

# **How Google-DoubleClick is Exploiting Antitrust Law's Weak Underbelly To Dominate Internet Advertising Going Forward**

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## **Summary of Conclusions**

- Google's brilliant acquisition of DoubleClick represents another critical building block in Google's shrewd strategy to **further dominate the Internet advertising market**.
- Google's "global growth strategy" is the public euphemism for its grand plan to systematically **foreclose its potential Internet advertising competition**.
- This acquisition of DoubleClick skillfully exploits antitrust law's weak underbelly, so it is **unlikely to be blocked by the Government**.
- Google is on path to increasingly dominate and **possibly effectively monopolize Internet search** in the next several years.
- Google is currently leveraging its search dominance into Internet advertising generally in much the **same way Microsoft leveraged its dominance** in operating systems into PC software applications (Windows) in the 1990's.
- Google's very sophisticated **(anti-)competitive foreclosure strategy** goes beyond acquisitions to include: share-buying "business partnerships;" systematic theft of intellectual property; systematic click fraud; weak Sarbanes-Oxley internal controls; predatory proposed regulation of broadband competitors; and aggressive competitive arbitrage of privacy law.

## **Outline of the competitive implications of the Google-DoubleClick merger:**

- I. What is Google's real (anti-)competitive endgame in buying DoubleClick?
- II. Why Google's acquisition of DoubleClick will likely pass antitrust muster.
- III. Why Google will increasingly dominate Internet search.
- IV. What other anti-competitive behaviors by Google position Google to dominate Internet advertising?

### **I. What is Google's real (anti-)competitive endgame in buying DoubleClick?**

**Google's \$3.1b purchase of DoubleClick brilliantly positions Google to further dominate Internet advertising in a way that is very difficult for antitrust authorities to prove is anti-competitive in a court of law.** Google has figured out an ingenious, predatory, anti-competitive, acquisition strategy, that exploits antitrust law's weak underbelly and that **positions Google to effectively dominate much of the Internet advertising market over the next several years.**

It is increasingly apparent that **Google is in the process of (anti-)competitively checkmating a wide swath of unsuspecting competitors** who haven't figured out Google's real endgame. Google's predatory acquisitions are only one facet of Google's overall "global growth strategy" to **foreclose future competition** and further dominate the Internet of the future.

Google's CEO Eric Schmidt, who at Novell was on the losing end of Microsoft's anti-competitive tactics in the 1990's, has obviously learned a thing or two from that seminal anti-competitive experience.

- Just as Microsoft vertically-leveraged (bundled/tied) its operating system dominance to dominate the office applications market via the Windows platform, Google apparently looks to vertically-leverage (bundle/tie) its keyword search dominance with DoubleClick's leadership in online banner/video display advertising, and with its Google-YouTube dominance in video search.
  - This vertical combination reportedly could give Google-DoubleClick upwards of 80% of the overall market for advertisements provided to third-party websites.
- Just like Microsoft became the default office applications platform for email, e-calendars, word processing, spreadsheets, and PowerPoint, for any user, **Google has obvious designs on becoming the default Internet advertising broker/platform for: keywords, website display ads, and TV, radio, newspaper/magazine advertising for the average large advertiser.**
  - The efficiencies of a Google comprehensive advertising platform would be enormous for advertisers, and would also threaten to radically dis-intermediate a wide swath of currently "silo-ed" content networks and advertising agencies.

- Google already has more private/intimate info on more American consumers than any other company through its dominant 50+% share of the search market. Combining this search dominance with the highly-complementary data-mining potential of DoubleClick, will give Google better online behavioral-targeting information on more American consumers than any other company -- by far. This leveraging of privacy information is one of the real keys to Google's Internet advertising effectiveness – and pricing power.

Google fully understands this huge strategic opportunity; and is going for it whole hog.

- If Google can combine the world's largest business "audience" ever-assembled (over a half billion people worldwide and growing rapidly) with the best data mining and behavioral targeting algorithms the world has ever seen, they are extremely well-positioned to predatorily disrupt multiple industries and distract them from thwarting Google's ultimate goal: to dominate all forms of Internet advertising in the future.
- If Google can gain the first-mover advantages of offering advertisers the super-efficiencies of cross-media-platform advertising optimization, i.e. a vertically-integrated/tied advertising platform, **individual advertising mediums and companies will largely be at their (anti-)competitive mercy going forward. Game. Set. Match.**

While Google's stated mission is to "organize the world's information," it's becoming increasingly obvious that Google's real business endgame is to become the dominant online-advertising distribution-network in much the same way that Microsoft cornered the PC software market in the 1990's.

- The DoubleClick acquisition, like Google's acquisition of YouTube, **is really all about achieving competitive foreclosure long term.** Google's "partnership" strategy is also all about competitive foreclosure: i.e. Google's buys market share dominance through a search exclusive: with Dell for computers, and with AOL and MySpace for users.
- More than any other company, Google may have figured out how to leverage first-mover advantage and network effects -- to **foreclose future competition in online advertising through vertical integration, strategic "partnerships," and other clever (anti-) competitive behaviors.**

## II. Why Google's acquisition of DoubleClick likely passes antitrust muster.

### A. There's minimal court precedent for blocking vertical mergers like Google-DoubleClick. *(This is antitrust law's under-appreciated weak underbelly.)*

- While the Department of Justice's horizontal merger guidelines, which cover competitors in the exact same market segment, are robustly designed to prevent market monopolization via acquisition, there is minimal court precedent for blocking a vertical merger like Google-DoubleClick on anti-competitive/antitrust grounds.

- The reason for the lack of applicable precedent is simply because courts of law demand *facts* and *evidence* of harm, not just plausible theories of potential problems like discussed above. Another reason is the sound constitutional principle of being innocent until proven guilty in a court of law. On top of that protective legal bastion, there is also a large and respected body of evidence that vertical mergers can produce real efficiencies that actually benefit consumers.
- In short, no matter how much antitrust authorities may come to worry about the *potential* anti-competitive effects of this transaction that I have posited above, I believe they will have a very tough time meeting the evidentiary burden of *proving* it is anti-competitive in court.

#### **B. The “cover” of a fast-changing innovative marketplace and “convergence.”**

- The Internet advertising space is among the fastest-changing part of the economy and among the most innovative. Current antitrust authorities have a natural and wise free-market and pro-innovation policy bias for letting markets evolve free of government interference, because Government has a long history of poor choices in: picking technologies, requiring divestitures and/or “managing competition.”
  - Government officials know there is a much greater likelihood of making a wrong and embarrassing call in a fast-moving market than in a more normal one.
  - Just like antitrust authorities did not have a problem with Google acquiring YouTube, they are unlikely to block Google from acquiring DoubleClick.
- Digital and Internet convergence is also highly disruptive and generally a welcome pro-competitive trend.
  - Convergence generally allows new entrants to attack bricks-and-mortar markets with the cost and distribution advantage of digital/Internet economics.
  - Convergence also works the other way, allowing bricks and mortar companies to invade the Internet space by leveraging their bricks and mortar assets like how Blockbuster is now competing with Netflix.
  - Convergence basically enables more companies to legitimately compete in more markets, which is generally a highly competitive development.

#### **C. Antitrust has forward-looking humility.**

- Over a century of antitrust experience has drilled a sense of forward-looking humility into antitrust officials about how hard it is to accurately predict the likely competitive impacts of a merger beyond one year -- maybe two.
  - The forward-looking, potential anti-competitive insights discussed earlier will be taken seriously only to the extent that they can be *legally proven* in the short-term.

### III. Why Google will increasingly dominate Internet search.

At 50% share of the U.S. Internet search market (and 75% of the UK search market) Google is already considered “dominant” by antitrust authorities, subjecting the company to greater antitrust scrutiny.

- In February 2007, the three main market share measurers of Internet search have Google’s market share at: 55.8% (Nielsen/NetRatings); 48.1% (ComScore Media Matrix); and 64% (Hitwise, which claims to use the largest sample size: 100,000).
- All three have #2 Yahoo and #3 Microsoft steadily losing share to increasingly dominant Google over the past few years.

#### So what are the reasons for Google’s increasing dominance in search?

Google claims to have a superior competitive product and the share numbers suggest that is at least partially true. But the conventional wisdom that Google has the best search engine is surprisingly superficial. While Google execs are eager to point out that people can choose another search engine, they know how powerfully enduring their lead in search really is. They know from the “Wintel” experience that the first-mover/brand leader in a new tech market has overwhelming network effect advantages that competitors simply can’t overcome.

Google’s founders have indicated in the past what they believe are the **two keys to search success (or search dominance): comprehensiveness of searched material and responsiveness/speed of Internet search.**

- Google’s breathtakingly broad mission: “*to organize the world’s information and make it universally accessible and useful*” is powerful evidence that Google understands how important comprehensiveness of info searched is to search leadership.
  - Google knows that for a competitor to realistically supplant Google they have to be able to legitimately claim that they search more content than Google.
  - That’s why Google bought YouTube to lead in the next generation of search -- video search. (Google-YouTube already has 60+% share of video search thanks to the soft underbelly of antitrust law).
  - That’s also why Google is currently trying to be first to digitize most all of the World’s books and publications. Google even had to invent the world’s fastest scanning technology in order to actually make real progress with this gargantuan library-copying task.
  - The (anti-)competitive reality here is that **Google’s search comprehensiveness efforts are extremely expensive to maintain**, and are not something that a new entrant or most any company but a handful in the world -- could hope to match -- even if they tried to.
  - Google appreciates that comprehensiveness of search is really a *relative* race, they just have to be able to verifiably claim that if you want search the

most info, Google searches demonstrably more content than any other search engine.

- The other big key to search success is speed of search results.
  - Users expect instantaneous answers. Google has achieved this by building one of the largest private networks of servers in the world. Google has spent billions on over one million servers that are arrayed in elaborate and highly sophisticated server farms. Google is so far advanced in this arena, that Google's servers are uniquely designed and produced only for Google.
  - Google loves to dismiss critics of their search dominance by saying that they are "but one search away of losing a customer." Not true. None of the other search engines have a million servers in their network. Google has largely won the search server farm race; as long as they continue to invest here they aren't going to get caught in the foreseeable future.

Nevertheless, Google is not leaving their dominance of the search market to the competitive dimensions of just achieving the best comprehensiveness and speed of search. **They appear to be aggressively supplementing those overwhelming advantages by proactively trying to corner the Internet search and Internet advertising markets via predatory foreclosure of potential competition.**

- Google's acquisition and "partnering" strategies can be looked at as the proverbial "belt and suspenders" approach to prevent any competitor from sneaking up from behind and pulling down Google's proverbial search "pants."
- Most importantly, **Google is the only company that has the growth, cash, and stock price to aggressively buy share and buy market dominance.**
  - **Google understands its greatest (anti-)competitive advantage is its stock price and the huge capital advantage and flexibility that its stock valuation confers.** That is the reason for the current Google buying spree; they know they are currently without peer.
  - Only Google could afford to pay:
    - An outrageously-high \$3.1 billion price for DoubleClick, a price that few independent analysts can justify with a straight face. Microsoft could not afford to match Google because Microsoft's stock has been basically flat for years.
    - A ridiculously-rich \$1.4 billion for YouTube, a company with basically no revenues and a potential multi-billion copyright infringement liability. (Does this jog any distant memories of Internet bubble valuations?)
    - A \$1 billion investment in AOL to be the exclusive search engine for AOL's very large Internet traffic share.
    - A \$900 million deal with MySpace to be the exclusive search engine for the explosively-growing audience of MySpace.
    - A major deal with Dell to be the exclusive search engine on Dell computers; financial details were not disclosed.
- To the informed eye, this **Google acquisition and "partnering" pattern bears an uncanny resemblance to what Microsoft did in the 1990's to foreclose potential**

**competition** and successfully dominate the operating system and office applications market.

#### **IV. What other anti-competitive behaviors by Google position Google to dominate Internet advertising?**

##### **A. Google's business model requires disrespect for others' property.**

To fulfill Google's imperial ambition/mission "*to organize the world's information and make it universally accessible and useful*" requires access to most all the world's information.

- The fact that many content owners do not want Google to digitize their intellectual property has not slowed fulfillment of its mission.
- Google's response to uncooperative content owners has been to take what it wants without permission or compensation.
- Google justifies this systematic business theft by hiding behind its company policy of encouraging "innovation without permission."

The evidence of Google's systematic disrespect for others' property, or theft, is substantial, mounting, and well documented by the mainstream media. Google is being sued for theft of intellectual property by multiple industries and companies:

- Publishers and authors who own the intellectual property which Google wants to scan and digitize without permission or compensation;
- Newspapers who own the headlines, summaries and photos that Google provides without permission or compensation;
- Trademark owners, who do not want competitors to be able to buy and profit from their trademarks as Internet search keywords;
- The Motion Picture Association for Google's proactive complicity and support of websites that encourage the illegal downloading of pirated movies; and
- Viacom, for widespread and rampant unauthorized posting of its intellectual property on YouTube.

**What is clear from this list is a pattern.** Unless all of these different industries and companies are proven to have brought completely baseless claims, which is unlikely given that they were not coordinated suits and that they occurred over a period of time, this systematic pattern of theft is a central part of Google's business model.

- In one sense, the modern search business that Google has pioneered depends on the availability of free inputs or free content.
- **Whether or not America's courts ultimately allow Google to use everyone's property without permission and for free while making long-term profit margins not found in any other legal or competitive industries -- will largely determine whether or not Google's business model is legal and hence sustainable long term.**
  - Simply, does the Internet giant called Google have clay feet?

Since Google's founders have set Google's mission to organize all information, and they have publicly explained the key to comprehensiveness of search in maintaining market leadership, it appears that Google is not going to let little obstacles like trademark or copyright law stand in the way of fulfilling their apparent imperial ambitions.

- It appears from the evidence above that **a case could be made that there is a deliberate and organized effort at Google to make money off stolen goods.**
  - Google gets paid roughly 11 cents per search.
  - If Google can offer popular information that is more likely to be searched and not have to pay for making it available, it is all profit no cost.
  - The problem with others trying to follow Google's business logic is that every business in America could become more profitable by just stiffing its suppliers.
- Since Google may be the first company that has depended so heavily on the theft of others' property for its profitability, it may be pioneering a whole new form of anti-competitive behavior.
  - **It's hard to imagine a more anticompetitive form of behavior than systematic theft of potential competitors' inputs.**
- Just because Google has a \$145b market cap and is the darling of investors and the media, does not make it a forthright and sustainable business model.
  - WorldCom also had close to a \$150b market cap and was the darling of investors and the media in 2000-2 before it became clear that WorldCom's supposed "market" advantages were not real and eventually were found to be illegal and unsustainable.
  - *(An historical footnote: At the time, my leading critical analysis of WorldCom resulted in then WorldCom CEO Bernie Ebbers routinely deriding me as the "Washington idiot analyst." I also was the first analyst to figure out and call WorldCom's demise in my "WorldCom Dead Model Walking" research series.)*

## **B. Google benefits from tolerating systematic "click fraud."**

Google is also engaged in another form of systematic illegal behavior that provides Google with supra-funding/profits and a powerful anti-competitive advantage: click fraud. **According to Click Forensics, 14.2% of all clicks on Internet ads are fraudulent.**

- Google has shown little interest in trying to stop click fraud because it is so profitable. And because of Google's dominance in search, this fraud disproportionately benefits Google competitively.
- If the estimate that 14.2% of all Internet clicks are fraudulent is even remotely accurate -- it means the search business model based on clicks may be one of the most fraud-prone industries in the economy.
  - Click fraudsters understand that every time they perpetrate and profit from click fraud their fraud-tolerant host Google gets paid too.
  - **To put this into perspective, 14.2% of Google's revenues is about \$1.5 billion a year based on 2006 revenues of \$10.6 billion and represents almost half of Google's 2006 operating income of \$3.5 billion.**

- Without those supra-fraud profits, Google’s stock would not be nearly as inflated and therefore Google could not leverage an inflated stock price to easily outbid competitors like cash-rich Microsoft -- and could not predatorily foreclose competition through acquisition.
- So how is turning a blind eye to fraud anti-competitive?
  - Ask AT&T and Sprint how difficult it was to compete with WorldCom, when WorldCom used fraud to inflate the value of its stock.
  - High-flying stocks like Worldcom then, and like Google now, **enjoy the benefit of high-valuation or “Monopoly<sup>®</sup>-like” play money to buy companies** like MCI for WorldCom, or Youtube/DoubleClick for Google.
- Tolerating or benefiting from systematic fraud provides a **powerful anti-competitive supra-capital advantage over competitors that obey the law and have forthright business practices.**

### C. Google obviously has porous Sarbanes-Oxley internal controls.

Google embraces a culture of “innovation without permission.” Google also formally encourages its employees to work on their own “personal” projects 20% of the time.

- What they see as a cultural virtue is actually an organization out of control, an organization without adult supervision – at least 20% of the time.
- A sound system of internal controls under Sarbanes-Oxley would not tolerate repeated major lawsuits that all stem from the disrespect of others’ intellectual property.
- A sound system of internal controls would not tolerate systemic click fraud.

How are shareholders interests protected by management allowing such serious and potentially reckless corporate liabilities to accumulate and fester without sufficient disclosure and management attention?

- **Have the Google executives that have been supposedly signing that their financial statements accurately represent their business to shareholders (under Sarbanes-Oxley law) – actually spent any personal time checking or ensuring that they actually do?**
- Google’s legendary business secrecy and general lack of transparency to shareholders relative to other companies, only exacerbates this potential shareholder vulnerability.

### D. Google is the net neutrality ringleader.

Another outrageous form of anti-competitive behavior perpetrated by Google is leading the coalition to pass “net neutrality” legislation that would effectively protect Google from any future advertising competition from the broadband industry.

- The legislative language that Google has consistently supported would make it illegal for only broadband providers to do the kind of business practices that Google routinely engages in.

- Moreover, Google has not been able to present any evidence of the problem that they believe requires legislation.
- Google's real game here is to continue to anti-competitively shift their Internet distribution costs to broadband companies to maintain their supra-profits.

A simple test could gauge if Google's net neutrality motives are pure or anti-competitive.

- Would Google agree to abide by any laws or restrictions that they propose be applied to their potential advertising competitors -- the broadband companies?

#### **E. Google arbitrages U.S. privacy laws and consumer privacy to their competitive advantage.**

Google has more private information on American consumers than most any company in America, while enjoying relatively the least privacy regulation. Google also has mastered data-mining and behavioral targeting of private information more than most any company in America, while also maintaining one of the weakest privacy policies in the sector.

- Google is currently **pushing the privacy envelope in its standard business practices and is currently operating way beyond the privacy expectations that American consumers have come to expect** as a result of long-standing strict privacy regulations of Americans' financial and communications information.
- Americans enjoy no such regulatory backstop of protection when dealing with Google, despite the fact that search data in many instances is much more "private" and "intimate" than financial or communications information is.

Google is (anti-)competitively exploiting and arbitraging this huge gap in current privacy laws to drive up ads rates, because they can more precisely target Internet advertising than any other competitor.

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