

MACROCOSM

DeFANGEd

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Political hysteria engulfs the FANG stocks, but there's no fundamental threat here.

[“First they came for the Socialists”](#)... then they came for the short VIX speculators... and then they came for the large-cap tech stocks. *It's the scariest phase of this correction, because those stocks have been market leadership for years.* Indeed, while after the S&P 500 corrected almost 12% from the late-January top, the cap-weighted FANG portfolio (Facebook, Amazon, Netflix, Google) corrected only 10% – and then rebounded to new all-time highs. Now, as of this writing, the FANG portfolio is down as much as 14% from *there*, to new lows for the year.

- Coming into this year, *we had been worried about “possible US antitrust action against Amazon, Google or Facebook – a political risk that we fear both parties might find common cause in triggering”* (see [“2018 Outlook: From Denial to Acceptance”](#) December 29, 2017).
- *The threat against these companies ended up coming from a different and unexpected direction – but one that is much more benign than antitrust action, which is the “nuclear option” of regulation.*
- *The hue and cry about the alleged abuse of Facebook customer data by Cambridge Analytica is powered-up by a media narrative that is able to connect the free-floating issue of data-privacy to the endless over-hyped anti-Trump hysteria. But just looking at the facts, we think it should be a simple matter for companies that use customer data to offer more robust choices to users about the collection of that data (already happening), and provide more protections against use of that data by third parties, and thus easily front-run or comply with any likely regulation along these lines.*
- We doubt very many users even care about their personal data, beyond obvious concerns about identity-theft. But even if data collection were constrained, we think that for all the high-flown tech-talk, the reality is that the vast majority of ad-targeting value is created by very simple and superficial data items (such as search-terms), which will always be able to be detected.
- Look at your own experience. How often do you even look at ads on Google or Facebook anyway – outside of the sponsored links that come up when you search for something you are interested in buying, right then and there? Of that small number, on what tiny fraction have you ever clicked, and of *that* even smaller number, how much money have you ever actually spent?

Update to strategic view

US STOCKS, US TECHNOLOGY STOCKS, US MACRO: Having outperformed throughout the present equity market correction, even making all-time highs, the FANG stocks have come in for a sudden drubbing, driven by a politically charged narrative about data abuse that we believe actually has little to do with such companies' business models. These stocks have provided leadership for years, so this is a test of the strength of sentiment as this correction drags on. Over the horizon, a more substantive potential threat – other than antitrust, which we had already identified – is the loss of the safe harbor from liability for content provided by users, afforded by Section 230 of the Communications Decency Act, and now eroded by the new Stop Enabling Sex Traffickers Act.

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- So, sure, long-standing market leadership was due for a test, and that's a test of overall confidence that could be quite consequential for sentiment and for the course of this correction. And any company has to deal with changing patterns of customer tastes and competing technologies. And say what you will about the valuations of these companies – that's another matter. *But we think it's quite an over-reaction to say that [data-driven companies' business models are fundamentally "under siege."](#)*
- Facebook is facing a unique risk if it turns out that recent data abuses violated [a 2011 consent decree](#) settling Federal Trade Commission charges that it had deceived customers by releasing data it claimed would be safeguarded. Theoretically, potential fines multiplied across millions of users could be ruinous.
- But across the sector, we think the true fundamental threat to these companies comes from something else entirely (and we don't mean antitrust which, sadly, is always a risk for any successful company).
- The [Stop Enabling Sex Traffickers Act](#) (SESTA), passed by the House on February 27 and the Senate on March 21 – now awaiting President Donald J. Trump's signature, which it seems he will provide ([Ivanka has come out in favor of it](#)) – establishes criminal liability on web sites that knowingly “promote or facilitate the prostitution of another person.”
- *The important thing here is that SESTA specifically overrides [Section 230 of the Communications Decency Act of 1996](#), which had specifically provided a safe harbor against such liability, by deeming web sites to be mere conduits of the words of their users; that is, they shall not “be treated as the publisher or speaker of any information provided by another...”*
- *Section 230 means that, like telephone and other communications firms before them, social media companies don't have to bear the crippling costs of monitoring every message they carry for potentially liability-creating content – or when such monitoring inevitably fails, bear the potentially open-ended costs of civil or criminal liability. Losing the safe harbor of Section 230 would indeed put these firms' business models fundamentally under siege. If you want something to worry about, SESTA – which was passed over [the concerted objections of the Internet industry](#) – could be seen as the thin edge of the wedge.*
- Such concerns are legitimate, but they are for the future, one headline at a time. For now, we think the travails of the FANG stocks – juiced up by politically-charged narratives about data abuses that don't truly go to the heart of the companies' business models – are just another necessary and expectable symptom of the long-overdue equity correction we are enduring.

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Recommended Reading

[Saving the heartland: Place-based policies in 21st Century America](#)
Benjamin Austin, Edward Glaeser and Lawrence Summers
Brookings Institution
March 8, 2018

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Bottom line

Having outperformed throughout the present equity market correction, even making all-time highs, the FANG stocks have come in for a sudden drubbing, driven by a politically charged narrative about data abuse that we believe actually has little to do with such companies' business models. These stocks have provided leadership for years, so this is a test of the

strength of sentiment as this correction drags on. Over the horizon, a more substantive potential threat – other than antitrust, which we had already identified – is the loss of the safe harbor from liability for content provided by users, afforded by Section 230 of the Communications Decency Act, and now eroded by the new Stop Enabling Sex Traffickers Act. ▶

Note: This report was amended after initial release to reflect the risk to Facebook of FTC-imposed fines.