Google's 4Q disappoints as advertising prices sink (Update)

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In this Jan. 17, 2012 photo, a sign for Google is displayed behind the Google android robot, at the National Retail Federation, in New York. Google Inc., releases quarterly financial results Thursday, Jan. 19, 2012, after the market close. (AP Photo/Mark Lennihan)

What was supposed to be a celebration of the most prosperous quarter in Google's 13-year history instead turned into a major letdown.

The disappointment sunk in Thursday after Google's fourth-quarter earnings report showed the Internet search leader fetched less money per click on its ubiquitous online ads.

That came as an unsettling surprise because investors had assumed a surge in online holiday shopping in the U.S. would enable Google Inc. to charge more for its ads. Instead, the average price decreased by 8 percent from the same time in 2010.

Google executives traced part of the decline to technical changes aimed at delivering more ads that attract people's interest. Those tweaks apparently paid off as the total clicks on Google's ads increased 34 percent from the previous year.

Most of the trouble seemed to be rooted in Europe, where government debt woes are hurting the economy, said Benchmark Co. analyst Clayton Moran. "I think everyone underestimated how quickly the European online ad market would suffer."

The weakening euro also converted into fewer dollars during the quarter, another factor that undercut Google.

It all added up to a dramatic slowdown in Google's earnings growth that alarmed investors. Net income edged up just 6 percent from the same October-December period in 2010, coming off year-over-year increases of more than 25 percent in each of the previous two quarters.

Google shares plunged $57.67, or 9 percent, to $581.90 in extended trading after the results were announced.

The showing could renew Wall Street concerns about Google's moneymaking prowess under the direction of co-founder Larry Page, who replaced Eric Schmidt as CEO last April. Page took the job with a reputation for being more willing to invest in long-term projects at the expense of short-term profits. In the latest quarter, Google's operating expenses rose 34 percent from the previous year, outpacing a 25 percent increase in revenue.

If Google's stock falls as sharply during Friday's regular trading as it did in Thursday's extended trading, the shares will be worth slightly less than they were when Page became CEO.

Even before the deceleration in Google's fourth-quarter earnings, analysts have been fretting that the company's proposed $12.5 billion acquisition of cellphone maker Motorola Mobility Holdings Inc. will crimp profits. The deal is still awaiting approval from regulators in U.S. and Europe.

Buying Motorola is part of Page's push to expand Google's empire beyond the dominant Internet search engine that generates most of the company's revenue. Much of the money is being poured into Google's Android software for smartphones, its Chrome web browser, its YouTube video site and a social networking service called Plus that is being quickly built to challenge Facebook.

Page, 38, made it clear he sees no reason to change what he has been doing so far. "I am very happy with our results overall in the quarter," he told analysts during a Thursday conference call.

More people probably would have shared in his ebullience if not for the curse of great expectations.

With more people than ever before shopping for holiday gifts and bargains on computers and mobile devices, Google was supposed to scale new financial heights in the October-December period.

Analysts had forecast Google would earn $3 billion for the first time during any three-month period since the company's 1998 inception. Instead, Google made slightly less money than it did a quarter earlier.

The company earned $2.7 billion, or $8.22 per share, in the fourth quarter. That compared to net income of $2.5 billion, or $7.81 per share, at the same time in 2010.

The most recent quarter included an $88 million charge to account for the diminished value of a $500 million investment that Google made in wireless network provider Clearwire Corp. in 2008. Google had previously absorbed a $355 million charge on its Clearwire investment.

If not for costs covering employee stock awards, Google said it would have earned $9.50 per share. Analysts surveyed by FactSet had expected $10.51 per share.

Revenue totaled $10.6 billion, up from $8.4 billion in the previous year. It's the first time Google's quarterly revenue topped $10 billion, but even that figure fell shy of analyst projections.

After subtracting ad commissions, Google's revenue totaled $8.1 billion. That was about $300 million below the average analyst forecast. Revenue would have been about $240 million higher had exchange rates in Europe remained steady with the third quarter's rates, according to Patrick Pichette, Google's chief financial officer.

While investors fixated on Google's falling ad prices, Page hailed the inroads the company is making beyond the Internet search engine that brings in most of its revenue.

The Plus service that Google introduced seven months ago now has more than 90 million users, Page said. That's more than double the approximately 40 million users of three months ago. Facebook still has a big lead with more than 800 million users after nearly eight years in existence.

About 80 percent of Plus users visit the service at least once a week, according to Google. The company is trying to increase the frequency by including recommendations about Plus accounts in its search results, a recent change that has raised questions about whether Google is abusing its position as the Internet's leading gateway to unfairly promote its own services over its rivals.

Page is hoping Plus can be as successful as Google's Gmail service, which now has 350 million accounts, and the Android software, which is now running on 250 million smartphones and other devices, according to numbers the company released Thursday.