

EARNING CALL Q2

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MARK

- Strong engagement strong across all apps.
- Exciting timeline for 2023
- Threads: seeing more active users than expected
 - ↳ Built by a small team aligned to year of efficiency
- Focus of 2024 of continue being lean
- AI recommended content +7% time spent
 - ↳ Reels is a key part of this
 - ↳ Seeing good progress in monetization.
- AI also monetize in ad tools used by most of advertisers.
- Paid messaging has doubled YoY.
- Partnered with Microsoft for Llama
- New products using Llama
- Quest 3 → mixed reality mainstream
 - ↳ Roblox coming to Quest. Horizon - team is focused on retention.

Rest of 2023 will be about creating stability for employees, removing barriers that slow them down, introducing new AI-powered tools to speed them down, and so on.

Headcount growth will be low. Many teams chose to let people go in order to hire different people with different skills they need - much of that hiring is going to spill into 2024.

Meta Advantage - almost all advertisers are using at least one of their AI-driven products.

Announced that WhatsApp Business users will now be able to create Click-to-WhatsApp ads for FB & IG without needing an FB account. # of businesses using paid messaging has doubled YoY.

Partnership with Microsoft to open source Llama 2 to make available for research and commercial use.

SUSAN

- Online commerce was up due to China reaching other markets
- Focusing on monetizing more efficiently Reels & Messaging.
- Leveraging AI to improve platform + products
- On-site conversion w/ click-to-massage ads.
- Bond offering in may?
- EU-US Data transfer → good news
 - ↳ See more regulatory headwinds.

- FoA represents 82% of overall expenses.
- RL revenue -3% due to lower Quest 2 sales.
- Reels continues to drive incremental engagement, especially through recommended content.
- Making progress with Reels monetization with 3/4 of advertisers now using it.
- Daily Ad Revenue of click-to-WhatsApp continues to grow quickly (+80% YoY)
- Investing in scaling other onsite objectives like lead generation and Shops Ads.
- Remain focused on evolving capital structure. Executed second bond offering in May and expect a measured pace of future debt raises as they work on improving overall cost of capital while maintaining positive/ neutral net cash balance.
- Continue to monitor regulatory landscape - positive development with European Commission's adoption of final adequacy decision which allows Meta to continue to provide services in Europe.

QUESTIONS

- ① Use cases for AI. Larger tech barriers to scale agent products.
Specifically about AI agents/ assistants built through Llama - use cases and technological barriers will need to overcome to scale across ecosystem.
↳ Turn into Connect.
↳ Llama 2 model will enable more products.

↳ 3 basic categories

→ Agents, Gen AI powered features (helping advertisers provide ads), productivity & efficiency internally (coding, etc.)

↳ Agents:

- Don't think there's going to be one single AI that people interact with.
- There will be a handful of experiences to connect with creators.
- Helping people to connect with businesses.
 - ↳ Improve interaction
 - ↳ Will also help Messaging business
- Will follow same playbook they do on product.
- Don't know how fast it will scale but want to have the capacity on hand.

- ② Extension of developer community. Microsoft announcement → shift to enterprise?
RL losses increase → color of components & ROI?

- Llama: we open source gets community standardized → makes recruiting easier.
- Safety & security expect to see improvements. Being open source means more eyes.
- Efficiency improvements. → will help w/ Meta Capex.
- Partnered with Microsoft b/c they don't have a public cloud offering.
- ↳ Enterprise users which resell have to do a deal with FB.

Gives example of Microsoft, Amazon or Google who could through their cloud offering resell the services, they believe in this case they should get some portion of the revenue. In the near term, does not expect to be a big revenue source but in the long term can be something.

• RL: will not break out numbers.

↳ Quest 3 → biggest release since 2020 → for 2024.

OUTLOOK:

- Higher depreciation expenses due to previous investments.
- Increase in payroll as they evolve workforce composition towards higher-cost technical roles.
- RL operating losses to increase significantly due to ongoing product development efforts in VR/AR and investments to further scale ecosystem.
- Reduction in 2023 CAPEX - cost savings + shift to 2024 from delays in projects and equipment deliveries rather than a reduction in overall investment plans.

↳ Later CFO states that they don't expect Llama to result in a separate topline enterprise revenue line

A lot of expenses related to bringing Quest 3 to Market. In the near term, is driver of many of the losses.

- ↳ Continue to work in AR, VR + Neural interfaces
- ↳ Likes that industry is also developing → gives confidence.
- ↳ Are leading in these areas.
 - long-term focus for evaluating ROI
 - ↳ Expect RL losses to increase, vision hasn't changed.

* Believes they have shown they can deliver good results in the near term while investing ambitiously in the long term.

③ Prioritizing time / changing priorities.

Adoption of Advantage+ products - driving improved results vs. rest of sector?

- Priorities have been consistent for a few years.
- Two segments that exceeded expectations: Llama + Threads.
- Expect focus on AI + the metaverse.
 - ↳ AI includes: Gen AI, tools for efficiency, recommendation systems.
- RL not getting adopted as fast as expecting but expect long-term to remain the same.
- DL revenue acceleration:
 - ↳ Lapping weak period
 - ↳ Improved Reels monetization + increased supply + improvements in performance.
 - ↳ Lower FA effects.
- Advantage Plus: seeing strong adoption in certain verticals
 - ↳ e-commerce + Retail: Continuing to launch features to unlock use cases for advertisers + make it easier for them to adopt Advantage+
 - ↳ A lot in the pipeline that they are excited about
 - ↳ Help advertiser to test ads quickly.
 - ↳ Promising area to continue to invest in.
 - ↳ Only one of the ways they are using AI to improve.

→ Talks about this in phases.

- ① Ranking + Recommendation + Safety Systems.
- ② GenAI: agents + additional features that will roll-out + other work focused on efficiency internally.
- ③ Metaverse

④ RL: ROI on the business.

- Helping shape next platform will help develop more products.
- Products will also unlock value for FA
 - ↳ Features that others don't allow to build.
 - ↳ More engagement opportunities.
- Long-term investments + thinks that will be the future.
 - ↳ Continual trends to be more immersive. (Text - photo - video transitions)

⑤ Learned from Threads. Lowered Capex (more specifics)

- THREADS:
 - ↳ TOO early to do this kind of analysis.
 - ↳ Haven't had success with standalone apps.
 - Doesn't know why it has worked still if its b/c of Twitter or what.
 - ↳ Great start so far but still much work to do.
 - ↳ Basic functionality to build + will later focus on growing + then worry on monetization.
 - Long-run: Adopting usual playbook to Threads.
- Capex: Cost savings in non-AI servers. Underutilized capacity + are trying to be more efficient.
 - ↳ Datacenter delays will shift to 2024 due to delays.
 - ⇒ 2024 capex will increase b/c of this + continued growth.

⑥ Open source. Q3 revenue outlook.

- Will continue to be both open source + not open models.
 - ↳ Since Meta's business is not focused on monetizing models very open source.
- Danger with open source: not at that point today. (Refers to everyone having access when it reaches a certain level of capability).
 - ↳ Not clear what that point would be.
- Different businesses will have open + closed.
- Easier b/c aren't selling access to models.
- Acceleration Q3: lapping weaker period, currency tailwind + will be benefitting from key priorities. Refers to past investments that have helped with monetization + increase engagement.

⑦ Capex: New products.

- Growth in AI investment is driving Capex.
 - ↳ Recommendation → feel good about ROI + continue to invest.
 - ↳ Setting up training clusters for Gen AI. Don't know what true capacity that is needed. (Training + Inference Clusters)
 - ⇒ Flexible → can shift some of Gen AI capacity to normal AI.

FOLLOW-UP Q1A TRANSCRIPT

- ① Reels & Threads: what goes into decision making process on when to leave a feature inside an app & when to make it a standalone app? Does it make sense to separate Reels from IG?
- Threads: what differences vs Twitter would get Threads to 1B users? (Twitter hit a wall around 250-300M)
- There is no black & white criteria to decide. Each option has its tradeoffs.
 - Reels is part of core experience in both FB & IG. Don't think they would break it out - complementary to the experience. Work done with Discovery Engine powering Reels has become important part of growing engagement.
 - Value proposition of Threads:
 - ↳ Openness. → Building decentralized interoperable experience
 - ⇒ Going to use Activity Pub social networking Protocol → people can be followed by people using their apps or other apps like Mastodon. Give creators broader reach.
 - ↳ Taking things they've learned from other apps to build productive & creative place to have conversations that are not just about news → broader discussion platform + share your ideas.

- ② Where do you think you are in terms of rebuilding ad tech stack post ATT?

Click-to-message ads → brand new advertisers? Would they have spent on another part of the platform or is it leading to incremental ad purchase?

- Have made meaningful improvements to performance & measurements.
 - ↳ Continue to grow conversions & receive constant positive feedback
 - ↳ Also have advertising facing AI & automation features like Advantage &
 - ↳ Feel good about how they perform relative to the market.
- Click-to-Messaging:
 - ↳ Supply: using same supply inventory in FB & IG
 - ↳ Demand: opens up a lot of new advertiser who may not have previously been interested.
 - ⇒ Specifically on the SMB side.
 - ↳ Click-to-Messenger is biggest since was first. Introduced later click-to-WhatsApp + click-to-IG Direct.
 - ⇒ Click-to-WhatsApp: growing fast → 80% YoY.
 - ↳ Continue to iterate & make easier to use for advertisers.

③ Will maintain OpEx split of 80-70 FdA-RL?

Reels adopted by 314 of advertisers. How was this done?

- Don't have OpEx numbers for 2024 yet.
 - ↳ 3 major themes for 2024 expense planning process.
 - ⇒ Infrastructure for AI investments
 - ⇒ Technical talent → high payroll expenses.
 - ⇒ RL
- Reels adoption: unlocked demand liquidity for Reels.
 - ↳ Started by bringing existing advertiser objectives into Reels.
 - ↳ Making Reels ad format more performant with a lot of new features to make ads more interactive + engaging.
 - ↳ Been able to increase ad load in Reels.

④ Legal-related expenses: increased G+A Guidance from \$1B to \$2B. How much is not recurring?

Reels: where is it on the monetization cycle?

- Q2 includes \$1.87B in legal expenses mostly related to IDPC + data transfer matter
 - ↳ IDPC was \$1.2B.
 - ↳ Continue to see increasing legal + regulatory headwinds in the EU + US.
 - ⇒ Adoption of guidelines that require penalties of % of global revenue for violation of certain regulations.
- Reels Monetization cycle.
 - ↳ Made good progress in reducing headwind.
 - ↳ Higher ad load + gained incremental time spent.
 - ↳ Expected neutrality by the end of the year.
 - ↳ Have to deal with fact that Reels come with slower scroll speed.

⑤ How did experience with content moderation affect vision for Threads?

What will happen when 1/4 of remain customers adopt Reels?

- Will apply what they have learned to deliver the ability to foster open + friendly + productive conversations.
- Reels: increased ad load but still remains well below feed + stories.
 - ↳ Will continue to test around structural constraint. Ex: show an ad on the bottom of an organic Reel.
 - ↳ Strategy is not based specifically on getting all advertisers on Reels.

⑥ Quest 3 Launch + Go to Market strategy.

Strategy around verticals (Retail, Social commerce) where transaction + payments fit in that strategy?

- Quest 3 is going to be a big improvement over Quest 2.
 - ↳ Going to establish MR as baseline for all headsets + hope will set the stage for AR glasses.
 - ↳ Hope it will appeal to both Quest 2 users who are looking to upgrade + new to category drawn by MR at a more accessible price than Quest Pro.
- Focusing on Shop Ads: expanded availability to all Shops with on-site check-out in the US.
 - ↳ Optimizing performance in the US before bringing to other markets.
 - ↳ Drives good results for advertisers.

⑦ Higher D/A next year. Process of evaluating useful life + potential for longer useful lives based on new innovations in datacenters + elsewhere?

- Extended useful life of CPUs → slowdown in performance gains.
- Still seeing strong performance gains in GPUs so those will depreciate on a shorter timeframe.
- Will continue to evaluate how to most efficiently use CPUs + GPUs across their fleet.

⑧ CapEx: have cut twice this year. How does it look like as a % of revenue?

Revenue Sustainability: Click-to-massage adoption in the West + China as a tailwind?

- Some of it is delays from projects of 2023 pushed to 2024.
- Cyclical component to capital intensity. They are at the precipice of some AI development. Hard to know right now.
- Historically have had a playbook of investing in consumer experiences first.
 - ↳ If there is an opportunity to build compelling retentive consumer experiences, they will do that + later find a way to monetize it. → Have been historically successful.
- Continue to see YoY Growth in Click-to-Massage in North America.
- Click-to-Messaging is mostly used by smaller advertisers.
 - ↳ Easy to use + alternative to having a website or app.
 - ↳ Focused on scaling with larger advertisers by investing in solutions to optimize for down-funnel objectives + enhanced reporting to meet their more complicated needs.
- Big opportunity for businesses to leverage AI agents to respond to messages at scale in the future.
- China ad spend accelerated → primarily in online commerce + gaming.

⑥ Marketing & Sales costs were down → Cause?

Expand on employee growth for 2024

Accelerated revenue outlook Better macro environment / internally driven?

• Headcount:

- ↳ Have reduced size through layoffs + have been in a hiring freeze.
- ↳ Some teams made deeper cuts to retool skill sets towards what they need going forward.
- ↳ Are being thoughtful about headcount budgets.
- ↳ Will see headcount #'s grow to reflect resumption of hiring freeze.
- ↳ Workforce will evolve towards more technical mix → higher cost.

• Marketing & Sales costs:

- ↳ Lower marketing spend + payroll → part of year of efficiency.
- ↳ Across-the-board budget cuts.

• Revenue:

- ↳ Lapping quarter with 4.5% deceleration → better comparison.
- ↳ Some stabilization → key segments like online commerce & gaming.
- ↳ Currency Effect
- ↳ Consistently trying to improve performance of ad products to deliver more conversions.
- ↳ There is a lot of potential volatility → have had sizable fluctuations in demand.