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AOL - Q2 2013 AOL Inc. Earnings Conference Call

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OVERVIEW:

AOL reported 2Q13 YoverY consolidated revenue growth of 2%.

CORPORATE PARTICIPANTS

Eoin Ryan *AOL Inc - SVP of IR*

Tim Armstrong *AOL Inc - Chairman & CEO*

Karen Dykstra *AOL Inc - CFO*

CONFERENCE CALL PARTICIPANTS

Brian Pitz *Jefferies & Company - Analyst*

Ross Sandler *Deutsche Bank - Analyst*

Peter Stabler *Wells Fargo Securities, LLC - Analyst*

Ron Josey *JMP Securities - Analyst*

Mark Mahaney *RBC Capital Markets - Analyst*

Laura Martin *Needham & Company - Analyst*

James Cakmak *Telsey Advisory Group - Analyst*

Mark May *Citigroup - Analyst*

John Blackledge *Cowen and Company - Analyst*

Benjamin Schachter *Macquarie Research - Analyst*

Eric Sheridan *UBS - Analyst*

Youssef Squali *Cantor Fitzgerald - Analyst*

PRESENTATION

Operator

Good day ladies and gentlemen, and welcome to AOL's second quarter 2013 earnings conference call. My name is Laura and I will be your coordinator for today. At this time, all participants are in a listen-only mode and later we will facilitate a question-and-answer session. As a reminder, this conference is being recorded for replay purposes. I'd like to turn the conference over to Mr. Eoin Ryan, Senior Vice President of Investor Relations. Please proceed, Sir.

Eoin Ryan *- AOL Inc - SVP of IR*

Good morning. Thanks, Laura, and everyone for joining us for our second quarter 2013 earnings call. You can find our Q2 earnings press release and accompanying slides and trending schedules on our Investor Relations website. On the call with me today is our Chairman and CEO, Tim Armstrong, and our Chief Financial Officer, Karen Dykstra. We will makes some brief remarks on the quarter and our overall strategy and then we will open up the lines for Q&A.

But first I will remind you that during this call, we may discuss our outlook for future financial and operating performance, corporate strategy, marketing and product plans, technology improvements, cost initiatives, planned investments, as well as expectations for the economy and online advertising in general. These forward-looking statements typically are preceded by words such as we will, we expect, we believe, we anticipate or similar statements. These forward-looking statements are subject to risks and uncertainties and our actual results could differ materially from the views expressed today. Reported results should not be indicative of future performance. Some of these risks have been set in our annual report form 10-K for the year ended December 31, 2012 filed with the SEC. All information discussed in this call is as of today, August 7, and we do not intend and do not undertake any duty to update this information to reflect future events or circumstances.

We will also discuss certain non-GAAP financial measures, including adjusted OIBDA and free cash flow. I will refer you to the press release on the investors relations section of our website for all comparable GAAP measures and full reconciliations. Finally, from time to time, we post information about AOL on our Investor Relations website at IR.aol.com and on our official corporate blog at blog.aol.com. And with that, I will turn it over to Tim.

Tim Armstrong - *AOL Inc - Chairman & CEO*

Thanks Eoin, and thanks, everyone joining the call today. AOL is continuing to move forward today with another quarter of solid results and growth. The Company is healthier, leaner and more focused today than it was a year ago, and as you will hear on this call, we are staying on our well-worn path of the following activities. Number one, innovating and investing against a concise set of growth brands and platforms. Number two, actively allocating our resources and reducing our costs. And three, organically growing and acquiring passionate talent to build differentiated and valuable platforms.

Our strategy areas remain consistent during Q2, and I just wanted to review them quickly with you. First is content. Build, distribute and monetize leading content brands globally. Second, video. Produce, syndicate and monetize video brands, including live video. Third is advertising platforms. Build, distribute, and monetize programmatic and brand advertising platforms for agencies, advertisers and publishers. And lastly, commerce membership. Bundle, distribute, and monetize consumer subscription services.

We are also very excited to announce that we are taking a precise step forward on our growth path in the advertising technology and video area with our agreement to acquire Adap.TV, the best programmatic video platform on the Internet. Adap.TV is a company with meaningful revenue and above-industry-average growth, and most importantly, above-industry-average leadership and talent. AOL and Adap.TV share a deep and direct vision on video and advertising and a will to aggressively pursue what we believe to be a decade-long industry shift that will move tens of billions of dollars from TV advertising to IP-delivered video advertising. I believe Amir, the founder of Adap.TV and the founding team of Adap.TV plus the 200 employees at Adap.TV are the best people in the world at making this transition. Over the last three years, AOL has rapidly scaled our video footprint and revenue, and when the acquisition of Adap.TV closes, we will have more than doubled our video revenue and have a combined audience reach of 140 million un-duplicated video viewers in the US. And only second to Google in reach at a 167 million viewers.

With the acquisition, AOL secures a leadership position in two of the most important spaces on the Internet, video and programmatic advertising. I am confident that this is a very smart and well-targeted use of our capital. Programmatic advertising is a term widely discussed in our industry, and often mislabeled. I wanted to discuss what programmatic is, and why it is important to our industry and to AOL. So let me spend a few minutes describing what I believe it means for the industry in general and AOL specifically.

Programmatic advertising is the automation of the advertising business, and is a natural progression of software integrating with advertising. Programmatic advertising is not low-quality or low-price inventory. It is a software platform that allows advertisers and publishers to yield manage planning, serving, targeting and measurement of advertising campaigns. Pricing is a function of ROI, yield management and brand engagement, not a function of automation or programmatic. Premium inventory and formats will continue to receive premium pricing in a programmatic environment, particularly as inventory is increasingly programmatically traded on private exchanges or in exclusive environments.

The advance of programmatic advertising is creating two specialty areas within advertising. One is media sales, and one is enterprise system sales. AOL is actively involved in both areas of programmatic advertising, and we believe that this is a nontrivial advantage to our business, customers and partners. The Adap.TV acquisition strengthens AOL in both areas of programmatic in media and in enterprise advertising. AOL's broader advertising strategy includes not only programmatic but the aggregation of attractive audience segments and brand experiences. As you will see from our results, all areas of our advertising business grew in Q2 and we would expect Adap.TV to continue to open up more advertising opportunities and growth for AOL.

We have spoken publicly about the barbell strategy of our advertising business, which connects programmatic advertising on one side with deep marketing services on the other side, and connects in the middle with data and analytics. And for AOL, our results show that we have created that barbell and are successfully executing against it in the marketplace.

Digging into the Q2 results, we made progress across our strategic portfolio. In content, with the Huffington Post we have done what we said we would do. We have scaled traffic and revenue, scaled video, and we have scaled globally. Under Arianna's leadership and vision, the Huffington Post has become a global Media Brand at scale, and we ar very happy to be partnered in the investment behind Arianna and Jimmy Maymann and the team at Huffington Post.

The Huffington Post over the last two years has moved from a US news site to a global Media Brand operating in over eight countries, with roughly 40% of the users coming from outside the US. In Q2, the Huffington Post launched Huffington Post Japan, and our first foray into Africa was HuffPost Maghreb. Video has become a big part of the Huffington Post success story as well, and the site is doing over 100 million video views per month. Huffington Post Live as part of the Huffington Post is also gaining traction and attention. We now have had over 8,700 guests join us from more than 85 countries on Huffington Post Live. Users are spending an average of 22 minutes per visit, 5 times the industry average, and we have had over 1.1 million comments left on the Huff Post Live platform.

HuffPost Live launched a live channel in partnership with Clear Channel this quarter on the on the iHeart Radio platform, and Huffington Post Live has won numerous awards, including a Salute To Excellence award for the best interactive digital news story from the National Association of Black Journalists. A Webby award for best news and information channel, and a Golden Eagle Award for best original nonfiction documentary.

We launched the HuffPost Aspen Ideas Festival in partnership with Walter Isaacson and the Aspen Institute on the Huffington Post. And finally, Arianna has a new area of the Huffington Post called the Third Metric, which is being built to help global consumers live better and healthier lives. We have kicked off in New York with a very successful conference that Arianna hosted, and she followed it up with a conference in London. And if you were in London last week, you could not miss Arianna, the Huffington Post, or the Third Metric. And we believe that is going to be a very large growth area on the go forward basis for the Huffington Post.

In our tech brands, TechCrunch Disrupt we ran in New York, which was very successful. We had a 50% increase in the number of registrants, 30% increase in revenue. As part of that, the Disrupt Hackathon had1,400 registrants, a 33% increase in the number of attendees and an 80% increase in the number of apps or hacks presented at the Hackathon. TechCrunch will be expanding globally. Next up is TechCrunch Rome, TechCrunch Tokyo, and TechCrunch Bangalore. And ending the year with TechCrunch Moscow. All of those will be happening in the second half of the year.

In our lifestyle brands category, the StyleList sites remain number one in fashion, beauty and style in comScore for the sixth consecutive month. And we had the highest revenue ever in June. MAKERS, our very well-known women's leadership site and property, had 5 million video views on MAKERS, and net we are currently launching one new MAKER every single week.

In video, we had 2.2 content-only views in Q2, growing approximately 40% year-over-year. We grew the number of videos in our library by over 70% year-over-year. And we now have close to 700,000 high-quality videos in our library. AOL On continued to sign up premium content providers looking for AOL distribution and web wide distribution. Those partners included Entertainment Weekly, Fortune, CNN Money, People and InStyle. We introduced live video programming at aol.com, running three live programs during Q2 in addition to the live auditions, where we had 500 people seen on the front of aol.com over a two-day period. And we will be launching AOL Live as a full program and part of our Company during Q3. In connection with AOL Live, we also announced a global advertising partnership with Publicis. That is groundbreaking, to be the first global live advertising partnership and program currently being constructed. And we will launch simultaneously with AOL Live.

In our advertising platforms area, we grew both programmatic advertising and marketing services. We grew the number and the pricing of reserve impressions sold. We grew the number of advertisers we work with by approximately 20% year-over-year. We grew revenue from the Ad Age Top 100 year-over-year and quarter-over-quarter. We grew our agency revenue by double digits year-over-year, and also growing quarter-over-quarter. Search has now grown year-over-year each quarter for the past year, and continues to be a growth area for AOL.

On the AOL Networks area specifically, we have brought in Bob Lord to run our AOL Networks business and we couldn't be happier. Bob's official start date was August 1. I have known him for the last -- over the last decade, and I know he will be a game changer for us. Bob is a well-known leader in our industry who managed a Company the size of AOL. He's a very big asset for us to get at AOL.

On the programmatic products, we are ramping up very quickly. AOP, our programmatic solution for display for the demand side, has become a meaningful contributor in Q2, with significantly growing year-over-year. Also growing significantly quarter-over-quarter, and that was launched last August, so a year from today. We are scaling nicely at the agency trading desk and at the direct client level, and believe we are taking share in the programmatic display space. Our SSP marketplace, which is the programmatic side of the publisher side of the business, is nascent. It was launched in Q2, but is truly growing rapidly quarter-over-quarter. And we signed up a tremendous amount of publishers for that product. We believe we are in a position to have a very exciting future with a marketplace product on the supply side.

Premium formats also continues to scale. Devil impressions grew year-over-year 30%. There are 55 Devil campaigns running today from 36 different advertisers. The Devil network revenue grew double digits year-over-year, and now we are reaching 180 million monthly users in the US with the Devil network.

In mobile, we are making meaningful progress on revenue. But more importantly, we have made progress on our mobile typing, and that should accelerate mobile revenue further. In Q2, we launched a unified mobile platform for common serving and SDKs for mobile apps. This allows us to monetize O&O and third-party Ad.com publishers' mobile inventory as well as our AdTech publishers.

In the commerce membership business, our team successfully brought churn down to a multi-year low of 1.4%, while ARPU grew year-over-year and that team continues to do a tremendous job. On our membership to commerce team is also testing and working on additional subscription services, which we've mentioned in the past, which are non-access subscriptions. The testing we have done over the last six months has allowed us to improve this offering, and we expect to move from alpha to beta test during the second half of the year.

As we look forward to Q3 and Q4, there are a number of items we will be working on very deeply at AOL. The first area is in consumer products, focus and innovation with a number of brand launches and meaningful areas that you will see in the second half of the year. The second is revenue improvements in our agency channel, the AOL Networks business, and some of our key brand areas, as well as search growth and launching of the new subscription service. We will continue to actively resource allocate, and we will continue to reduce non-edge spending. And what I mean by non-edge spending is we want to have all of our investments go as close to our consumers and customers as possible, and out from the middle of the Company to those edges. And you will see us continue to do that.

The last area I wanted to walk through is Patch, and the meaningful progress we are working on to bring Patch to profitability. The steps we are taking on Patch are the following. We have segmented all the Patches into three buckets. First bucket is established and successful Patches, the second bucket is emerging Patches that have all the signs and signals of being successful, and the third bucket is a set of Patches that may have traffic or revenue traction, but don't have both. And we have operations there that need improvement. Each segment has a specific strategy broken out by DMA. There are a set of DMA's that AOL will operate, and there is going to be a set of DMA's that we will auction into partnerships or potentially exit. At the same time, we will continue to decrease the cost structure of Patch. We have decreased the cost structure of Patch roughly 25% already this year, and we would expect to remove more cost out of Patch going forward.

The cost reductions are likely to take three forms. First is a reduction in non-Town expenses found in the Patch corporate area. Second is a reduction in field management and overlay areas. And third are reductions realized by the optimization of the Town structures and the segmentation I just discussed around the Patches. The vision for Patch remain simple. Put a platform in towns that allows offline things we done online. Patch's platform needs to do three simple things. Allow people to get high-quality information locally, allow people to upload and share information, and allow people to transact advertising and commerce with online tools. Going forward, any and all of the investments in Patch we have focused squarely on those three things. As an investor, you should recognize that the changes we are making to Patch will negatively impact traffic and revenue, but they will meaningfully improve profitability and AOL's profitability. We have promised to get Patch to profitability in Q4, and we will do that.

AOL is improving as a Company. We are growing, and we are aggressively pursuing major market opportunities, and we are doing it on a leaner frame. Overall, I am very pleased with the Q2 results, very pleased with our talent, and very pleased to welcome the Adap.TV team. And after spending time with them over the last year, and we had a dinner last week in Palo Alto, I can say that the alignment with our current team led by Ron Harnevo, and the alignment with Amir's team at Adap.TV is something that I hope you will all watch over the coming years.

Lastly, before I turn it over to Karen, I just want to thank Karen and her team, and Julie Jacobs, our General Counsel, for helping successfully complete the Adap.TV deal. And for Karen Dykstra specifically for leading the deal and the acquisition internally. My money as investor remains next to yours, and we plan on increasing AOL's value to consumers, customers and partners. And I want to turn the call over to Karen.

Karen Dykstra - *AOL Inc - CFO*

Thanks Tim, and good morning everyone. We have a lot to get through this morning, so I am going to go through the quarter's results quickly, talk a little further but Adap.TV, talk about our cost reduction efforts, and leave plenty of time for your questions. Before I get to the quarter results, I wanted to add to what Tim said about the Adap.TV transaction. It is right in line with our strategy. Fastest-growing area of the Internet, incredibly talented team, high revenue growth Company that achieved a positive adjusted EBITDA in their past four quarters this year. I'm very excited about the growth that will come with this transaction, and I will add my thanks to the team.

Moving on to the second quarter results, the highlights for the quarter are the following. Revenue and profit continues to grow and the quality of both is encouraging and sustainable. We continue to make progress this quarter reducing our expenses. Adjusted OIBDA margins improved in total and in two of our three reportable segments, despite continued investment for future growth. We continue to pursue the growth strategy that we previously outlined, and we have made investments accordingly.

On a consolidated basis, revenue grew 2% year-over-year in Q2, reflecting 7% growth in global advertising revenue and a 5% decline in subscription revenue. Revenue growth was also negatively impacted by the absence of revenue this quarter from Studio Now, which we divested in Q1 of 2013. All of our advertising lines grew year-over-year once again in Q2, and growth came back -- came from both sides of the barbell, deep marketing solutions and programmatic. We believe we are in a unique position to offer our advertiser partners access to deep marketing and programmatic solutions across all formats and media at scale. We are making real progress in expanding our offering and are focused on a meaningful acceleration of our growth rate. Acquiring Adap.TV will further strengthen our opportunity here. And I will get more into that in a moment.

Global display revenue was driven by growth in domestic and international markets, and a growing number of advertisers find more impressions on a reserve basis and at a higher reserved adds -- add serve prices on AOL properties. This is very promising. Third party network revenue reflects growth in the sale of our premium formats, including video, across the network. In Q2 we saw a significant increase in demand for our DSP, AdLearn Open Platform, or AOP. We launched AOP last August, and it is now contributing meaningfully to our results. Our ability to expand our network offering organically through the launch of this product is very encouraging, and speaks to the strength of our team. We hope to see a similar impact from our SSP, AdTech Marketplace through the remainder of the year. Bob Lord is now on board as CEO of AOL Networks, and we believe we are well-positioned to take advantage of the large opportunity in this space.

In search, the growth driver continues to be revenue for search growth across our properties, particularly aol.com. This quarter marks four consecutive quarters of year-over-year global search. I mention this for perspective, because we returned to global search growth in Q3 last year for the first time in three years. Search remains a growth area for AOL and we expect that to continue.

Next, as subscription revenue trends continue to improve with a 5% decline in revenue, representing the lowest rate of decline in over eight years. Churn for the quarter was a historical low 1.4% per month, leading to a 15% decline in subscribers. The decline in subscription revenue was mitigated by a 12% increase in ARPU, as we continue to benefit from price increases in the second half of 2012 and in early 2013. Our subscription team has done an exceptional job improving our subscription revenue by continually increasing the value of this subscription bundle for our subscribers while deploying highly successful retention and win back programs. Looking forward to the remainder of 2013, in the absence of further price increases, we are likely to experience more difficult comps, which will result in a moderate uptick in the rate of revenue decline. We are happy with our progress here, and like all areas of AOL, we are pursuing avenues of potential growth for our subscription offerings. Now turning quickly to the segments.

The Brand Group headline is that revenue grew strongly, driven by 9% growth in global display and 12% growth in global search revenue. Segment margins improved meaningfully within the Brand Group, moving from a $15 million loss last year in this quarter to an adjusted OIBDA loss just shy of $2 million this quarter. Importantly, this improvement has come even while we continue to invest in this business for future growth. In membership, the improved subscription trends continue to drive the results of this segment and led to margin improvement in already high-margin segment.

As I noted, we are laser-focused on growth opportunities in this segment, but in the short term, revenue and margin will be moderately impacted as we lap price increases put in place in the second half of 2012.

At AOL Networks, the segment's overall growth rate was negatively impacted by approximately 2 percentage points by the absence of revenue from Studio Now, which we divested in Q1. Beyond that, the headline is that our investment in programmatic products and services is showing positive results. Our agreement to acquire Adap.TV adds significantly to our already robust offering for advertisers and publishers, and we believe it positions AOL Networks as a must-buy programmatic solution. In Q2, third-party revenues grew. However, we believe we can increase the rate of growth based on market trends and our discussions with advertiser and agency partners, and heightened focus on our agency relationships. We have the leadership, a highly talented team with deep industry and technical experience, and the products that should lead to accelerated growth in AOL Networks.

Turning to profitability, adjusted OIBDA grew 14% year-over-year, resulting in significant margin improvement on a segmented basis. In the Corporate and Other, adjusted OIBDA improved by almost $18 million year-over-year, primarily driven by lower year-over-year G&A expenses. We have made significant progress here, and continue to look for better ways to be more efficient. During the quarter, we also benefited from reimbursement in Q2 2013 of legal expenses from prior periods related to an escrow settlement, and lower marketing and outside services costs.

In general, we are operating with increased efficiency and focusing on areas where AOL can create engaging experiences and products and services for our consumers, subscribers and partners. Along those lines, we are methodically choosing investment areas and areas to prune expenses. You will see us make significant progress against our cost structure for the remainder of 2013. I expect we will reduce expenses throughout the organization, with no areas untouched. Patch has been our most visible investment area and we are significantly reducing our investment in Patch, as Tim just mentioned. We remain fully committed to Patch as a solution for connecting hyper-local communities, and while we are moving forward aggressively with product enhancement, we also remain committed to achieving run rate profitability by the end of the year. In all, I would expect us to make significant progress in reducing our expense base in the second half of the year while continuing to reinvest for future growth in our areas of strategic importance. The net impact should improve adjusted OIBDA this year by at least $30 million from the current mean estimate of $435 million, and of course this will set a lower expense bar going into 2014.

Turning now to the balance sheet, we ended the quarter with $483 million in cash and cash equivalents. Free cash flow for the quarter was $57 million. Remember that the cash flow for Q2 last year included $96 million from the license of our patent portfolio to Microsoft. Q2 last year -- Q2 was further impacted this year by the early receipt of a payment from a large partner in Q1, which typically we would have received in Q2 this year. Excluding those items, free cash flow for the period grew strongly and we continue to convert adjusted OIBDA to free cash flow at an efficient rate.

In July, we entered into a five-year $250 million senior secured revolving credit facility, which I believe significantly strengthens AOL's capital structure and marks another step forward in our financial progress. The facility is currently undrawn. We bought back approximately $50 million of stock, or 1.4 million shares, in Q2, leaving approximately $50 million left on our prior authorization. And in July, our Board authorized the repurchase of another $150 million, bringing our total current authorization to approximately $200 million. In less than two years, we have bought back approximately 35 million shares at what we believe to be very attractive prices. Our intent is to continue to execute opportunistically under the current authorization.

Finally, this morning we announced our agreement to acquire Adap.TV for $405 million, which we believe significantly expands AOL's global video leadership position. We now have a full range of offerings on both sides of the barbell in video, with deep marketing opportunities for advertisers to brand premium video experiences as well as end-to-end, fully-integrated programmatic solution in video. Our combination of assets is unique in this space. Adap.TV has had remarkable growth, growing revenue over 200% and over 100% in 2011 and 2012, respectively, to end 2012 with $75 million in revenue and close to breakeven in EBITDA -- as they term it, EBITDA versus our OIBDA. They have been slightly EBITDA positive for the past four quarters. In the first half of 2013, Adap.TV grew revenue over 100%, with EBITDA in excess of [$1 million] (corrected by company after the call), so momentum is continuing. The Adap.TV team has built a first-rate organization, with significant network effect, and we are very excited to combine it with the AOL On premium content network to offer a full-service video solution for publishers and advertisers for campaigns across all screens.

The purchase price of $405 million consists of approximately $322 million in cash and $83 million in stock. AOL will realize certain tax benefits from the acquisition, including NOLs and deductions from vested options cashed out at close, with a total present value of approximately $25 million. Additionally we will adopt Adap.TV's equity incentive plan and convert un-vested options from Adap.TV's stock option plan into AOL restricted stock. As such, we should receive a benefit from a tax deduction when restricted stock vests, and also from the retentive effects that this will have with the Adap.TV employee base. The stock will vest over the next three years, and we review this -- we view this as a significant asset in the deal. We expect to close the deal in late August or early September, and clearly, we are excited to move forward. And I can't emphasize enough how excited we are to move forward with this transaction.

As we focused on the transaction, we did look hard at our expenses across the Company, and in particular at AOL Networks and the cost structure there. We reduced expenses in anticipation of this transaction, starting this past week. And we are looking at it on a holistic basis, with our Networks group restructuring, and the transaction will be approximately $0.06 per share dilutive in 2013 and about $0.31 in 2014, based primarily on estimated non-cash amortization of intangibles. As I stated earlier, the company Adap.TV is projected to continue to be EBITDA-positive going forward.

It's been a busy couple of weeks, and a very busy quarter, as you can see from all of the activity that I mentioned. To conclude, we clearly are keeping busy and have a consistent trend of improvement, which we intend to accelerate. Q2 results mark another step forward, and today's announcement even further progresses on our strategy. And with that, I will open up for questions. Turn it to the operator.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Brian Pitz, Jefferies.

Brian Pitz - *Jefferies & Company - Analyst*

Tim, congratulations on what seems to be a great deal for you guys. Just a quick question, a little deeper dive on Adap.TV. Why Adap.TV? There is lot of assets in the private space right now, in either programmatic or online video. What kinds of things did you do to get yourself comfortable that this is the right asset for AOL, given all those names out there? And can you comment on, was this a competitive bid process or not?

Tim Armstrong - *AOL Inc - Chairman & CEO*

Why Adap.TV? I think, basically, just so investors know, and you know, Brian. This is a space that we have looked at really closely for the last year, and we have spent a number of different iterations with different companies. We looked at build versus buy in our scenario. And really, there is three reasons why Adap.TV. The first is, Adap.TV is the only player who's got a marketplace, meaning buyers and sellers, are built out at scale on the platform. And more importantly, underneath that, that marketplace is Adap.TV is a true technology Company with, I think, some of the best computer scientists in the world at it. And also some of the best product people, and a very strong sales organization. Although the decisions that they make and what they have built as a Company is essentially product and engineering led and driven, which I think is really important in the space as software starts to get into advertising.

The second thing that is important is their growth rates in comparison to some of the other assets out there. And I don't know everybody's growth rates individually, but I know the ones that are visible. Adap.TV's model, because it has a network effect behind it, with advertisers and publishers, allows for, essentially, a high scale frequency network that gets smarter and smarter over time. And the output to that is actually seen in their growth rates. Adap.TV, on a dollar-for-dollar basis, advertiser-for-advertiser basis, and publisher-for-publisher basis, on a faster, more accurate network effect can do video programmatic, I think, better than anybody else can. And the third area, and this will cover both your second question and the third pillar of my first answer, is acquisitions and our ability to get very, very talented people here is really the reason that we did the Adap.TV purchase.

I think you see a lot of purchases that happen across M&A where there may be good ideas, a good technology, but really what drives good ideas and good technology are the people. And I think Adap.TV has the best team in the space. It is led by the best founders, it has the best product people, has the best sales leader, and I think that's a very important piece. And then we have been able to leverage the knowledge and power of our current video team, Ron and Tal and Hunan, the people from Five Men who run our video team in combination with Adap.TV. And I think that's powerful. And then we have a leader like Bob Lord coming in, who is very knowledgeable in this area. So I think the combination of those three areas, that's why we bought it. We don't buy assets any other way than the following way, and then for the entrepreneurs that I've met with and the people that we have bought, they will know what I'm about to say very well.

When we sit down with people to acquire companies, we essentially say, we want to do something that is fair for the investors and founders and employees of the Company. And we want to do something that is fair for AOL. And the second piece is, we will not buy companies where the principles aren't staying around. And whether or not there are other people who want the asset or not want the asset, we believe that in this case, we have our fair Company at a fair deal. Sorry -- a great Company at a fair deal for both sides. I think Amir wanted more, I wanted less, and we ended up the middle. And the reality overall is, if you look at the public comps around Adap.TV, and you think about the fact that they are growing much faster in some cases 2 times to 3 times the growth rates of some of the other assets. I believe we got a very, very fair deal done at a very good time period in the middle of probably the largest change in advertising overall. So as an individual investor, let me take off my Chairman-CEO role hat off for a minute. If I had to pay my percentage share of the Adap.TV deal myself, personally, out of my bank account, I would've paid it. I think it's that strong of a deal on both sides.

Brian Pitz - *Jefferies & Company - Analyst*

Great, and congrats again.

Operator

Anthony DiClemente, Barclays.

Unidentified Participant - *Barclays Capital - Analyst*

This is Ryan on for Anthony. Just one question on AOL Networks. Other than Studio Now, is there anything you can call out that led to the acceleration in growth? And anything you can say about margins declining year-over-year and the outlook for margins at that business?

Karen Dykstra - *AOL Inc - CFO*

I think that the Studio Now was the only -- was the most clear difference quarter-to-quarter. I think we have been focusing on our DSP and our SSP, and the focus has been to accelerate that. In the middle, the network, the growth had slowed. In terms of margin improvement in the future, I think, first of all, I just talked about the cost reductions that we had and started last week in AOL Networks. And I think in terms of margin improvement, we will see that. We will see as we finish the acquisition on Adap.TV that acceleration happening. We have also been investing in our sales force in the AOL Networks, and in our product, having just completed some more investment in the SSP. We are also expanding internationally with those products. So what you see and what you are looking at, I suspect, in the quarter, is the difference in the margin on the same amount of revenue in AOL Networks quarter-to-quarter, and it reflects those incremental investments in the AOL networks group.

Unidentified Participant - *Barclays Capital - Analyst*

Great.

Karen Dykstra - *AOL Inc - CFO*

Also, I would say that the -- offsetting it we saw more on domestic display side taking some of the growth from the network [piece].

Operator

Ross Sandler, Deutsche Bank.

Ross Sandler - *Deutsche Bank - Analyst*

Just two questions. Tim, there seems to be a fair amount of confusion out there around what is going on in your display business. The potential impact from ad networks and programmatic on pricing. Seems like there was minimal impact in 2Q, and you noted shifting more inventory away from ad.com and into your direct sales and your premium channel. So can you talk about how the lower CPM display industry may or may not be impacting your higher CPM display business? And then Karen, just a second follow-up on Adap.TV. We agree the space is very attractive, and this is a great Company, but based on the numbers you gave, you are paying about 5 times 2012 revenue, around 3.5 times revenue 2013. That's a pretty significant premium versus what the public is currently paying for Tremor and YouMe. So what makes Adap.TV that unique? And how can you guys accelerate their agenda as part of AOL versus as an independent?

Tim Armstrong - *AOL Inc - Chairman & CEO*

Ross, thanks for the question. The display business overall -- and let me -- I will go as quickly as possible but as precisely as possible. Programmatic -- the introduction of software automation into advertising is non-price dependent. And what I mean by that is, the ROI and engagement and metrics that advertisers want typically are able for them to be pretty transparent about. And the pricing that we saw during Q2, and I will give you an example. I was in Palo Alto, I won't mention the name of the customer. But I met with one of the largest direct advertisers on the Internet for the last ten years last Thursday in Palo Alto. And essentially, they came to the meeting and said, we would like to have AOL be one of our five or six giant strategic partners for 2014, but we want to not only do direct response with you anymore. We want to go actually on this side of the barbell as well and do marketing services and brand advertising.

And when I asked the question, because they were very interested in programmatic also, essentially the low end CPM business, which has been highly dominated by the direct response advertisers. That business is getting faster and more networked with software overall. Pricing is variant by customer in the low CPM category and direct response categories, overall. But as software gets better and better and better is why we are so interested in Adap.TV being able to really transparently show advertisers the value they're getting. When advertisers are very educated and understand the inventory and the ROI very well, they start to migrate into pricing patterns that actually are not price-dependent. They are dependent on the ROI. And the second piece is, on the high end of the CPM's, which we saw stability and growth in the premium side of our business and premium formats. That side of the business also, as you get into programmatic and private marketplaces, I would expect that pricing to be stable or to go up over time.

And there may be disruption curves by customer as they figure this out, but the software over a longer period of time should make the process stuff more efficient. It actually, I believe, in a long period of time, is going to make advertising more competitive overall, because advertisers will want the best inventory and best ROI and those -- and it will be faster more transparent. So I think there's been a lot of noise in the industry around programmatic, but if you actually look factually under the hood, you basically see premium pricing on premium audiences and premium formats. You see advertisers getting smarter and smarter about the ROI and the targeting abilities and transparency on an individual bulk impressions to individual impressions and you see the part of business I think that is getting disrupted is the old banner business. And part of the reason it is getting disrupted is because there are better formats and better processes out there, and that's why you see us doing the Adap.TV deal and migrating more towards the premium side of the business. Because we can give advertisers better results and publishers better yield.

Karen Dykstra - *AOL Inc - CFO*

And let me address the second part of the question, in terms of the price and the multiples on Adap.TV. First of all, I think you have to think about it -- as Adap.TV as a different business, as a different business model. It's a technology solution that automates the trading of media, while the others are more like ad networks that buy and sell for a margin. So the move from manual to automatic is really transforming digital advertising, and that is where Adap.TV benefits. I think it has a -- it's tough to think about it as a platform. It is not necessarily a network. It has network. It's a programmatic. And you can see that if you look at their -- the detail in their model, you can see them consistently growing.

They have a very high revenue growth, stronger than the others. And you can see that the headcount applied to that model is lower than the others, which reflects a programmatic solution. Their product, their platform is very strong and has an ability to scale and scale internationally. And I think I would look at them in terms of the revenue, the revenue growth, and then their ability to prove out the model on a profit basis, which they have already done. So we think that the combination of those things, and as we looked at this product, we looked at it totally differently than the others that you are comparing it to, as a different business model. And stronger and a better fit with AOL.

Tim Armstrong - *AOL Inc - Chairman & CEO*

And Karen, maybe to put a finer point on it. Ross, there's two advertising businesses. We are going to be in the media sales business and the enterprise business. Adap.TV is a very, very scalable global enterprise solution. And I think if you compare that type of system, and there is only a couple of them in the world, in comparison to other prices that you brought up. We believe Adap.TV has a -- is a very different business. It is in 60 countries, and we believe that the price we paid on a multiple basis compared to their growth rate. If you look at other peoples' growth rates and with their valuations are, Adap.TV, we believe, is a good value for our shareholders and a good value for the Adap.TV shareholders.

Ross Sandler - *Deutsche Bank - Analyst*

Great.

Operator

Peter Stabler, Wells Fargo Securities.

Peter Stabler - *Wells Fargo Securities, LLC - Analyst*

First of all, a follow-on on Ross's question. Tim, if you step back and look at shifts of revenue across the industry, would it be fair to say that you look at the concerns around the display business as being somewhat misplaced? Programmatic being singled out as the great threat here? Would it be fair to say that the growth out of video here is really coming perhaps out of display? And that's where the focus should be? And then secondly - and when I say, display, I mean standard display. And secondly, getting into the Adap.TV here. What kind of synergies do you see with the Adap.TV platform, and some of the recent work you have announced with Mediaocean? Can you talk a little bit about progress on the Mediaocean front and the larger picture workflow issues that Adap.TV might also solve here? Hope that makes sense.

Tim Armstrong - *AOL Inc - Chairman & CEO*

Sure. So one, I -- Pete, you have something very significant, which is a lot of the video market today has come from display. And Adap.TV is actually targeted at a different market, which is the transition of the $240 billion TV business into the Internet IP connected device and video delivery business. That is significant for a couple different reasons. One is that you have an industry in TV where, on the consumer side, people are demanding IP connect. And that's why you see actually a lot of the announcements in the broader media industry over the last few months around why there is a much contention around cable and video or TV. Adap.TV, essentially, if you look at the difference in the process of how TV ads are bought and sold versus what Adap.TV does, there is not a small difference. There's a pretty significant difference, and something that may take months to plan and buy can be done in a matter of tens of minutes on the Adap.TV platform.

And we believe, like all other spaces, that the -- Clay Christiansen's model of getting 80% of the value at 10% or 15% of the cost. That's what Adap.TV brings to that marketplace, specifically focused on IP connected video and not on the display side overall. And we are very, very bullish about that. And I would remind people -- I think on the last call we talked about this year being the first year that the humans in the industry had actually gotten together and tried to planned TV and video together, and that is only going to continue. And Adap.TV is at the forefront of that. Second piece is the synergies with Adap.TV, I would break down into a few different buckets. The first bucket is actually we already work with Adap.TV, and we very deeply know how the two of us can work to a greater degree together to help fuel Adap.TV. I would specifically say, and this is important, that one of the synergies is actually letting Adap.TV run really quickly and independently towards the spaces that they been targeting. So I think we sort of have an idea of how to leverage and fuel them, a little bit like we do with the Huffington Post, from our assets, but let them manifest destiny pursue their grand vision. Which is really why we are interested in partnering with them.

And then the third area is there are synergies over a longer period of time, with the ability for us to together grown a larger enterprise solution of software that we can be bringing to the holding companies and the clients and the publishers. And the second piece is a synergy around the ability to plan, target, measure, and do deep analytics and data around advertising. And that is something in the future -- not in the short-term, but in the future. We will work with them on a systemization standpoint. I would say, I've spent a lot of years to two decades in this industry, and I have been through with the Adap.TV team both on the technology product and sales side with Bob Lord, and Ron Harnevo and Karen and other folks. We have a deep understanding of what they have built. And if I compared what I saw when I came from traditional to Internet, through the search days until now, they built the equivalent of what I saw during the search days in the video space. Which is a different space and a brand marketing space, and could be a tremendous synergistic asset to our barbell strategy in investment.

Operator

Ron Josey, JMP Securities.

Ron Josey - *JMP Securities - Analyst*

Certainly a busy quarter. I wanted to switch topics and talk a little bit about Patch, specifically, Tim. And talking about those three different buckets you talked about. Can you break that down in terms of the number of towns that are out there? I think there is around 900 today. And then provide some insight into how AOL can actually partner with the Patches, and maybe the timeframe? And then real quick, Karen, just to confirm you comments on EBITDA. Did I hear correctly that, relative to Street consensus, you believe EBITDA can be $30 million higher?

Karen Dykstra - *AOL Inc - CFO*

I will just -- the last one was a quick one. Yes, that's what I said. That we believe that the cost reductions would raise EBITDA by $30 million from the current consensus of $435 million.

Tim Armstrong - *AOL Inc - Chairman & CEO*

All right. And then on the Patch question, I would say couple things about Patch. One is, we are been able to spend a lot more time with Patch, as we have gotten the rest of AOL focused and going and work through some of the big things on the AOL Corporation side. We are been able to spend a significant amount of time with Patch and really start to look at the profitability commitment and how do we get there, the most efficient and effective way overall. And I think our top-level viewpoint on Patch, is Patch is really tapped into a consumer need. It's had very fast traffic growth. It's the high -- I think it's the largest, highest external traffic property we have as a business in terms of percentage of external traffic. So there is a consumer need there. On the town metrics, the three buckets essentially is about 900 Patches, at a broad basis. It's not exactly there, but in a rough justice manner, it's about one-third, one-third, one-third, overall.

So one-third are basically very good-looking things, viable business models that we want to pursue. One-third look like they are going to get to that first bucket. And one-third basically look like in the timeframe and focus we have right now on getting a profitability, it's going to be tough for us to get there in a timeframe standpoint. I'm going to caveat this by saying, we have a deeper review. We have a board meeting tomorrow. The board's mission to us is to get to the profitability metrics. So we are going to be reviewing this in detail with the board, so I will not go into tons of detail, because we don't have an approved proposal yet around it. But the important part of the partnership [fund] is, over the course of time, Patch, because of -- essentially on a DMA standpoint, we have picked out the most valuable towns around large cities.

If you think about the retraction of local media and the investment changes you have been seeing this week with some of the changes of hands in the large media properties. Most of the significant off-line media companies have not been able to invest in digital, because they've had to essentially work on their off-line properties on a cost standpoint. And many of them have come to us over time wanting to partner in those DMA's around using the Patches. So we believe one of the pathways that we are pursuing, and have been in setting a meetings with people, is essentially the partnership between traditional media assets and Patch in those DMA's. And I think it is early to tell. Our number one North Star goal is to get Patch to profitability. And to make the tough decisions around Patch to get there. And then as part of the partnership, so one piece of it, I would, for investors to know, we have a deep analytic group working on Patch. And I think its got our full attention and one of the major priorities for us in Q3 and Q4.

Ron Josey - *JMP Securities - Analyst*

Great.

Operator

Mark Mahaney, RBC.

Mark Mahaney - *RBC Capital Markets - Analyst*

Wanted to ask a question on the subscription revenue. That 5% year-over-year decline is one of the lowest we've seen -- or maybe in years. It is in years. I know you talked about it increasing in the back half of the year. But do you think, with a broader range of products, the lower churn, that there is a scenario under which that subscription revenue actually bases out and then starts to grow again sometime in the next two years?

Karen Dykstra - *AOL Inc - CFO*

I think that would certainly be our intent, that we have a lot of activity going on around building new subscription bundles to add on to that. So we have an investment going on to build out new products. What I said, and what you noted that I said, is that we will probably see a slight increase in the decline in the back half of the year as we lap the price increases. But we continue to surprise ourselves, really, in terms of our ability to manage that. And our team is quite strong and quite experienced. So what the exact timeline is, I could not say, but it is certainly our intent to turn that around and grow with additional product bundles.

Operator

Laura Martin, Needham.

Laura Martin - *Needham & Company - Analyst*

A couple questions for you, Tim. First, on the video CPM's. We're hearing from one of your competitors that generally in the market, video CPM's have come down from about $23 to $18. And I'm wondering if you're seeing video CPM pressure? And more generally, is there something different about video that we won't have unlimited inventory and over the next decade end up with the commoditization of video as we've seen in text? Let's start with that one.

Tim Armstrong - *AOL Inc - Chairman & CEO*

Laura, good to hear from you. On the video side, I think the pricing -- what I said before, has all been dependent on what the inventory is. Overall I think if you look across our spectrum of inventory on video, we actually -- there is probably some cases where it's been going up and going down. Overall, we feel pretty confident that video inventory from a pricing standpoint will remain stable. And something that we are going to continue to invest in overall, as you see from the Adap.TV business. The second piece, which I think is pretty important around that, is the reason I was talking about the -- going from bulk media down to individual impressions is -- and private marketplaces is, advertisers in general, especially video advertisers, adapt deals with 70% or 80% of the top 100 advertisers.

Those advertisers demand the high-quality experiences and want to build their brand equity. And I think from a brand equity standpoint, the premium areas around video will probably stay premium. And the other areas, I think there will be a curve of videos overall. But we would fully expect from the partnership we see, and from the deals that we have been doing, that there is a pretty high demand. People are willing to pay for sites found in motion, and there is probably going to be a spectrum of pricing. But we believe overall that pricing in video will remain strong, and eventually leg out to what probably off-line video looks like over time.

Laura Martin - *Needham & Company - Analyst*

Very helpful. On Patch, Tim, last question. The third that are in the lower bucket, how are those different? When you look at the patterns of what makes a Patch -- let's call it a failed Patch, or an underperforming Patch compared to the two groups that are either going to hit the metrics or are already at the metrics. What is different about the ones that didn't work?

Tim Armstrong - *AOL Inc - Chairman & CEO*

I think this is a couple things. One is, essentially, some of those Patches should be merged together. On a DMA look and a data look, those Patches may appear to be different. But when you actually live in the towns, an example is, one town may have no downtown commercial center, and use another town's downtown commercial center. There is aspects of just how towns are essentially set up, when you get down to that level. And then the second piece, I would say, is just from a timing, human standpoint of whether or not we have been able to spend enough time and traction in those areas. I -- essentially, the 900 communities that we had targeted on a data-centric way support pretty robust commerce and consumer demand.

But then I think, as we've gone through and spent a lot of time looking through the data and information and structures, you start to see that there is a bucket. As a matter of fact, the third bucket is smaller than one-third of the total Patches, but it's still within a ballpark. But I think those are areas where we are really trying to optimize overall. And I think, from our standpoint, that's -- it's an important part of the next version of Patch is to get to within a scale within the Patches that we focus on the Patches that we know can be successful partner on. Some of the ones that we could do better with partners, and really, really deeply work on the product and technology stack but do it in a profitable way.

Operator

James Cakmak, Telsey.

James Cakmak - *Telsey Advisory Group - Analyst*

Can you just talk about, Tim, how Adap.TV is going to -- or how it will help you capture television ad dollars? You recently announced a partnership with Mediaocean, and what is the ecosystem going to look like as you incorporate -- integrate Adap.TV? And what should we expect from the brand television advertising dollar front?

Tim Armstrong - *AOL Inc - Chairman & CEO*

Sure. Actually, I think I forgot to answer Pete's question about the Mediaocean piece overall. But the simplest way to think about our video business overall -- and let me relate it to the outside partners we deal with. Is there's three parts to our video business. There is owned and operated videos, and things that we are doing across our brand portfolio, and then live versions of that video, which is Huff Post Live and AOL Live. There is very large syndication business that we built up with AOL On, which goes out to tens of thousands of publishers and has the 700 high-quality assets. And the third area is essentially what Adap.TV will be bringing, which is a marketplace -- a real-time marketplace of buyers and sellers overall. So if you look at those three areas, one of the integrations that we have done is with Mediaocean. We have a partnership with FreeWheel.

We essentially have taken a strategy of allowing our video assets to be within and to partner within the ecosystems that major agencies and clients use, and publishers use overall, to essentially their serve or put advertising on videos. The partnership with Adap.TV -- essentially, Adap.TV is an open, unbiased marketplace. So Adap.TV works with all of the video ecosystem players. And again, we were -- before we acquired them, we were just one of their partners. So our ability to use Mediaocean and some of the other assets we have around the serving and monetization of videos will be enhanced -- already was enhanced by the Adap.TV partnership overall.

So I would look at our two syndication business and O&O business as media businesses. And I would look at the Adap.TV as a universal joint of unbiased of plug-ins for us on the video space. And again, you've seen the announcement we made with Mediaocean and with FreeWheel and partners like that, where we are plugging directly into the measurement and planning of the TV space directly. As a matter of fact, AOL's inventory is one of only a couple -- or a few partners that actually shows up when you're planning TV inventory. Our inventory shows up inside of those planning systems. I think that will be enhanced by Adap.TV.

Operator

Mark May, Citigroup.

Mark May - *Citigroup - Analyst*

On the -- question around the publisher side of Adap.TV's business. Is there any potential halo effect or cross marketing opportunity with some of your other businesses, here? Meaning, might you be able to draft off of ad.com's significant publisher relationships? Or as you're trying to scale out your SSP, might that business be able to draft off of the 9,500-some odd publisher deals that Adap.TV has, et cetera. Or am I just thinking of this not the right way as really working within a silo?

Tim Armstrong - *AOL Inc - Chairman & CEO*

You are thinking very clearly this morning, which is nice to hear, but part of the Adap.TV, and I think the reason the Adap.TV team, Amir, [Cheg], and Dan were excited about doing the deal with us, is we are one of the most significant suppliers of software to publishers in the world. So we have AdTech, the ad serving Company, we have ad.com, and we have the recent marketplace addition that we have done. And I think if you talk to our ad.com team, the Dave Jacobs, the Don Kennedys of the world, they would tell you that the Adap.TV synergies for the publisher side of our businesses are going to be significant. And I think the Adap.TV people feel that way as well. And essentially, the way to think about it is, publishers need a full stack of technology just like the advertisers do.

And on the publisher side of the business, we will have the first fully developed stack of our cross-screen publisher solutions that will hit display and hit video. Although I will point out again, Adap.TV is going to operate as a separate entity out of the gates, and we are going to let them pursue their manifest destiny overall. Over time, I think we will be able to bring a more unified approach to enterprise sales to publishers, which will be important. But one of the reasons we are doing this deal is because there are direct synergies with the customer base we have and the customer base of Adap.TV could be serving more of. And I've got already gotten notes from both publishers and a holding company executives this morning, essentially understanding the fact that Adap.TV is directly synergistic with the rest of our business.

Operator

John Blackledge, Cowen and Company.

John Blackledge - *Cowen and Company - Analyst*

Two questions. First of Patch. What will the cost for Patch -- for each Patch be, post the restructuring? I think it's historically been about $150,000 per Patch. And if you were to get Patch to profitability by 4Q '13, do you expect profits to grow off that 4Q '13 base? Or would we see normal seasonality in that business? And then on the subscription side, wondering if you could expand on the prospects for Gather, which I think you said is going into Beta? And how that product could potentially help the segment get to a more flattish revenue trajectory over time?

Tim Armstrong - *AOL Inc - Chairman & CEO*

The cost for Patch is something we have brought down over time. I -- about $150,000 number is actually dated. We been able to significantly reduce the Patch number since -- and I don't remember when we released that number, maybe 1 year ago or 1.5 years ago. But it's substantially below that. The new models we are working on for Patch would reduce it significantly below the significant reduction we already have overall. So I think on a cost per town basis, just to remind people, most of the media markets were in support $7 million to $30 million zip code level media market. The towns that do roughly $900 million of commerce. If you cut out autos and real estate, they probably do $350 million to $400 million in commerce.

So these are big markets that we would expect to run at a number much lower than $150,000 for the Patches that will remain operating. And then the second piece is that we get to the Q4 profitability. Our goal is to have a ongoing, profitable business. There is very big seasonality in local. So I don't know whether or not, from a seasonality standpoint, an adjustment level, there will be some kind of adjustment around that. But out -- just so you're clear about it as an investor, our goal is to have a profitable business that runs every year with profits. And regardless of seasonality. So I don't know, Karen, I don't know if you want to -- but I think that is our goal.

Karen Dykstra - *AOL Inc - CFO*

Yes, that would be the goal. And the second part of the question, I think, was about Gather (multiple speakers) and the subscriptions. So I think we are very encouraged by our early marketing efforts on Gather. We have previously had it maybe earlier in the summer as a launch, but because of some of our investments in cost done, and so on. We have moved it slightly to the fourth quarter launch. So there is a slight difference in timing. But we are very encouraged with what we have seen so far, and we are hopeful about it. I can't put a point in time in which we are crossing the line on the subscription revenues, because as you know, our legacy subscription business is quite large. But we are working furiously on those bundles and are encouraged by early piloting.

Tim Armstrong - *AOL Inc - Chairman & CEO*

One thing I would just say is, Karen's point is -- we -- part of the reason for pulling it back was we were able to add more partners. So I -- we have a pretty significant list of partners that will be integrated. And also the product has gotten much simpler. So I think delaying it is going to allow us to come out with a more robust product with a much simpler process for consumers, which I think the Gather teams believes is very beneficial overall.

John Blackledge - *Cowen and Company - Analyst*

Great.

Operator

Ben Schachter, Macquarie Research.

Benjamin Schachter - *Macquarie Research - Analyst*

Just want to follow-up on Gather and then a couple of other points of verification. On Gather, can you talk about the go-to-market strategy here? Is it just going after current subscription guys who will potentially canceling? Or is it going to be a much broader rollout? And then can you talk about how much you're going to invest in that product? And then some clarification. On the pricing on Adap.TV, when you talk about the revenue numbers, are those revenue numbers for the media buy? Are those the gross revenue number or net revenue number?

Karen Dykstra - *AOL Inc - CFO*

I will hit the pricing on Adap.TV first, because I think that's the shorter answer. And then we can talk about the Gather further. So the number that I quoted for their 2012 revenue is a gross number. Their net number is somewhere in the 30%, 40% range, and they will report gross revenues.

Tim Armstrong - *AOL Inc - Chairman & CEO*

And then on the Gather, essentially, I won't go into detail, because it's -- we are not out there with it yet, and I want to give the team room to do what they think they should do. But essentially, Gather is -- will be launched outside of the AOL network. This is about adding new subscribers outside of AOL's core membership base. It will be offered to AOL's membership base. And then there are two specific demographic targets that we are going after with Gather, and there will be specific regions we go after with Gather. So from a standpoint of the product itself, the product essentially is targeted at saving consumers energy, time and focus by aggregating subscriptions and essentially is targeted at a couple unique demographics and a couple -- or more than a couple areas. One of the areas is outside of AOL. The other area is on a regionality effect, but we will have more information on that as we get closer to launch, and probably discuss it more on the next call.

Operator

Eric Sheridan, UBS.

Eric Sheridan - *UBS - Analyst*

Tim, Karen, first to come at the networks piece a different way. If we thought about, Tim, the way you were thinking about investing in networks before Adap.TV, is anything -- would buying Adap.TV up front with capital change the cost curve. So that future profit margins in networks might be different because of the up-front buy of the assets today as opposed to things you might have invested in longer-term? And then second question, one thing we haven't talked about yet on the call is the Publicis deal that was announced in July in terms of the live Internet advertising partnership. And I wanted to understand how that gets rolled out? And then the second part is, how the Publicis/Omnicom deal might change that partnership over time?

Tim Armstrong - *AOL Inc - Chairman & CEO*

Sure. Basically, on the AOL networks revenue and cost strategy overall, we have been really trying to be concise about this. We believe that software, over a long period of time, is going to help us migrate the AOL Networks business, and it's part of the Adap.TV, to essentially serve more media impressions with less cost. And one of the things in the investment numbers you are seeing in AOL Networks is an investment that Karen talked about in AOP, which is the marketplace for advertisers -- I'm sorry, the demand-side platform for advertisers end marketplace place. The supply-side automated systems around programmatic.

We are going to continue to invest in those areas. I think the long-term outcome for those is essentially to have a model where on a per impression and per dollar basis, we are running at a much higher revenue and profit per head than we are running today. And if you want to talk about the macro migration of our business, that is what you are seeing. And by the way, we are doing now while we are continuing to grow partnerships with advertisers, partnerships with publishers, pricing, those things. So we are doing a very good job, actually, of migrating that business in that area.

Karen Dykstra - *AOL Inc - CFO*

If I could jump in before you get to Publicis, if I could. We have, as Tim said, been doing a good job and we have been investing in a number of things that we talk about, which goes to the cost structure in our current quarter increase in cost. We have been investing in the sales force. We have added significantly to the sales force, particularly to sell AOP. And we are seeing great results with the team that has been selling AOP. We've been building out AOP. We are taking out increased international sales and focusing on expanding globally with the Network Products. This -- as we close on the acquisition of Adap.TV, will allow us to continue to focus on some of those other products.

We now have a programmatic Video Solution, and we can use that and enable us to bridge between our products and a programmatic video. But I think it allows us to focus on our current stack, as well, and continue to go harder of the sales avenue. So although I think our expenses certainly have increased because of sales, marketing, product, engineering, international expansion, all of those things are positioning us better so that when we do join with Adap.TV, we will be in a much better spot to accelerate our growth.

Tim Armstrong - *AOL Inc - Chairman & CEO*

Karen and I both expect AOL Networks business at a scale to become a profitable growing business with better margins over time, period.

Karen Dykstra - *AOL Inc - CFO*

Yes.

Tim Armstrong - *AOL Inc - Chairman & CEO*

On the Publicis relationship and PAL, and again, this is something that Bob Lord is working closely with Publicis on. Number one is, sight, sound and motion is significant coming to the Internet at scale. It's part of the reason for the Adap.TV transaction. Part of the reason you're seeing our video business take off. We believe that Live is a category that is underserved on the consumer and advertising side. The PAL relationship, The Publicis/AOL Live relationship, was born essentially out of a meeting that we had Maurice Levy and his senior team a year ago in New York. I think it was actually in August. Last year in New York, we spent a day together talking about where the future of business was going. And from that side of the business, we felt like live real brand publishing of video is going to be an important part of a future. We tested for the last year with them a whole bunch of from areas, Arianna's team at Huffington Post tested. We tested across some of our content properties and on the network. A series of live advertising tests.

And then with AOL Live, the launching of that platform, Publicis and PNG had come in with Secret, the deodorant, to do that testing. And I think the partnership was actually born out of a very deep planning experience we had with them and that a whole bunch of testing. The Omnicom/Publicis merger in relation to what that agreement is, I don't know what the potential outcome is. I only know what I see from inside the Publicis group, which is the CEO's of the group leaders in different brands inside of Publicis have reached out. We have a significant amount of work going with them for the AOL Live launch. And for deals like Huffington post Live and other things. So I would hope the Omnicom/Publicis deal helps enhance the PAL partnership overall, but I will leave that up to our relationship with Maurice and John Wren. And we will work closely with them and whenever that deal closes to figure out what that means. But I would say the continued work with Publicis is happening today on a daily basis.

Eric Sheridan - *UBS - Analyst*

Great.

Eoin Ryan - *AOL Inc - SVP of IR*

Laura, it looks like it's 20 minutes past the hour, so I think we just have time for one more.

Operator

Youssef Squali, Cantor Fitzgerald.

Youssef Squali - *Cantor Fitzgerald - Analyst*

I will make it brief with two quick ones. Tim, as you look at your AdTech's stack, obviously have made a number of acquisitions. But do you feel that there is some -- any element left that you need to have to offer an end-to-end offering from publishers all the way to advertisers? Do you feel you are good with what you have, and you will just be able to grow it organically? And then, Karen, not to beat a dead horse on this Ad network, but you guys on the last call did talk about acceleration of growth in that line, driven by some increased hiring of salespeople and increase in investment? So versus that expectation, maybe you can brief us as to what changed between then and what you guys are now?

Tim Armstrong - *AOL Inc - Chairman & CEO*

On the AdTech stack, what is missing. Again, you saw us go for a pretty significant amount of time without us doing really any large acquisitions, and we had done a by-side acquisition on a retargeting product, which, again, a very talented team inside of AOL Networks. The Adap.TV fills out what we believe is the number one strategic area that we were focused on overall. And I think from our strategy as a Company, we have rated that the number one area. And I think we are all very happy as a management team to have closed on that. The AdTech stack, just to give you broad strategy of what we are doing, is Adap.TV fills the number one largest hole for us. And we are excited about that team and the future for that business. On the other areas, we specifically have been doing a lot of organic building within that stack. I think some of the things that we launched during Q2, cross-screen optimization, the tie in on the mobile serving and SDK serving of advertising is really big for us in general.

And AOP and marketplace were primarily organic investments that we made. So I think if you look forward for us in the AdTech space, I would guess we are doing to do more organic investing than anything else at this point. I will reserve my right to change that. But from the information I know today, and where I see us going, I think we are putting a lot of resource and time and energy into engineering and product. If you look out to the future, advertisers and publishers are going to want real-time, accurate, high-quality, results-oriented advertising that touches consumers and advertisers and publishers with material benefits. Underneath that is the ability to -- you have to serve cross-screen. It has to be IP delivered, and it has to be done not in bulk but on an individual impression basis. And I believe our stack is one of the leading -- I believe with today, we have the number one best programmatic video stack in the marketplace. So I believe we will be going organic first until we change our direction.

Karen Dykstra - *AOL Inc - CFO*

The second part of the question was about our acceleration and investment in AOL Networks and our increased investment and comments from last time. We had an increase -- a further increase in expenses and investment in this quarter, driven by some marketing for digital New Fronts and continued increase in our investment in additional sales organizations. We also had some increased spend on video production, related to the original Slate and various items that were video focused in the quarter. So I think the expense part was continued from what the comments from last quarter. And also I would say that we have had further -- selling more on a reserve basis that a third-party basis. And that impacted the quarter. But I think a way to think about it is that we talked directionally about accelerating growth, investments in network, and the products and the sales in growth internationally as a -- where we are aiming at and for the future. And based on this acquisition, as well as the investments that we have continued to make in the second quarter, I think that still holds true from what I had commented on last quarter. This is what we think -- we do believe that it will accelerate, and we continue to invest.

Tim Armstrong - *AOL Inc - Chairman & CEO*

(multiple speakers) Just to wrap the call up, again wanted to really welcome the Adap.TV founders, Tag, Amir, and Dan, to the Company and their teams, which I think will be a big addition on both sides there overall. And wanted to just -- we did not really go through it in as much detail, but I would remind you from where we were a few years ago today, we announced second consecutive growth in all advertising lines, second consecutive quarter of adjusted OIBDA growth, nine sequential quarters of ad revenue growth, 5% growth in display revenue growth, 7% growth in advertising revenue, global advertising growth, 8% in search, 5% subscription revenue decline, and the churn dropped to 1.4% and 9% third-party revenue growth. EPS of $0.35 versus $0.17 from the quarter last year.

And we added $150 million repurchase reauthorization. And we repurchased $50 million of stock. AOL is a Company on the move. We are aggressively pursuing what our opportunities are. We have significant talent, focus, and operational rigor going at this point, and I think we have a lot more work to do as a business. But you have a fully engaged management team, a lot of talent, Bob Lord joining, Susan Lyne is here, Karen is here. A lot of new management in the last year who was very strong and very experienced and we are going to really continue to pursue our opportunities aggressively. Thanks for joining the call, and we will see you next quarter.

Operator

Thank you for your participation in today's conference. This concludes the presentation. You may now disconnect, and have a good day.
