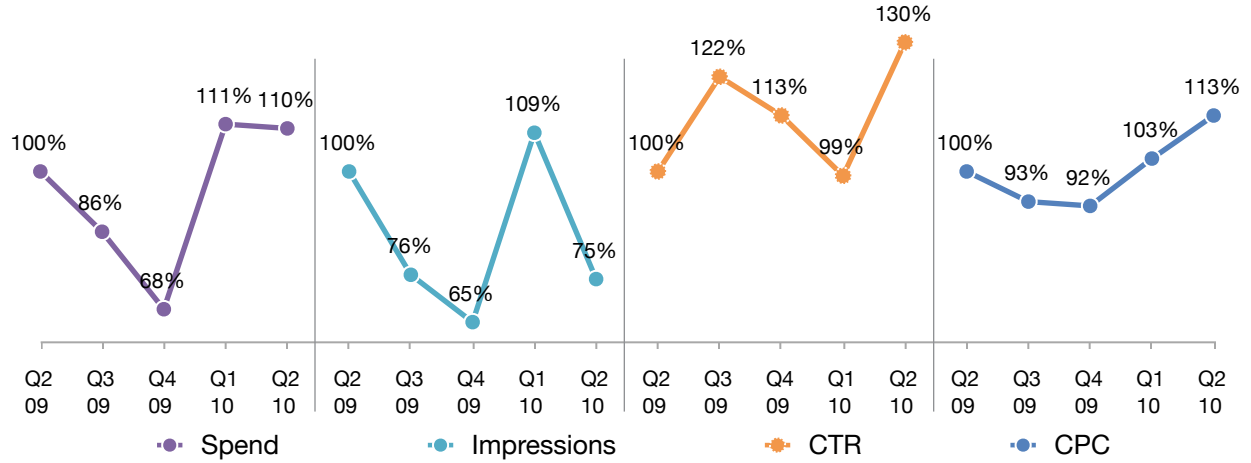
To understand the key drivers behind retail growth, we analyzed a sample of our retail clients who tracked revenue and order volume. In this sample, the average increase in spend was 25% YoY, and the average increase in revenue was 22% YoY. Interestingly, while the average order size had only increased 4% YoY, the conversion rates increased by 18% YoY.

The data shows that YoY, the increase in spend has been primarily driven by an increase in CPC and not by an increase in consumer click volume. Despite seeing relatively flat click increases and flat order size increases, advertisers were able to generate more revenue by increasing conversion rates. The increase in revenues in turn enabled them to spend more on SEM.

Travel

Travel is showing signs of recovery as spend is up 10% YoY while CPCs are up 13% YoY.

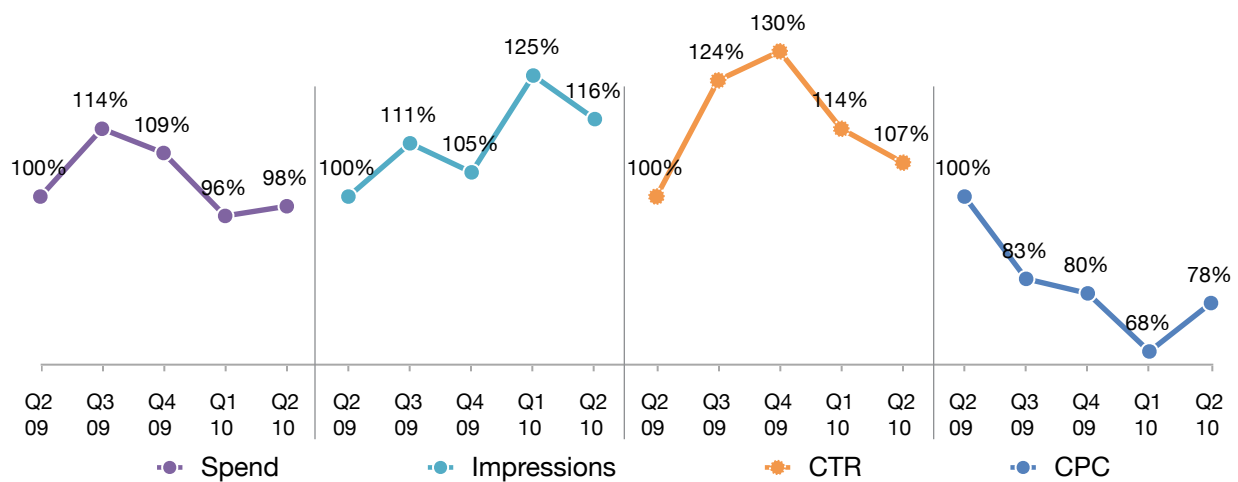
US Travel Sector Trends



Finance

Finance has seen the weakest numbers so far. While YoY spend is flat, CPCs are still down 22% YoY.

US Finance Sector Trends



Definitions

Click Share – Amount of share received by a particular engine of all paid clicks as calculated by the formula: paid clicks on a particular search engine/total paid clicks across all engines.

Cost Per Click (CPC) – Amount paid by a marketer per user click on a paid search ad(s). CPCs are determined by an auctioning process and are a good indicator of market conditions. Increases in CPCs indicate advertisers are willing to spend more on advertising and a decrease in CPCs indicate that advertisers are willing to spend less.

Impressions – Number of views of an ad by a consumer on a particular search engine. Impressions indicate consumer interest in a product. The more consumers search the higher the impression volume, the less consumers search the lower the impression volume.

Return on Investment (ROI) – A measure of profitability based on how much a marketer received in terms of results compared to how much was invested. Also known as a measure of efficiency.

Spend Share – Amount of share that marketers spend buying paid search on a particular search engine as calculated by the formula: particular search engine spend/total search engine marketing spend.

Methodology

This analysis was completed based on data from Efficient Frontier search engine marketing customers and the resulting Efficient Frontier's Customer Index. The Efficient Frontier Customer Index represents a subset of Efficient Frontier clients who have spend data for six consecutive quarters or more whose resulting SEM metrics are then normalized to average industry category contributions established by multiple third party data providers. The Efficient Frontier Customer Index consists of a fixed sample of large scale U.S. search engine advertisers across multiple sectors, including finance, travel, retail and automotive. The Efficient Frontier Customer Index sheds light on trends in search engine spending and performance on a year-over-year (YoY) and quarter-over-quarter (QoQ) basis.

About Efficient Frontier

Efficient Frontier is a leading digital performance marketing company managing search and display optimization for large-scale marketers around the globe. Founded in 2002, Efficient Frontier pioneered the application of modern portfolio theory to Search Engine Marketing and today combines its core predictive modeling algorithms and bidding technology with comprehensive value-added services to manage more than \$900 million in annual digital spend globally. The largest and most sophisticated advertisers and agencies partner with Efficient Frontier to achieve and sustain optimal campaign performance and growth in highly complex and competitive marketplaces. The company is headquartered in Sunnyvale, California, with offices in New York, the United Kingdom, France, Germany, and India, and technology licensing partnerships in Japan and Australia. Efficient Frontier is a privately held company with funding from Redpoint Ventures and Cambrian Ventures. For more information, please visit www.efrontier.com and subscribe to the Efficient Frontier blog at blog.efrontier.com. You can also follow us on twitter.com/efrontier and facebook.com/efrontier.