

Facebook valuation will be high, but justified, expert says

February 8 2012, By Neil Schoenherr



(PhysOrg.com) -- Facebook's initial public offering (IPO) filing shows real numbers for profit and revenues, which are likely to drive a valuation that could be as high as \$100 billion.

This astronomical number does require some aggressive assumptions about future growth, but the high valuation may be more justified than for other internet companies, says an expert at Washington University in St. Louis.

"This is a huge market cap for such a young firm," says Mark T. Leary, PhD, assistant professor of finance at Olin Business School.

"But I think there are a few factors that separate Facebook from some of the earlier Internet IPOs that may have been over-hyped," he says.

The Internet itself is a more established advertising medium than it was in the late 1990s, Leary says.

“There is less uncertainty about the total size of the market and other firms have proven the viability of a business model based largely on online advertising revenue,” he says. “But I think this model is only viable for the ‘winners’ in capturing online share.”

The other important element is that Facebook has already established itself, to some extent, as the winner in the social networking arena, he says.

“They are more mature than the typical firm we saw going public at the height of the Internet bubble.” Leary says. “Their user base is huge and they are already profitable.

“And unlike some other Internet companies, like Groupon, Facebook’s competitive position seems sustainable. Once everyone’s part of their network, there are high costs of switching to another social networking site that tries to start up.”

“So while I’m sure the \$100 billion valuation requires some aggressive assumptions about future growth, the downside risk in terms of revenue generation seems much lower for Facebook than other net firms,” Leary says.

Google holds the record for the largest U.S. Internet IPO by raising \$1.9 billion at a [valuation](#) of \$23 billion in 2004.

“I think the comparison with Google comes not just from the size of the offering, but Facebook is the first firm since Google to attract such a large and loyal following, which obviously enables them to attract advertisers,” he says. “For Facebook, growth in users is likely to slow

down in the coming years. The challenge going forward is finding new ways to leverage that large user base to grow earnings.”

[Facebook](#) says it hopes to raise as much as \$10 billion when it begins selling shares this spring.

Among U.S. companies, only Visa Inc., General Motors Co. and AT&T Wireless have held larger offerings than \$10 billion.

Provided by Washington University in St. Louis

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