Financial Advisers Still Leery of Facebook Stock

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By Daisy Maxey

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Mark Zuckerberg

Financial advisers say they might consider friending Facebook Inc.'s (FB) stock at the right price, but they haven't seen enough from the social-networking company yet to know what that price is.

"Everything's a good deal at the right price," said Pat Dorsey, director of research at Sanibel Captiva Trust Co., a Sanibel, Fla., firm that manages about $1.1 billion in assets. "This is not a bad business, but it's a very uncertain business right now."

Shares of Facebook went public in mid-May at $38 and closed that day at $38.23. Things have been downhill since. The stock took another tumble Thursday when early investors were freed to sell a portion of their stakes. It traded at $19.31 recently, down 3.5%.

The viability of Facebook's advertising model is one question in advisers' minds.

Mr. Dorsey wonders how the advent of smart devices will affect the Menlo Park, Calif., company. More people are accessing Facebook from their smartphones rather than their personal computers, which makes delivering advertising harder, he said. "The screen real estate is just smaller; you're glancing at your phone on the train; the odds that you're going to click on an ad are less," he said. "You're not in 'gathering information' mode." In addition, Facebook's shares currently trade at 30 times forward earnings, and "you're projecting the earnings of a company in an industry that didn't even exist five years ago," said Mr. Dorsey. "There's going to be a little bit of uncertainty."

Louis Stanasolovich, a financial planner with Pittsburgh-based Legend Financial Advisors, which oversees about $350 million in assets, didn't buy Facebook shares at the launch, and isn't ready to do so now. He'd like to see Facebook generate some profits before deciding on where its stock offers value. The social network's advertising revenue model is challenged and it might do better to copy Google Inc.'s (GOOG) advertising model, Mr. Stanasolovich said.

Facebook's revenue rose 32% in the second quarter, beating analysts' expectations, but it showed a loss.

George Kiraly Jr., an adviser with Short Hills, N.J.-based LodeStar Advisory Group, which oversees about $15 million in assets, said he might consider buying shares near $15. However, average investors should tread carefully, Mr. Kiraly said. Lockup expirations in October, November and December will permit Facebook employees to sell more than 1.4 billion shares of the stock. That will likely trigger additional selling through the end of the year, he said. "I certainly wouldn't buy ahead of those shares coming to market," he said. "I'm sure the hedge funds are in there shorting."

But S&P Capital IQ analyst Scott Kessler upgraded shares of Facebook to buy from hold last week ahead of the lockup expiration. He's expecting the stock to outperform and has set a 12-month price target of $25. Much of investors' reaction to Facebook has been rooted in emotion, which is a typically unhealthy way to judge investments, Mr. Kessler said, adding that "Facebook's growth story is a lot stronger than people think." S&P Capital IQ expects the company to generate annual growth of 25% or more organically for the next three years. It sees a lot of e-commerce potential in Facebook's users combined with its data, Mr. Kessler said. More advertising could drive more business on PCs or mobile devices, and Facebook's management is focused on those opportunities, he noted.

"I don't dispute that there are challenges to monetizing users," he said. "And, yes, they've had some issues in terms of mobile."

Facebook, however, has highlighted recently that its Sponsored Stories, advertising using images and names of users who "like" products, is generating more than a million dollars a day in revenue, Mr. Kessler said. And while advertising on mobile devices is a challenge, Facebook has been able to create more informative, less intrusive advertising, he said.

Also, investors seem to overlook the fact that Facebook has no debt and a net $10 billion in cash and investments, Mr. Kessler said.

"It's a complicated and confusing story," he said. "We by no means think that Facebook has figured all of this out. But the growth is there, and we expect it to be sustainable for at the least three years."

Daisy Maxey is a Dow Jones columnist who writes about matters of interest to advisers, including hedge funds, annuities, closed-end funds and new trends in mutual funds. Her columns are available to Dow Jones subscribers.