

Q2 2020 Earnings Call

Company Participants

- Dave Wehner, Chief Financial Officer
- Deborah T. Crawford, Vice President of Investor Relations
- Mark Zuckerberg, Founder, Chairman and Chief Executive Officer
- Sheryl Sandberg, Chief Operating Officer

Other Participants

- Brian Thomas Nowak, Analyst
- Douglas Till Anmuth, Analyst
- Eric James Sheridan, Analyst
- Heather Bellini, Analyst
- Justin Post, Analyst
- Mark Shmulik, Analyst
- Mark Stephen F. Mahaney, Analyst
- Ross Adam 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's Second Quarter 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 T. Crawford {BIO 5934723 <GO>}

Thank you. Good afternoon and welcome to Facebook's second quarter 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. A 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>}

Thanks, and thanks everyone for joining us today. I hope you're all doing okay and staying healthy. This was a strong quarter for us, especially compared to what we expected at the start. There are now more than 3.1 billion people using our services every month to stay connected and more than 180 million businesses who use our tools to connect with customers. We also had more than 9 million active advertisers across our services as many shifted their business online.

As I said yesterday, the tech industry is an American success story. Products we build have changed the world for the better and improved people's lives. Our industry is one of the ways that America shares values with the world and one of the greatest economic and cultural exports of our country. Facebook is part of this story. We started with an idea to give people the power to share and connect, and we built services that billions of people find useful. I'm proud that we've given a platform to make -- for people to make their voices heard and giving small businesses access to tools that only the largest players used to have.

Since COVID emerged, people have used our services to stay in touch with friends and family who they can't be with in person and to keep their businesses running online, even when physical stores are closed. In many ways, amidst this very difficult period for people around the world, our services are more important now than ever before. It's worth reflecting on this for a moment, because there's a fundamental difference between how the vast majority of people actually experience our services and the impression you'd get if you just read much of the commentary about Facebook. Imagine going through this pandemic two decades ago when the Internet was nascent. Facebook didn't even exist. Sheltering-in-place is incredibly disruptive now, but until recently it would have meant almost no connection with your friends and the broader economy. Most of the small businesses whose storefronts had to close would have gone under and there wouldn't have been another infrastructure like the Internet that they can move quickly to in order to stay afloat.

There are people sharing their day-to-day experiences with friends, communicating in groups with people who share interests and watching entertaining content, buying and selling things, this is how the vast majority of people use our services. Yet, some seem to wrongly assume that most of the content on our services is about politics, news,

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misinformation or hate. Then let me be clear, it's not, these make up a small part of the content on our services, although they are all things the people generally tell us they would like to see even less of. We do not profit from misinformation or hate. We do not want this content on our platforms. People come to our services to connect with the people they care about. That's why people are using our services at record levels now and enabling more of those meaningful social interactions. This is how we succeed.

And we have a plan to further reduce the amount of harmful content. Our AI systems already proactively identified about 90% of the hate speech that we removed before anyone even reports it and no other Internet service does anything remotely as sophisticated as this and we are committed to continuing to improve. We're having an independent audit done of our community standards enforcement report, which is our transparency report on how effectively we are removing harmful content. We're also opening ourselves up to an audit from the Media Rating Council to look at our content monetization policies and brand safety controls. And we're going to work with the Global Alliance for Responsible Media to provide greater transparency into our measurement of hate speech numbers.

Now some also seem to wrongly assume that our business is dependent on a few large advertisers. Now while we value every single one of the businesses that use our platforms, the biggest part of our business is serving small businesses. Our advertising is one of the most effective tools that small businesses have to find customers, to grow their businesses and to create jobs. And that's why I am often troubled by the calls to go after Internet advertising, especially during a time of such economic turmoil like we face today with COVID.

It's true that making it more difficult to target ads would affect the revenue of companies like Facebook, but the much bigger cost of such a move would be to reduce the effectiveness of the ads and opportunities for small businesses to grow. This would reduce opportunities for small businesses so much that it would probably be felt at a macroeconomic level, and was that really what policymakers want in the middle of a pandemic and recession?

The right path I believe is regulation that keeps people's data safe while allowing the benefits of this kind of personalized and relevant advertising.

Looking forward, I expect the rest of this year to continue to be unpredictable. From a health perspective, with COVID growing quickly in the US, there is currently no end in sight for when our teams here will be able to return to our offices. It is incredibly disappointing, because it seems like the US could have avoided this current surge in cases if our governments had handled this better. For Facebook's part, we are continuing to show our COVID Information Center to share authoritative health information. To date, we have directed more than 2 billion people to see it in order to see important health messages, including interviews with Dr. Fauci and recently information about why wearing a mask is so important.

During this time, we found that most Facebook employees can productively work remotely. Even before COVID, we had a long-term goal of enabling more remote work, since the ability to fill present even when you're remote is a core aspect of our own product work on video presence and workplace and virtual and augmented reality. We're using this moment to accelerate these plans. And I expect that up to 50% of our employees will be remote long term within the next five years to 10 years. This will enable us to attract and retain broader pools of talent regardless of where they live.

Economically, with the initial CARES Act stimulus ending here in the US, it's unclear what the economic outlook will be during this next period. I continue to believe that getting the virus under control is the most important step we can take towards economic recovery. For our part, we are accelerating our work to help small businesses sell online through our services. We launched Facebook Shops to let businesses set up a storefront and sell across our apps and that is scaling quickly. We're going to have more to share there soon.

WhatsApp business now has 50 million people using it and is growing quickly. We've also granted -- we've also created grant programs to help small businesses during this period, including a \$100 million program to support small businesses globally, and another \$100 million program, specifically to support black-owned businesses, black creators and non-profits that serve the black community here in the US.

Politically, COVID has added a heightened level of uncertainty to this year's elections. Because of the virus, many people may not want to go to the polls in person. So, the voting by mail will be more important than ever. And since many people haven't voted by mail before, it's critical that we get official voting information in front of people and help people register to vote.

We've built a Voting Information Center and our goal is to help 4 million Americans register to vote in the election. This will be the largest voting information drive in American history, and double the number of people that we helped register in 2016 and 2018. We've already started attaching links to official voting information to any posts from political candidates discussing voting and our goal is to help people register to vote regardless of what these candidates or posts are saying. We're also continuing to focus on stopping election interference including removing voter suppression. We've already broadened our policies here and adopted new policies to partner with local election officials to remove false information on voting in the period leading up to the elections. And we are currently considering additional steps that we might take.

With all this going on, I've been impressed by how much progress our team has been able to make on our proactive product priorities and around building a private messaging platform, enabling small businesses and commerce and building the future computing platforms around virtual and augmented reality. We know it's Messenger rooms in April and people around the world can now join a room from any of our apps or even if you don't have an account with us at all.

We extended Messenger Kids this quarter to 140 new countries and territories helping a lot of parents as they look for ways to safely preserve their children's friendships remotely.

And our AR and VR and hardware products keep getting better. We saw an increase in portal sales across the whole product line this quarter and Quest which we launched last May already has more usage than any other device in our ecosystem.

As I told Congress yesterday, I am proud of the services we build and how they improve people's lives. I'm thankful to everyone at Facebook who is doing this important work, and to all of our partners and everyone else who is on this journey with us, and now I'll hand it over to Sheryl.

Sheryl Sandberg {BIO 15339456 <GO>}

Thanks, Mark, and hi, everyone. I want to start by building on what Mark said about hate speech. Facebook stands firmly against hate, being a platform where everyone can make their voice heard is core to our mission, but that does not mean it's acceptable for people to spread hate. It's not. We don't benefit from it and we never have. Our users don't want to see it and our advertisers don't want to be associated with it. For years, we spent billions of dollars on teams and technology to find and remove hateful content and to protect the integrity of our platforms generally, and we've become a pioneer in using artificial intelligence to remove hateful content at scale. We've made real progress, and in many ways, we've led our industry and being more transparent and more proactive at enforcement. A recent study from the European Commission shows that these investments are paying off and that Facebook acts faster and removes a greater percentage of the hate speech on our services than other major Internet platforms.

We've made real progress. But this work is never finished. Earlier this month, we met with the organizers of the ads boycott and other civil rights leaders to listen to their concerns and we published our civil rights audit. We were the first social media company to undertake an audit of this kind, an independent two-year review of the civil rights impact of our products and practices. It's clear we have a lot more to do and we are working every day to meet this challenge, not because of pressure from advertisers but because it is the right thing to do.

We are also working every day to support people and businesses through this difficult period. The pandemic is not just a public health crisis but an economic crisis that has hit businesses around the world hard. I want to talk about what we're seeing in our own business and how we are supporting small businesses as they transition online in order to weather the storm. After seeing flat year-over-year revenue growth in the first few weeks of April, we saw a considerable recovery in May and June. Our total ad revenue for Q2 was \$18.3 billion, which is a 10% year-over-year increase. This demonstrates not only our resilience as a company but a wider trend that has been underway for some time. People are spending more and more time online, so businesses need to be online too. This was true long before the pandemic but it is especially true now that people can't always get together in person.

In the United States before the crisis, one in three companies still did not have a website. Now more and more businesses realize they have to be online. This month, in partnership with the World Bank and OECD, we published our first global state of Small Business Report based on a survey of more than 30,000 small business leaders across more than

50 countries. The data paints a sobering picture of the struggle businesses are facing, but it also points to the scale of the digital transformation we are witnessing, in the majority of countries, at least one-third of SMBs reported earning a minimum of 25% of their sales from digital channels in the previous 30 days.

Over the years, we've invested in free unpaid tools to help businesses in this increasingly digital-first economy. Anyone can set up a digital storefront on Facebook or Instagram for free in just minutes. That is why now more than 180 million businesses use our tools every month. Along with our free tools, personalized advertising is a lifeline for businesses, especially small businesses, who can't afford broad campaigns aimed at mass audiences. For just a few dollars, now more than 9 million advertisers use our platforms to reach audiences interested in their products and we enable this in a way to protect people's privacy and produces measurable results.

In today's economy, when businesses are struggling and customers aren't physically walking into their stores or restaurants, this is more important than ever. Due to social distancing restrictions. Italian coffee shop owner, Niccolo Toronto, had to get creative and re-imagine what a virtual coffee experience could look like. With the help of Facebook, Instagram and WhatsApp, he promoted online sales and free home delivery to people interested in coffee within 10 miles to 12 miles of the store and he saw a 20 times return on ad spend. And it's not just small businesses that have used personalized ads to help them pivot. At the onset of the pandemic, Kirkland's, home furnishing retailer in the US, shifted its focus online and used Facebook ads targeted at adults within 10 miles to 15 miles of their stores to drive sales with curbside pickup. This is the type of customer acquisition that is only possible with personalized ads. And as a result, they saw a 24 times return on ad spend and a three times increase in the sales directly attributable to Facebook.

As Mark discussed, regulatory and platform challenges threaten this lifeline for businesses, but we remain committed to doing everything we can to help them adapt, so they can survive and thrive in the online economy. We recently launched the Business Nearby tool to help people find businesses in their neighborhoods and we continue to develop Shops to make selling online quick and easy.

We know making tools available is not enough. We also need to ensure business owners have the digital skills to use these tools effectively. In March, we launched our Business Resource Hub to share free training and resources, and since then, over 20 million people have visited. We then launched our Summer of Support program in June to share even more advice for businesses, whether or not they use our services. Since launch, more than 15 million people have tuned in to hear practical tips for rebuilding and strengthening their business.

In addition to tools and training, businesses have told us they need direct financial help. In mid-March, we announced a \$100 million grant program to help small businesses around the world, and since we opened applications for the program, we've seen a huge amount of interest from black-owned businesses. So we know they are facing enormous challenges. Black businesses have faced systemic barriers for generations and have also been hit hardest by the economic impact of the pandemic. Last month, we announced an additional \$100 million investment in black-owned small businesses, black creators and

non-profits that serve the black community in the US. Our grant program is on top of the goal we set previously to spend at least \$1 billion with diverse suppliers next year and every year thereafter. As part of this, we'll spend at least \$100 million annually with black-owned suppliers from facilities to construction to marketing agencies and more.

To COVID crisis is lasting longer than anyone hoped and expected. We are acutely aware of the responsibility we have to keep people connected during this turbulent time and to help businesses weather the storm and transition to the digital economy. I want to close by saying how grateful I am to our partners around the world who continue to give us valuable feedback and hold us accountable and to our incredible teams who are deeply committed to making progress on the issues that matter most and launching new products that continue to make a real difference in people's lives.

Now, here's Dave.

Dave Wehner {BIO 2419389 <GO>}

Thanks, Sheryl, and good afternoon, everyone. We continue to operate in an uncertain and challenging environment around the world. At the same time, we are seeing accelerated participation in the digital economy and Facebook is helping alleviate the economic challenges associated with COVID-19. We are pleased to support people and businesses through these very trying times.

Turning now to our results. Our Q2 growth and engagement metrics reflected increased engagement due to the impact of the pandemic. However, as expected, we are seeing signs of normalization as shelter-in-place measures have eased around the world. I would provide more detail in the outlook.

In June, we estimate that approximately 2.5 billion people used at least one of our services on a daily basis and that approximately 3.1 billion people used at least one of our services on a monthly basis. Note that these Q2 family metrics reflect new data from our recent user survey and certain methodology improvements. Further details are included in the earnings slides on our IR website.

Facebook itself continued to grow with daily active users reaching 1.79 billion, up 12% compared to last year. DAUs represented approximately 66% of the 2.7 billion monthly active users in June. MAUs grew by 287 million or 12% compared to last year.

Turning now to the financials. Q2 total revenue was \$18.7 billion, up 11% or 12% on a constant currency basis. Had foreign exchange rates remained constant with Q2 of last year, total revenue would have been \$297 million higher.

Q2 ad revenue was \$18.3 billion, up 10% or 12% on a constant currency basis. As Sheryl mentioned, ad revenue growth in the quarter was stronger in May and June relative to April. In terms of verticals, we saw particular strength from both new and existing online commerce and service advertisers who primarily leverage our direct response ad formats.

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Facebook has been a lifeline of economic activity during a time when offline activity has been curtailed. Our growth was primarily driven by small and medium-sized businesses around the world who leveraged our advertising platforms to connect with customers. As a result, we continue to see increased diversification among our advertiser base. In Q2, our top 100 advertisers represented 16% of our ad revenue, which is a lower percentage than a year ago.

On a user regional basis, ad revenue growth was strongest in US and Canada, Asia-Pacific and Europe, which grew 14%, 11% and 9% respectively. Rest of world declined 6% and was impacted by challenging macroeconomic conditions, as well as foreign currency headwinds.

Turning now to our price and volume metrics. In Q2, the total number of ad impressions served across our services increased 40% and the average price per ad decreased 21%. Similar to last quarter, the growth in impressions was primarily driven by Facebook mobile newsfeed due to product changes and increased engagement compared to last year.

The decline in average price per ad was largely attributable to the economic impact of pandemic, although we saw year-over-year pricing trends improve in the latter half of the quarter.

Other revenue, was \$366 million, up 40% driven primarily by sales of Oculus and Portal products.

Turning now to expenses. Q2 total expenses were \$12.7 billion, up 4% on a reported basis. Excluding the \$2 billion expense that we recorded in Q2 of last year related to our settlement with the FTC, total expenses were up 24% year-over-year and 11 percentage point deceleration compared to Q1. The biggest factor in the deceleration of expense growth from the first quarter was a decline in people-related costs like travel, events and amenities as our employees worked almost entirely from home.

By line item, the trends were as follows. Cost of revenue increased 16% driven primarily by depreciation related to our datacenter spend. R&D grew 35% driven primarily by investments in core products, as well as our innovation efforts, notably in AR VR.

Marketing and sales grew 18% driven primarily by consumer and growth marketing, and finally, excluding the FTC expense from Q2 of 2019, G&A expenses grew 30% driven primarily by higher legal expenses.

As Mark mentioned, we continue to invest throughout the economic downturn in order to build products and services for the future. We had our strongest hiring quarter ever in Q2 adding over 4,200 net new hires primarily in technical functions. We ended the quarter with over 52,500 full-time employees, up 32% year-over-year. We are pleased with our ability to recruit on board and retain talent in this environment.

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Operating income is \$6 billion representing a 32% operating margin. Our tax rate was 16%. Net income was \$5.2 billion or \$1.80 per share.

Capital expenditures were \$3.4 billion, driven by investments in datacenters, servers, office, buildings and network infrastructure. Note that this is a decline 11% compared to last year, primarily due to a pause in the datacenter construction for roughly half the quarter due to the shelter-in-place measures. We have since resumed our datacenter construction efforts with proper safety precautions in place. In Q2, we announced a new datacenter in Illinois, which will be supported by 100% renewable energy. We remain committed to minimizing our environmental impact, and earlier this month, we published our inaugural sustainability report, which is available on Facebook sustainability website.

Free cash flow was \$514 million, and as a reminder, this is net of the \$5 billion FTC settlement that was paid in Q2, but as previously noted, was expensed in 2019.

We purchased \$1.4 billion of our Class A common stock and ended the quarter with \$58.2 billion in cash and investments. In July, we closed our investment in Jio Platforms Limited and paid approximately \$5.8 billion in cash.

Turning now to the outlook. As I mentioned earlier, we are seeing signs of normalization in user growth and engagement as shelter-in-place measures have eased around the world, particularly in developed markets where Facebook's penetration is higher. Looking forward,, as shelter-in-place restrictions continue to ease, we expect a number of Facebook DAUs and MAUs to be flat or slightly down in most regions in Q3 compared to Q2.

In the first three weeks of July, our year-over-year ad revenue growth rate was approximately in line with our Q2 ad revenue growth rate of 10%. We expect our full quarter Q3 year-over-year ad revenue growth rate to be roughly similar to this July performance. There were several factors contributing to this. First, continued macroeconomic uncertainty, including the pace of recovery and the prospects for additional economic stimulus. Second, the expectation that some of the recent surgeon community engagement will normalize as regions reopen. Third, the impact from certain advertisers pausing spend on our platforms, related to the current boycott which is reflected in our July trends. And lastly, headwinds related to ad targeting and measurement, including the impact of regulations such as the California Consumer Privacy Act as well as headwinds from expected changes to mobile operating platforms, which we anticipate will be increasingly significant as the year progresses.

Turning now to expenses. We expect total expenses in 2020 to be in the range of \$52 billion to \$55 billion narrowed slightly from our prior range of \$52 billion to \$56 billion. We expect capital expenditures to be approximately \$16 billion at the high end of our previous \$15 billion to \$16 billion range as we have resumed center construction efforts earlier than expected. However, a great deal of uncertainty remains in our outlook and our full-year capital expenditures will depend on how the pandemic impacts our ability to construct datacenters and refresh equipment.

Turning now to tax. We expect our full-year 2020 tax rate to be in the mid teens, although we may see fluctuations in our quarterly rate depending on our financial results. We are proud that the role Facebook has played in keeping people connected during the COVID crisis and the role that we have played in helping businesses reach consumers online during these challenging times.

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

Questions And Answers

Operator

We open the lines for a question-and-answer session. (Operator Instructions) Your first question comes from the line of Eric Sheridan from UBS.

Q - Eric James Sheridan {BIO 17860961 <GO>}

Thank you so much for taking the question and thanks for all the color in the commentary. Maybe two if I can. In terms of what you want to accomplish on e-commerce for the platform broadly over the medium to long term, what are the key investments and sort of launch initiatives we should be looking for from the outside in that are still part of the building blocks to accomplish sort of the announcement around Facebook Shops, all the excitement about bringing more and more merchants and sellers on the platform globally. Just want to understand sort of the pathway forward both in terms of either the initiatives or maybe even the numbers.

And then maybe one quick one on the advertising side, how much of the headwind is the current brand advertising environment? We continue to hear about direct response advertising trends improving quickly and maybe even in some verticals back to existing pre-COVID levels. How should we think about the recovery in brand advertising and what headwind that might be for the platform as you look out to the second half? Thanks so much.

A - Mark Zuckerberg {BIO 15103277 <GO>}

Yes, I can take the second -- the first part and then Sheryl can probably take the second one. In terms of the big milestones for small businesses and commerce, we're mostly focused on two types of products. The first is Shops, which we started rolling out a lot more broadly this year and what that basically allows any small business to put in a catalog and then have a shop across Instagram and Facebook to start eventually across all of the apps, you'll be able to bring up a shop and you'll be able to transact across all of that. We're building out Facebook Pay to make it to that you buy something in one place, your credit card is stored, it's easier to do follow on transactions in any of the apps. It will be a better consumer experience and sales will convert better. There will also be a natural value for small businesses of being able to connect the advertising that they're doing across their services with their shops to be able to go from inspiring somewhat at the top of the funnel, all the way down through driving sales. So that's going to continue scaling it. We'll have more to share there on metrics in that soon.

The other area that I'm quite excited about is messaging commerce. And what we're seeing there is, it's particularly important especially in developing countries. But we are seeing a lot of small businesses just conduct a significant portion of their business over Messenger or over WhatsApp. And in the medium term, I think the way that we're probably going to build a business around that, we already offer the business API and that will be meaningful, but there are also these click to messaging ads which have been more successful than I think we had even hoped would that basically allow people to get customers' attention in especially Facebook and Instagram and direct them to a thread where they can do commerce and messaging. Messenger to start and we're really working on ramping that up in WhatsApp as well.

But as payments grow across Messenger and WhatsApp and as we're able to roll that out in more places, I think that that will only grow as a trend.

So those are the two areas that we're really focused on e-commerce. It's worth noting, like I said in my opening remarks, this really is primarily focused on small businesses, individual entrepreneurs. Small businesses are the biggest part of our business, not the large businesses, of course, we want them to be using our platform too. We want to serve everyone.

But if you as investors or analysts or anyone who is thinking about our business, really the accurate way to think about what we do is that we are in the business of serving small businesses and all of these different things that we're doing are going to be geared towards enabling those folks to grow, reach customers and create jobs around the world.

A - Sheryl Sandberg {BIO 15339456 <GO>}

I can talk about the trends in brand advertising. I think what we've seen not just this quarter, but for many years, is that advertisers large and small are really interested in measurable results. I think that's the best thing we offer, and that's what people come to us.

I think sometimes think of brand advertisers as a large advertisers and certainly large advertisers often do brand campaigns, but both large and small advertisers we see on our platform are increasingly interested in measurable results. We also believe that we provide a better advertising experience for both the marketer in terms of ROI and the end user in terms of seeing something that they're more interested in when the ads are more personalized and the more, they're driving to a measurable result, the more they tend to be targeted to a specific audience, and I think the better they work. And so we're definitely seeing a trend towards what you said in this question as direct response, but it's not just direct response anymore. It's any kind of measurable result and we offer a lot of different actions you might want someone to take. And that is definitely and much more important than brands in driving our business, has been for a while and that trend continues.

Operator

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

Q - Brian Thomas Nowak {BIO 16819013 <GO>}

Thanks for taking my question. I have two. One for Mark, one for Dave. Mark, the first one is on India, you've made a series of investments in the last couple of years there. Can you talk to us about sort of your vision for the product offering and the consumer and the SMB pain points you're most focused on solving and the investments that you need to really make there to create that into a real business for Facebook?

And then secondly, Dave, it seems like you're talking about more than 50% of the employee base essentially working remote next five years to 10 years. I understand you're not going to give us sort of math or quantify, but maybe just talk to us about some of the puts and takes in areas where you could see long-term efficiency internally for more people working remote as well as potential higher costs from a larger remote workforce? Thanks.

A - Mark Zuckerberg {BIO 15103277 <GO>}

Sure. I can take the India question. It's very connected to what I was just talking about around message commerce. A lot of people use WhatsApp, especially in India, there is a huge opportunity to enable small businesses and individuals in India to buy and sell things through WhatsApp. We want to enable that. That starts with enabling payments. A big part of the partnership that we have with Jio will be to wire up and get thousands of kiranas, small businesses across India on-boarded onto WhatsApp to do commerce there. and we're really excited about the opportunity there. And once we prove that out with Jio in India, we are planning on expanding it to more folks in India and to other countries as well. But there is no doubt that India is a huge opportunity. It is the largest country by the size of our community that we're serving already. It should be one of the faster growing business opportunities as well to help businesses grow there. And we're very excited about that.

Before I hand it over to Dave to talk about the remote work, I'll just add that on principle, the reason why we're shifting to more remote work is we think that culturally it will allow us to attract more talented people. We're not doing this primarily as a cost-saving measure. So Dave can talk a bit about his analysis there, but I don't think we really have a clear picture of how that might play out, but I can tell you that that's not the primary goal of how we're approaching this.

A - Dave Wehner {BIO 2419389 <GO>}

Yes, Mark. That's consistent with what I was going to say to Brian. The main thing we're trying to do was access a greater talent pool, which ultimately might give us more opportunity to grow headcount. So I think there is an effect there that's I think in addition to cost in the sense that we would have a greater pool of people that we could recruit from. And so I think that's one thing to think about. And then, yes, there might be some savings on office and amenities and the like, but that's potentially offset by more travel to do to be able to bring people into offices and for our sites and other things to be able to collaborate effectively. So we don't know exactly where the puts and takes are going to come out on that.

Operator

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

Q - Justin Post {BIO 3469195 <GO>}

Great. Maybe I can ask one shorter term and one longer term. You've guided a 10% in July and for the quarter about the same for ad revenues. Could you talk about some of the potential headwinds in the second half a little more detail, especially any Apple IDSI [ph] changes or how that could impact your business?

And then on the longer term, Mark, I believe four or five years ago, you talked about messaging and you're aware of the Asia comps, do you feel like that business is really starting to gel and materialize, you obviously had some positive comments and can that be something that starts to contribute in two or three years? Thank you

A - Dave Wehner {BIO 2419389 <GO>}

Okay. I'll take the first one there, Justin. So, I mean there is going to be a few factors that are obviously important in the second half. One of the things that we called out was the macro side of things, which we don't know precisely how the overall economic climate is going to develop, but we do know that some stimulus is probably flowing to some extent through to our business and the current CARES acts, for instance, is expiring at the end of July and we don't know what the subsequent economic stimulus will look like. And to the extent that stimulus decreases in the future and recession lingers, that could impact consumer purchasing power for advertisers in areas like e-commerce, so that we'll have to see how that plays out.

In addition, we did specifically call out changes on mobile operating platforms and that as you correctly identified, we specifically with the Apple latest announcement regarding iOS 14 in mind. So this is one of the factors that has -- that is included in our outlook for Q3, but it really will have more of a pronounced impact in Q4 and beyond, given the rollout begins late in Q3.

We're still trying to understand what these changes will look like, and how they will impact us and the rest of the industry. But the very least, it's going to make it harder for app developers and others to grow using ads on Facebook and elsewhere. So, advertising clients are asking us how to maintain their performance and we're working on it. But our view is that Facebook and targeted ads are a lifeline for small businesses, especially in a time of COVID. And we are concerned that aggressive platform policies will cut that lifeline at a time when it is so essential for small business growth and recovery.

Operator

Your next question comes from Ross Sandler from Barclays.

A - Mark Zuckerberg {BIO 15103277 <GO>}

Okay. I guess I can talk about the messaging business. It's -- overall here, it's basically the levers that I've talked about so far on this call. I think it's taken us a little longer than I would have hoped for payments to get released on WhatsApp in a number of countries, that's certainly a building block. The WhatsApp business app is growing incredibly quickly though in terms of number of businesses who are signed up for that. So that part of the ecosystem I think is going quite well.

API adoption is growing reasonably well as well for businesses. The click to messaging ads are valuable for businesses. But we're seeing them more use -- that shows up more in kind of the revenue and the ads that we're seeing on the Facebook and Instagram side than registering direct commerce that's happening inside the the messaging apps, but it's useful nonetheless. I mean I think we're pretty open to where the revenue comes to us. But we're pretty focused on making sure that we can help small businesses grow and find customers and connect and helping people interact with all of the individuals, all the friends that they want and then all the businesses that they interact with, increasingly, I think that there is -- that's that's becoming part of one broader platform. I certainly think that's happening in messaging and continue to be very excited about that.

Operator

Your next question comes from Ross Sandler from Barclays.

Q - Ross Adam Sandler {BIO 15948659 <GO>}

Great. Just to follow up on the SMB commentary. So Dave, you mentioned that that was the primary driver of growth. And we appreciate the top 100 mix down to 16% versus I think 20% four years ago. So it seems like that's been coming down steadily. I guess the SMB side, it's a little counter-intuitive with so many business, the failures going on with COVID. So can you guys just talk about, is it the penetration of the 60 million SMBs already on Facebook in terms of the buyer -- app buyer penetration that's going up or what's driving that resurgence in growth from SMBs in the current environment? Any color there would be helpful.

A - Sheryl Sandberg {BIO 15339456 <GO>}

Yes, I think it's both. When you think about SMBs, you're certainly right that a lot of businesses are struggling. But at the same time, businesses have to pivot online, and so on this call, we updated our overall numbers. We now have over 180 million businesses using our free tools and we now have over 9 million advertisers. So what we're seeing is that increasingly businesses of all sizes but including small businesses have to find their customers online, people aren't walking into stores as much, have to find new ways to deliver products like curbside pickup, like shipping. So they are increasingly moving online. And you see a lot of businesses around the world that even in very developed markets like the United States before this not even having a website of any kind. So we become a place you can set up a website, set up a digital storefront. It's free. It just takes minutes. You know how to do it, because you've already used Facebook or Instagram as a consumer.

So we're just seeing more and more businesses migrate online and we're seeing more and more businesses become advertisers. This acceleration of e-commerce, you're seeing it not just with us but if you look at all the verticals out there, things that can be done online are obviously doing better in this time than things that rely completely on things that are offline. But it really is just an acceleration of a trend we've all seen for a very long time. The Coronavirus crisis is making this happen more quickly, but the migration online and migration to using very personalized ads to find people who are interested in your products is something that we've -- I think helped drive and are continuing to help drive, and we're proud of the role we play on this. It's really important for job growth around the world and for the health of small businesses.

Operator

And your next question comes from the line of Doug Anmuth from JPMorgan.

Q - Douglas Till Anmuth {BIO 5591566 <GO>}

Thanks for taking the questions. I just wanted to dig a little deeper on some of the e-commerce topics. Sheryl, I know it's still early obviously with Facebook Shops. I was hoping you could help us understand the feedback and traction you're seeing there. And then just, when you think about monetization over time, do you expect more of that through incremental advertising dollars or through commission fees of sellers' use checkout?

And then second, Mark, can you comment on your efforts with WhatsApp Pay in India, in Brazil and I know you've met some resistance there. How does that get resolved in those markets? Thanks.

A - Sheryl Sandberg {BIO 15339456 <GO>}

So we launched Shops in May as you know and Shops give a really immersive full screen storefront, so it enables businesses to build their brands and drive product discovery. If you think about what we've done for a really long-time, we exist in many ways at the top of the funnel and we help drive people down, but we are a great place on Facebook and Instagram for discovery. And then increasingly, we're able to drive people down the funnel, all the way through the purchase.

So Shops helps do that on the advertisers side, but they also help small businesses with free online tools. We're very committed to this, but in terms of how it's going, it's very early. We are seeing nice results from businesses and the people who are using these Shops. Our focus is getting the product experience right. And as we do, we're going to make it available to more and more businesses.

If you look into the foreseeable future or several years future, advertising is such a high margin business that obviously it contributes much more to the bottom line than any other fees we might charge. And I think we see this as really focused on increasing the experience people can have, going all the way through the funnel of purchase on Facebook and the experience businesses can have and closing that loop and selling

online and migrating online. That's more important than the actual incremental dollars you would get from any fees charged by these services.

Operator

(Multiple Speakers) Your next question comes from the line of Youssef Squali from SunTrust.

A - Dave Wehner {BIO 2419389 <GO>}

Sorry. We missed out the second part of that question.

A - Mark Zuckerberg {BIO 15103277 <GO>}

Yes, I mean there wasn't much of an update here. I mean I was just saying that we're working with regulators in those countries and are optimistic that we'll be able to move forward, although it's taking longer than we would ideally like.

A - Dave Wehner {BIO 2419389 <GO>}

Okay. We can go to next question.

Operator

Your next your next question comes from Youssef Squali from SunTrust.

Q - Youssef Squali {BIO 1506420 <GO>}

Great, thank you. Switching topics a little bit, Mark, one area where we're seeing just incredible growth in engagement is online gaming and streaming in particular, you guys recently got Mixer from Microsoft, it looks like Facebook is now firmly in third place in that market. What is your value proposition to gamers relative to the big competitors basically Twitter and YouTube? How do you monetize it over time, is it. as Sheryl just talked about on a different topic, mostly advertising? And is it conceivable that gaming may become kind of the third leg of that stool, your third largest revenue source over time after Facebook and Instagram? Thanks.

A - Mark Zuckerberg {BIO 15103277 <GO>}

So, the value proposition is community. And that's true for all kinds of creators, who are posting content and video like what we're doing in Watch as well. Our channels are ones where you're not just distributing content, but you're building up a community and able to communicate with people in a number of ways, which is something that is just a lot harder to do on a YouTube or a Twitter or other products like that even though those are also great products for streaming. So we're seeing that on gaming. A lot of people appreciate that. We're also able to distribute the video and get it to a lot of people, so that part is working well too.

I agree with you overall that gaming is going to be increasingly important in the future. The other area of course where we have a very large investment in gaming is the area

around virtual and augmented reality. With that, a big part of the use there, I mean we're seeing exciting work both from independent developers and large AAA developers and increasingly some of the in-house studios that we've acquired as well.

So we're going to continue focusing on gaming. I agree that, that's a big area.

A - Dave Wehner {BIO 2419389 <GO>}

Yes. And I would just add, Youssef that gaming continues to be a top five vertical for us in terms of advertising and we saw strong growth in the second quarter, especially in the beginning of the quarter when prices were lower in the auction, we saw a lot of demand from our gaming advertisers. And so I think a good example of where the auction is very effective at filling in. So we continue to be important top of the funnel discovery for game developers around the world.

Operator

And your next question comes from the line of Heather Bellini from Goldman Sachs.

Q - Heather Bellini {BIO 2268229 <GO>}

Great. Thank you so much for taking the question. Most of them have been answered, but just a couple of quick ones. Dave, I was wondering if you could just, you gave us some great commentary to think about Q3. So thank you for that. Just wondering if you could share with us kind of pricing trends at the end of the quarter and into July?

And also just given the uncertainty on the second half of the year for all the reasons you mentioned, any comments you want to share with us on kind of how to think about even qualitatively seasonality in Q4?

A - Dave Wehner {BIO 2419389 <GO>}

Hey, Heather. Yes, I think to get the second part of your question, I think it's going to be really hard in to look into Q4 with any certainty here given we just don't know what the macroeconomic situation is going to look like. It's hard to predict, August and September, much less looking that far into the future. And I think that's going to be a big thing to think about. I think clearly e-commerce will continue to be really important as we go into Q4, given that big macro theme for us in the whole industry has been the strength of e-commerce through the second quarter. So I would expect that play into the fourth quarter as well to some extent, as with the holiday season.

In terms of pricing trends, we did see pricing improved through the quarter. So early in the quarter, demand was much weaker. So we saw pricing depressed throughout the throughout the world and we saw, as I mentioned, just before to Youssef, we saw backfill with some advertisers coming into taking advantage of low prices for like games, e-commerce providers as well, and then as prices improved throughout the quarter, we saw some of those advertisers pull back as others came into the auction and began winning more, but it continues to be as noted from the price volume metrics in the script, it

continues to be a depressed environment. And so, we're obviously just from a macroeconomic perspective concerned about that.

As we get further into the year as well, I do want to point out, we've got targeting -- advertising targeting and measurement headwinds, that will affect pricing as well. That will be, we believe more pronounced in Q4, given some of the, for instance, the Apple IDSA changes, which I think could prove to be a challenging headwind.

Operator

Your next question comes from the line of Mark Mahaney from RBC.

Q - Mark Stephen F. Mahaney {BIO 3027058 <GO>}

Thanks. I wanted to ask about the addressing the boycott issues, and Mark, I particularly want to ask whether you think there is a reasonable efficient solution in here? I know how you come out and you've been pretty clear about your thoughts on trying not to moderate too much content, trying not to be in that role, but are there the solutions that you've talked about and introduce things like labeling. Is that not addressing the issues, the concerns of some of the boycott participants, how hard you think it will be to address their concerns?

And then if I could stick on this with political advertising. I know you've said in the past you didn't think it was that material, but the numbers are relatively sizable. We're talking about a couple of billion, it should be online. And I think as far as I can tell, Facebook offers just about the best way to do political ad targeting different districts et cetera, why wouldn't you see a reasonable boost to ad revenue in the back part of this year from political ad campaigns? Thanks a lot.

A - Sheryl Sandberg {BIO 15339456 <GO>}

I can talk about the ads boycott. So it's an interesting situation we find ourselves in, because I think oftentimes when companies are boycotted it's because they don't agree with what boycotters want, and that's not true it all here. We completely agree that we don't want hate on our platforms and we stand firmly against it. We don't benefit from hate speech. We never have. Users don't want to see it, advertisers don't want to be associated with it. And we've been working for a really long-time to get better at this to finding it. And as I said in my remarks, I think in many ways we lead our industry in transparency and execution. We're going to keep working really hard at this not for financial reasons or advertiser pressure, because it's the right thing to do.

In terms of how we resolve it, we work across the board, we have worked with and continue to talk to the civil rights organizations that are boycotting us. We had a meeting with them and Mark, a few weeks ago. We continue to work really closely with other civil rights organizations, as well as our civil rights auditor on the many improvements we're trying to make. But we're also working with industry and groups that I think can be really helpful, GARM and MRC particularly, GARM is working with us to partner on brand safety standards to help us come to definitions and independent oversight for the industry and we're optimistic that we'll be able to work with them to address advertiser concerns.

We're also working with the Media Rating Council, the MRC, and undertaking an independent brand safety audit and we'll be able to share the scope of that by the end of Q3.

A - Dave Wehner {BIO 2419389 <GO>}

And Mark, just it's Dave on political ads. I mean I think the fact is we just have such a large and diversified advertising business and political ads are just a small part of the overall advertising landscape even in election years. So we factored in the 2020 political advertising spend as part of our Q3 commentary. And again, I would just point to the backdrop factors that I outlined in my comments in terms of things out there including macroeconomic headwinds, normalization of engagement trends when COVID restrictions ease, the boycott and then headwinds on targeting and measurement.

A - Sheryl Sandberg {BIO 15339456 <GO>}

Operator, we have time for one last question.

Operator

Your last question comes from the line of Mark Shmulik from Bernstein.

Q - Mark Shmulik {BIO 21311083 <GO>}

Yes. Hi. Thanks for taking the question. So the first, I know we've talked about this a little bit. But with WhatsApp business growing to 50 million users, and I think the last number there was 5 million. That's pretty astounding growth. Any color you can share on what drove that growth?

And then secondly, as you know, as we just think about the growth kind of quarter-to-date in July, and I know you called out the rest of the world was the one that declined due to structural headwinds, any incremental color you can share if some of that's been resolved or what that looks like? Thank you.

A - Dave Wehner {BIO 2419389 <GO>}

I can take the second part. I guess first on the rest of world. So I think what you've got going on in terms of rest of world weakness. There is probably I think a few factors. First, you've just got foreign currency headwinds, particularly in places like Brazil and so that played a role in the year-over-year decline in rest of world. Secondly, rest of world had a lower exposure to what I'd call sort of online verticals, things like e-commerce and games and it's more exposed to things like traditional retail and brand. And with COVID, the online verticals performed well and those dependent ultimately like on in-person conversions and interactions less so. So I think that impacted rest of world as well.

And then finally, it's not clear whether stimulus in the developed world also played into it, it gave more strength in those markets as opposed to rest of world. That could also be part of the relative strength in more of the developed world rather than the developing world.

FINAL

A - Mark Zuckerberg {BIO 15103277 <GO>}

And on what's driving the growth in WhatsApp business? I mean I really just think it's a good simple product execution and there is a ton of organic demand for people to interact with businesses and I think for small business owners in particular to have some separation between their personal WhatsApp accounts and their business accounts and some of the additional features and tools that you get through WhatsApp Business to be able to connect with people and manage that a bit better.

So, I think that that will continue growing quite well. And we have a long roadmap ahead to build up all the different commerce features that we talked about on this call, but also have been talking about for a while now. And I think that that's one of the exciting opportunities ahead of us that we're going to be focused on building for the next few years years, but which we think is pretty fundamental for serving people and enabling small businesses and entrepreneurs around the world. We're excited to get at it.

A - Sheryl Sandberg {BIO 15339456 <GO>}

Great. Thank you 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.

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