

Meta Platforms, Inc. (FB)
First Quarter 2022 Follow Up Call
April 27th, 2022

Operator: Good afternoon. My name is Jen and I will be your conference operator today. At this time, I would like to welcome everyone to Meta's First 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 one then the number four on your telephone keypad. This call will be recorded. Thank you very much. Ms. Deborah Crawford, Meta'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 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 events.

During this call, we may present those GAAP in certain non-GAAP financial measure. 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 "one" then the number "four" 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's speakers. Your first question comes from the line of Justin Patterson with KeyBanc. Please proceed.

Justin Patterson: Great, thank you very much. There's clearly a lot going on around AI investment. As you move through this current phase of the investment cycle, how should we think about the pace of product innovation going forward? Or said differently is just getting the AI up and running today detracting from the pace of some other product investments? Thank you.

David Wehner: Yes, Justin. I think – the framing that I would give for what we're doing on the AI front really links to a couple of the key priorities that we talked about a lot on the call. The first is helping support the Reels effort in terms of being able to rank and rate unconnected content to be able to serve up to people in Reels.

Second, it's an important part of what we're doing to rebuild our ad stack, to be more effective at ads with less data. So what we're doing with our investments in AI, I think it's very much on point with a couple of the key priorities and the Family of Apps. And so, it's definitely an important part of the investment landscape and what we're trying to do to accelerate product growth both on the engagement and the ad side. Shall we go to the next question?

Deborah Crawford: Next question?

Operator: Your next question is from the line of Ross Walthall with Cleveland Research. Please go ahead.

Ross Walthall: Hey guys. Thanks for the opportunity. I had a few questions. One was just on commerce and some of the in-platform efforts for conversion. How are those efforts evolving over time? It seemed like on the call we talked more about things like Click to Messenger ads versus some of the other solutions like Instagram Checkout, so just curious if you guys see a different path forward there than originally outlined?

And then second, on the measurement solutions, I think you guys mentioned Conversion API Gateway. Can you just talk more about what this tool is and what it'll provide for SMB customers?

Dave Wehner: Yes, I can take the first part and then Susan can take the second part. Yes, I think when we talk about kind of what our mitigations are for the ad headwinds that we're facing, we sort of talk about the improvements that we're making in driving more onsite conversions. And when we sort of take it from that lens, things like Click to Messaging ads today, it's a multi-billion dollar business growing double-digit percentage.

So in terms of today what's having an impact on the on-platform efforts for conversion, Click to Messaging is just significantly bigger than things like Shop ads, though, Shop ads is clearly an important strategy. Commerce – e-commerce is our biggest vertical. Obviously it's got challenges with the overall compares coming off of COVID, the targeting and measurement headwinds hit that sector significantly. But it's our biggest sector and having an onsite conversion option for Shops is an important part of this strategy.

So ultimately that's going to be a big opportunity for us to drive onsite conversions through Shops, but today in terms of dollars and growth things like Click to Messaging ads are a bigger part of this solution, which is why we were kind of highlighting them.

Susan Li: And then your second question, which I think was about CAPI Gateway. So CAPI itself, the Conversions API, is a pixel alternative by which advertisers can send data directly to Facebook, and the Conversions – the CAPI Gateway is basically a version of this that is trying to make it more accessible because today CAPI integration

requires significant technical expertise and partner integration. And so, smaller advertisers who lack in-house dev teams aren't able to set it up.

We launched CAPI Gateway, I think, last September. And so, that's intended to help advertisers set up CAPI more quickly and easily without sort of significant in-house developer resources. It's a self-service configuration option that you can access directly through Meta Events Manager, and there's actually like a pretty clearly laid out website intro to how to use it and how to get it set up. So that's the CAPI Gateway recap.

Operator: And our next question is from the line of John Blackledge with Cowen. Please go ahead.

John Blackledge: Great, thanks. Two questions, first on the short-form video. Dave, how will Reels kind of differentiate itself in short-form video? And I know you've talked a lot about the AI efforts, but like, will the AI efforts -- will it be the content itself? Will there be more exclusive content on Reels over time? Just any color there would be helpful.

And then secondly on Metaverse efforts, you guys are opening a retail store in a few weeks. Do you envision a large retail footprint over time as kind of part of the strategy that scales hardware and Metaverse efforts? Thank you.

David Wehner: Yes, on Reels and differentiation we think we're well positioned to bring the social element to the short-form video experience since Reels sits on top of people's social graphs, so we think we can benefit from that. We've seen that sharing Reels generates conversations and engagement, and it also provides a helpful signal for ranking since sharing a Reel is a pretty good indication that it's high quality.

And so, that can feed into our ranking algorithms. So that's kind of the way in which we differentiate Reels, but obviously we've got to bring more content creation and engagement but those two things flywheel and the fact that we're getting 20 percent time on Instagram and Reels is a good indication of us starting to get that flywheel going.

We certainly don't -- we certainly have not announced any plans for a large retail footprint at this point. You know, that's very much a showcase, not yet part of a broader strategy.

John Blackledge: More of a test or something. OK, thank you so much.

David Wehner: Yes.

Operator: Our next question is from the line of Deepak Mathivanan with Wolfe Research, please go ahead.

Deepak Mathivanan: Great, thanks for taking the questions. Dave, can you provide additional color on the second quarter revenue guide? Obviously there is full quarter impact from Russia, Ukraine, and then also the incremental softness in Europe.

But how do you incorporate some of the broader potential macro uncertainties from other markets, you know, that could manifest in the next few months? And then more broadly, how do you think about the cyclical of the ads business to macro themes? Obviously you are a very sizable ads business, but curious to hear your thoughts on that.

David Wehner: Yes, well on the Q2 guide, I think we have said that it is factoring in a continuation of the headwinds that we saw in the first quarter, as well as the situation in the Ukraine. You know, Ukraine kind of hit us on a couple different dimensions.

We obviously stopped serving ads in Russia, and stopped accepting ads from Russian advertisers and that was in aggregate a point and a half of revenue in 2021. But there's also just a broader impact to ad demand, and we saw pretty significant slowdown in Central and Eastern Europe, we saw that impact Q1 ad demand in Europe more broadly.

But we've seen an introduction of just -- you know, additional uncertainty in the macroeconomic landscape that corresponded with the war, that we think has compounded the challenges and headwinds that advertisers were already facing.

And so we're assuming that those do persist, and that's reflected in our Q2 outlook. You know, there's just general lots of macro uncertainty with rates going up, with inflation, you've got supply chain challenges, you've got Chinese -- you have Chinese lockdowns.

So there's a lot of different things that are, you know, part of the reason that we give a broad range of guidance for Q2 revenue. But I think it is -- it is a challenging time from a forecasting perspective. So I think the range sort of acknowledges that.

Operator: Our next question is from Ron -- our next question is from...

David Wehner: Go ahead.

Operator: ...Ron Josey with Citi, please go ahead.

Ron Josey: Great, thanks for taking the question. Maybe two, please. Just last quarter, Dave, there was so much talk about competition, in this quarter we're hearing Reels is 20 percent of time spent on Instagram. So can you just talk about feature parity of Reels from a product perspective?

Understood your comment on the social aspect of it all. And just any progress around content creation? And then maybe a bigger picture question is as Meta's evolving ad system does more with less and the importance of AI and ML just thinking about the building blocks to get there.

Is it right to think duration in the feed, greater focus on transactions with Click to Message can all improve recommendations that lead into this next version of the ad

system? So we're sort of seeing these improvements to the ad system on a rolling basis. Thanks.

David Wehner: Thanks, Ron. I can take the first part. I think the big picture short-form is a huge opportunity. It's obviously, as a category has taken a lot of growth, a lot of the growth in the market has been in short-form. Clearly, TikTok has done quite well with short-form. I think with Reels we've got a strong competitor in the market.

But there's a lot of work that we need to do and on a number of areas. The three that I would call out were -- are discovery, and there it's about improving ranking with the AI and machine learning investments that we're making. As I mentioned, sort of leaning into social sharing.

And also leveraging the fact that we've got great products with Feeds that we can use as a means to introduce Reels to people. So that's discovery. Then on creation, it's improving the tools and making it easier to produce compelling content easily.

Some examples of that are things like we've enabled auto-generated captions for creators, we've launched clipping tools to make it easy to turn live or video on demand videos into Reels.

And then the third thing is just monetization, which is we've recently introduced our Reels bonus play program as a part of our billion dollar creator investment. So we're trying to build more direct monetization opportunities for creators into Reels. And we think that's also important to just driving content creation.

Susan Li: On your second question about the ads building blocks in particular in a world with less data, I would kind of direct you back to the comments we've made about how we are adapting to the signal loss environment broadly.

In the near term, there obviously is the specific tools that we're helping to build such as CAPI, CAPI Gateway, AEM, that sort of thing. We're also building a lot of different ad formats that are intended to move third-party data on-site to first-party data.

The Click to Messaging ad format is one that is growing quickly, and has been a really exciting line of growth for us. A lot of our investments in commerce fall into that space also. And then the sort of long-term investments in privacy-enhancing technologies we hope those will very much be the building blocks of revenue in the long run privacy environment.

And we've talked about some of those in the past, secure multi-party computation, on-device learning, differential privacy. So there are a lot of -- those are long, multi-year journeys that we are on, that we will -- that will require a lot of engineering investment. But we hope will fundamentally make our ad products more effective in the new data environment.

Ron Josey: Thank you.

Operator: The next question is from the line of Brian Fitzgerald with Wells Fargo. Please go ahead.

Brian Fitzgerald: Thanks, guys. Maybe two quick ones, follow-ups. Some of the digital or social agencies have noted an increase in video ads in part for seeding retargeting campaigns.

We're just wondering if you've seen anything like that, are advertisers using things like completed videos to seed retargeting at a higher rate than in the past? Maybe to retarget a website visit? So video retargeting is the first question.

Second one is just there have been reports in the trade press that Reel ads has stepped up maybe towards the later part of the quarter even small, medium businesses are shifting budgets back. Was there an inflection point in the quarter in terms of delivering improved results for advertisers?

Susan Li: I don't think we have anything specific to say about the video retargeting campaigns.

David Wehner: No, video ads in -- for -- performed -- was a -- growth area for the company in general. Obviously, a direct response, in general, is important for us and I would imagine that there's use cases that are like that that are seeing adoption in video. But I don't have specific examples to give there, Brian.

Brian Fitzgerald: OK.

David Wehner: And then on your second question, Susan can add any color here, but I don't think there's an inflection point in the quarter. The only inflection point in the quarter was really the war in Ukraine, which was a negative inflection point in terms of how the business was trending. So that's -- I don't think there was anything I would call out specifically on the ROI side.

Susan Li: No, except to say that the demand decline that we saw there would have played through to pricing generally.

David Wehner: Yes, so, when pricing goes down...

Brian Fitzgerald: Yes.

David Wehner: ...then ROI goes up. So perhaps that is a correlation.

Brian Fitzgerald: OK. Thanks, Dave, thanks, Susan.

Operator: Our next question is from the line of Rich Greenfield with LightShed Partners, please go ahead with your question.

Rich Greenfield: Hi, thanks for taking the question. I guess just a little going back to sort of one of the questions that was asked at the end of the main call on TikTok competition. Last quarter Mark had basically said the problem is not that Reels isn't growing really quickly, but it's that TikTok is really growing quickly as well off of a very large base.

Do you think that you're now taking share or are you still not gaining share or even losing share to TikTok competitively? And then I have a quick follow-up on AI.

David Wehner: Yes, I don't think I have anything on that front, Rich. I think we're pleased, obviously, with the growth that we're seeing in Reels. Everything we see TikTok remains a very strong competitor in the market.

I think it's -- I think the third-party data is -- we have access to some of the same data that you do so I think you can look at that. But I think they continue to perform well. And then what was your question on AI?

Rich Greenfield: Well, I guess when you -- when you think about the engagement, Dave, you clearly talked about engagement improving relative to the beginning of the pandemic. And I guess there's two things that you're really doing, one is obviously Reels. But the other is AI, which is not just Reels but it's Stories, it's Feed, et cetera.

So when you look at those two factors is there one that's more significant in driving the improvements and engagement or is it equal? Just how do we think about those two factors improving engagement overall?

Dave Wehner: Well, I think overall, I think Reels is -- and some of this is obviously where we're focusing our product efforts, where we're introducing Reels in Feed a lot. So what we're doing is really also intentionally trying to seed and grow that product.

So there's certainly organic growth from Reels. But there's also, sort of, intentional, getting Reels in front of people in Feed. So I think it's a combination of those factors that is important. But overall, I would say video engagement broadly is probably the bigger macro driver. And then within that, Reels is part of it.

But on Facebook, we've talked about video being around 50 percent of the time. Video's been important for Facebook, even separately from Reels. Things like Facebook Watch have been an important driver of growth over that kind of longer aperture time frame. So video is the bigger driver.

I don't think AI is a -- we -- obviously, we rank people's Feeds, we do all of that. But kind of the more substantial investment we're making in, kind of, hardcore machine learning is more in front of us than behind us on that front. So I think I would really point to video and then Reels within video as being the drivers there.

Operator: Your next question is from the line of Mark Mahaney, with Evercore ISI. Please go ahead.

Mark Mahaney: OK, thanks. If I could throw out three questions? When you talk about e-commerce slowdown, you simply mean versus the really strong growth that e-commerce had at the peak of COVID, it's not like you're making any comments about near term slowdowns in e-commerce? I just wonder if you could just clarify that?

Susan Li: Yes, it's slowing down, certainly, relative to peak COVID for a variety of reasons, which I think we've...

Mark Mahaney: Yes, yes.

Susan Li: ... mentioned.

Mark Mahaney: But there's nothing -- there's no recent commentary you're making about a slowdown?

Dave Wehner: Well, I mean, it's recent in the sense that in Q1, e-commerce was a driver of the deceleration of growth even from Q4. So I mean, we're comparing against...

Mark Mahaney: I got it.

Dave Wehner: I mean, Q1 and Q2 were very strong quarters still within the -- what we think as some of the pull forward of e-commerce growth during COVID that we saw.

I mean, if you just look at the -- not Facebook's stats but more broadly, certainly for the U.S., you can see e-commerce as a share of retail really skyrocketed during COVID. We weren't certain as to whether some of those trends would hold.

It seems that they've reverted back to the prior trend line, which means that e-commerce is growing substantially more slowly. And it's kind of shedding share relative to retail. At least in the near term, we think it'll probably start growing again as a share of retail. But right now, it's offline retail that's doing relatively better from a growth perspective. And we're less...

Mark Mahaney: Yes.

Dave Wehner: We're less geared towards that.

Mark Mahaney: Got it. Got it, thanks for clarifying that. And then the other two quick questions, when the CEO talks about operating margins, I always find that really exciting and I'd listened to Mark. And so, it sounds like what you're saying is that you're going to -- you're going to take excess profits or whatever from the Family and put -- and use that to fund Reality.

But the way you're going to run the business, the operating -- the growth goal is you'll make sure that you'll always continue to grow. You won't allow investments in Facebook Reality Labs to undermine the goal of constantly growing operating profit.

I think that's the most direct way of what he said. I don't he's actually said anything about margins. Are you trying to maintain a certain margin level, too, or just simply making sure that you're always growing operating profits? And so, if that means -- if that means bringing down investment spend in Facebook Reality Labs you'll do that. But you'll just simply grow operating profits. Can you just clarify that?

Dave Wehner: Yes, let me take a crack at that. I think -- I would say what -- first of all, I love the fact that you're excited about CEOs talking about margins, I am too, Mark. But yes, I think what Mark said to be specific is the goal is to grow -- continue to grow the Family of Apps business and get that back to better growth rates.

We think that could be high margin growth rates, which means that we'll be generating excess operating profits, operating profit dollar growth from Family of Apps which we can then invest in Reality Labs while still growing overall profit.

I would say that's the goal. Now I think Mark was clear that there will be times where we might face macroeconomic challenges, short term volatility, which means that that goal cannot be met because we would have to -- and in that situation we may elect to trade-off short term profitability for the importance of the long term investments that we're making.

But the goal is to continue to grow operating profits and fund Reality Labs through that growth of the Family of Apps business.

Mark Mahaney: OK. That's great. That's very shareholder friendly and love to hear that. Last thing is when you talk about this -- what occurred to me is that this differentiation, a really competitive advantage you have in Reels is you've got these massive social signals that no other short-form video company has.

I think -- at least I think you do versus the biggest competitor out there. I think you do. And so does that actually have a P&L implication associated with it, i.e. you don't need to spend as much actually buying content, seeding original content because you got so much -- so damn much of it just coming through social channels and you got social signals.

Could I read into that or any comments on how much you think you need to spend on original content in order to boost -- in order to grow Reels?

Susan Li: I think the social signals, which we certainly believe are part of what is differentiating about the Reels platform will help us leverage people's social graphs to make sure that we are ranking Reels as effectively as possible. We've seen that sharing Reels generates conversation, which is good for engagement and it's just a very helpful signal for ranking.

Having said that, we are also focused on attracting creators to the platform as well as we can via making creation as easy as possible and proving tools to make it easier to produce compelling content easily and also via creator monetization.

So Dave mentioned, I think, the Reels Play Bonus program earlier that's one of a many pronged effort as part of the \$1 billion creator investment that we had announced a while ago.

Mark Mahaney: OK. Thank you very much for your help.

Dave Wehner: Thanks, Mark.

Operator: And next question is from the line of Ygal Arounian with Wedbush. Please proceed.

Ygal Arounian: As -- just speaking to e-commerce a little bit and there's been a lot of discussion lately just kind of like an existential crisis with direct-to-consumer advertisers, obviously a big proportion of your advertising base.

With the challenges they're seeing, are you seeing a greater amount of churn or any indications that businesses are shutting down or that advertisers might be going to other -- to other methods like offline advertising in a way where it's going to take you some time to kind of put all these pieces together and they're shifting to these different formats in a way that's kind of faster than you're able to catch up? It's the first question, if that makes sense.

Dave Wehner: Yes. I mean, I think broadly obviously we got a very diversified advertising business. The -- I would say the longer tail of the advertising business continues to be quite healthy. We're seeing good growth from our SMB advertisers. I would say on the e-commerce side there's clearly headwinds and challenges just given the macro dynamics of how consumers are behaving, so that led to less, I think, dollar investment from those advertisers in customer acquisition.

I think -- I don't know that those advertisers are going to different formats because most of them are online. And so, I think they might be allocating budgets possibly under other online advertising formats, but I don't think they're going to offline.

We're seeing our sort of what we characterize as retail categories doing relatively better, and those are people who have like omnichannel offline businesses as well and they're actually advertising still more on online. So I think it's your pure play e-commerce players are advertising less. I would say your omnichannel guys are a little bit more active, but yes. That's the color I would give.

Susan Li: I'll just add that DTC is obviously a subset of the e-commerce vertical and we are seeing it I think similarly impacted, but not, I think, necessarily disproportionately so.

Ygal Arounian: OK. And then just on some of the things you're implementing around the first-party data or trying to implement around first-party data and integration and CAPI. Can you just help us understand what -- understanding some of the things that you're putting in place around it, but can you just help us understand the process?

And I've heard – I've heard things about partners and brands being hesitant in sharing first-party data. Are – for advertisers that are relying on CAPI, what's the feedback like? Are there other solutions that people are starting to rely on, third-party solutions? Just what's been the process of getting people on board as you build these things out? Thanks.

Susan Li: So I think CAPI has been I think a useful tool in integration for advertisers who have adopted it to I think a kind of – a question that came up earlier I think it was it is a big lift to integrate. So I think that the kind of the next step in that particular journey was CAPI Gateway to make it easier to integrate on a self-serve basis for a broader and smaller range of advertisers.

So I think in terms of – I mean, we are – we're building a variety of tools that I think we are helping advertisers understand how they work, how they work in terms of the aggregation and anonymization and time delay processes and why the tools sort of are the most effective – most effective ways for us to help them measure ad performance in the current -- in the current ATT environment.

And then the longer-term investments, I think are much further out in terms of timeframe. So I think that's something that you'll see play out on a multiyear basis.

But we are -- you know, with some of the things that we've talked about we are working on a private lift measurement, I think that's something that we've tested with a small number of advertisers, so we're kind of building out the -- we're taking baby steps, I would say towards building towards those long-term tools.

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

Operator: Our last question comes from the line of Benjamin Black with Deutsche Bank, please go ahead.

Benjamin Black: Thanks for the questions. I have sort of two follow-ups. So curious what you're seeing sort of broadly in terms of ad budget shifts from your SMB clients, given measurement and targeting challenges to alternative channels like Search in particular?

How has that trended since the signal loss last year? And then secondly another follow-up to the content investments on Reels. Sort of beyond direct monetization, is sharing ad revenue with creators in your longer-term plans?

David Wehner: Yes, I can take the Reels revenue one, and then I can maybe do both -- let's see. Yes, we want Reels to be a place where creators can make money and build businesses, and we're testing different models as part of our \$1 billion creator fund, and we're experimenting with revenue share. But at least in the near term we don't think revenue share will be the predominant model.

And then in terms of ad budget shifts from SMB clients, we see the results of our peers as well. I would say generally SMB has been -- has held up well. But facing

overall headwinds with overall business. SMBs are adopting some of our onsite conversion tools more aggressively than the larger clients with things like Click to Messaging ads where SMBs have been particularly fast adopters, so that's been helpful.

Benjamin Black: Thank you.

Deborah Crawford: Thank you for joining us today, everybody. We appreciate your time, and we look forward to speaking with you again.

David Wehner: Thanks, all.

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