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Online Salvation?

The embattled newspaper business is betting heavily on Web advertising revenue to secure its survival. But that wager is hardly a sure thing.

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Even the most committed newspaper industry pessimist might begin to see a little sunshine after talking to Randy Bennett. Yes, the print business is "stagnant," acknowledges the Newspaper Association of America's new-media guru. And yes, he says, newsrooms are under pressure. But -- and here comes the sun -- newspapers have staked out a solid position on the Internet, he says. Internet revenue is growing smartly: In 2003, Bennett points out, newspapers collected a mere $1.2 billion from their online operations; last year the figure was nearly $2.7 billion. "We're growing at a double-digit rate," he says.

This is the kind of news that soothes beleaguered publishers and journalists. As print circulation and advertising swoon, the newspaper industry, and news providers generally, have looked for a lifeboat online. Newspapers were the first of the mainstream media to extend their traditional news franchises into the world of pixels, giving them an important "first mover" advantage. Web sites run by local newspapers typically remain the most popular sources of news and the largest sources of online advertising in their local communities.

Predictions about where the Internet is headed are, of course, hazardous. A dozen or so years after it began to become a fixture in American life, the Internet is still in a formative stage, subject to periodic earthquakes and lightning strikes. Google didn't exist a decade ago. Five years ago, no one had heard of MySpace. Facebook is just four years old, and YouTube is not quite three. Washington Post Executive Editor Leonard Downie Jr. compares the current state of the Internet to television in the age of "Howdy Doody."

Even so, a few dark clouds are starting to form in the sunny vista. Consider a few distant rumbles of thunder:

--After years of robust increases, the online newspaper audience seems to have all but stopped growing. The number of unique visitors to newspaper Web sites was almost flat -- up just 2.3 percent -- between August 2006 and August 2007, according to Nielsen/NetRatings. The total number of pages viewed by this audience has plateaued, growing just 1.8 percent last year.

--Newspaper Web sites are attracting lots of visitors, but aren't keeping them around for long. The typical visitor to nytimes.com, which attracts more than 10 percent of the entire newspaper industry's traffic online, spent an average of just 34 minutes and 53 seconds browsing its richly detailed offerings in October. That's 34 minutes and 53 seconds per month, or about 68 seconds per day online. Slim as that is, it's actually about three times longer than the average of the next nine largest newspaper sites. And it's less than half as long as visitors spent on the Web's leading sites, such as those run by Google, Yahoo! and Microsoft.

Many news visitors -- call them the "hard-core" -- linger longer online, but they're a minority. Greg Harmon, director of Belden Interactive, a San Francisco-based newspaper research firm, estimates that as many as 60 percent of online newspaper visitors are "fly-bys," people who use the site briefly and irregularly. "Everyone has the same problem," says Jim Brady, editor of washingtonpost.com. The news industry's continuing challenge, Brady says, is to turn "visitors into residents."

--As competition for visitors grows, news sites are rapidly segmenting into winners and losers. In a yearlong study of 160 news-based Web sites (everything from usatoday.com to technorati.com), Thomas E. Patterson of Harvard University found a kind of two-tier news system developing: Traffic is still increasing at sites of well-known national brands (the New York Times, CNN, the Washington Post, etc.), but it is falling, sometimes sharply, at mid-size and smaller newspaper sites.

"The internet is redistributing the news audience in ways that [are] threatening some traditional news organizations," concluded Patterson in his study, produced for the Joan Shorenstein Center on the Press, Politics and Public Policy. "Local newspapers have been the outlets that are most at risk, and they are likely to remain so."

Patterson suggests that some of the declines at newspaper sites may be due to increased competition from local broadcast stations, particularly TV. Although they got a late start on the Internet, local TV stations are beginning to catch up, thanks to copious video news clips and strong promotional capabilities. "A lot of papers are close to maxing out their local audiences," Patterson said in an interview. "It's hard to know where more readers will come from... They have to figure out how to deal with a pretty difficult future."

In other words, for many, that first-mover advantage has vanished.

Most ominous of all is that online ad growth is beginning to slow. Remember those confidence-building double-digit increases in online advertising revenue? They're fading, fast. In the first quarter of this year, the newspaper industry saw a 22 percent gain in online revenue. Not exactly shabby, but still the smallest uptick (in percentage terms) since the NAA started keeping records in 2003. In the second quarter, the industry rate slipped again, to 19 percent. The third quarter promises even less, considering what various companies have been reporting lately. E.W. Scripps Co. saw a 19 percent increase. The Washington Post Co. said its online revenue was up 11 percent in the period, the same as Gannett's. Tribune Co. saw a gain of 9 percent. McClatchy was almost in negative territory, with a weak 1.4 percent increase for the quarter and the year to date.

All of which begins to hint at one of the deeper economic challenges facing online news providers. Even as advertisers move from traditional media to new media, a big question lingers: Can online ad revenue grow fast enough to replace the dollars that are now being lost by the "old" media? And what happens if they don't?

At the moment, the Internet has a long way to go. Newspapers collected $46.6 billion from print advertisers last year; they took in another $11 billion in circulation revenue in 2004, the last time the NAA compiled the total. Even with the double-digit increases online, that's more than 20 times what they're generating from the Internet. Among the industry's most cutting-edge publishers, the Internet still accounts for only a fraction of the overall pie. The leading online newspaper company, the New York Times Co., derives only about 11 percent of its revenue from the Web. This fall, MediaNews Group, which publishes 57 daily newspapers, including the Denver Post and the San Jose Mercury News, touted plans to increase its share of Internet revenue to 20 percent – by 2012.

Philip Meyer, author of "The Vanishing Newspaper" and a former journalist and University of North Carolina journalism professor, believes that it's "in the interest of both newspapers and advertisers to shift content to the Internet." Advertisers get narrower target audiences for their products, he notes, and greater accountability, since they can monitor consumers' behavior. "Newspapers can at last grow their businesses without being held back by the variable costs of newsprint, ink and transportation," he said in an e-mail interview. "In the recent past, newspaper owners have preferred to cut fixed costs, like editorial staff, which gives a quick boost to the bottom line but weakens their hold on the audience. Using technology to cut the variable costs is a better strategy even though the payoff takes longer."

Shedding the big overhead costs of the old media is certainly an attraction of the new one. The problem is, an Internet visitor isn't yet as valuable as a print or broadcast consumer. The cost of reaching a thousand online readers – a metric known in advertising as CPM, or cost per thousand – remains a fraction of the print CPM. The price differential can be as much as 10-to-1, even though many newspaper Web sites now have online audiences that rival or exceed the number of print readers.

Some of this disparity is a result of the witheringly competitive nature of the Web. Unlike the print business, in which newspaper publishers generally enjoy near-monopoly status, the online news world is littered with entrants – from giants like MSNBC.com and AOL.com, to news aggregators like drudgereport.com, to blogs by the millions. This makes it tough for any online ad seller to do what newspaper publishers have done for years – keep raising their ad rates. "Ultimately, it comes down to supply and demand," observes Leon Levitt, vice president of digital media for Cox Newspapers. "And there's an awful lot of supply out there."

Harvard's Patterson offers a more intriguing, and perhaps more unsettling, theory about why it's hard to squeeze more money out of online advertisers: Web ads may not be as effective as the traditional kind. "I'm not sure [advertisers] are convinced yet about how terrific a sales tool [a Web display ad] is," he says. "The evidence isn't strong yet that it can drive people into a store the way a full-page newspaper ad can. They're less confident about what they're getting online." Moreover, unlike their here-and-gone counterparts on the Internet, print subscribers still stay around long enough to see an ad. Some 80 percent of print readers say they spent 16 or more minutes per day with their newspaper, according to Scarborough Research.

These dynamics could change, perhaps as stronger news sources emerge on the Web and weaker ones disappear. But even if the newspaper industry continued to lose about 8 percent of its print ad revenue a year and online revenue continued to grow at 20 percent a year – the pace of the first half of 2007 – it would take more than a decade for online revenue to catch up to print.

Journalists, or indeed anyone with an interest in journalism, had better pray that doesn't happen. Because online revenue is still relatively small and will remain so even at its current pace, this scenario implies years of financial decline for the newspaper industry. Even a 5 percent decline in print revenue year after year might look something like Armageddon. Newspapers were already cutting their staffs before this year's advertising downturns. A sustained frost of similar intensity would likely lead to even more devastating slashing. The cuts could take on their own vicious momentum, with each one prompting a few more readers to drop their subscriptions, which would prompt still more cuts. Some daily papers would undoubtedly fold.

Some remain confident that these dire scenarios won't come to pass. "I don't foresee [print dying] in my lifetime," says Denise F. Warren, chief advertising officer for the New York Times Co. and its Web sites. "I'm still bullish on print. It's still an effective way to engage with the audience." On the other hand, she adds, "The business model will keep evolving."

Yes, says Phil Meyer, but it may evolve in ways that render many daily newspapers unrecognizable to today's subscribers: "You want a prediction?" he says. "There will be enough ads for ink on paper to survive, but mainly in niche products for specialized situations."

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Question: Do you see a smart online business model for traditional media that will permit newspapers and other publications to continue to do deep reporting and attract talented journalists?

CRAIG NEWMARK: Not yet. While there are people working on it... no one's figured it out yet.

– From an online Q&A with Craigslist founder Newmark, posted on nytimes.com on October 10.

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To restore the industry's momentum online, executives like Denise Warren suggest the key may simply be more. More new editorial features that will attract new visitors and keep the old ones engaged on the site for longer.

The Times, for instance, expanded three "vertical" news and feature sections last year (real estate, entertainment and travel) and this year is fleshing out similar sections on business, health and technology. In early December, the paper will launch a Web version of its fashion and luxury goods magazine, called T. The paper has also stopped charging for its op-ed columns, after having determined that it could attract more readers – and hence more advertising dollars – by removing the "pay wall" that blocked unlimited access.

(The Wall Street Journal is also considering doing away with online subscriptions and moving to a free, ad-supported model, the Journal's new owner, Rupert Murdoch, said in mid-November.)

Washingtonpost.com has added more blogs, more video and special features, like a religion and ethics discussion called On Faith. In June, it started a hyper-local site-within-the-site called (LoudounExtra.com that focuses on exurban Loudoun County in Virginia. Coming next summer: a complete redesign of the site. With so much movement, Brady isn't concerned about traffic slowing down. "I'm not worried that people's interest in the Internet has peaked," he says. "There's a whole generation coming up that uses the Internet a lot more."

Cox Newspapers is focusing on its papers' local markets with freestanding niche offerings that target specific demographic groups underserved by the main newspaper, such as young mothers and pet owners and local sports fans, says Leon Levitt. The idea is to assemble a larger, geographically concentrated online readership bit by bit, with as many as seven to nine specialized publications, he says.

Harvard's Patterson has a simpler idea: Just play the news better online. His study of news sites found "substantial variation" in how local sites display news, with some pushing blogs, ads and "activity lists" over breaking news. "If local news is downplayed, local papers are conceding a comparative advantage in their competition with other community sites for residents' loyalties," the study concluded. "If national and international news is downplayed, local papers may increase the likelihood that local residents will gravitate to national brand-name outlets."

The news may be the primary product, but the way the news is served online needs to be updated, too, says Mark Potts, a Web-news entrepreneur and consultant. He says newspaper-run sites are falling behind the rest of the industry in their use of technology. "For the most part, once you get past the bigger papers, newspapers are not up to date" online, he says. "They've got some video, a podcast, some blogs, yes, but mostly...they're just pasting the newspaper up on the screen. That was barely OK five years ago." Potts ticks off the tools that news sites usually lack: social networking applications, database-search functions, mapping, simplified mobile-device delivery technology, services that let readers interact with one another, etc. His one-word description for the state of newspapers online: "Stodgy."

On the ad side, traditional news organizations are starting to join, rather than trying to fight, some of the Internet's giants. In recent months, major newspaper companies have struck alliances with Yahoo! and Google in an attempt to pair newspapers' strength in selling local advertising with the search engines' superior technology and national reach.

In the first phase of a multipart alliance, some 19 newspaper companies that own 264 daily papers have linked their online help-wanted advertising to Yahoo!'s HotJobs recruitment site. When an advertiser seeking to hire, say, a nurse, in St. Louis buys an ad through the St. Louis Post-Dispatch, the newspaper places the ad on its site, which is co-branded with HotJobs and automatically linked to HotJobs' national listings. As a result, the advertiser gets his message in front of both local job candidates and others across the country. HotJobs, in turn, gets a local sales agent – the Post-Dispatch – to sell more listings. Although the partners have revealed few financial details about the arrangement, revenue from such ads is split between the newspaper and Yahoo!, with the newspapers taking a majority of each dollar generated.

In a second phase of the alliance that is now being tested, publishers such as McClatchy, Lee Enterprises, Media General, Cox and others will attempt to do something similar with display ads. Using Yahoo!'s search capabilities and technology, the companies hope to marry national and local display ads to their visitors' interests. People interested in, say, pickup trucks (as identified by tracking software and registration questionnaires), would likely see national ads for Ford, and perhaps for local Ford dealers, when they logged on to a newspaper's site. Such highly targeted advertising would command much higher CPMs than plain old banner ads, says Cox's Levitt.

While it's still too early to declare victory, the general scheme of the partnership has drawn praise from Wall Street. Deutsche Bank analyst Paul Ginocchio has estimated that some members of the consortium could see online ad growth rates of 40 percent for the next two years, thanks in large part to revenue generated by the Yahoo! tie-in.

However, other publishers have declined to join the Yahoo! consortium, in part out of concern that newspapers may be giving away too much to Yahoo! and leaving readers little reason to visit the newspapers' own sites. For example, Gannett and Tribune Co. are developing a display advertising network of their own.

Another group of publishers, including Hearst, E.W. Scripps and the New York Times Co., have turned to Google. Under an experimental program that was expanded this summer, Google is running auctions that enable thousands of smaller advertisers to bid on ad space – size, section and date of their choosing – on some 225 newspaper Web sites. The newspapers are free to accept the offer, reject it or make a counteroffer (Google says more than half the bids have been accepted). The process is streamlined by Google's technology, which automates billing and payments.

A little less cooperation might help, too. Some argue that news providers made a huge strategic mistake when they decided to make their content available to others online. "Free riders" like Yahoo.com, MSN.com, Google and AOL.com have built massive franchises – far larger than any traditional mainstream news site – in part by posting news stories created and paid for by others. These days, of course, anyone can assemble a series of links and headlines to become a "news" site. The Shorenstein Center put it bluntly in its recent study of news on the Internet: "The largest threat posed by the Internet to traditional news organizations...is the ease with which imaginative or well positioned players from outside the news system can use news to attract an audience."

"It's a terribly unfair deal," says Randy Siegel, the publisher of Parade, the weekly newspaper magazine. "Newspapers need to negotiate a more equitable share with search engines that are making billions of dollars by selling ads around newspaper content without the costs of creating that content.... The book industry and the movie industry don't give their content away."

Arkansas Publisher Walter Hussman Jr. knows he sounds like a man from another century when he says it, but he thinks newspapers shouldn't be free, online or off. He rues the day that the Associated Press, which is owned by the newspaper industry, agreed to sell stories to the Yahoos and AOLs of the world. Free or bargain-priced news, Hussman says, cheapens everyone's news. Free, he says, "is a bad business model."

Hussman has an idea that's so old and abandoned it seems almost new: Make people pay for the news they want, even in the Internet age. Hussman obviously is swimming upstream with this notion. Not long after the New York Times stopped charging for its op-ed columns under the now-jettisoned TimesSelect initiative, the Sacramento Bee dropped subscription fees for Capitol Alert, the paper's Web site for political news.

The newspaper Hussman publishes, the Arkansas Democrat-Gazette in Little Rock, is one of the few that charge a fee ($4.95 a month) for full access to its site. The site has a modest base of 3,000 subscribers, but Hussman says walling it off protects a more lucrative franchise: the newspaper. He believes it's no coincidence that the Democrat-Gazette's print circulation is growing – about 2,000 daily in the latest six-month period that ended in September – at a time when so many others are sliding.

But what about the ad revenue that the newspaper is giving up with such a restricted Web site? Hussman says ad rates are so low online that they often don't cover the cost of producing original journalism. Example: An online gallery of photos from a local high school football game might generate 4,000 page views. If an advertiser paid $25 for each thousand views – a premium figure, by the way – the photo feature might generate $100, barely enough to pay the photographer for his work.

"I know what I'm saying is going to sound too simplistic to some people, but it seems to be working," he says. "The reason I advocate this is not some ideological or esoteric reason or because of pride of authorship. I'm basing this on experience."

Hussman sees an industry that generates nearly $60 billion a year in print ad sales and subscription fees, and that supports the expenditure of roughly $7 billion a year on newsgathering operations, and worries about it all slipping away in an era in which news is so abundant – and so free. "It would be wonderful if someone could figure out a way" to do all that online, he says before concluding, "but I just don't see it now."

Paul Farhi is a Washington Post reporter who writes frequently about the media for the Post and AJR. He has written about the San Francisco area's news blues, hyperlocal news Web sites and the business magazine Portfolio in recent issues of AJR.

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