Facebook, Inc. (FB)
Third Quarter 2020 Follow Up Call
October 29th, 2020

Operator: Good afternoon. My name is Julianne, and I will be your conference operator today. At this time, I would like to welcome everyone to Facebook's third quarter results follow-up Q&A call.

All lines have been placed on mute to prevent any background noise. To ask a question, please press star, then the number one on your telephone keypad. This call will be recorded. Thank you very much. Ms. Deborah Crawford, Facebook's Vice President of Investor relations, you may begin.

Deborah Crawford: Thank you. Good afternoon, and welcome to the follow-up Q&A call. With me on today's call is Dave Wehner, CFO, and joining him for the first time this afternoon is Susan Li, VP of Finance.

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 certain 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 back over to the operator for the first question.

Operator: We will now open the lines for a question-and-answer session. To ask a question, press star, followed by the number one on your touchtone phone. Please pick up your handset before asking your question to ensure clarity.

If you are streaming today's call, please mute your computer speakers. Your first question comes from Ross Sandler from Barclays. Please go ahead. Your line is open.

Ross Sandler: Hey, Dave, how's it going? Just wanted to follow up on two things that came up on the main call. First is on the IDFA. So in the blog post you guys put out a couple months ago, you talked about a 50% impact to FAN.

And I was just curious what the impact to owned-and-operated ad rev might be from IDFA, if any? Do you expect some of that reduction in FAN to find its way over into owned-and-operated?

And then the second question is, it sounded like Sheryl was talking about how some of the uptick that you're seeing right now in e-commerce, the -- you know, we shouldn't really carry forward these growth rates next year, because whether it's e-commerce or some of these other kind of COVID winner categories that are growing really fast right now, they might roll over.

So I guess, just can you help us with putting some numbers around that dynamic? Are the COVID winner categories like as much as half of the ad revenue at this point? And how do you think that's going to play out next year? Thanks a lot, guys.

Dave Wehner: Yes, so, sorry, let me make sure I'm unmuted. Yes, thanks, Ross. Let me first also just welcome Susan Li to the call. Susan is our VP of Finance who heads our Financial Planning and Analysis group, our Treasury group, and our Corporate Finance group, so wanted to welcome Susan.

Ross, on your first question on IDFA, we don't have any update to those estimates for FAN. I think it's important to note that iOS 14 covers -- there's a couple changes as it relates to privacy targeting and measurement. And one of those is how you can use IDFA.

That's going to disproportionately impact the app install category. And that's a big portion of the FAN advertiser base, so it's going to disproportionately hurt FAN. And so that's why we've singled out that issue.

Now, the fact that that got deferred -- the enforcement of that got deferred by Apple into 2021 means that we're still operating FAN and it's still working. I think there are going to be issues with how well FAN will work with iOS, so, longer term, I think there are some strategic questions there.

But there are broader policy-level changes with iOS 14 which will have impact on our core advertising business. We haven't given specific quantification of that, but we do think that will be a headwind into 2021 as those are implemented.

So we'll see that from both IDFA as well as the broader policy measures on iOS 14. On e-commerce, I'm going to let Susan fill in some detail on that.

Susan Li: Yes, so on e-commerce, we have seen over the last two quarters since the pandemic began really an acceleration of what had been historically a slower moving trend.

If you look at data provided by the U.S. Census Bureau, e-commerce as a percentage of U.S. retail sales was growing by an average of 1 percentage point for the last four years. Beginning Q2, the share basically jumped from 12% to 16%. So really accelerating that trend, I think that's something like four years of change happening in the course of a quarter or two.

So as we look forward, I think there's real uncertainty in terms of the outlook, both in terms of what happens with COVID, the broader economy, whether the reopening of society gradually leads to sort of a return to more brick-and-mortar retail.

And this could mean slower growth for us when that happens, and that's something that would certainly impact our 2021 outlook.

Operator: Your next question comes from Stephen Ju from Credit Suisse. Please go ahead. Your line is open.

Stephen Ju: OK, thank you. Hi, Dave, how are you?

Dave Wehner: Hey, Stephen.

Stephen Ju: Hi. So I guess, you know, going back to March and April when this hit, I think there was a certain amount of panic on the consumer, supply chain was affected and advertisers panicked, as well.

And unfortunately it looks like we're heading into a second wave of this, so -- but it seems like the consumer, as well as the advertisers, and we've kind of been through this already, unfortunately. So it seems like people should be better prepared for what follows.

So, as you talk to advertisers, I mean, you're probably having more of these advertiser conversations than any of us sitting in this room, what are they telling you in terms of their plans?

Are their plans, you know, media plans -- are they still up in the air right now? What are the conversations like between the larger advertisers versus some of the SMBs that you talk to right now? Just kind of a sense in terms of what you're hearing in the market. Thanks.

Dave Wehner: Sure, I can give some broader color, and Susan can feel free to jump in if she has anything additionally to add. What we've seen is -- the big theme is, of course, the online shift that we've seen in our sort of e-commerce and retail categories, where that's been a driver of growth as people seek to replace what would have been offline sales with more online sales and Facebook and Instagram being a great channel through which to do that.

And we've seen a lot of direct response advertisers and players just looking to drive conversions. So I think generally we've seen that be a consistent trend that really picked up after a -- I think an initial downturn in most categories in the sort of April timeframe. We really saw that pick up in Q2 and Q3, with e-commerce being a driver.

More recently, I think we've seen some signs of recovery in some of the other categories. We've seen brand spend come back somewhat in the back part of Q3. So I'd say we've seen some signs of a more return to normal. So I think that's promising.

How it plays out with a second wave is unclear. It's unclear what benefits we got from, for instance, stimulus in the first wave, which I think did support the consumer. So I think it's uncertain.

I think we do think we're well positioned for Q4, with the trend towards online commerce and how that plays out in Q4. And then as you get into 2021, we're going to be -- you know, a question of kind of where things shake out with COVID, a return to normal. How does that affect either the pace of the shift to online, is there a potential for a reversal to more offline sales? We just don't know at this point, and that's why we're calling out the uncertainty.

Stephen Ju: OK, thank you.

Dave Wehner: Yep.

Operator: Your next question comes from Michael Levine from Pivotal Research Group. Please go ahead. Your line is open.

Michael Levine: Yeah, thanks for the question, guys. Another just clarity point around IDFA. Dave, I know you've definitely highlighted that -- you've highlighted, obviously, app installs and FAN could be disproportionately impacted. But can I just ask you to break it down sort of simply for just the core service and the way you guys do targeting?

I mean, my sense is, Facebook probably has got the most robust 1P data that's out there, but partly why you guys are the gold standard with targeting is you're looking at other behaviors that folks are doing with the SDKs across mobile devices.

I mean, are you guys trying to almost just parallel path and see, is there a way that you could try to go ahead and as effectively target or maybe if there's some signal loss, somewhat mitigate that?

I mean, is that a fair categorization to try to think through the way you guys looking at IDFA having a negative impact into next year?

Dave Wehner: Yeah, I mean, we're certainly looking at our -- obviously, our business clients are asking us what we can do to help mitigate any of the impact of these changes that the platforms make. And we think that we're positioned as well as anybody to help with that.

But it's certainly going to be a disruption for these businesses in terms of how they've been using targeting and measurement. So we do think it will impact the business. So we're working it, you know, various paths to help mitigate that. But despite that, we're going to face headwinds next year as these changes are implemented.

Michael Levine: Got it. Thank you so much.

Dave Wehner: Sure.

Operator: Your next question comes from Lloyd Walmsley from Deutsche Bank. Please go ahead. Your line is open.

Lloyd Walmsley: Yeah, thanks. I guess the first one would just be, do you think that if you had to shut down FAN, a lot of that demand is obviously coming in and going in to your own algorithmic placement, automated placement. So do you think a lot of that demand would just stay and flow back into the core?

And then, yeah, I guess going back to Ross's question on the notion that e-commerce has been kind of a tailwind that could become a headwind, I mean, 21% growth this quarter isn't -- it's not exactly where you were prior to the pandemic.

So we're not far off. But, I mean, shouldn't there be other things that recover that kind of offset that? Or are you more talking about kind of the Q4 benefit that you'll have to comp against next year?

Susan Li: Yeah, thanks, Lloyd. I'll take the question on FAN. One of the nice things, certainly, about running an auction across the whole platform, including our own properties and including off of Facebook, is that when -- if we -- any demand that were to run through FAN, we would be able to basically run that through the auction, and the auction would determine the right place to place that demand on Facebook or Instagram.

So I think that is -- I think that's certainly one of the benefits of how our system works and is run. Now, having said that, nonetheless, losing -- shutting down FAN is not something that we'd be excited to do, and we certainly would not want to lose that inventory.

Dave Wehner: And, Lloyd, I'd add, as well, the rationale for any need to make any moves on the Audience Network would be that the -- at least on iOS, it's harder to do the app install targeting. I think that would carry through to targeting on Facebook, as well.

So I think they would still struggle with being able to be as effective with their ads on Facebook. On e-commerce, where we see that potentially becoming a tailwind is that's been obviously the shining star of the story over the past two quarters.

And what -- whether we've sort of pulled forward that shift to online by several years, what are the implications of what we've been experiencing, which has been this slow and steady shift to online, which we've seen benefiting our business over the last several years? Does that become any sort of headwind to growth?

We really just don't know. I mean, we could certainly be at this higher level and we continue to grow. We could see that as things open up, there's a reversion to more offline selling.

We simply don't know. So it's I think more of an uncertainty than any certainty. And so that's why we're calling it out as a risk. We really just don't understand how this is going to play out in the long run.

I think it's a story, by the way -- this is not a Facebook story. This is clearly an industry story. You've seen a number of companies benefit from this, you know, shift from offline commerce to online commerce, whether it's Amazon or Shopify or others, and I think we're all going to be trying to figure out what this means as we comp against it next year.

Operator: Your next question comes from Alan Gould from Loop Capital. Please go ahead. Your line is open.

Alan Gould: Thank you. I've got two questions. First, the headcount has been growing about 4,000 a quarter. Do you think in '21 it grows at that rate or an even higher rate?

And, secondly, the quarter just reported, the up 22%, that was after July, was up 10%. Did August and September each grow sequentially? Was September stronger than August? We know the two were obviously greater than July.

Dave Wehner: Yes, why don't I take the second one, and then Susan can take the first one on headcount growth. We're not going to break out kind of month by month revenue trends. But we did start out with a weaker July followed by improvement in August and September. And those growth rates have stabilized.

And that's one reason we expect Q4 growth to be higher than the reported growth rate in Q3, because obviously we saw August and September being stronger. So that's kind of how we're looking at Q4.

Susan Li: On the headcount question we added just over 4,100 heads this quarter, and last quarter I think we added just over 4,200 heads. So, two really strong hiring quarters for us.

This has been, candidly, a good environment for us to hire in and attrition has also been lower. And that really translates into a good opportunity for us to invest during an environment where our business is also performing well.

So we do expect -- we have a lot of investments in the works for 2021. Mark spoke to a lot of them on the call, and we hope to be able to hire to support those investments.

Operator: Your next question comes from Jason Helfstein from Oppenheimer. Please go ahead. Your line is open.

Jason Helfstein: Thanks. I have just two. So one I have from a DAU versus family metric. So, obviously, we saw DAU slow. Family metrics didn't. You did kind of talk about the DAU slowing, so did you think DAU is still kind of the best tracking metric? Or should we be paying more attention to kind of family metrics?

And then, look, we've all been asking about Facebook Shopping for a while. And I think the response has been it's early and kind of not material yet. And yet now we're seeing how you guys have really kind of fast-forwarded a lot of the work and shipping those products.

And so to the extent that e-commerce trends do actually continue and that we don't go backwards as far as putting the genie back in the box, I mean, why wouldn't that finally be at the point where it actually is kind of added into the business, where you just wouldn't have been, because the products were at a much earlier stage, call it, you know, two, three quarters ago? Thanks.

Dave Wehner: Why don't I -- I can take the DAU one. And then, I don't know, Susan, if you want to take the Shopping one.

And, DAU versus family metrics, we have a -- there's a daily active family number as well as a daily active Facebook number, so I do think over time we think the family metric is the most relevant, were monetizing across multiple surfaces today.

Instagram, obviously, Facebook, and then in -- you know, as we build more of our business messaging with WhatsApp, that will be increasingly relevant.

So we do think that the family metric over time is going to be the better metric to be tracking, but we're continuing to supply both the Facebook and the family metric at this stage.

Susan Li: Jason, on the question about Shops, you know, Shops is still in its very early days, both in terms of the experience on Instagram and on Facebook.

And we are really focused on trying to get that experience right for both consumers and advertisers. For consumers from the perspective of making it as seamless a browsing and transactional experience as possible. For advertisers, giving them the tools that they need in order to easily upload their inventory into a Shop and create the Shop experience that they want.

It's not planned to be a material contributor for Q4. But we are optimistic about our ability to build out the right experience for our businesses on our platform in the long run. And I think this will be especially important given some of the data and targeting headwinds that we're talking about for next year.

Operator: Your next question comes from Kevin Rippey from Evercore ISI. Please go ahead. Your line is open.

Kevin Rippey: Hey, thanks for taking the question, Dave, and nice to have you aboard, as well, Susan. I was just wondering, in terms of the OPEX guidance for next year, in terms of absolute dollars, some of that has to come by way of headcount growth and paying salaries.

Some of it's coming by way, I assume, you know, technical infrastructure expenses, i.e. like putting stuff in data centers.

I'm just curious, like, is there a natural limitation to how many absolute dollars you guys can grow OPEX in a year by way of effect that either universities don't produce enough engineers or product managers or chip foundries or whoever your technical providers are aren't making enough stuff to go around between you and perhaps the other people in sort of tech universe that are buying that stuff?

Like, just trying to get a sense, is there like a natural gravity to how much money you guys can spend in a year or how much you can grow your spend in a year?

Dave Wehner: Kevin, I can at least start that question. I think ultimately you kind of hit on two of the big elements of our cost structure. It's headcount and it's infrastructure. Those are the two biggest elements. There's also sort of OPEX spend kind of independently from headcount.

I would say next year, headcount growth, we're currently comping at about 32% year-over-year growth in the third quarter versus last year. If you were to go back a year ago, we were growing at 28%. So we have accelerated our headcount growth.

And, you know, part of that is our success at hiring in this environment. And so we've seen also very good retention of existing people at Facebook.

And so I think that's giving us an ability to continue to grow -- I think Susan mentioned that earlier on the headcount question -- our ability to continue to grow and recruit and retain technical talent.

That has historically been a constraint on growth, but we're doing well right now on that front. And so that gives us some confidence of our ability to kind of deploy these dollars and investing in our product next year.

And there's a lot of priorities. We've got our longer-term Facebook Reality Labs work. We've got Messaging, Commerce, Reels, tons of products and initiatives. And so finding the technical talent to deliver against those is important, but we're doing well on that front as represented by our headcount growth rate in Q3.

And then we're continuing to build out our data centers and put servers into operation, and that's flowing through on the depreciation front. And then I did mention, as well, on the main call that we benefited in 2020 of having sort of reduced office operations and travel expenses. And that's to the tune of probably about $1.5 billion of savings in our 2020 expenses.

And as we go into 2021, we are anticipating a return at some point to a more normal level of operations, which means that that savings will kind of, as the year progresses, disappear. And it will be at a higher rate, because that tends to track the headcount, and we're going to be larger next year in terms of headcount. So that's also factoring into our outlook.

Operator: Your next question comes from Mark Zgutowicz from Rosenblatt Securities. Please go ahead. Your line is open.

Mark Zgutowicz: Hi, good evening. Two questions. One, wanted to get a sense of the Shop Marketplace, not to be confused with Shops. Just curious what kind of engagement you've been seeing there, sort of what -- how you see the pace of investment there, sort of what your expectations are in terms of engagement there over the next year or two?

And then, question on just the pace of brand spend that you've seen coming back, others have seen it come back quite strong. I'm just wondering if it's enough to move the needle one way or another?

Obviously, you have much more exposure on the DR side, but I was just curious, given all the chatter about the brands, the July boycott, et cetera, sort of what that pace has been like.

Dave Wehner: Yes, Mark, why don't I take the first one of the Shop Marketplace and then Susan can talk about the brand spend.

On Shop, the actual tab is something that is early days. We started testing that in Q3, so it's quite early on that front. Similar -- that's on Facebook.

On Instagram, we launched IG Shop globally in Q3, which is a shopping destination within Explore where people can discover products and brands. And we are testing the new Shop tab in the main navigation bar on Instagram as well.

And then you mentioned Marketplace. That's sort of a separate effort within Facebook, which is more about consumer to consumer. That was slower in Q2 with the original lockdowns related to COVID, but we've seen some good recovery there.

We got hundreds of millions of MAU in 90-plus markets, and that's primarily -- that's monetized via ads. But we've seen that sort of snap back more recently, so that's promising. Susan, you want to cover brand spend?

Susan Li: Yes, Mark, so on brand spend the strength we saw in Q3 was really primarily driven by that shift from offline to online commerce, by really strong growth in SMBs and DR ads.

That said, we did see some improvement in brand spending especially towards the back half of the quarter. We saw some recovery in brand-heavy verticals like travel, auto, entertainment start to come back, and that compares especially to relatively weaker levels in Q2.

Operator: Your next question comes from Mark Shmulik from Bernstein. Please go ahead. Your line is open.

Mark Shmulik: Hey, Dave, hi, Susan. Couple questions, if I may. Going back to kind of DAP-MAP, I know, you know, in the U.S., that kind of sequential decline. But if we looked at it on a DAP-MAP basis, kind of including the Instagram and WhatsApp, directionally do the trends look the same? Or is there some divergence?

And then the second question, beyond Shopping and Commerce, it certainly seems like there's a lot of new potential ad products kind of coming to the market. Obviously, we've got like vertical video potential in Reels, Groups, and now Neighborhoods, IGTV, Watch, Live, et cetera.

As we think there are some of those incremental opportunities, you know, any sense you can give us on how to think about ranking them in terms of how close they are to coming to market and prioritization? Thank you.

Dave Wehner: Let's see. On the DAP versus MAP, Mark, I want to make sure I understand your question. What -- I guess, do you mean -- do the relative engagement of, on DAP-

MAP family versus -- Facebook standalone? What was your question about that? Did we lose Mark? OK.

Well, I guess I'll give my best there. I think we've seen pretty consistent DAP -- DAU to MAU trends. Some of our products tend to have higher engagement levels, especially messaging products like WhatsApp, people using them very frequently.

Facebook has had a fairly consistent DAU to MAU user over time. It bounces around, but we've seen a fairly consistent ratio there. So I don't think any big changes on that front. In terms of the product initiatives, why don't I let Susan go ahead and start on that?

Susan Li: Yes, so I think the -- you mentioned the new product experiences we were building out. And I have Groups, Reels, and Neighborhoods I think as three of the ones that you mentioned.

You know, with any of the new consumers experiences that we build, we obviously -- the bulk of our early focus is really trying to make them as valuable and as engaging for the consumer audience that they're targeted at as possible.

From the list that you mentioned, Groups, we do -- we are testing ads in the Groups tab. They appear in the Feed section of the Groups tab. And that's still pretty early and limited. We certainly think that there will be a path towards showing ads in Reels, and that's something that we're thinking about when to put on the roadmap.

And then there are other consumer experiences that are much more nascent and that don't have ads on them at all, and where we’re still -- really the focus is on the consumer experience itself and Dating would be an example of that.

Operator: And, Mark Shmulik, your line is open again.

Dave Wehner: Oh, I think -- Mark, I just wanted to make sure we answered your DAP-MAP question.

Mark Shmulik: Covered. Thank you.

Dave Wehner: OK.

Operator: Your next question comes from Rich Greenfield from LightShed. Please go ahead. Your line is open.

Rich Greenfield: Hi, thanks for taking the question. I wanted to follow up on Susan's comment about Shopping. You rolled out I think to every merchant now the ability to actually have Instagram Checkout. And I assume that's going to flow into Facebook, as well.

But could you give us some color -- first of all, how many merchants actually have adopted Instagram Checkout? How does it actually impact conversion in terms of purchase and, therefore, drive your ability to increase the ad rates that you charge? Or any way to contextualize the importance of what Instagram Checkout has meant?

Obviously, you've hit the go button on rolling it out globally after a very slow kind of tempered rollout. Obviously, the pandemic I'm sure accelerated it. But what's been the learnings from Checkout so far?

Dave Wehner: Yes, Rich, why don't I take that? I think we're encouraged by the adoption levels. As you're aware, we've expanded that to all U.S. businesses.

We've waived selling fees through the end of '20, but we aren't providing any specific stats or updates on how many businesses are using it [inaudible]. I think we're going to have to wait and get more data as that rollout progresses.

Deborah Crawford: Operator, I think we're going to take one last question.

Operator: Thank you. Your last question comes from John Blackledge from Cowen. Please go ahead. Your line is open.

John Blackledge: Great, thanks. Two questions. First, on ad pricing, it was down 9% in Q3, an improvement from Q2. Just giving your guide of accelerating top-line in Q4, should we think about pricing firming further in the fourth quarter and just any puts and takes there?

And then just checking on one other item. Sheryl mentioned 10 million advertisers in Q3. I think that was up from 9 million in Q2. So is it accurate that you guys added a million advertisers in the third quarter? Thank you.

Dave Wehner: Well, Susan, you want to take the ad pricing one and I'll take the active advertisers?

Susan Li: Yes, sure, so, as you know, we run an auction. And so for us, the pricing dynamics are very dependent and also the supply growth dynamics and impression growth. For us, we've seen, impression growth from both ad load and user growth this quarter.

And I think as we look forward, both the sort of return to pre-pandemic levels of engagement, which will sort of temper the amount of supply growth, in addition to, I think, more limited ad load growth generally going forward means that we will -- we do expect that revenue growth in 2021 will be more reliant on pricing. And that means that we'll be more subject to a lot of the targeting measurement headwinds that we mentioned earlier.

Dave Wehner: And then, John, on the active advertisers -- we're not -- we're sort of providing that metric ad hoc. And so it's -- I don't think it should be viewed as -- timing as precise as each quarter we're sort of providing an exact number. We're sort of providing an occasional number on that front.

We are seeing good advertiser growth in the pandemic environment. That's clear. But I wouldn't take these as being precise numbers or precise timing that we're committing to on that front.

Deborah Crawford: 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.