

Facebook, Inc. (FB)
Fourth Quarter 2020 Follow Up Call
January 27th, 2021

Operator: Good afternoon. My name is Gabriel, and I will be your conference operator today. At this time, I would like to welcome everyone to Facebook's fourth 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 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: Thank you. 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 touch-tone 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.

We ask that you please limit yourselves to one question and one follow-up question. Thank you. Your first question will come from the line of Jason Helfstein of Oppenheimer. Please go ahead.

Jason Helfstein: Thanks. So, first, maybe just to probe a bit deeper, I think we're having a hard time seeing why the shift to e-commerce does not continue and, in fact, turns into a headwind.

I think we understand what you're saying as far as, if consumer spending shifts to categories like travel, that would be negative, but to the extent -- maybe just elaborate a bit more, because it really does seem that the adoption of these e-commerce ads just continue to grow.

And then, second, can just elaborate a bit more on the underseas data transfer issue and how you see it effecting the company? Thanks, Dave.

Dave Wehner: Sure, Jason. And then Susan can jump in if she has anything else to add.

So on the e-commerce shift, I think really -- I think everyone expects that the landscape will continue to shift towards e-commerce and online. But the question is the pace of the shift. So, for instance, in Q2 and Q3, the Census Bureau data for the U.S. showed that e-commerce sales grew 45% and 37%, respectively -- the strongest growth rates since 2002.

Just because you saw that online shift accelerate and that had a favorable impact on our growth rates, and even if we continue to see it shift towards online commerce, meaning that online commerce is growing greater than GDP or retail sales, it's still going to grow at a lower rate probably than represented in 2020, given the pandemic.

So I think it's a headwind to growth. It doesn't mean that it's going to revert back to offline sales. And then, obviously there's the product versus services shift in spend.

That one probably feels like you could see -- people are buying a lot of products now because that's where their disposable income is going, because they can't travel, they can't do other things.

I think that has broad implications. They're buying things that maybe next year they're going to take a pause on buying, whether that's, you know, clothes or iPhones or whatever. We just don't know. So that's where I think we see some of the headwinds.

On the European data transfer issue, as I mentioned in my comments, there's continuing uncertainty about the viability of transatlantic data transfers in light of recent European regulatory developments. And so we're continuing to monitor that. We're working hard to resolve it, but we don't know about what the timing may be for a resolution.

And this has to do with the ability to move data back to the U.S. It's not a Facebook-specific concern. It relates to European concerns of that aspect of U.S. law and the ability of U.S. government to potentially get access to European user data.

And so this is a large political issue for the U.S. and the E.U. to settle upon. But if the IDPC, who is our regulator, maintains their position and the situation is not otherwise resolved, it could impair our ability to operate material portions of our business in Europe.

So we don't think that's a likely outcome, but it's certainly a possible outcome, given where we are right now. And so that's why we're raising it as a risk.

Jason Helfstein: And then just a quick follow-up, I mean, we're all noticing how much better you are doing with e-commerce ads, meaning very specific to Facebook and Instagram. You don't think that those improvements could offset some of the macro comps that you're alluding to this year?

Dave Wehner: Well, when you say offset the macro comps, I mean, I think the macro comps are going to be a headwind to growth. I mean, I think the -- if you look, we delivered revenue growth which was the highest in two years.

And part of that is execution, but a big part of that is the macro environment that we're operating in and some of the favorable tailwinds to our business that that involves, the shift to online commerce and the greater share of personal consumer expenditures going to products versus services.

You know, we don't have a crystal ball to know exactly how 2021 is going to play out, but I think we are just trying to call it straight about those being true macro tailwinds to our business and that, when we look out, we think that those -- that consumer shift -- the e-commerce shift isn't going to happen as quickly and the product and services split is probably going to normalize.

So those will likely not be tailwinds -- and given the strong growth we had in Q4 this -- last year, they're going to be headwinds.

Jason Helfstein: OK. Thank you.

Dave Wehner: Thanks, Jason.

Operator: Your next question will come from the line of Brian Fitzgerald of Wells Fargo. Please go ahead.

Brian Fitzgerald: Thanks, Dave. Two quick ones and just want to see if we can drill down a little bit on this. It sounded like on the call you guys confirmed that you'll be using Apple's consent request notification to gather targeting consent, even though you're no longer using IDFA. I'd hate to kind of mince words, but we just want to understand if we have it correct.

And then trying to think about the opt-out rate, what it might look like, we were wondering if you could kind of compare or contrast that to what you're expecting there maybe versus what you thought going into GDPR a few years back?

Anything you could tell us in the final analysis about how people did not opt out during GDPR transition and the impact on ARPU that had for those who did? Any thoughts there would be great.

Dave Wehner: Yeah, I mean, I think -- oh, go ahead, Susan, you take it. Take it.

Susan Li: I was going to talk about the upcoming Apple changes. So when Apple begins to implement these features, which we are expecting to be at some point in Q1, but there's a little uncertainty, they -- they're requiring app developers, including us, to show an in-app prompt asking people for permission if we want to use their information for personalized marketing. And that's broader than just IDFA.

And in fact, for us, the impact of losing IDFA is relatively speaking smaller. That primarily impacts ads that are targeting app objectives, like app installs.

The sort of ability to use the third-party data piece, that's what we're really requesting users opt in for us to be able to use. And that's the sort of more important component of this.

That's something that we use as part of our ads ranking and targeting and measurement, and this is sort of a policy requirement from Apple in this change, which is a little bit different from IDFA, which is sort of a more specific technical component.

Dave Wehner: Yeah, and then in terms of opt-out rates, we're not giving specific guidance on that, but we do expect there to be high opt-out levels. And that's what's factored into our outlook. So we do think -- we do expect that to be something that we're going to have to navigate.

Brian Fitzgerald: Got it. Thanks, Dave. Thanks, Susan. Appreciate it.

Dave Wehner: Thanks, Brian.

Operator: Your next question will come from the line of Michael Nathanson from MoffettNathanson. Please go ahead.

Dave Wehner: Next question...

Michael Nathanson: Dave?

Dave Wehner: Yep.

Michael Nathanson: Hey, thanks. I have two for you. Maybe Susan could jump on the first, too. You know, when you're talking about the GDPR impact from a couple years ago, I wonder like what lessons have you learned.

When you look at the changing growth in Europe, could it be due to Brexit worries, economic slowdown? But, you know, did you see any real lasting impact to your business from whatever privacy changes were put through a couple years ago? That's one.

And, two, is -- I was going to ask Mark this, but since you're the representative on the call, do you have a good sense of, will we see any Section 230 regulatory change in the near term?

I mean, it seems like it's a constant talking point. But I wonder, what's your position on -- is this an inevitable change? Or is it going to be a political football for a while now?

Dave Wehner: You want to take the first one, Susan, and I'll take the Section 230 or...

Susan Li: Yeah. So the first question was kind of about the longer-term impact of GDPR in Europe. Is that right?

Michael Nathanson: In Europe, right, right.

Susan Li: Yeah, when we look at sort of the impact of the GDPR implementation, and if you look at sort of the treatment that we implemented of what the consent flows looked like, those are quite different, I think, from what things will probably look like with the upcoming Apple changes.

I think we feel like we've managed through the GDPR implementation quite well. There's obviously been some impact on Europe, but that's not the -- that's not been -- a material part of like the recent trends in Europe.

Dave Wehner: Yeah, I think it's a question, Michael, of -- often the devil is in the details in how you implement specific consents. And so the Apple iOS 14 consent is effectively drafted by Apple and not by the app developers themselves.

So you've got a little bit less ability to message the customers -- you know, there's a little bit less control on the customer's part and a little bit more control in Apple as the platform, you know, really kind of instituting a consent flow that they require.

On the concerns about Section 230, I think it's really -- it is a political -- I think there are basically opposing forces. I think while there might be bipartisan support for changing Section 230, there's not bipartisan support as to what 230 does and what changes they would like.

I think on one hand, the -- sort of the simplistic model is that Democrats have generally wanted the platforms to exert a more heavy hand in terms of moderating content and the Republicans' concern has been around just the opposite, which is that the platforms have been, you know, operating too aggressively to moderate content and have thus -- and are thus sort of taking a political stand and stifling one side's political views.

So I don't think that there is a -- as far as I'm aware -- that there's a clear bipartisan approach to how to modify 230. And given that, I think it's very unclear -- especially in a Senate environment that's quite split, how Section 230 reform moves forward.

But I think there is clear bipartisan interest in addressing Section 230. So how that plays out I think is very uncertain. And I would expect there will be debates about it. It's not clear what the path forward would look like.

At some point, I would expect Section 230 to get reopened and addressed. Whether that can be done with this current Congress or not is less clear.

Michael Nathanson: OK, thanks, Dave and Susan. Thank you.

Dave Wehner: Yep.

Operator: Your next question will come from the line of Mark Shmulik of Bernstein. Please go ahead.

Mark Shmulik: Yes, hi, Dave, hi, Susan. A couple questions. The first just on the user story. You know, last quarter, you kind of guided down sequentially in North America, just kind of given some of the, I guess, tail-off from the COVID-related bump.

Has that normalized? Or would you expect that to normalize going forward? Or can we still expect continued potential erosion, if and when we do reopen?

And then the second question, as it relates to the other revenue, certainly the Quest 2 headset was a big part of that. But any dimensionalization you could do around the different kind of components or contributors to "other" would be a great help, thank you.

Dave Wehner: Why don't I take the user question, and then on the other revenue, Susan can take that one?

You know, I think that the story is on sort of -- like North American users, in mature markets like U.S. and Canada, we're still above pre-COVID engagement levels, so I think we're still somewhat like 5 million above where we were in Q4 of '19.

So I do think there is still some potential volatility around DAU as it relates to North America and still a potential for some reversion there, as it relates to sort of peak engagement levels coming off a pandemic.

You know, we re-engaged inactive users, as opposed to necessarily getting new users in North America. So I think there is still some potential around volatility there. At least at the sort of levels we've seen.

And then, Susan, you want to take the other revenue question?

Susan Li: Yeah, so on other revenue, the overwhelming share of that is the Quest 2. Other components, certainly we had strong Portal sales over the holidays, also.

And then sort of the games payments business that we've had for a long time is kind of the -- is the other big chunk of that. But Quest 2 is by far the largest driver.

Mark Shmulik: Great, thank you.

Dave Wehner: Thanks Mark.

Operator: Your next question will come from the line of Kevin Rippey of Evercore ISI. Please go ahead.

Kevin Rippey: Hey, thanks for taking the question, guys. On the call, Mark used I think the phrase anti-competitive behavior on behalf of Apple. I was wondering if you can maybe just talk through how you guys are thinking about venues by which you might resolve that anti-competitive behavior?

Is it just investing in sort of mitigating technologies? Or are there sort of other steps you guys are thinking of that are on the table? Thanks.

Dave Wehner: I think Mark sort of was clear that we're focused on continuing to try and build the best products, make the case for those products with consumers. So that's the focus of our efforts.

Obviously, calling attention to where we think there's a difficult environment is part of that. But continuing to make the case by building the best products is our biggest focus.

Kevin Rippey: Got it, thanks.

Operator: Your next question will come from the line of Heath Terry of Goldman Sachs. Please go ahead.

Heath Terry: Great, thank you both. To the extent that there was a -- modest, obviously, very modest decline in engagement in the UCAN region, beyond the COVID reversion that you talked about, is there any concentration in terms of property or profile of user that you would identify?

And then, looking ahead, to the extent that we can, is there any direction you could share on how much more COVID reversion or other drivers of engagement, positive or negative, you would expect in the quarters ahead?

Dave Wehner: Yeah, I mean, he sort of addressed that a bit, but I'd say, in general, we're sort of at a pretty high level of engagement in U.S. and Canada, and where we saw during COVID sort of older cohorts who were inactive kind of coming back to Facebook, we've seen some of that sort of come back off.

And so, I don't think this is a -- I'd say we'd expect some volatility, modest volatility around this. It could go one way or the other, but it's pretty -- you know, it's relatively stable.

But I think given that we've gained some engagement around COVID, we've seen some of that revert. We do think there's a little bit of pressure there.

Operator: Your next question will come from the line of Ron Josey of JMP Securities. Please go ahead.

Ron Josey: Great, thank you. Hi, Dave, hi, Susan. I wanted to maybe touch a little bit more on Stories. You know, up until now, it's been -- I think it's been called out sort of as a headwind to monetization. And this quarter I think we talked about it being an effective direct response tool. We saw overall pricing up 5%.

So, Dave, can you just provide a little more insight on how Stories is becoming a bigger part, or if at all, within buys across Facebook and Instagram? I mean, we use the term "must buy" often, you know, talk about who's buying Stories.

I think it was mentioned in DR, but any insights on just how that's going and how that's impacting the impression growth, which decelerated relative to pricing a little bit more? Thank you.

Dave Wehner: Yeah, we're seeing Stories be one of the contributors to impression growth. So it's obviously a part of the growth story.

I would say, the way I'd characterize it is, Stories are at lower prices than Feed ads, but those -- that gap is improving because of the progress we're making with direct response ads on Stories. So, I think that's one of the highlights that we called out, as it relates to pricing.

It's -- the biggest factor in pricing is just the slower impression growth kind of naturally leads to higher pricing growth in the auction as demand has been high because of the things that we've called out related to the tailwinds to the business for online commerce and general commerce being strong.

So -- but within that context, I'd say the additional factor is the improvements to the direct response environment we've made on Stories. So that gives us, you know, as we see continued growth in impressions on Stories and we continue to make progress with making those units more effective for direct response advertisers, we think that's a good growth driver in 2021.

Ron Josey: Right on. Very helpful. Thank you.

Dave Wehner: Thanks, Ron.

Operator: Your next question will come from the line of Dan Salmon of BMO. Please go ahead. Dan Salmon, please go ahead.

Dan Salmon: Hey, guys, sorry about that. Evening to both of you. Dave, one quick question, first for you. You guided to stable or improving year-over-year revenue growth sequentially in Q1 and Q2. You also said you expect the impact from the iOS changes to begin late in Q1.

I think that should roughly coincide with the trough of your ad business a year ago in the early stages of the pandemic. So can you just tell us about the balance of those two factors in the second quarter guidance?

And then for Susan, I just want to come back to Apple's ATT prompt rolling out. To be clear, are you suggesting that Facebook will be asking something separately in a pre-prompt or just confirming that you'll be showing the prompt?

And then just, second, you said your biggest focus for the iOS changes was potential restrictions to certain third-party data as the most material part of the changes. What specific data are you referencing? And how is that used? Thank you, sorry.

Dave Wehner: OK, so I'll take the first one. And the biggest factor in the Q2 revenue growth is by far going to be the fact that we're lapping a weak quarter related to the initial pandemic shock. So that -- we got that for the last few weeks of March. And then, certainly the beginning of Q2, and through most of Q2, you know, more challenging demand environment, but we did see throughout Q2 things rebound.

But overall Q2 is going to be an easier comp, because it was so depressed from COVID in 2020. That's a much bigger impact than the beginning of the iOS 14 rollout. So, yeah, I think it's a different order of magnitude impact.

Susan Li: On the iOS question, I don't think we've said anything publicly yet about whether we're showing a pre-prompt, although that's certainly one of the options available. So I think that's the first part of that question.

And then I think the second question you asked was about sort of what data is being collected. Was that right?

Dan Salmon: Yeah, the third-party -- you said that your bigger focus was not on IDFA restrictions, but certain third-party data that you may be restricted. What exactly is the data you're referencing there? And how is it used?

Susan Li: Yeah, so -- for us, any ads that -- so, as an example, ads that result in some kind of off-site conversion -- that data -- if it isn't on-site first-party data for us, that would be third-party data that would be -- would sort of in the current world be something that we'd be able to use as part of our ranking and ads targeting and measurement systems.

And so those types of signals, which, I think have been an important part of our ads targeting, if users opt out, won't be available to us anymore.

Dan Salmon: Yeah. OK, that's great. Thank you, Susan, and thank you, Dave.

Dave Wehner: Yes.

Operator: Your next question will come from the line of Stephen Ju of Credit Suisse. Please go ahead.

Stephen Ju: OK, thank you. So, Dave, if I may ask for a clarification on what you said on the public call, just so we're crystal clear, so when you talked about impact being at a platform level for IDFA, are you just basically saying that advertiser ROI may drop, but it'll drop across the board for everybody and, hence, Facebook will fare equally, if not better, than everybody else in terms of overall wallet share as effectively a relative gain?

I don't want to put words in your mouth, but I just wanted to clarify that...

Dave Wehner: Yeah, I think that's generally the right way to think about it. I do think that there are going to be advertisers who are, by virtue of some of the dynamics that Susan has talked about, for instance, you know, an ability to use website conversion data to optimize an ad -- ad performance for e-commerce or something like that -- they could find that they're not able to advertise anywhere effectively now because of the Apple changes.

And so that's -- so I think you're going to get people who drop out of advertising on iOS in general -- so I do think that, whereas we might be able to maintain or possibly improve our share of wallet, as you said, I do think you're just going to get advertisers and businesses who are going to decide that it's not cost-effective to advertise.

That's going to mean they're not going to grow as much, and that's going to mean they're not going to hire as much, and I do think that the one cost that we're trying to make sure that everyone who is involved understands is having a large platform like Apple set this sort of policy is going to have potential economic impact more broadly, in terms of small businesses and job creation and the like.

One of the bright spots in growth in the last, you know, 10 years has been the ability of people to leverage advertising more effectively to grow their businesses. It's a big benefit that we think we bring to the table for the economy, for small businesses. It's something that we've continued to highlight in all of our earnings calls, because we believe it deeply.

We think that's a challenge and it's not a great thing for economic growth in general to make a real -- this type of move against targeted advertising. So that's kind of what I would say as it relates to the two dynamics going on.

Stephen Ju: Got it. And...

Deborah Crawford: Operator, I think -- oops, sorry, go ahead.

Stephen Ju: Sorry. I don't think you guys disclosed the number of advertisers on this particular call. Is it still at around 10 million? I think Mark talked about 200 million businesses overall, right?

Dave Wehner: We haven't updated the disclosures. So it continues to grow, but we've just said that over 10 million advertisers and over 200 million businesses.

Stephen Ju: Got it. All right. Thank you.

Deborah Crawford: Great, thanks. So, Operator, we are going to take one last question.

Operator: OK. Your last question is going to come from James Lee of Mizuho Securities. Please go ahead.

James Lee: Thanks for taking my questions. Hey, Dave. Thanks for taking the questions here. Some in the agency we're talking to, they are saying that your company is offering a

new conversion API maybe to potentially mitigate risk of losing IDFA or even cookies. Is there any way you can provide some color on how that works? Thanks.

Susan Li: Yeah, so there are some APIs built by either us or Apple that let us receive data, albeit, an aggregated, not-user-level form, for example. So it's less effective than the way that we receive data today.

But these are -- depending on the API, certainly Apple could choose to change the design of APIs that they build to make them less effective or to create new policy restrictions that would prevent us from using some of these.

So these are -- these are sort of possible short-term mitigations, but they're still subject to uncertainty.

James Lee: OK, great, thank you.

Deborah Crawford: All right, thank you, everybody, for joining us today. We appreciate your time. And we look forward to speaking with you again.

Dave Wehner: Great, thanks.

Operator: Ladies and gentlemen, this concludes today's conference call. Thank you for joining us. And you may now disconnect your lines.