

Has Facebook's Value Taken a Hit?

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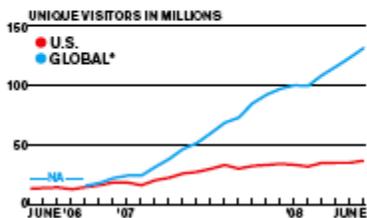
Facebook founder Mark Zuckerberg. Noah Berger/The New York Times/Redux



Ballmer cut a deal for a stake in Facebook last year that valued it at \$15 billion Samuel Kubani/AFP/Getty Images

THE TWO FACES OF FACEBOOK

U.S. growth is slowing, while worldwide increases are strong



Data: ComScore

*WORLDWIDE INCLUDING U.S.



Insiders at Facebook are selling stock in the social-networking giant, and the prices they're getting for their shares suggest the sky-high valuation backers once placed on the company may prove unrealistic.

Just a few months ago, Facebook was widely viewed as the next Google (GOOG) in Silicon Valley. Microsoft (MSFT) bought a small preferred equity stake last October that the two companies said implied a valuation of \$15 billion for all of Facebook. Shareholders in the still-private company appeared to be setting themselves up for a blockbuster initial public offering.

But in recent months, a number of current and former executives have put some of their common stock up for sale. Laurence Albuquerk, who brokers the sale of stock in private companies in the Valley, says he knows of at least nine people who have sold or are trying to sell Facebook shares. He estimates that "dozens" are unloading stock, through him or other brokers. Another finance executive, who would not speak for attribution, confirmed Facebook insiders are selling. Among those who have reportedly sold are founder and CEO Mark Zuckerberg and departing vice-president Matt Cohler. A Facebook spokeswoman said both declined comment for this story.

The prices for Facebook shares in these transactions reflect a total valuation far lower than \$15 billion. Albuquerk, the founder and managing director of EB Exchange Funds, says that two current directors and one former executive recently contacted him about selling some of their stock for prices implying a \$5 billion valuation. He also says that two investment firms have bought large chunks of Facebook stock at a valuation of about \$3.75 billion. Hans Swildens, founder of Industry Ventures, a San Francisco firm that buys stock in private companies, says his firm has been talking with a growing number of Facebook employees. "There's a lot of interest among people to sell shares," says Swildens.

The stock sales at Facebook don't necessarily mean Microsoft CEO Steve Ballmer cut a bad deal. The software giant paid \$240 million for a 1.6% stake, but it bought preferred stock that carries special rights. For example, it has "liquidation preferences" that mean it gets paid before common stockholders if the company is sold. Microsoft also got rights to place international ads on Facebook.

Rank-and-File Grumbling

Stock sales are unusual at technology startups. In the past, entrepreneurs rarely had the chance to cash in until their companies went public or were sold. When they do sell, it can create conflicts of interest with venture backers and other employees who hadn't realized the same wealth. Eric Hippeau, managing partner at venture firm SoftBank Capital, says none of the two dozen companies his firm has invested in have programs for employees to sell stock. "I'd tell them to get back to work," says Hippeau.

The sales at Facebook have led to controversy within the graffiti-covered walls of its Palo Alto (Calif.) offices. After employees heard that Zuckerberg and Cohler had sold, there was grumbling among the rank and file, say two sources who have spoken with staff.

Facebook is taking steps to address the issue. On Aug. 5 the company issued a statement announcing it will help current employees sell some of their stock. "To provide employees with a financial cushion while we continue to build the company, Facebook has designed a onetime program to enable employees to realize some liquidity," the company said in a statement. Facebook declined to outline details of the plan. But VentureBeat, a blog that first reported the existence of the program, said the plan would limit Facebook workers to selling 20% of their vested stock options at a \$4 billion valuation, starting this fall.

The company is also putting restrictions on stock sales by some employees who leave the company, BusinessWeek has learned. Facebook is requiring such workers to sign agreements that prevent them from selling shares at more than a \$3.75 billion valuation, according to one source close to the company. That figure has special significance. According to a lawsuit involving Facebook filed in federal court, the startup's board approved a so-called formal valuation resolution required by the Internal Revenue Service valuing the common shares at \$3.75 billion.

There are at least two possible reasons for the restriction. First, it could suppress stock sales by employees who think their shares are worth more. Second, it could help Facebook avoid raising its valuation with the IRS. Raising it could trigger tax bills for employees and make it harder to lure top talent.

There are several reasons that Facebook is likely worth less than the \$15 billion value it cited when announcing the Microsoft deal. The public equity markets have gotten crushed over the last year, and skittish investors have also lost their appetite for IPOs.

And the social-networking business doesn't look as promising as it did 10 months ago. Growth in the number of U.S. users at Facebook, MySpace, and other sites has slowed this year. Social networks have also struggled to generate revenue through advertising at the rates originally expected. Google, which places ads on News Corp.'s (NWS) MySpace, has said making money off social networks has proven difficult.

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