

Future of Yahoo! at Stake

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The poor results announced in January by Yahoo! have managed to whet the appetite of Microsoft, which is now looking to acquire the firm. At the moment, its \$44+ billion offer has been deemed unsatisfactory, although the door has not been closed on negotiations. In addition to trying to renegotiate a higher selling price, Jerry Lang could try to seek out another suitor, such as AOL or News Corp. He had better hurry, though, because his room to maneuver is shrinking with each passing day. Some of the most important Yahoo! shareholders are starting to exert some pressure in hopes that the company's chief exec will give concede to the terms offered by Steve Ballmer, his counterpart at Microsoft and the one behind the takeover bid. Accepting the initial proposed price—which was well above the real value of the shares' trading price—would immediately see a hefty profit. Temptation is difficult to spurn.

Ballmer will be persistent as his company needs Yahoo! in order to boost its share in the search and online advertising market, which is currently controlled by Google. If he ultimately gets his way, another obstacle will be awaiting: making the deal translate into value creation—which is no easy task. Both companies have overlapping products (such as their respective email and instant messaging services) and, above all, two different, if not opposing, company cultures. While it is true that Yahoo! no longer represents the Internet's technological vanguard as it did early on, it is still far more agile and innovative than Microsoft, which was born out of, and for, the personal computer. The more conservative strategy of the company founded by Bill Gates is better suited to maintaining control of its huge installed base of software products than to taking the Web by storm.

The mere possibility of a merger between its two rivals has triggered a quick response from Google. In order to impede the transaction, it is sending warnings to alert public opinion and antitrust authorities that Microsoft seeks to monopolize the Internet just as it has done with the markets for desktop operating systems and Web browsers. Moreover, it proposes to financially support Yahoo! so that it may resist “the bearhug” being applied by Microsoft, by way of practices such as outsourcing its advertising. While ruling out its own takeover bid (which would be flatly rejected by antitrust authorities), it is seeking the involvement of third parties, such as Disney, and Time Warner, the owner of AOL, a company that Google holds 5% of and which has now emerged as a bona fide candidate.

Google's decisive reaction comes as a surprise because there is no reason to assume that a merger of Yahoo! and Microsoft would in itself mean the birth of a rival capable of gaining ground in the short term. According to Hitwise, at the end of the year its share of the search engine market was 65.98%, far above the 20.88% attributed to Yahoo! and the 7.04% chalked up to Microsoft. It is precisely this predominance that has given Google the energy it needs to break into the once-closed territories of Microsoft, such as that of office software. Furthermore, its two immediate rivals are backpedaling in the search-engine arena. The fact is that a simple merger would not reverse this trend.

That said, although the battle for searches and online advertising (in its current state) appears to be a lost cause for Microsoft, the war is far from over. In both areas, there are still many possible and necessary moves to be made and some of those may in fact come from Yahoo!, which in recent years has invested in new technologies involving open-source and grid computing. One potential nightmare for Google would be to see its rivals finding the way to improve the efficiency of searches, personalize advertising or effectively include multimedia elements to that complement or replace the predominant text. And, on top of that, to see these potentially disruptive innovations have the vast resources of Microsoft behind them. But there is another scenario that should not be overlooked: that by taking over Yahoo!, the heavy machinery of the Redmond-based company would eventually crush the entrepreneurial capacity of Yahoo! In that case, the initial gain in market share would vanish quickly, and Google, which would be able to snap up some of the human talent flowing out of Yahoo!, would further consolidate its dominance of the post-PC environment, where it has demonstrated it is more adept than anyone else.