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HEADLINE: The Search Engine That Isn't a Verb, Yet

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BODY:

IN July 2001, three months after Terry S. Semel, the former Warner Brothers studio co-chief, took over as chief executive of **Yahoo,** he excitedly called a news conference with Sir Howard Stringer, the chairman of the Sony Corporation of America. The past and present movie moguls described in glowing but vague terms a new partnership. Sony would buy some advertising on **Yahoo, and Yahoo** would help Sony develop a new Web site.

''We're not quite married,'' Sir Howard told reporters, hinting at possible closer ties between the companies in the future. ''But at least we're holding hands.''

Mr. Semel is not flirting with media companies anymore. Yes, Sony is still an advertising client, but there is little more to the relationship than that.

In a world where movie studios, record labels and television networks are fought over like so many poker chips, Mr. Semel simply doesn't want to play that game. The company refuses to answer questions about whether Mr. Semel might be tempted to return to Hollywood to run a mainstream media company, like Walt Disney, or otherwise become caught up in the takeover battle between Disney and Comcast.

Yahoo's future, Mr. Semel says, is almost exclusively on the Internet and, even at the age of 60, he wants to be part of it. ''I love what I do,'' he said last week. ''I didn't need a job when I came here. I wanted the opportunity to help build a great company. And we have only taken the first steps.''

The next steps could be among his most challenging. Under Mr. Semel, Yahoo has become a big hit on Madison Avenue, with advertising revenue surging ahead of its traditional rivals, America Online and Microsoft's MSN. Yahoo now has about 70 of the top 100 national advertisers as clients, so it no longer bothers to announce new ones -- let alone hold news conferences with their chief executives.

But now Mr. Semel must win over a tougher audience: Silicon Valley. In many ways, Yahoo's main rival is Google, started five years ago by two brainy Stanford graduate students who believed, against conventional wisdom, that sophisticated computer science could produce better Web searches.

They were right. Google has become not only a verb but also a profitable company with a reported $1 billion in sales. It is expected to be the hottest initial public offering this year. And now Google is preparing to offer a free e-mail service, people close to the company said, in a bid for Yahoo's most important source of loyal customers.

Mr. Semel, meanwhile, inherited a Web search business that was largely a Potemkin village. Yahoo was founded in 1994 as a directory of cool Web sites, but most users considered it a search engine. The company, however, saw itself more as a place that packaged experiences for consumers and sold ads. So it had other companies do the hard technical work of indexing billions of Web pages, which is what search is all about. That led Yahoo, before Mr. Semel arrived, to hire Google, unwittingly giving its future rival crucial early exposure.

Mr. Semel soon realized that the company had helped create a monster. So he has spent $2 billion trying to assemble his own Google, buying Inktomi, the Web search software company, and Overture Services, the pioneering seller of search advertising.

Last week, Yahoo finally replaced Google's search results with its home-brewed search engine, which uses a robot, called Slurp, to read Web pages. Experts say Yahoo's new search engine is credible and roughly comparable to Google's. And more important, Yahoo appears committed to the sort of engineering work that is needed to improve the quality of Web searches.

''THE playing field is much more level now, and both companies will go full-tilt boogie to retain the crown in search innovation,'' said John Battelle, who is writing a book on Web search and was a publisher of The Industry Standard, the magazine that was once the voice of the dot-com boom.

Mr. Semel says the new search engine is just the beginning of a rapid series of improvements to Yahoo's search capabilities. Many of these, he says, will try to exploit Yahoo's two main advantages over Google -- its vast array of original content and a database with information about its 133 million registered users. Knowing where searchers live and what their interests are, Yahoo believes, will let it present results that are more relevant and advertising that is more focused.

In addition, he is turning his attention to Yahoo's specialized areas, like finance and music, which he plans to bolster through a series of major product introductions and acquisitions over the next year. ''I don't think we sleep a lot,'' he said two weeks ago, sitting in one of Yahoo's nearly identical purple conference rooms. ''This has to be a year of great growth.''

In Hollywood, Mr. Semel was considered the least showy mogul of show business, preferring to tend to the business of Warner Brothers in the background. When he arrived at Yahoo, in the spring of 2001, he methodically reigned in the company's bubble-fed frenzy to be everything to everyone online.

He has also tried to insulate Yahoo from the vicissitudes of the advertising market by creating products that consumers will pay for, but so far he has found few. He talked at first of charging fees for premium versions of the company's major categories, like news and sports. Research showed that there was not much demand there, and the idea was dropped.

Last year, Yahoo introduced a $9.95-a-month online video service called Yahoo Platinum, with a mix of news, sports and entertainment. It was a flop and closed down.

The company, however, has been quite successful in a few subscription services. Merrill Lynch estimates that Yahoo had revenue of $52 million last year from its online personal ads, $33 million from its premium e-mail product and $62 million from services for small businesses.

Mr. Semel said it would take time for people to become accustomed to paying for online services. ''In the early days, like in cable, people want basics, like extra e-mail storage, and maybe fantasy sports,'' he said. ''They aren't looking for complex packages.''

But Mr. Semel came up with a way to increase fee income without having to sell services, one customer at a time. He persuaded SBC Communications to include a bundle of Yahoo services, including e-mail, with its high-speed Internet service. SBC pays a fee of $2.10 a month for every customer on the service, according to Merrill's estimate.

That is not as big a business as the Internet service run by America Online and MSN, but the profit margin for Yahoo is high, and the SBC-Yahoo subscriber base is growing while that of its larger rivals is shrinking. Yahoo has worked out similar deals with British Telecom and Rogers Cable in Canada.

Even so, Mr. Semel has thrown out his initial goal of earning half the company's revenue from fees and is enjoying a wild ride as online advertising rebounds.

Wenda Harris Millard, an ad sales veteran who joined Yahoo to run its advertising sales just as Mr. Semel took the helm, is widely credited with helping Yahoo win back advertising agencies, which had grown disenchanted with online advertising after the dot-com crash. She sponsored seminars and research projects that helped advertisers understand how to best use the young medium. And Yahoo, like other online media companies, allowed advertisers to have bigger, more interactive advertising formats.

''When I talked about online advertising, everyone looked at me a little cross-eyed a few years ago,'' Mr. Semel said. ''We felt if we got really good at doing what advertisers wanted, we could take share from others with any uptick in the market.''

Jordan Rohan, an analyst at Schwab Soundview Capital Markets, estimates that Yahoo's nonsearch advertising grew by 22 percent in the fourth quarter of 2003, twice the rate of other specialized content sites. Many of Yahoo's key pages, like its home page and its main movie page on Thursday nights, are regularly sold out. Mr. Semel said that the rates it charges for nonsearch ads increased about 20 percent last year.

ULTIMATELY, Yahoo wants to take share not from other online sites but from television and other traditional media. Of all the time people spent last year using media, 4.9 percent was on the Internet. But online advertising represented only 2.3 percent of all advertising. ''Advertisers are looking to get out of the broken model of television,'' Ms. Millard said. ''They want to find the men between 18 and 34. We have them on Yahoo.''

While Yahoo's main advertising business rebounded by making ads bigger and more intrusive, it is having even more success with search ads, which are small, text only and unobtrusive. This sort of search advertising, invented by Overture's predecessor, Goto.com, is easy to sell, even to the smallest businesses. Overture says it has 100,000 advertisers, and Google claims 150,000, most of whom entered the ads themselves on a Web site, associated them with search terms and paid with a credit card. The advertisers bid for a prominent ad placement for a certain search term, and then pay that rate each time a user clicks on the ad.

Indeed, both Overture and Google have an enviable problem: advertisers are willing to pay for far more clicks than there are clicks to go around. So Google has been moving aggressively beyond search sites to place its ads on news and information sites, using computers to pick which ads relate to each page displayed. Overture was much slower to strike similar deals, but it is working to place its ads on various parts of the sprawling Yahoo service.

But for Mr. Semel to get real value from his $2 billion investment in search companies, he will have to make Yahoo's search product so good that people stop associating search with one word: Google.

THAT won't be easy. For the moment, it is enough that Yahoo has become a credible alternative, argued Jeff Weiner, a protege of Mr. Semel's from Warner Brothers who now runs Yahoo's search unit. ''You have a second player now,'' he said. ''If you go to Google and you didn't find what you want, you have somewhere else to go.''

Of course, Yahoo isn't done, and Mr. Weiner said that there would be a series of improvements to the search system in coming months. Many of them take advantage of its data about users.

''Personalization will ultimately change the way search is delivered,'' Mr. Weiner said. In particular, he hopes that by watching users over time, the search engine can guess what sort of information they are looking for -- or, as he put it, ''If you type in flowers, do you want to buy flowers, plant flowers or see pictures of flowers?''

Another plan is to create search systems for Yahoo's specialized areas, like finance, jobs and travel. Last fall, the company introduced a highly regarded search service in its shopping channel that lets users specify prices, brands and product attributes. Each specialized search engine, of course, also creates opportunities for specialized advertising.

The biggest new advertising opportunity is in searches related to merchants and other information in a local area. Yellow-pages advertising is a huge market that has yet to move online, and both Yahoo and Google see local search as their way to claim their share. Mr. Weiner says Yahoo should have an advantage because it already has address information for many users.

But Larry Page, the co-founder of Google, dismisses the idea that Google is disadvantaged. ''How long does it take to type your ZIP code, maybe five seconds?'' he said in an interview this month, adding that Google would be quick to add personalization features if it felt that they would help users.

Still, Google watchers see the company making efforts to expand its own database of registered users. For instance, it sponsored Orkut.com, a new social networking site, which for now is by invitation only but is attracting thousands of users. Google's rumored entry into a free e-mail service would be a much bigger move and a more direct threat to one of Yahoo's strongest areas.

Mr. Page did not discuss the e-mail service directly, but he did say that Google's aspirations have moved beyond its initial, already immodest, mission statement: ''to organize the world's information.''

''We are trying to put our effort into things that really matter to people that we can make significantly better,'' he said.

Mr. Semel, characteristically, declined to talk about Google or any other competitors, just as he would not discuss battles of media titans. But that doesn't mean he is not competitive.

''I am not one who likes to be fashionable at the moment,'' he said. ''I want to win the race.''

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GRAPHIC: Photos: Terry S. Semel, Yahoo's chief, is competing with Google in the search game. (Photo by Terrence McCarthy for The New York Times)(pg. 1)
Terry S. Semel, Yahoo's chief executive, with Jerry Yang, a co-founder of the company. Yahoo's new search engine, which uses a robot named Slurp to read Web pages, went into use on the site last week. (Photo by Bloomberg News)(pg. 10)Chart: ''Search Results''Google became the most-used Web search engine last year, overtaking Yahoo.Graph tracks share of searches by U.S. users for Google, Yahoo, Time Warner and Microsoft in 2003.(Source by comScore Networks)(pg. 11)

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