

Q4 2020 Earnings Call

Company Participants

- David Wehner, Chief Financial Officer
- Deborah Crawford, Vice President of Investor Relations
- Mark Zuckerberg, Chairman Of The Board, Chief Executive Officer, Founder
- Sheryl Sandberg, Chief Operating Officer, Director

Other Participants

- Brian Nowak, Analyst
- Colin Sebastian, Analyst
- Doug Anmuth, Analyst
- Eric Sheridan, Analyst
- John Blackledge, Analyst
- Justin Post, Analyst
- Ross Sandler, Analyst
- Youssef Squali, Analyst

Presentation

Operator

Good afternoon. My name is Mike, and I will be your conference operator today. At this time, I would like to welcome everyone to the Facebook Fourth Quarter and Full Year 2020 Earnings Conference Call. All lines have been placed on mute to prevent any background noise.

After the speakers' remarks, there will be a question-and-answer session. (Operator Instructions). This call will be recorded. Thank you very much.

Ms. Deborah Crawford, Facebook's Vice President of Investor Relations. You may begin.

Deborah Crawford {BIO 5934723 <GO>}

Thank you. Good afternoon, and welcome to Facebook's fourth Quarter and full year 2020 earnings conference call. Joining me today to discuss our results are Mark Zuckerberg, CEO; Sheryl Sandberg, COO; and Dave Wehner, CFO.

Before we get started, I would like to take this opportunity to remind you that our remarks today will include forward-looking statements. Actual results may differ materially from

those contemplated by these forward-looking statements. Factors that could cause these results to differ materially are set forth in today's press release and in our quarterly report on Form 10-Q filed with the SEC.

Any forward-looking statements that we make on this call are based on assumptions as of today and we undertake no obligation to update these statements as a result of new information or future events.

During this call, we may present both GAAP and non-GAAP financial measures. Reconciliation of GAAP to non-GAAP measures is included in today's earnings press release.

The press release and an accompanying investor presentation are available on our website at investor.fb.com.

And now, I'd like to turn the call over to Mark.

Mark Zuckerberg {BIO 15103277 <GO>}

All right. Thanks, everyone for joining us today. I hope you're all staying healthy and well. Our community and business had a strong end of the year, as COVID continue to keep many of us apart and at home, people and businesses continue relying on our services to stay in touch and create economic opportunity.

2.6 billion people now use one or more of our apps each day and more than 200 million businesses, mostly small businesses use our free tools to reach customers. Those numbers give a sense of scale, but some of the stories we here show the impact. Groups have formed, where COVID long haulers are helping each other through the scary experience, where there's not much else to turn to. Teachers are sending class assignments to students through WhatsApp, local bookstores and coffee shops are using Instagram, to let customers know they're open for curbside pickup, we saw people come together to raise \$1.8 billion for non-profits and personnel causes through our fundraising tools last year. And including \$175 million for COVID-related causes alone. I'm proud of the role that our services played and helping people support each other during what has been such a hard time.

Now, I spent a fair amount of time on recent earnings calls, talking about our election integrity efforts. So I'm not going discuss them at length today, but if you want to call out that according to our estimates, we easily surpassed our goal to help 4 million people register to vote, as part of the largest-ever effort -- largest effort to distribute authoritative voting information in recent history. And I want to thank everyone involved in our teams and outside involved with that effort.

So today, I'm going to focus on our product work, and specifically, I'm going to focus on four themes that I'm excited about for the year ahead. Communities, private messaging, commerce tools for small businesses, and building the next computing platform.

FINAL

Bloomberg Transcript

FINAL

So let's start with communities. I think that helping people build community is one of the most important things that we can do. Our social fabric is made of multiple different layers through which we get our social support. First, we have friends and family and that's the most personal layer, then we have communities we're part of, where we feel a sense of purpose and belonging, explore interests, develop skills, grow as individuals and then meet new people. And then finally, there is the safety net that society and government provide. And in many parts of the world, there has been an unfortunate decline in community participation over the last several decades, that's second layer. And this is not something that we can solve alone, but I think we can help.

So now that we've helped billions of people stay connected with friends and family, helping everyone find and participate in communities that are meaningful to them has been our next goal and we even updated our mission a few years ago to reflect this, making it give people the power to build community and bring the world closer together.

Today more than 600 million people are now members of a group on Facebook that they consider to be meaningful in their lives. This is growing steadily over time. And I hear all the time from people who are in parenting groups that there are major resources, they navigate raising kids or from people who found a group that shares the same health condition and they can lean on that community for knowledge and support or from people who moved to a new place and joined local groups to meet people and get situated.

Our product focus now is to develop this community infrastructure beyond feeds and message boards to help people build and run full self-sustaining community institutions. So we're building tools to help groups get this done together and provide support for people that span messaging, video chat and even communities own websites, and we're exploring different ways to raise funds including donations, merchandise and membership fees to help group leaders support their communities operations and hire people for different roles that are needed to build sustainable communities for the long term.

So as we continue to focus on this, we need to make sure that the communities that people connect with are healthy and positive, and that's something that we've been focused on for a while now. One way of course that we do this is by taking down groups that break our rules against things like violence or hate speech. And in September, we shared that we had removed more than 1 million groups in the last year alone. But there are also a lot of groups that we may not want to encourage people to join even if they don't violate our policies.

So for example, we stopped recommending civic and political groups in the US ahead of the elections, and we're continuing to fine-tune how this works. But now we plan to keep civic and political groups out of recommendations for the long term, and we plan to expand that policy globally. And to be clear, this is a continuation of work we've been doing for a while, to turn down the temperature and discourage divisive conversation and communities.

FINAL

No along these same lines, we're also currently considering steps that we can take to reduce the amount of political content in newsfeed as well. We're still working through exactly the best ways to do this, and to be clear, of course, we're still going to enable people to engage in political groups and discussions, if they want to, these can often be important and helpful and there can be ways that people organize grassroots movements or speaking out against injustice, and we learned from people with different perspectives. So we want these discussions to be able to keep happening, but one of the top pieces of feedback that we are hearing from our community right now is that people don't want politics and fighting to take over their experience on our services.

So one theme for this year is that we're going to continue to focus on helping millions of more people participate in healthy communities and we're going to focus even more on being a force for bringing people closer together.

Next, let's talk about private messaging. As we've discussed before, while people enjoy connecting with friends and communities in the digital equivalent of a Townsquare in apps like Facebook and Instagram, the fastest growing social experiences are about connecting privately in the digital equivalent of the living room in services like WhatsApp and Messenger. So that's why we kicked off a big effort a couple of years ago to re-imagine what a modern social platform would look like if you build it from the bottom up to be privacy first.

And we identified several core principles, a private social platform should be built around the most intimate interactions that we have, and that's one on one conversation.

The most important aspect of privacy and security is that your conversations should stay between you. And that means that your conversations should always be end-to-end encrypted and they should disappear when you're done with them. The safety and reducing spam matter too. And that means that we should maintain a minimum amount of metadata to build sophisticated tools to stop bad actors using these services. And you should have a choice over what services you use. So we should make messaging as interoperable as possible across our apps.

And finally, no matter what, we should only store peoples' data in countries where we know we can keep it secure and we should continue opposing data localization in countries with weak records on human rights or privacy. I think that these are the privacy principles that matter most to people. First and foremost people care that their conversations stay private. But after that people also care about safety and other convenience too. And from this perspective WhatsApp and the direction that we're heading in with Messenger are the best private social apps available,

Now, we have a lot of competitors to make claims about privacy that are often misleading. Apple recently released so-called nutrition labels, which focused largely on metadata that apps collect rather than that the privacy and security of peoples' actual messages, but iMessage stores non intend encrypted backups of your messages by default unless you disable iCloud. So Apple and governments have the ability to access most people's

messages. So when it comes to what matters most, protecting peoples' messages. I think that WhatsApp is clearly superior.

Now since I try to use these earnings calls to discuss aspects of business strategy that I think are important for investors to understand, I do want to highlight that we increasingly see Apple as one of our biggest competitors. iMessage is a key (inaudible) of their ecosystem. It comes pre-installed on every iPhone and they preferenced it with private APIs and permissions, which is why iMessage is the most used messaging service in the US. And now we are also seeing Apple's business depend more and more on gaining share in apps and services against us and other developers.

So Apple has every incentive to use their dominant platform position to interfere with how our apps and other apps work, which they regularly do to preference their own. And this impacts the growth of millions of businesses around the world, including with the upcoming iOS 14 changes, many small businesses will no longer be able to reach their customers with targeted ads. Now Apple may say that they're doing this to help people, but the moves clearly track their competitive interests. And I think that this dynamic is important for people to understand because we and others are going to be up against this for the foreseeable future.

Now our messaging services continue growing, but it is an uphill battle, and our services just need to be that much better as private social platforms to succeed. So to make sure that we remain the best, a couple of years back we kicked off a number of long-term efforts that have started shipping recently and more of these projects are on strengthening encryption, ethical [ph] morality, interoperability and offering other tools are going to be shipping throughout this year.

So now let's talk about commerce. Our goal here is to give every individual entrepreneur and small business access to the same kinds of tools that historically only the big companies have had access to. We've always cared about this, but the pandemic has made it more urgent. So it used to be the case that only large companies could afford to have analytics or targeted advertising capacity to reach their customers, and it was expensive to build these capabilities and it often required building teams and storing large amounts of data in-house which and most small businesses can't do. And so one of the things that I'm most proud of is that we build the tools, so we can offer these same capabilities to small businesses often for free.

So when you hear people say that we hold a lot of data that's because hundreds of millions of businesses that would have otherwise had to do this individually, I mean, would have had no easy way of doing so are now using our services to help them reach customers. And when you hear people say that we're connecting data from lots of sources, that's to help small businesses reach customers more efficiently.

Big companies often do this themselves, but small businesses can't a lot of times, so we do this for them. So when you hear people argue that we should be doing these things or that we should go back to the old days of untargeted television ads, I think that what they're really arguing for is a regression, where only the largest companies have this

capacity, small businesses are severely disadvantaged and competition is diminished. So with our commerce tools, we've made it so that a business can set up a shop ones and then they will have an online storefront in both Facebook and Instagram immediately and eventually on WhatsApp and Messenger as well.

And we recently expanded Checkout to all US businesses making the process of buying a lot more seamless, and as the lockdowns have continued, we saw more businesses, more small businesses and creators also use Paid Online Events as a way to make money. WhatsApp is also an important part of our strategy here. More than 175 million people message in WhatsApp business account every day and we're building new features to make it even easier to transact with businesses in the app.

We introduced Carts, which lets people browse catalogs, select multiple products and send the order as a message to a business. And the more people that interact with businesses, the better tools that we're going to need to provide for businesses to help them support their customers. Many businesses need more than a phone to manage their customer service. So we are building tools to let businesses store and manage their WhatsApp chats using our secure hosting infrastructure if they would like.

I mean, we're in the process of updating WhatsApp's privacy policy in terms of service to reflect these optional experiences. Now to clarify some confusion that we've seen, this update does not change the privacy of anyone's messages with friends and family. All of these messages are end-to-end encrypted which means we can't see or hear what you say, and we never will, unless the person that you message chooses to share it. And business messages will only be hosted on our infrastructure if the business chooses to do so.

So we want everyone to know the lengths that we go to, to protect your private messages. So we are moving the date of this update back to give everyone time to understand what the update means.

Finally, let's discuss our work building the next computing platform. This is one of the areas that I'm most excited about our progress heading into 2021. If you look at the history of computing, every 15 years or so, a new major platform emerges that integrates technology more naturally and ubiquitously into our lives, starting with mainframes and PCUs and browser-based computing and then mobile. And I believe that the next logical step here is an immersive computing platform that just delivers this magical sense of presence that you're really there with another person or in another place. Our phones can't deliver this and neither can any other technology that has come before it.

This is going to unlock the types of social experiences that I dreamed about building since I was a kid and it's what we're building towards at Facebook Reality Labs. We launched Quest 2 in October, and it is on track to be the first mainstream virtual reality headset. We designed it so that anyone can jump in with the best and most immersive experience out there. And at a price that makes it available to as many people as possible. And I think the Facebook has done more than any other company to help bring virtual reality to the mainstream. And it's been great to see so many people embraced this

especially this year during the pandemic. We're seeing people use it to play games with friends when they can't be together in-person to do workouts in their living room or to meet with colleagues while they're working from home. So there are a lot of reasons. The Quest 2 was one of the holiday gifts this year.

And we are also seeing a growing ecosystem of developers building amazing new experiences for the platform. Right now more than 60 Oculus developers are generating revenue in the millions and that's nearly twice as many as a few months ago. In previous quarters, I've talked about our long-term future goals, when it comes to virtual reality, but I think that this quarter's results show that this future is here.

Augmented reality glasses are going to be a key part of this vision too. We're still working on some of the foundational technology to underpin these and the ultimate product is still some years away, but this year we are excited to deliver a first glimpse of what will be when we launched our first pair of smart glasses from Ray-Ban in partnership with Luxottica. And during this pandemic, we've also seen Portal has proven to be a great way for people to stay connected especially over the holiday as families had to celebrate apart. This year, we're focused on expanding the role of Portal and virtual reality presence into the workplace bringing more features that can improve remote presence, collaboration and productivity.

2021 has a lot of unknowns. We don't know when vaccines are going to be widely available when our teams will be back in the office, or when our lives are going to start feeling normal again. But what I do know is that we are going to keep investing in and innovating on the big themes that I discussed here in order to put more power in the hands of people and small businesses.

I personally believe that technology can unlock progress and opportunity and that the full story of the Internet has not yet been written. That's why I'm hopeful for the year ahead and grateful that you're all on this journey with us.

And now, here is Sheryl to talk about our business.

Sheryl Sandberg {BIO 15339456 <GO>}

Thanks, Mark, and hi, everyone. Like Mark, I hope everyone is safe and healthy. This was a strong quarter for our business as the acceleration of online commerce we've seen during the pandemic continued into the holiday season. Our total revenue for Q4 was \$28.1 billion, which is a 33% year-over-year increase, our fastest growth rate in over two years.

After a really difficult year for so many businesses, this holiday period was important, and while many businesses are still struggling, the good news is that Q4 was stronger than expected for retail. In the US, the National Retail Federation reported net sales in November and December went up 8% year-over-year and online sales were up 24%.

This holiday period was also longer. Compared to previous years, advertisers started spending earlier and sustained that spend well beyond Black Friday and Cyber Monday.

We saw robust performance across regions as well as an improvement in brand advertising.

The strength of our Q4 performance is a result of years of investments in free and paid tools to help businesses succeed online. Even before the pandemic, businesses were going digital, but COVID made this a necessity.

Almost overnight, businesses had to create digital storefronts, figure out how to take online orders and find new ways to reach their customers. For many small companies, these steps or even just setting up a website or mobile app can be difficult and expensive. Our free and paid tools helped solve these problems for businesses around the world. With so many businesses struggling when the pandemic hit, we asked our teams what do businesses need and how can we help. First, they need the tools to get their business up and running online, so what can we do to make our simpler and more effective, and can we build new ones to help them.

Second, they need the digital skills and know-how to succeed, so how can we help more businesses with training and resources. And third, they need their voices to be heard. So can we use our scale to amplify their voices and tell their stories. We've been asking these questions throughout the last year and into Q4.

On the first, we accelerated our work on tools to make it easier for people to find brands and products they love and for businesses to manage their online presence and connect with customers. Mark talked about some of the new tools we've launched like Shops and Paid Online Events. In the fall, we also rolled out Facebook Business Suite, a new interface to help businesses manages their Pages or Profiles across our apps.

We also continue to invest in making our products as effective as possible, so businesses can get more value for every dollar they spend. Personalized ads are privacy safe and help businesses reach customers where they are, which has been more important than ever during the pandemic.

One notable area of progress this past year was in Stories ads, which have become more effective for direct response advertisers. One business that use Stories ads is Carlota Flower Lab, a florist in Los Reyes, Mexico. Before COVID, they made 70% of their revenue from face to face workshops. So when the pandemic hit, founder Paola Mendoza had to get creative. She has personalized ads on Instagram to reach new audiences and even found her first international customers with campaigns targeting California and Texas.

One campaign for Dia de los Muertos, the Day of the Dead led to a 24 times return on ad spend, helping Paolo triple her annual revenue in 2020 despite COVID.

On the second, resources and training, we did some big things in 2020. We created a Business Resource Hub a one-stop-shop for resources and trainings for small businesses that we've continued to build out through the end of the year.

FINAL

Bloomberg Transcript

We committed to reach 1 million members of the Black community and 1 million members of the Latinx and Hispanic communities in the US with free digital skills trainings through our Elevate Program by 2023. And we re-imagined our boost with Facebook events to reach businesses virtually with a 100 million people tuning in throughout the year. This included our 12 week Season of Support to help businesses across 16 countries prepare for the holidays.

On the third, a great example of how we amplify the voices of our businesses in Q4 is our Buy Black Friday campaign. One of my favorite campaigns ever. In the US black-owned businesses closed at twice the rate of others after the start of the pandemic, so we wanted to help people shop with them over the holidays. We created ways for people to find black businesses in their local area, a gift side featuring products from Black businesses across the US. And even a Buy Black Friday show on Facebook Live that was seen by 15 million people.

One of the small businesses we featured is a vegan skincare brand called Redoux from New York City. Its Founder Asia Grant appeared on the Buy Black Friday show now became one of her most successful sales days ever. The campaign gave her record revenue in web traffic and she was even able to hire more people, something that's so important given current unemployment rates.

Business owners like Asia and Paola have worked hard to adapt and grow in line. But lots of businesses will continue to struggle in 2021. So we're going to keep listening to them and building on what we did last year. That means improving our products and tools to help businesses seamlessly manage their online presence, advertise across our apps and communicate with customers through business messaging.

It means making more training available through programs like She Means Business for women and Elevate for diverse communities. And it means finding more ways to amplify their voices, whether it's sharing the stories of small businesses worried that Apple's iOS 14 changes will hurt their ability to reach customers or showcasing small businesses and gift cards and products like businesses nearby.

I want to close by saying how grateful I am to all the businesses around the world who work with us. So partnership helps us build the tools you need, so you can continue to grow in higher, and as always, I'm grateful to our incredible teams who have done so much to help businesses survive this difficult year including coming up with great ideas like Buy Black Friday. I hope that 2021 is a better year for everyone.

Now here's Dave.

David Wehner {BIO 2419389 <GO>}

Thanks, Sheryl, and good afternoon, everyone. Q4 was a strong quarter, capping off a solid year for our business as full year 2020 revenue grew 22% to \$86 billion. We have been encouraged to see improved demand for our ads during the second half of the year after facing significant headwinds at the onset of the pandemic. Our results reflect the

ongoing strength in the digital economy and the value we're providing to millions of businesses who use our services to reach consumers and generate sales.

Let's begin with our community metrics. In December, we estimate that approximately 2.6 billion people used at least one of our services on a daily basis and that approximately 3.3 billion people used at least one on a monthly basis. Facebook daily active users reached 1.84 billion, up 11% or 188 million compared to last year. DAUs represented approximately 66% of the 2.8 billion monthly active users in December. MAUs grew 299 million or 12% compared to last year.

Consistent with our outlook, US and Canada DAU declined 1 million sequentially as usage continue to normalize from peak COVID levels experienced earlier in the year.

Turning to the financials. All comparisons are on a year-over-year basis unless otherwise noted. Q4 total revenue was \$28.1 billion, up 33% or 32% on a constant currency basis. We benefited from a currency tailwind and had foreign exchange rates remained constant with Q4 of last year. Total revenue would have been \$339 million lower.

Q4 ad revenue was \$27.2 billion, up 31% or 30% on a constant currency basis. The growth in advertising revenue was largely driven by a strong holiday shopping season for retail, which benefited from the ongoing shift to online commerce.

On a user geography basis, ad revenue was strongest in Europe, which grew 35% and benefited from currency tailwinds. US and Canada grew 31% and Asia-Pacific grew 29%. Rest of world growth improved to 25% but continue to be significantly impacted by currency headwinds.

In Q4, the total number of ad impressions served across our services increased 25% and the average price per ad increased 5%. Impression growth was driven by both Facebook and Instagram. The increase in average price per ad was driven primarily by Facebook mobile feed, as well as pricing improvement in Instagram Stories.

Other revenue was \$885 million, up 156% due to strong Quest 2 holiday sales. We've been encouraged by the positive reception of Quest 2 since its October launch.

Turning now to expenses. Q4 total expenses were \$15.3 billion, up 25% compared to last year. In terms of specific line items, cost of revenue increased 49% driven primarily by hardware costs related to Quest 2 sales core infrastructure investments and payments to partners.

R&D increased 34% driven primarily by hiring and investments in core products, as well as our consumer hardware efforts. Marketing and sales increased 8% driven by hiring and marketing spend. Lastly, G&A expenses decreased 13% as we lap charges related to the default legal settlement recorded in the fourth quarter of 2019.

FINAL

Bloomberg Transcript

In the past year, we added a record 13,600 net employees and reached our goal of adding 10,000 employees in tech and product roles. We ended the year with over 58,600 full-time employees, up 30% compared to last year. We continue to be pleased with our ability to recruit onboard and retain talent in this environment.

Fourth quarter operating income was \$12.8 billion, representing a 46% operating margin. Our tax rate was 14%. Net income was \$11.2 billion or \$3.88 per share. Capital expenditures were \$4.8 billion, driven by investments in data centers, servers office facilities and network infrastructure.

Free cash flow was \$9.2 billion and we ended the quarter with \$62 billion in cash and marketable securities. For the full year, we repurchased \$6.3 billion of our Class A common stock and had \$8.6 billion remaining in our prior authorization as of December 31. Today, we announced a \$25 billion increase in our stock repurchase authorization.

Turning now to the outlook, We continue to face significant uncertainty as we manage through a number of cross-currents in 2021. We believe our business has benefited from two broad economic trends playing out during the pandemic. The first is the ongoing shift to online commerce. The second is the shift in consumer demands towards products and away from services. We believe these shifts provided a tailwind to our advertising business in the second half of 2020 given our strength in product vertical sold via online commerce and our lower exposure to service verticals like travel.

Looking forward, a moderation or reversal in one or both of these trends could serve as a headwind to our advertising revenue growth. At the same time, in the first half of 2021, we will be lapping a period of growth that was negatively impacted by reduced advertising demand during the early stages of the pandemic. As a result, we expect year-over-year growth rates in total revenue to remain stable or modestly accelerate sequentially in the first and second quarters of 2021.

In the second half of the year, we will lap periods of increasingly strong growth, which will significantly pressure year-over-year growth rates. We also expect to face more significant ad targeting headwinds in 2021. This includes the impact of platform changes, notably iOS 14, as well as the evolving regulatory landscape.

While the timing of the iOS 14 changes remains uncertain, we would expect to see an impact beginning late in the first quarter. There is also continuing uncertainty around the viability of transatlantic data transfers in light of recent European

Regulatory developments. And like other companies in our industry, we are closely monitoring the potential impact on our European operations as these developments progress.

Turning now to expenses. We expect 2021 total expenses to be in the range of \$68 billion to \$73 billion, unchanged from our prior outlook. This is driven by investments in technical and product talent as well as continued growth in infrastructure costs.

We continue to expect 2021 capital expenditures to be in the range of \$21 billion to \$23 billion, driven by data centers, servers, network infrastructure, and office facilities. Our outlook includes spend that was delayed from 2020 due to the impact of the pandemic on our construction efforts.

Turning now to tax. We continue to expect our full-year 2021 tax rate to be in the high-teens.

In closing, 2020 was unique operating environment that introduced a number of unforeseen challenges. We have been pleased with our team's ability to adapt in order to maintain the reliability of our services, deliver new products and experiences and support the millions of businesses, who use our platforms to reach consumers.

With that, Mike let's open up the call for questions.

Questions And Answers

Operator

We will now open the lines for a question-and-answer session. (Operator Instructions)

Your first question comes from the line of Brian Nowak from Morgan Stanley.

Q - Brian Nowak {BIO 16819013 <GO>}

Thanks for taking my question. I have two. The first one for either Mark or Sheryl. Appreciate the color on commerce. I was curious is for any encouraging quantifiable signposts or learnings that you've seen so far on Instagram Shopping that sort of give you confidence you're making progress and building out this opportunity?

And then the second one. Dave, I appreciate the comment on the forward outlook in the outlook commentary, I guess the question is you sort of talk about this shift to consumer expenditure towards products away from services and it could potentially be a headwind in the back half as it reverses. The last quarter you mentioned you had 10 million advertisers. So maybe talk to us about sort of some of the segments of advertisers you think that you're missing and what initiatives you have in place to sort of broaden the advertiser base to bring more services on the platform? Thanks.

A - Sheryl Sandberg {BIO 15339456 <GO>}

I can take the first. With Instagram Shopping, we launched a new Shop tab on Instagram in Q4, and this is built on other shopping efforts we've had. We see this as an overall part of our commerce efforts. We've always been I think a great place for people to discover new products and services. But we are very interested in taking people all the way down that funnel from discovery to purchase to finding products and services, to checking out and as well. And our shopping efforts are part of that. We're seeing nice uptick. It's still

really early days, but we think businesses are having a good experience and people are having a good experience.

And as always with our ad products and with our commerce products, we want to make sure we provide a great experience to the end-user, so that they can find the things they are looking for.

A - David Wehner {BIO 2419389 <GO>}

Hey, Brian. It's Dave. Yes, the data that we've looked at, there really is that when you look at the data from the US, it basically showed that in Q3, while the services consumer spend was still down year-over-year, spending on goods actually surge to record levels, so the highest in like 15 years. We don't have the results for Q4, but we expect that sort of trend continued.

If you look at the balance of our business, it tends to skew more towards products relative to the overall GDP and-or the overall consumer spend in for instance, the US, so we just think we're overall exposed, a little bit more to products. We continue to invest to improve our exposure and travel and starting in service areas like travel, but our expectation would be in 2021 we'll continue to have a similar skew towards products as we had in the past, we will continue to make investments to make our ad products more relevant for services as well.

Operator

Your next question comes from the line of Doug Anmuth from JPMorgan.

Q - Doug Anmuth

Great. Thanks for taking the question. For Dave and Sheryl, we know you mentioned significant ad targeting headwinds, but as your view on IDFA changed at all over the past few months. I'm just curious how you're thinking about Facebook's ability now to offset some of the impact just through things like limited login mode and new APIs and other conversion tools and data.

And then if you could just talk a little bit more about how you're thinking about the impact across FAN and then the core products? Thanks.

A - David Wehner {BIO 2419389 <GO>}

Sure. Doug, I'll take that. So I don't think our outlook has changed in any significant way on iOS 14, we continue to believe that that will be a headwind in the ads business, it's -- our view, not just limited to IDFA but broader than that is we're going to have to be providing a prompt asking people for permission to use third-party data to deliver personalized ads. So that's going to be true whether you're using IDFA or not.

And we do expect there to be high opt-out rates related to that. And that's factored into our outlook. We expect that to roll out sometime, we expect later in Q1, but the timing is

FINAL

Bloomberg Transcript

uncertain and Apple hasn't given clarity on that at this point. And we do expect that we'll have increasing impact through the year as more users adopt iOS 14 and go through those permissions.

When you think about what the mitigations might be, obviously, there is going to be mitigation of the impact on us to some extent just because this is a platform-wide change. And so it will impact everyone and so that's going to, that's going to mitigate it to some extent. And in addition, over time, we hope to help businesses by providing more on-site conversion opportunities through initiatives like shops and also click to messaging ads.

And as it relates to specifically the audience network products, obviously that's going to have a significant impact on audience network on iOS as we've explained in the past, but it's -- but the broader impact given the size of that business is really to our -- to the core advertising business on iOS.

Operator

Your next question comes from the line of Eric Sheridan from UBS.

Q - Eric Sheridan {BIO 17860961 <GO>}

Thanks so much for taking the question. Maybe two, if I can. Mark just conducting your comment, what do you see is some of the key investments either on the hardware side or the content application side to unlock the opportunity based on what you recently saw with the success of Oculus in the holiday period, where there was a piece of hardware obviously that's sold through quite well and how do you think about aligning investments against the opportunity in the coming years?

And then maybe I don't know if it's for Sheryl or Dave. But maybe I could just follow up a little bit on Doug's question when you think out to the language you are using about the back half of the year, is there any sense you can give us quantitatively about how to think about some of the tougher comps you'll see as we move through '21 versus identifying the degree of the severity of different outcomes from some of the headwinds? Thanks so much.

A - Mark Zuckerberg {BIO 15103277 <GO>}

I can take the first one. So when we started working on virtual and augmented reality, we basically laid out a task, where we knew that virtual reality would be practical to build first and we view that, that it's kind of all part of one continuous ecosystem for spatial immersive computing and presence. So the key things that we're trying to do with VR now, I do believe that Quest 2 is the first mainstream virtual reality product, it is doing quite well. And I'm really proud of what we've been able to do there. The goal there is -- we keep on shipping content and titles and working with developers and shipping new capabilities to the device. Like last year, we shipped the ability to do now hand tracking. It's no one expected to be possible yet, but the team working on that. It's really great work and it just made the device better and increase the value. So there -- we're continuing to work on new hardware as well. The new hardware will kind of fit the same platform, so the content that works on Quest 2 should be forward compatible and that

way we're going to build one to a larger installed base around the virtual reality headsets that we have.

And at the same time, we're building towards a future with some of this -- the fundamental technology investments that we're making to be able to provide augmented reality glasses that hopefully will be able to support a lot of the same content in this ecosystem over time and take advantage of a lot of these foundational investments that we've made.

So this is -- this continues to be a long-term -- a long-term investment. I think it's very important both for the vision of what we want to do. Like I said in my script before earlier, it's just -- some of the things that we're able to build with VR and AR are the types of social experiences that I wanted us to -- I wanted to build since I was a kid, and I'm excited to build to unlock that and I also think strategically it's important for us to have a little more control of our own destiny in terms of the operating systems and platforms that all of our services operate on. So continue to be very focused on this and optimistic about what we're seeing.

A - David Wehner {BIO 2419389 <GO>}

Yeah, Eric. It's Dave just coming back to your question, I think the context is we have this -- we've had a tremendously strong quarter Q4 of this year, number of factors we talked about driving that. A couple of are pandemic-related which is just a shift to online commerce as well as the ongoing -- the shift to more spend on products versus services. In Q4, we also saw strength with sort of our full range of advertisers. We have seen sort of small and medium-sized businesses come back and start getting strength in Q2 and Q3 or Q3 specifically and then Q4, we also saw strengths in some of our largest advertisers as well.

So as you look out in 2021, I think we're just going to be facing tougher comps in the back half of the year. Some of those things related to the -- related to the pandemic have the potential to revert whether it's more consumer expenditures shifting towards services away from products, so that will make it a little bit of a tougher comp and then you layer on top of that headwinds to growth related to privacy-related headwinds, the biggest factor there as iOS 14. So we certainly anticipate growth, but we're just looking at tougher comps as we hit the back half of the year given really most importantly the strength that we saw this year. And then on top of that, the headwinds that we're seeing from some of the privacy changes.

Operator

Your next question comes from the line of Justin Post from Bank of America.

Q - Justin Post {BIO 3469195 <GO>}

Great, thank you. I guess I'll ask about regulation. I know -- I know it's a tough topic. First Mark, in your prepared remarks you elevated a little bit competition with Apple. Is there anything going on with iOS 14 besides IDFA that maybe put you in more direct competition with Apple?

And then secondly, obviously, the FTC filed their case since the last earnings call. Maybe just open forum, any thoughts on that, that you're able to share? Thank you.

A - Mark Zuckerberg {BIO 15103277 <GO>}

Well, in terms of the competition with Apple specifically, I laid out rear four product focus areas and with the exception of the work that we're doing on communities, which I think is quite separate from the work that they do. The other three areas I think are going to have very significant competitive overlap with Apple. In messaging certainly iMessage is the most popular service in the US. I think because of the fact they pre-install it and give their app several advantages that other apps don't have.

In commerce and supporting small businesses, I think there, you have some of the iOS 14 changes that we think are going to be very problematic especially for small businesses. And then longer term as we move towards building the next computing platform, I think we would expect to see them as more of a competitor there as well.

So I do think that this is sort of shaping up that -- we face many competitors, right. There are a lot of competitors in the core social app work that we do. (technical difficulty)

Operator

Excuse me, this is the operator. I apologize, but there will be a slight delay in today's conference, please hold and the conference will resume shortly. Thank you for your patience. Speakers, we are now connected.

A - Mark Zuckerberg {BIO 15103277 <GO>}

Was there another question on the last one that I was supposed to answer?

A - David Wehner {BIO 2419389 <GO>}

Well, there is question about the FTC.

A - Mark Zuckerberg {BIO 15103277 <GO>}

Hey, guys. We're back.

A - David Wehner {BIO 2419389 <GO>}

Are we on now through this line?

Operator

Yes. You are connected.

A - David Wehner {BIO 2419389 <GO>}

Okay.

A - Mark Zuckerberg {BIO 15103277 <GO>}

All right. So where did I lose you?

A - David Wehner {BIO 2419389 <GO>}

I think you had covered the question of the dynamics related to the competitive landscape. And then there was a follow-on question around the FTC case and any thoughts that we have on that. I don't think we have anything, we necessarily are commenting on at this point.

A - Mark Zuckerberg {BIO 15103277 <GO>}

Yeah, nothing on the case. I mean, on regulation overall, because I think some of the question was focused on that. The point that I would highlight is I actually think it would be very helpful to us and the Internet sector overall for there to be clear rules and expectations on some of these social issues around how content should be handled, around how elections should be handled, around what privacy norms governments want to see in place, because these questions all have trade-offs. Right. The content and elections -- the elections questions have trade-offs between giving people free expression, and a voice, but some of their trade-offs again safety and privacy and other social equities, they're all very important and it's -- I think you very difficult for a private company to balance those -- and I think it will be much better to have, just to be clear guidance and clear rules for the Internet. So that's going to be something that we continue to advocate for.

A - David Wehner {BIO 2419389 <GO>}

Mike, we go to the next question.

Operator

Your next question comes from the line of Ross Sandler from Barclays.

Q - Ross Sandler {BIO 15948659 <GO>}

Hey, guys. A question about the price volume. Can you hear me?

A - David Wehner {BIO 2419389 <GO>}

Yeah. I can hear you now.

Q - Ross Sandler {BIO 15948659 <GO>}

Question about the price versus volume metrics Dave [ph] just mentioned, is the first quarter in a long time. The price I think was up year-on-year. I know there's a lot of factors that go into that. But you also mentioned that you're seeing strong traction from DR advertisers around the stories format.

So maybe just a little bit more color on where we are in the stories versus feed, price dynamic and what kinds of DR advertisers you're seeing the most traction around these

Stories ads? Thanks a lot.

A - David Wehner {BIO 2419389 <GO>}

Yeah. Sure, Ross. So I mean, as you know with the auction dynamic, the growth in pricing is that really depend on impression growth. And we saw impression growth slowed this quarter to 25% from the Q3 rate of 35% and some of that is just due to lapping product optimizations on Instagram during Q4 of '19 as well as just a normalization of engagement trends on Facebook, and so we would expect that sort of overall story to continue into Q1 with those trends.

And then we're also continuing to make iterative improvements that enhance the performance and benefit pricing over time. And the one example that we give there is Instagram story is that as you know, it's been an area we've been focused on to try and make DR performance through better ads interactivity, work better on stories and we've been seeing some good progress there. So we called that out as well as being a driver of price improvement.

There is still a gap with Stories ads and feed ads, but we've been pleased with the progress we've been making on that front.

Operator

Your next question comes from the line of Colin Sebastian from Baird.

Q - Colin Sebastian {BIO 6373379 <GO>}

Great, thanks very much. Two quick ones from me. I guess given the ongoing efforts on private messaging. I'm curious ultimately what will differentiate Messenger from WhatsApp other than branding or geographies, there is an inevitable and consolidation of functionality there?

And then secondly Reels [ph]. I know it's still early, but any update on performance or uptake as well as the roadmap, the monetization I think would be helpful. Thank you.

A - David Wehner {BIO 2419389 <GO>}

Mark, do you want to take this?

A - Mark Zuckerberg {BIO 15103277 <GO>}

Yeah. I can take the first one, I mean the biggest connection for -- the biggest difference between Messenger and WhatsApp is obviously the connection to Facebook and the kind of same identity and graph that you use on Facebook comes with you to Messenger. So even if you can send messages across the different apps and there is more interoperability and we bring the same world-class privacy features to both. I think that that will still make the apps feel fairly distinct.

I also think the -- kind of static and the focus of the apps on how much different functionality they include will vary. I think WhatsApp is always had -- we've always focused a lot on making it a very utilitarian experience and placed more of a premium on simplicity there. So we'll continue adding new functionality, but we're more focused on keeping that minimal, whereas in Messenger, we have a lot more tools and features for expression, and I would expect that we'll continue adding more there as well.

A - Sheryl Sandberg {BIO 15339456 <GO>}

On the second with Reels, we're really pleased with the early data on consumption and we have a bunch of work ahead of us to make it easier for people to create and discover content. We've now rolled out the product into over 50 countries. In monetization of it, we've launched branded content tagging Reels, so that helps creators share of the content and monetize. We launched shopping in Reels and we've said that we will launch ads the timing has to be determined. And we're going to follow the same pattern we followed on other things like stories.

We launched a consumer product, we make sure there's product market fit and people are using it, then we launched an ad product and we make sure that it's beneficial for consumers. And as David answered I think the last question, we work very diligently quarter-by-quarter on the basis point improvements that help us scale our product. So we will do things to make it easier for people to create the right -- is to create the right ad format.

We will do things to make those ads get to the person who might be looking for that product or service.

Operator

Your next question comes from the line of Youssef Squali from Truist Securities.

Q - Youssef Squali {BIO 1506420 <GO>}

Great. Thank you very much. I have two questions, please. Mark, I want to go back to the first theme that you discussed of communities and how you're looking to potentially de-emphasize civic and political groups. How important or how large is civic and political content on that side? Is there a way to quantify or quantify the engagement with it, to see if this is one of the headwinds that you guys talk about in terms of potentially emerging in 2021?

And second on the regulatory headwinds, there is just increasing talk of about Section 220 protection. I know it's, it's a thorny subjects about from where you stand, how do you see Facebook and not just really Facebook, but other social media platforms dealing with it and if it was either to be narrowed or even completely eliminated? Thank you.

A - Mark Zuckerberg {BIO 15103277 <GO>}

Sure. I can probably take both of those. Yeah. I don't know if we have any stats to share on size of civic and political content, but it's a pretty small minority of the content, and all the

FINAL

feedback that we have from our community suggests that the vast majority of people would like to stay that way. And I think there has been this trend I think across society where a lot of things have become politicized and politics, has kind of had a way of creeping into everything. And I think a lot of the work that we are -- a lot of the feedback that we see from our communities that people don't want that in their experience.

They come to our services to connect with friends and family, to connect communities that they care about. And I think that we can potentially do a better job of those core jobs that we have and do a better job helping to bring people together and helping to promote healthier communities. If we can reduce the amount of politics on our services.

Now, I mean, it's a -- we'll have to balance this carefully because we have a deep commitment to free expression. So I believe that people want to be able to discuss the stuff or Join groups. This should certainly be able to do that. But I just don't think that it's serving the community, particularly well to be recommending that content right now.

But one thing to mention just because you were asking about the headwinds and all that is, I don't think that this is a factor in any of that and Wehner can jump in if there is any more that you want to add on that, but I don't think that that's what he had in mind in any way there. Wehner, I'll skip a beat for you to jump in if you want before going to the next question.

A - David Wehner {BIO 2419389 <GO>}

Yeah, no, I was just going to say that exact thing. You said this is not something that's factoring into our outlook. It's not a -- it's not a headwind is a factor in our 2021 outlook and certainly on the ads front as well. Political always extremely small it's low single-digit revenue even in an active political quarter like we had. So no, it's not factoring in on the ad side or the engagement side in our outlook.

A - Mark Zuckerberg {BIO 15103277 <GO>}

Yeah. And now going to your 230 question, I do think and I testified this -- about this in Congress. I do think that Congress should update section 230 to make sure that it's working the way that people intent, right, after I think being in place for almost 25 years? And the Section 230 has been very important. It's helped to give rise to the Internet as we know, we are today and it's given Internet platforms tools to be able to balance free expression and safety, and I think it's also gone pretty far in terms of helping to ensure the values like free expression are built into the Internet's DNA.

So I think that any changes should be thought through very carefully and should be thought through, not just from the perspective of what a larger company you like Facebook or a Google or a Twitter could handle in terms of updating their content moderation policies, but also from the perspective of making sure the new companies can continue to emerge, I think that's very important as well. So we supported changes in this for a while back in 2018.

We supported a change to prevent sex trafficking and will support similar efforts to tackle harms like child exploitation, imagery [ph] and material and opioids and will also support any push to make content moderation systems more transparent. The details on all this of course matter but we hope to go to work with the new Congress on this.

A - Deborah Crawford {BIO 5934723 <GO>}

Operator, we have time for one last question.

Operator

Your last question comes from the line of John Blackledge from Cowen.

Q - John Blackledge {BIO 7387802 <GO>}

Great, thanks. Two questions. Mark, on community, could you just provide further details on layering more services for Facebook groups and expectation for uptake of those new services and could community evolve as a meaningful monetization driver in the coming years?

And then on IDFA maybe for Dave or Sheryl, how do you think advertisers are prepared for the changes and will the long tail advertisers be more impacted than the larger more sophisticated advertisers? Thanks.

A - Mark Zuckerberg {BIO 15103277 <GO>}

I can speak to the first point. First, for the business. And I don't think we look at community separately from friends and family. They are both different types of content that show up in news feed and that people interact with. But my guess is that it's probably already a pretty meaningful driver of the business and the value that people get from the services today. So, absolutely, I think as this continues to grow. It should be in the future.

The big trend that we're -- that we're looking at now, that I tried to call out in my remarks earlier is that right now, there is a spectrum of different kinds of groups and communities on Facebook. Everything from meme groups that people find very entertaining and fun to groups that people really turn to for support when they have kind of serious issues in their lives. And I think right now though most of these communities, they have this backbone of -- there's a feed, there are ways to message people.

But when I think about the physical communities that I'm a part of, in my life, they often have more of an institutional structure, there are sub-communities. There are people who -- it's their full-time job to basically help people engage and basically help people navigate them, I'm thinking about things like the synagogue [ph] that I'm that I am a member of, right?

I mean, there are people there whose job it is, is to help engage the congregation and help them get basically the most out of everything that the institution has to offer, and

FINAL

Bloomberg Transcript

that's a very important kind of our community organization and I would love for more institutions like that to be able to organize and build community more effectively online.

So there are lots of just different tools that I think that -- if we provide spanning messaging, spanning video chat, these organizations own websites and other things that they do, that if we can help in a lot of those areas, then we can make it that groups on Facebook or not just a feed in a place we post some content and maybe engage on a post but that we can really help more organizations build up community institutions like that. I think that that could be a very big contribution and something that I'm excited about technology.

A - Sheryl Sandberg {BIO 15339456 <GO>}

To your second question, we think it's a really important question and one that we take very seriously. So small businesses are very reliant on personalized ads. The ability to use data in a very privacy-safe way to get the customers who are interested in their products and services and that makes sense. Big businesses, we can buy an ad to the whole country, we can buy an ad to an whole region. Small businesses can't, they have to precise audiences they want, and I think one of the mainstays of our business is we've enabled that targeting in a very privacy-safe way without giving information without permission to advertisers.

And what's happening with IDFA is that small businesses are really concerned, because they're worried that they're not going to be able to buy effective advertising. If all personalized ads went away, small businesses would see a 60% cut in website sales. Now, we don't think Apple's contemplating going that far that quickly, but that is the general direction of what would happen. And you can see that that would be very detrimental to their business.

It's also very detrimental to economic growth because so much of our job growth comes from small businesses. I think it's worth noting. It's not just about advertisers. Some of these changes also impact developers and other forms of businesses. We are starting to hear from creators and developers who are worried that some of their free services will have to start charging or shut down, force them into subscriptions or other impairments for revenue.

Now not all small businesses are aware of these challenges. So we are hearing from more and more of them. So we're very concerned.

A - Deborah Crawford {BIO 5934723 <GO>}

Great. Thank you everybody for joining us today. We appreciate your time and we look forward to speaking with you again.

Operator

Ladies and gentlemen, this concludes today's conference call. Thank you for joining us. You may now disconnect your lines.

FINAL

This transcript may not be 100 percent accurate and may contain misspellings and other inaccuracies. This transcript is provided "as is", without express or implied warranties of any kind. Bloomberg retains all rights to this transcript and provides it solely for your personal, non-commercial use. Bloomberg, its suppliers and third-party agents shall have no liability for errors in this transcript or for lost profits, losses, or direct, indirect, incidental, consequential, special or punitive damages in connection with the furnishing, performance or use of such transcript. Neither the information nor any opinion expressed in this transcript constitutes a solicitation of the purchase or sale of securities or commodities. Any opinion expressed in the transcript does not necessarily reflect the views of Bloomberg LP. © COPYRIGHT 2021, BLOOMBERG LP. All rights reserved. Any reproduction, redistribution or retransmission is expressly prohibited.

Bloomberg Transcript