

The Dialectics of Cost-Per-Click (CPC) Advertising

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Introduction

Leading economists are calling the current economic meltdown one of the worst in history, and are stressing the need for a new and more responsible capitalism. This is notable, but by no means new. As far back as 1848, Karl Marx theorized that unconstrained capitalism contained the seeds of its own destruction: the dialectic of capitalism.

Marx argued that there was an inherent conflict between the base of capitalism and its superstructure. The economic base of capitalism was industrial production. The superstructure was the system of private property, under which people owning the technical apparatus received the lion's share of the returns. The two were mutually incompatible with each other.

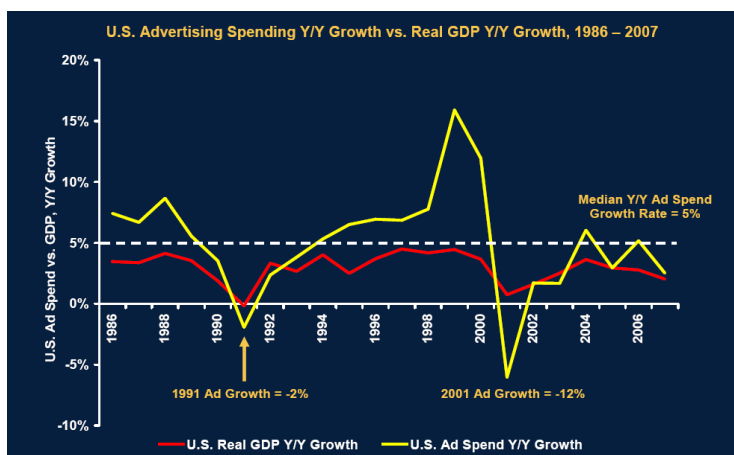
Why?

The base of capitalism (industrial production) relied on community members working together in an organized and interdependent manner. On the other hand, the superstructure (private property) was highly individualistic. A complex capitalistic society would need rigid structure and direction, but capitalists themselves would seek out a ruinous freedom.

There is an important lesson for online advertising professionals here. There are a variety of pricing models available today, and it is important to examine the dialectics within each of them to see which of them will prompt a race to the bottom, and which will result in a steady state.

To be more specific, this white paper will specifically examine the rapid growth of the Cost-per-Click advertising pricing model's dominant in the marketplace today. eMarketer projects that search engine marketing accounted for as much as 40% of the Internet advertising spend in 2008.

The CPC pricing model has moved from strength to strength since the last recession in 2000-2002. As you might recall back then, even as online advertising declined by 27%, CPC advertising grew by a staggering 820%.



The shift was primarily driven by the fact that CPC advertising allowed advertisers to pay for clicks and not just for wasted impressions. Advertisers warmed up to the offerings of Google and other search engines, and ever since, the growth of CPC advertising has continued unabated.

However, like the example of unconstrained capitalism referenced earlier, CPC advertising cannot maintain its growth in its current state. It contains within it factors that run counter to its promise of increased returns and the measurability of online advertising, which in turn will cause it to slow down, and in the long term give way to other pricing models.

In this white paper, we will examine the inherent dialectics of online advertising and look at the measures that our industry can take to prevent another race to the bottom.

Problems with CPC Campaigns

1. Higher cost of keywords

Portland-based software company Jama relied heavily on Google for its customer acquisition. However, acquiring customers through search was proving to be an increasingly expensive proposition.

"The average cost-per-click was getting more expensive. In some cases certain words were up to \$5 to \$10 a click, and our average cost-per-lead was exceeding \$100," said John Simpson, Director of Customer Outreach and Marketing. "We were doing optimization techniques -- changing the copy on our site, changing the words we bought -- and it was helping, but only a little."

Frustrated with the inability of search engine marketing to generate qualified leads in a cost-effective manner, Jama allocated its search marketing budget towards charitable contributions to see if the resulting publicity could generate as much business.

Jama is not alone.

In large part due to a sizeable universe of advertisers competing over a limited pool of keywords, the cost of keywords is rising sharply. A 2007 Doubleclick Performics Search Trends Report shows that there were nearly six times as many keywords with a cost-per-click (CPC) of more than \$1 in January of 2007 than the prior year. The cost-per-keyword increased by 33% and the cost-per-click rose by as much as 55%.

Often the increase in keyword costs is driven not only by increased competition among companies, but also between a company and its retailers. The corporate entity deploys a search campaign for branding. Retailers bid

on the same keywords to drive sales. The net result is a steep increase in the cost-per-keyword, as companies and retailers engage in bidding wars to sell in the end, the same product. The rising cost of keywords is making it increasingly difficult for advertisers to increase ROI solely through CPC advertising.

2. Increasing click-fraud rate

In the third quarter of 2008, the Click Fraud report maintained by Click Forensics showed a 16% industry click fraud rate. The report said that average click fraud rate of PPC advertisements appearing on search engine content networks (e.g. Google AdSense and Yahoo! Publisher Network) was as high as 27.1%.

Botnets were the primary factors driving the increased click-fraud rate.

"Although click fraud rates were relatively unchanged in the second quarter, we found that the methods used to commit click fraud have become increasingly more sophisticated and difficult to detect," Tom Cuthbert, President, Click Forensics said in the report.

By rewarding clicks (as opposed to actual sign-ups), less than scrupulous individuals have an incentive to indulge in click-fraud.

Even though a report issued by Google suggests that the click-fraud rates on its search network (which accounts for a large share of CPC advertising) is as low as 2%, the Click Forensics report suggests that with more sophisticated bot technologies, click fraud will remain a pain point for marketers using CPC.

3. Lack of transparency

Search engines commonly deploy algorithms to determine the cost-per-click and the position of the advertisements. Yahoo!, Ask.com and Google (Quality Score) each have their own algorithms to determine the amount marketers will have to pay for a given advertisement.

The problem is that there is little to no transparency in these algorithms. It is difficult for marketers to determine how landing page quality, the quality of the ad copy and variations on the bid price work together to determine the exact position and price of the search advertisement.

To give just one example, the Google Adwords Help section says that the Quality Score depends on a variety of factors:

- The historical click-through rate (CTR) of the keyword and the matched ad on Google; note that CTR on the Google Network only ever impacts Quality Score on the Google Network—not on Google.
 - Your account history, which is measured by the CTR of all the ads and keywords in your account.
 - The historical CTR of the display URLs in the ad group.
 - The quality of your landing page.
 - The relevance of the keyword to the ads in its ad group.
 - The relevance of the keyword and the matched ad to the search query.
 - Your account's performance in the geographical region where the ad will be shown.
- Other unspecified relevance factors.

The ambiguity in the criteria makes it difficult for the marketer to optimize campaigns accurately and garner maximum return on investment.

And as if that's not enough, there is yet another element to the lack of transparency.

Many times, it is difficult for the online marketer to know exactly where the click is coming from. Search networks often encompass a large number of sites beyond the primary entity, while "content network" advertisers often have to contend with less than desirable placements.

4. Difficult to tie-in campaign and business metrics

Metrics such as clicks, click-through rates and cost-per-clicks are far removed from actual business metrics like acquisitions and sales. As a result, many marketers are unable to correlate the two, and cannot optimize campaigns in an effective manner to help drive business revenue.

According to the "2007 Marketing ROI and Measurements Study" from Lenskold Group and Marketing Profs, only 9% of marketers say their ability to measure the financial returns across all forms of marketing is "as good as it needs to be." That percentage actually declined from 2006, when it was 16%.

A McKinsey Report "How Poor Metrics Undermine Digital Marketing" written after a survey of 340 senior executives around the country sums it up aptly: hobbled by nascent technologies, inconsistent metrics, and a reliance on outdated media models, marketers are failing to tap the digital world's full power.

As can be seen above, CPC campaigns fall short when it comes to helping marketers tie in front-end campaign metrics to business results, which is especially important during a recession.

Similar to the problems of unconstrained capitalism as described by Marx, the issues with CPC advertising are powerful forces that can prevent it from realizing its promise, and in fact might contribute to its downfall.

We are already beginning to see these issues impact CPC advertising. To quote from an article in The Wall Street Journal, "Gap Widens in Online Advertising":

"There are signs that search may eventually take a hit.... John Aiken, Managing Director of research firm Majestic Research, says some smaller businesses have begun cutting back the number of keywords they are buying in recent months... He says Google is "potentially stretching for dollars," noting that it has begun displaying more ads for some keywords."

New solutions for new economic times

With its ability to deliver broad reach and an engaged stream of users at a higher ROI than CPM display banners, search advertising will continue to remain an important component of online media plans.

However, as can be seen above, there are problems with CPC campaigns when it comes to addressing marketer needs. The fundamental root of these problems is that pricing mechanisms for CPC campaigns charges advertisers for clicks – and not for actual sign-ups. By removing the emphasis on the click, we will begin to arrive at a more comprehensive solution and prevent so to speak, the demise of online advertising.

Cost-per-Lead (CPL) advertising enables marketers to pay only for qualified leads. Clicks and impressions are irrelevant in CPL campaigns. By migrating to CPL pricing models, advertisers will be able to move beyond the click to a metric that is a hard ROI-driver.

This is not without precedent. Marketers shifted from CPM advertising toward CPC pricing models during the 2000 – 2002 recession. During the current economic downturn, they need to continue that progression, and move even higher up the ROI ladder.

Imran Khan, Managing Partner, JP Morgan says, "The Internet is more and more a performance driven model!" Daniel Taylor, a senior analyst in Yankee Group's Consumer Research group sums it up: "CPC advertising is a placeholder for CPL advertising."

CPL campaigns complement CPC campaigns in important ways:

1. Higher returns

CPL advertising allows marketers to pay only for qualified leads rather than for clicks. Advertisers can build a pipeline of responsive leads that have expressed explicit interest in the advertiser offer. These leads can be remarketed to over a period of time.

Dunhill Vacations has been deploying CPL campaigns for the last two years to grow their newsletter. With over one million subscribers, Dunhill vacations has been ranked by Hitwise as among the top 25 fastest growing properties on the Internet.

Dunhill Vacation News, their travel newsletter, has a diverse client base of advertisers such as Royal Caribbean Cruise Lines, Costa Cruise Lines, Jet Blue, Apple Vacations, Marriott Hotels and Fairmont Resorts. Dunhill Vacations continually needs to find subscribers that fit the diversity of their travel clients and what they are promoting.

"CPL does a far better job than CPM or CPC when it comes to increasing ROI. It's the most efficient way to acquire leads today," said Kurt Homfelt, CEO, Dunhill Vacations. "Leads from CPL campaigns have vastly outperformed any CPM and CPC campaigns that we have tested. Our open rates have increased by more than 30% in the past nine months due to our CPL initiatives. Our engagement level (CTR'S) within our subscriber base has increased by more than 35% as well."

And it gets better. Because Cost-per-Lead models don't force advertisers to pay for clicks, there is no incentive for racketeers to indulge in click-fraud.

There is also little risk of paying for fraudulent sign-ups.

"Our system automatically validates leads for email domain names, zip codes and geographic IP addresses," says Zephirin Lasker, CEO and Co-founder, Pontiflex, the industry's first open and transparent CPL market. "What's more, our clients do not have to pay for duplicate leads. We compare leads acquired from the campaign with those in the in-house database and eliminate duplicates."

2. Transparency

Until recently, there was a lack of transparency in the online lead generation market, a failing that prevented advertisers from generating leads for their brand efficiently.

It's important to make a distinction here.

The market for sales leads – leads that are generated on the basis of demographic criteria and sold to multiple advertisers – is fairly mature.

However, a large portion of online advertising is deployed to generate brand specific marketing leads. For example, brand marketers at companies like Coca-Cola and Southwest Airlines looking to sign-up people for their newsletters or member loyalty programs have no use for generic sales leads. They want leads that have signed up specifically for their offers.

Brand marketers also want to maintain control of their brand by controlling their media placements. The lack of transparency and control over campaign placement has been a long standing problem in the lead generation industry. Traditionally, advertisers have had little or no insight into where their lead generation campaigns are actually running. Due to the lack of visibility into campaign placements, online marketers have not been able to ensure quality or optimize campaigns to meet their goals.

But in a manner that would make Adam Smith proud, the market has responded to the advertiser demand for increased returns. Transparency is now a reality in the online lead generation market.

Marketers can now leverage CPL pricing models to generate marketing leads by insisting on complete transparency from the very beginning of the planning process. Open and transparent CPL marketplaces like Pontiflex enable advertisers to plan their CPL campaigns just as they would a TV, print or online banner campaign. Utilizing transparent online lead generation, advertisers can:

- Select publisher venues based on campaign goals. This is critical because some publishers will do a better job at generating leads for direct mail lists, while others will have a high composition of people that participate actively on community sites.
- Determine the contextual relevance of the publisher with their brand and offer.
- Obtain relevant metrics for each publisher: marketers can access information such as monthly impressions, average CPL, average lead volume/day and other figures to help them plan and allocate their online budgets.

CPL advertising offers advertisers complete transparency into the factors that affect their campaign ROI. Unlike CPC campaigns, there's no Quality Score "black-box" inhibiting advertiser visibility into campaign criteria that influence ROI.

3. Easily tie in marketing metrics to business results

With metrics like impressions and click-through rates, banner and search campaigns can be far removed from hard business results like registrants, acquisitions and sales. On the other hand, metrics such as the number of leads and Cost-per-Lead metrics directly tie in to these all-important business metrics.

Marketers not only want to drive revenue, they want to be able to easily prove how their marketing results actually help drive business.

With CPL advertising, they don't have to calculate acquisition costs using complex tracking methodologies. In CPL campaigns, marketers pay only for acquisitions. They can exactly calculate the returns on their marketing dollars before the campaign, which is especially comforting in a tough economy.

Due to its ability to provide guaranteed returns on marketing dollars, CPL pricing models have great appeal to business executives who are laser focused on the company bottomline. It's no wonder that a recent IBM research study found that two-thirds of senior marketers expect 20 percent of ad revenue to move away from impression-based sales, in favor of action-based models within three years.

Conclusion

In tough economic times, marketers tend to favor advertising vehicles that deliver a higher return on investment. The last economic downturn from 2000 – 2002 saw a sharp growth in Cost-per-Click advertising, which allowed marketers to pay only for clicks as opposed to wasted impressions.

Since 2002, CPC campaigns have grown and are projected to exceed over 40% of the advertising spend. However with the rising cost of keywords, increasing click-fraud rate, lack of transparency and the gap between campaign metrics and business results, marketers are increasingly finding it difficult to increase marketing ROI with CPC campaigns.

Transparent CPL advertising enables advertisers to solve the problems faced in CPC campaigns by paying only for qualified leads. It allows advertisers to increase returns on marketing dollars and enables the promise of online advertising.

Through open and transparent CPL advertising, online marketers can buy leads in a cost-effective way. They can buy marketing leads – leads that are unique to their brands and never resold. They can then use these leads to drive engagement and revenue by building responsive online communities such as brand sites, member reward programs, and newsletters. By choosing open and transparent lead providers, they can directly tie business revenue to campaign performance. By paying only for leads, they can produce guaranteed returns on online advertising.

While CPC campaigns deliver broad reach and will continue to be an integral part of online marketing plans, advertisers will have to allocate a portion of their marketing budgets to transparent CPL advertising in order to increase returns on their marketing investment, and prevent the demise of online advertising.

About Pontiflex

Pontiflex offers advertisers a single point of connection to the entire performance advertising market. Through Pontiflex, advertisers can run ads on websites, social networks and mobile apps, and connect to the right people no matter where they are. Pontiflex enables advertisers to run ads on a Cost-per-Lead (CPL) pricing model. Advertisers pay only for people that have signed up for their advertisements, and not for wasted clicks or impressions.