

## Business

- Facebook:
    - ↳ Increase of 17% in DAV (1.04 billion) + 25% increase in mobile DAVs (934 million)
    - ↳ Biggest source of engagement is News Feed which displays an algorithmically-ranked series of stories + ads individualized for each person.
  - Instagram for photos + video sharing
  - Messenger for messaging for individuals + businesses.
  - WhatsApp for messaging fast.
  - Oculus: VR technology
- Substantially all revenue comes from ads that can appear on FB, Instagram, 3rd party apps + websites.
- Technology:
    - ↳ Centered on continuous innovation creating + improving products that are social by design.
      - ⇒ place people + social interaction at the core of product experience.
    - ↳ Significant investments in tech to improve existing products + services + develop new ones, as well as for marketers + developers.
    - ↳ Investing long term in connectivity efforts, artificial intelligence research, + VR, to develop tech FB believe will help them better serve communities.
      - \* Seems to be first time mention AI in their IRK as a research point.
  - Employees: 12,091 ⇒ increase from around 9K.
    - ↳ Continue to increase headcount at a strong rate.

## RISKS FACTORS

### BUSINESS + INDUSTRY

- New products / changes to existing may fail to attract / retain users / generate revenue.
  - ↳ Oculus: FB has no experience with this type of technology.
  - ↳ WhatsApp + investments in growing Messenger when service isn't monetized / efforts to monetize in the future might not be successful.
- Local + Foreign laws + regulations regarding privacy, data protection + other matters.
  - ↳ In October 2015, the European Court of Justice invalidated the European Commission's 2006 Safe Harbour Decision as a legitimate basis on which FB could rely for transfer of data from EU to US.
- Plan to continue making acquisitions.
- Technologies have been developed that can block the display of FB ads.
  - ↳ Particularly on personal computers.
  - ↳ If these technologies continue to proliferate, particularly in mobile, it will continue to have adverse results.
- All payment revenue is generated in personal computers. Expect to continue to decline in the future.
- Design, manufacturing + supply chain risks ⇒ new risk specified due to Oculus.
  - ↳ Relies on 3rd parties to manufacture Oculus products.
  - ↳ SEC's conflict mineral rule requires public companies to disclose origin, source + chain custody of specified minerals.
- Inventory Risks due to Oculus:
  - ↳ Rapid changes in product cycles + pricing, defective merchandise, change in consumer demand + spending patterns, change in consumer taste with respect to Oculus products.

### OWNERSHIP OF CLASS A COMMON STOCK

- FB does not intend to pay dividends.
- ↳ Will reinvest. Currently contain a restriction due to their credit facility.

## PROPERTIES

- Entered into an agreement to lease an entire office building in London, UK.
  - ↳ Currently under construction.

## Selected Financials

- 44% increase in revenue + 56% increase in costs.
- Reduction of Operating Margin from 40% to 35%.
  - \* Based assumption done in 2014 that since WhatsApp + Oculus are not adding significant sales + their focus is in growing / developing, FB revenues will be financing these companies.

## Management Discussion + Analysis

- 3 Revenue Growth Priorities:
  - ↳ Capitalize shift to mobile
  - ↳ Grow # of marketers using ad products
  - ↳ Make ads more relevant + effective through continued adoption of newer ad formats + tools for marketers.
- Investment Priorities:
  - ↳ Core products + services
  - ↳ Next generation services (Instagram, Messenger + WhatsApp)
  - ↳ Long term innovation efforts ⇒ connectivity efforts, VR, AI Research.

### TRENDS in USER METRICS

- User metrics do not include Instagram or WhatsApp users.

METRIC	Δ YoY	DRIVERS
DAU	17%	Mobile usage ⇒ Desktop usage is decreasing
Mobile DAU	25%	Increase of 34% of only mobile users
MAU	14%	Mobile usage ⇒ Desktop usage is decreasing
Mobile MAU	21%	Increase of 56% of only mobile users.
ARPU	27%	\$11.9¢ with largest increase in the US.

- \* These metrics do include the use of the Messenger app

## COMPONENTS OF RESULTS OF OPERATIONS

- Cost & expenses main increase was in R+D which almost doubled in value.
  - ↳ Almost half of the R+D costs were share-based compensation expenses.
    - ⇒ Share-based compensation expense YoY was fairly the same for all other cost divisions.
    - ⇒ R+D almost doubled which heavily increased share-based compensation (went from 11 to 13% of revenue).
- Decrease in Payment Revenue for the first time

## REVENUE ↑44%

- Increase in News Feed ads on mobile.
  - ↳ Estimate mobile represents 77% of total ad revenue.
- Factors that influenced growth in mobile ads:
  - ↳ Increase in demand for ad inventory driven by increase in # of advertisers.
  - ↳ Increase in mobile user growth & engagement.
  - ↳ Increase in frequency + number of ads displayed on News Feed, as well as quality, relevance & performance of those ads.
- Avg price per ad increase of 140% + # of ads delivered decreased by 38%.
  - ↳ Avg price increase driven by non-News Feed product change during Q3 2014 which decreased # of ads but increased prominence.
  - ⇒ Also affected by greater percentage of ads being shown on News Feed.
  - ↳ Reduction in # of ads is due to change above + shift to mobile.
- Decrease in payments ⇒ decrease in revenue from games played on personal computers, partially offset by an increase in other fees revenue related to acquisitions closed in second half of 2014.
  - ↳ With shift towards mobile use, expected to continue decline in the future.
- No customer represented +10% of revenue.
- Strengthening of US dollar vs. foreign currencies (primarily euro) had an unfavorable impact on revenue.
  - ↳ Full year results would have been \$119 higher.

## COST OF REVENUE ↑33%

- Slight decrease as a percentage of revenue.
- Increase in operational expenses related to datacenters & technical infrastructure.
- Amortization of intangible assets increased due to full year impact of acquisitions.
- Expect 2014 to increase as they continue to expand datacenter capacity + technical infrastructure to support user growth, increased engagement & delivery of new ad services + products.

## RESEARCH + DEVELOPMENT ↑81%

- Growing at a faster rate than revenue ⇒ has consistently weighed more % wise each year.
- Driven by share-based compensation expense ⇒ full-year impact of acquisitions.
- Employee headcount growth of 45% ⇒ increase in payroll + benefits expense.
- Plan to continue hiring in 2014.

## MARKETING + SALES ↑42%

- Also growing at a faster rate than revenues.
- Increase in amortization ⇒ full year impact of acquisitions.
- Increase in payroll + benefits ⇒ +32% employee headcount.
- Increase in marketing expenses.
- Plan to continue increasing in 2014.

## GENERAL + ADM ↑33%

- Slight decrease as % of revenue.
- Increase of 36% in employee headcount.
  - ↳ Increase in share-based compensation.
- In lesser extent higher legal + other professional services fees.
- Plan to continue increasing.

## INTEREST + OTHER INCOME/EXPENSE, NET ↑63%

- Decrease in foreign exchange losses.
- Increase due to higher invested cash + interest rates.

## LIQUIDITY + CAPITAL RESOURCES

- \$1.90B held by foreign subsidiaries. **Bookmarked P53** ⇒ Trapped Cash.
- FB adds back share-based compensation expense of \$290B to their Cash Provided by Operating Activities. \*Validate how this impacts results\*
  - ↳ They do the same every year.

## NOTES TO FINANCIAL STATEMENTS

- Acquisitions:
  - ↳ Completed several business acquisition for a total of \$488 M.
    - ⇒ Related to business combination involving land & buildings adjacent to their HQ
    - ⇒ Were not material to financial statements.
- IPR+D: technological feasibility has not been established + they have no alternative future use.
  - ↳ Continued to be accounted for as indefinite intangible assets ⇒ no amortization.
- Operating lease: **Bookmarked P78**
- FB has a financing obligation, building progress - leased facility
  - ↳ Lease agreement in London, UK
  - ⇒ Values representing what the lease obligation will be. Includes \$62M that is included in PP+E.
  - \*Already capitalized.
- # of shares: **Bookmarked P80**
- Stock Options: **Bookmarked P81**
- FB has US federal + state net operating loss carry forwards.
- Revenue by geography: **Bookmarked P84**
- \*FB made an amendment including information required by Items 10-14 of Part III
  - ↳ Includes information on Management, Board of Directors, compensation package for management.
  - ⇒ Summary of compensation table in P.116.