

Tech, Media & Telecoms

Sector Review – February



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1. Sector Overview

- Expected changes on net neutrality have strongly affected telecoms, tech and cable companies and force for action.
- The valuation of transactions in the social media industry continues to be of huge interest in a month where markets seem to have recovered from the shocks in January. While Facebook rides the wave of optimism with their \$19 bn acquisition of WhatsApp, the slowed user growth of Twitter triggered a \$6 bn drop in market cap.
- Positive signals were received from the tech giants HP and Microsoft. Where the former showed improvements in last two quarterly earnings announcement, the latter sets sails towards cloud based business with its new CEO Satya Nadella – a cloud computing expert.
- Deal activity keeps momentum in cable industry with Comcast near to closing a \$45.2 bn bid for Time Warner Cable and Altice raising \$1.8 bn in its IPO. News of John Malone planning his succession at Discovery Communications and Liberty Global felt disturbing in that manner. Also, street beat on subscribers makes US pay TV Cablevision ever more attractive as a target.
- Further deals are in the pipeline according to media rumors: Sony is expected to sell of its struggling PC business with Vaio PC to private equity investor JIP or the Chinese industry player Lenovo. Further, America Móvil seemed to be undervalued making it a target company with high regulatory risk.

TMT Universe:

- Comcast
- Facebook
- Google
- Microsoft
- Portugal Telecom

This month's detailed company review:

- Facebook



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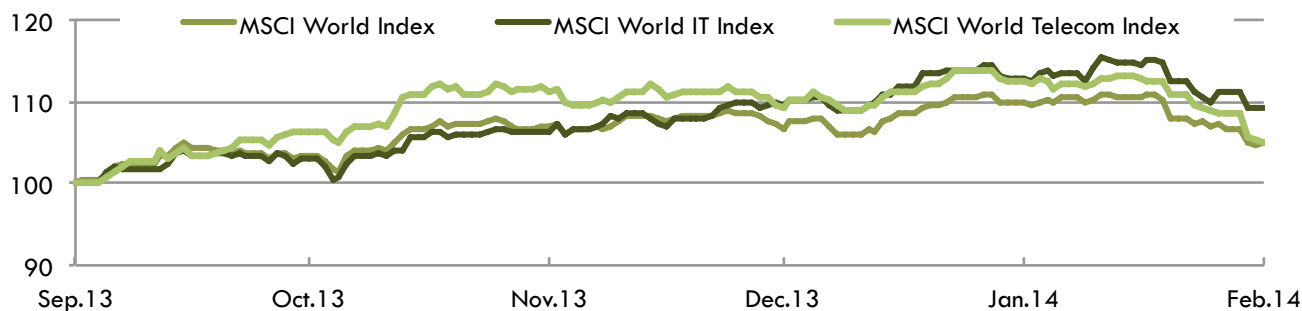
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TMT Sector vs. Overall market



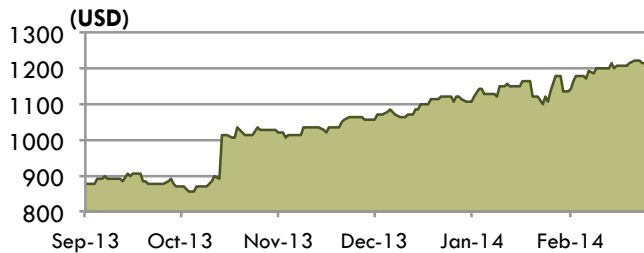
- During this period, the indexes that serve as benchmark for the TMT sector, specifically the Information Technology and Telecom sector, followed a similar path. From December to January the indexes slight increased due to the growth in the deal flow of these sectors, namely the acquisitions by Lenovo, Liberty Global and Google. Both sectors performed better than the MSCI World Index which shows the intensity of deals flow in the TMT industry.

3. Followed Companies

Google

(Ticker: GOOG US)

- Google announced to compete in US cable TV and telecommunications market by building fiber optic networks responding to deal talks of Comcast and TWC. The fourth quarter results again beat all expectations but earnings growth. Nokia turning towards Android operating system despite the new ownership is seen as another success for the software company.



| | | |
|---------------------|---|----------|
| Price (USD): | ↑ | 1,215.65 |
| Target Price (USD): | | 1,313.00 |
| Up/downside: | | 8.0% |
| Performance 3M: | | 15.4% |
| P/E Ratio: | | 33.4x |
| ROC/WACC: | | 1.3x |

Microsoft

(Ticker: MSFT US)

- The new CEO Nadella is elected to find the new profitable paths of Microsoft amid a step down by Bill gates from the chairman position. Besides the major news Orange is said to be in talks with Microsoft to develop its sharing platform internationally.



| | | |
|---------------------|---|-------|
| Price (USD): | → | 38.31 |
| Target Price (USD): | | 39.00 |
| Up/downside: | | 1.8% |
| Performance 3M: | | 0.0% |
| P/E Ratio: | | 13.5x |
| ROC/WACC: | | 2.3x |

Portugal Telecom

(Ticker: PTC PL)

- Fitch's downgrading of PTs Issuer Default Rating to BBB- is in expectation of the prospective merger with Oi, that could result in an even lower rating. The reported Q4 profits drop by 35 % due to foreign exchange losses, fierce competition in domestic mobile market and restructuring costs in Brazil.

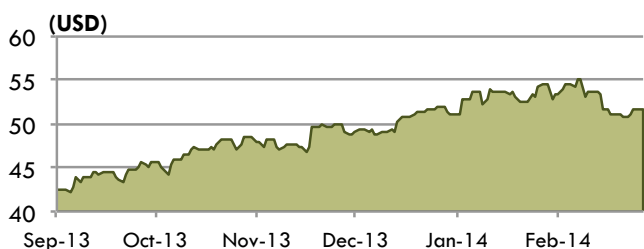


| | | |
|---------------------|---|-------|
| Price (EUR): | ↑ | 3.25 |
| Target Price (EUR): | | 3.60 |
| Up/downside: | | 10.7% |
| Performance 3M: | | 0.8% |
| P/E Ratio: | | 8.6x |
| ROC/WACC: | | 0.8x |

Comcast

(Ticker: CMCSA US)

- For comcast the merger with TWC explains the latest drop in share price. While the transactions seeks approval from regulatory agencies, Liberty shows interest in acquiring possible divestures. Latest news estimate the possible spin-off with 3 million subscribers. Also on the heels, was the joint announcement with Netflix paying more for faster service in future.

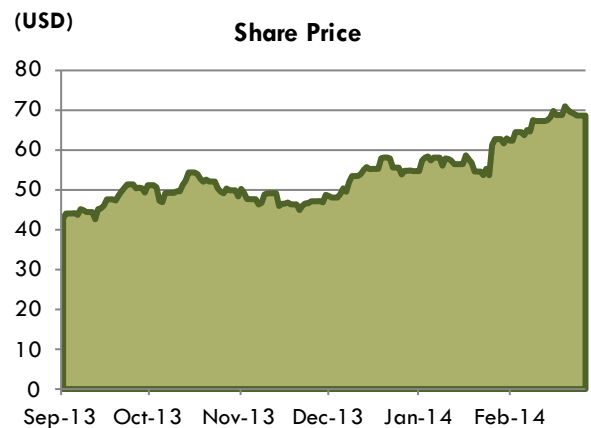


| | | |
|---------------------|---|-------|
| Price (USD): | ↑ | 51.69 |
| Target Price (USD): | | 60.00 |
| Up/downside: | | 16.1% |
| Performance 3M: | | 6.0% |
| P/E Ratio: | | 20.9x |
| ROC/WACC: | | -2.7x |

3. Stock Analysis: Facebook

Corporate News

- In February it was announced that Facebook acquired Whatsapp for \$ 19bn, being \$ 15bn paid in stock and \$ 4bn in cash. This \$ 15bn stock payment illustrates that Facebook is effectively sharing a large portion of the risk in this dreadfully speculative deal with WhatsApp. The amount it is paying for this start-up is 11 times more than that Google paid to acquire Youtube. This acquisition is Facebook's largest by far, softening the \$1bn paid to Instagram in 2012 which was ranked by that time as the social media website's previously major transaction.
- Whatsapp is a leading player in the chat app world having more than 450mn users. In the last years this segment has grown rapidly being the Whatsapp's figures far-fetched: Its users send almost as many messages as the number of text messages sent over the entire global telecoms network and 70% of its users send messages on a daily basis being the engagement rate of Whatsapp higher than that of Facebook. Furthermore, this acquisition will allow Facebook to gather users and to enter in the chat app market with the creation of the Facebook Messenger. The establishment of a mobile service it is also possible which would enforce Facebook's position in the social network market.



| Facebook (USD) | |
|----------------------------|---------|
| Current Price (03/02/2014) | 68.46 |
| 52-week high % change | -4.2% |
| Median Target Price | 71.32 |
| Market Capitalisation (mn) | 173,903 |
| Return on Common Equity | 10.9% |
| Dividend Yield | N/A |
| Beta (vs. S&P500) | 0.48 |
| Total Debt/Equity | 3.1% |

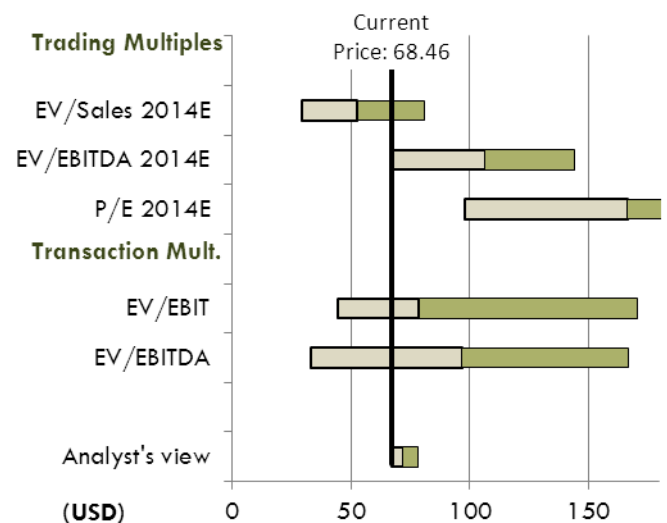
Market Performance

- Facebook performed very well in the last months, witnessing an upward trend. However, after the announcement of this acquisition, Facebook's share price fell around 3%. This is a normal reaction once the market is sceptical about purchases, specially about the performance that the acquirer will have after this purchase and the validity of the value the buyer paid. Since 24th of February, Facebook's share price has been slight decreasing, shifting from roughly \$ 72 to \$68.46 in the end of the month.

Valuation Summary

- Facebook is priced fairly according to both analysts and transactions multiples. However, it is slightly undervalued under the P/E trading multiples.

Valuation Summary (Price per Share)



Comparable Analysis

| Company Name | Currency | MCap (mn) | Enterprise Value (mn) | EV/Sales | | | EV/EBITDA | | | P/E | | |
|-----------------|----------|-----------|-----------------------|--------------|-------------|-------------|--------------|--------------|--------------|---------------|---------------|--------------|
| | | | | LTM | 2014E | 2015E | LTM | 2014E | 2015E | LTM | 2014E | 2015E |
| Facebook | USD | 170,982 | 160,009 | 16.3x | 14.2x | 10.8x | 41.9x | 23.5x | 17.8x | 114.1x | 53.7x | 40.1x |
| Twitter | USD | 30,587 | 28,550 | 50.1x | 23.2x | 14.5x | -54.4x | 162.7x | 71.6x | N/A | 5993.3x | 278.0x |
| Linked In | USD | 24,072 | 21,748 | 15.6x | 10.3x | 7.7x | 119.3x | 41.9x | 28.8x | 876.5x | 124.8x | 74.9x |
| Groupon | USD | 5,684 | 4,542 | N/A | 1.4x | 1.3x | 27.5x | 15.8x | 11.3x | N/A | 79.4x | 33.8x |
| Google | USD | 402,001 | 346,553 | 5.4x | 6.3x | 5.3x | 19.3x | 13.4x | 11.2x | 32.8x | 22.7x | 19.1x |
| Zynga | USD | 4,411 | 2,869 | 1.9x | 3.5x | 3.1x | 39.0x | 35.0x | 20.4x | N/A | 457.3x | 111.8x |
| 75th Percentile | | | | 16.3x | 13.2x | 10.0x | 41.2x | 40.2x | 26.7x | 495.3x | 374.1x | 102.6x |
| Median | | | | 15.6x | 8.3x | 6.5x | 33.2x | 29.2x | 19.1x | 114.1x | 102.1x | 57.5x |
| 25th Percentile | | | | 5.4x | 4.2x | 3.7x | 21.4x | 17.7x | 12.9x | 73.5x | 60.1x | 35.3x |

- Facebook is valued slightly above the range of the majority of its peer companies for 2014 and 2015 Sales, being the only exception Twitter that is priced above Facebook. On the other hand, in which regards the P/E 2014 multiple, Facebook is the second lowest multiple which means that Facebook has been considerably cheap comparing to its peers.
- In part, this 2014 forecasts can be explained by the recent acquisitions that Facebook has undertaken, namely Whatsapp's. Markets are sceptical about acquisitions and promptly react forcing the price to go down.

Precedent Transactions

| Announced Date | Target | | Buyer | | EV (USD mn) | EV/EBIT | EV/EBITDA |
|-----------------|----------------------|---------|-----------------------|---------|-------------|--------------|--------------|
| | Company | Country | Company | Country | | | |
| 18-Apr-05 | LDH Corp | JP | Fuji Media Holdings | JP | 410 | 61.0x | 55.0x |
| 08-Aug-07 | ECS Holdings Ltd | SGX | VST Holdings Ltd | HKD | 107 | 6.0x | 5.6x |
| 08-Sep-09 | SINA Corp/China | CH | Sequoia Capital China | CH | 180 | 27.0x | 26.5x |
| 10-May-11 | Skype SARL | US | Microsoft Corp | US | 8,500 | 411.6x | 46.7x |
| 04-Sep-11 | Compaq Computer Corp | US | Hewlett-Packard | US | 25,321 | 14.3x | 7.9x |
| 75th Percentile | | | | | | 61.0x | 46.7x |
| Median | | | | | | 27.0x | 26.5x |
| 25th Percentile | | | | | | 14.3x | 7.9x |

- In the last years many deals reached the Tech sector. Facebook acquired Instagram for around \$1 bn, Viber was acquired by Racutem Inc. for \$900 mn, Google purchased Youtube for \$1.65 bn, Microsoft bought Skype for \$8.5 bn and many others. The ones from United States have been the ones on the spot light. However, there are many deals reaching Asian countries that also have a huge relevance.
- When these kind of deals are announced there are often some criticisms about the value that had been paid. In fact, sometimes is hard to explain why tech companies pay that much, but the core of the question is the additional users that the acquisition might provide. It is important to underline that the pricing game is not about what people believe that makes sense but what traders care about.