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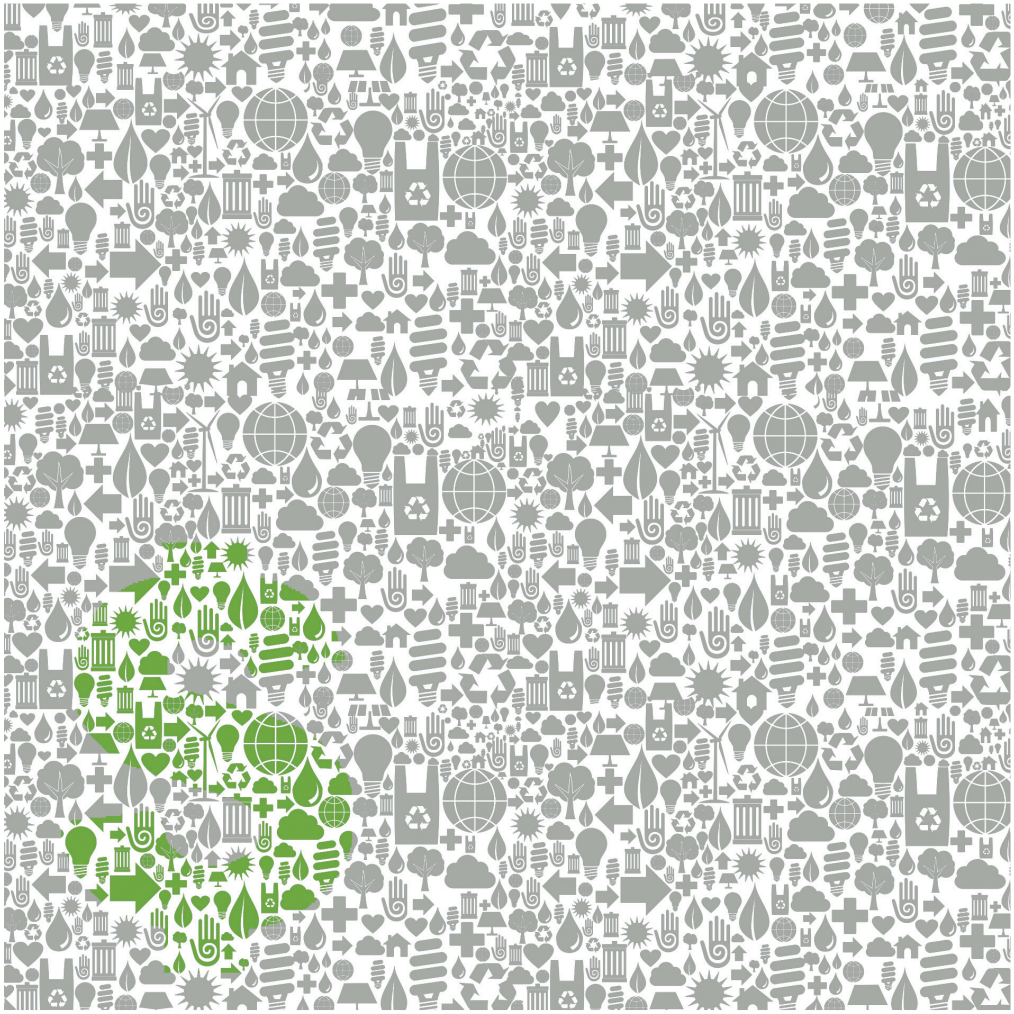
INSIGHTS



Native Advertising

With Great Power Comes Great Responsibility

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1. INTRODUCTION

Digital advertising takes many forms and digital publishers are continually testing the tension between providing a good user experience versus maximizing monetization. While banner ads (those rectangular ads commonly seen along the sides or top of a website) are considered the industry standard for online advertising, it is widely acknowledged that they have become ineffective. Decades of irrelevant targeting and misleading tactics have resulted in users training themselves to ignore or avoid banners altogether. The average person is served over 1,700 banner ads per month (*comScore*), but how many of us can recall even a single one? As a result of "banner blindness," click-through-rates ("CTRs," a sign of ad effectiveness) for these ad units are an abysmally low 0.1% (*DG MediaMind*). In fact, a person is more likely to survive a plane crash than click on a banner ad (*Solve Media*).

Enter "native advertising," a rapidly growing approach to advertising that embeds ads or marketing messages directly into the content flow or user experience. Native advertising formats range from sponsored articles that mimic editorial content on a news website to "in-feed" ads that users see as they are scrolling through their social network feeds (**see figure 1.1.**). It is no surprise that consumers are more likely to see and engage with advertising if they physically can't avoid it, and mobile native ad units generate CTRs that are more than 6 times that of regular mobile banner ads (*Celtra, Opera*). Due to their effectiveness, native ads have quickly become a part of the offering of almost every media outlet, including leading franchises like the New York Times, the Atlantic, and Time, Inc. Advertisers have also been eager to leverage the format, driving native advertising spend to $7.9 billion in 2014 (*BI Intelligence*). However, some of these implementations have caused concern (even anger), particularly among journalists who worry that the blurred lines between editorial content and advertising will erode consumer trust in journalistic integrity.

AGC believes that native advertising formats can be powerful delivery mechanisms for digital advertising and are inherently benign but when paired up with compelling and relevant ad content, could ultimately enhance the user experience and drive greater revenue for publishers. While challenges certainly exist, industry participants will, by necessity if not moral guidance, eventually figure out ways to maintain high integrity and quality while effectively delivering marketing messages. In pursuit of this tremendous opportunity, dozens of native advertising companies have emerged, ranging from content creation and advertiser platforms to publisher widgets and tools companies. These native advertising businesses are growing rapidly, fueled by a large expanding market and over $300 million in venture capital (*Content Marketing Institute*) in just the last two years. This report examines some of the key players, trends and challenges within the native advertising industry.

1.1. Examples of Native Advertising Formats

In-Feed Ads

- Ads delivered into a publisher's normal content well
- Written by or in partnership with the publisher's team to match the surrounding stories

Recommendation Widgets

- Ad/paid link delivered via a widget
- Integrated into main content well
- Does not mimic the appearance of editorial content feed

Paid Search Listings

- Commonly found above the organic search results
- Looks like the surrounding results (with the exception of disclosure aspects)

IAB Standard with Native Elements

- IAB standard units containing contextually relevant content
- Standard placement and appearance

Promoted Listings

- Found on sites that do not have a traditional editorial content well
- Designed to blend into the browsing experience and presented to look identical to the existing offering

Custom Integrations

- Customized implementations that do not neatly fit into the above categories
- Tailored to each site/service

Source: IAB

2. NATIVE ADVERTISING LANDSCAPE

Companies across the native advertising ecosystem generally fall into 3 categories:

- **Digital Publishers / Services Companies** with strong in-house native advertising capabilities that enable them to create and deliver native advertising into their own properties.
- **3rd Party Native Ad Platforms** that provide ad network, exchange, targeting, mediation and/or management for digital publishers and app companies.
- **Native Ad Content Creation** services that help brands, agencies, and publishers create content that is customized and relevant to an ad unit or platform. (Note: We intentionally leave out digital agencies so as to focus more on technology rather than services companies.)

2.1. Native Advertising Representative Companies

Native Focused Digital Publishers / Services

Aol., bing, BuzzFeed, DISQUS, Expedia, facebook, FANCY, Flipboard, foursquare, Google, LinkedIn, Pinterest, priceline.com, snapchat, StumbleUpon, tripadvisor, tumblr., twitter, WANELO, weVIT, YAHOO!, yelp

3rd Party Native Ad Platforms

Adaptly, ADSNATIVE, ampush, appsfire, brandnetworks, Chartboost, DistroScale, Fyber, Gravity, gumgum, KARGO, kiip, namomedia, nativeX, NATIVO, one spot, OpenX, outbrain, polar, sharethrough, simplereach, SHIFT, SOCIAL CODE, SOCIALFLOW, Spredfast, supersonic, Taboola, Tapjoy, triplelift, Vungle, YieldMo, Zemanta, ZergNet, ZUMOBI

Native Ad Content Creation / Management

Contently, curata, kapost, livefyre, NewsCred, Percolate, persado, RebelMouse, Scripted, Skyword, visual.ly, zmags

Sources: Company Websites, Crunchbase, CapitalIQ

3. THE APPEAL OF NATIVE ADVERTISING

According to the IAB, native advertising encompasses "paid ads that are so cohesive with the page content, assimilated into the design, and consistent with the platform behavior that the viewer simply feels that they belong." The idea is not all that new as sponsored articles in print publications and infomercials on TV are forms of native advertising that have existed for more than a half a century. Even within digital advertising, search companies like Google, Bing and Yahoo have been showing sponsored search results (a form of native advertising) for over a decade. The more recent innovation within native advertising is in its application within digital publishing and across social networks.

It is widely acknowledged that traditional banner ads are not very effective. "Traditional digital advertising has become wallpaper. It doesn't improve anyone's experience on a site and readers, myself included, pretty much look past it," says GE's Global Head, Media Strategy, Jason Hill. Poor display ad performance has resulted in declining CPMs, driving publishers to continually search for new and better ways to increase ad revenue. Many publishers are turning to content marketing as a more effective way to connect audiences with the marketing messages of advertisers. Content marketing, the practice of delivering an advertising message in the form of a piece of quality content, resonates with digital audiences, 70% of which say they would prefer to learn about products through content versus through traditional advertisements. The challenge with content marketing has always been the ability to achieve scale with a bespoke solution.

Native advertising is a natural delivery tool for content marketing and one that has the potential to generate significant scale. By delivering advertisements that are content rich and in the same format as the content audiences are looking to consume, marketers hope to provide a much more seamless advertising experience. Some native ad formats are deliberately integrated into the article or content with which the consumer is engaged, and may be contextually relevant as well. This tactic has led to higher engagement rates (benefiting advertisers), thereby allowing sites to charge higher CPMs (benefiting publishers). Also, native in-feed ads have proven to be an effective ad format for mobile devices where the small screen size and user experience make it difficult for traditional banner ads. As a result, native advertising has become an important tool in the kit of publishers and marketers with 75% of publishers currently running some form of native ads, according to Wenda Millard, President and COO of MediaLink.

3.1. Native Advertising Advantages for Publishers and Advertisers

Category	Advantages
Strong Engagement	▪ Integrated into the user experience and hard to avoid. ▪ Consumers looked at native ads 52% more frequently than display ads.[1] ▪ 18% higher lift in purchase intent and 9% lift for brand affinity responses than banner ads.[1]
Greater Potential for Virality	▪ Sharing functionality built into many native ad formats. ▪ Higher production value content marketing more likely to be shared. ▪ 32% of users willing to share a native ad versus just 19% for display ads.[1]
More Effective on Mobile	▪ Better format for small screens and content consumed via feeds. ▪ >1% CTRs for native mobile ads vs 0.15% CTRs for native display ads.[2]
Better User Experience	▪ Potentially less disruptive to the user experience. ▪ Heavy content marketing presence within native advertising provides a more informative ad experience for consumers.

Source: 1) Sharethrough/IPG Media Lab study. 2) Polar Media Group, Celtra

4. NATIVE ADVERTISING HEADWINDS

Native advertising is rapidly becoming a widely-adopted distribution mechanism for advertising and a valuable monetization vehicle for publishers. However, the success of the various native advertising implementations will ultimately depend on the respect that they have for the associated content and the user experience. Native advertising that is natural to the user experience, contextually relevant, entertaining and/or informative can improve consumer perception of both the publisher and the brand. Sadly, as with banner advertising, quality ideals are hard to maintain in the face of declining profits. As a result, consumers are sometimes bombarded with senseless native ads claiming things like “Top 10 VCs” and “Top 15 Entrepreneurs.” Perhaps more concerning are carnival style rope-a-dope ads that leverage shocking images or sensational headlines in an attempt to “click-bait” the user. These ads can generate a lot of clicks but not the best impression for a brand to make upon a consumer. Furthermore, as consumers get inundated with a greater number of native ads, will those ads become the new “normal” and be ignored the way banners are?

Popular perception also matters, and that perception is particularly skeptical regarding native advertising that is presented within reputable news outlets. Columnist Bob Garfield, a former Ad Age Editor-at-Large, compares publishers selling native advertising to an island that mined guano-catalyzed minerals until depletion. "With every transaction," he said, "publishers are mining and exporting a rare resource: trust. Those deals will not save the media industry. They will, in a matter of years, destroy the media industry: one boatload of shit at a time." In a now famous rant on his show “Last Week Tonight,” host John Oliver argues in a scathing rebuke that native advertising is destroying the separation between “church and state” in the media (link). Transparency is both a brand and publisher imperative. Advertising that is not transparent erodes consumer trust, and ultimately is a poor ROI for advertisers.

4.1. Common Concerns/Criticisms of Native Advertising

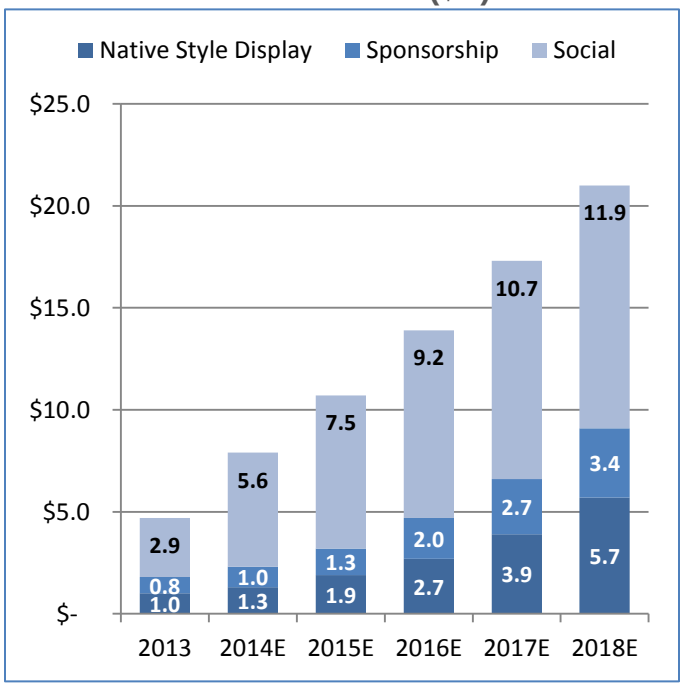
Category	Concerns/Criticisms
Editorial Integrity	▪ Potential to erode editorial independence by confusing the line between content and advertising.
Quality Issues	▪ Publishers may overlook ad quality in exchange for greater incremental revenue. ▪ Irrelevant/misleading native ads may turn consumers off, driving down effectiveness.
Scalability	▪ Multitude of formats creates scalability and pricing challenges. ▪ Some native ad types inherently counter to standardization and therefor hard to scale.
Regulation	▪ In December 2013, the FTC hosted workshop to discuss the impact of native ads – declaring that some native ads were unlawful. ▪ Self-regulation within the industry will be critical to avoid federal intervention.
Overexposure	▪ Consumers may gain “banner blindness” towards native ads as they become more commonplace and less novel.
Measurement Issues	▪ No standardized process for measurement - should native ads be measured with branding metrics or performance metrics?

Source: AGC Partners

The central issue seems to be whether native advertising can be done responsibly. Bob Liodice, president and CEO of the ANA, summed it up well when he said “Native advertising is proving to be a win for marketers, consumers, and publishers. However, consumers must be able to tell the difference between native advertising and editorial. As such proper disclosure is mandatory. Marketers have a responsibility to be transparent to maintain trust, and they must play a lead role in working with publishers to ensure proper disclosure.”

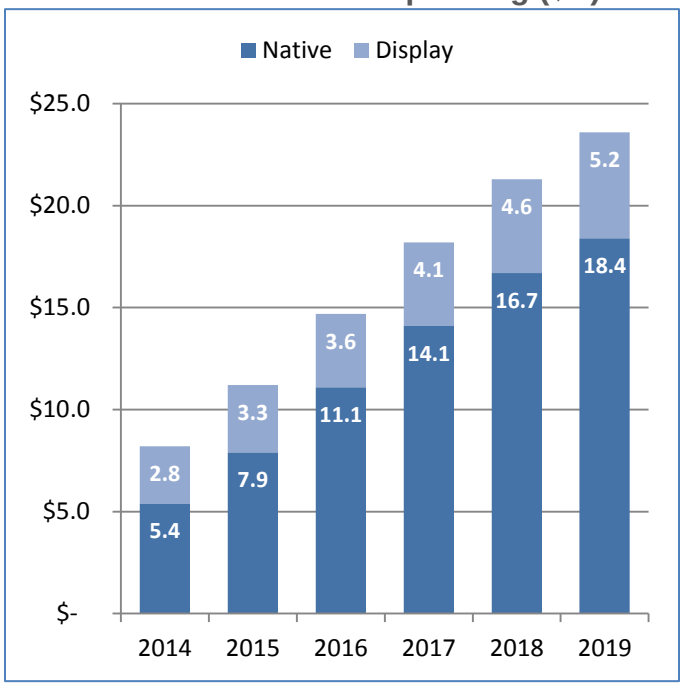
5. MARKET SIZE AND TRENDS

5.1. U.S. Native Ad Revenue ($B)



Source: BI Intelligence, IAB

5.2. U.S. Social Media Ad Spending ($B)



Source: BIA/Kelsey, eMarketer

NATIVE ADVERTISING TRENDS

Marketers are bullish on native advertising and ad dollars continue to flow into these ad formats. Executives from top brands including Ford, Kimberly-Clark, General Electric, and Hewlett Packard plan to boost native advertising spend in the next year or more (*eMarketer*). An estimated 63% of marketers say they'll be spending more on native advertising this year (*Association of National Advertisers*). Enthusiasm around the format is expected to drive total U.S. Native Ad Revenue from an estimated $7.9 billion in 2014 to $21.0 billion in 2018 (**see figure 5.1.**).

Native advertising across social networks will continue to account for the lion's share of native ad dollars (**see figure 5.2.**). Services like Facebook, Twitter and LinkedIn have made native ads the foundation of their monetization. Combining massive audiences with targeted native ads has been a recipe for success for these companies. Facebook, perhaps the largest native ad company in the world, generated $11.5 billion in advertising revenue in 2014, the majority of which is from native formats (in-feed on desktop, in-stream on mobile).

Other digital media giants are following suit. Yahoo's Stream Ads, which appear within the content well of Yahoo properties and closely mirror the editorial content on those sites, have been a big hit with advertisers. Launched in 2013, Stream Ads already account for approximately 40% of the display ads that Yahoo runs. Gemini, Yahoo's ad-buying marketplace, allows advertisers to programmatically purchase native ads across its properties. Yahoo also recently launched a content recommendation system (similar to Taboola or Outbrain) that includes additional publisher content as well as sponsored content from Yahoo's advertisers. AOL runs its own native ad units across its mobile properties such as Huffington Post, TechCrunch and Engadget, and recently purchased content recommendation platform Gravity in 2014 to extend its native ad capabilities to 3rd party publishers.

6. CAPITAL MARKETS ACTIVITY

Despite the rapid growth in native advertising, it remains a relatively nascent market. Large public companies like Facebook, Twitter, Yahoo and AOL are investing heavily in building products to drive native advertising across their own offerings as well as that of third parties. Meanwhile, venture capitalists are funding a new crop of consumer services (Snapchat, Pinterest, Buzzfeed) and technology providers (Taboola, Outbrain, Spredfast) that are native advertising focused. Technology providers, in particular, will require greater amounts of capital as they achieve escape velocity due to growing demand from publishers and agencies without internal native advertising capabilities.

6.1. Native Advertising Financings, Sorted by Size of Most Recent Round

Company Name	Most Recent Raise	Amount ($M)	Round	Investors	Total Invested Capital ($M)
1. SnapChat	Dec-14	485	D	August Capital; KPCB; 2 Others	648
2. Pinterest	May-14	200	F	Andreesen Horowitz; Bessemer Venture Partners; 4 Others	763
3. Taboola	Feb-15	117	E	Fidelity Management; Marker; 5 Others	157
4. Tumblr (Yahoo!)	Sep-11	85	E	Insight Venture Partners; Spark Capital; 6 Others	125
5. brandnetworks	Jun-13	68	ND	AEA Investors	68
6. Buzzfeed	Aug-14	50	E	NEA; SoftBank; RRE Ventures; 3 Others	96
7. Flipboard	Dec-13	50	C	GGV; KPCB; Goldman Sachs; 3 Others	161
8. Outbrain	Oct-13	35	E	LSVP; HarbourVest; Carmel Ventures; 5 Others	99
9. LiveFyre	Feb-15	32	D	USVP; Hillsven Capital; Greycroft Partners; 3 Others	67
10. TapJoy	Jul-11	30	D	JPMorgan	71
11. NewsCred	Jan-14	25	C	InterWest Partners; FirstMark Capital; IA Ventures	47
12. Spredfast	Jan-14	24	E	Silver Lake Waterman	88
13. Percolate	Mar-14	24	B	WPP; GGV Capital; Sequoia Capital; 2 Others	35
14. Persado	Jan-15	21	B	BCV; AMEX Ventures; Citi Ventures	36
15. Fancy	Feb-15	20	D	CCC; Carlos Slim Domit	124
16. Chartboost	Jan-13	19	B	Translink Capital; Sequoia Capital; SK Telecom Ventures	21
17. StumbleUpon	Mar-11	17	B	DAG Ventures; Accel Partners; 4 Others	19
18. Vungle	Feb-14	17	B	Google Ventures; Crosslink Capital; Aol Ventures; 3 Others	26
19. Foursquare	Feb-14	15	D	Microsoft	162
20. Supersonic	Jul-14	15	B	Greylock Partners; SAIF Partners	23
21. Zumobi	May-07	12	A	Oak Investment Partners; Hunt Ventures	12
22. Adaptly	May-12	11	B	Valhalla Partners; Time Warner Investments; Social Starts	13
23. Gravity (AOL)	Oct-12	11	B	Upfront Ventures; August Capital; Redpoint Ventures	21
24. Skyword	Sep-14	11	ND	Cox Media Group	26
25. Disqus	May-11	10	B	Union Square Ventures; North Bridge Growth Equity	11
26. Sharethrough	Sep-14	10	D	North Bridge Growth Equity; Silver Creek; 3 Others	38
27. YieldMo	Oct-14	10	C	Google Ventures; Time Warner Investments; 3 Others	22
28. RebelMouse	Aug-13	10	A	Oak Investment Partners; SoftBank Capital	13
29. Scripted	Nov-14	9	B	Redpoint Ventures; Crosslink Capital; Storm Ventures	15
30. Contently	Jan-14	9	B	Lightbank; Sigma West; Countour Venture Partners	12

Source: CrunchBase, CapitalIQ

7. M&A ACTIVITY IN NATIVE ADVERTISING

Given the early stage of the native advertising market, M&A activity has been fairly modest. The bulk of the transactions have centered around large digital media companies, digital publishers and ad tech businesses making tactical acquisitions to fill key capability gaps and accelerate time to market (i.e. Twitter's acquisition of Namo Media). As a result, 3rd party native ad platforms have been the primary area of focus for acquirors. As more of the leaders in that category achieve scale and success, transaction volume and valuations should accelerate as those companies become acquirors themselves and/or targets for some of the large technology buyers playing catch-up in this rapidly growing market.

7.1. Native Advertising Acquisitions

	Date	Target	Acquirer	EV ($M)	Category
1.	02/19/15	Zeega	Buzzfeed	ND	3rd Party Platform
2.	02/12/15	Streak Media	Fluent	ND	Publisher / Service
3.	02/11/15	Niche	Twitter	ND	3rd Party Platform
4.	02/10/15	Appsfire	Mobile Network Group	30	3rd Party Platform
5.	01/29/15	Ebyline	IZEA Holdings	ND	Content Creation
6.	01/21/15	Kosei	Pinterest	ND	3rd Party Platform
7.	01/06/15	Selectable Media	Meredith	23	3rd Party Platform
8.	12/10/14	Plethora Mobile	Publisher's Clearing House Digital	ND	3rd Party Platform
9.	10/28/14	MobFox	Matomy Media Group	18	3rd Party Platform
10.	09/29/14	Tagroom	Moko Social Media	ND	3rd Party Platform
11.	09/29/14	Video Natives	Adyoulike	ND	3rd Party Platform
12.	09/08/14	Vidaao	Skyword	ND	Content Creation
13.	09/03/14	Luminate	Yahoo!	ND	Content Creation
14.	08/04/14	Perfect Market	Taboola	ND	3rd Party Platform
15.	07/24/14	Viator	TripAdvisor	200	Publisher / Service
16.	07/21/14	Flurry	Yahoo!	270	3rd Party Platform
17.	07/09/14	Clear Content Marketing	Skyword	ND	Content Creation
18.	06/22/14	Bizo	LinkedIn	175	3rd Party Platform
19.	06/19/14	Snappy	Twitter	ND	3rd Party Platform
20.	06/10/14	Adconion Direct NA and AU	SingTel	235	3rd Party Platform
21.	06/10/14	Kontera	SingTel	150	Content Creation
22.	06/04/14	Namo Media	Twitter	ND	3rd Party Platform
23.	06/04/14	Fyber	RNTS Media	190	3rd Party Platform
24.	05/08/14	AppHome	appnext	3	Content Creation
25.	04/21/14	HowStuffWorks.com	Blucora	45	Publisher / Service
26.	03/18/14	SavvyMom Media	Ideon Mobile	ND	Publisher / Service
27.	03/18/14	UrbanMoms	Ideon Mobile	ND	Publisher / Service
28.	01/23/14	Gravity	AOL	91	3rd Party Platform
29.	01/22/14	Zmags	The Gores Group	ND	Content Creation
30.	01/07/14	Plista	GroupM	ND	3rd Party Platform
31.	10/10/13	Hubbl	Airpush	ND	3rd Party Platform
32.	10/08/13	Visual Revenue	outbrain	ND	3rd Party Platform
33.	09/09/13	MoPub	Twitter	350	3rd Party Platform
34.	07/18/13	Thoughtleadr	Chaotic Moon Studios	ND	3rd Party Platform
35.	06/30/13	TapCommerce	Twitter	ND	3rd Party Platform
36.	06/20/13	Tumblr	Yahoo!	1,100	Publisher / Service
37.	01/03/13	Punchfork	Pinterest	ND	Publisher / Service
38.	08/10/12	Blinq	Facebook	ND	Content Creation
39.	08/04/10	mSpoke	LinkedIn	1	3rd Party Platform

Sources: 451 Research, CapitalIQ

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***** *Indicates deals completed by Linda Gridley while at Gridley & Company,* **+** *Indicates deals completed by Gee Leung at Mesa Global*