

Facebook Annual Report 2012

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Abstract

From teenagers to Edythe Kirchmaier, the oldest person with a Facebook profile at age 105, people of all ages have joined the social media revolution (Neporent, 2013). According to a recent study by PewInternet, “Internet users under 50 are particularly likely to use a social networking site of any kind,” and Facebook remains the most-used social networking platform (Duggan & Brenner, 2013). Although some investors found the company’s 2012 results disappointing, Facebook’s mobile efforts and victories over the last year hint at success in expanding onto handheld devices in 2013, as more users migrate to smartphones and tablets.

Financial Story

Harvard student Mark Zuckerberg launched Facebook, originally known as thefacebook, in February 2004 as a social networking platform for college students (Yadav, 2006). Facebook's mission is to make the world more open and connected. People use Facebook to stay connected with friends and family, to discover what's going on in the world, and to share and express what matters to them ("Key Facts," n.d., para. 1).

"In August 2005, thefacebook was officially called Facebook and the domain facebook.com was purchased for a reported \$200,000" (Yadav, 2006). Facebook's initial funding, equal to approximately \$40 million, came from Peter Theil (co-founder of PayPal), Accel Partners and Greylock Partners (Yadav, 2006).

Facebook unveiled Facebook Platform in May 2007, an initiative that invited third-party software makers to create programs for the service and make money on advertising (Stone, 2009). Hundreds of new features, or "social applications," were created as a result, leading Facebook's valuation to soar during the summer of 2007. In October, "Microsoft outbid its archrival Google to invest \$240 million for a 1.6 percent stake in Facebook, which valued the company at a startlingly rich \$15 billion" (Stone, 2009).

When Facebook hit 100 million users in 2008, the median age of a new member was 26 years old (Grandoni, 2012). On January 7, 2009, Facebook hit 150 million users. Zuckerberg said, "If Facebook were a country, it would be the eighth most populated in the world, just ahead of Japan, Russia and Nigeria" (2009). The year 2009 brought another exciting change when the Like button was introduced, allowing users to like their friends' content with one click (Pearlman, 2009).

Facebook expanded the use of the Like button on April 10, 2010, allowing users to

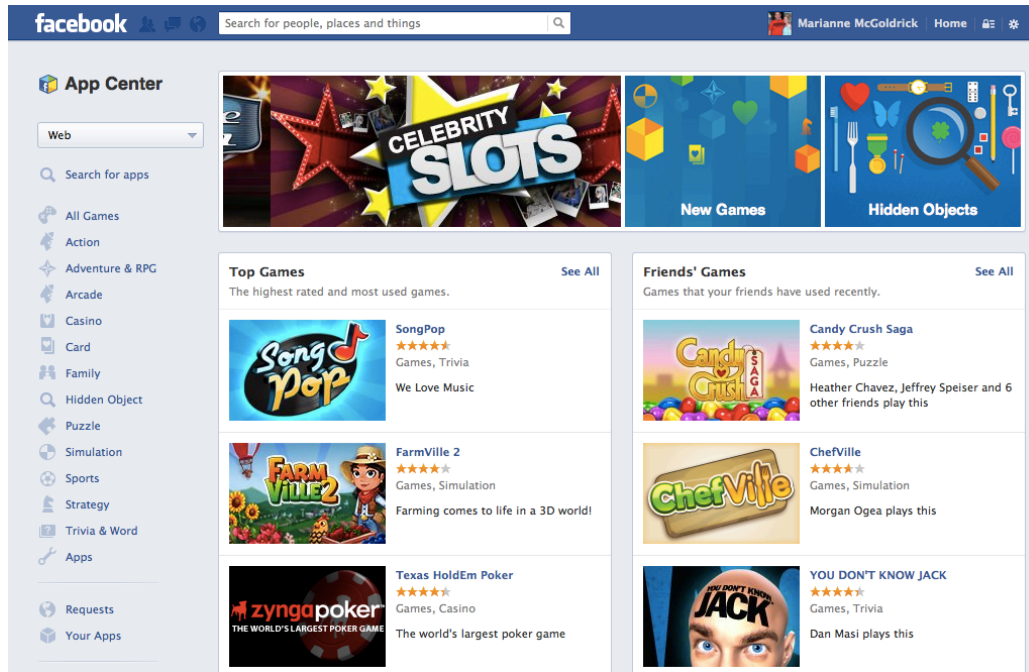
like website content on partner sites such as CNN, ESPN and IMDb (Siegler, 2010).

According to Mashable, “50,000 websites installed the Like button in its first week, and that number rose to 100,000 in less than a month” (Parr, 2011). One year after the launch of this new feature, a study done by Eventbrite concluded that a “Like” was more profitable than a tweet (Parr, 2011). Facebook hit another milestone on July 21, 2010 when it hit 500 million users. The median age of a Facebook member dropped to 23 years old.

In January 2011, Facebook “raised \$1.5 billion from Goldman Sachs and Digital Sky Technologies. The investment gives the company a valuation of approximately \$50 billion” (Segall, 2011). Facebook also confirmed its plans to begin filing public financial reports by April 2012, a move likely to coincide with an IPO (Segall, 2011).

On May 18, 2012, just one month past Facebook’s initial prediction, the company held its initial public offering. Facebook shares began trading around 11:30 a.m. at \$42.05 per share (De La Merced, 2012). Shares in the company fell soon after, more than once testing the offering price as the floor. “Shares of the social network giant closed at \$38.23, just 0.6 percent above the initial public offering price [\$38 per share] — a price that represented 100 times historical earnings” (De La Merced, 2012).

After becoming a publicly traded company, Facebook began to focus on advertising revenue and the mobile user. On June 7, 2012, Facebook launched the App Center, featuring mobile and web apps such as Draw Something, Pinterest and Nike + GPS (Wyndowe, 2012). “To make it easier to find social apps for mobile, the App Center is available in the Facebook iOS and Android apps, as well as Facebook.com” (Wyndowe, 2012).



Mobile improvements continued in August when the company announced a faster iOS app. “Facebook 5.0 for iOS is twice as fast as the previous version when launching the app, scrolling through news feed and opening photos in feed” (Johnson, 2012). On September 6, 2012, the social media site announced that they would be teaming up with Instagram – yet another way of improving Facebook’s mobile experience (Schroepfer, 2012). New Facebook advertising features in 2012 included (Wasserman, 2012):

- Ads that appear in News Feeds
- Ads that run on the right-hand side of your homepage
- Ads within the News Feed on your mobile device
- Ads that appear when you log out
- Offers

Facebook’s efforts were fruitful. According to their Form 10K Annual Report, “We had 680 million MAUs who used Facebook mobile products in December 2012, an increase of

57% as compared to 432 million MAUs who used Facebook mobile products in December 2011” (“Form 10-K Annual Report,” 2013). The report also noted there was a 36% increase in advertising revenue from 2011 to 2012, which largely contributed to the 37% revenue increase from 2011 to 2012 (“Form 10-K Annual Report,” 2013).

	Year Ended December 31,			2011 to 2012 % Change	2010 to 2011 % Change
	2012	2011	2010		
	(in millions)				
Advertising	\$ 4,279	\$ 3,154	\$ 1,868	36%	69%
Payments and other fees	810	557	106	45%	425%
Total revenue	\$ 5,089	\$ 3,711	\$ 1,974	37%	88%

Mobile revenue represented approximately 23% of advertising revenue for the fourth quarter of 2012, up from approximately 14% of advertising revenue in the third quarter of 2012 (“Form 10-K Annual Report,” 2013).

After fourth quarter earnings were announced on January 20, 2013, Robert Hof of Forbes wrote, “Revenues hit \$1.59 billion, up 40% and better than Wall Street forecasts of \$1.53 billion, and profits before certain charges were 17 cents a share, beating forecasts of 15 cents. But the stock’s getting hammered in immediate after-hours trading, down nearly 7%” (Hof, 2013). This may have sprung from some investors feeling that Facebook needs a more diversified revenue stream. Others may feel concerned that “Zuckerberg has declared 2013 an investment year, with high spending on new ad products and other features that will depress profit margins” (Hof, 2013).

Today, most of Facebook’s one billion users are women, at 72%, and it is most actively used by individuals ages 18 to 49 (Duggan & Brenner, 2013).

Facebook

% of internet users who use Facebook

		Use Facebook
All internet users (n=860)		67%
a	Men (n=418)	62
b	Women (n=442)	72 ^a
Age		
a	18-29 (n=164)	86 ^{bcd}
b	30-49 (n=254)	73 ^{cd}
c	50-64 (n=231)	57 ^d
d	65+ (n=183)	35
Education attainment		
a	Less than high school/high school grad (n=261)	60
b	Some College (n=250)	73 ^a
c	College + (n=345)	68
Household income		
a	Less than \$30,000/yr (n=223)	68
b	\$30,000-\$49,999 (n=152)	62
c	\$50,000-\$74,999 (n=127)	69
d	\$75,000+ (n=248)	73
Urbanity		
a	Urban (n=261)	72
b	Suburban (n=442)	65
c	Rural (n=157)	63

Source: Pew Research Center's Internet & American Life Project Omnibus Survey, December 13-16, 2012. N=860 internet users. Interviews were conducted on landline and cell phones. The margin of error is +/- 2.9 percentage points for results based on internet users.

Note: Percentages marked with a superscript letter (e.g., ^a) indicate a statistically significant difference between that row and the row designated by that superscript letter, among categories of each demographic characteristic (e.g. age).

The average age of the new member is 22, and “a majority of Facebook users -- 600 million -- are using mobile phones to log on to the social network” (Grandoni, 2012). It’s no surprise then that during a call with analysts on January 30, 2013, “Zuckerberg said the company plans to spend heavily to recruit talent in 2013 as the company pushes forward with new product development, particularly ‘mobile-first’ services” (Oreskovic, 2013). Analysts might be unhappy about a potential reduction in profit margins, but they would be even unhappier if Facebook wasn’t working to find new opportunities for growth.

Executive Summary

Facebook's mission is to make the world more open and connected. People use Facebook to stay connected with friends and family, to discover what's going on in the world, and to share and express what matters to them ("Key Facts," n.d., para. 1). Keeping members connected is exactly what Facebook accomplished in 2012 through its mobile efforts and, therefore, mobile efforts should be the theme of this year's annual report.

According to a recent study done by comScore, "53% of all cell phone owners in the U.S. have smartphones as their primary device" ("Mobile Devices," 2013). Downloaded applications were used by 54.2% of mobile subscribers in 2012, and social networking sites were accessed by 39.2% of subscribers ("Mobile Devices," 2013). "As mobile usage grows, the activities Internet users perform via their smartphone will account for a greater share of overall time spent online across all devices. Categories like mobile social usage will be the drivers and beneficiaries of this trend" ("Mobile Devices," 2013). This rapidly growing rate of smartphone and application use in the U.S. makes Facebook's advancement of mobile pertinent to its survival.

As of December 31, 2012, there were 680 million monthly active users (MAUs) who use Facebook mobile products ("Key Facts," n.d., para. 4). That's more than two times the United States population. This number is also up from 432 million MAUs in 2011 – a 57% increase ("Form 10-K Annual Report," 2013). Numbers never would have reached these heights if it were not for Facebook's mobile efforts in 2012. Mobile milestones of 2012 include the following:

1. June: App Center introduced (Wyndowe, 2012)
2. August: Acquired Instagram, a photo-sharing service with over 100 million

- registered users (Schroepfer, 2012)
3. August: A faster Facebook 5.0 for the iPhone and iPad is released (Johnson, 2012)
 4. November: The Share button was made available on mobile (Koolwal, 2012)
 5. December: Facebook for Android 2.0 released (Fung, 2012)
 6. December: Poke for Mobile introduced (“Introducing Poke for Mobile,” 2012)

In summary, as mobile usage continues to grow across the country, and the globe, Facebook’s mobile advances must grow with it.

Letter to the Shareholders

Dear Fellow Shareholders,

Your company earned \$5 billion in 2012, up 37% from \$3.7 billion in 2011, and the highest annual revenue in company history. The increase was due primarily to a 36% increase in advertising revenue during 2012 as compared to 2011 (“Form 10-K Annual Report,” 2013). As of December 31, 2012, the closing price of our Class A common stock was \$26.62 per share as reported on the NASDAQ Global Select Market (“Form 10-K Annual Report,” 2013).

I must say 2012 was a big year for our enterprise. Facebook is committed to our company vision. Facebook’s mission is to make the world more open and connected. People use Facebook to stay connected with friends and family, to discover what’s going on in the world, and to share and express what matters to them (“Key Facts,” n.d., para. 1). This could not be achieved without the help of our shareholders and investors, and this could not have been achieved without this year’s mobile innovations.

As of December 2012, we have 680 million MAUs who used Facebook mobile products, an increase of 57% as compared to 432 million MAUs who used Facebook mobile products in December 2011 (“Form 10-K Annual Report,” 2013). We introduced a new place for users to find social apps in June 2012. The App Center is available in the Facebook iOS and Android apps, as well as Facebook.com (Wyndowe, 2012). In August 2012, we acquired Instagram, a photo-sharing service with over 100 million registered users (Schroepfer, 2012). We also released a number of new Facebook apps for the iPhone, iPad, and Android devices. These releases were built to improve the speed and quality of our mobile product offerings (“Form 10-K Annual Report,” 2013). For the year ended

December 31, 2012, we estimate that mobile advertising revenue was approximately 11% of advertising revenue as a whole. Mobile advertising was not offered prior to the first quarter of 2012 (“Form 10-K Annual Report,” 2013).

We had 4,619 employees as of December 31, 2012. This is an increase of 44% from the end of December 2011. As we ramp up our investment in technical staff, sales and marketing, and general and administrative personnel in 2013, we expect headcount growth to continue (“Form 10-K Annual Report,” 2013).

Looking at the results of 2012, what pleases me most is how well our company performed, not in financial terms, but in human terms. We were always there for our users, providing new and improved ways for them to stay connected to family and friends. While we are proud of how we rose to meet the challenges faced this year, we are also keenly aware of the ongoing need to innovate and improve service to the members of Facebook. This is the only way we will be able to thrive going forward. Part of this ongoing innovation will be the continued investment in our mobile efforts in 2013.

We have able leaders, ample opportunities, high financial performance against our competition and, most important, focus on building a quality business. We are more passionate than ever about our future and the positive impact we can make on the world by keeping it more connected, one Facebook member at a time.

Thank you for believing in us, and we look forward to even more success in 2013.

Sincerely yours,

Mark Zuckerberg

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