

Twitter Inc TWTR (NYSE) | ★★★

Last Price	Fair Value	Consider Buy	Consider Sell	Uncertainty	Economic Moat™	Moat Trend™	Stewardship	Morningstar Credit Rating	Industry Group
44.13 USD	39.00 USD	23.40 USD	60.45 USD	High	Narrow	Positive	Standard	—	Online Media

Twitter User Growth Shows Promise, but Stock Price Reflects Too Much Optimism

Updated Forecasts and Estimates from 30 Jul 2014

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The primary analyst covering this company does not own its stock.

Research as of 30 Jul 2014
Estimates as of 30 Jul 2014
Pricing data through 01 Aug 2014
Rating updated as of 01 Aug 2014

Currency amounts expressed with "\$" are in U.S. dollars (USD) unless otherwise denoted.

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Investment Thesis 30 Jul 2014

Twitter and its users benefit from the network effects typical of a broad content distribution platform. The company counts 271 million monthly active users, an impressive number for a media platform that has captured both attention and budgets from advertisers. Engagement with the Twitter platform is naturally social, reinforcing the desire to share and react to information in real time. The company would argue that it is the largest "real-time" social network in the world, and we would agree.

There are many self-selected groups within Twitter, connected by interests. Users may follow celebrities (for example, One Direction and LeBron James), work interests (for example, human capital), and local interests (for example, Chicago events or breaking news). Each user's experience is highly personalized, based on how users create their networks, interact with the content, and post their own content. Twitter is building a unique and proprietary customer data set.

In our view, the most important growth levers for Twitter are market share, users, and time spent. Perhaps the most important aspect supporting our positive view on growth is the complementary nature of Twitter to traditional content and media. This will allow Twitter to more cheaply acquire content that flows through its media platform.

Still, growth in users has been slowing. Furthermore, the company is competing for advertising dollars with juggernauts such as Facebook and Google. Last, as advertisers may struggle to measure the success of ad campaigns, the company may struggle to attract new ad dollars.

Still, we believe the marketing data that Twitter is gathering through the proprietary interest graph will piggyback on the momentum created by Facebook. As advertisers have continued shifting spending to online media, large tranches have remained offline—particularly in TV advertising—because of traditional considerations, including brand-building objectives and broad reach.

Vital Statistics

Market Cap (USD Mil)	26,034
52-Week High (USD)	74.73
52-Week Low (USD)	29.51
52-Week Total Return %	—
YTD Total Return %	-30.7
Last Fiscal Year End	31 Dec 2013
5-Yr Forward Revenue CAGR %	59.9
5-Yr Forward EPS CAGR %	—
Price/Fair Value	1.13

Valuation Summary and Forecasts

	Fiscal Year:	2012	2013	2014(E)	2015(E)
Price/Earnings	—	NM	441.3	70.0	
EV/EBITDA	—	NM	97.3	31.8	
EV/EBIT	—	NM	NM	NM	
Free Cash Flow Yield %	—	-0.2	-0.3	2.1	
Dividend Yield %	—	—	—	—	

Financial Summary and Forecasts (USD Mil)

	Fiscal Year:	2012	2013	2014(E)	2015(E)
Revenue		317	665	1,354	2,375
Revenue YoY %		198.1	109.8	103.6	75.5
EBIT		-77	-636	-609	-190
EBIT YoY %		-39.5	724.9	-4.2	-68.8
Net Income, Adjusted		-79	-45	74	506
Net Income YoY %		-51.6	-43.4	-264.7	583.3
Diluted EPS		-0.68	-0.24	0.10	0.63
Diluted EPS YoY %		-57.7	-64.9	-141.0	548.9
Free Cash Flow		-104	-708	-712	-43
Free Cash Flow YoY %		-34.8	582.2	0.6	-93.9

Historical/forecast data sources are Morningstar Estimates and may reflect adjustments.

Profile

Twitter is an Internet platform that individuals and companies use to post short messages (a maximum of 140 characters) that are publicly visible. The company counts more than 271 million monthly active users. Individuals tend to self-organize based on topics of interest (for example, finance or sports) and form a loose social network. Advertising generates nearly 90% of revenue. The service is mostly known for its real-time content.

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Morningstar Analysis

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Twitter's second-quarter results came in above our near-term forecast across three metrics: revenue, users, and revenue per user. The robust user growth numbers coupled with continued strength in advertising revenue have a meaningful impact on our near-term forecast and also provide us with more optimism that Twitter can come closer to approaching a mass-market advertising platform alongside competitors like Google and Facebook. As a result, we are increasing our fair value estimate more than 25%; we are also reiterating our narrow moat rating. However, we believe the current stock market euphoria may prove overly optimistic, and the shares are unlikely to earn appropriate returns.

Quarterly revenue grew 124% versus 2013 to \$312 million, led by advertising revenue (89% of the total) posting 129% annual growth. Monthly active users also grew a healthy 24%, leading us to increase our expectations for MAUs to approximately 300 million by the end of 2014. Additionally, we have increased our revenue forecast to account for the company's success in rolling out new ad formats, increasing ad revenue per user 84% to \$1.02 for the quarter. The disparity between U.S. and non-U.S. markets remains wide (roughly 5 times higher as measured by revenue per timeline view), although management said it expects this gap to converge as smartphone penetration continues to grow outside the more developed markets. We agree with this assertion, and we are becoming more positive (although not certain) that Twitter will become an effective mass-market advertising platform. We are increasing our base-case and bull-case forecasts to reflect this increased likelihood.

Despite our more optimistic view, we believe the shares are overvalued at these levels. Although we believe the real-time nature of the Twitter experience provides a unique advertising opportunity, it does not approach the effectiveness in reach or customer conversion that

companies such as Google and Facebook provide. While we believe Twitter is integral to many advertising budgets, we do not expect the firm to disrupt companies that can provide deeper targeting and broader reach. Ultimately, we believe the growth in ad revenue per user and total revenue opportunity will slow and will be unlikely to reach similar levels to the category leaders in the Internet sector.

Valuation, Growth and Profitability 30 Jul 2014

For our valuation, we take a weighted average of our base-case, bull-case, and bear-case scenarios. Based on this weighted average, we are increasing our fair value estimate to \$39 per share from \$29 to account for a significantly higher bull case and modestly higher base case, driven by acceleration in monthly average users and higher ad revenue per user metrics.

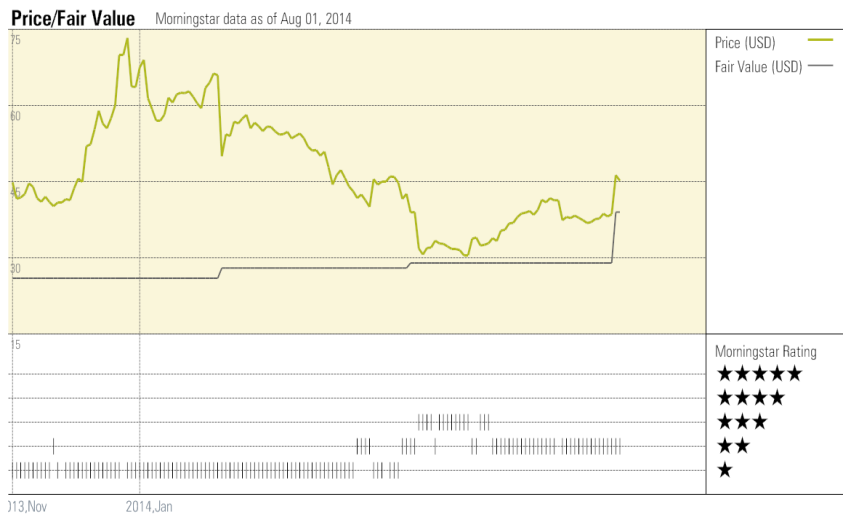
In our base-case scenario, several growth levers contribute to revenue and cash flow growth, and although the firm achieves meaningful growth in users, Twitter's network reaches about half of Facebook's user base. In this model, MAUs grow at a 21% compound annual growth rate through 2022. Additionally, ad revenue per user grows at a 22% CAGR to nearly \$13. We also consider different usage levels within the user base. In the base case, heavy users contribute \$19 per year and casual users contribute only \$4 per year. Total company revenue reaches \$13 billion in 2022, while operating margins reach 28%. Returns on invested capital are approximately 20% at the end of our forecast period. Based on our 10-year discounted cash flow model, this scenario yields a \$30 fair value estimate.

Scenario Analysis

In our bull-case scenario, we expect the company to achieve a reach similar to Facebook's, although our model does not explicitly consider time spent on the service. In this model, MAUs grow at a 29% CAGR through 2022. Additionally, ad revenue per user grows at a 28% CAGR. We consider different usage levels within the user base. In our bull case, heavy users contribute \$30 per year while casual users

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contribute only \$4 per year. Total company revenue exceeds \$35 billion in 2022, while operating margins reach 29%. ROICs are approximately 26% at the end of our forecast period. Based on our 10-year DCF model, this scenario results in a \$76 fair value estimate.

Our bear-case scenario is a key component of both our investment thesis and valuation. We believe Twitter has built assets that are competitively differentiated and durable, even if it is unable to translate its platform into a mass-market social network. While we have highlighted the lack of reach that may ultimately plague the company in our downside scenario, we believe that other companies, namely Facebook and Google, would find value in the highly differentiated "one to one," "many to one," and "one to many" media platform. Twitter's unique customer data would have even greater value when combined with data from Facebook or Google, in our view. Furthermore, both of these firms would find a high degree of synergy and would probably eliminate the bulk of Twitter's existing sales and marketing infrastructure to support advertising revenue. Of course, Facebook and Google would not be the only firms to place a high economic value on Twitter, but we believe

these two provide the most logical fit. In the event that Twitter is unable to acquire a mass market beyond its early adopters, the company would be acquired. Based on our 10-year DCF model, this scenario results in a \$18 fair value estimate.

Economic Moat

Twitter's narrow economic moat is built on several important characteristics: reach, network effects, and unique customer data. Twitter and its users benefit from the network effects typical of a broad content distribution platform. The company counts 271 million monthly active users, an impressive number for a media platform that has captured both attention and budgets from advertisers. During the fourth quarter of 2013, Twitter also reported more than 150 billion "timeline views," growing 26% versus the prior year. Timeline views are Twitter's metric for reporting engagement, a measure of the frequency at which users are reading tweets (messages). This level of engagement is likely to be misunderstood, in our view, as competitors are frequently reporting other measures of engagement. Taken at face value, Twitter's reach alone is insufficient, in our view, to create massive competitive advantages today and thereby offer support for a wide moat. For example, in the United States, companies such as Yahoo (narrow moat), Google (wide moat), and Facebook (wide moat) have much greater reach, both for desktop and mobile users.

Moat Trend

Twitter's positive moat trend is based on the increasing importance of the media distribution platform and its growing insights about its users, which should help support its unique value proposition. Twitter's interest graph forms a unique and proprietary database of user data, supporting the company's moat. While Facebook claims to own the "social graph," Twitter's social network is forming the "interest graph" of its users. In conversations with users, individuals say Twitter provides unique connections to celebrities (for example, Katy Perry has more than 44 million

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followers), politicians (President Obama has more than 38 million followers), brands (comedy website Funny or Die has more than 6 million followers), sports (the NFL has more than 5 million followers), and pundits (venture capitalist Fred Wilson has more than 250,000 followers). Users can tailor their timeline and create lists based on their interests. Individuals can also interact with tweets, including through replies, "retweets," "favorites," "following," or forwarding on to an individual by e-mail, outside the Twitter ecosystem. Each of these actions represents a different level of engagement, generating additional data for the Twitter customer database. We believe advertisers will be able to successfully target branding and direct-response campaigns on Twitter better than most competitive platforms.

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Bulls Say/Bears Say

Bulls Say

- ▶ Twitter's ad revenue per user continues to grow, surpassing other social networking companies, including LinkedIn.
- ▶ The company recently agreed to a commercial deal with the National Football League to distribute proprietary content (short replays) to Twitter users, demonstrating the importance of Twitter to partner companies.
- ▶ If Twitter is able to attain a similar user base to Facebook, the upside opportunity versus our current view is meaningful.

Bears Say

- ▶ Twitter's growth in MAUs is slowing, indicating that the market could be reaching a level of maturity.
- ▶ Twitter's user base is significantly smaller than those of companies such as Google, Facebook, and Yahoo, and some advertisers require massive reach before allocating budget to a digital platform.
- ▶ Twitter is highly dependent on one advertising product, and new advertising could turn users away from the service.

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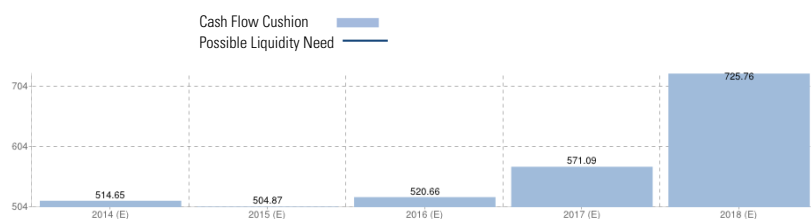
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Credit Analysis

Five Year Adjusted Cash Flow Forecast (USD Mil)

	2014(E)	2015(E)	2016(E)	2017(E)	2018(E)
Cash and Equivalents (beginning of period)	841	1,643	1,616	1,713	2,160
Adjusted Available Cash Flow	1,434	589	685	811	1,048
Total Cash Available before Debt Service	2,275	2,232	2,302	2,525	3,208
Principal Payments	—	—	—	—	—
Interest Payments	-4	-4	-4	-4	-4
Other Cash Obligations and Commitments	—	—	—	—	—
Total Cash Obligations and Commitments	-4	-4	-4	-4	-4

Cumulative Annual Cash Flow Cushion



Adjusted Cash Flow Summary

	USD Millions	% of Commitments
Beginning Cash Balance	841	3,804.8
Sum of 5-Year Adjusted Free Cash Flow	4,568	20,665.5
Sum of Cash and 5-Year Cash Generation	5,409	24,470.3
Revolver Availability	—	—
Asset Adjusted Borrowings (Repayment)	—	—
Sum of Cash, 5-Year Cash Generation, Revolver and Adjustments	5,409	24,470.3
Sum of 5-Year Cash Commitments	-22	—

Credit Rating Pillars—Peer Group Comparison

	TWTR	Sector	Universe
Business Risk	6	—	—
Cash Flow Cushion	1	—	—
Solvency Score	4	—	—
Distance to Default	—	—	—
Credit Rating	—	—	—

Source: Morningstar Estimates

Note: Scoring is on a scale 1-10, 1 being Best, 10 being Worst

Financial Health & Capital Structure

Twitter's balance sheet is solid, holding approximately \$2 billion of net cash. We expect the company to invest heavily in sales and marketing, product development, and capital expenditures, resulting in negative free cash flow until 2015. Although the operating model is unproved thus far, we expect the company to eventually translate 15% of sales into free cash flow.

Enterprise Risk

The biggest risk to our investment thesis is that the growth potential has saturated, and Twitter never grows into the mainstream Internet population. As a niche product, advertisers are unlikely to dedicate a large percentage of their advertising budgets to the platform. Additionally, the company must successfully launch new advertising products in order to increase ad revenue per user, translating into top-line sales and bottom-line cash flows. Ultimately, the operating model has not been proved, so our operating margin assumptions may prove unattainable as well.

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Management & Ownership

Management Activity

Name	Position	Shares Held	Report Date*	InsiderActivity
MR. EVAN WILLIAMS	Director	3,213,802	13 Nov 2013	—
MR. MIKE GUPTA	CFO	1,178,975	02 Jun 2014	130,254
MS. VIJAYA GADDE	General Counsel/Secretary	818,686	26 Jun 2014	43,795
MR. ALEXANDER ROETTER	Senior VP, Divisional	746,095	07 Jul 2014	78,680
MR. RICHARD COSTOLO	CEO/Director, Director	582,660	06 Nov 2013	—
MR. ADAM BAIN	President, Divisional	526,290	06 Nov 2013	—
LUCA BARATTA	Chief Accounting Officer/Vice President, Divisional	334,290	22 Jul 2014	139,673
DAME MARJORIE MORRIS SCARDINO	Director	4,018	04 Dec 2013	—

*Represents the date on which the owner's name, position, and common shares held were reported by the holder or issuer.

Fund Ownership

Top Owners	% of Shares Held	% of Fund Assets	Change (k)	Portfolio Date
BlackRock Global Allocation Fund	1.32	0.51	1,033	30 Apr 2014
Vanguard Total Stock Mkt Idx	1.19	0.08	5,176	30 Jun 2014
MS INVF US Advantage	0.74	4.08	-136	30 Jun 2014
Harbor Capital Appreciation Fund	0.63	0.63	1,583	30 Jun 2014
Morgan Stanley Inst Mid Cap Growth Port	0.43	1.49	-103	31 Mar 2014
Concentrated Holders				
INVEXIN	—	11.90	-15	30 Jun 2014
Renaissance IPO ETF	0.01	10.67	—	30 Jul 2014
Merchfondo FI	0.03	6.63	—	30 Jun 2014
Interfund Equity USA Advantage	0.10	4.79	20	30 Jun 2014
Fideuram Fund Equity USA Advantage	0.06	4.73	11	30 Jun 2014

Institutional Transactions

Top 5 Buyers	% of Shares Held	% of Fund Assets	Shares Bought/Sold (k)	Portfolio Date
Rizvi Traverse Management, LLC	14.94	—	85,171	31 Dec 2013
Spark Management Partners II, LLC	5.69	—	32,414	31 Dec 2013
Benchmark Capital Management Co. VI, L.L.C.	5.54	—	31,567	31 Dec 2013
Union Square Investment Co	4.88	—	27,839	31 Dec 2013
Institutional Venture Management XII LLC	2.70	99.73	15,895	31 Mar 2014
Top 5 Sellers				
T. Rowe Price Associates, Inc.	2.19	0.14	-4,647	31 Mar 2014
Fidelity Management and Research Company	0.02	—	-1,842	31 Mar 2014
Kleiner Perkins Caufield & Byers LLC	2.60	58.39	-1,703	30 Jun 2014
INSIGHT HOLDINGS GROUP, LLC	2.82	45.09	-1,500	30 Jun 2014
Davis Selected Advisers	0.21	0.16	-791	31 Mar 2014

Management 30 Jul 2014

Dick Costolo has served as CEO since October 2010, having worked at the firm since 2009. Before joining Twitter, Costolo ran several startup technology companies, including a company that was sold to Google, where he then worked for a couple of years. The management team consists of several nonfounders, including Mike Gupta (formerly of Zynga and Yahoo) as CFO and Adam Bain (from News Corporation) as president of global revenue.

This management team has been credited with improving the infrastructure and technology powering the Twitter application, as well as delivering new advertising products and scaling revenue growth. We believe its interests are aligned with shareholders', although we acknowledge that Twitter's limited operating history and lack of history as a public company provide little evidence. Still, we are encouraged that, unlike other high-profile initial public offerings, this company has not used a dual-class structure for its common shares.

Investors should be aware that venture capital firms will own roughly 46% of the outstanding shares, and their objectives may be more short-term than other shareholders'. We would expect most of those shares to be sold into the open market some time after the lockup period expires (180 days after the company begins trading).

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Analyst Notes

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Twitter's second-quarter results came in above our near-term forecast across three metrics: revenue, users, and revenue per user. The robust user growth numbers coupled with continued strength in advertising revenue have a meaningful impact on our near-term forecast and also provide us with more optimism that Twitter can come closer to approaching a mass-market advertising platform alongside competitors like Google and Facebook. As a result, we are increasing our fair value estimate more than 25%; we are also reiterating our narrow moat rating. However, we believe the current stock market euphoria may prove overly optimistic, and the shares are unlikely to earn appropriate returns.

Quarterly revenue grew 124% versus 2013 to \$312 million, led by advertising revenue (89% of the total) posting 129% annual growth. Monthly active users also grew a healthy 24%, leading us to increase our expectations for MAUs to approximately 300 million by the end of 2014. Additionally, we have increased our revenue forecast to account for the company's success in rolling out new ad formats, increasing ad revenue per user 84% to \$1.02 for the quarter. The disparity between U.S. and non-U.S. markets remains wide (roughly 5 times higher as measured by revenue per timeline view), although management said it expects this gap to converge as smartphone penetration continues to grow outside the more developed markets. We agree with this assertion, and we are becoming more positive (although not certain) that Twitter will become an effective mass-market advertising platform. We are increasing our base-case and bull-case forecasts to reflect this increased likelihood.

Despite our more optimistic view, we believe the shares are overvalued at these levels. Although we believe the real-time nature of the Twitter experience provides a unique advertising opportunity, it does not approach the

effectiveness in reach or customer conversion that companies such as Google and Facebook provide. While we believe Twitter is integral to many advertising budgets, we do not expect the firm to disrupt companies that can provide deeper targeting and broader reach. Ultimately, we believe the growth in ad revenue per user and total revenue opportunity will slow and will be unlikely to reach similar levels to the category leaders in the Internet sector.

Twitter's Solid Quarter Still Doesn't Justify Stock Price 30 Apr 2014

Twitter delivered along our expectations, yet, an overly enthusiastic investor base seems to have reacted more negatively to the company's first-quarter results. We believe the stock price has more downside than upside at current levels, and we would encourage investors to look to alternatives, notably Google, at this time. Still, after adjusting our model, we are slightly increasing our fair value estimate to \$29. Also, our narrow moat rating remains, and we believe the company is making strides investing in its economic moat.

Overall revenue grew 119% to \$250 million, paced by ad revenue growing 125% to \$226 million. For our purposes, we aren't overly concerned about the lack of GAAP profitability (posting a net operating loss of \$129 million) as our investment thesis primarily depends on growth in users (monthly active users, or MAUs) and continued increases in revenue per user. MAUs grew 6% sequentially, a positive sign, although we note that our valuation still calls for a faster reacceleration of user growth over the next six to eight quarters. On the monetization front, while there is no cause for alarm, a modest sequential decline in revenue per user (from \$0.91 to \$0.89) prevents us from becoming more bullish in our valuation. Our long-term model calls for a near-tripling of revenue per user to more than \$11 per year. Given the premium to our fair value estimate and our optimistic assumptions, we believe investors should watch from the sidelines and wait for a more reasonable entry point.

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Analyst Notes

Twitter's Fourth Quarter Disappoints; Market Underappreciates the Risk of Slowdown in User Growth 06 Feb 2014

Twitter's first quarterly earnings report as a public company showed strong growth in advertising revenue, although continued deceleration in user growth and surprisingly weaker engagement metrics spooked investors who sold the stock off after the earnings announcement. Even after the sell-off, we believe the stock is overvalued, in spite of a very modest increase to our fair value estimate, to \$28 from \$26. We're sticking with our narrow economic moat rating unless the firm is able to re-accelerate growth in its user base.

Total company revenue grew 116% to \$243 million, with more than 90% coming from a direct sale of advertising products. Based on management guidance and our revised forecast, we expect advertising revenue to exceed \$1 billion in 2014. Additionally, for the first time in the company's existence, the company posted positive operating income after backing out the impact of stock options. Clearly, the company benefited from a strong seasonal quarter, but we would expect the longer-term trend of operating leverage to continue.

At today's stock price, we think investors should be more concerned about Twitter's limited reach, and the slowdown in new user growth should reinforce this risk. Since we initiated coverage on Twitter in advance of the IPO, our valuation and bull case scenarios have projected strong revenue growth, driven by re-accelerating gain in new users. This growth is far from certain, however. If Twitter is near a saturation point for its user base, even our valuation may prove too optimistic.

MAUs (monthly active users) grew only 4% sequentially to 241 million, and U.S.-based MAUs grew only one million to

54 million. Investors depending on an immediate lift were clearly disconcerted, and we also expected the media frenzy surrounding the IPO to deliver more robust gains in users. However, we are not altogether disappointed, and we note the firm has not launched any meaningful initiatives to acquire new users. For our valuation and investment thesis, we anticipate MAU growth to surge in the second half of 2014.

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Morningstar Analyst Forecasts

Financial Summary and Forecasts

Fiscal Year Ends in December

	3-Year Hist. CAGR	Forecast					5-Year Proj. CAGR
		2011	2012	2013	2014	2015	
Growth (% YoY)							
Revenue	186.5	276.0	198.1	109.8	103.6	75.5	59.9
EBIT	—	88.8	-39.5	724.9	-4.2	-68.8	—
EBITDA	—	80.7	-95.6	11,369.0	-147.1	205.6	—
Net Income	—	143.8	-51.6	-43.4	-264.7	583.3	—
Diluted EPS	—	80.7	-57.7	-64.9	-141.0	548.9	—
Earnings Before Interest, after Tax	—	87.9	-42.8	800.8	-9.2	-78.7	—
Free Cash Flow	—	157.4	-34.8	582.2	0.6	-93.9	—

	3-Year Hist. Avg	Forecast					5-Year Proj. Avg
		2011	2012	2013	2014	2015	
Profitability							
Operating Margin %	-79.9	-119.9	-24.3	-95.6	-45.0	-8.0	-2.6
EBITDA Margin %	-59.2	-97.1	-1.4	-79.0	18.3	31.8	29.3
Net Margin %	-62.1	-154.4	-25.1	-6.8	5.5	21.3	16.3
Free Cash Flow Margin %	-96.3	NM	-32.7	NM	-52.6	-1.8	-6.9
ROIC %	-16.3	-18.8	-9.8	-20.4	-14.2	-3.1	2.6
Adjusted ROIC %	-17.9	-19.9	-10.9	-23.0	-15.6	-3.4	2.7
Return on Assets %	-28.8	-45.6	-10.2	-30.8	-14.2	-2.4	2.1
Return on Equity %	29.6	162.6	-37.6	-36.1	-16.2	-2.8	3.3

	3-Year Hist. Avg	Forecast					5-Year Proj. Avg
		2011	2012	2013	2014	2015	
Leverage							
Debt/Capital	0.09	0.06	0.16	0.06	0.05	0.05	0.04
Total Debt/EBITDA	—	-0.42	-25.03	-0.38	0.80	0.26	0.29
EBITDA/Interest Expense	-30.93	-44.21	-2.19	-46.39	55.92	170.88	284.63

Valuation Summary and Forecasts

	2012	2013	2014(E)	2015(E)
Price/Fair Value	—	2.45	—	—
Price/Earnings	—	NM	441.3	70.0
EV/EBITDA	—	NM	97.3	31.8
EV/EBIT	—	NM	NM	NM
Free Cash Flow Yield %	—	-0.2	-0.3	2.1
Dividend Yield %	—	—	—	—

Key Valuation Drivers

Cost of Equity %	10.0
Pre-Tax Cost of Debt %	2.2
Weighted Average Cost of Capital %	10.0
Long-Run Tax Rate %	29.0
Stage II EBI Growth Rate %	12.0
Stage II Investment Rate %	40.0
Perpetuity Year	15

Additional estimates and scenarios available for download at <http://select.morningstar.com>.

Discounted Cash Flow Valuation

	USD Mil	Firm Value (%)	Per Share Value
Present Value Stage I	3,704	19.6	4.62
Present Value Stage II	3,132	16.5	3.91
Present Value Stage III	12,116	63.9	15.12
Total Firm Value	18,952	100.0	23.65
Cash and Equivalents	2,234	—	2.79
Debt	-198	—	-0.25
Preferred Stock	—	—	—
Other Adjustments	1,489	—	1.86
Equity Value	22,478	—	28.05

Projected Diluted Shares 801

Fair Value per Share (USD) —

The data in the table above represent base-case forecasts in the company's reporting currency as of the beginning of the current year. Our fair value estimate may differ from the equity value per share shown above due to our time value of money adjustment and in cases where probability-weighted scenario analysis is performed.

Twitter Inc TWTR (NYSE) | ★★★

Last Price	Fair Value	Consider Buy	Consider Sell	Uncertainty	Economic Moat™	Moat Trend™	Stewardship	Morningstar Credit Rating	Industry Group
44.13 USD	39.00 USD	23.40 USD	60.45 USD	High	Narrow	Positive	Standard	—	Online Media

Morningstar Analyst Forecasts

Income Statement (USD Mil)

Fiscal Year Ends in December

	2011	2012	2013	Forecast	
				2014	2015
Revenue	106	317	665	1,354	2,375
Cost of Goods Sold	62	129	267	420	712
Gross Profit	45	188	398	934	1,662
Selling, General & Administrative Expenses	92	146	440	785	1,021
Research & Development	80	119	594	758	831
Other Operating Expense (Income)	—	—	—	—	—
Depreciation & Amortization (if reported separately)	—	—	—	—	—
Operating Income (ex charges)	-127	-77	-636	-609	-190
Restructuring & Other Cash Charges	—	—	—	—	—
Impairment Charges (if reported separately)	—	—	—	—	—
Other Non-Cash (Income)/Charges	—	—	—	—	—
Operating Income (incl charges)	-127	-77	-636	-609	-190
Interest Expense	2	2	11	4	4
Interest Income	—	—	—	30	30
Pre-Tax Income	-130	-79	-647	-583	-164
Income Tax Expense	-1	0	-2	-29	-58
Other After-Tax Cash Gains (Losses)	—	—	—	—	—
Other After-Tax Non-Cash Gains (Losses)	—	—	—	—	—
(Minority Interest)	—	—	—	—	—
(Preferred Dividends)	-36	—	—	—	—
Net Income	-164	-79	-645	-554	-107
Weighted Average Diluted Shares Outstanding	103	117	190	761	801
Diluted Earnings Per Share	-1.60	-0.68	-3.41	-0.73	-0.13
Adjusted Net Income	-164	-79	-45	74	506
Diluted Earnings Per Share (Adjusted)	-1.60	-0.68	-0.24	0.10	0.63
Dividends Per Common Share	—	—	—	—	—
EBITDA	-103	-5	-525	-443	143
Adjusted EBITDA	-103	-5	-525	247	755

Twitter Inc TWTR (NYSE) | ★★★

Last Price	Fair Value	Consider Buy	Consider Sell	Uncertainty	Economic Moat™	Moat Trend™	Stewardship	Morningstar Credit Rating	Industry Group
44.13 USD	39.00 USD	23.40 USD	60.45 USD	High	Narrow	Positive	Standard	—	Online Media

Morningstar Analyst Forecasts

Balance Sheet (USD Mil)

Fiscal Year Ends in December

	2011	2012	2013	Forecast	
				2014	2015
Cash and Equivalents	219	203	841	1,643	1,616
Investments	331	222	1,393	1,393	1,393
Accounts Receivable	40	112	247	464	683
Inventory	—	—	—	—	—
Deferred Tax Assets (Current)	—	—	—	—	—
Other Short Term Assets	7	17	93	93	93
Current Assets	596	554	2,575	3,593	3,786
Net Property Plant, and Equipment	62	186	333	386	318
Goodwill	37	69	363	363	363
Other Intangibles	6	4	78	78	78
Deferred Tax Assets (Long-Term)	—	—	—	—	—
Other Long-Term Operating Assets	—	—	—	—	—
Long-Term Non-Operating Assets	19	19	18	18	18
Total Assets	721	832	3,366	4,438	4,562
Accounts Payable	5	8	28	29	59
Short-Term Debt	23	49	87	87	87
Deferred Tax Liabilities (Current)	—	—	—	—	—
Other Short-Term Liabilities	21	53	110	225	394
Current Liabilities	48	110	225	340	540
Long-Term Debt	21	66	111	111	111
Deferred Tax Liabilities (Long-Term)	14	12	60	60	60
Other Long-Term Operating Liabilities	5	19	21	42	74
Long-Term Non-Operating Liabilities	—	—	—	—	—
Total Liabilities	87	207	416	553	784
Preferred Stock	835	—	—	—	—
Common Stock	0	0	0	0	0
Additional Paid-in Capital	68	974	3,945	5,434	5,434
Retained Earnings (Deficit)	-270	-349	-995	-1,549	-1,655
(Treasury Stock)	—	—	—	—	—
Other Equity	0	-1	0	0	0
Shareholder's Equity	633	624	2,950	3,885	3,778
Minority Interest	—	—	—	—	—
Total Equity	633	624	2,950	3,885	3,778

Twitter Inc TWTR (NYSE) | ★★★

Last Price	Fair Value	Consider Buy	Consider Sell	Uncertainty	Economic Moat™	Moat Trend™	Stewardship	Morningstar Credit Rating	Industry Group
44.13 USD	39.00 USD	23.40 USD	60.45 USD	High	Narrow	Positive	Standard	—	Online Media

Morningstar Analyst Forecasts

Cash Flow (USD Mil)

Fiscal Year Ends in December

	2011	2012	2013	Forecast	
				2014	2015
Net Income	-128	-79	-645	-554	-107
Depreciation	24	73	111	166	333
Amortization	—	—	—	—	—
Stock-Based Compensation	60	26	600	628	613
Impairment of Goodwill	—	—	—	—	—
Impairment of Other Intangibles	—	—	—	—	—
Deferred Taxes	-2	-1	-9	—	—
Other Non-Cash Adjustments	5	8	6	—	—
(Increase) Decrease in Accounts Receivable	-33	-74	-112	-216	-220
(Increase) Decrease in Inventory	—	—	—	—	—
Change in Other Short-Term Assets	-3	-7	-12	—	—
Increase (Decrease) in Accounts Payable	-1	3	8	1	30
Change in Other Short-Term Liabilities	7	24	55	114	169
Cash From Operations	-71	-28	1	139	818
(Capital Expenditures)	-12	-51	-76	-220	-264
Net (Acquisitions), Asset Sales, and Disposals	-19	-2	-44	—	—
Net Sales (Purchases) of Investments	-294	102	-1,186	—	—
Other Investing Cash Flows	—	—	—	22	32
Cash From Investing	-325	49	-1,306	-198	-232
Common Stock Issuance (or Repurchase)	495	2	2,013	1,489	—
Common Stock (Dividends)	—	—	—	—	—
Short-Term Debt Issuance (or Retirement)	—	—	—	—	—
Long-Term Debt Issuance (or Retirement)	-15	-39	-70	—	—
Other Financing Cash Flows	—	—	—	-628	-613
Cash From Financing	480	-37	1,942	861	-613
Exchange Rates, Discontinued Ops, etc. (net)	0	0	0	—	—
Net Change in Cash	85	-16	638	802	-27

Twitter Inc TWTR (NYSE) | ★★★

Last Price	Fair Value	Consider Buy	Consider Sell	Uncertainty	Economic Moat™	Moat Trend™	Stewardship	Morningstar Credit Rating	Industry Group
44.13 USD	39.00 USD	23.40 USD	60.45 USD	High	Narrow	Positive	Standard	—	Online Media

Comparable Company Analysis

These companies are chosen by the analyst and the data are shown by nearest calendar year in descending market capitalization order.

Valuation Analysis

Company/Ticker	Price/Fair Value	Price/Earnings			EV/EBITDA			Price/Free Cash Flow			Price/Book			Price/Sales		
		2013	2014(E)	2015(E)	2013	2014(E)	2015(E)	2013	2014(E)	2015(E)	2013	2014(E)	2015(E)	2013	2014(E)	2015(E)
Facebook Inc FB USA	1.21	91.1	47.9	36.9	37.1	25.0	18.1	369.2	46.6	30.4	11.8	12.5	9.8	17.7	15.5	12.0
LinkedIn Corp LNKD USA	1.06	134.7	114.6	86.2	63.2	47.6	32.3	164.7	84.6	58.2	9.9	9.1	8.8	17.1	11.1	8.5
Average		112.9	81.3	61.6	50.2	36.3	25.2	267.0	65.6	44.3	10.9	10.8	9.3	17.4	13.3	10.3
Twitter Inc TWTR US	1.13	NM	441.3	70.0	NM	97.3	31.8	NM	NM	47.0	12.3	6.7	6.9	54.6	19.2	11.0

Returns Analysis

Company/Ticker	Last Historical Year Total Assets (Mil)	ROIC %			Adjusted ROIC %			Return on Equity %			Return on Assets %			Dividend Yield %		
		2013	2014(E)	2015(E)	2013	2014(E)	2015(E)	2013	2014(E)	2015(E)	2013	2014(E)	2015(E)	2013	2014(E)	2015(E)
Facebook Inc FB USA	15,103 USD	10.2	18.1	20.5	9.5	29.0	30.6	12.8	22.2	24.7	9.9	17.2	19.3	—	—	—
LinkedIn Corp LNKD USA	3,353 USD	1.3	-0.7	3.1	1.4	-0.7	3.0	1.5	-0.9	3.1	1.1	-0.7	2.2	—	—	—
Average		5.8	8.7	11.8	5.5	14.2	16.8	7.2	10.7	13.9	5.5	8.3	10.8	—	—	—
Twitter Inc TWTR US	3,366 USD	-20.4	-14.2	-3.1	-23.0	-15.6	-3.4	-36.1	-16.2	-2.8	-30.8	-14.2	-2.4	—	—	—

Growth Analysis

Company/Ticker	Last Historical Year Revenue (Mil)	Revenue Growth %			EBIT Growth %			EPS Growth %			Free Cash Flow Growth %			Dividend/Share Growth %		
		2013	2014(E)	2015(E)	2013	2014(E)	2015(E)	2013	2014(E)	2015(E)	2013	2014(E)	2015(E)	2013	2014(E)	2015(E)
Facebook Inc FB USA	7,872 USD	54.7	54.4	28.8	421.2	86.4	34.8	-20.6	154.1	29.3	-69.9	-593.0	54.0	—	—	—
LinkedIn Corp LNKD USA	1,529 USD	57.2	44.4	31.7	-15.9	-177.1	-445.3	742.4	9.2	33.0	-134.3	-154.5	NM	—	—	—
Average		56.0	49.4	30.3	202.7	-45.4	-205.3	360.9	81.7	31.2	-102.1	-373.8	54.0	—	—	—
Twitter Inc TWTR US	665 USD	109.8	103.6	75.5	724.9	-4.2	-68.8	-64.9	-141.0	548.9	582.2	0.6	-93.9	—	—	—

Twitter Inc TWTR (NYSE) | ★★★

Last Price	Fair Value	Consider Buy	Consider Sell	Uncertainty	Economic Moat™	Moat Trend™	Stewardship	Morningstar Credit Rating	Industry Group
44.13 USD	39.00 USD	23.40 USD	60.45 USD	High	Narrow	Positive	Standard	—	Online Media

Comparable Company Analysis

These companies are chosen by the analyst and the data are shown by nearest calendar year in descending market capitalization order.

Profitability Analysis

Company/Ticker	Last Historical Year Net Income (Mil)	Gross Margin %			EBITDA Margin %			Operating Margin %			Net Margin %			Free Cash Flow Margin %		
		2013	2014(E)	2015(E)	2013	2014(E)	2015(E)	2013	2014(E)	2015(E)	2013	2014(E)	2015(E)	2013	2014(E)	2015(E)
Facebook Inc FB USA	1,500 USD	76.2	80.0	83.0	43.9	57.0	61.0	35.6	43.0	45.0	19.1	35.4	38.0	4.8	33.2	39.6
LinkedIn Corp LNKD USA	192 USD	86.7	87.2	87.7	24.6	21.2	23.7	3.1	-1.7	4.4	12.6	10.9	11.9	10.4	13.2	14.5
Average		81.5	83.6	85.4	34.3	39.1	42.4	19.4	20.7	24.7	15.9	23.2	25.0	7.6	23.2	27.1
Twitter Inc TWTR US	-45 USD	59.9	69.0	70.0	-79.0	18.3	31.8	-95.6	-45.0	-8.0	-6.8	5.5	21.3	-11.2	-6.0	23.3

Leverage Analysis

Company/Ticker	Last Historical Year Total Debt (Mil)	Debt/Equity %			Debt/Total Cap %			EBITDA/Interest Exp.			Total Debt/EBITDA			Assets/Equity		
		2013	2014(E)	2015(E)	2013	2014(E)	2015(E)	2013	2014(E)	2015(E)	2013	2014(E)	2015(E)	2013	2014(E)	2015(E)
Facebook Inc FB USA	1,500 USD	12.8	10.0	7.8	11.3	9.1	7.2	61.7	123.7	170.5	0.4	0.2	0.2	1.3	1.3	1.3
LinkedIn Corp LNKD USA	— USD	—	—	—	—	—	—	—	—	—	—	—	—	1.3	1.4	1.4
Average		12.8	10.0	7.8	11.3	9.1	7.2	61.7	123.7	170.5	0.4	0.2	0.2	1.3	1.4	1.4
Twitter Inc TWTR US	198 USD	6.7	5.1	5.2	6.3	4.8	5.0	-46.4	55.9	170.9	0.4	0.8	0.3	1.1	1.1	1.2

Liquidity Analysis

Company/Ticker	Market Cap (Mil)	Cash per Share			Current Ratio			Quick Ratio			Cash/Short-Term Debt			Payout Ratio %		
		2013	2014(E)	2015(E)	2013	2014(E)	2015(E)	2013	2014(E)	2015(E)	2013	2014(E)	2015(E)	2013	2014(E)	2015(E)
Facebook Inc FB USA	188,140 CAD	3.82	4.59	5.86	10.71	9.95	10.47	10.71	9.95	10.47	—	—	—	—	—	—
LinkedIn Corp LNKD USA	24,569 USD	19.58	17.80	17.45	4.29	3.23	2.73	4.29	3.23	2.73	—	—	—	—	—	—
Average		11.70	11.20	11.66	7.50	6.59	6.60	7.50	6.59	6.60	—	—	—	—	—	—
Twitter Inc TWTR US	26,034 USD	4.44	2.16	2.02	11.42	10.55	7.01	11.42	10.55	7.01	9.65	18.86	18.55	—	—	—

Research Methodology for Valuing Companies

Components of Our Methodology

- ▶ Economic Moat™ Rating
- ▶ Moat Trend™ Rating
- ▶ Moat Valuation
- ▶ Three-Stage Discounted Cash Flow
- ▶ Weighted Average Cost of Capital
- ▶ Fair Value Estimate
- ▶ Scenario Analysis
- ▶ Uncertainty Ratings
- ▶ Margin of Safety
- ▶ Consider Buying/Selling
- ▶ Stewardship Rating

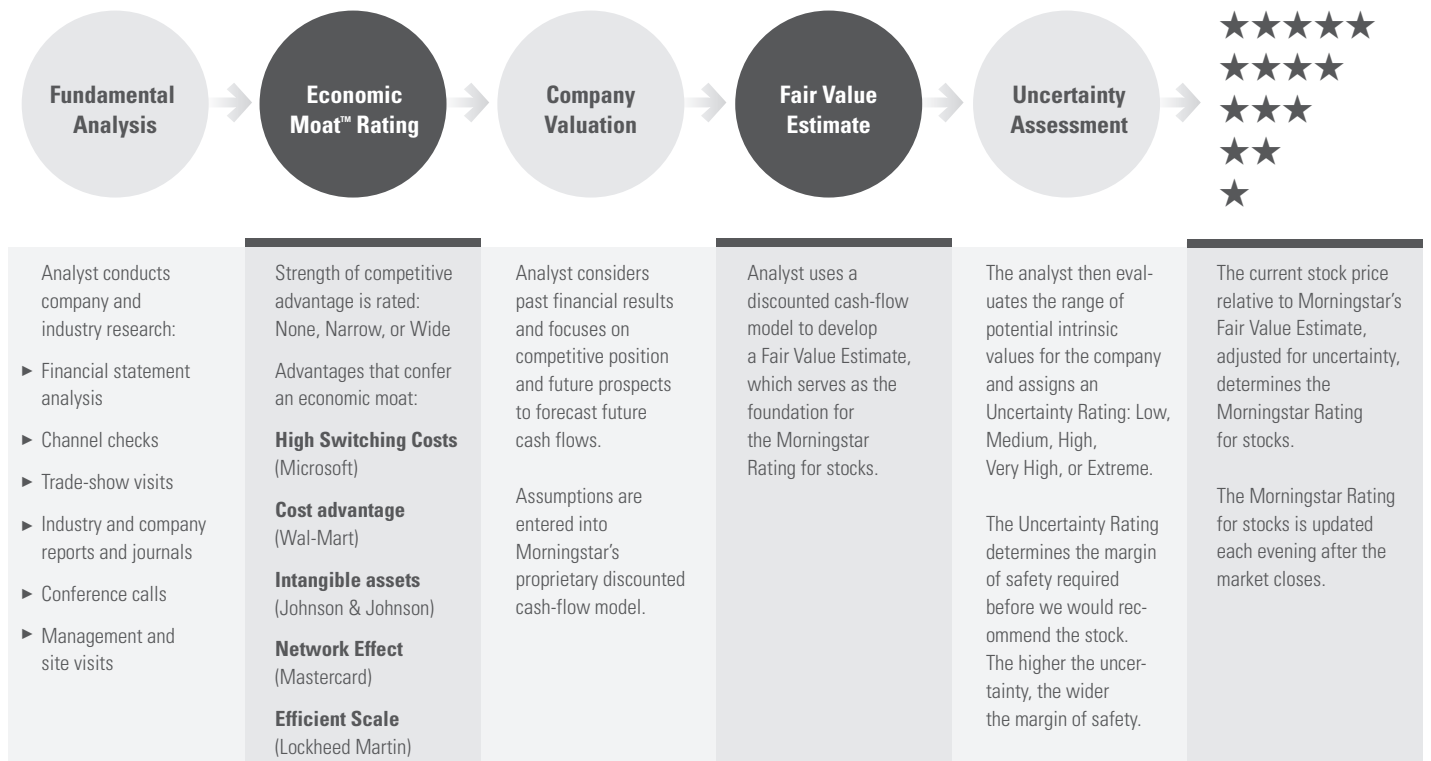
The Morningstar Rating for stocks identifies companies trading at a discount or premium to our analysts’ assessment of their fair value. A number of components drive this rating: (1) our assessment of the firm’s economic moat, (2) our estimate of the stock’s intrinsic value based on a discounted cash-flow model, (3) the margin of safety bands we apply to our Fair Value Estimate, and (4) the current stock price relative to our fair value estimate.

The concept of the Morningstar Economic Moat™ Rating plays a vital role not only in our qualitative assessment of a firm’s investment potential, but also in our valuation process. We assign three moat ratings—none, narrow, or wide—as well as the Morningstar Moat Trend™ Rating—positive, stable, or negative—to each company we cover. There are two major requirements for firms to earn either a narrow or wide moat rating: (1) the prospect of earning above-average returns on capital; and (2) some competitive edge that prevents these returns from quickly eroding. The assumptions we make about a firm’s moat determine the length of “economic outperformance” that we assume in the latter stages

of our valuation model. We also quantify the value of each firm’s moat, which represents the difference between a firm’s enterprise value and the value of the firm if no future net investment were to occur. Said differently, moat value identifies the value generated by the firm as a result of any future net new investment. Our Moat Trend Rating reflects our assessment of whether each firm’s competitive advantage is either getting stronger or weaker, since we think of moats as dynamic, rather than static.

At the heart of our valuation system is a detailed projection of a company’s future cash flows. The first stage of our three-stage discounted cash flow model can last from 5 to 10 years and contains numerous detailed assumptions about various financial and operating items. The second stage of our model—where a firm’s return on new invested capital (RONIC) and earnings growth rate implicitly fade until the perpetuity year—can last anywhere from 0 years (for no-moat firms) to 20 years (for wide-moat companies). In our third stage, we assume the firm’s RONIC equals its weighted average cost of capital, and we calculate a continuing value using a standard

Morningstar Research Methodology for Valuing Companies



Research Methodology for Valuing Companies

Detailed Methodology Documents and Materials*

- ▶ Comprehensive Equity Research Methodology
- ▶ Uncertainty Methodology
- ▶ Cost of Equity Methodology
- ▶ Morningstar DCF Valuation Model
- ▶ Stewardship Rating Methodology

* Please contact a sales representative for more information.

perpetuity formula. In deciding on the rate at which to discount future cash flows, we ignore stock-price volatility. Instead, we rely on a system that measures the estimated volatility of a firm's underlying future free cash flows, taking into account fundamental factors such as the diversity of revenue sources and the firm's fixed cost structure.

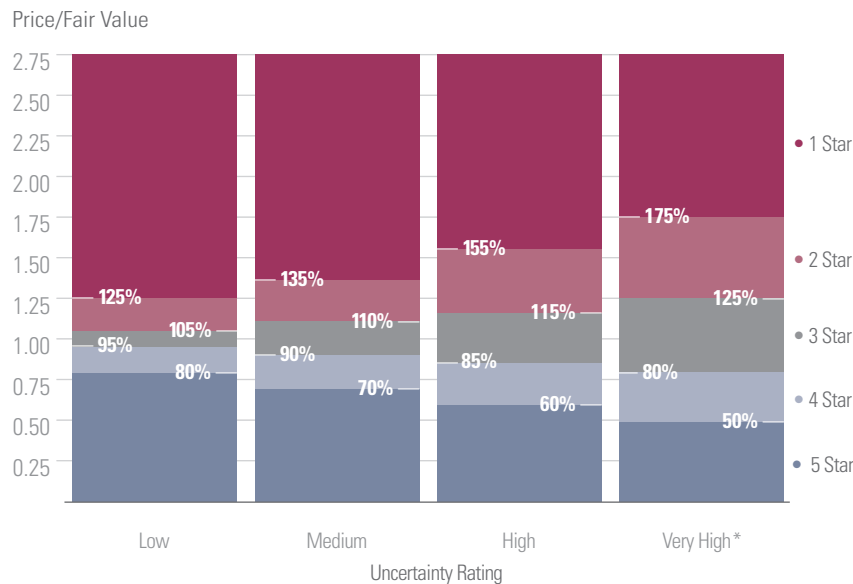
We also employ a number of other tools to augment our valuation process, including scenario analysis, where we assess the likelihood and performance of a business under different economic and firm-specific conditions. Our analysts typically model three to five scenarios for each company we cover, stress-testing the model and examining the distribution of resulting fair values.

The Morningstar Uncertainty Rating captures the range of these potential fair values, based on an assessment of a company's future sales range, the firm's operating and financial leverage, and any other contingent events that may impact the business. Our analysts use this range to assign an appropriate margin of safety—or the discount/premium

to a fair value we apply in setting our consider buying/consider selling prices. Firms trading below our consider-buying prices receive our highest rating of five stars, whereas firms trading above our consider-selling prices receive our lowest rating of one star.

Our corporate Stewardship Rating represents our assessment of management's stewardship of shareholder capital, with particular emphasis on capital allocation decisions. Analysts consider companies' investment strategy and valuation, financial leverage, dividend and share buyback policies, execution, compensation, related party transactions, and accounting practices. Corporate governance practices are only considered if they've had a demonstrated impact on shareholder value. Analysts assign one of three ratings: "Exemplary," "Standard," and "Poor." Analysts judge stewardship from an equity holder's perspective. Ratings are determined on an absolute basis. Most companies will receive a Standard rating, and this is the default rating in the absence of evidence that managers have made exceptionally strong or poor capital allocation decisions.

Morningstar Margin of Safety and Star Rating Bands



* Occasionally a stock's uncertainty will be too high for us to estimate, in which case we label it Extreme.

Morningstar’s Approach to Rating Corporate Credit

- ▶ Offers a proprietary measure of the credit quality of companies on our coverage list.
- ▶ Encapsulates our in-depth modeling and quantitative work in one letter grade.
- ▶ Allows investors to rank companies by each of the four underlying components of our credit ratings, including both analyst-driven and quantitative measures.
- ▶ Provides access to all the underlying forecasts that go into the rating, available through our institutional service.

Purpose

The Morningstar Corporate Credit Rating measures the ability of a firm to satisfy its debt and debt-like obligations. The higher the rating, the less likely we think the company is to default on these obligations.

The Morningstar Corporate Credit Rating builds on the modeling expertise of our securities research team. For each company, we publish:

- ▶ Five years of detailed pro-forma financial statements
- ▶ Annual estimates of free cash flow
- ▶ Annual forecasts of return on invested capital
- ▶ Scenario analyses, including upside and downside cases
- ▶ Forecasts of leverage, coverage, and liquidity ratios for five years
- ▶ Estimates of off balance sheet liabilities

These forecasts are key inputs into the Morningstar Corporate Credit Rating and are available to subscribers at select.morningstar.com.

Methodology

We feel it’s important to perform credit analysis through different lenses—qualitative and quantitative, as well as fundamental and market-driven. We therefore evaluate each company in four broad categories.

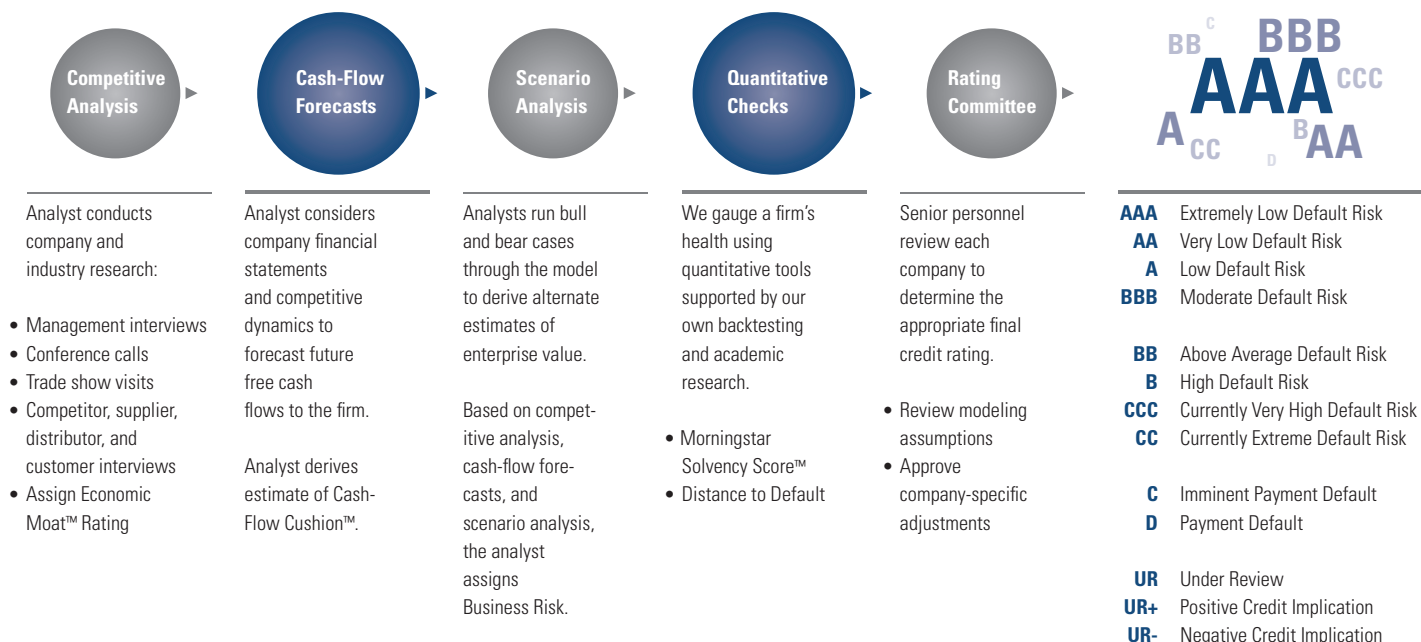
Business Risk

Business Risk captures the fundamental uncertainty around a firm’s business operations and the cash flow generated by those operations. Key components of the Business Risk rating include the Morningstar Economic Moat™ Rating and the Morningstar Uncertainty Rating.

Cash Flow Cushion™

Morningstar’s proprietary Cash Flow Cushion™ ratio is a fundamental indicator of a firm’s future financial health. The measure reveals how many times a company’s internal cash generation plus total excess liquid cash will cover its debt-like contractual commitments over the next five years. The Cash Flow Cushion acts as a predictor of financial distress, bringing to light potential refinancing, operational, and liquidity risks inherent to the firm.

Morningstar Research Methodology for Determining Corporate Credit Ratings



Morningstar's Approach to Rating Corporate Credit

The advantage of the Cash Flow Cushion ratio relative to other fundamental indicators of credit health is that the measure focuses on the future cash-generating performance of the firm derived from Morningstar's proprietary discounted cash flow model. By making standardized adjustments for certain expenses to reflect their debt-like characteristics, we can compare future projected free cash flows with debt-like cash commitments coming due in any particular year. The forward-looking nature of this metric allows us to anticipate changes in a firm's financial health and pinpoint periods where cash shortfalls are likely to occur.

Morningstar Solvency Score™

The Morningstar Solvency Score™ is a quantitative score derived from both historical and forecasted financial ratios. It includes ratios that focus on liquidity (a company's ability to meet short term cash outflows), profitability (a company's ability to generate profit per unit of input), capital structure (how does the company finance its operations), and interest coverage (how much of profit is used up by interest payments).

Distance to Default

Morningstar's quantitative Distance to Default measure ranks companies on the likelihood that they will tumble into financial distress. The measure is a linear model of the percentile of a firm's leverage (ratio of Enterprise Value to Market Value), the percentile of a firm's equity volatility relative to the rest of the universe and the interaction of these two percentiles. This is a proxy methodology for the common definition of Distance to Default which relies on option-based pricing models. The proxy has the benefit of increased breadth of coverage, greater simplicity of calculation, and more predictive power.

For each of these four categories, we assign a score, which we then translate into a descriptive rating along the scale of Very Good / Good / Fair / Poor / Very Poor.

Overall Credit Rating

The four component ratings roll up into a single preliminary credit rating. To determine the final credit rating, a credit committee of at least five senior research personnel reviews each preliminary rating.

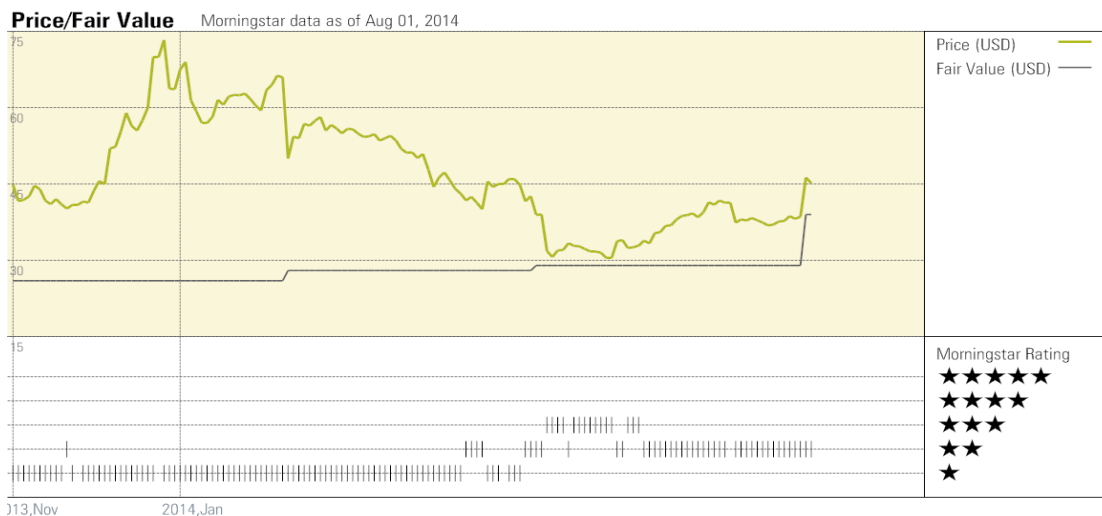
We review credit ratings on a regular basis and as events warrant. Any change in rating must be approved by the Credit Rating Committee.

Investor Access

Morningstar Corporate Credit Ratings are available on Morningstar.com. Our credit research, including detailed cash-flow models that contain all of the components of the Morningstar Corporate Credit Rating, is available to subscribers at select.morningstar.com.

Twitter Inc TWTR (NYSE) | ★★★

Last Price	Fair Value	Consider Buy	Consider Sell	Uncertainty	Economic Moat™	Moat Trend™	Stewardship	Morningstar Credit Rating	Industry Group
44.13 USD	39.00 USD	23.40 USD	60.45 USD	High	Narrow	Positive	Standard	—	Online Media



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