



# HEDGEYE

## TWITTER IPO BLACKBOOK

TECHNOLOGY  
NOVEMBER 2013

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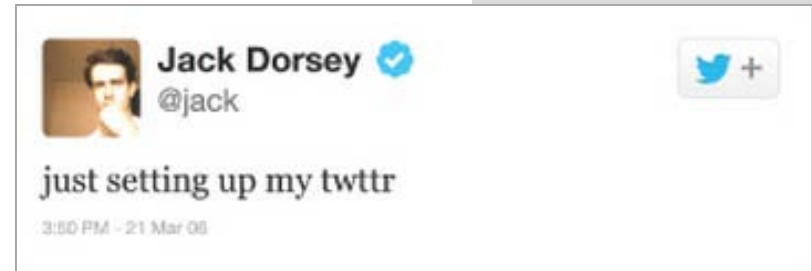
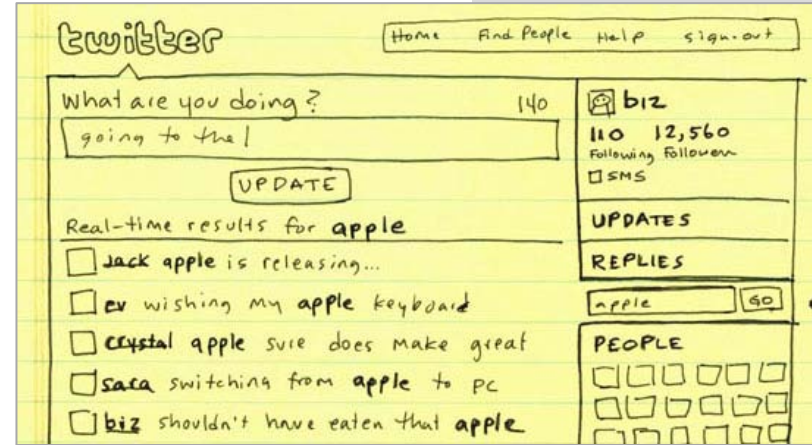
# TWITTER OVERVIEW

# TWITTER HISTORY



## A BRIEF INTRODUCTION

- Twitter was launched in 2006
- The original product was an SMS platform for users to “share what you’re doing”
- The platform has since evolved to a global platform for “content creation, distribution, & discovery”



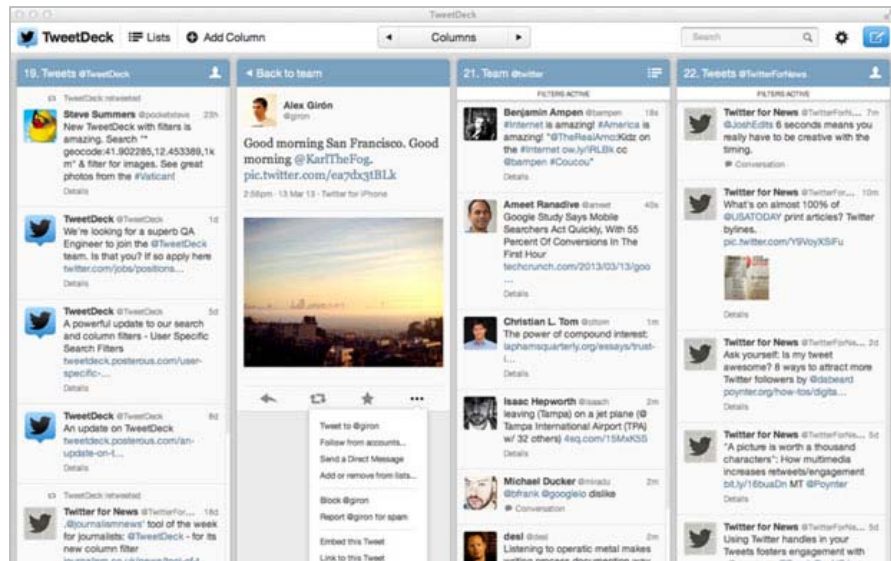
# TWITTER TODAY



- 9<sup>th</sup> ranked site in terms of traffic in the US, 10<sup>th</sup> globally
- 3<sup>rd</sup> largest social media site (behind Facebook & Google +)
- 230 million Monthly Active Users (MAUs):
- 100 million Daily Active Users (MAUs)
- 500 million tweets generated daily
- 48 billion online impressions of tweets on external sites
- Over 6 million website have embedded twitter on their site
- 45% of Super bowl ads used a hash tag (#)
- Twitter added 2,100 of its 2,300 employees since 2010

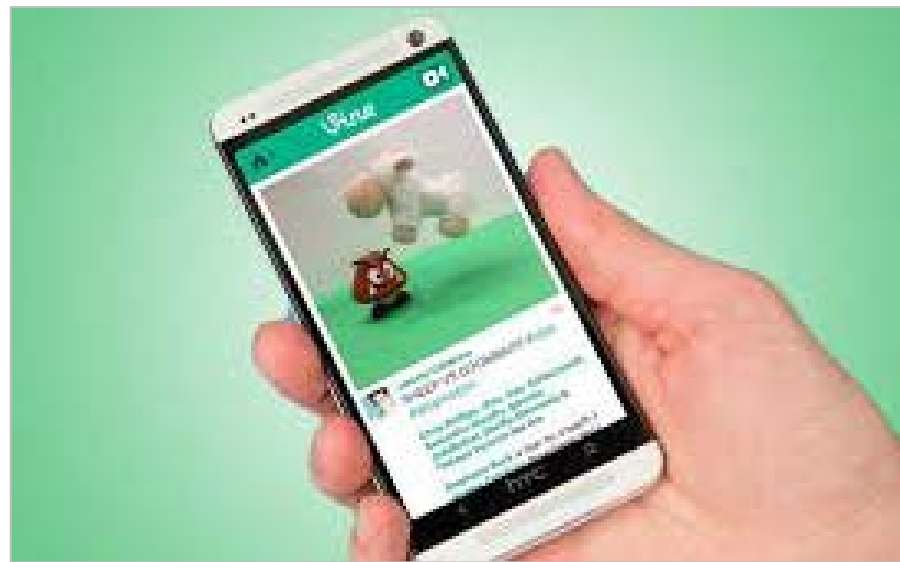


# KEY PRODUCTS



## TWITTER/TWEETDECK

Flagship Product: Social Media Platform for consuming and distributing information spanning multiple topics



## VINE

Similar to Twitter, with the major distinction being short-video sharing

# STAKEHOLDERS



Users

## USERS

Implicitly refers to those that consume content and/or converse with other users, but includes all members on Twitter (including Platform Partners & Advertisers)



Platform partners

## PLATFORM PARTNERS

These are primarily content creators distributors looking to reach a broader audience, and drive interest/traffic to their own websites/media outlets



Advertisers

## ADVERTISERS

Twitter's primary source of revenue. Includes Platform partners looking to gain followers/drive traffic, and companies looking to promote their products/services



# USER STATISTICS

## USER PROFILE

- 232 million Monthly Active Users (MAUs)
- Over 40% of Users access daily
- 53 million US MAUs (~22% US penetration)
- 179 million Int'l MAUs (~17% addressable penetration)
- 76% of user access Twitter through a mobile device
- 55% of users tweet, the remainder consume content



Users

MAU Internet Penetration levels remain relatively low

Twitter users are mostly international

Most access Twitter with Mobile devices

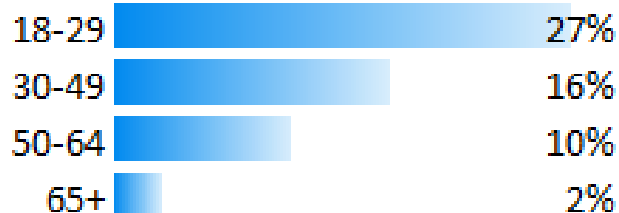
# USER DEMOGRAPHIC

## PENETRATION LEVELS FAIRLY BALANCED

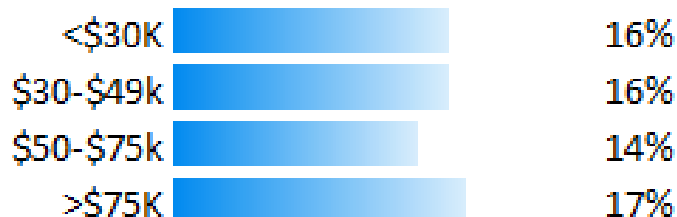
### SEX



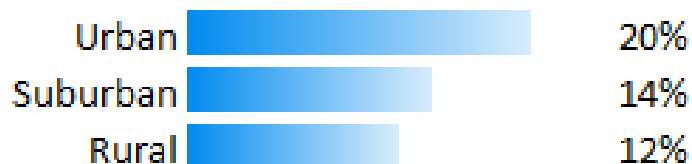
### AGE



### INCOME



### SETTING



Users

The major demographic divergence is within age cohorts

SOURCE: PEW  
RESEARCH

# PLATFORM PARTNERS

## ESTABLISHED AND EMERGING ENTITIES



Platform partners

Twitter offers established entities with a medium to expand reach

Also provides “emerging” entities with medium for outreach

# ADVERTISING PRODUCTS

## PROMOTED TWEETS, ACCOUNTS, & TRENDS



Advertisers



Twitter generates over 91% of its revenues from advertising

71% of it ad revenue comes from mobile

# ADVERTISING PRODUCTS

## SOPHISTICATED TARGETING



Keywords



Interests



TV ads



Device



Followers



Look-a-likes



Search



Location



Gender

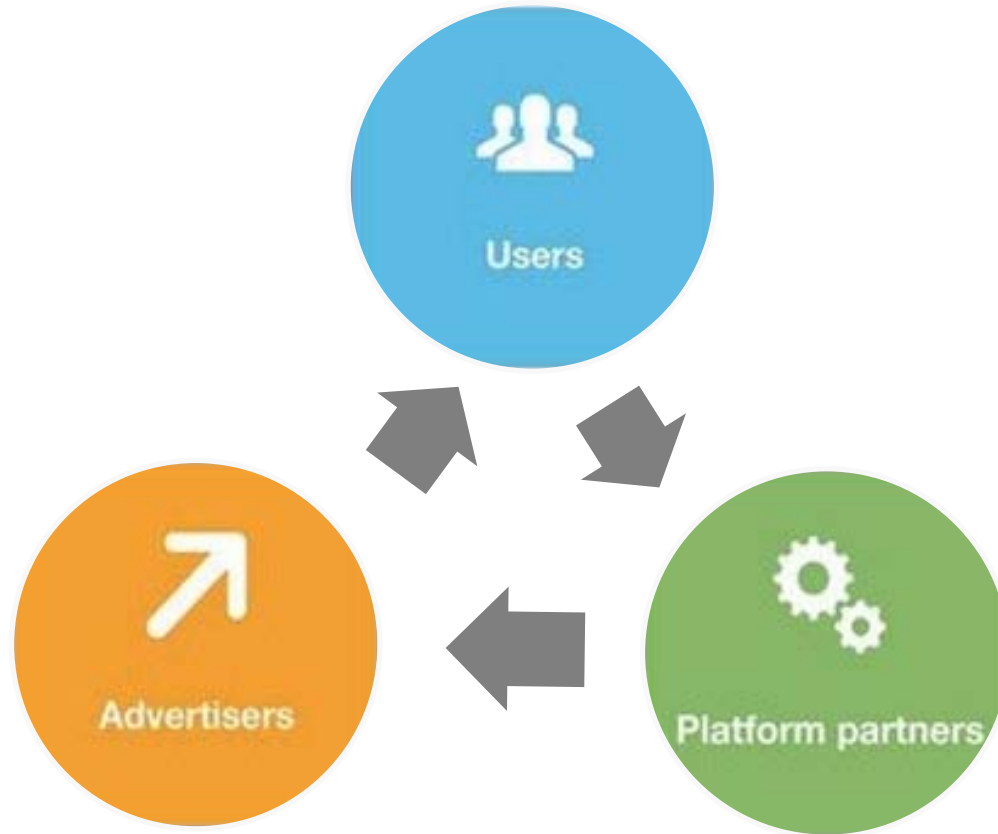


Advertisers

Twitter produces **“Interest Graphs”** based on user activity

This allows for more effective ad targeting

# BUSINESS MODEL



## VIRTUOUS CYCLE

Users, Platform Partners, and Advertisers attract each other to Twitter. A growing user base attracts both Platform Partners and Advertisers looking for broader reach, while publicity from each drives users to Twitter.



# FUNDAMENTALS & THESIS



1

## **CURRENT MODEL HAS LIMITED RUNWAY**

TWTR's business model currently has limited avenues for monetizing its platform, which makes the company heavily reliant on user growth

2

## **THE MODEL CAN BE FIXED/EXPANDED**

TWTR can implement rather simple measures to monetize the platform more effectively, and potentially enhance user growth.

3

## **IT'S UP TO MANAGEMENT**

TWTR's growth to date has been driven by focusing on the user experience, which will not be enough going forward. Priority needs to fix and monetize the model.



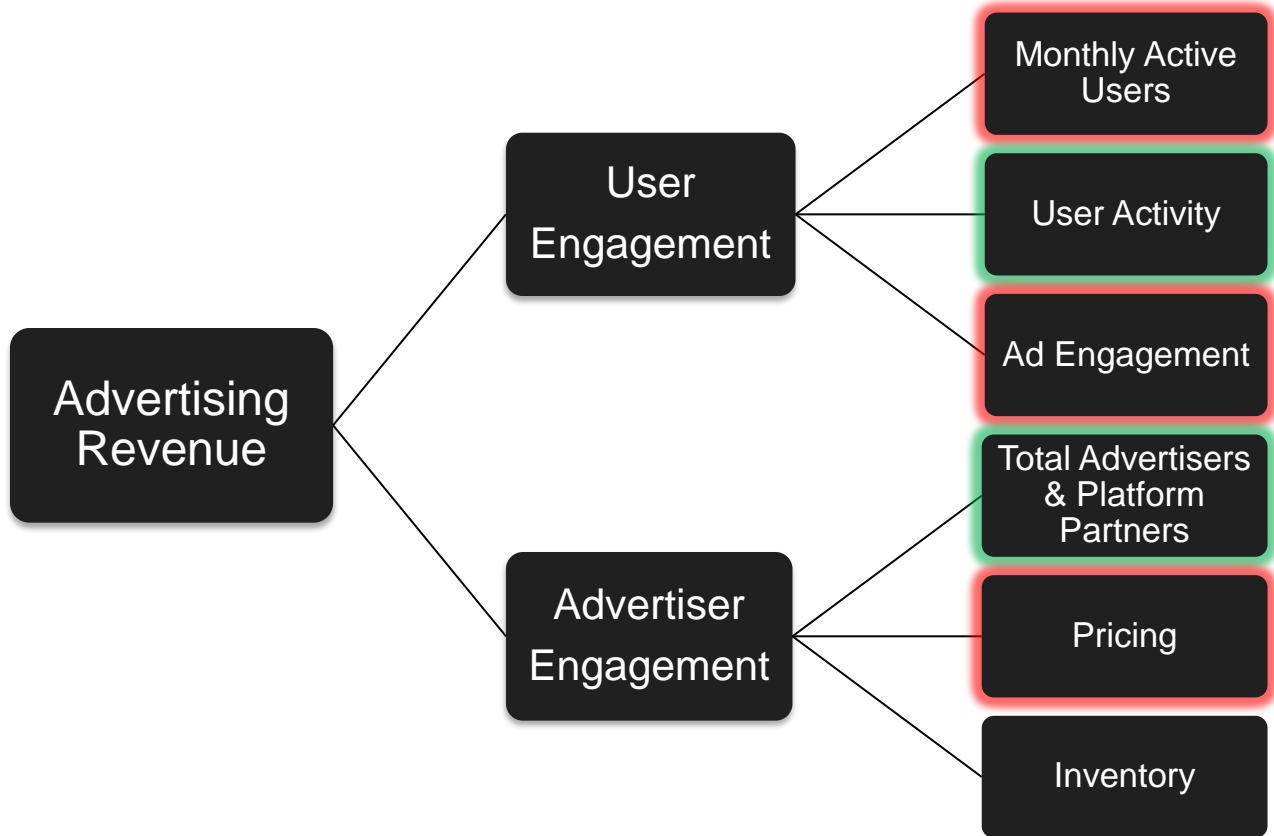


# **BUSINESS MODEL ANALYSIS**

# ADVERTISING REVENUE DRIVERS



## CURRENT MODEL: TAILWINDS & HEADWINDS

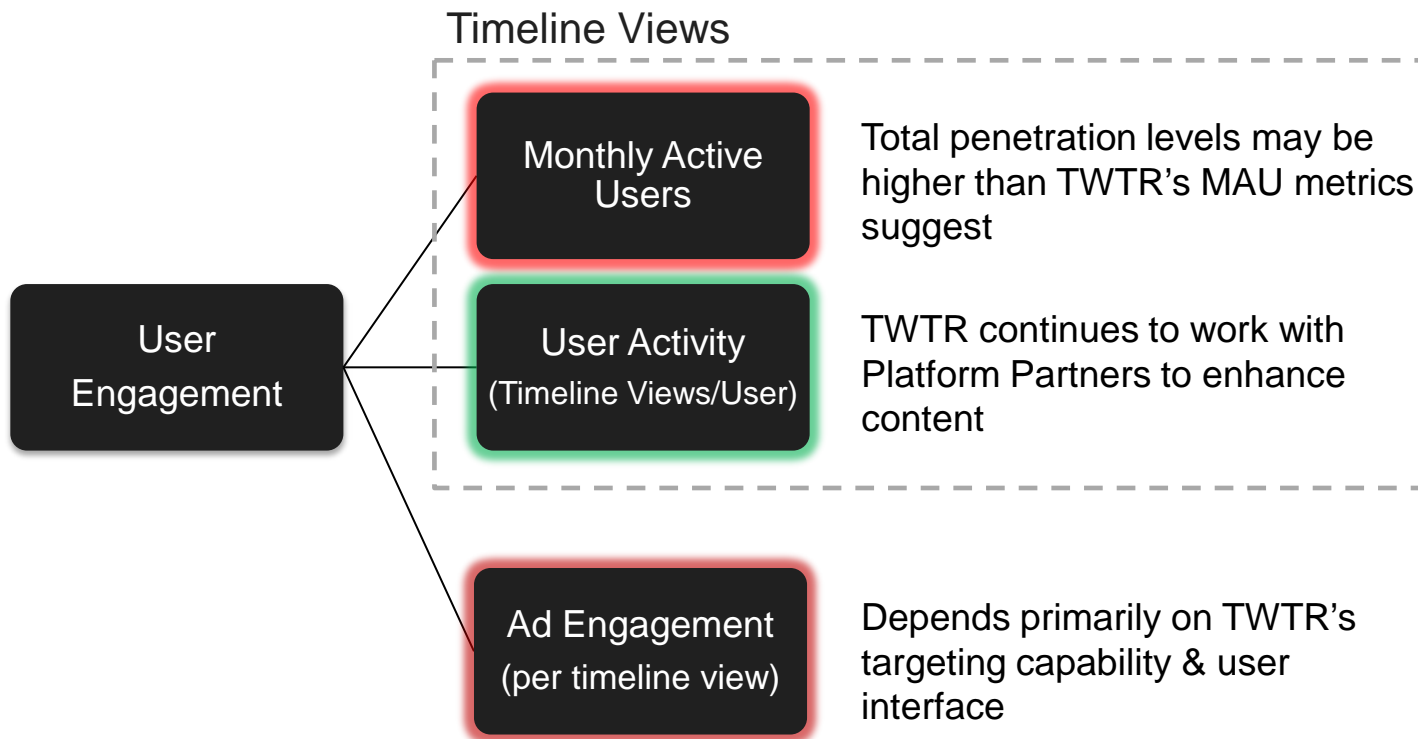


Based on the company's stated growth objectives, this is a snapshot of how we see the prospects for each of its revenue drivers

# AD REVENUE DRIVERS: USERS



## USER ENGAGEMENT: **HEADWIND**/TAILWINDS



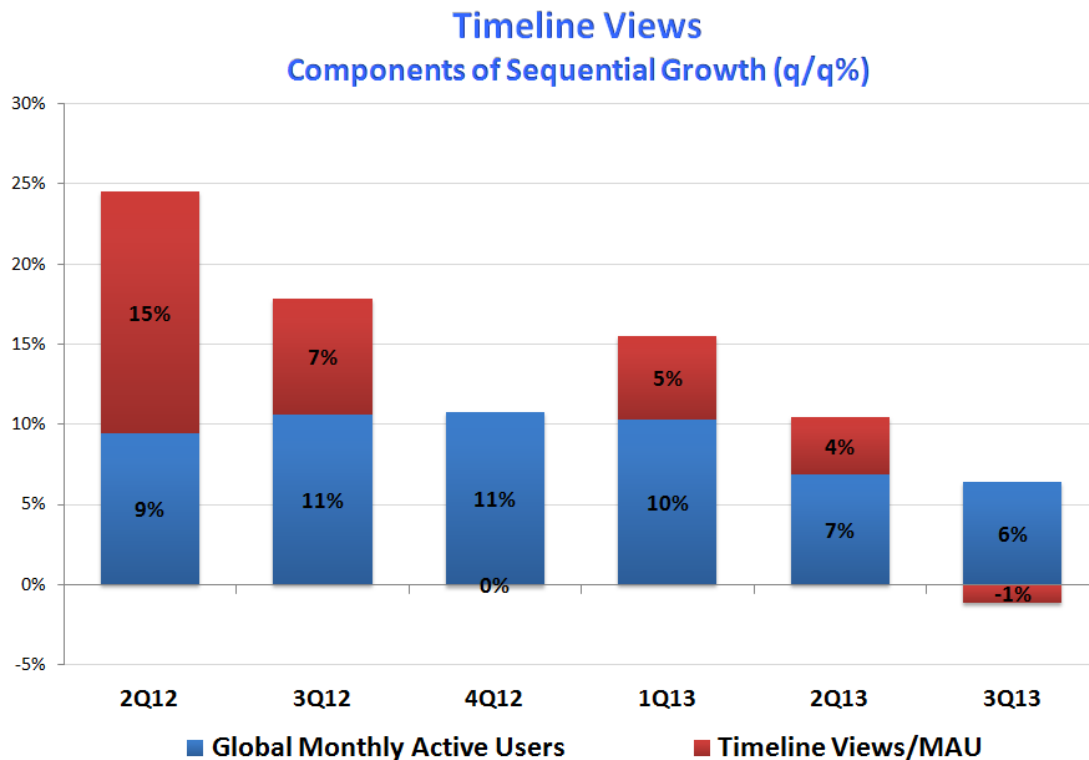
Twitter gets paid when the user engages with the ad

That is a function of total timeline views & the rate of ad engagements

# TIMELINE VIEWS DRIVERS

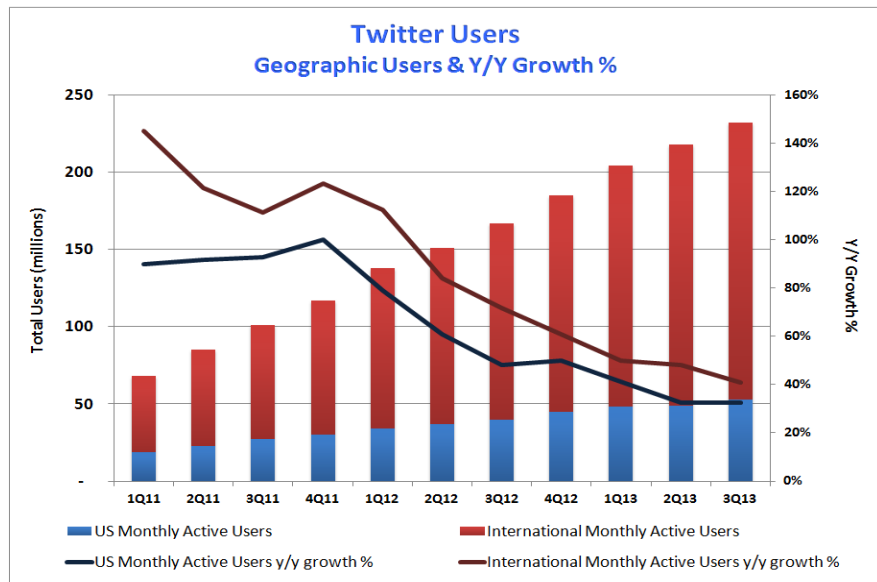


## USER GROWTH HAS MATTERED MOST



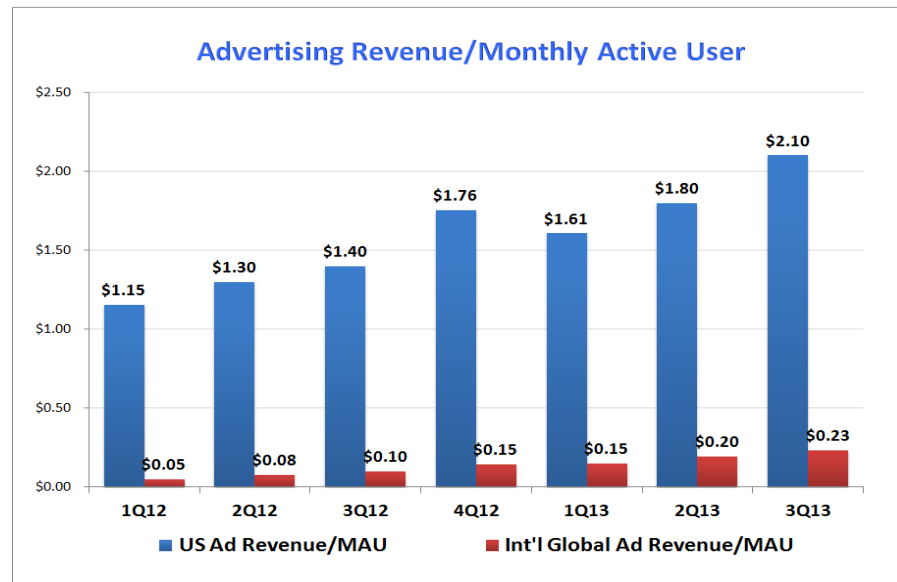
In the last 5 quarters, users have been the primary driver of growth in timeline views

# U.S. DRIVES REVENUES



## USER GROWTH FAVORS INT'L

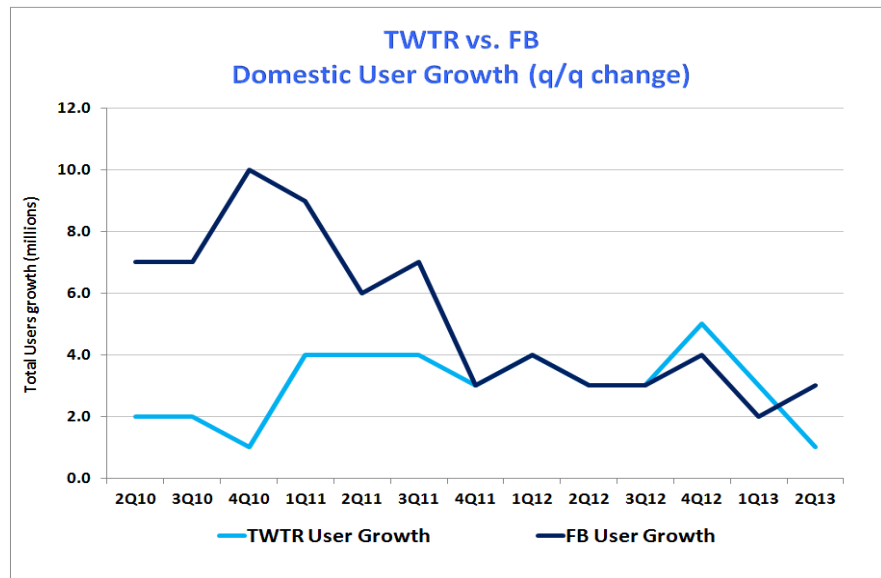
Despite the considerably higher user base, international growth continues to outpace the US, which is only an issue because ...



## MONETIZATION FAVORS THE US

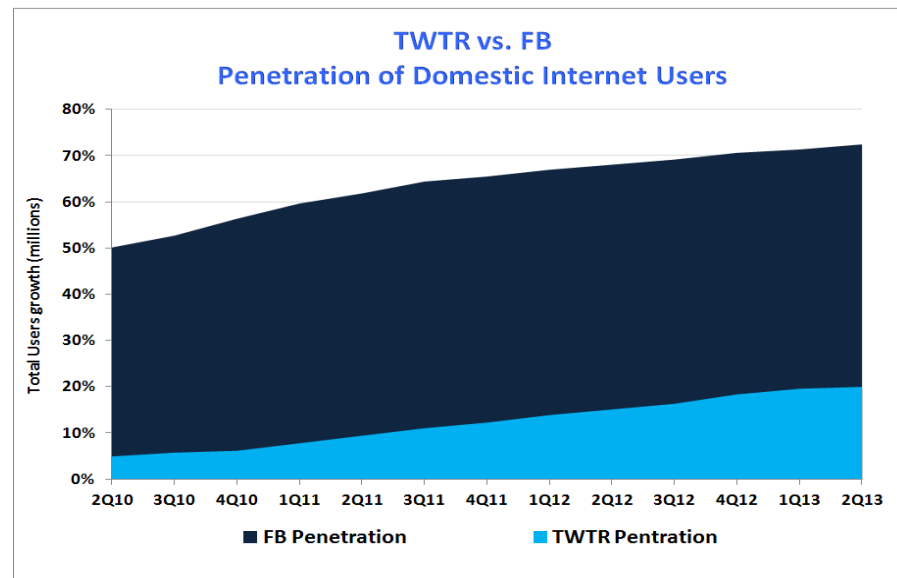
By a wide margin. With the US representing over 70% of revenues. US User Growth will have a disproportionate impact on the TWTR's financials

# FB STILL OUTGROWING TWTR



## FB GAINING MORE USERS

In terms of absolute member gains, FB has been gaining more members than TWTR on average over the past 3 years



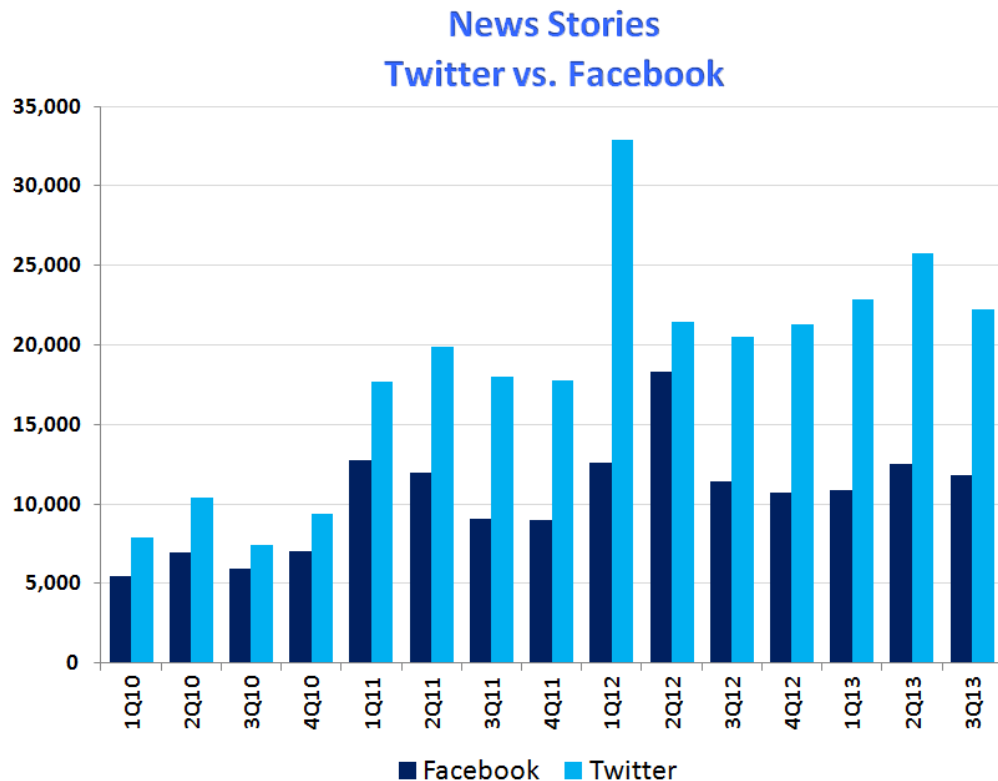
## FB PENETRATION MUCH HIGHER

TWTR is ~22% penetrated in US and currently growing users in the 30% range on a y/y basis, which is comparable to FB's growth when it was at ~55% penetration

# WHILE TWTR PUBLICITY IS HIGHER



## TWTR HAS BEEN GAINING MORE PUBLICITY



TWTR has received more publicity

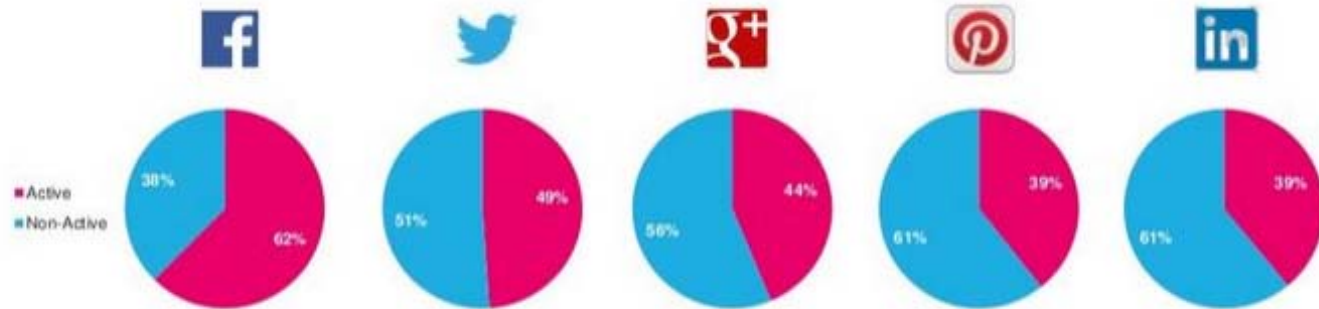
FB has been the net winner in membership growth

# TWTR U.S. USERS: LIMITED RUNWAY?

## ACTIVE USERS $\neq$ TOTAL USERS

### FACEBOOK MAINTAINS THE HIGHEST ENGAGEMENT RATE AMONG ACCOUNT OWNERS

Active Usage Measurement - % of Account Owners that are Active on the Platform in the past month globally, Q2 2013



The engagement rate of active users to account holders decreased for all top 5 social networks compared with Q1 2013. Despite that, Facebook still remains the leader in engaging its audience with 62% of active account holders. The gap between engagement of Google+ and Twitter has widened over the past quarter with microblog's account holders being 10% more likely to use it actively than those who signed up to Google+. The two main emerging platforms proved to be equally engaging in Q2 2013.

Twitter's U.S. penetration in terms of monthly active users is relatively low at ~20%, but total users and penetrations could be much higher, suggesting a shorter runway for membership growth

Source: GlobalWebIndex, Questions: On which of the following social platforms do you have an account? & On which of the following services have you used or contributed to in the past month?  
Base: % of internet users globally aged 16 to 65



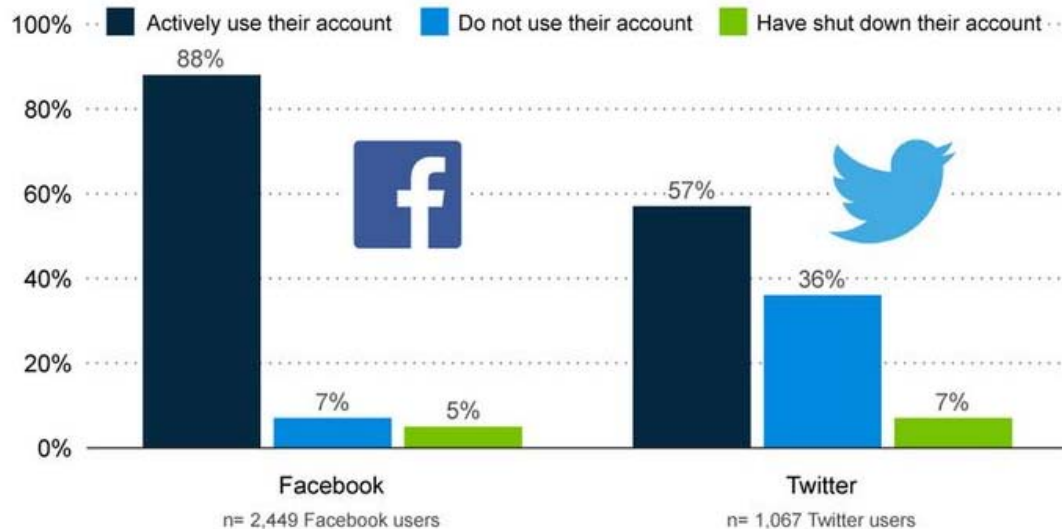


# TWTR U.S. USERS: LIMITED RUNWAY?

## ACTIVE USERS $\neq$ TOTAL USERS

### Twitter Has a Quitter Problem

% of Facebook and Twitter members who do or do not use their respective accounts (as of October 2013)

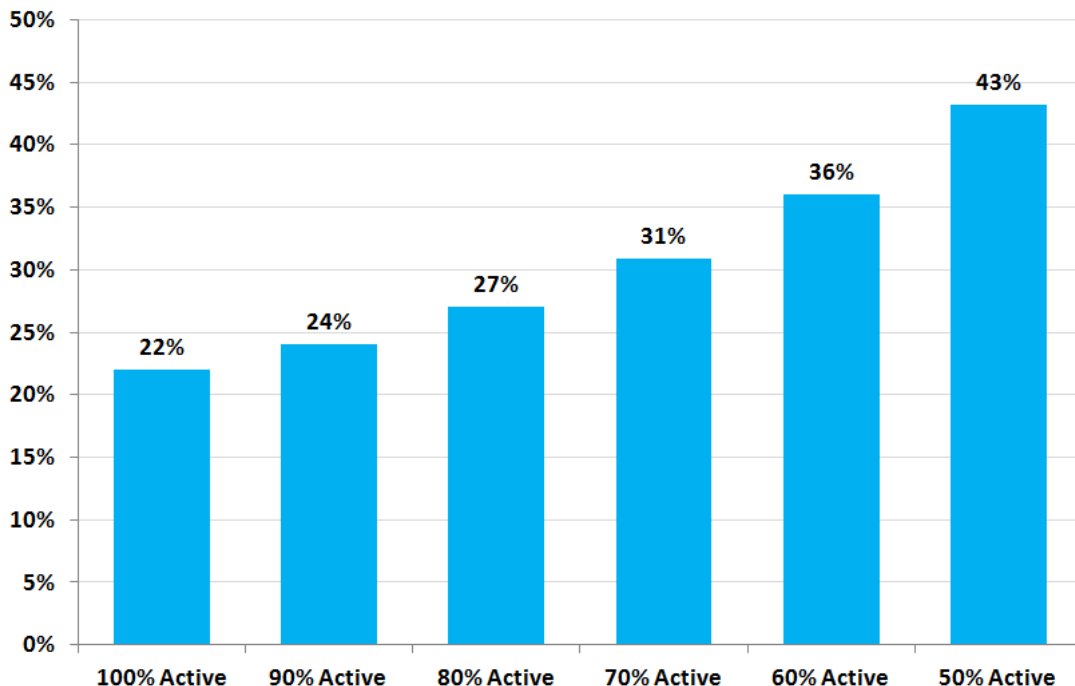


Another perspective suggesting Total User Penetration is higher than the reported figures for Monthly Active Users suggest

# TWTR U.S. USERS: LIMITED RUNWAY?

## TOTAL US USER PENETRATION IS HIGHER

Twitter Total Users: US Penetration Levels  
Active Users/Total Users

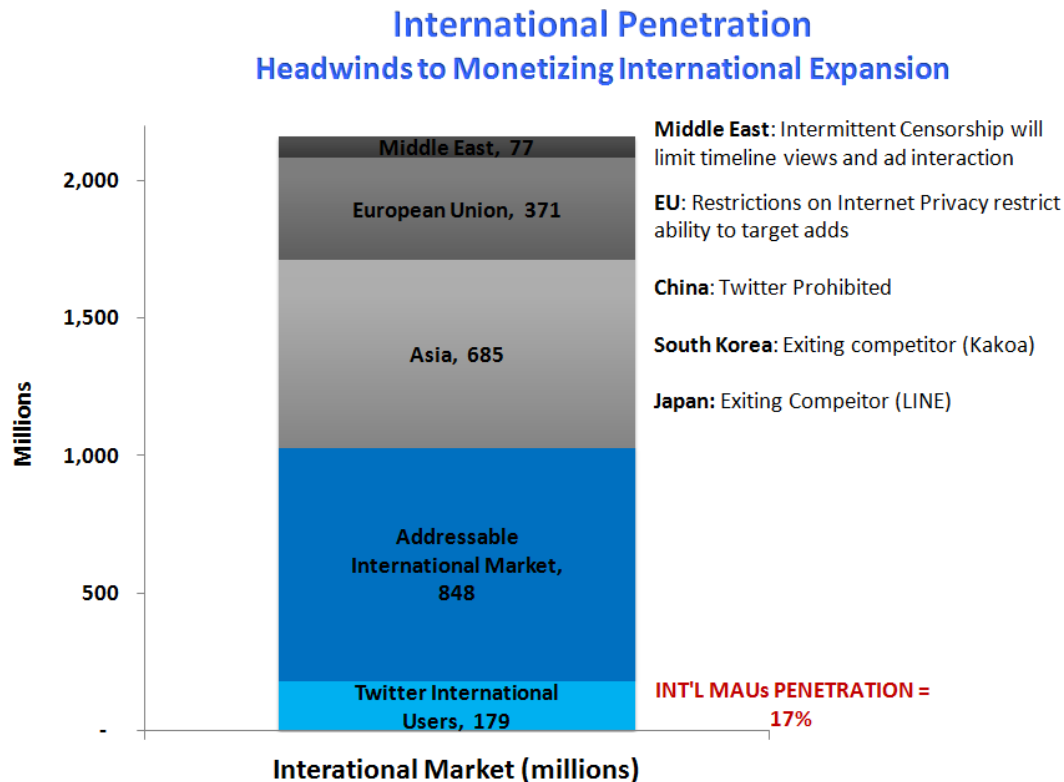


If 100% of TWTR's total users are active, then total U.S. penetration levels are only 22%.

But in reality, penetration levels are likely higher.

# TWTR INT'L USERS: MONETIZATION?

## HEADWINDS TO INT'L EXPANSION?

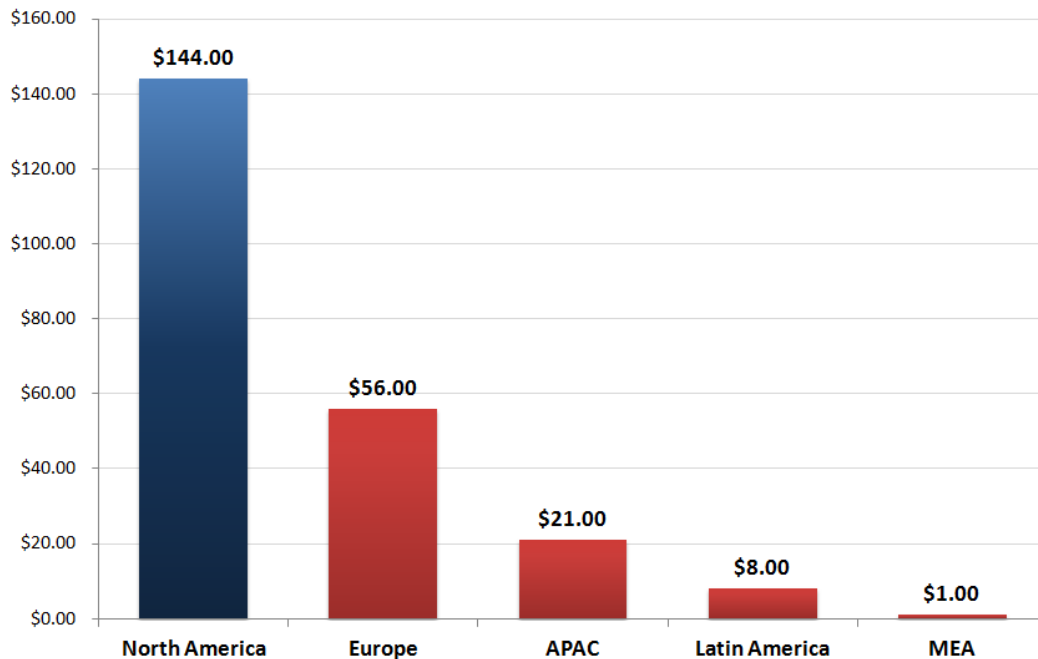


There are headwinds to user growth and monetization in the international landscape. TWTR's international ARPU is already lower than the US. We expect incremental int'l user growth will be even less accretive

# TWTR INT'L USERS: MONETIZATION?

## INT'L MEMBERS WORTH MUCH LESS

Per-Capita Digital Marketing Spend by Region

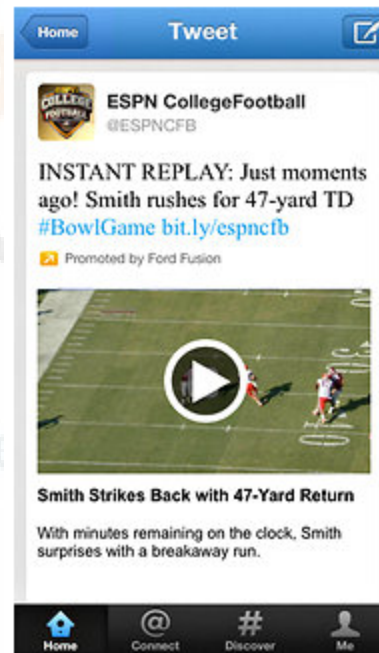


Source: eMarketer.com, comScoreDataMine.com

~40% of Digital Ad spend flows through North America.

International membership growth will come at significantly lower yields than the US.

# USER ACTIVITY



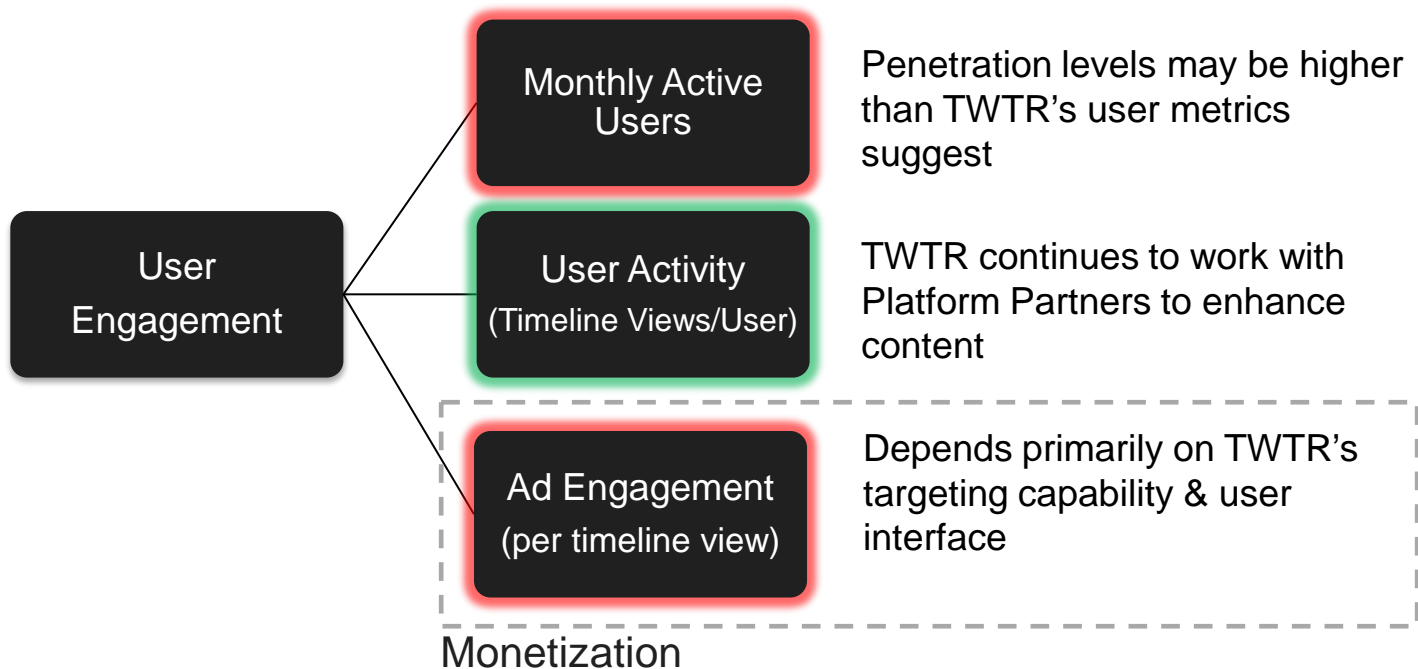
## TWTR PARTNERSHIPS ENHANCE CONTENT

TWTR has an active focus on enhancing content by expanding relationships with platform partners. A positive for user activity, but not sure if enough to drive meaningful growth in timeline views

# AD REVENUE DRIVERS



## AD ENGAGEMENT: **HEADWIND**/TAILWINDS



Twitter primarily gets paid when the user engages with the ad

That is a function of total timeline views & the rate of ad engagements

# AD ENGAGEMENT: PRODUCTS



## PROMOTED TWEETS, ACCOUNTS, & TRENDS

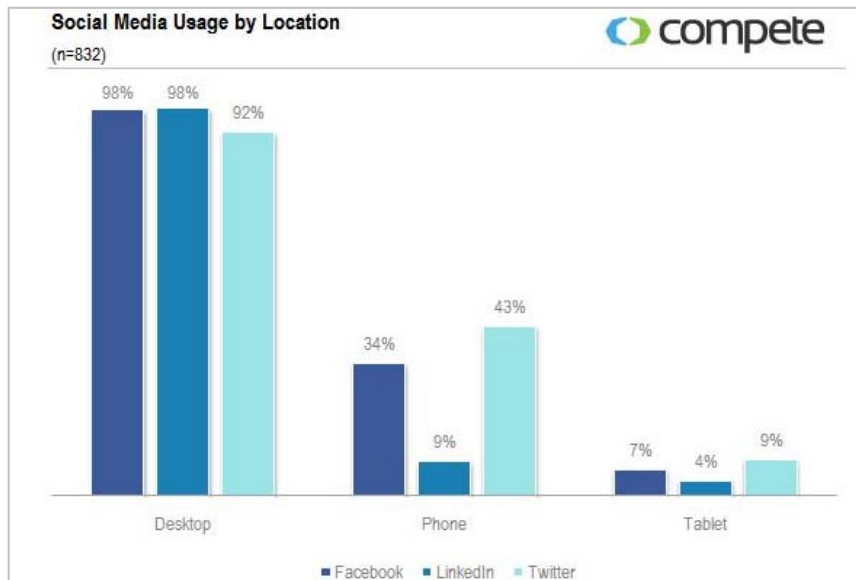
*"We generate substantially all of our advertising revenue through the sale of our three Promoted Products: Promoted Tweets, Promoted Accounts and Promoted Trends" (TWTR S-1)*



76% of users access Twitter using a mobile device

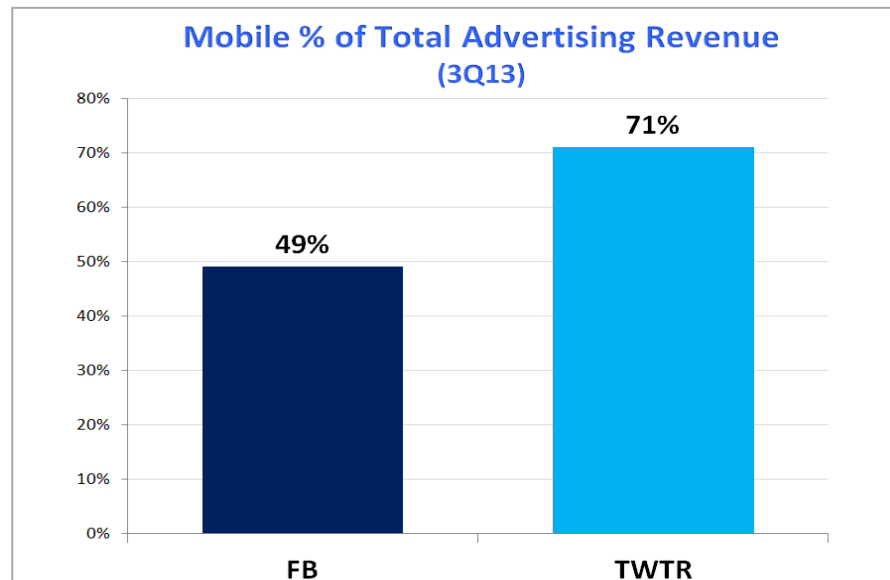
Mobile drives 71% of advertising revenue

# TWTR VS. FB USAGE & REVENUES



## USAGE PATTERNS ARE SIMILIAR

TWTR slightly lags FB in desktop usage, while TWTR is marginally higher in mobile



## BUT TWTR RELIANT ON MOBILE

Despite similar usage patterns between mobile & desktop, TWTR has more difficulty monetizing desktop platform

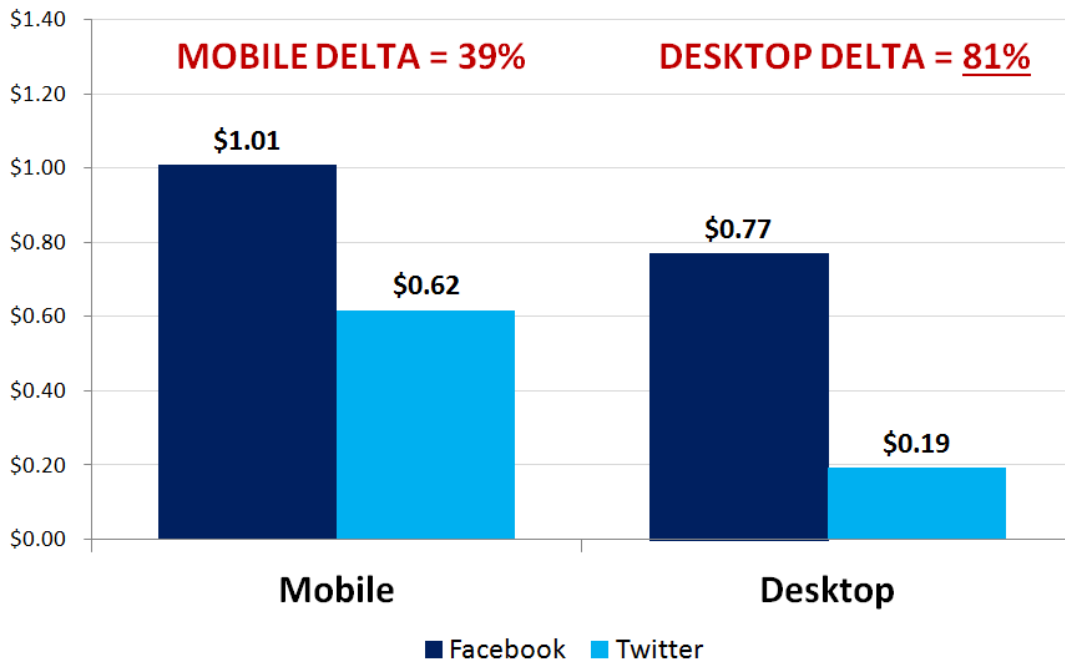


# TWTR LACKING IN MONETIZATION



## MONETIZING THE USER (ARPU)

TWTR vs. FB  
ARPU by Device



FB leads in both metrics, which partially due to TWTR's ad structure and a higher int'l user %.

However, the wide delta between Desktop ARPU suggests TWTR barely monetizes its desktop users

# AD ENGAGEMENT: PLATFORM ISSUES

## PLATFORM NOT BUILT FOR MONETIZATION

1 Majority of ad revenue tied to user engagement

2 Twitter's Desktop Interface limits chances for the user to engage

3 Growing TweetDeck Penetration exasperates this issue

Even if advertiser demand and ad inventory were to increase, TWTR needs engagement to drive revenues

# TWITTER DESKTOP USER INTERFACE

## ADS ARE STATIC AND NOT ALWAYS IN VIEW

The screenshot displays the Twitter desktop interface. On the left sidebar, the 'Who to follow' section contains three entries: 'Fidelity Investments @Fidelity' (with a 'Follow' button and a 'Promoted' label), 'Blair Seideman @bcs92usa' (with a 'Follow' button), and 'CIO.com @CIOOnline' (with a 'Follow' button). Below this, the 'Trends' section shows a list of hashtags, with 'DRose' highlighted as a 'Promoted' item. The main feed on the right shows a series of tweets. The first tweet, from 'MSG @TheGarden', is highlighted with an orange border and contains a promotional message for a 50% discount on tickets for the Zelda Symphony. Subsequent tweets are from 'Slate @Slate', 'The Atlantic @TheAtlantic', 'Business Insider @businessinsider', 'Gawker @Gawker', 'WSJ China News @WSJchina', and 'The Health Care Blog @THCBstaff'. The 'Promoted' label is visible on the first tweet in the feed.

Promoted ads do not change during use, and with one scroll, each of the promoted products are out of view; limiting chances for engagement.

FB freezes the advertising pane and refreshes the ads within it.

# TWEETDECK USER INTERFACE



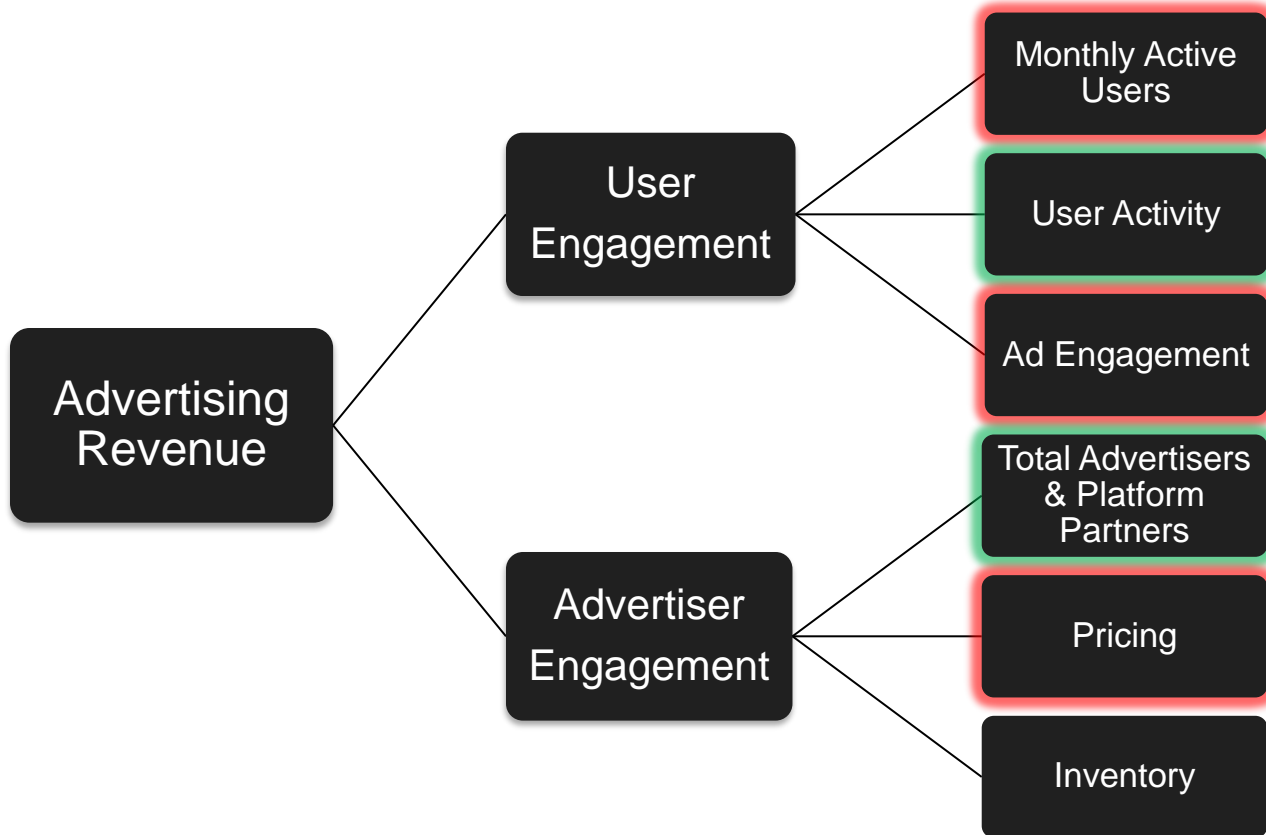
## INVERSE RELATIONSHIP BETWEEN USAGE AND AD PRODUCTS

TweetDeck allows users to organize followed accounts into streaming panes. The issue is that the more accounts a user follows, the quicker the stream. So Promoted Tweets may not be visible for long.

# ADVERTISING REVENUE DRIVERS



## CURRENT MODEL: TAILWINDS & HEADWINDS

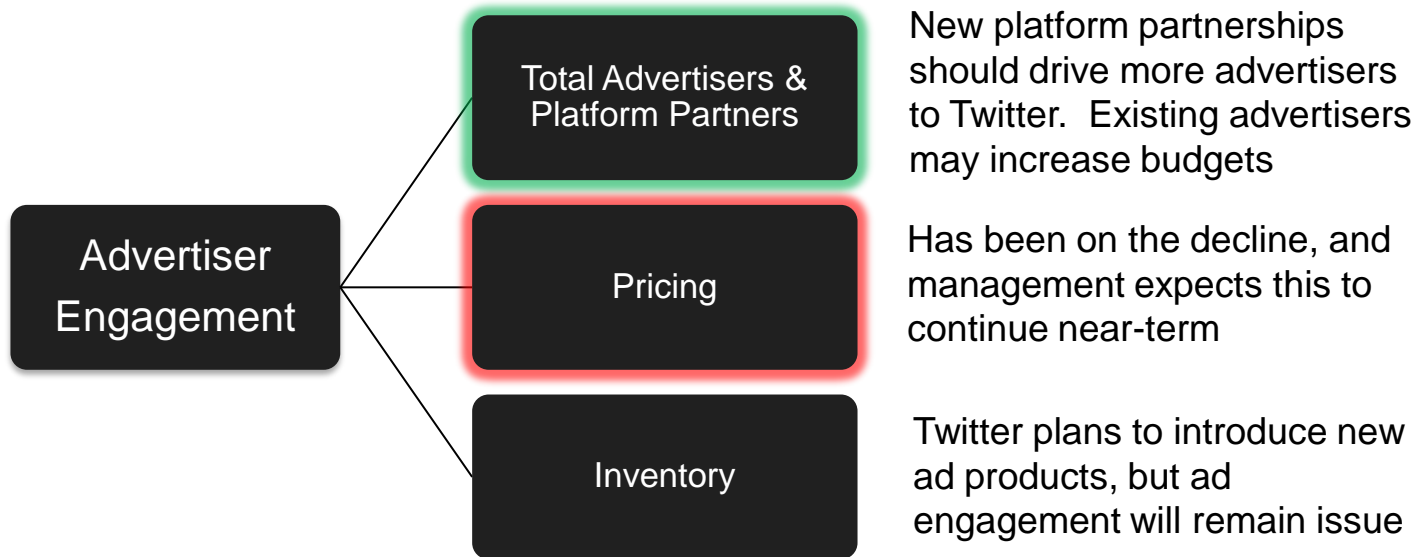


Based on the company's stated growth objectives, this is a snapshot of how we see the prospects for each of its revenue drivers

# REVENUE MODEL: ADVERTISING



## ADVERTISERS: **HEADWIND**/TAILWINDS



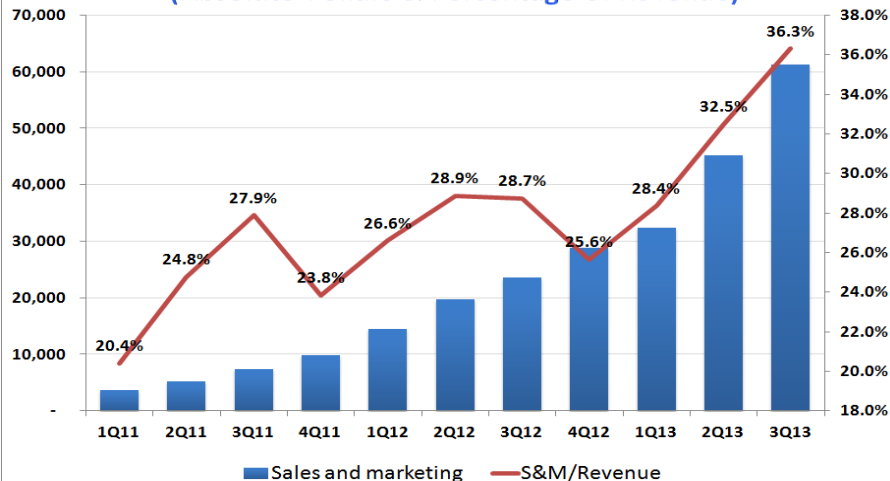
Red Borders  
are where we  
see emerging  
headwinds to  
TWTR's  
Growth  
Trajectory;

Green the  
Opposite

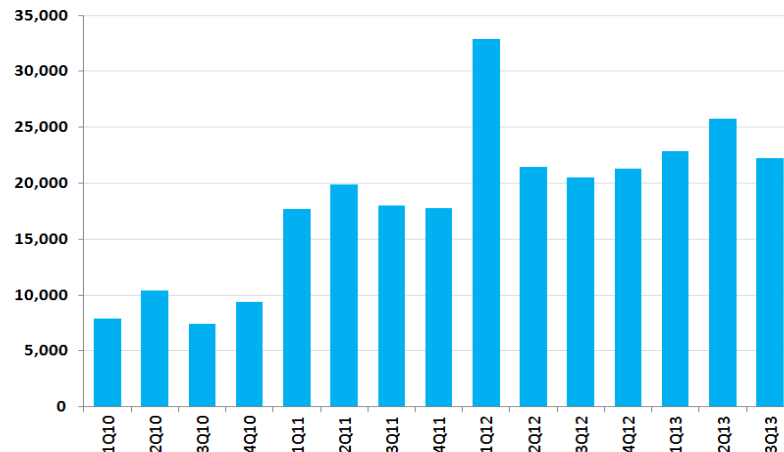
# ADVERTISING DEMAND DRIVERS



**TWTR Sales & Marketing Expenses**  
(Absolute Dollars & Percentage of Revenue)



**News Stories**  
**Twitter**



## TWTR INVESTING IN SALESFORCE

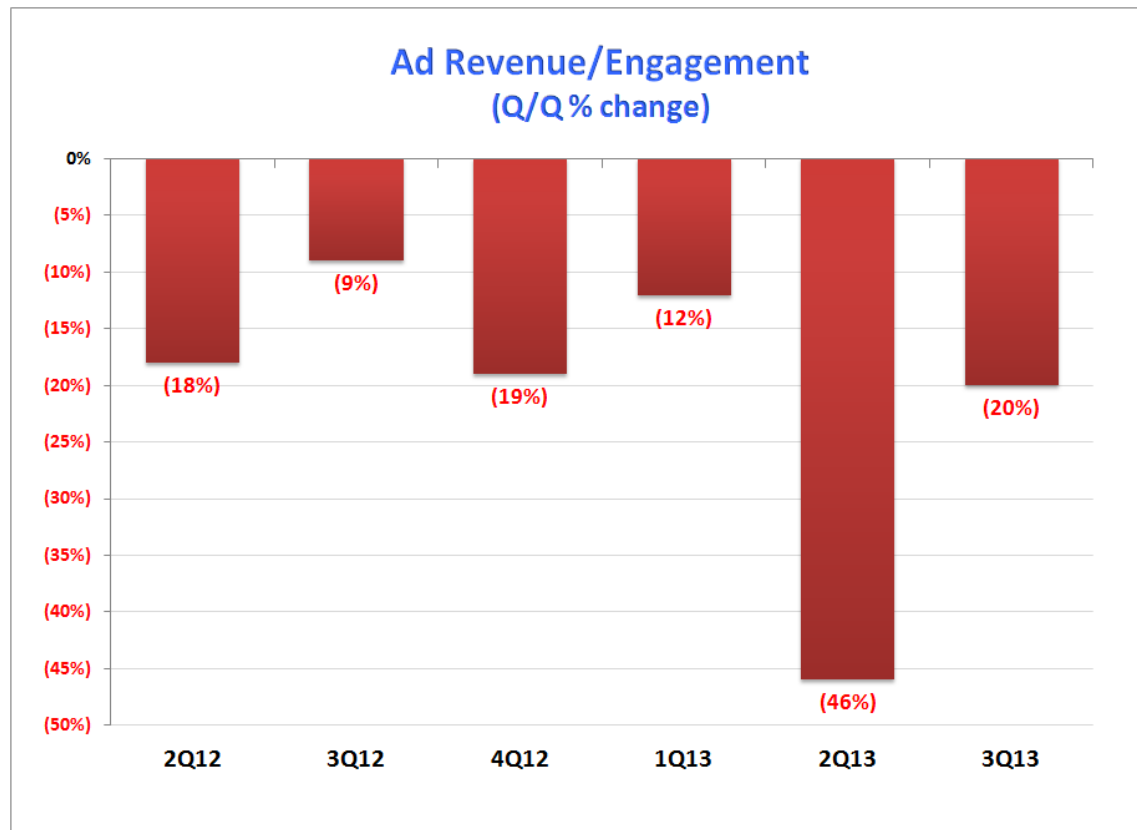
Twitter has been investing in Sales & Marketing, which should help with outreach and penetration into the digital market

## PUBLICITY SHOULD ALSO HELP

As a stand-alone driver, general publicity should help drive advertiser interest

# PRICING VS. INVENTORY

RISING INVENTORY = DECLINING PRICES



TWTR plans to add new ad products, which will increase supply, and pressure so pricing further



A map of the African continent is centered on the page, composed of a mosaic of various social media icons. The icons are in shades of blue, green, and purple, set against a light background. The map is surrounded by a dense field of smaller, faded social media icons, creating a textured, digital effect.

# **FIXING THE BUSINESS MODEL**

# TWTR'S STATED GROWTH STRATEGY



Users

## USERS

- Geographic Expansion
- Mobile Applications
- Product Development



Platform partners

## PLATFORM PARTNERS

- Integrate More Content Types
- Partner With Traditional Media



Advertisers

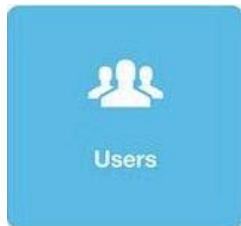
## ADVERTISERS

- Improve Targeting Capability
- Geographic Expansion
- New Ad Formats



## PRIORITIZE PLATFORM MONETIZATION

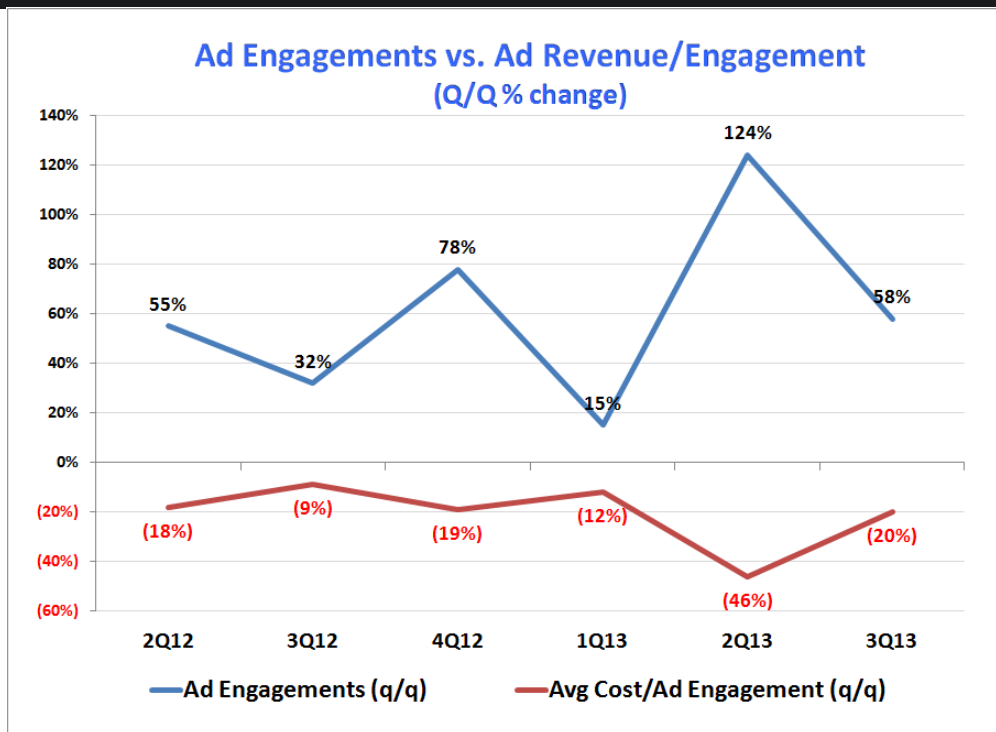
Simple fixes to the user interface will make a big difference in ad engagement. Closing the gap between TWTR and FB ARPU is a significant opportunity



## PRIORITIZE U.S. USER GROWTH

If penetration of Monthly Active User's is only ~22%, then TWTR still has an opportunity for growth and/or to reengage a far more lucrative US user

# SUPPLY DRIVES AD ENGAGEMENT?



## SUPPLY MAY MATTER MORE THAN CONTENT

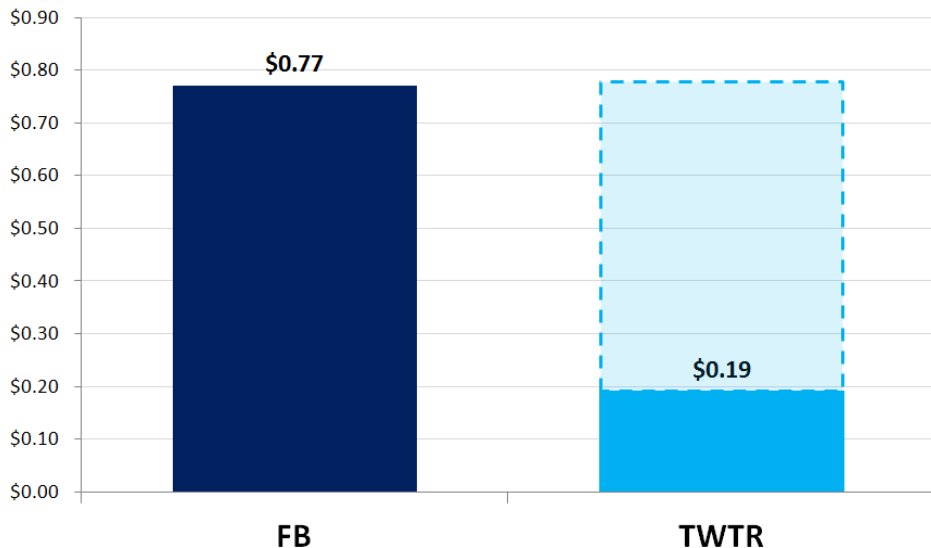
TWTR's ad engagements have risen as cost has declined; suggesting rising ad inventory has been the main lever of ad engagements. **Addressing its platform issues (hence supply) could have the same effect.**

# PLATFORM MONETIZATION



## Desktop ARPU (3Q13)

DELTA = 81%



## EASY FIXES

1. Freeze the Advertising Pane
2. Refresh the Ads within the Pane
3. Calibrate the TweetDeck Feed

## ADDITIONAL OPPORTUNITIES

1. Increase Promoted Tweet Placements
2. More Ad Products on TweetDeck

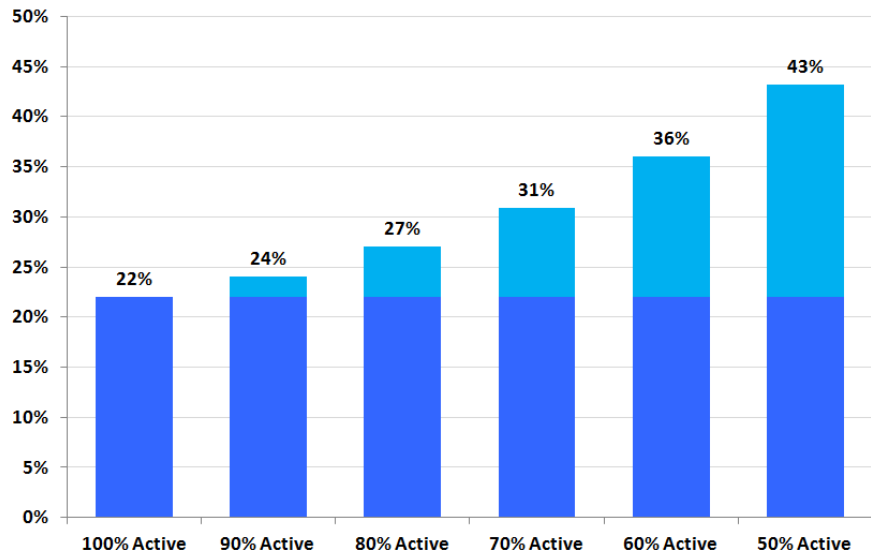
## TWTR'S MOST TANGIBLE GROWTH OPPORTUNITY

The wide delta between TWTR's and FB's Desktop ARPU is also its most immediate growth driver if it addresses its User Interface limitations

# U.S. USER GROWTH



Twitter Total Users: US Penetration Levels  
Active Users/Total Users



## OUTREACH

1. Direct Marketing Campaign
2. Increased Partnership (e.g. Amplify)
3. Inactive User Targeting

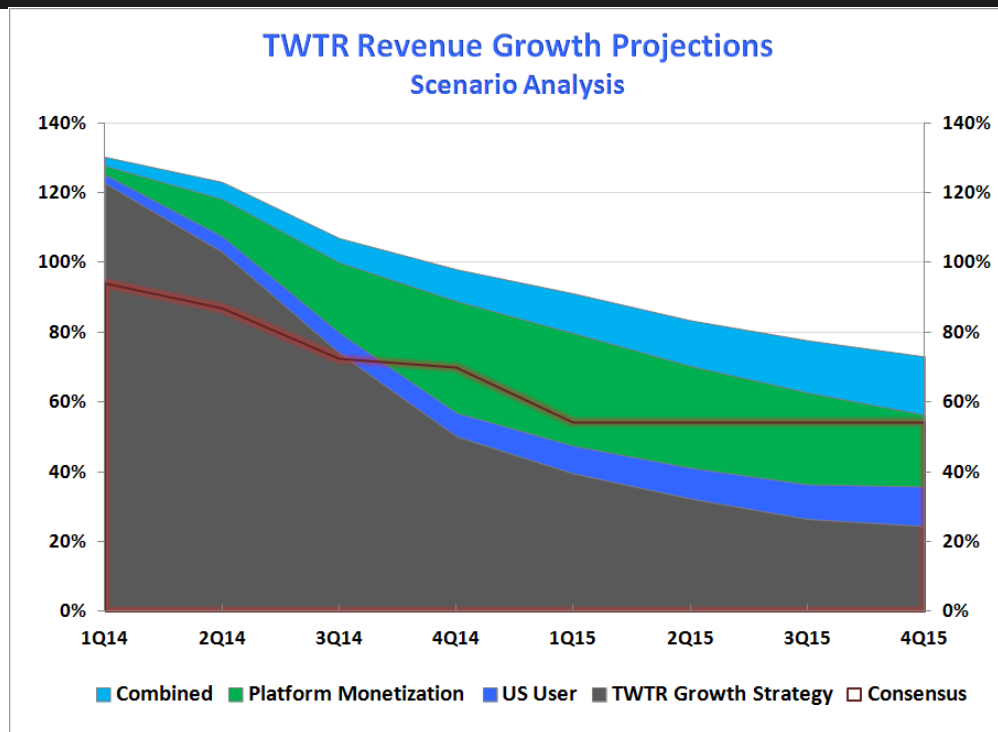
## FUNCTIONALITY

1. User Tutorials
2. Improved Interface Functionality

## TWTR NEEDS TO TAKE A MORE AGGRESSIVE APPROACH TO US GROWTH

Monthly Active User penetration is only 22%, so there remains a opportunity for growth from both reengaging inactive users and growing organic membership.

# REVENUES GROWTH SCENARIOS



## TWTR'S CURRENT GROWTH STRATEGY ISN'T ENOUGH, BUT HAS OPTIONS

While we are above consensus in 1H14, we expect growth will slow as the tailwind from prior inventory increases wanes in 2H14. But Platform Monetization and US User Growth initiatives could be major drivers



# VALUATION



# BE MINDFUL OF THE SHARE COUNT

## DILUTION DOWN THE ROAD

TWTR SHARE COUNT ANALYSIS	
	<u>Shares</u>
Current Shares Outstanding (pre-IPO)	474,696,816
<u>Initial Public Offering</u>	<u>Shares</u>
Initial Public Offering	70,000,000
Contingent Initial Public Offering	10,500,000
<b>Total IPO</b>	<b>80,500,000</b>
<b>Shares Outstanding After IPO</b>	<b>544,696,816</b>
<u>Sources of Dilution</u>	<u>Shares</u>
Stock options (strike @ \$1.84)	42,708,824
RSUs outstanding as of 9/30/13	85,657,603
Warrants (strike @ \$0.34)	116,512
RSUs granted post 9/30/113	7,202,952
MoPub acquisition	14,415,887
<b>Total Dilution</b>	<b>150,101,778</b>
<b>Full Potential Diluted</b>	<b>694,798,594</b>
<b>Full Potential Diluted + Contingent</b>	<b>705,298,594</b>

TWTR has multiple sources of share dilution following the IPO

Floated Shares could increase by over 25%

# LOFTY IPO VALUATION?

## PREMIUM VALUATION WHEN FULLY DILUTED

IMPLIED TWTR VALUATION BASED ON IPO PRICE RANGE VS. FB & LNKD					
TWTR IPO Price		\$23.00	\$24.00	\$25.00	
METRICS	FB	LNKD	TWTR		
Market Cap*	120,329	26,622	15,980	16,675	17,370
P/S 2013	15.5x	17.6x	25.0x	26.0x	27.1x
P/S 2014	11.4x	12.4x	14.0x	14.6x	15.2x
P/S 2015	8.8x	9.1x	9.1x	9.5x	9.9x

\* Assumes total diluted shares of 695 million (prior slide)

FB Historical P/S Ranges			
	Min	Avg	Max
Year 0	6.7x	10.5x	17.4x
Year 1	5.3x	8.2x	13.0x
Year 2	4.1x	6.5x	9.9x

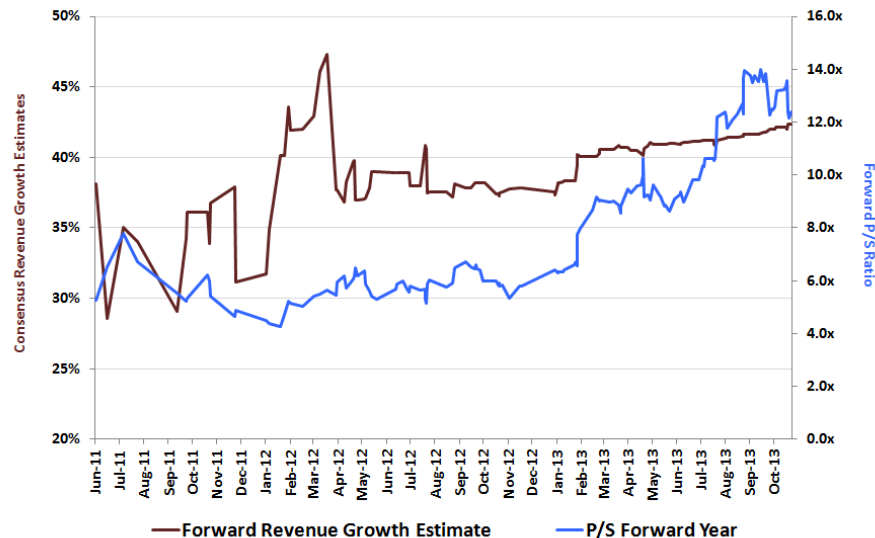
LNKD Historical P/S Ranges			
	Min	Avg	Max
Year 0	5.4x	7.9x	19.8x
Year 1	4.3x	6.7x	14.0x
Year 2	3.2x	5.8x	10.3x

After applying TWTR's fully diluted share count to its market cap, TWTR would trade above or near the historical peak P/S multiples of both FB & TWTR

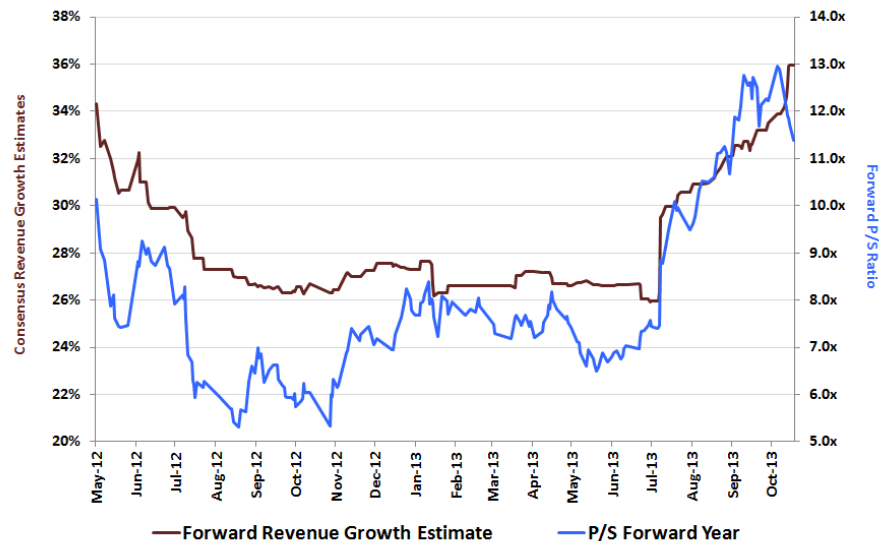
# ALL ABOUT EXPECTATIONS



LNKD: Forward P/S Ratio  
vs. Consensus Revenue Growth Estimates



FB: Forward P/S Ratio  
vs. Consensus Revenue Growth Estimates



## GROWTH EXPECTATIONS DRIVE MULTIPLE EXPANSION

We expect a similar dynamic for TWTR. Our concern here is that Consensus estimates 2015 estimates appear lofty, and a slowing growth expectation could pressure the shares

# WHAT TWTR'S WORTH...TODAY

## P/S MULTIPLE VS. REQUIRED RETURN

### TWTR VALUATION TABLE

Hedgeye 2015 Revenue Estimate (millions)	1,570
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TWTR 2014 Target Price Scenarios				
Forward P/S Multiple				
11.0x	12.0x	13.0x	14.0x	15.0x
\$24.90	\$27.10	\$29.40	\$31.60	\$33.90

		HEDGEYE CURRENT VALUATION				
		Forward P/S Multiple				
		11.0x	12.0x	13.0x	14.0x	15.0x
Required Return	10%	\$22.40	\$24.40	\$26.50	\$28.40	\$30.50
	15%	\$21.20	\$23.00	\$25.00	\$26.90	\$28.80
	20%	\$19.90	\$21.70	\$23.50	\$25.30	\$27.10
	25%	\$18.70	\$20.30	\$22.10	\$23.70	\$25.40
	30%	\$17.40	\$19.00	\$20.60	\$22.10	\$23.70
	35%	\$16.20	\$17.60	\$19.10	\$20.50	\$22.00

Given all the risks we've highlighted for TWTR, we have a hard time justifying an entry point above the top end of its IPO range



# CONCLUSION



## We're Not Buying the Hype

1 The company's stated growth objectives are not enough to compensate for larger headwinds across its business model

2 TWTR management can address some of these issues if it chooses to do so. Until then, we can't get behind the company

3 We can't justify an entry point on the stock above its stated IPO price. If the stock rips on the IPO, we will be evaluating the other side of the trade



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# HEDGEYE

## TWITTER IPO BLACKBOOK

TECHNOLOGY  
NOVEMBER 2013