Why Yahoo's troubles reflect bigger problems for media

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Two years into Marissa Mayer's tenure as Yahoo's chief executive, there are still big questions about the direction of the company. It's hard to sum it up better than the following chart, which shows that the estimated value of the company's stake in Chinese Internet Company Alibaba is worth nearly as much as the company's entire market cap.

Yahoo has the same problem that many other media companies – newspapers included – are facing: how to make money selling online ads on desktops and on mobile devices.

Even for those who don't give a hoot about Yahoo – or the legacy of Marissa Mayer – the company's woes reflect an important shift in consumer habits. Now, people use mobile devices to look things up. And tiny mobile ads are even less lucrative than the big ones that splash across computer screens.

Yahoo is particularly vulnerable. Google has recently been making less money off each ad its sells, but its volume offsets any falloff in the value of each ad. That's given it time to develop better mobile ad products; a report from Adobe reports that Google's actually now seeing modest per-click revenue growth after years of stagnating. Microsoft's Bing division is struggling with the same issues, too, but it's just one division in a very diverse company (albeit one that just laid off 14 percent of its employees.)

Yahoo has no such fallback plans – and it's starting to really show in its earnings reports. Total revenue last quarter fell three percent to $1.04 billion. That's despite a 100 percent increase in Yahoo's fledgling mobile display and mobile search ads, which simply don't provide enough money to combat the shift from desktop ads to cheaper mobile ads. Overall, search revenue actually ticked up 6 percent, but the company was dragged down by sliding revenue in the display ads, which dropped seven percent to $394 million.

Since the earnings report, shares have dropped nearly 6 percent, to just under $34 per share, as grim information about Yahoo's core business has started to sink in.

In fact, the brightest spot in the earnings report was the announcement that Yahoo will be able to hang on to 68 million more shares of Alibaba stock, post-IPO, than originally thought. That's hardly an endorsement of Yahoo's core business.

To Mayer's credit, she's taken on a tough job. She was Yahoo's fifth CEO in four years in 2012, after a long period of mismanagement and dithering over whether the company was a media, tech or advertising firm. As she's settled in to her role, she's articulated a vision of Yahoo as a company that's essentially all three: a company that makes money off of good apps filled with good content.

To that end, she's built out the company's news and video catalog, striking deals to get exclusive rights to historic episodes of Saturday Night Live, and hiring Katie Couric to lend some star power. She's built up her tech talent roster, by way of a $1 billion purchase of Tumblr and deals with dozens of startups that have added of young entrepreneurs to Yahoo's ranks. And she's focused heavily on improving Yahoo's mobile presence, with a suite of well-received apps and a new system for selling mobile advertising.

But so far the rebuilding efforts, ambitious as they are, haven't balanced out the downward trends in Yahoo's core search and desktop advertising business. To date, the apps have been more about getting Yahoo back onto the average consumer's radar than a major revenue play. Mayer tellingly talks about active users rather than revenue when touting app success.

It's too early to say Yahoo's doomed, by any means. Mayer's definitely managed to change the conversation around Yahoo, casting it as a comeback kid rather than a dying dinosaur. And it continues to be the subject of fascination. Merger speculation caught fire after reporters saw Mayer and AOL chief executive Tim Armstrong deep in conversation last week.

But Yahoo's troubles only reinforce that selling online and mobile ads is tough business these days – and that the company's substantial stake in Alibaba is easily its brightest spot.

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