

# Facebook M&A Call to Acquire Oculus

## Company Participants

- Brendan Iribe, CEO and Co
- David Ebersman, CFO
- Deborah Crawford, Director IR
- Mark Zuckerberg, Chairman, CEO

## Other Participants

- Brian Pitz, Analyst, Jefferies & Company
- Brian Wieser, Analyst, Pivotal Research Group
- Mark Mahaney, Analyst, RBC Capital Markets
- Mark May, Analyst, Citi
- Ron Josey, Analyst, JMP Securities
- Youssef Squali, Analyst, Cantor Fitzgerald

## Presentation

### Operator

Thank you for joining us today to discuss Facebook's Acquisition of Oculus. Now I'd like to turn the call over to Deborah Crawford, Director of Investor Relations at Facebook.

### Deborah Crawford {BIO 5934723 <GO>}

Thank you. Good afternoon. Welcome to the call. And thank you for joining us on such short notice.

Joining me on the call today are Mark Zuckerberg, CEO of Facebook; Brendan Iribe, CEO and co-founder of Oculus; and David Ebersman, CFO of Facebook.

Before we get started, I would like to take this opportunity to remind you that our remarks today will include forward-looking statements and 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 on our annual report on Form 10-K 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 event.

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

**Mark Zuckerberg** {BIO 15103277 <GO>}

Thanks, Deborah. And thanks, everyone, for joining us today. I'm excited to announce that Facebook has reached an agreement to acquire Oculus VR, the leader in virtual reality technology. Our mission in Facebook is to give people the power to share. And make the world more open and connected.

For the past few years, this has mostly meant building mobile apps that help you share with the people you care about. We've made a lot of progress on mobile. As of last week, there are now more than 1 billion people actively using our mobile apps alone.

More than 20% of the time that people spend in apps on mobile phones is using Facebook services. And more than half of our ad revenue comes from mobile.

We still have a lot of work to do on mobile. But at this point we feel strong enough in our position that strategically we also want to start focusing on building the next major computing platform that will come after mobile.

The history of our industry is that every 10 or 15 years, there's a new major computing platform, whether it's the PC, the web, or now mobile. History suggests that there will be more platforms to come and that whoever builds and defines these, will not only shape all of the experiences that our industry built. But also benefit financially and strategically.

Mobile is the platform of today. And now we're starting to also get ready for the platforms of tomorrow. To me, by far the most exciting future platform is around vision, or modifying what you see to create augmented and immersive experiences.

Today's acquisition is a long-term bet on the future of computing. I believe Oculus can be one of the platforms of this future. Oculus builds virtual reality technology with the Oculus Rift headset and the unique software platform and services around it.

When you put on their goggles, you enter a completely immersive computer-generated environment, like a game, or a movie scene or a place far away.

The incredible thing about the technology is that you feel like you're actually present in another place with other people. It's different from anything I've ever experienced in my life and many people who try it also say the same thing.

Oculus's mission is to enable you to experience the impossible. Their technology opens up the possibility of completely new kinds of experiences.

Immersive gaming is the first big opportunity and Oculus already has big plans here they won't be changing. The beta version of the Rift is highly anticipated by the gaming community. And Oculus has already received orders for more than 75,000 development kits, which is pretty crazy by itself.

These developers are mostly gamers. So this is a strong signal of how much people want to develop games for Oculus and how excited they are about it as a gaming platform.

We're going to focus on helping Oculus build out their product and develop partnerships to support more games and accelerate their plans. And they'll continue operating independently within Facebook to do this.

But gaming is just the start. After games, we're going to make Oculus a platform for many other experiences. Imagine enjoying a court-side seat at a game, studying in a classroom of students and teachers all over the world, consulting with a doctor face to face, or going shopping in a virtual store where you can touch and explore the products you're interested in, just by putting on goggles in your own home.

This is really a new social platform. By feeling truly present, you can share unbounded spaces and experiences with the people in your life. Imagine sharing not just moments with your friends online. But entire experiences and adventures. These are just some of the potential use cases.

But if you think about the social applications alone, this can change the way we communicate with our friends, families and colleagues. Little details like being able to make eye contact with someone with zero latency makes you feel like you're really present together.

Oculus has the potential to be the most social platform ever. Today, social networks are about sharing moments. And tomorrow, they'll be about sharing experiences.

We think people will love using this technology and we're making a long-term bet that immersive, virtual and augmented reality will become a part of people's daily lives.

So that's where we see the opportunities ahead for Oculus in future of computing. I'm really excited to have this opportunity to work with Brendan and his entire team. They've already achieved significant breakthroughs with just a small team. And we're looking forward to helping them scale their efforts over the coming years.

Now, before I close, I just want to make one more point. For almost the last year, I've framed our strategy as three high-level goals over the next ten years; connecting

everyone, one; two, understanding the world; and three, building the knowledge economy.

With this acquisition, now each of those initiatives has an ambitious long-term bet associated with it, in addition to our important near-term work as well.

For number one, connecting everyone, for the long term we have Internet.org, our initiative to make free basic internet services available to everyone in the world. And for connecting everyone, we also have our near-term efforts for our messaging and growth.

For number two, understanding the world, we have our ambitious AI Research Group, which is trying to build a unified model of how every person (inside) the world is connected to each other. In the near term, our efforts here are in search and newsfeed. And will help your network surface more useful information to you.

And for number three, building the knowledge economy, that's really about building future technology platforms. And we now have Oculus joining us, which long term can be one of the next important computing platforms. And of course we will continue to focus on our extremely important work of building out our advertising platform as well, as part of this.

So with this in place, you should now have a clearer view of what our full strategy looks like over the next three, five and ten years. I look forward to updating you on our progress in each of these areas during our regular quarterly updates.

Thanks for joining today. And now I want to turn it over to Brendan.

**Brendan Iribé** {BIO 17301790 <GO>}

Thanks, Mark. We're thrilled that Oculus VR is joining forces with Facebook and we're really looking forward to working together to create the best virtual reality platform in the world.

In 2012, we started Oculus with the vision of making incredible, affordable and ubiquitous virtual reality available to the world. Virtual reality definitely sounds like something out of science fiction. But science fiction has a habit of becoming fact. And we believe that virtual reality will connect people in ways that they never before thought.

VR opens up entirely new opportunities. They jet a new generation of creative, compelling and engaging services that will fundamentally change the way we live, play, share. And communicate.

We started with a focus on next-generation gaming. Now we're teaming up with Facebook to invent the future. Facebook and Oculus share a common vision for the opportunities that virtual reality presents to the world.

Facebook's mission is to connect the world. And Oculus is focused on developing a new medium that allows people to connect in entirely new ways.

A few months ago, when Mark and his team came down to visit our offices, it was immediately clear that the two teams share a passion for building a new world-changing communication platform. Moreover, our teams are culturally aligned with a focus on driving impact, moving fast. And hiring the best and brightest.

As Facebook has grown, they continue to invest in efforts like the Open Compute Project, their initiative that aims to drive innovation and reduce the cost of computing infrastructure across the industry.

This is a team that's used to making bold bets on the future. All of this gives us the perfect foundation for collaboration. Facebook brings greater scale, with unique resources and capabilities that accelerate virtual reality's future.

By opening doors to new partnerships, helping develop the core functionality of our product. And supporting us with recruiting, marketing and infrastructure, the Oculus team can focus on doing what we do best, solving hard problems and delivering on the dream of virtual reality.

We have a thriving community of developers and content creators who are building for the Oculus platform. With more than 75,000 orders for developer kits received so far, we are dedicated to making the Oculus Rift the best virtual reality platform in the world. And that vision depends on the creativity and imagination of our incredible community.

Today's announcement is about bringing even greater energy and resources to our work. So that we're in an even better position to deliver our platforms to more people. We're looking forward to building the future with Facebook.

Thank you.

**David Ebersman** {BIO 2425453 <GO>}

Thank you, Brendan. And good afternoon, everyone. This is David. I now want to start by briefly reviewing the details of the transaction.

Facebook will acquire Oculus for a total of approximately \$2 billion, made up of \$400 million in cash. And 23.1 million Facebook shares.

The agreement also provides for an additional \$30 million earn-out to be paid in a mix of cash and stock-- \$300 million, I'm sorry. \$300 million earn-out to be paid in a mix of cash and stock if Oculus achieves certain milestones.

The transaction is expected to close in the Second Quarter of 2014.

In the near term, Oculus isn't expected to have a material impact on Facebook's revenues.

As Mark said, we're very excited to announce this acquisition. In the next 10 years, we know that the platforms on which we operate will evolve. We see great promise in virtual reality as a potentially important new platform and we're very impressed by the leadership position that Oculus is establishing in this space, as evidenced by the striking progress they've already made and the strong interest in their product by the developer community.

We believe the combined strength of Facebook and Oculus will help drive the broader development and adoption of virtual reality technology, enabling over time a range of services including and beyond games. And making these services relevant and important for millions of people.

Facebook will bring our capabilities, along with our close relationships with a broad range of developers, to help accelerate Oculus's growth.

Over the past few months, we've announced two important strategic acquisitions, WhatsApp and Oculus. These are unique assets that fit well with our strategic goals. They build out the portfolio of investments we're making to drive future growth and to ensure that we're well-positioned strategically to create value for our shareholders over the next decade.

Now, let's open the call for questions.

## Questions And Answers

**A - Deborah Crawford** {BIO 5934723 <GO>}

Operator, we're ready for the first question.

### Operator

Mark May

**Q - Mark May** {BIO 4280734 <GO>}

Hi. Thanks for taking my question. Some of the questions that we're getting from investors after this announcement is, clearly Facebook has been making a few big, bold bets in the last couple of years; this acquisition, WhatsApp, Instagram, etc. But the questions I'm getting are; can you point me to some of the data points or milestones?

Even if early on, the management is executing on some of the early strategic initiatives or outcomes that you're looking to get out of these deals. So I was just wondering if maybe with Instagram, we're a couple years into that deal. Can you

give investors some confidence that the execution and some of the reasons why you bought that company have begun to play out, to give us some comfort that, as you look to do more big, bold bets like this, that we can have confidence in the management's ability to execute on these large deals? Thanks.

**A - David Ebersman** {BIO 2425453 <GO>}

Thanks, Mark. This is David. I can go first. I think with Instagram, the priority for the Company from the beginning was to continue to grow the networks that they were building at that time, which we felt had the opportunity to grow from 20 million active users at the time we announced the deal, to many fold bigger than that. And we were planning or hoping they would get as big as 100 million people using the service.

What you've seen in the two years since we announced the transaction is they've done, I think, considerably better than we anticipated or expected in terms of growing the size and importance of their network over time.

So we obviously have other objectives for each transaction. It's going have a different set of goals associated with it. But we think Instagram is really a nice proof point of the effectiveness of the strategy we've taken in terms of really leading these companies to continue executing on their roadmap, taking advantage of Facebook only in areas that can really help them to grow more effectively.

**A - Mark Zuckerberg** {BIO 15103277 <GO>}

Yes, I mean I'll add a little to that. Like David said, when we agreed to acquire Instagram is that one day we thought it could reach 100 million people or more. And within the first two years of working with them, we're already at 200 million.

So that I think, that was an initial test case for us, because before that we had no experience with having a company join us and continue to operate independently. So the overwhelming success in the partnership that we've been able to forge with Kevin at Instagram and showing how that works has really been a great example for how we want to do things going forward.

It's hard to comment on what we expect will happen with WhatsApp and now Oculus, because neither of those deals have closed yet. But the theory for WhatsApp, which I think is extremely likely and compelling, is that they're on a path to have a billion people using their product in the near future. And there just are not that many services in the world that can reach a billion people. And all the ones that do just have to be incredibly valuable.

Similarly, Oculus, there are not that many companies that are built on core technology that can be the next major computing platform. And the Oculus team is the clear leader here. I mean they have the quality of their product, even their development kit, I mean they probably could ship it as a consumer thing if they wanted, because it's so high quality and so much better than anything that anyone

has built before. And all the best people in the field come to work at Oculus, because this is where you go if you want to work on this technology.

So in each of these cases, there's a clear thesis. With Instagram, we're already way ahead of where we hoped to be. With WhatsApp, the theory is we're going to get to a billion people. And with Oculus, it's that they're the clear leader in something that has the potential to be the next important, or one of the next most important computing platforms.

**Q - Mark May** {BIO 4280734 <GO>}

Great. Thanks.

**A - Deborah Crawford** {BIO 5934723 <GO>}

Next questions, please.

**Operator**

Mark Mahaney

**Q - Mark Mahaney** {BIO 3027058 <GO>}

Great. Thanks. Hi. Brendan, can I ask you a question? I know you talked about the—the press release talks about the applications for virtual reality technology beyond gaming to be in nascent stages. But as you have built out the (technical difficulty) over the next two or three years, what do you think will be the most interesting commercial, social, industrial, whatever applications? What do you think is closest to hitting-- for the ire to hit the fire? Thanks.

**A - Brendan Iribe** {BIO 17301790 <GO>}

Sure. Thank you. So we started in gaming. And that's obviously where Oculus got its kickoff. John Carmack, who is the creator of Doom and Quake, was one of the first to create the prototype with Palmer Luckey. We got involved shortly after that and we really had this vision to where it could go with immersive gaming and long-term entertainment.

Then as we started developing virtual reality. And as we actually got a lot of the hard problems solved, we started to realize that virtual reality, it was going to be a lot about gaming. And it was going to be a lot about entertainment and different aspects of that, variations of that.

But something that we didn't expect in the beginning that became really obvious, was how big the potential was for the social experience. And when you truly feel, in virtual reality, that you're actually present in another space. And look around and the brain is just completely convinced that it's comfortable and it's Okay. But it's an entirely new, impossible place. Something fundamentally changes and you start to realize how big this can be.



Then, in that same sense of presence, in that same sense of a new space, if you can see somebody else, if you can actually look at them and your brain believes that they are right in front of you, you're not looking through a screen or a 2D window. But they're actually right in front of you. You know, you get the goose bumps. You do really start to realize just how big this can be and how big social and communications, how big of an impact it'll have on those industries.

And as we realized that. And as we were talking to Mark and the Facebook team, it just became incredibly obvious and exciting for us to partner up and to create that new social platform.

**Q - Mark Mahaney** {BIO 3027058 <GO>}

Okay. Thanks, Brendan.

**A - Deborah Crawford** {BIO 5934723 <GO>}

Next question?

**Operator**

Brian Pitz.

**Q - Brian Pitz** {BIO 6994205 <GO>}

Great. Thanks. You briefly mentioned some other devices out there. We've recently seen the Sony VR headset for the PS4 and there's been some chatter around Microsoft maybe working on a similar product. Any concerns around new upcoming technologies that maybe we haven't seen in the marketplace?

Then just a couple of housekeeping—when does the full-blown headset actually launch? And will Oculus actually get any Board seats on Facebook? Thanks.

**A - Mark Zuckerberg** {BIO 15103277 <GO>}

Sure. So what we've seen is the Oculus product that they have now is way ahead of anything else that's out there. I mean Sony I think has demoed something very early. Microsoft hasn't even got to the point where they have anything to demo yet.

And not only that. But the team is way further ahead in terms of just having so many of the most talented people at Oculus, that we feel good about that.

The other thing that I think is important here is that in order to build a really big computing platform, there are a bunch of important use cases that you need to support. So whether you're looking at mobile and how people spend their time, or PC as before, we've measured this more with mobile. But what we see is about 40% of the time that people spend overall is in gaming. And about 40% is also spent on social communication. So about half of that is in Facebook, which is nice.

And what we basically believe is that unlike the Microsoft or Sony pure console strategies, if you want to make this a real computing platform, you need to fuse both of those things together. And with that—when Brendan and I were talking about this and what Oculus is doing and how Facebook can add to that, that I think was the opportunity that we saw in working together, is to have this transcend the traditional console opportunity, to really make it more of a ubiquitous computing platform.

And (inaudible) these two companies. They're really the only ones that are set up to have that happen.

**A - Brendan Iribe** {BIO 17301790 <GO>}

Yes, I couldn't agree more.

**A - Deborah Crawford** {BIO 5934723 <GO>}

Then the launch, there was another question about when we can give a launch; (inaudible) answer that question and comment.

**A - Mark Zuckerberg** {BIO 15103277 <GO>}

We don't have anything to say on that now. There are development kits. You can order them. They're good.

**A - Brendan Iribe** {BIO 17301790 <GO>}

Really good.

**A - Deborah Crawford** {BIO 5934723 <GO>}

Okay, Operator, next question please.

**Operator**

Brian Wieser, Pivotal

**Q - Brian Wieser** {BIO 16451167 <GO>}

Hi. Thanks for taking the question. I have a more general philosophical question. How do you tend to think about M&A and the buy-versus-build consideration? I mean you mentioned that they're ahead with the technology. But we also talked about this being sort of a very long time horizon issue. So to the extent that you could develop internally, I'm just wondering how you think about that more philosophically. Not necessarily just with Oculus.

**A - Mark Zuckerberg** {BIO 15103277 <GO>}

Well in this case, the analysis, we did think about what would happen if we tried to build it from scratch. And the first thing that we realized is, in addition to being many years behind where they are in technology, they already have all the good people in the industry.

So this is not a thing that, at least in terms of really intense graphics systems and hardware hacking that on consumer electronics that Facebook has done in the past. So this is a part of the culture that we needed to build out.

What we started thinking about that. And reallyâ€”I mean the way that I started this process was thinking about now we have this strong position on mobile and we're feeling increasingly good about that. And we have this position now where we feel like we should be looking ahead in thinking about what the next platforms are going to be.

Then we kind of backed into that from there. And decided Okay, well we think vision is going to be the next really big platform. It might take five or ten years to get there, just kind of like how the first smartphones were really introduced in about 2003 and then only reached a billion people about 10 years later. So we were thinking about what the next platforms are going to be.

Then from there we kind of backed intoâ€”well, all right. Well if we really want to be able to help push this forward, this is the realâ€”this is the team that we want to work with they're years ahead. So that actually became a pretty clear decision from our point.

The bigger question on their side wasâ€”they had so many options in terms of what they could do, in terms of building this out independently or working with anyone who they want because they're the clear leaders in a very exciting space.

So it was just through the conversations that we had and each of us getting excited about what we could add to each other's efforts was what I think made this come together.

#### **A - David Ebersman** {BIO 2425453 <GO>}

The only thing I'd add, sort of, to the philosophical point you asked about. I think we've laid out in our communications over time three consistent strategic pillars that we're trying to invest in, to try and build the most valuable service that we can.

In each of those areas, ideally we'd like to be making investments that are going to bear fruit over a shorter term, an intermediate term. And a longer-term horizon. A lot of those investments are going to come from our internal R&D efforts and our internal product development. But we want to be able to complement those with M&A where that makes sense.

So we've been pretty selective over the ten-year history of the Company in terms of the acquisitions we've done. We'll continue to use it selectively as a tool where we feel we can access really extraordinarily valuable and unique assets.

#### **A - Deborah Crawford** {BIO 5934723 <GO>}

Next question.

## Operator

Ron Josey

### Q - Ron Josey

Great. Thanks for taking the question. So Mark, just real quick, I really appreciated your comments on thinking about the next 10 years and Facebook's three key goals. Just thinking more about "do you think there's more to do from a continued acquisition perspective, or do you think the product set is good to go, at least for now in the short term, given I know we're 10 years out from really the short term, medium term and long term?

Then, Mark, if you can talk a little bit more, maybe help us with understanding the valuation if that's possible. I know we're awfully early here. But that would be helpful. Thank you.

### A - Mark Zuckerberg {BIO 15103277 <GO>}

Sure, I guess you can take the valuation if you want. (inaudible) the first question.

Yes, I think the key thing to keep in mind on this, is these are all incredibly rare companies. Right. So we'll go a long period of time without doing anything like this. Then I think we're in this kind of rare period now where we've just done two really close to each other.

So I definitely don't think you should expect us to make multiple multi-billion dollar acquisitions within a couple of months, frequently. But I mean the way that we're thinking about this is, WhatsApp is one of the incredibly rare companies that we think will reach a billion people. And every company that reaches a billion people is incredibly valuable.

And also, there are not that many things that are candidates to be the next major computing platform. And this company, Oculus, has a very clear lead in doing that. And we felt like we could apply a lot of levers to accelerate their growth.

So these are two kind of rare instances. And in the future where we find rare companies, we'll consider this. But I think that the rate will certainly not continue.

### A - David Ebersman {BIO 2425453 <GO>}

In terms of valuation, the financial analysis that we did focused primarily on the games business because it's the furthest along. And it's the clearest opportunity where we have other businesses we can compare it to. And we felt comfortable we could justify the sole value of the acquisition just on the games opportunity if Oculus continues to execute it as we expect.

On top of that, we see tremendous financial and strategic upside if we're successful in taking the platform into other areas like communications and entertainment. And we know there's already people in various industries that are interested in the technology.

So if we can make that happen together, we think the technology will be worth multiples of the purchase price.

**Q - Ron Josey**

Thank you very much.

**A - Deborah Crawford** {BIO 5934723 <GO>}

Operator, I think we have time for one last question.

**Operator**

Youssef Squali

**Q - Youssef Squali** {BIO 1506420 <GO>}

Thank you very much. So I guess to us, it seems like we've been hearing about virtual reality technology for a while and without really having seen any major mass adoption, maybe with the exception of some gaming.

So I guess the question is; why now? Why do you feel that we're on the cusp of something big, if that's what you doâ€”if that's how you feel? But also I think you made a comment about opportunity in five to ten years. So maybe a little clarity on that.

Then what do you envision the Oculus business model to look like eventually? Is it mostly hardware sales? Is it advertising/licensing? Or all of the above? Maybe you can help us there. That would be great. Thanks.

**A - Mark Zuckerberg** {BIO 15103277 <GO>}

Sure. So in terms of timing on why VR is now possible. And Brendan should jump in if I miss anything here. But my understanding is technically, one of the things that's driving this is that folks can now start to reuse components that are being mass-produced for phones at low prices that are small enough and powerful enough, that you can repurpose to do the really intense graphics work that's necessary to render a full world quick enough to not make someone motion sick.

So I mean just to give you a sense of how this goes, you kind of need to getâ€”as soon as you move your head, you need to get down to generating and rendering on the screen in front of the person a completely updated world withinâ€”so about 15 to 20 milliseconds, or else it's just too jarring to feel real to a person.

And this team now, for the first time, has been able to do that at a cost-effective price and then there's advantages beyond this, too. So they're doing that powered off of a PC today and hopefully in the future they'll be able to do that powered off of more and more ubiquitous computing devices as well. So that I think is why it's possible now. And why it's going to be exciting now.

In terms of "and what's going to be possible in the future, you know I do think gaming is a start and once you start getting a network effect around people gaming, there are obvious communication cases. There are pretty interesting things that people have built just using the development kits.

Like people will build a model of a place far away. And you can just go see it, right? And it's like teleporting. You actually believe that you're there. And that's really "so I feel there's a real breadth of interesting things that just we haven't seen on any other platform before, because they haven't made sense. Just kind of like how there are mobile apps that didn't make sense to be on PC. I think you're going to see that and it's going to take a while for that to develop, which is partially why I think this is a five-plus year thing.

In terms of our own business model, we're clearly not a hardware company. We're not going to try to make a profit off of the devices long term. We view this as a software and services thing, where if we can make it so that this becomes a network where people can be communicating and buying things and virtual goods and there might be advertising in the world. But we need to figure that out down the line. Then I think that's probably where the business will come from, if I had to say.

But for the foreseeable future, the main goal that we have is just building out the product, using the different levers that Facebook has to make the product affordable to people, to make it ubiquitous. And use the different technologies that Facebook has developed to bring it to market as soon as possible.

**Q - Youssef Squali** {BIO 1506420 <GO>}

All right. Thanks Mark.

**A - David Ebersman** {BIO 2425453 <GO>}

(multiple speakers) business models. The only comments I would add is that clearly the near term focus is going to be on investing in the platform and making it successful. That's got to be the priority.

If we are successful in building the kind of platform that we think we can build here, there should be lots of different monetization opportunities and it's too early to make any concrete plans in terms of exactly what our approach will be.

**Q - Youssef Squali** {BIO 1506420 <GO>}

Thanks, David.

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**A - Deborah Crawford** {BIO 5934723 <GO>}

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

**Operator**

And this concludes today's conference call. You may now disconnect.

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