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The path to social network riches

By Mason Wiley

Advertising on social networks can be very expensive -- with little payoff. Here's an easy solution to this cost problem.

Social networks are commanding attention -- for good reason. Millions and millions of people visit them daily (and to many an employer's chagrin, hourly). Given the sheer number of users and their length of stay, the big social networking sites like MySpace, Facebook and others should be an advertiser's paradise. But they're not -- yet.

Ironically, the huge number of impressions generated by social networks poses challenges for advertisers. For example, buying all those eyeballs on a cost-per-thousand (CPM) ad model can be prohibitively expensive for many. And unlike sites centered around a specific interest, social networks attract so many different types of people that targeting is difficult. Behavioral targeting offers promise, but hasn't yet evolved to the point at which it can guarantee a positive ROI.

A new ad model has emerged that can. The cost-per-acquisition model (CPA) provides advertisers with a guaranteed way to ensure ad efficiency, while also opening the door for social networks to monetize more of their traffic.

The benefit of CPA for advertisers

The CPA model is ideal for social networking sites because it eliminates virtually all the risk for advertisers of buying on a CPM basis. As a performance-based model, advertisers pay a fee only for the results their CPA campaign generates. That result can be any transaction specified by the advertiser. For example, an advertiser places a CPA campaign on ESPN.com. Rather than paying for all the people who see that ad, the advertiser only pays the publisher for each user that not only clicks on the ad but also follows through and completes the desired action as defined by the advertiser -- anything from an email submit or qualified lead to a sale or paid membership.

Through its 1:1 ratio of pay-per-action, CPA changes the rules for advertisers. The need for narrow targeting to eliminate ad waste becomes irrelevant since there is no waste. Similarly, there's almost no possibility for click fraud since advertisers only pay for results. And unlike CPM, the results of a CPA campaign are directly verifiable through tracking technology, which enables advertisers to determine which ads convert and which do not. For example, an A/B test of landing pages can be measured against the actions completed via any number of creatives or landing pages as well as the conversion processes. The path to purchase is easily tracked back to the source, including the placement of the original creative.

But the single greatest appeal of CPA for advertisers is that it is performance-based. With advertising costs directly tied to results, it provides them a way to advertise with full accountability and control. Advertisers simply establish the actions -- signups, sales, leads, etc. -- they want to reward, and establish how much they're willing to pay. If online publishers think the campaign will generate sufficient response with their audience base to meet revenue goals, they can choose to run the campaign.

Certainly, by running campaigns based on the promise of a potential future reward, publishers are taking a risk. But given that CPA campaigns are more aggressively focused on generating response than the many revenue-sharing campaigns available, it's a gamble that has been paying off for them. Now, social network publishers are finding that CPA can pay off for them, too.

The benefit for social networks

Like any publisher site, social networks want to maximize advertising revenue. Cost-per-thousand is the most prevalent model they use to do it, and it seems to make sense because CPM focuses on the number of impressions generated -- and these sites generate a lot of them. The problem is that these impressions come from an incredibly broad cross-section of the population, many of which can be irrelevant to a given advertiser. As mentioned above, although these sites generate billions of impressions, targeting the right ones is challenging. While targeting users based on where they have clicked (behavioral targeting) can help improve the odds, it is by no means an exact science or a guarantee that a sufficient number of users will perform the desired action.

These inherent challenges under the CPM model have limited the appeal of social networks for advertisers. The result has been a tremendous surplus of excess inventory that despite all best efforts just can't be sold. And a lot of those billions of impressions have gone un-monetized. But now that's changing thanks to CPA.

With CPM, the advertiser assumes the risk by paying the publisher for uncertain potential results. In CPA the publisher assumes the risk by running ads for uncertain potential payments. But when its remnant inventory at issue, the publisher runs no risk; it is inventory that would otherwise go unsold. So it only stands to reason that a social networking site will make more money running CPA ads on remnant inventory than it can just selling space based on CPM alone.

Conclusion

The CPA model is not new, but it has evolved to be a highly cost effective way for advertisers to use social network sites, and an effective way for social networks to generate increased revenue. And new widgets and applications are emerging for social networks that can make CPA even more powerful in the future.

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