

## Background

Facebook has begun trialing a new advertising platform called Facebook Exchange. Currently in its testing phase, the exchange will allow brands to bid on ads targeted at specific Facebook users based upon data from third party DSP's (Demand Side Platforms). The ultimate ambition is for Facebook to drive up advertising revenue by increasing the ROI of its ad units via greater relevance, better market pricing of the ads, and/or improved monetization of their inventory. However, while third-party DSP cookie data can now be applied within Facebook, the social network will not allow the cross pollination of their personal data. In other words Facebook data can't be used to improve targeting outside of the Facebook ecosystem. Nonetheless, the new exchange represents a significant change in the way Facebook sells advertising as well as their willingness to make better use of their data.

## Details

In simplistic terms the exchange will work like the following way. A user visits a Web site (e.g., KitKat.co.uk) and interacts with some content, which is recorded on a DSP's cookie. When that user re-visits Facebook, the social platform will now recognize the DSP's cookie data and what content that user has consumed elsewhere. The DSP will then be called into action and the bids will be made with the highest bid winning. The targeting will be drawn from specific anonymous data contained with the cookie and served from the DSP. The user will be served with preloaded content from the advertiser.

The ad units will be Facebook's unique ad formats rather than IAB standards. Critically at this time the exchange will not include Facebook's premium ad units, including the recently launched mobile sponsored stories. Furthermore, the exchange will be limited to the US for now with a roll-out later this year, or early next, most likely to the UK.

## Implications

For the past six months there has been a contentious industry debate over the effectiveness and performance of Facebook inventory, particularly the premium ad units over the self-serve marketplace (e.g., is it worth five times the price?). While Facebook is testing inclusion of some premium ad units in the marketplace, the launch of the exchange won't resolve this fundamental debate given that Facebook will most likely only put a small portion of their US marketplace inventory (~5%, no premium units) into the exchange, and establish bidding parameters and controlled inventory supply to influence the price. The small and controlled scale of the current model suggests their intent to minimize any broader impact on premium pricing while starting to build data proof points around their ad unit's broader impact. One potential benefit of the new system is a better attribution model, i.e., moving beyond a "last click" model and giving Facebook ads more credit for their overall impact on a consumer journey. Facebook is surely gambling that

this is the case (or have researched it) and thus are counting on the new exchange to increase the valuation of its marketplace ads, thus perhaps closing the pricing gap with the premium ads and laying the foundation for a broader biddable combined inventory.

### **Summary**

Facebook's new offering will perhaps answer a few critics in being able to demonstrate correlation between web site visits and Facebook's ability to truly add value to its customer's bottom line. If executed well by Facebook with the user's privacy remaining protected to placate concerns, this is a very powerful advertising weapon to understand consumer behavior, convert and innovate for an advertiser. Given the controlled nature of the exchange, Facebook will carefully follow the results to make certain it doesn't destabilize their broader business, particularly given the recent IPO issues.