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Piper Jaffray & Co.

Related Companies:	Share Price:
GOOG	414.69
YHOO	29.00

Yahoo! Inc. (YHOO - $29.00)

Outperform — **Volatility: Low**

Technology

Yahoo Expects Low End of Q3 Guidance; Sell-off Creates Buying Opportunity

KEY POINTS:

- Q3 tracking towards the bottom end of guidance range
- Weakness attributed to search & branded (auto & finance)
- Automotive weakness is likely a short-term seasonal effect
- Panama investment likely impacting NT monetization
- Sell-off creates buying opportunity for Yahoo as well as other online ad names (GOOG, AQNT, VCLK, TFSM, WSSI)

- **Q3 Tracking to Low End of Guidance**. Yahoo indicated today at a conference that Q3 was tracking towards the low end of guidance ($1,115M-$1,225M in revenue and EBITDA of $445M-$505M) with weaker than expected advertising spend from both search and branded (automotive and financial services sectors). We currently estimate revenue of $1,170M and EBITDA of $477M, both near the midpoint of guidance.
- **Auto Advertising Slowdown Appears to Be Short Term.** Our discussions with a major auto advertising services firm suggests that there was a slowdown in new car launches in Q2 and Q3, which could have a modest impact on Yahoo's Q3 revenues. That said, our discussion indicated that there should be a significant increase in new car launches in Q4 and 1H07. Additionally, we believe there was increased advertising activity for employee discount pricing in the summer of 2005 which did not repeat this year. Hence, we believe the slowdown in auto advertising referenced by Yahoo is primarily a seasonal effect and we would expect a reacceleration in Q4 and 1H07. Our discussions also indicated that we are not seeing any material slowdown in online spending by the auto companies on an annual basis – our checks indicate 30%-35% growth expectations for 2007.
- **Panama Investment Could Be Impacting Near-Term Search Monetization.** Our checks with online search advertisers and SEMs indicate that Yahoo may have lost some ground in search monetization in Q3 as engineering resources were pulled from incremental enhancements in order to work on the company's upcoming Panama search platform release. That said, we believe the concerns over Panama are priced into shares and Yahoo should resume monetization improvements with the release of Panama in Q1.
- **Sell-Off Creates a Buying Opportunity.** We believe the Yahoo sell-off following updated guidance creates a buying opportunity for Yahoo shares as well as other online advertising companies (GOOG, AQNT, VCLK, TFSM, WSSI). Yahoo currently trades at 9x our current 2007 EBITDA despite conservative EBITDA estimated growth of 23%. We maintain our Outperform rating and believe investors with a 6 month or longer time horizon should benefit as Yahoo rolls out its Panama platform in Q1 and expected continued strong growth in branded advertising.

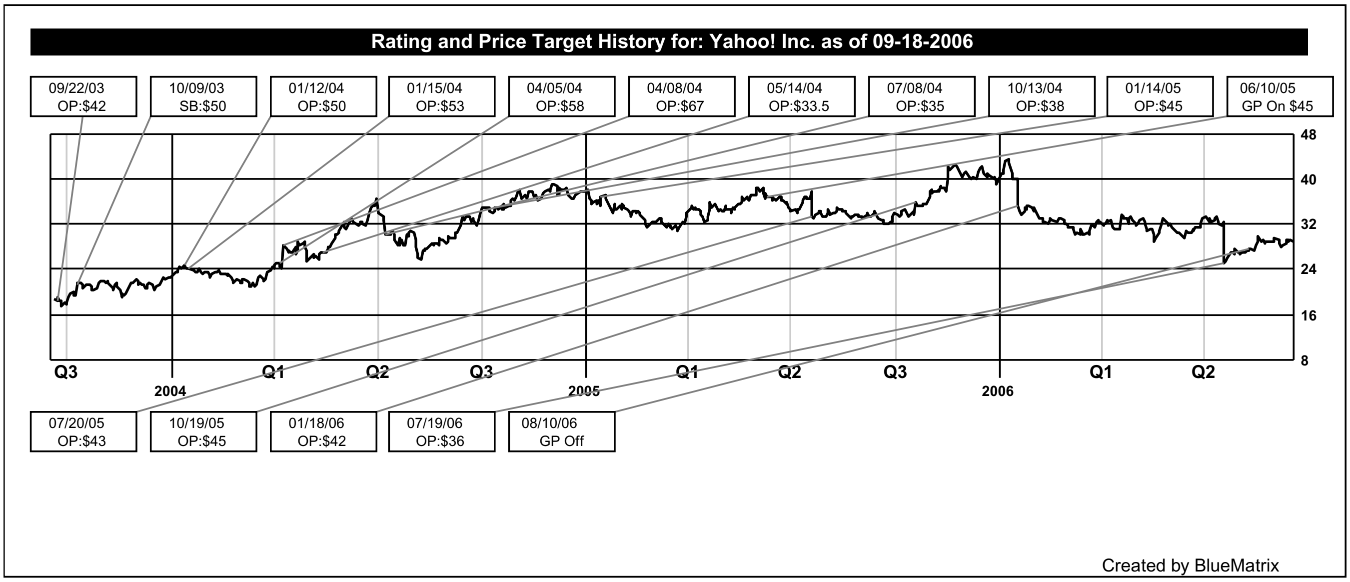
PRICE TARGET AND JUSTIFICATION:

Our Price Target is $36, based on 15x 2007E EBITDA.

RISKS TO ACHIEVEMENT OF TARGET PRICE:

Risks include competition, slowdown in advertising, failure in new market segments, and poor execution.

Important Research Disclosures



Notes: The boxes on the Rating and Price Target History chart above indicate the date of the Research Note, the rating, and the price target. Each box represents a date on which an analyst made a change to a rating or price target, except for the first box, which may only represent the first Note written during the past three years.

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I: Initiating Coverage

D: Discontinuing Coverage

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R: Resuming Coverage

T: Transferring Coverage

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OP: Outperform

MP: Market Perform

UP: Underperform

NA: Not Available

UR: Under Review

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Piper Jaffray

			IB Serv./Past 12 Mos.	
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SELL [UP]	24	4.02	3	12.50

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Important Research Disclosures

Analyst Certification — Safa Rashtchy, Sr Research Analyst
— Aaron M. Kessler, Sr Research Analyst

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- **Outperform (OP):** Expected to outperform the relevant broader market index over the next 12 months.
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- **Suspended (SUS):** No active analyst opinion or no active analyst coverage; however, an analyst investment opinion or analyst coverage is expected to resume.

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- **Low:** The stock price has moved up or down by more than 10% in a month in fewer than 8 of the past 24 months.
- **Medium:** The stock price has moved up or down by more than 20% in a month in fewer than 8 of the past 24 months.
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