

Monday, January 30, 2006

The bubblelicious benchmarks of ROI in Google

For amusement I have been watching the share price of Google for awhile now. I remember being taken aback at the lunacy of it all when I heard the CNBC cheerleading squad call for \$400 back when it was still in the \$200 range. Well, it's been trading above \$400 for quite some time now and the other day on a long car drive I did some back-of-napkin calculations to compare what gives you the greatest ROI from Google.

First, some review (at least I hope this is review

The object of investing is what? It is to obtain an adequate return on capital commensurate with the risk.

Why does one buy a stock? Trick question. Most people will say "to sell it a higher price", buy low, sell high, etc. This is why most people buy stocks, and in case you didn't notice, most people lose money in the stockmarket.

You buy a stock to gain ownership in a business, and thus to partake in a portion of its earnings.

Circling back to the top and closing the loop: you make investments in order to generate returns on those investments.

Remember that as we work through the following:

Google's AdSense program is truly ubiquitous across the internet. Nearly everybody has those contextual text ads on their websites and they are a true bonanza for content and forum related sites. Some people are making truly stupendous amounts of money monthly from AdSense revenues.

Take a website that earns a steady \$25/day in AdSense (I know a modest website that does this much and its far closer to the bottom end of the ladder than the top). That's \$750 month, or \$9,000 a year in income. Lets figure \$100/month for a server and bandwidth, you're looking at net \$7,800 annually in free cashflow, paid monthly out of Google and to the website owner.

Now, Google is currently trading at a p/e multiple of about 95 (!). So it's earning about \$4.50 share. Divide 4.5 into 7,500 to arrive at the number of shares of Google you would need to own to get the same earnings = 1,666. You would need to own 1,666 shares of Google to derive the same earnings as our hypothetical website earning \$25/day via AdSense. 1,666 shares of Google would cost you \$713,731 on the open market today.

Which gives you the better ROI? Owning shares in Google or owning a website that earns income via Google AdSense?

Consider that there is a fairly liquid marketplace for revenue generating websites and current valuations are anywhere between 1 to 5 years' revenues. Even at the top valuation, you should be able to buy an established revenue generating website earning \$25/day for around \$40,000.

I think this may be the internet equivalent of the "inverted yield curve" as we see an alternate method to extract cold hard cash out of a company trading at nearly 3-digit earnings multiple that doesn't even pay dividends.

Posted by Mark Jeftovic in Living off the net at 13:57

\$25/day for around \$40,000...this is not true, a \$25/day website you will easily find on auctions for around \$5000
Anonymous on Jul 27 2006, 03:57