AOL seeks new edge in Silicon Valley

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Brad Garlinghouse, AOL Inc.'s executive overseeing operations in Silicon Valley, inhabits a windowless office at a former Netscape data center. But Garlinghouse's sparse surroundings -- the University of Kansas graduate has decorated with little more than a framed "Sports Illustrated" cover featuring his alma mater's basketball team -- betray their temporary status.

As AOL completes layoffs that will eliminate a third of its employees worldwide, the company is eying both an expansion and a new home in Silicon Valley, in hopes of tapping the area for expertise and inspiration. Garlinghouse said local employees should increase to 350 from 200 by the end of the year.

Through a newly established venture-capital arm, Garlinghouse said AOL also plans to invest in up to eight promising, early stage start-ups over the period.

Though based in New York, AOL has a history in Silicon Valley. The expansive former headquarters of Netscape, a doomed Internet browser company that AOL bought in 1998 for $4.2 billion, sits down the street from Garlinghouse's current location.

AOL may be seeking a bigger space in Silicon Valley, but Garlinghouse said the old Netscape facility wouldn't be appropriate for a company looking to exorcise ghosts of the past.

"AOL is a different company than even a few months ago," Garlinghouse said. "Part of rejuvenating AOL overall means having a stronger West Coast presence, and being more deeply tapped into not just the talent base that's here, but also the entrepreneurial and start-up community."

In that sense, AOL's local starting point is appropriate. Garlinghouse's office is also a short walk, in the opposite direction of the old Netscape offices, from the site of a factory once used to produce chips for Fairchild Semiconductor. Fairchild, a seminal company founded in the 1950's, helped transform the area from agricultural hub to technology and innovation center.

"The culture we're trying to create is that of a big, well-funded start-up," Garlinghouse said. "We need to do things differently, we need to take chances, we need to change our culture and we need to be nimble."

Following a disastrous merger with Time Warner Inc. a decade earlier, AOL was spun off to shareholders in December. Once best-known for its Internet access business, the company now is trying to distinguish itself with online services, content and advertising.

To be sure, it faces considerable challenges.

Google Inc., which has its headquarters on the other side of U.S. 101 in Mountain View, acquired a 5 percent stake in AOL for $1 billion in 2005 -- only to sell it back last year for $283 million.

In financial disclosures made by Time Warner before it spun AOL out, it reported that the unit saw online advertising sales fall 18 percent in the third quarter that ended in September, while shedding 400,000 subscribers in the period. AOL has relied on its subscribers, as a captive audience for its online offerings.

Wall Street analysts expect AOL to report fourth-quarter revenue of $764 million when it posts results on Wednesday, according to Thomson Reuters data. That's a little more than half of the $1.26 billion in net revenue recently reported by rival Yahoo Inc. for the same period.

AOL's strategy of focusing on specific Internet content subject "verticals" including sports and music has a reasonable chance at success, according to Citigroup analyst Mark Mahaney. "They have a shot at this, just as decent a shot as anyone else," Mahaney said.

Garlinghouse, a former Yahoo executive, said AOL aims to use its status as an underdog to its advantage.

"There are a lot of interesting things we can do that take advantage of the fact that we're not number one," he said. "We can do things that are a little bit more disruptive, a little bit more entrepreneurial, and take a few chances that are harder to take when you're the biggest player out there."

Garlinghouse garnered a lot of public attention at Yahoo, when he wrote an internal memorandum criticizing the company for spreading itself too thinly across multiple areas. The memo was later leaked to the press and became known as the "Peanut Butter Manifesto." Garlinghouse left Yahoo in 2008, and joined AOL last fall.

Part his job now also includes overseeing a venture capital group, tasked with investing in start-ups that could help contribute to AOL's innovation.

AOL Ventures plans to invest in seed or early-stage rounds in between four and eight start-ups by the end of this year, Garlinghouse said.

AOL Ventures is an initiative spurred by AOL CEO Tim Armstrong, a former Google executive who took the top job last year. Armstrong valued Silicon Valley's start-up culture, Garlinghouse said, and wants AOL to tap into it. "AOL over the years I think had become increasingly apart from that," Garlinghouse said.

Now, with "almost all" of AOL's job cuts and restructuring behind it, Garlinghouse said he can better focus on expanding his outpost. "For parts of AOL, the center of gravity is absolutely the East Coast," he said, "but for other parts of where AOL is going, the center of gravity will absolutely be the West Coast."