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Presentation

OPERATOR: Good day, and welcome everyone to the Google Inc. conference call. Today's call is being recorded. At this time, I would like to turn the call over to Ms. Krista Bessinger, Director of Investor Relations. Please go ahead, ma'am.

KRISTA BESSINGER, DIRECTOR, IR, GOOGLE: Great. Thank you. Good afternoon, everyone, and welcome to Google's first quarter 2008 earnings follow-up conference call. With us are Patrick Pichette, Chief Financial Officer; and Jonathan Rosenberg, Senior Vice President of Product Management. I will quickly cover a few housekeeping items and then we'll open the call immediately to your questions. If you could, please limit yourself to one question and one follow-on.

Also please note that this call is being webcast from our Investor Relations website located at investor.Google.com. Please refer to our website for important information including our earnings press release and related slide deck and a replay of this call will be available on our website in a few hours. Please note that we routinely post important information on our Investor Relations website located at investor.Google.com. We encourage you to make use of that resource. So as a reminder, the purpose of this follow-up call is to give participants the opportunity to ask more detailed financial and product questions in an efficient and Reg FD compliant manner. Now I'll quickly cover the Safe Harbor statement.

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Some of the statements we make today may be considered forward-looking and these statements involve a number of risks and uncertainties that could cause actual results to differ materially. Please note that these forward-looking statements reflect our opinions only as of the date of this presentation and we undertake no obligation to revise or publicly release the results of any revision to these forward-looking statements in light of new information or future events. Please refer to our SEC filings including our annual report on Form 10-K for the year ended December 31, 2008, as well as our earnings press release for a more detailed description of the risk factors that may affect our results. Copies can be obtained from the SEC or by visiting the Investor Relations section of our website. Please note that certain financial measures we use on this call such as EPS, net income, operating margin, and operating income, are expressed on a non-GAAP basis and have been adjusted to exclude charges relating to stock based compensation. We've also adjusted our net cash provided by operating activities to remove capital expenditures which we refer to as free cash flow. Our GAAP results and GAAP to non-GAAP reconciliation can be found in our earnings press release. So with that, we're ready to take your questions. Operator.

Questions and Answers

OPERATOR: Thank you. (Operator Instructions) We'll pause for just a moment to assemble the roster. Our first question from Heath Terry from FBR.

HEATH TERRY, ANALYST, FBR: Great. Thank you. Just wondering, as we look at the operating expense lines, we obviously saw pretty big declines in R&D and sales and marketing and we know from the headcount number in those areas that there wasn't as much of a decline. Can you talk to us about how you're getting those kind of cost savings without using headcount as a reduction and then just from the increase that we saw in G&A, is there anything outside of the charges related to the change in stock-based compensation that's driving that up this quarter?

PATRICK PICHETTE, CFO, GOOGLE: So I'll answer that question. The overall, what you have seen, as we mentioned on the prior call that the biggest change from quarter-to-quarter, if you wish, and the trajectory of our costs, is, as we mentioned on the prior call, was this issue of the bonus accrual in Q4, which was kind of higher than we had originally planned because our results were better and now we're resetting the plan as what is a typical plan for the year so we're starting again fresh, and those bonus accruals which are tied to labor flow into different categories that do include R&D. It is -- it's also fair to say that across many of our categories of costs, we've continued to be quite diligent about our trajectories and you see them, that also is part of our results in a number of categories. So we continue to be prudent and that is essentially the biggest element that would have flowed through the Q4 to Q1 expenses.

HEATH TERRY: And so just for the follow-up side of that, is it fair to say that looking at that delta in the bonus accrual is a reasonable expectation of kind of what your plans are for the level business needs to be at for outperformance to happen, and us to see the same thing that we saw in the fourth quarter last year for the necessary bonus accrual catch-up?

PATRICK PICHETTE: I'm not sure I understand the question. If your question is will -- like we have now reset our plan at let's say that it's 100%, right, whatever 100% is.

HEATH TERRY: Yes.

PATRICK PICHETTE: So now we're running this year with the expectation of 100% and we hope to beat that in terms of -- because you always hope to beat your plan but that's what we're running with right now. If between now and the end of the year we see a big ramp-up in our performance, as we see that we will take appropriate accruals at that point.

HEATH TERRY: Great. That was my question.

PATRICK PICHETTE: Okay. Let's go to the next question.

OPERATOR: We'll take our next question from Jim Friedland from you Cowen and Company.

JIM FRIEDLAND, ANALYST, COWEN & COMPANY: Thanks. Wanted to ask a question on Google apps that was indicated early in the last call as a key area for investment. And at this point in the evolution, is the investment more on new features or are you starting to do more in terms of building up an enterprise sales force and are you seeing additional enterprise wins, especially in this environment on the cost savings and can you name any?

JONATHAN ROSENBERG, SVP, PRODUCT MANAGEMENT, GOOGLE: Sure. This is Jonathan. We had some pretty large deployments this quarter. Avago, which I think is the semiconductor division of HP deployed the app suite

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to several thousand, maybe 5,000 or 6,000 users. We had some progress in one of the big Mexican, states of Mexico too which we launched in early Q1. We also had quite a bit of progress on the EDU side with 60 colleges and universities that we signed deals with. Some of them I believe were Cornell and Georgetown. I know we signed other significant deals with T-Mobile, Fujisoft, Euro Master which I think is a subsidiary of Michelin. So I think there's significant progress there.

The kind of functionality that we're working on are some of the big -- some of the big holes that I think we still had in the suite, offline support was probably one of the more significant pieces, as was better synching with mobile devices. We're seeing pretty strong demand and traction in organizations in sort of the 3,000 to 15,000 size range. We're getting a lot of help with the reseller program that we launched and I think your observation about what is the state in a cost challenging environment, I think we are seeing that we've got a number of customers who are using the paid apps version. I think we're signing on more customers because of the cost savings relative to competitors. There's a big Forester study that showed that we're a fraction of the price of the competition even relative to their Cloud based offerings.

So I think we're doing pretty well. There's one category, manufacturing and spinoffs of large companies, seem to make a lot of sense, particularly when a company's building new infrastructure and we've got some examples. I think the Avago example is one of those and I know there are more.

JIM FRIEDLAND: Are there particular -- sorry, are there particular industries where apps are being sort of better adopted at this point versus others where maybe it's a little bit more complex and harder to get into?

JONATHAN ROSENBERG: I'm not sure I could establish any correlation in terms of the categories of industries, I think it's more a function of how the users and the IT departments are set up. Certainly, the educational institutions have made relatively quick and robust progress, as have companies that I mentioned that have sort of spun out and are out to start from scratch and build and don't have the legacy dynamics that established companies do. But I think that's really the only broad observation that I could make. It's more a function of the size of the Enterprise than it is the industry. So it's a few to several or 10,000 even 15,000.

KRISTA BESSINGER: I think we'll go to the next question, please.

JIM FRIEDLAND: Thanks.

OPERATOR: And we'll take our next question from Steve Weinstein from Pacific Crest.

STEVE WEINSTEIN, ANALYST, PACIFIC CREST: Great. Thank you very much. Just trying to understand, you had almost a full quarter still benefit from the DoubleClick acquisition and so when I look at your US business where you're reporting basically 3% growth, without DoubleClick, was the business in the US basically flat year-over-year?

PATRICK PICHETTE: I don't have those details. So I won't answer it. It is true that we have -- so if you think of the coming quarters, DoubleClick will be -- like we're finishing the first year of DoubleClick. What I can say which is a factual statement is we had in Q1, we're finishing the first full year of recognizing revenues for DoubleClick but now DoubleClick is integrated in all the display business so in Q2 you'll see the effect of that.

STEVE WEINSTEIN: Okay. As a follow-up, then, hopefully you can clarify one more thing on the G&A expenses. So if we back out basically the $46 million in expenses you kind of recognize as sort of one time, is that the fair run rate to work on right now? I guess I'm missing something about how the bonus accruals is going to change throughout the year.

PATRICK PICHETTE: No, what I've mentioned is that the bonus accrual that we took in Q4, that did not get moved into Q1 because we reset it much more than offset these additional expense pressures that we talked about.

STEVE WEINSTEIN: Much more. All right. Thanks.

KRISTA BESSINGER: Next question, please.

OPERATOR: And we'll take our next question from Richard Fetyko from Merriman and Company.

RICHARD FETYKO, ANALYST, MERRIMAN & COMPANY: If you were to compare the mobile and the display initiatives and if you include YouTube within the display, which one do you expect to be bigger opportunity the next two, three years? And then a follow-up up on that, could you elaborate more on the display ad strategy, you have

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the ad exchange, you have also the AdSense for display or for content that you're integrating display into. Just give us a little more color on what sort of strategy or products you're emphasizing within that display initiative.

PATRICK PICHETTE: I guess I'm not -- basically, I mean, broadly, the story and the strategy is to address the issues of and the challenges around the way display ads are bought and sold and we do fundamentally believe that those are going to change over the coming years and we're trying to bring much more measurability, the kind of efficiency that we had with Search advertising to display and make it much more efficient for both advertisers and publishers to offer better ads for users. So I mean, it's basically building the largest scale network that we can, that's going to give the best ROI to advertisers on the one side and the best yield to publishers on the other.

So if we get full integration of DoubleClick and Google products we're going to have the combination of this big leading platform for advertisers to create and manage the most effective campaign and publishers to, on the other side manage and monetize their inventories so I think it's the combination of being able to do both of those things, we expect will be very, very powerful. It's hard for me to handicap whether or not the scope of overall revenue on the display side or the mobile side will be bigger. We're obviously very, very excited about both and making strong progress in both.

RICHARD FETYKO: So I don't have a sense of what the size of those industries would look like in two or three years. All right. Thanks.

KRISTA BESSINGER: Next question, please.

OPERATOR: We'll take our next question from Doug Anmuth from Barclays Capital.

DOUG ANMUTH, ANALYST, BARCLAYS CAPITAL: Thanks for taking my question. Can you provide some color, Patrick, on the reasons for the sequential decline in other costs of revenues?

PATRICK PICHETTE: Hold on just for a second. I'll just take a look at my notes here. A gain in other cost of revenue, if I just go through my notes, they are still tied mostly to payroll issues, rather than equipment issues or machine utilization. And so that's basically it.

DOUG ANMUTH: So just to clarify, so you're saying more related to the bonus accrual than to--?

PATRICK PICHETTE: That's correct.

DOUG ANMUTH: Depreciation?

PATRICK PICHETTE: That's correct.

DOUG ANMUTH: Thank you.

KRISTA BESSINGER: Next question, please.

OPERATOR: And we'll go next to George Askew from Stifel Nicolaus.

GEORGE ASKEW, ANALYST, STIFEL NICOLAUS: Thank you. George Askew, at Stifel Nicolaus. I'm going to address this bonus issue one more time. I'm just trying to get a sense of the size of the bonus accrual in the first quarter. If you look at it as a percentage of sales, for example, in the first quarter '09 compared to the year-ago quarter, first quarter '08, was it materially different?

PATRICK PICHETTE: I don't have the answer to that question. But I think again, in general terms, if you think of your modeling, I think looking at run rates from a year ago or may be useful to get a sense of magnitude versus Q4 because Q4 as I said was sufficiently different and actually it does make a difference between Q4 and Q1.

GEORGE ASKEW: Okay. Okay. Fair enough. And then secondly, as a follow-up, there's media reports hinting this late this afternoon here that YouTube is partnering to stream full length movies, TV shows, et cetera, a redesign happening there. Is there -- what can you tell us about this kind of news on YouTube and the redesign that appears to be imminent?

JONATHAN ROSENBERG: This is Jonathan. Certainly, what we're hearing from both viewers and advertisers is that they want premium content and the premium viewing experience and we want YouTube to be as comprehensive as Search there and we want to attract as much professional quality content as we can and advertisers as we can of all sizes and types. I believe there's a conference or some additional details on the Sony issues coming out directly from the folks at YouTube. So you might want to take a look and watch for that. They should have all of the details about the Sony relationship and dynamics from Sam Bruno.

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GEORGE ASKEW: Got you. Okay. Fair enough. Thank you.

KRISTA BESSINGER: Next question.

OPERATOR: And we'll take our next question from Mark Mahaney from Citigroup.

MARK MAHANEY, ANALYST, CITIGROUP: Just one quick financial goals question. In past historic years I think there was a goal and I know it was stated at Investor Days in the past to simply expand pro forma operating income sequentially as long as possible. Is that still a goal within the Company, that happened this quarter but is the way as you think about the financial goals, is just to expand that sequentially going forward, that non-GAAP operating income?

PATRICK PICHETTE: So two points. I wasn't there in the old days when whoever who have said what. But certainly under my rule, we don't give any guidance going forward on any of these dimensions. All I think it's important that people understand is we are -- we're demonstrating responsible management over our resources. You should consider as you think of your modeling, you know, the fact that we talked at length on the previous call that our revenues are seasonal and you just got to think of our expenses as much more of a kind of fixed cost. They're not seasonal in a way. So our labor is not seasonal and our expenses are not. Because we're still growing. So that's the mindset that you should apply to your modeling.

MARK MAHANEY: Thank you.

KRISTA BESSINGER: Next question, please.

OPERATOR: We'll go next to [Sumit Suna] rom JMP Securities.

SUMIT SUNA, ANALYST, JMP SECURITIES: Yes, thank you. Couple of questions. If you could talk about the networks business, understandably you've been taking some initiatives over the last couple of quarters to clean it out. When can we start to see improvement in that business, when you end these initiatives and then I have a housekeeping follow-up.

PATRICK PICHETTE: Could you clarify exactly -- are you asking about AdSense for Search? What exactly are you asking?

MARK MAHANEY: The Google networks business, I'm just looking at that, kind of open it up over here. It was down sequentially a little bigger than it was down last quarter. So I'm talking about that, you had some -- you were getting rid of some arbitrage, players, things like that. When are those activities -- when do you think that ends?

PATRICK PICHETTE: Some of that relates to partner issues. Some of it is the network clean-up. I think that to date, the clean-up has been largely successful, but it's kind of an ongoing cat and mouse game, just like e-mail spam. So I don't think I would necessarily want to suggest that the clean-up issue has been fixed. I think we did start engaging pretty aggressively in those efforts last year and we've made great progress. I think the other piece that you may see is there's probably some FX issues and other partners that we have that our built in there that are seeing the same kind of economic issues that we have as well as having to sort of understand which partners are in the overall mix, which is a factor. We don't give you the full list of those dynamics.

MARK MAHANEY: Sure. In terms of the follow-up, can you talk about the correct share count to use. You had repriced some options. Would these become dilutive any time during the year?

PATRICK PICHETTE: Restate the question for me, please.

MARK MAHANEY: You repriced some options, some underwater options, do they become part of the diluted share base now that they are in the money? They were priced at my sense is about 306.

PATRICK PICHETTE: No, not any time soon is the answer. Very small, very small. So you wouldn't count on them.

MARK MAHANEY: Okay. Thank you very much.

PATRICK PICHETTE: Just to complement Jonathan on the -- to come back to the issue of the network, I mean, there is a difference between obviously AdSense for search and AdSense for content and clearly two types of businesses with two different kind of rationales, if you think in the behavior and the content side obviously branding oriented display campaigns as I mentioned a bit earlier. So on that side, obviously remaining challenging in Q1 because those

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advertisers kind of typically will shift to more relative to their performance based advertising if they have a chance and tighter budgets. So really a tale of two cities between the AdSense for Search and AdSense for content. Just to complement Jonathan's.

JONATHAN ROSENBERG: I agree. That's correct.

SUMIT SUNA: Sure. Thank you.

KRISTA BESSINGER: Next question, please.

OPERATOR: And we'll take James Mitchell from Goldman Sachs.

JAMES MITCHELL, ANALYST, GOLDMAN SACHS: Hi, thank you for taking my question. Can you talk about the impact of no longer providing rebates to agencies on your revenue growth in the international business?

PATRICK PICHETTE: Hold on just for a second.

JONATHAN ROSENBERG: You're referring to the best practices funding?

JAMES MITCHELL: Indeed.

JONATHAN ROSENBERG: Which we've phased out over the course of the last year. Patrick wasn't here for all of that, so.

PATRICK PICHETTE: What would be specific, James, in your question, like what would you like? What do you want?

JAMES MITCHELL: There was something that materially impacted the first quarter or is it something that because it was phasing over the last year, it's been more--?

PATRICK PICHETTE: No, it wouldn't have been material.

JAMES MITCHELL: Okay. Thank you.

KRISTA BESSINGER: Next question, please.

OPERATOR: We'll go next to Youssef Squali from Jefferies & Company.

YOUSSEF SQUALI, ANALYST, JEFFERIES & COMPANY: Thank you. So just to reiterate on the BPF, our understanding is that a number of agencies were still getting a fair amount of money, somewhere between 6 and 7% back as of Q4 and starting January 1, that went down to zero. So you're saying that the year on year decline of 9% call it in the UK I guess was not materially impacted by that?

PATRICK PICHETTE: That's correct. For total revenue, you may have had one agency for whom it would have mattered for that agency but in the total of our revenues it wouldn't have been material.

YOUSSEF SQUALI: Clarification. Why was DoubleClick revenues weaker this quarter? I think on the prior call, you kind of talked about that but you didn't kind of provide the reasons why.

PATRICK PICHETTE: Well, I think there's two elements on it. One is seasonality because if you think of DoubleClick and Q4 it's been a very strong quarter for the display advertising related to the Christmas, certainly in North America which is a big element of the DoubleClick and then second is the entire economic environment right now is putting a lot of pressure on that business. So it's the combination of these two things that really we're seeing in the market.

YOUSSEF SQUALI: Okay. That's helpful. Thanks, Patrick.

PATRICK PICHETTE: You're welcome.

KRISTA BESSINGER: And next question, please.

OPERATOR: We'll take our next question from Christa Quarles from Thomas Weisel Partners.

CHRISTA QUARLES, ANALYST, THOMAS WEISEL PARTNERS: I was wondering if you guys to dig into some of the mobile data a little bit more. I guess what I'm seeking is in this example that you have in Japan, do you have a sort of RPS relative to what you're seeing in other markets in terms of increase? I listened to your mobile webinars where you guided advertisers to bid maybe 4X with their bidding on the PC, simply because there are fewer chances to

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be shown. I mean, is there I guess any quantification whatsoever you can provide around how monetization is ultimately different on the mobile relative to the PC?

JONATHAN ROSENBERG: I think it's really too early. It's too early to say. I think that we -- we certainly see the promise, we think. I mean, if you're asking specifically about Japan or are you asking--?

CHRISTA QUARLES: Well, I guess what I'm trying to ultimately do is quantify. I thought Eric's comment was really interesting that you guys are now, what was it, 8% mobile browsing share.

JONATHAN ROSENBERG: I think I said that.

CHRISTA QUARLES: Or you said it. Yes. Somebody said it. Which is the first time I had seen that data out of you guys. So again, trying to quantify what this opportunity could ultimately mean and if monetization ultimately becomes even more intriguing, interesting in a mobile context relative to a PC one, then people might get more excited.

JONATHAN ROSENBERG: Yes. I personally think mobile is going to be very significant. I talked in my prepared remarks about how powerful the phones are and the degree to which search traffic is up over five times in the last couple of years. It is the case that nearly 80% of our mobile search queries come from outside of the US so a lot of the lessons that we're learning at this point are lessons that we're learning from markets like Japan to some extent, China and India.

I think the thing you really have to look at is if we've got 100 million, 175 million SmartPhones shipping in 2009 and they all have this much, much different, very rich mobile browsing experience, you're basically talking about something that didn't exist on phones a couple of years ago. They didn't have the processing power. They didn't have the battery life. They didn't have the rich display. They didn't have an impact mechanism that worked well. We didn't have the kind of fast networks that we have today and we're now seeing many people, many developers understand that the web is this wonderful platform for these mobile apps and they could be fast. They could be location aware. They can offer a rich experience and even work offline and that I think is fundamentally going to change the whole value equation with these devices. And you're going to see that users are much more likely in my opinion in the long run to consummate a transaction against an ad that they were served on a mobile phone because they're much -- they're probably clicking on that ad or interested in that ad because they're out somewhere and ready to go consummate a transaction.

So I think there's lots of reasons to think about where the business is going and where these phones are going, which make us very excited. There's not a great deal of data yet on what the pace of revenue growth will be there. Other than what we're seeing in Japan, which is very promising.

CHRISTA QUARLES: Just want to follow-up on the mobile side, you guys have an investment in Clearwire. Obviously there's broad based concerns there, would you guys ante-up further if they needed additional cash or I guess what's the -- is there any plan around that investment?

JONATHAN ROSENBERG: The lawyer across the table is telling me to tell you we don't comment on future potential investments.

CHRISTA QUARLES: All right.

JONATHAN ROSENBERG: One thing I would actually urge you to think about when you look at some of these other markets like Japan is that in some of these markets there are many users who only access the web through their mobile devices and that makes the dynamic very, very different. And of course, Japan is far ahead in terms of mobile consumption than other markets so it's an interesting market to look at in terms of where I think the trends are going to be.

CHRISTA QUARLES: Got it. Thanks, guys.

PATRICK PICHETTE: Thank you, Christa.

KRISTA BESSINGER: Next question, please.

OPERATOR: We'll go next to Justin Post from Merrill Lynch.

JUSTIN POST, ANALYST, MERRILL LYNCH: Hi, I apologize if you've already addressed this but one of the things I see really interesting on YouTube is the quantity of searches and it's becoming one of the leading search engines out there and I think you've rolled out some new ads, what is the click through rates on some of those video

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advertisements that are showing up in sponsored search results? Are you happy with that and do you see that as maybe one of the bigger opportunities on YouTube and if not, what really is working right now?

JONATHAN ROSENBERG: I think we're still in the experimental stage on a lot of this. There's no doubt from a traffic perspective, the YouTube phenomenon continues. We're definitely hitting on an ongoing basis new playback and upload highs. We're basically at this point looking at multiple different ad formats. We're certainly monetizing hundreds of millions of videos in the US every month, which more than the total of US monthly views on any other online video site. We don't give you the specifics in terms of click through rates but we've got a whole bunch of new form and new content. We just launched in-stream ads on long form content so if you do a query on YouTube for Star Trek Charlie X which is one of the episodes you'll see an example of some of the new ads that we have there. Omid mentioned the home page format ad that we have which we're very, very happy with the results on which basically is a masthead that goes across the top. I think today it's Frank 2 and yesterday it was Volvo. We've also got the promoted videos which we launched last quarter which are doing pretty well but I can't give you any more details on the click through rates.

JUSTIN POST: Okay. And can you tell us how the engine is doing as far as profitability? Any thoughts on margins? Are they getting better or worse? And then just a follow-up on DoubleClick. Are all those revenues going in the licensing line and did display help your overall growth rate, the 6%, was display something that grew faster than that and helped the overall growth rate?

PATRICK PICHETTE: So I think on the display side, it does go, right, through the licensing line. So it does and then you can back out if it does make -- DoubleClick, sorry, yes, DoubleClick does go through that line.

JUSTIN POST: So we can kind of back that out and see how it's affecting the overall growth rate.

PATRICK PICHETTE: I guess so.

JUSTIN POST: Okay. Great. Thank you.

KRISTA BESSINGER: Next question, please.

OPERATOR: We'll go next to Jeffrey Lindsay from Sanford Bernstein.

JEFFREY LINDSAY, ANALYST, SANFORD BERNSTEIN: Thank you. Just want to ask about the large reduction in traffic acquisition cost. This was due to mix shift or is it that you're rolling off expensive deals? What I'm interested in is how sustainable is that, that trend, and then if you could just mention -- I don't know if it's public or not, just how long you've got to run on the current AOL and Ask deals?

PATRICK PICHETTE: Okay. So the short answer is it is mix. And we obviously don't comment on any deals that we have in our pipeline. I think it's also, if you look at our Q4 '08 versus Q1 '09, our Google TAC versus Google total revenue on the Google side, it's gone up slightly and that's -- if you think of -- there's the mix within the category and then there's mix between categories and on the Google side, obviously it reflects the growth in our revenue from tool bars and browser distribution agreements. So that's how I would think about it.

KRISTA BESSINGER: Next question, please.

OPERATOR: We'll take our next question from Jeetil Patel from Deutsche Bank.

JEETIL PATEL, ANALYST, DEUTSCHE BANK: Couple of questions. Broadly two different questions. If you adjust for FX and you look at your CPCs, they look like they were still up or flattish on a year on year basis when adjusting for FX but not as much as before. Can you talk about I guess conversion rate coming off and I guess in particular, which regions are more -- are you seeing more pronounced changes in CPC or conversion rates out there that could fluctuate the overall CPC trend. And then second, I guess it looks like the UK obviously fell pretty quickly in terms of revenue, constant currency and then came back. US it seems like more of a steady decline but holding its own and rest of world is kind of a mixed bag. I guess can you characterize where do you think we are in the rest of world camp in general in terms of kind going through this recession and seeing that impact in some of your regions? Is it probably early stages similar to US trend or does it look like it will pace similar to the UK? Thanks.

JONATHAN ROSENBERG: So this is Jonathan. I mean, we don't really break out the components of the RPM equation so I'm not sure I'm going to give you a whole lot of color here. You can't derive price directly from paid clicks growth. In the total amount of information that we give you, I think I did say on the call that some of what we're seeing on CPC is mix issues. It's particularly mix issues from the smaller emerging markets. It's certainly an FX component. It's certainly the lower dollar items and the issue of conversions being relatively lower than they had in the past and as

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Eric mentioned the auction working and advertisers, advertisers lowering their bids. So I think that that is -- those are components. We certainly had seen a lot of CPC growth in the quarters before the economy collapsed. But I can't give you any more detail than that.

JEETIL PATEL: I guess in some of the nascent regions that are still ramping, if you open up more distribution or more coverage, are you seeing bid prices improve like you saw over the course of the last couple years here or in some of the more mature markets or is it a different dynamic in some of these emerging markets?

JONATHAN ROSENBERG: So I think that we're seeing different because a lot of those markets are sort of at the more nascent stages of the growth rate so if you sort of map them against what we saw in the US or the UK which was actually the leading market and said they're N years behind us, many of them are on growth trajectories that are strong but obviously they're being, just as we were a few years ago, but obviously that's being dampened by the economic dynamics just like things are here and of course you also have the FX effects there too.

KRISTA BESSINGER: Next question, please.

OPERATOR: We'll go next to Ross Sandler from RBC Capital Markets.

ROSS SANDLER, ANALYST, RBC CAPITAL MARKETS: Hey, guys. One kind of high level question and then one or -- one or two accounting questions. Follow-up on the pharma ads issue earlier. So looks like the FDA may actually require all these pharma advertisers to add all the disclosures to their ad creatives. Is that a fairly easy task for Google to increase the available character length on those particular ads or is that going to be a little bit more challenging, given the complicated technology?

JONATHAN ROSENBERG: Yes, I'm not sure what we're actually going to do there. I'm not convinced that we won't be able to come to some agreement in terms of what the right solution is with respect to some of these issues. Certainly, it wouldn't be ideal if we had to modify the user interface to accommodate substantially more information. Can it be done? Yes. Is it easy? Maybe not.

ROSS SANDLER: Okay.

JONATHAN ROSENBERG: So we're going to find a way with the advertisers to make this work in one way or another and you could do it within the existing creatives if you had to.

ROSS SANDLER: I mean, just a quick follow-up on that. Are the advertisers actually still doing stuff right now or are they completely on hold until this issue gets resolved or can you not comment on that?

JONATHAN ROSENBERG: I believe there are some things that have been shut off but I don't know all of the details about what subset of the activity there has been shut off. Some of them are I think attempting to change relative to the new standard which they need to try to address. It's not really as big a deal I think as folks are making it. I know that I said that health was a vertical that was doing particularly well and pharma is important but it's really a pretty small segment of the whole vertical.

ROSS SANDLER: That's good color. And then Patrick, if we can just get a little more clarification on the accounting around the hedging program, kind of going forward. So the way it was explained before, was an 18 month kind of rolling forward of these contracts. So why did we see the one-time boost in the first quarter and are we to expect more of that or is it -- how do we think about the accounting around the hedging program?

PATRICK PICHETTE: Okay. So the fundamental issue that you have is it's not one-time. It just happens that as every quarter we set up another tranche of hedges. Some for the immediate short-term that we don't have covered yet, but covered more and all the way to 18 months out. Think of it as kind of you're building the equivalent of a ladder every quarter, kind of filling the pipeline as every quarter retires so in Q3 of '08, we happened to -- that's when we actually put originally the first set of pound hedges that we built over a couple of quarters and now we'll have a full 18 month ladder built over the coming quarter. So that we'll just be rolling that entire set of hedges every quarter going forward but in Q3 we put in a bunch of them for the next quarter and the next quarter and the decreasing rate, not rates but exposure levels all the way down to 18 months and it happened that the ones we put in Q3, because of where the pound went, gave us a substantial gain for Q1.

I mean, next quarter, we'll have more hedges that will kind of come to fruition and we'll have to decide what to do with the options that we've got. It's not a one time item. The real item that happened is the ones that we had put in September because of the wild fluctuation and variability of the pound over the last six months, we just happened to

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gain a lot. Had we had, I'll give the extreme other case where assume that the pound had gone nowhere, had been very stable through the entire period, right? We would have spent the money and we would have had no benefits because there's nothing to capture because there's no volatility. So it really was driven, the last six months, and -- in a way, I really feel for the investment community and the analysts trying to run these models. I really do feel for everybody because you have such high volatility in the last kind of nine months and because of that is compounded by the FAS 133, that says well, if you're in or you're out, you've got to book it all or not the minute that you get a decent amount of volatility. It just swings the numbers all over the place.

So what we have to think about, from our perspective, is we continue to have a very stable hedging program in place. It continues to deliver us the value when there's high volatility which is what happened and, we, because of the forced mark-to-market you have a decent amount of numbers floating around but shouldn't worry about that too much.

ROSS SANDLER: That's helpful. One last question, I promise the last one. On the bonus accrual issue, so a couple years ago Google used to accrue for bonuses with kind of a progressive growth manner so 1Q the accrual was kind of the lowest and it ramped up throughout the year and 4Q was the highest and then in 2Q '07 you went to more of a flat quarterly accrual program. Take $100 spread it out over the course of four quarters, that is going to be 25, 25, 25, 25 or does it start at 10 go up higher on the bonus accrual issue.

PATRICK PICHETTE: We tried to, if you think about it, we tried to -- as they -- when you start the year, you have a plan in place and that plan you accrue according to what you think the year's going to unfold and that's all we do and then as the year unfolds, we would if we had more information to raise the accrual, would do so. So that's how we plan the year. That's why the number has gone down relative to Q4 because I mean, if there's a good proof of how uncertain an unchartered territory we live in, look at Q4 and our results in Q4 and the economic activity that was really in all of the turmoil that was happening, we had a very strong revenue quarter in Q4. And that created a bonus accrual that, if you had thought even, kind of September or August, right, we hadn't foreseen. So we're very happy with the results and therefore happy to take the accrual and celebrate with all the Googlers and now we're back to our regular territory, of here's the year and here's the plan the way we go. That's why variability. Because the world is very uncertain and we're living through it right now, all of us together.

ROSS SANDLER: Thanks. That's very helpful.

KRISTA BESSINGER: Next question, please.

OPERATOR: We'll take our next question from Sandeep Aggarwal from Collins Stewart.

SANDEEP AGGARWAL, ANALYST, COLLINS STEWART: Thank you for taking my questions. Jonathan, one question is, we are seeing little bit higher traction for Search engine optimization and so question to you is does that -- how does that basically -- does that mean the ecosystem of paid search is expanding or does this mean there's some potential threat to the paid search campaign? And then I have one follow-up question.

JONATHAN ROSENBERG: I guess I'm not sure what is the perceived threat that you're articulating, as a result of search engine optimizers?

SANDEEP AGGARWAL: Well, if I'm running a Google ad campaign and then I'm also running searching an optimization, Google receiving the money I'm running more, optimizing my website, landing pages, et cetera, in that case am I likely to cut my paid search budget and I look at someone for search and payment optimization?

JONATHAN ROSENBERG: I honestly don't have any idea. You're basically saying is there going to be a shift in AdWords spending, spending on SEOs. And I don't know.

SANDEEP AGGARWAL: Okay. And just one question, Patrick. On a sale team side, just one thing. I think too many things happened too quickly. Is there -- I know Omid tried to address some of those things in the previous call you hosted but is there any of the read through in terms of is there -- if this is -- should we expect some more changes in the sales structure, sales channel or anything else of that sort?

PATRICK PICHETTE: We have no plans right now. I think that the work that was done by the team was very well done and that's why, as you can imagine, for any organization, the last thing you want is announcement every two weeks of changes. That just drives everybody nuts. And so we had an opportunity in the sales group to do the things that we announced and so we did announce them a few weeks ago and right now we have no more plans. I mean, it's obvious that the world continues to be quite uncertain. Right? So in that kind of world, you've got to stay flexible but right now we have no other plans.

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SANDEEP AGGARWAL: And just one thing about, is there going to be any future revenue contribution from that discontinued audio business?

JONATHAN ROSENBERG: Is there going to be any--?

PATRICK PICHETTE: No.

SANDEEP AGGARWAL: Okay. Thank you very much.

JONATHAN ROSENBERG: Sandeep, I'm just thinking about your original question a little bit and I think the one comment that I could offer is I don't tend to think of these advertisers that we have as having fixed budgets and I think it's kind of unlikely that someone who is running an AdWords campaign where they're measuring the ROI that on an incremental basis is experiencing positive ROI from each incremental AdWords click. It seems unlikely that they would throttle that budget back if they're making positive gross margin on each of the AdWords clicks. So what you're proposing seems unlikely to me but plausible.

SANDEEP AGGARWAL: Okay. Sure. Thank you so much.

KRISTA BESSINGER: We have time for two more questions, operator.

OPERATOR: Thank you. We'll take our next question from Brian Bolan from [Start Event & Company].

BRIAN BOLAN, ANALYST, START EVENT & COMPANY: Hi. I want to touch back on the question or the idea that Eric brought up, the ROIs moving more into Google's favor. As we look at the moving parts in there, we just look at like clicks and searches, costs and conversions, with the market pretty much moving cost lower, isn't that going to be the major factor or what is really driving the ROIs up anything more than just the costs coming down as advertisers moving out of the space? And is there anything that will, other than keeping the costs low, allow for advertisers to actually really stage up and spike into the market to push ROIs higher?

JONATHAN ROSENBERG: I think really the main thing that drives ROI is to the degree to which we're able to develop better ads and ad systems, that target more efficiently and are more -- deliver an ad such that if the user clicks on it, they're more likely to consummate a transaction. I think the conversion rate is probably the most significant component and that's a function of the targeting of the ad and the creative on the ad. Also, some of the tools that we offer with respect to optimizing users website, which analytics and the website optimizer, things that allow the advertiser to get higher conversion rates on their site. I think that's basically the kind of things that we're going to do that will improve, that will continue to improve ROI.

BRIAN BOLAN: Okay. And you talked about the optimizer there. About what percent of customers are using the optimizer?

JONATHAN ROSENBERG: I don't think that we've said. You'd have to talk to customers directly yourself. There is a blog post if you look at -- if you type conversion optimizer on Google where we describe some of the details of a study that we ran with a bunch of advertisers from which I got the percentage improvement and different pieces but we don't release that number. A pretty large portion of our advertisers are using some of the various -- some subset of the various tools that I've mentioned, the website optimizer, the key word piece, the conversion optimizer, Google analytic.

BRIAN BOLAN: Great. Thanks a lot.

KRISTA BESSINGER: Last question, operator.

OPERATOR: Thank you. We'll take our final question from Robert Haley from Gabelli.

ROBERT HALEY, ANALYST, GABELLI & CO.: Great. Thanks. Wanted to just ask one question on your paid click growth. And if you could talk about what's driving that growth, whether it's growth in the number of advertisers using Google or maybe talk about paid click growth on a per advertiser basis. And how that's impacted by changes in budgets, allocated to Google, versus changes in consumer click-through behavior?

PATRICK PICHETTE: I'll make just a broad statement and then let Jonathan complement if you wish. There is -- I mean, our traffic continues to grow. I mean, so if you think of general principles of what's going in our favor, our traffic continues to grow and we continue to have paid clicks to our network. There are different effects within that, which obviously at the macro level, if you're in a mature market like the US versus an emerging market like India, you get mix issues, you get vertical issues and you get value issues and that's basically how we think about it and manage it. I don't know if Jonathan you have additional information you want to share or if I missed something big.

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JONATHAN ROSENBERG: I mean, Patrick got the biggest thing, it's clearly query growth is the primary driver there and beyond that I don't think we really go into detail on the other components of the equation. I don't think that there's significant activity with advertisers withdrawing themselves from a budgeting perspective all together. I would echo what Omid said there, that to the extent we are impacted by budget reductions, it tends to be the larger organizations where a CFO, somebody in Patrick's role basically says we want to cut budgets N percent across the Company and that impacts the CMO. That's much less a factor in the small and medium businesses and interestingly, it's less a factor even in some very large companies that really understand the concept that Omid mentioned about Google being a sales channel as opposed to a marketing expense and I would take to heart the comments about the auto industry where I think you're otherwise seeing the relative shrinkage in overall marketing budgets and yet some robust growth in paid search and online advertising.

So I think there is still value. I think we're seeing a lot of value in terms of shift in markets like that one from a budget perspective. By the way, the one other obvious area there is I don't think you're seeing much budget reduction at all in the pure play online companies who really understand and measure the metrics of a lot of this traffic. I think they're much less budget -- they're much less prone to adjusting their budget.

KRISTA BESSINGER: Great. So thank you everyone for your time today. If you have any further follow-up questions, please don't hesitate to contact either myself or Maria. We're happy to answer your questions, and thanks again for your time.

OPERATOR: And this concludes today's conference. We thank you for your participation. You may now disconnect.

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