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STATE OF THE INDUSTRY

LiveRail's Q3 2008 review of online video advertising

LiveRail Research Department

HIGHLIGHTS

- Online video advertising spending to grow >55% next year
- US online video advertising spending expected to hit \$962m in 2009
- Confusing array of technology and ad unit standards constraining current growth rates
- Video ad spending still represents just 2.36% of all online advertising
- Average In-Stream CPMs reach \$15.80
- In-Stream (pre/mid/post roll) still representing 88% of all video ads
- 20.95% of internet video streams being monetized
- Video publishers generating an effective monetization rate of \$4.05 per thousand streams

INDUSTRY NEWS ROUND UP

MIXED SUCCESS FOR NBC'S OLYMPIC STRATEGY

Despite significant market buzz, and a special Silverlight-powered site, industry analysts are suggesting that NBC's web coverage of the Olympics was a very mixed success. NBCOlympics.com streamed 72 million videos and generated 1.2 billion page views; to put this into perspective, Yahoo Sports (which had no video) achieved an average of 4.7 million visitors a day versus NBC's 4.3 million (*source: Nielsen Online*).

eMarketer have suggested that NBC's Olympics video ad revenue totaled only \$5.75 million.

The eMarketer estimate does not include banner-ad revenue generated by NBC's 1.2 billion page views, which we estimate would have generated an additional \$12 million. However, this is still a very small proportion of the \$1bn NBC generated by their coverage overall. Given that NBC paid \$900m for exclusive video rights to the Olympics, resulting in profits of roughly \$100 million, it seems a shame that they were not able to monetize the event more successfully online.

We put this down to two major factors. First, their decision to limit the availability of content so as to avoid cannibalizing TV viewership (surveys of viewer usage and preferences have suggested this fear is substantially unfounded) and secondly, their decision to use a Silverlight-based player. Silverlight, despite being technologically promising, is still poorly distributed, with a very small installed base relative to the industry leader, Adobe Flash.

THE RISE AND RISE OF HULU

Despite still being substantially smaller than YouTube, with 88 million videos served compared to YouTube's 4.2 billion, analysts are now beginning to suggest that Hulu will be the more successful business, thanks to its ability to sell advertising across 100% of its inventory, compared to just 3% for YouTube.

This is thanks to its policy of only serving high-quality original content, and securing licensing deals from content owners, rather than allowing users to upload content themselves. This approach has removed the risk of displaying copyright-infringing content, or content of questionable quality - both prime risk factors for most advertisers.

According to one estimate, Hulu could enjoy \$90 million in revenue in its first year. YouTube's estimated worldwide revenue total for 2008 is \$200 million this year, approximately half that generated domestically. Given that Hulu caters almost exclusively to a US audience, both YouTube and Hulu could see roughly the same US revenues this year.

IAB ANNOUNCES VAST

In July, the IAB (Interactive Advertising Bureau) released its first public draft of its “Digital Video Ad Serving Template” (VAST). VAST is intended to provide a standardized communication protocol between video players and ad servers, allowing technology providers to build players and ad servers that are more easily compatible and interchangeable. Publishers who use the standard will be able to plug into multiple third-party digital video ad servers and networks without additional development.

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The current lack of standards for ad server integrations within media players has created a significant hurdle to adoption of new platforms for many publishers. Also, the complexities of re-integrating with new vendors have increased barriers to entry, preventing dynamic, open competition in the technology sector.

The public comment period will last until September 10, 2008, after which feedback will be collated, reviewed and a final version of the document released shortly after. We expect broad industry adoption of VAST to take between 9-18 months from the date of release and feel confident that the importance of standardized integrations is such that most vendors will adopt a VAST-compliant platform strategy in this timeframe.

LIVERAIL JUNCTION

In August, LiveRail announced Junction, a new publisher tool to facilitate the complex task of managing relationships with multiple ad sources. Junction gives publishers the flexibility to request and display ads from any ad source, ad network or ad server without making adjustments to their media players or back-end infrastructure, reducing the lead time to going live with new ad partners, minimizing unfilled inventory and maximizing revenue. Junction also takes care of the complex process of distributing available inventory among partners and content owners, allowing publishers to divide their inventory according to sales rights and track revenue share accordingly. It is seen as an important tool not just to help minimize the technical difficulties of working with multiple partners, but also to manage the problem of making online video a viable business.

eMARKETER REVISES ONLINE VIDEO AD SPEND NUMBERS

eMarketer again revised their estimates for the size of online video advertising spending in the US in August. Estimates for 2008 were revised down to \$505m, with 2009 readjusted to \$750m and the industry expected to cross the billion dollar mark in 2010 to a total of \$1.15bn

INDUSTRY CHALLENGES

Q3 2008 has been categorized by a continuation of confusion and a proliferation of ad units, technology vendors and metrics. Many solutions have been developed to address the fundamental issues holding back the successful monetization of online video content, but few have stood out as a silver bullet or managed to achieve critical mass in the market. We believe this is due to several factors, and have identified 6 key challenges that the industry must overcome:

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CHALLENGE	DESCRIPTION
No True 3rd Party Ad Serving	Almost all video ad servers require that campaigns be manually booked within their own system, and in many cases, that the publisher is integrated directly with that platform. There is still no ubiquitous technology analogous to “ad tags” from the display advertising world.
Reporting Discrepancies	Publishers are continuing to experience confusion and frustration as publishing platforms and ad servers deliver different measurements on performance.
Confusing Array of Ad Formats	From “linear video interactive ad with companion ads” to “non-linear non-overlay ads” the industry has succeeded in developing a proliferation of formats, but the abundance of options (and confusing terminology) has created difficulties for advertisers in terms of purchasing decisions, delivery of creative and measuring engagement, delivery and ROI.
Non-standard Integrations	Video players and ad servers do not have a standard protocol for the request, response and display of advertising. Publishers who wish to receive ads from one partner may find that they need to undertake a totally new technical integration in order to receive ads from another; this has prevented fluidity in the market for technology and among ad networks.
Inconsistent Terminology	Although the IAB has tried to set standard definitions for metrics and units, the industry has still failed to adopt a consistent lexicon for the description of both units and metrics

CHALLENGE	DESCRIPTION
Measuring Effectiveness	Whereas direct response advertising can easily be shown to be effective or not, brand advertisers using online video have difficulty proving the effectiveness of their campaigns. Technology to measure metrics like “brand lift” will help prove the usefulness of video advertising improving ROI and enhancing optimization.

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While the IAB has made steps to tackle some of these issues, the nature of the organization does not permit it to impose any of these standards, nor does it always provide the simplest solution, given its desire to satisfy the broad (and often diverging) interests of its members. Additional vendor consolidation and the emergence of market leaders may help resolve some of these issues.

VOLUMES AND VALUES

Q3 2008 has been an successful period for online video advertising, with improving adoption, perception, spending and performance across a variety of metrics.

Overlays

Average overlay click-through rates: 1.1%

Click-through rates from overlay ads to websites: 10.6%

Close out rates for overlays are 81%

Click-through rates for standard overlays: 0.8%

Animated overlay click through rates are: 4.2%

Completion rate for video ads launched as a result of clicking on an overlay are: 90%

Average CPMs for overlay ad campaigns are \$18.40

Current size of the market for overlays: approx. \$70m

We estimate that overlays (and other non-linear ads) represent 12% of video ads served

In-Stream (pre/mid/post roll)

Average completion rates are 79% for 15 second pre-rolls

Average completion rates are 84% for 30 second pre-rolls

Click-through rates for in-stream ads (to advertisers' websites): 11.5%

Average CPMs for in-stream ad campaigns are \$15.80

Current size of the market for in-stream ads: approx. \$550m

We estimate that in-stream ads represent 88% of video ads served

Industry-Wide

- 153 billion US video streams projected for calender 2008

- Estimated calendar 2008 US online video advertising of \$619m

- At these volumes, video publishers are achieving an **effective monetization rate (EMR) of \$4.05 per thousand streams**. This figure is calculated by dividing the total dollar amount spent on US video advertising by the total number of US streams, which represents the average CPM for videos diluted by the fill rate

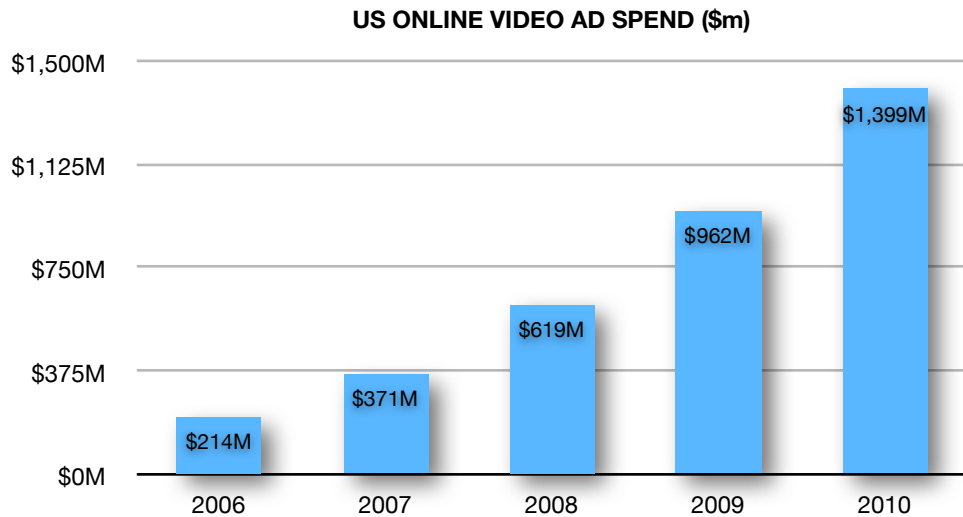
- Given our overlay and in-stream ad unit data, and assuming each monetized video asset contains 1.2 billable ad units, we estimate the average monetized video asset nets an eCPM of \$19.33

- At this rate, we find that only 20.95% of video streams are currently being monetized, meaning that four fifths of video streams are displayed without any in-video advertising.

FORECASTS

	2006	2007	2008	2009	2010
US Online Video Ad Spend (\$m)	\$214	\$371	\$619	\$962	\$1,399
Growth (%)		73.25%	66.86%	55.47%	45.42%
US Total Online Ad Spend (\$m)	\$16,879	\$21,206	\$26,168	\$31,248	\$36,215
Growth (%)		25.64%	23.40%	19.41%	15.90%
Video as a % of total spend	1.27%	1.75%	2.36%	3.08%	3.86%

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About LiveRail

LiveRail is a venture capital-backed startup providing technology products and services for online video advertising. The company's video-focused approach allows it to deliver superior advertising technology tools, empowering publishers and advertisers to make the most of the opportunities of online video. LiveRail is based in San Francisco, California. For more information, please visit www.liverail.com.

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Disclaimer

The figures, statements and statistics contained in this report have been gathered and compiled by LiveRail through observing activity on its own network, collating data/reports from third parties including ad networks, advertisers, publishers and technology partners both formally and anecdotally, statistics gathered from third-party white papers and by general observance of the industry. Statements in this document are accurate to the best of our knowledge; however, LiveRail makes no guarantee as to their accuracy for any purpose.