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Disintermediation of Online Display Advertising

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Moving away from a digital media landscape dominated by companies who can deliver billions of impressions to companies who can deliver precise audiences based on specific data.

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Note: I originally wrote this document in late 2008 and it was entitled, "Future Failure of Ad Networks." I do not feel that the old title would be fair, as many ad networks will still exist in tomorrow's marketplace but in new capacities. Without further ado…

In the early to mid 1990's, the way we advertised online was by contacting sites directly and having them put our banners and buttons (and sometimes a text link) on their site in a fixed placement. Sites like HotWired, Multex, Pets.com, and others were very active in having advertising on their sites and were seeing the early fruits to generating revenue by accepting online advertising.

One of the inefficiencies in the early days of online advertising was the lack of a system in which served advertisements. Hard-coded placements were OK in the beginning (really only due to lack of other options) but as more and more advertisers were shifting some ad budget to the web, the volume of banners and buttons increased. Web publishers had to manually put up, take down, and measure for each advertising campaign and this became extremely burdensome.

A few smart people recognized this issue and created a solution that is what we know today as the ad-serving system. Web publishers inputted a bit of code on their websites where they wanted to accept advertisements and from there, a serving system would dynamically place any number of predetermined advertisements into these placements on specific pages of websites. The immediate benefit was creating efficiencies in trafficking the advertisements but another benefit arose…. Measurement.

Historically, media measurement was either via a direct response method of a unique phone number on DRTV spots, or research studies of how campaigns were doing in-market via a qualitative (and sometimes quantitative) study that utilized a panel of respondents that would be statistically valid to make an assumption for the mass. These ad-serving systems, though new at the time, knew how many times an ad was served and delivered (impression) as well, as, a few other metrics. Marketers were now able to purchase advertisements in a package of every thousand impressions (CPM) and the entire online marketing industry started to scale.

Measurement evolved and instead of brand managers and media professionals just looking at how many advertisements served for a client, they wanted to gauge some form of "response," so the *click* was observed. When an ad impression was live on a page, how many people actually clicked the advertisement and were taken to the destination URL of that particular ad-unit. This was a way that media professionals and brand managers could start to justify how much value online advertising afforded… you can measure in near real-time how many people you've persuaded to leave the content they were consuming and view your particular message and promotion. You didn't have to wait for call-centers to report their DRTV numbers nor an in-market study to come

back months later, the reporting happened in either daily or weekly formats. To this day, we consider this disruptive to the measurement of the advertising world.
So now that we have *clicks* established as a metric, we needed to establish a performance indicator as to how many clicks were considered a successful campaign. In the late 90s, we established the CTR, or click-thru-rate, that allowed us to quickly see how many people were clicking on specific creative messaging online in a percentage form such as 1.27%. Initially, click-thru-rates were extremely high as online advertising was new and novel, but over time, these click thru rates have come down significantly.

Today, we actually tend to use the CTR as a piece of campaign measurement, but not the main portion of it. The reason for this is that CTR is only one indicator of how a campaign is doing as people consume much media online and sometimes, don't want to click a particular ad-unit, but still register and recall an advertisement. Google, Microsoft, Yahoo!, and many other companies are establishing something called engagement mapping & conversion attribution which helps spread the attribution of a click over multiple ad impressions as in our current advertising model, the last-ad viewed and subsequently clicked gets 100% of the attribution. This is a flaw in the current system but much money and brainpower is in market and testing new methodologies.

Now that we've established a base of where online marketing has come from, lets look at the sell side of the business. Every day, there are thousands of websites created, though only a small percentage of websites (<20%) get the majority of the web traffic. This is a commonly known theme known as the Long Tail. Marketers have a vast landscape of advertising choices when looking in the digital world with hundreds of millions of websites to place media on and an increasingly growing digital world filled with opportunities in mobile, games, digital TV, and so on. One of the things that keep media folks up at night are the myriad of choices to place their media dollars.

Companies have emerged that quantify website traffic and validate it, to make a media planner's life much more manageable since there are so many opportunities. ComScore, @plan, Quantcast, Compete, Lookery, Google Ad Planner, TrafficIQ, and many others have come up with nifty tools that are we can use to find out the composition of an audience of a particular site, find estimated (or validated) traffic levels, time spent, and so on. Since the majority of media folks are extremely busy, the top 10 sites in each category in these tools generally get most of the advertising budgets because it's a lot easier and sometimes safer to purchase media from the largest sites (and for many other reasons). Note the long tail effect referenced here.

If an ad agency has a client who wants to advertise online, there may be well over a dozen properties on a particular media plan. Trafficking creative to all of these properties, signing all of the insertion orders and logistical paperwork, and coordinating this effort is a comprehensive task. In the late 90s and early 2000s, Advertising Networks emerged that promised (and delivered) two things: making a media planner's life easier by only dealing with one property but getting reach into many and aggregating eyeballs to deliver an “uber” media buy that could potentially be bigger than buying the in a particular category. Advertising historically was a reach & frequency game, so having as much reach as possible was a sexy proposition that ad networks could provide, which afforded them much early success.

The business of advertising networks is fairly simple and straightforward but making a network happen is not an easy task. There are generally three sides to a network business: the sell, buy, and technology sides. The sell side is where ad networks work with ad agencies and marketers directly to get advertising dollars that fund the buy and technology sides. The buy side is where ad networks go out to publishers (commonly known as business development in digital media) and try to represent their inventory, either exclusively or non-exclusively. The promise of a network to many sites is that since they may not be large enough to appear on a media plan as a stand-alone entity, if they were rolled into a “network” or “mutual fund” if you will, they will be a part of the buy and will see revenue that they would not have normally recognized. The technology side of the business handled all of the trafficking and in the 2000s, developed ways to contextually, behaviorally, and socially target users.

The buy side of the network is where we’re going to spend some time analyzing. Generally, business development folks are tasked with going out to solidify as many agreements as possible as to lock-up the potential market to dissuade competitors from entering. It’s similar to street wars. Business development agreements for networks either are “free” to the publisher, meaning, that a publisher who doesn’t have a lot of clout could make available a certain amount of inventory on their site and if a network could fill it, they would do so. If not, the publisher would not see any monies from the network. If a network had a bit more clout in the industry, a business development team would guarantee that particular publisher a set amount of money and in some cases, the money was advanced to the publisher, much like a record deal is struck in the music industry.

Publishers measure the effectiveness of networks based on the eCPM, or the effective CPM (our yield for simplicity sake) that a network generates for them. If a network can deliver an eCPM of $4.95 and the site directly could only generate an eCPM of $3.50, then the network is positive for the publisher. The higher the eCPM is for a particular publisher, the better a publisher views a network. With competing networks, this is a very important metric to look at, especially as a publisher can work with many networks at any given time. Note the “e” in the CPM (“effective CPM”).

Networks have non-liable inventory (non-exclusive, free) and liable inventory (guarantees, sometimes exclusive, advances) and now have to optimize the type of inventory they are serving in a particular campaign for a brand. This is known as yield management. So, when an agency calls up a network to do business, the network is essentially giving the agency a *bag of trail mix*. What is trail mix you might ask? Trail mix is multiple items that someone once found in their kitchen and put them together right before they went hiking to provide energy throughout the period of exercise. One may favor the almonds in trail mix over the raisins, or the M&Ms over the peanuts, but the inventory of the trail mix is what is most important.

A network has a fiduciary responsibility to return dollars for their publishers. The publishers who have been given guarantees and advances generally sit on the top of the pyramid and because we live in a mostly for-profit world, networks need to return their dollars ahead of the rest. Because the more "expensive" publishers generally perform better (why else would you give them an advance or guarantee?), all of their inventory needs to be optimally spread out across many campaigns to effectively bring up their performance. Because a marketer's campaign is going to have many impressions, think of it as trail mix – there are going to be some good, bad, and ugly impressions as part of the mix, but there should be *just enough* good impressions that yield a positive campaign result.

The art and science of an ad network is really in the yield management, similar to a mutual fund, where you have many positions and you are optimizing which to use at what time, to return the most value back to both the network and the advertiser (shareholders if you will). It's extremely tricky and usually done by some very smart people and algorithms.

The initial ad networks were black boxes (non transparent); you didn't know where your advertising dollars were going to end up, other than say Advertising.com's network but at the end of the day, it usually worked out positive. Marketers used the metrics described in this document and networks were able to optimize their performance to hit prescribed goals. In the mid 2000s, marketers requested transparency within their media plans and networks have emerged (or opened up their kimono) that are fully transparent. This gives assurance to brands that they aren't appearing on a website that may be contextually irrelevant to a particular brand.

Networks have had a great ride so far, but are moving toward a big brick wall that could determine their fate rather sooner than later. This big brick wall is the promise of advertising exchanges, or platforms that allow any publisher, big or small, to allocate inventory to be bought, sold, or traded, at fair market price with the addition of usually free targeting and bring-your-own-data. Some of these exchanges are blind, some are listed by vertical, and others are transparent. Google, Microsoft, AOL, Fox, Yahoo!, and many others are moving into this space and the promise of not just online advertising being made available but all digital advertising is extremely interesting such as digital TV, radio, print, etc.

Why does this displace networks in the traditional sense? The targeting and aggregation of sites is now in the hands of media planners and brands directly. The value of networks has been marginalized dramatically in terms of delivering media impressions. In my opinion, the networks that will survive in the medium to long term will be those who flip their entire model of selling impressions to selling data. The data that networks have collected over the years is extremely valuable. Specific Media has been known to dominate the automotive segment because of their wealth of data.

Because of the rising data industry, we're seeing upstarts like BlueKai, Lookery, Datran, TargusInfo, Bizo, and Exelate (and others) emerge as essentially data exchange players. We're also seeing some of the current ad networks starting to create dashboards that give media and brand folks insight into specific audiences that are visiting a particular site.

We're also seeing full service shops like MDC Partner's Varick Media Management emerge that sit on top of multiple ad exchanges with powerful yield management systems hooked into multiple data sources that are giving agencies and marketers excellent service and returns (performance) in this brand new world of ad exchanges. Additionally, VMM has found a way to unbundle the impression – making a media buy *an audience buy*. After all, media does not buy products, audiences do.

Many of the major ad holding companies are moving into this space with their units Havas Digital, VivaKi, B3, Ecosystem, and others.

In a world where ad networks have to deliver a bag of trail mix to both net positive return for clients and themselves, ad exchanges net promise of only buying inventory that works positively for a particular client, and if for some reason there is inventory that is purchased that is negative, the ability to sell or trade it off is available.

Written by Darren Herman, President and founder of Varick Media Management.

Darren Herman *is a globally recognized digital media pioneer who is inspired by the white space that exists between advertising, media, and technology. Over the past 12 years, Herman has started five companies, sold two, and raised more than $40M in venture capital from top tier investors such as Intel Capital, NBC Universal and Morgenthaler. His companies achieved numerous awards Razorfish's critically acclaimed, "Breakout Company of the Year" and AlwaysOn's "Top 100 Private Company." He also personally won BusinessWeek's Top Entrepreneur award in 2006. He has been featured in an MTV documentary and is frequently quoted in global marketing, technology and financial periodicals.*

Over the past decade, Darren has stewarded clients such as Viacom, Panasonic, Sony Pictures, MTV, AT&T, eBay, Hewlett-Packard, Intel, American Eagle Outfitters, and Starz (amongst many others) into digital media campaigns utilizing search, rich media, traditional display, digital video, video games, mobile, and digital out-of-home.

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