Fonte: Business Week, n. 3962, p. 60-70, 5 Dec. 2005.

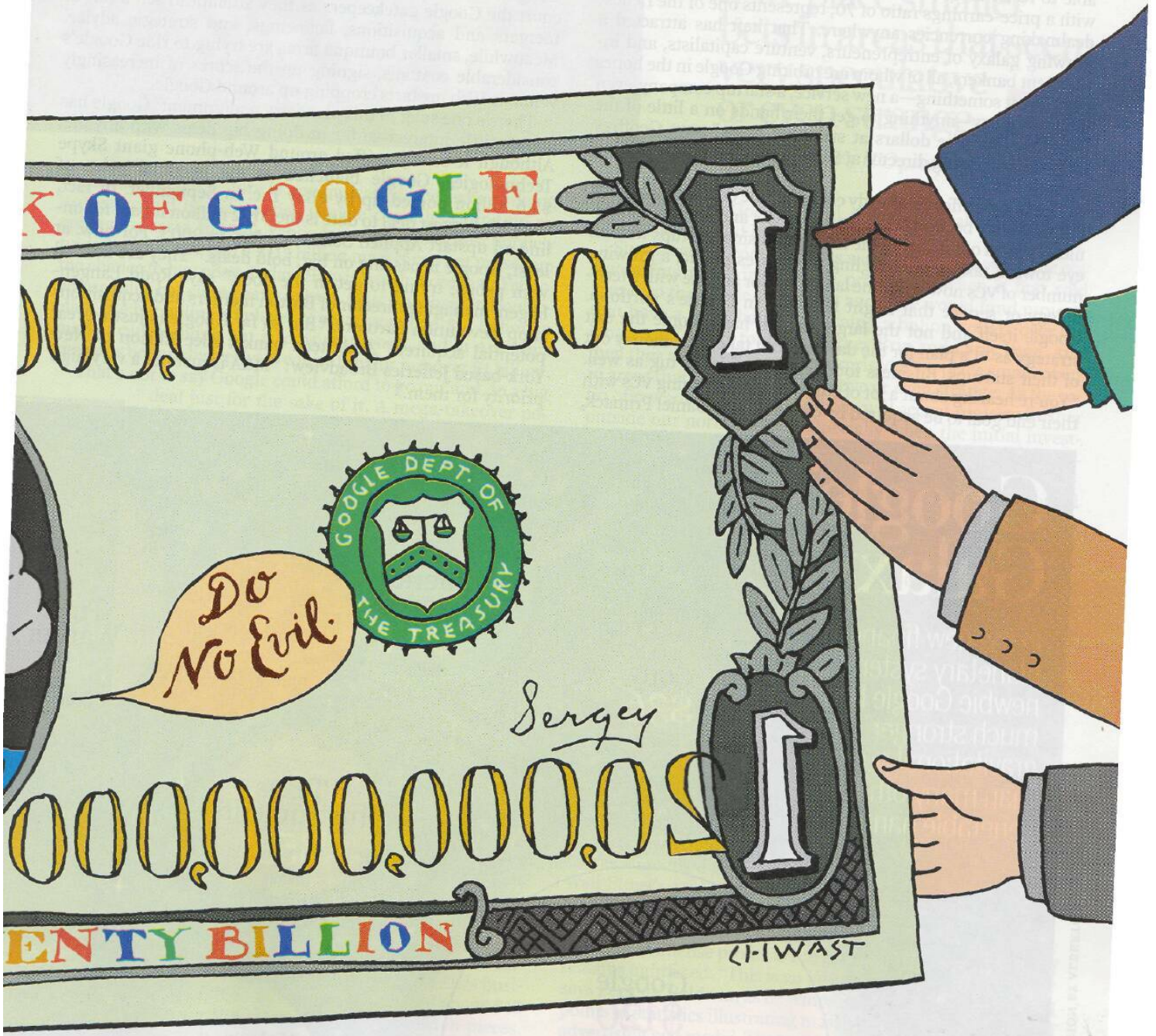
Googling

With a market cap in orbit and more cash than a small nation, Google is altering the tech industry's behavior. But when does its long-awaited shopping spree begin?

BY ROBEN FARZAD AND BEN ELGIN

SEYMOUR CHWAST

for Gold


K OF GOOGLE
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WITH THE NEWS THAT SHARES of online search giant Google Inc. had crossed the lofty $400-per-share mark on Nov. 17, the world may have witnessed something akin to the birth of a new financial planetary system. Given its market cap of $120 billion, double that of its nearest competitor, Yahoo!, Google now has the gravitational pull to draw in a host of institutions and company matchmakers unable to resist the potential profit opportunities. Google stock, with a price-earnings ratio of 70, represents one of the richest dealmaking currencies anywhere. That heft has attracted a growing galaxy of entrepreneurs, venture capitalists, and investment bankers, all of whom are orbiting Google in the hopes of selling it something—a new service, a startup company, even a new strategy—anything to get their hands on a little of the Google gold. "The dollars at stake are huge," says Geoffrey Baldwin, managing director at San Francisco investment bank Perseus Group.

The Google effect is already changing the delicate balance in Silicon Valley between venture capitalists and startup companies. Instead of nurturing the most promising startups with an eye toward taking the fledgling businesses public, a growing number of VCs now scour the landscape for anyone with a technology or service that might fill a gap in Google's portfolio. Google itself and not the larger market has become the exit strategy as VCs plan for the day they can take their money out of their startups. Business founders have felt the tug as well. "You're hearing about a lot of entrepreneurs pitching VCs with their end goal to be acquired by Google," says Daniel Primack, editor of *PE Week Wire.*, a dealmaking digest popular in VC circles. "It's a complete 180 [degree turn] from the IPO craze of five years ago; now Google is looked at like NASDAQ was then." Other entrepreneurs, meanwhile, are skipping the VC stage altogedier, hoping to sell direcdy to Google.

SHOPPING SMALL
So far, Page and Brin prefer embryonic, tech-focused startups

On Wall Street, the Google effect, while less profound, is still clearly in force. All manner of investment banks, from giants such as Morgan Stanley and Credit Suisse First Boston to midsize players such as Allen & Co., have dispatched bankers to Google's Mountain View (Calif.) headquarters, the better to court the Google gatekeepers as they attempt to sell a raft of mergers and acquisitions, financings, and strategic advice. Meanwhile, smaller boutique firms are trying to ride Google's considerable coattails, signing up the scores of increasingly valuable Web upstarts cropping up around Google.

There's one snag in this planetary realignment: Google has shown little interest so far in doing big deals with anyone. Although it briefly sniffed around Web-phone giant Skype Technologies, Google blanched at the eventual price of $2.6 billion ponied up by eBay Inc. in September. In fact, Google's biggest deal to date is the $102 million it paid for online ad upstart Applied Semantics Inc. in 2003. For now, at least, Google is passing on big, bold deals. "They are flooded with people trying to get in the door," says Rodd Langenhagen, managing director of Boston mergers and acquisitions shop Revolution Partners. "But so far Google is just a great potential acquirer." Adds tech banker Alec Ellison of New York-based Jefferies Broadview: "M&A is just not a very high priority for them."

ILLUSTRATION BY ALBERTO MENA/BW

> We would fund projects that have a 10% chance of earning a billion dollars.... Do not be surprised if we place smaller bets in areas that seem very speculative or even strange
>
> *—From Google's IPO prospectus*

But if dot-com history is any indication, the risks of doing nothing could be substantial. Google could be sitting on an ephemeral asset. In 1999, Yahoo Inc., Google's closest publicly traded equivalent, had a $115 billion market cap but passed up the chance to buy eBay. Today, eBay is worth more than Yahoo, whose value has since nearly halved. At its 1999 height, Doubleclick, the big online ad player of yesteryear, had $14 billion in market cap. It didn't put it to work, though, and in April this year was bought by a private equity firm for just over $1 billion.

That's not to say Google could afford to go out and do a big deal just for the sake of it. A mega-takeover potentially could wreak havoc on Google. Even Piper Jaffray Go's. Internet analyst Safa Rashtchy, one of Wall Street's biggest Google bulls, says: "If they were to buy AOL or eBay, it would hurt the stock." Says David C. Drummond, Google's head of corporate development: "We're not going to manufacture opportunities solely because of the currency." (Although Google prefers not to comment on its dealmaking plans, it did make Drummond, as well as its investment bankers, available for some questions.)

All the same, the lure of a big deal could prove hard to resist, particularly if Google's strategic position is threatened. For the past two months, Google has been battling Microsoft Corp. at the bargaining table for a stake in Time Warner Inc.'s AOL unit, possibly through an expanded partnership or a joint venture. Google has all but owned the AOL relationship since 2002, providing both search technology and ads. AOL has meant big business for Google, accounting for 11% of its $2.6 billion gross revenues in the first half of this year. But perhaps more compelling to Google is AOL's access to reams of content owned by sister companies such as Time Inc. and cable channel HBO.

The negotiations are taking Google into uncharted territory. Some analysts value AOL's business as high as $20 billion, including about $12 billion for the coveted portal and search pieces. The search kingpin could prevail with an expanded partnership and shell out virtually nothing. But the fact that Google is still at the high-stakes table shows how much it could lose if AOL walks.

Such strategic contingencies weren't mapped out in the coy statements made in Google's prospectus when it first sold shares to the public 15 months ago. "We would fund projects that have a 10% chance of earning a billion dollars over the long term," wrote founders Sergey Brin and Larry Page. And then they added: "Do not be surprised if we place smaller bets in areas that seem very speculative or even strange. As the ratio of reward to risk increases, we will accept projects further outside our normal areas, especially when the initial investment is small." That's enough to give hope but not much direction to would-be partners and dealmakers.

Rainmakers at blue-chip investment banks are accustomed to a certain level of respect—something that Google is unwilling to grant automatically. Just ask Goldman, Sachs & Co. Goldman famously got the boot from the elite group selected to manage Google's IPO after Brin and Page caught wind of the firm's backroom lobbying of one of Google's largest VCs for a bigger stake in the deal. The bank has been trying to crawl out of the woodshed ever since. Goldman declined to comment.

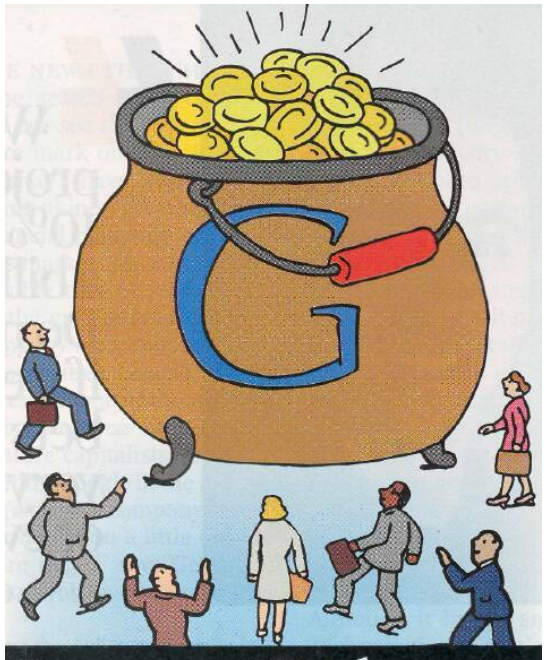
"The First Inning"

IN FACT, BRIN AND PAGE HAVE made a sport of snubbing Wall Street since they co-founded the company in 1998. They've made it clear that Google plays by its own rules and values. Their August, 2004, IPO filing reads more like a manifesto than the usual drab financial boilerplate. And by masterminding the IPO as a modified Dutch auction, they thumbed their noses at Wall Street's traditional trust-us-and-we'11-handle-everything way of doing business.

Still, many bankers believe that in the new Google-centric universe, immense profits are to be made, even if Google itself remains tightfisted. "This is an investment banking gold rush," says Perseus' Baldwin, as he whips out a glossy pitch book and points to statistics illustrating massive changes in the world of advertising and media. Those trends may be led by Google, but they imply some wrenching tectonic shifts throughout the media world. And in those dislocations lies opportunity for

astute investors and dealmakers.

Last year U.S. advertising spending was an estimated $300 billion to $400 billion. Just $10 billion of that was spent online, even less than for ads in the Yellow Pages. By contrast, newspaper and direct telephone markets were worth five and nine times as much, respectively. Yet, according to Forrester Research Inc., households now spend at least 30% of their media time online, while the Internet has just 5% of total ad spending. That situation won't last for long. According to the Interactive Advertising Bureau and PricewaterhouseCoopers, online ad revenue grew 34% in the latest quarter, with total 2005 revenue on track to grow by 25%, to at least $12 billion; newspaper ad revenue, by contrast, is slated to grow less than 3% this year. Baldwin says that Perseus has a backlog of six portal and e-marketing transactions poised to benefit from this revenue reallocation in Google's wake, and is on pace to complete at least 30 deals in 2005, twice last year's tally.



Investment Bankers

With its $120 billion market cap and $8 billion in cash, Google is a magnet for mergers-and-acquisitions bankers. And its massively disruptive effect on the media market is putting a long roster of smaller outfits—from advertisers and e-marketers to Old Economy mainstays—in play, giving bankers lots of deals to hawk.

Google's own bankers have also seen the possibilities lurking in the company's $120 billion shadow. "You almost bank on other companies becoming successful because of Google," says banker Quincy Smith of Allen & Co., which represents Google. He points to Advertising.com, an e-marketing client that appeared on his radar when he noticed that 40% of its revenue came through Google. Allen & Co. helped sell the company to AOL for $435 million in June, 2004—demonstrating how even a dormant Google made the bank money. Another major Google banker hammered home the 5% online ad market share figure in a presentation to institutional shareholders interested in Google's $4.2 billion secondary share offering on Sept. 16: "I told them, 'Oh my God, we're just in the first inning. Advertising will be completely turned on its ear.'"

In the Silicon Valley food chain, the first to lay bets on which way things will shake out are the venture capitalists whose fate is now firmly entwined with that of Google. Ifs not a very comfortable position for VCs, who view Google with a mixture of disdain and envy. Googlers, as they're known—many of whom have emerged from their company's remarkable increase in value with sizable personal fortunes—work in one of the cushiest corporate campuses in the Valley. There's the free cafeteria that was started by Google's millionaire former chef, who used to work for Jerry Garcia of the Grateful Dead, as well as facilities for volleyball, foosball, and rollerblading. After their workouts, Googlers can snack in a stocked pantry or enjoy an on-site massage. Young Googlers' preoccupation with these perks tend to drive mature VCs to distraction. "If I hear one more [punk] complain about his omelet, or tell me he's bored with the smoothie selection, I'm gonna, I don't know," splutters one.

Of course, such luxuries aren't the real problem. Ifs what the VCs perceive as arrogance and a lack of respect for the role they play. VCs, after all, have at some point identified, believed in, nurtured, and funded—not to mention made huge profits from—the biggest names in techdom, from eBay to Cisco Systems and Google itself. Yet many feel that Google accords them roughly the same respect as it does vendors bidding on the groundskeeping contract.

Startup Day

MANY VCS, FOR EXAMPLE are still turning over the Google Startup Day." VCs, who are used to making elaborate and proprietary pitches to potential investors, were instead summoned as a group to take turns making their spiels to Google's 10-person corporate development group. "Check out the gall," says one, sharing an Aug. 3 e-mail from Google's in-house M&A team. "Hi Very Senior Partner," the mass memo says by way of salutation. After explaining the hoops through which the VCs

LIKE A SUPERNOVA

The shares of these companies once soared to the heavens. Now they've come down to earth, if they're even still around.

Data: Bloomberg Financial Markets

ILLUSTRATIONS BY SEYMOUR CHWAST; CHART BY ERIC HOFFMANN/BW

would have to jump to go to Startup Day, it asks those interested to "please fill in the attached spreadsheet with a brief description of each company and its business/technology, an overview of the team, any data points you would like to share, and a perspective of why the company might work with Google." Says the aggrieved VC: "Did it ever occur to them that this was like asking us to do their homework for them? Ifs the height of arrogance." Not so, responds Google's Drummond: "This was an attempt at outreach," he says. "Most VCs do like to talk to us. Google is very much involved in the venture community—a lot more than people understand."

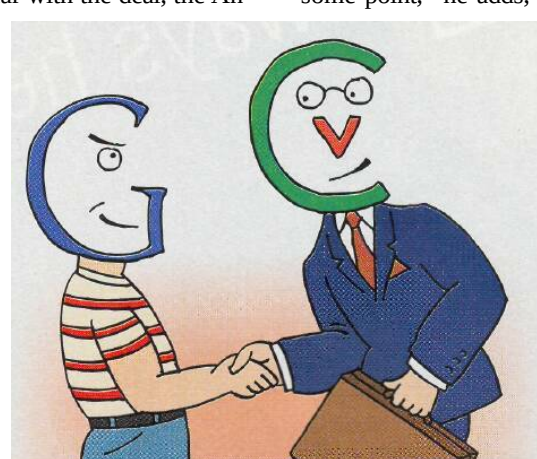
All the same, two Google insiders privately groused to *BusinessWeek* about the stunt. These companies would be foolish to cough up their trade secrets to Google, they contend, while the search giant offers little information in return.

Although Startup Day never happened, Google said it did subsequently meet with individual VCs. As Credit Suisse First Boston's George Boutros, a lead Google banker, says: "If Google wants access to the venture community, Google gets access to the venture community."

Plug'N'Play Acquisitions

VCs HAVE ANOTHER more concrete reason to resent Google: With its deep pockets and its unwillingness to give quarter to outside professionals, it's now a growing competitor to Valley VCs. Google can easily afford to swoop in and outbid any VC for a startup, particularly if Brin and Page truly mean they would be happy with a l-in-10 chance of an investment paying off big. That's encouraging entrepreneurs to "bootstrap it"—go it alone, lean, mean, and cheap, without the help of expensive VCs, in the hopes of pocketing a bigger share of the proceeds of a sale to Google. For example, Google bought both Blogger.com parent Pyra Labs and wireless player Android Inc. directly from their founders. According to people familiar with the deal, the Android buyout was essentially a bet on the company's star-studded cast, including engineering whiz Andy Rubin, who previously had founded handset maker Danger Inc. Cofounder Page, the sources say, put the acquisition on the fast track.

Indeed, Google strongly prefers to gobble up startups before they have embarked on a sales and marketing strategy, viewing companies that are completely tech-focused as a better cultural fit. It prefers to acquire small, local technology teams that it can simply plug into its headquarters. "Two guys in a garage with nose rings and a dog trying to catch lightning in a bottle" is how banker Smith characterizes the bias. Case in point: Last year Google snapped up Keyhole, a digital mapping company based next door in Mountain View, for an undisclosed sum. Its team moved down the road and within six months, Keyhole was providing the satellite technology behind Google's celebrated mapping tool.



Venture Capitalists

Venture capitalists are hatching and funding startups designed to appeal to Google. Even if the company doesn't bite, the VCs will have no shortage of suitors from among Google's rivals. But Google's penchant for small buyouts is emboldening entrepreneurs to skip the VCs and proceed directly to Mountain View when they're ready to sell.

Conversely, Google has passed on larger, out-of-town deals, in large part because of integration worries.

Google is creating a whole new ecosystem for entrepreneurs, says Baris Karadogan of U.S. Venture Partners, a high-tech VC firm in Silicon Valley. Karadogan says he's closely watching a group of entrepreneurs who are designing a highly specialized online advertising tool, hoping to sell it to Google for $50 million. "Before," he laments, "you needed a VC. Now you can build a Linux-based data system for $100,000 and survive long enough to sell without ever raising a venture round."

The suits inside Google don't fare much better than the outside pros. Several current and former insiders say there's a caste system, in which business types are second-class citizens to Google's valued code jockeys. They argue that it could prove to be a big challenge in the future as Google seeks to maintain its growth. They deem the corporate development team as underpowered in the company, with engineers and product managers tending to carry more clout than salesmen and dealmakers.

A banker who interviewed for a Google corporate development job came to a similar conclusion. "They just aren't very focused," says the prospective hire, who didn't get the job. "They're biased against businesspeople, and their deal strategy is pretty much, 'O.K., if we see something, then we'll look at it.'" The candidate, a Wall Street tech M&A specialist who was looking for a change of scenery and a more relaxed lifestyle, calls the experience "chaotic, bureaucratic, and very rigid." Strung out over more than nine months and numerous coast-to-coast flights, the courtship culminated in a jarring "pop quiz." The corporate development team suddenly broke from the script and gave the banker a laptop and 40 minutes to value a business, suggest a strategic buyer, and present a case to the entire team.

Drummond rejects the accusations that Google is anti-businesspeople. He says Google has hired many MBAs and bankers and is constantly assessing its dealmaking strategy. "At some point," he adds, "it might make sense for us to be [acquisitive] like a Cisco or GE."

Apparently, that time has not yet come. Surprisingly for a company of Google's size, clout, and business needs, it doesn't yet have a thriving in-house VC arm. And that's despite some glaring holes in its product lineup. "We're clearly not going to do everything right," concedes Drummond. "There are areas we miss that others will fill out." For starters, Google has a long way to go to match the breadth, depth, and richness of Yahoo's portal. Ditto a peer-to-peer marketplace along the lines of an eBay, as well as Microsoft-like software applications.

Despite the hurdles they face, don't expect any of the legions of investment bankers, VCs, or entrepreneurs to fold their tents and go home. The stakes are too big, and everyone wants in. To steal a note from the Google home page: Feeling lucky? ■

-With Catherine Yang in Washington

Filthy Rich, But Froogle

Brilliant, careful, and skeptical, Googlers are the toughest customers in the Valley when it comes to investment services

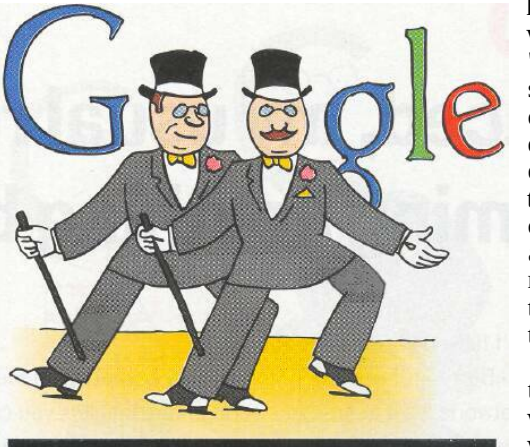
BY ROBEN FARZAD

HIGH-END WEALTH MANAGERS ARE being drawn irresistibly into the Google orbit. Ifs not hard to see why. Since going public in August, 2004, Google's stock has nearly quintupled from its $85 IPO price, levitating 130% in the past six months alone. That kind of space shot has created some very wealthy people—an estimated 1,000 millionaires and 5 billionaires at the last count—making Google that rare company where one in five staffers is a millionaire, at least on paper.

That makes Google a gold mine for wealth managers, whose eyes well up at the very idea of all the recurring fees that can come from employee assets. Advisers are all over Mountain View, cold-calling Googlers, buttonholing them at geek expos, booking restaurant banquet rooms, and jumping through just about any hoop for a shot at pitching some of the coveted 5,000 employees. (On occasion, the level of some managers' zeal dents their chances. One programmer remembers getting a phone call at 2 a.m. The broker kept dropping names off the employee's online networking profile as though he knew them personally, until the apoplectic Googler realized what was going on and slammed down the phone.)

Google ultimately green-lighted in-house presentations from six firms: UBS, JPMorgan Chase, CSFB, Morgan Stanley, and, notably, independents Presidio Financial Partners and Sanford C. Bernstein & *Co.* (Google likes to root for underdogs and has a cultural penchant for those without obvious conflicts of interest.) Not that the winners had time to run victory laps once they'd won their privileged access to the Googleplex. Bragging rights aside, they still had their work cut out for them in signing up the rich Googlers.

Some would-be sellers go to extraordinary lengths. Take Carlo Panaccione, a Mountain View area high-net-worth manager at LPL Financial Advisors. First he enrolled his young daughter in a local private school popular among Google families, all the better to meet unwary Googlers. Now he's planning a mommy-and-me-type seminar wherein parents can learn financial basics alongside their children. "A lot of them have young kids," he explains. "They do lots of multigenerational planning."



Wealth Managers

Hordes of high-net-worth brokers and money managers are chasing the hundreds of newly minted millionaires—and a handful of billionaires—at Google. They court the young Googlers on the phone, in restaurants, and in conferences. Their goal: Start decades-long relationships that will produce an endless bounty of fees.

Red Herrings

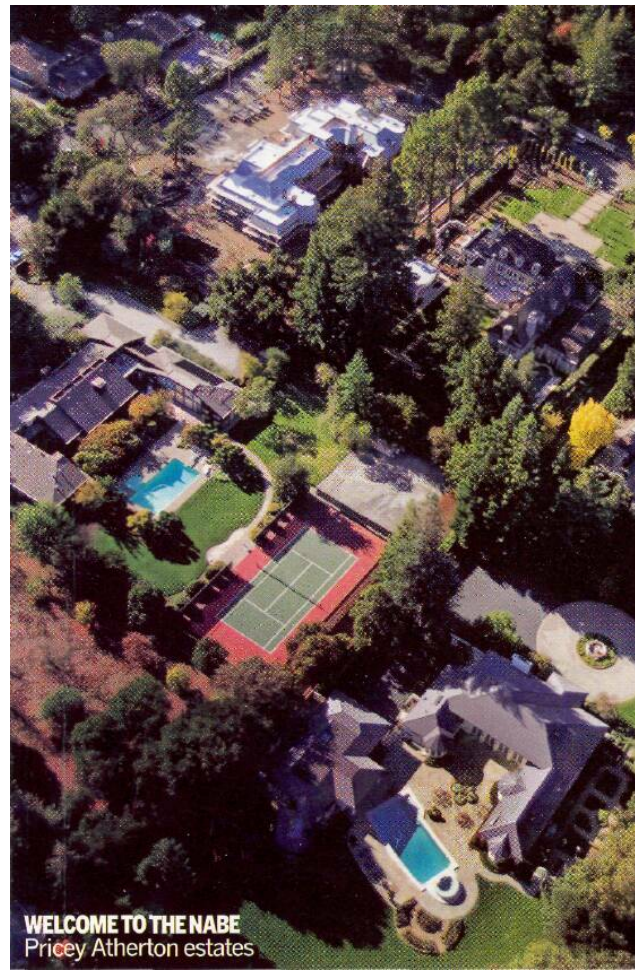
GOOGLE EMPLOYEES, whose ranks include large numbers of brilliant engineers and quants, are tough nuts to crack. While they may not necessarily be the most financially savvy, they are quick studies and obsessive researchers who talk amongst themselves incessantly. That means brokers have little chance of winning them over with prefabricated sales presentations. "Ifs an intellectual sparring session," says Brodie L. Cobb, managing director of San Francisco-based Presidio. "They do due diligence in spades. They test every hypothesis and never take anything at face value." Adds LPL's Panaccione: "You're not walking into a room and telling them to jump into this great mutual fund. If s much more complex than that. These are very careful, skeptical people."

Many start by asking bluntly why they shouldn't handle their own wealth-management duties. As Web whizzes, they point out, nothing could be easier for them than running a portfolio with an online brokerage. The brokers' rejoinder: People as rich as they are need someone to give their financial affairs full-time attention owing to taxation, estate planning, and other complexities.

What follows in the interviews is usually a prolonged back-and-forth. It often involves a grilling on financial arcana such as alpha, a measurement of

superior investment returns, and asset allocation. To test how advisers think on their feet, Googlers will often throw in red herrings and parenthetical asides about the "random walk" theory of stock pricing. And of course they expect a thorough walk through the mechanics of options collars, which guarantee a future fixed price for their Google stock in return for surrendering the upside. "If you offer a service that has a weakness," says Cobb, "these engineers will find it. They drill down and must understand everything before committing. If you try to gloss over even the smallest thing, they will call you out. These guys get it."

Flash and ostentation cut no ice at Google. Managers hoping to sign up clients need to leave their Aston Martins at home in the garage. The status vehicle of choice at the Googleplex is the Toyota Prius hybrid, which both co-founders Sergey Brin and Larry Page drive. Google even offers employees a $5,000 credit for buying an environmentally friendly hybrid car.



WELCOME TO THE NABE
Pricey Atherton estates

Being up on the ins and outs of big-time philanthropy, on the other hand, does carry weight with Googlers. Social responsibility, both corporate and individual, is a fundamental part of the Silicon Valley culture. Google.org, for example, the company's $1.2 billion philanthropic arm, was conceived to address global poverty and environmental challenges.

For personal giving, Community Foundation Silicon Valley reports that it has helped at least a dozen Google families to set up donor-advised funds since the firm's IPO. "It's a terrific response given how recent the IPO was," says foundation spokeswoman Michelle McGurk.

"Giving Back"

CONSIDER FRANK JERNIGAN, a former senior software engineer who left Google in June after four years at the company. He was attracted by the philanthropic approach. "This was my way of giving back, to help other people with the resources I've been given," he says. Toting his IPO windfall, Jernigan met with three separate wealth managers on Google's campus. Ultimately he signed up with Bernstein, which he says won him over with its independence and the way it pitched him on setting up a foundation. Bernstein will manage his investments, while a philanthropic service, Foundation Source, helps him find recipients in HIV research and homeless causes. "I just get to do the fun part," he says.

Other personal-service vendors are also working frantically to land Google clients by thinking—and marketing—like a Googler. Brande Kramer, the Silicon Valley manager of matchmaker Ifs Just Lunch, says he's still trying to set up an on-campus presentation at the Googleplex. "You would be crazy not to make contacts over there," he says.

If you type the "GOOG" ticker into Google's search line, you'll find Silicon Valley homebuilder James Witfs ad for new homes in the area on the sponsored links margin. Shrewd real estate players like Witt pay as much as $3 for each click on the two-square-inch pieces of pixilated property. With typical five-bedroom homes selling for a cool $5 million—and estates usually at least twice as much—that's a bargain price for such ad space. "Rather than buy an expensive ad aimed at dumb people watching the Superbowl, I would rather target someone smart enough to get hired at Google," says Witt.

Despite their reputed arrogance, rich Googlers show humility in managing their own finances. Whether it's putting money into charity or taking some of their Google dollars off the table and moving them into other investments, they're not about to fall into the same trap that hurt hundreds of former paper millionaires in Silicon Valley.

Panaccione can tick off scores of former clients, employees of such companies as Netscape Communications Corp. and portal-Internet service provider Excite@Home, who saw their once-considerable net worth vanish into thin air in a matter of months. (Once valued at $35 billion, Excite ended up worthless. Its old headquarters, just up the road from Google's, was recently converted into a hospital.)

Converting at least part of their Google stock holdings into other forms of investment seems to make eminent sense for the Googlers. "No matter how incredibly great Google is doing now," says Panaccione, "at some point there will be a Google-killer out there." Adds Geoffrey D. Baldwin, managing director of San Francisco investment bank Perseus Group: "If the world [can] change as rapidly as it has in Google's favor, it could just as rapidly change away from them." This time, the engineers are listening. ■ *-With Jessi Hempel in New York*

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