



## The magic box of Facebook

As it prepares to sell 10% of its equity, what risks and opportunities lie ahead for Facebook?

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### The phenomenal growth of Facebook

The recent announcement by Facebook of an Initial Public Offering (IPO) of its shares has long been anticipated. The company plans to raise some \$5 billion for existing shareholders including founder Mark Zuckerberg who currently owns 28% of the business, by offering for sale somewhat less than 10% of its total equity.



The iconic social media site is not yet eight years old and yet the registration documentation filed with the United States Securities and Exchange Commission (SEC) shows the company making \$1 billion in profit last year. A quite remarkable figure when it is considered that its business model is based on the voluntary provision of personal information; but this of course is gold dust for advertisers, from whom Facebook derives the vast majority of its revenue. Facebook, in the SEC registration

documentation, points out that its phenomenal growth (88% revenue growth last year, and 154% the year before), will, not unexpectedly, begin to slow over time.

#### Risk factors - loss of users

Whilst it should be anticipated that the relatively small number of shares on offer will be voraciously snapped up by investing institutions, the future risk factors the business faces highlighted in the registration document, merit more than just a cursory glance. Key to its success is ensuring a growing, active user base, in order to generate increasing advertising revenue, and increasingly to sell more add on services. Currently the company claims to have 483 million daily active users, and 845 million monthly users, and loss of users would naturally enough lead to a loss of advertising revenue.

#### Risk factors - commercial pressures

The public sale of shares, even though representing only a small part of the company, is likely to increase the commercial pressures on the company to continually deliver growth in its business. Ensuring a balance between user goodwill and the interests of advertisers is likely to become increasingly problematic. Highlighting the difficult balance it faces, Facebook has been criticised on a number of occasions for changes it has sought to make to its systems and policies, which it has been argued would have a detrimental impact on users' personal privacy, with the latest barrage of privacy related criticism coming in respect of its recently begun roll-out of users' Timeline profiles.

#### Risk factors - competition

A further risk factor of note highlighted by Facebook relates to the significant competition pressures it faces, with the likes of Google, Twitter and Microsoft (which incidentally currently owns around 1% of Facebook) being prominent amongst Facebook's competitive rivals. Despite the huge profits Facebook is currently generating, it points to that fact that some of its rivals have significantly greater financial resources than it itself possesses, and such resources may be used aggressively in attempts to take business away from Facebook. One can almost visualise ranks of competition lawyers being readied for a future fight.

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