

Touchbutton

Issue 5

Facebook likes Instagram

Observers of bubbles and manias will no doubt be watching closely the purchase of Instagram by Facebook for \$1bn, and the upcoming listing of Facebook at the eye popping estimated market capitalisation of around \$100bn. Not bad for a company making \$1bn a year in profits, although Instagram win the prize for stretched values, with barely any revenue stream, let alone profitability.

What is going on? Simply put, this is all to do with the race to control social networking. Instagram is almost certainly not worth \$1bn, but it has 30 million users, most of whom probably use Facebook too, and between these happy snappers they upload 5 million photos a day onto the Instagram website, all via smartphones, an area where Facebook may be behind the curve. Control of this sharing of photos from smartphones is crucial for Facebook, because if they lose their grasp of social networking via portable devices, a crucial part of which is photos, then things could unravel for them very quickly. If it hadn't been Facebook getting the chequebook out, it might have been Google or even Apple, and Facebook simply cannot allow this to happen.

For readers brought up on a diet of delivering a can of film to Boots and being told to come back in a fortnight, the pace of change in this area of our lives is breakneck. From an investment standpoint, pursuing these bubbles is potentially dangerous: a new technology bubble is forming nicely, especially at the individual stock level, and it has little appeal to us as long term preservers of wealth.

It is hardly surprising that some investors, including us, prefer to leave the whole dot.com segment of the market to braver souls. Values in the old fashioned sense are almost impossible to pin on companies, and fashions can change very rapidly, leaving what looked like valid business models well and truly high and dry. It is not for nothing that Warren Buffett sticks to businesses that he understands. When he bought Wrigley's Chewing Gum, he happily proclaimed that however much he thought about it, he didn't think the internet would change the way people chew gum. Facebook's Mark Zuckerberg is probably wishing his business model was as simple.



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