August 10, 2015

Maynard J. Webb, Chairman
Yahoo! Inc.
701 First Avenue
Sunnyvale, California 94089

cc: Board of Directors
Marissa A. Mayer, President and Chief Executive Officer
Kenneth A. Goldman, Chief Financial Officer

Dear Maynard,

We have enjoyed our interaction with you, Marissa, and Ken over the past year and appreciate the ongoing dialogue regarding opportunities to create value at Yahoo! Inc. ("Yahoo" or the "Company"). As we discussed with you during our phone conversation on July 27th, we have serious concerns with the performance of Yahoo's core Search and Display advertising businesses ("Core Business"). It has been our hope that by now Yahoo would have addressed these concerns through prompt actions to restructure the business, reduce costs, improve profitability, and stem revenue declines. However, thus far, the Company seems to only be focused on revenue without regard for cost and profitability trends in the business that continue to deteriorate at an alarming rate. Although management has been trying to focus investor attention solely on the growth of the MaVeNS business, this alone will not suffice. It is the responsibility of management and the Board of Directors (the "Board") to drive improved consolidated financial results across all of Yahoo. To date, consolidated financial results have been consistently declining for the past three years with no end in sight.

On our recent call, you had asked that we share with you our observations on the declining profitability as well as our thoughts on how to improve the performance of the Core Business. We have outlined our views below and look forward to discussing these ideas with you in further detail.

Yahoo's Core Business

Although Yahoo's stock price performance over the past few years has been strong, the primary driving force behind this has been the significant increase in value of Yahoo's stake in Alibaba Group Holding Limited ("Alibaba"), not the performance of Yahoo's Core Business. Our analysis focuses on Yahoo's operations and evaluates the profitability of its Core Business, including MaVeNS.

We believe the right way to measure Yahoo's performance is to focus on the Core Business, which excludes the Company's non-operating and non-cash items that are currently included in Yahoo's reported Adjusted EBITDA. In the table below, we have further adjusted Yahoo's reported Adjusted EBITDA to isolate the Core Business' performance by excluding the TIPLA amortization, gains from patent sales, other patent revenue, and Yahoo Japan revenues/royalties.

Adjustments from reported EBITDA to Core Business EBITDA

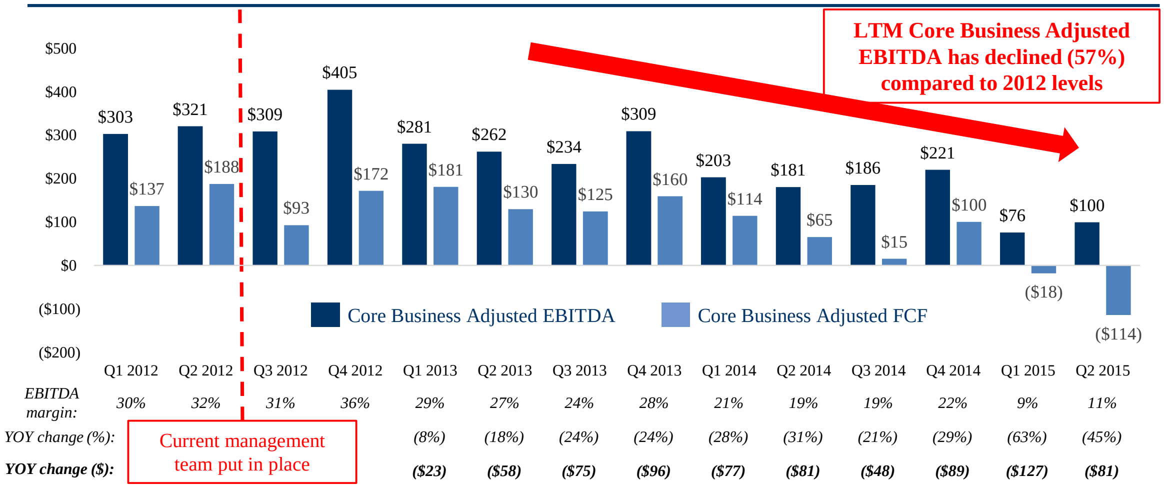
	Q1	*Q2*	*Q3*	*Q4*	**2012**	*Q1*	*Q2*	*Q3*	*Q4*	**2013**
Adjusted EBITDA - core operating business										
Company reported adjusted EBITDA	$384	$398	$408	$509	**$1,699**	$386	$369	$331	$478	**$1,564**
Less: Gains from Patent sales	$0	$0	$0	$0	**$0**	$0	($10)	$0	($70)	**($80)**
Less: TIPLA Amortization	($11)	($11)	($24)	($34)	**($80)**	($35)	($34)	($34)	($34)	**($137)**
Less: Other Patent Revenue	$0	$0	$0	$0	**$0**	$0	$0	$0	$0	**$0**
Less: Yahoo Japan Revenues/Royalties	($70)	($66)	($75)	($70)	**($281)**	($70)	($63)	($63)	($65)	**($261)**
Adjusted EBITDA - Core Business	**$303**	**$321**	**$309**	**$405**	**$1,338**	**$281**	**$262**	**$234**	**$309**	**$1,086**
% margin	*30.4%*	*31.9%*	*31.2%*	*36.3%*	***32.6%***	*28.9%*	*26.9%*	*23.8%*	*28.1%*	***27.0%***
% growth						*(7.5%)*	*(18.2%)*	*(24.2%)*	*(23.6%)*	***(18.8%)***
Core operating business free cash flow										
Adjusted EBITDA - Core operating business	$303	$321	$309	$405	**$1,338**	$281	$262	$234	$309	**$1,086**
(-) Taxes	($56)	($27)	($76)	($83)	**($242)**	($30)	($50)	($32)	($41)	**($153)**
(-) Capex	($110)	($106)	($140)	($150)	**($506)**	($70)	($82)	($78)	($109)	**($338)**
Core operating business free cash flow	**$137**	**$188**	**$93**	**$172**	**$590**	**$181**	**$130**	**$125**	**$160**	**$595**

	Q1	*Q2*	*Q3*	*Q4*	**2014**	*Q1*	*Q2*	*Q3E*	*Q4E*	**2015E**
Adjusted EBITDA - core operating business										
Company reported adjusted EBITDA	$306	$340	$306	$409	**$1,362**	$231	$262	$220	$281	**$994**
Less: Gains from Patent sales	$0	($62)	($1)	($35)	**($98)**	($2)	($9)	$0	$0	**($11)**
Less: TIPLA Amortization	($35)	($34)	($34)	($67)	**($169)**	($69)	($69)	($60)	$0	**($198)**
Less: Other Patent Revenue	$0	$0	($22)	($22)	**($43)**	($22)	($22)	($22)	($22)	**($87)**
Less: Yahoo Japan Revenues/Royalties	($68)	($64)	($64)	($66)	**($261)**	($63)	($63)	($63)	($63)	**($250)**
Adjsuted EBITDA - Core Business	**$203**	**$181**	**$186**	**$221**	**$790**	**$76**	**$100**	**$76**	**$197**	**$448**
% margin	*20.7%*	*19.2%*	*19.0%*	*21.5%*	***20.1%***	*8.5%*	*11.2%*	*7.4%*	*18.2%*	***11.5%***
% growth	*(27.5%)*	*(31.1%)*	*(20.7%)*	*(28.7%)*	***(27.2%)***	*(62.7%)*	*(45.0%)*	*(59.1%)*	*(10.7%)*	***(43.3%)***
Core operating business free cash flow										
Adjusted EBITDA - Core operating business	$203	$181	$186	$221	**$790**	$76	$100	$76	$197	**$448**
(-) Taxes	($4)	($8)	($58)	($52)	**($123)**	$41	($58)	($40)	($40)	**($98)**
(-) Capex	($85)	($107)	($112)	($68)	**($373)**	($135)	($155)	($124)	($117)	**($531)**
Core operating business free cash flow	**$114**	**$65**	**$15**	**$100**	**$295**	**($18)**	**($114)**	**($88)**	**$40**	**($180)**

Source: Company filings and Starboard Value estimates.

As you can see in the chart below, **Yahoo's Core Business EBITDA has been decreasing at an alarming rate.** In fact, in Q1 and Q2 of 2015, **Yahoo's Core Business became free cash flow negative**. Additionally, on a year-over-year basis, the magnitude of the decline keeps continuing and accelerating without benefit of lapping or stabilizing. This should be enormously alarming for management and the Board.

Yahoo's Core Business Adjusted EBITDA



Source: Company filings and Starboard Value estimates.
Note: Reported adjusted EBITDA from Yahoo adjusted for gains on patent sales, TIPLA amortization, Yahoo! Japan revenue and royalties, and other patent revenue.

We acknowledge that the industry's shift from PC to mobile has contributed to this decline, but the main reason behind the massive decline in profitability is the Company's excessive spending on SG&A and low return on investment in R&D initiatives and acquisitions.

Since Q1 2012, annual operating expenses have increased by greater than $550 million. **<u>This increase in costs explains greater than 70% of Yahoo's Core Business Adjusted EBITDA decline</u>**. Yahoo's Core Business Adjusted EBITDA of $1,338 million in 2012 has declined to $582 million for the last 12 months. We believe approximately $550 million of the decline is attributable to the Company's excessive spending and only $200 million of the decline is due to industry and business trends, including the shift from PC to mobile. It is not acceptable to blame the Company's challenges on the declining (and increasingly smaller) legacy portion of its business and highlight only the growth in MaVeNS, which actually is, in large part, a result of the legacy business' decline.

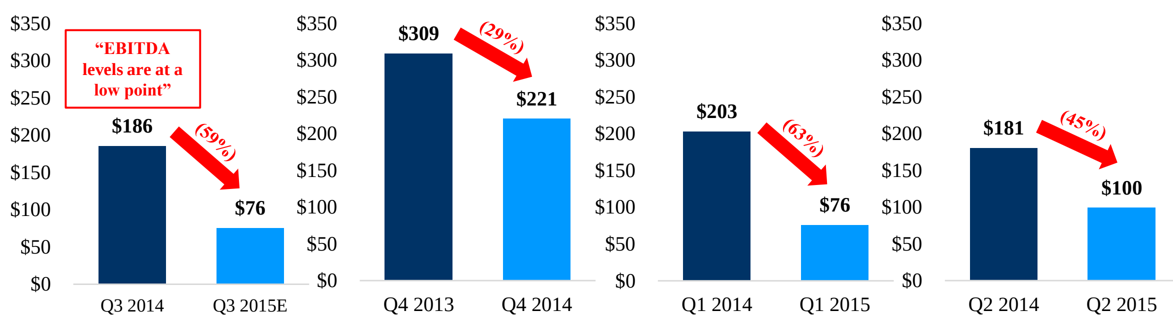
Profitability has dramatically decreased despite the fact that over the last three years Yahoo has spent approximately $5.7 billion[1] in acquisitions and product development costs. Despite these massive investments, Yahoo's LTM revenue ex-TAC and Core Business Adjusted EBITDA declined by 2% and 57% since 2012, respectively. Not only do we believe that many of the

[1] Company filings. Assumes Yahoo spent $230 million on the Polyvore acquisition (according to Bloomberg reports).

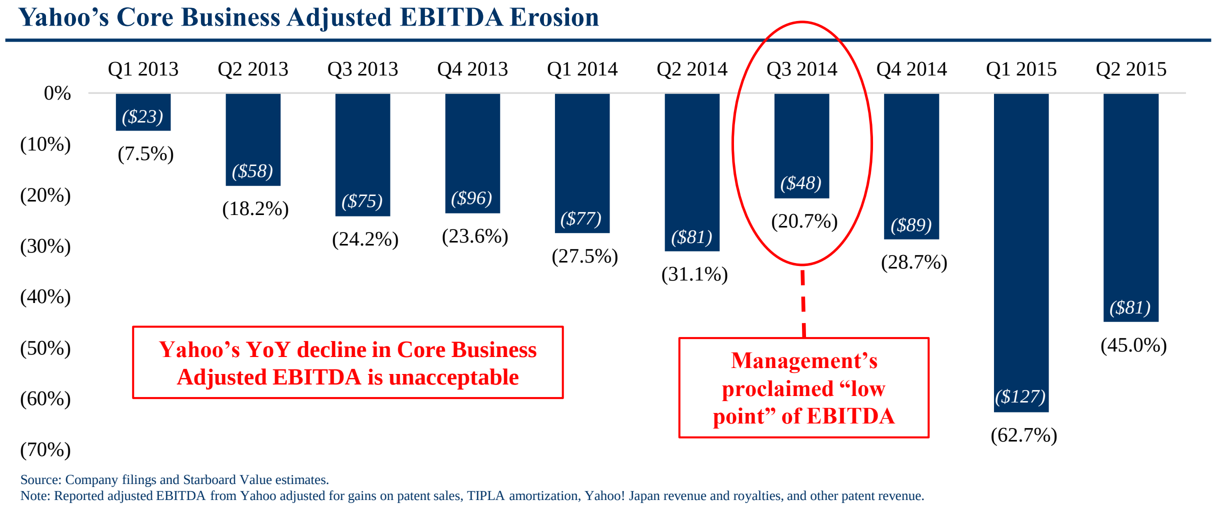
acquired companies were, and still are, losing a considerable amount of money, but we also believe that these acquisitions, on a combined basis, have failed to deliver material revenue growth. In fact, we believe that an overwhelming number of the acquired start-ups have actually been shut down after being acquired by Yahoo. The Company's strategy to spend several hundred million dollars each quarter to buy high priced high multiple companies is akin to death by a thousand cuts. It has not worked thus far, yet Yahoo continues to spend significant capital on unprofitable and value destructive acquisitions.

Recent public commentary by management also increases our significant concerns that management and the Board may not be aware of the severity of the current situation. On Yahoo's Q3 2014 earnings call, management affirmed that *"EBITDA levels are at a low point and [the Company expects] to see improvements with revenue growth in 2015…"* Since then, the Company reported massive year-over-year declines in Core Business Adjusted EBITDA to the tune of (29%) or ($89 million) in Q4 2014, (63%) or ($127 million) in Q1 2015, and (45%) or ($81 million) in Q2 2015. EBITDA levels were clearly not "…at a low point." In addition to these declines, based on our estimates, Yahoo's Core Business Adjusted EBITDA is expected to continue to decline (59%) year-over-year (see below).

Core Business Adjusted EBITDA continues to decline after management's assurance that Q3 2014 was a "low point"



Source: Company filings and Starboard Value estimates.
Note: Reported adjusted EBITDA from Yahoo adjusted for gains on patent sales, TIPLA amortization, Yahoo! Japan revenue and royalties, and other patent revenue.



Profitability is clearly getting worse at an alarming rate and free cash flow has now gone negative, yet management and the Board are not taking appropriate action and are making statements which are out of touch with reality. The Company has shown extreme reluctance to right-size Yahoo's bloated cost structure. The Company's lack of urgency to address Yahoo's Core Business' profitability is enormously troubling. It is further alarming to hear the Company is "thrilled" and "extremely pleased" about their recent performance when Q2 2015 was the second consecutive quarter with negative free cash flow. The Core Business turnaround was the primary reason that the current management team was hired in 2012 and, to date, the results have been disappointing. Going forward, management must work closely with the Board to set aggressive budgets and financial goals that demonstrate significant near-term improvements in financial results which balance the desire to grow with the need to generate acceptable levels of profitability and returns on investment. The Board needs to represent the shareholders and provide the proper oversight and guidance to return Yahoo to profitability. The Board needs to make sure budgets are acceptable and management is held accountable to meeting these goals. Claiming success by growing MaVeNS while consolidated financial results massively deteriorate is unacceptable.

Key Elements of a Turnaround Plan for Yahoo

Management and the Board have a tremendous opportunity to create significant value for shareholders through a combination of reducing costs and pursuing a more favorable search agreement. We believe that the execution of these operational initiatives would produce tremendous value for shareholders, and should be within the control of management and the Board.

Cost reduction opportunity: Based on our extensive due diligence, we believe that Yahoo has an opportunity to reduce costs by $330 to $570 million. As a benchmark, this would simply offset the approximate $550 million increase in SG&A and R&D spend that occurred over the last three years. This level of cost reduction opportunity should be easily achievable given the current management team reportedly had a similar cost reduction plan prepared at the time of joining Yahoo. This was before Yahoo's cost structure increased by $550 million.

We believe the primary lever to achieve this profitability goal is a rationalization of the expenses for products, content, and initiatives that have little prospect of contributing meaningful revenue in the reasonably near future. We believe many of Yahoo's Display properties are currently losing a significant amount of money. Through our extensive due diligence, we believe only a small percentage of Yahoo's properties are profitable. Some of the most profitable Display properties include Yahoo! Home Page, Yahoo! Search, Yahoo! News, and Yahoo! Mail, but unfortunately, we believe the vast majority of other properties do not generate enough unique users to be profitable.

We also believe that there are opportunities to reduce expenses throughout the entire organization including corporate G&A. We understand and recognize that management and the Board have been largely focused on driving growth but it is crucial to balance that desire with the need to produce acceptable levels of profitability and return on investment.

Search Agreement Opportunity: We believe Yahoo has an opportunity to improve the economics from its current agreement with Microsoft and create value for shareholders by switching providers. Yahoo currently generates less than other industry peers in its Search agreement with Microsoft that limits the revenue per 1,000 searches it receives. We believe by partnering with another provider's algorithm to power Yahoo! Search, instead of Microsoft, the Company could generate an incremental $15 per 1,000 searches in mobile and an additional $20 per 1,000 searches in PC. We have heard media speculation that Yahoo is currently in trials with another provider, and if this is true, we believe Yahoo should continue the trial and eventually switch providers.

<u>**We believe the time has come for Yahoo's management and Board to narrow Yahoo's focus to areas where it can demonstrate a high return on investment and a sustainable competitive advantage.**</u> Cash flow continues to decline and free cash flow is now negative. It is time to make the hard restructuring decisions. It is time to show leadership and focus to return Yahoo to acceptable levels of profitability. Yahoo's inability to identify significant cost reduction opportunities has been due to Yahoo's current desire to aggressively invest in product

areas or other initiatives where Yahoo, in our view, has a low probability of ultimate success. It is time to shift focus and strike a better balance between the desire for growth and the need for improved profitability, a strong return on investment, and a more narrow focus on areas where Yahoo has a competitive advantage and can win.

We appreciate the ongoing dialogue and your willingness to engage with us, but we are frustrated with the operating performance and lack of progress to date. We expect to hear details of a broader restructuring at Yahoo including elements laid out in this letter. We are available to discuss and review the contents of this letter at your convenience. It is our sincere hope that we can work constructively together for the best interests of all Yahoo shareholders.

Best Regards,

Jeffrey C. Smith
Managing Member
Starboard Value LP