

Description

Facebook, Inc. is an online media company. It operates social networking platforms **Facebook** and **Instagram** and messaging platforms **WhatsApp** and **Messenger**. It offers solutions to advertisers and marketers to engage with its users.

November 1, 2018

Facebook, Inc. does not report the breakdown of revenues per platform but it is estimated to be about 80% **Facebook** 20% **Instagram** while messaging platforms are not yet monetized.

- 98.5% of revenues come from advertising (91.5% Mobile, 7% Desktop).
- 50% of revenues come from North America ...
- ... though the region only represents 10% of MAUs (Monthly Active Users) versus 40% for Asia, 16% for Europe and 32% for the rest of the World.

Facebook, Inc. direct clients are media buyers that bundle big corporate ad budgets together. Though the company does not disclose any information about its clients, it is estimated that the largest corporate advertisers on its platforms are the traditional big ad spenders (Samsung, P&G, Microsoft, AT&T, Amazon, Nestlé, Unilever, Walmart, etc...)

Facebook, Inc. was founded by Mark Zuckerberg and fellow Harvard students in 2004 and rapidly became a hugely popular social networking platform. But it really became strongly profitable nearly 10 years after it fully embraced its advertising business model under the impulsion of COO Sheryl Sandberg, a former Google executive.

The company acquired **Instagram** in 2012, **WhatsApp** in 2014 and virtual reality hardware maker **Oculus** in 2014. It also invests in other long term initiatives but with no foreseeable impact on revenues.

Due to its dominant position in social media, **Facebook Inc.** is relentlessly attacked by media, politicians and users and is blamed for about anything (undermining elections, disseminating fake news, causing social unrest, promoting scientific misinformation, being used for bullying and harassment, etc...).

Despite the bad press, user engagement remains very strong and **Facebook Inc.** platforms are seen as a unique tool by advertisers and marketers to understand and reach consumers.

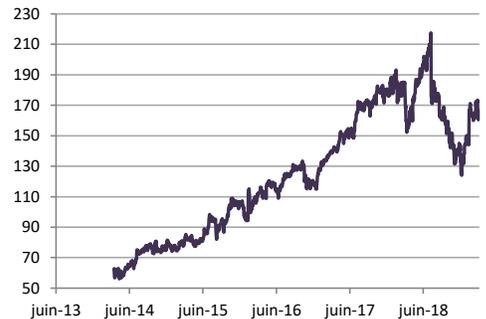
Sector Communication Services
Industry Media & Entertainment
Mkt Cap (\$bn) 474.0

Price 166.08
1Y Range 123.02 - 218.62
200 D Histo Volatility 42%

(in USD MM)

Revenue 55'838
EBITDA 29'228.0
EBITDA Margin 52.3%
1 Year Fwd. P/E 18.2
Dividend Yield 0.00%

5 Year Price Action



Source : Bloomberg

Union Securities Research Team
research@unionsecurities.ch

Union Securities Switzerland SA
11 Cours de Rive
1204 Geneva, Switzerland
<http://unionsecurities.ch>

Investment Case

Despite all the bad press on privacy, advertisers are sticking to **Facebook Inc.** as it provides access to a huge user base and analytics that allow advertisers to better target consumers.

Users metric remain healthy as well and a renewed focus on “friends & family” and *Stories* (see glossary) should drive more engagement. *Instagram* is growing at a fast pace and allows **Facebook Inc.** to stay in touch with younger demographics.

2019 should be a year of transition with lower growth and a focus on addressing privacy issues and investing in security and content. Growth will be a function of volume, offsetting price declines as advertisers increasingly shift from *Newsfeed* to *Stories*.

2020 should see a strong boost in growth with an improvement in pricing led by *Stories*. Longer term, new initiatives such as e-commerce or the monetization of *WhatsApp* and *Messenger* have the ability to maintain growth at high levels. One way to monetize messaging platforms could be to merge with *Instagram*.

Stock price exhibit some volatility around news flow but valuation is low for a high growth company (18x 1Y Fwd PE) and earnings expectations have already been reduced sharply. Analysts now expect revenue growth of 21% to be only slightly above the 19% growth of the mobile ad industry spending.

Facebook Inc. is a fantastic cash machine with strong growth prospects. Valuation is very reasonable and there is ample room for Facebook to monetize further its *Instagram* and messaging platforms.

It has all the qualities required to be part of our core **Global Leaders** portfolio.

Recent Events

- 2018 was marked by a number of privacy and fake news scandals;
- 4Q18 earnings came well above expectations as advertisers and users ignored those scandals;
- Four key executives left the company in Q1 2019, including Chief Product Officer Chris Cox who had worked at the company since the very first years;
- On March 2019, CEO Zuckerberg released a statement in which he claimed that Facebook would become a privacy-focused social network.

Bullish Case

- **Increased monetization and better pricing drives up revenues**
- *Stories* drive higher ad pricing
- Development of e-commerce
- Monetization of messaging platforms

Bearish Case

- **User fatigue, privacy issues or increased competition leads to a slowdown in advertising revenues growth**
 - Loss of market share to competition
 - Loss of key audiences
-

SWOT Analysis

Strengths	Weaknesses
<ul style="list-style-type: none"> • Dominant position <ul style="list-style-type: none"> ○ Huge user base (2.3Bn MAUs) ○ Strong global presence • Offers unique analytics and targetability to advertisers • Owns multiple platforms <ul style="list-style-type: none"> ○ Reaches multiple demographics ○ Ability to fend competition through acquisitions • Very high profitability <ul style="list-style-type: none"> ○ Content is “free” as it is produced by users ○ 80% gross margins (70% for Google) • Strong Technological infrastructure <ul style="list-style-type: none"> ○ Emphasis on research and development • Strong corporate culture <ul style="list-style-type: none"> ○ Double headed top management (Zuckerberg and Sheryl Sanders) ○ Strong IT Culture ○ Innovative workforce 	<ul style="list-style-type: none"> • High dependence on Facebook and Instagram <ul style="list-style-type: none"> ○ No monetization of messaging platforms • High dependence on advertising revenues • Tainted image <ul style="list-style-type: none"> ○ User privacy issues ○ Frequent media backlash • High regulatory pressure • High reliance on the US <ul style="list-style-type: none"> ○ Lower monetization of international markets compared to the US. ○ No access to the Chinese Market • Low barrier to entry
Opportunities	Threats
<ul style="list-style-type: none"> • Higher Ad volumes <ul style="list-style-type: none"> ○ New user segments ○ Opening of the Chinese market • Higher Prices <ul style="list-style-type: none"> ○ Stories ○ Better pricing in Asian and emerging markets • Monetization of messaging platform <ul style="list-style-type: none"> ○ Directly, ○ Or through the merger of <i>Messenger</i> and <i>WhatsApp</i> with <i>Instagram</i> • Entry in the Chinese Market • e-commerce <ul style="list-style-type: none"> ○ Leverage Instagram as an e-commerce platform • Long term opportunities <ul style="list-style-type: none"> ○ Augmented and Virtual Reality ○ Dating ○ Payments ○ Video streaming (<i>Facebook Watch</i>, <i>IGTV</i>) • Corporate structure <ul style="list-style-type: none"> ○ Create a holding company like Alphabet ○ Increase buybacks ○ Further consolidate the industry 	<ul style="list-style-type: none"> • Clients <ul style="list-style-type: none"> ○ Loss of marketers due to privacy issues ○ Deterioration of global advertising spending ○ Balancing of ad budget between online and TVs • Users <ul style="list-style-type: none"> ○ Slowing engagement ○ Loss of younger demography ○ Missing Generation Z ○ Maturing markets ○ Online ad fatigue • New competition <ul style="list-style-type: none"> ○ Amazon is entering the ad markets • Management issues <ul style="list-style-type: none"> ○ Departure of key people • Cybercrime • Regulatory <ul style="list-style-type: none"> ○ Higher accountability ○ Higher transparency ○ GDPR implementation • Peaking margins <ul style="list-style-type: none"> ○ Failure to monetize WhatsApp and Messenger ○ Increasing investments ○ Rising operational costs ○ Need to spend more to acquire quality contents

Glossary

- **MAU** : Monthly Active Users
- **DAU** : Daily Active Users
- **Engagement** measure user's interaction with social contents such as "shares", "likes" and comments
- **Stories** are short and ephemeral user-generated photos or videos uploaded to the user's *Facebook* or *Instagram*
- **News Feed** is the traditional feed seen by *Facebook* users

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