Protracted CEO Search Passes 100 Days

Investors Growing Impatient - Turning Attention to the Board

Over 100 Days is Too Long. Several weeks back, we thought the CEO search was finally coming to an end and that a decision was imminent — we were wrong. Conversations we had with industry participants indicated that Jack Dorsey was the most logical choice, particularly with no “superior” external candidate surfacing. We are stunned that we have now passed over 100 days since the announcement of the former CEO’s resignation, particularly since the board had discussions with him about stepping down since Dec. 2014. Feedback we hear from investors is that the process has taken too long.

Investors Now Focusing on The Board. Investors are now focusing on the cause of protracted process, with eyes turning towards the board and search committee. We understand that it is paramount that a diligent and thorough search process is conducted; however investors are now questioning if the board’s lengthy search has become detrimental. We continue to see 2 key risks as this drags on: 1) continued brain drain; 2) waning advertiser confidence.

What’s the Hold Up? At this point, some investors believe the board needs to come to terms with having a CEO who is also CEO of another company. We think this is less of an issue for several reasons: 1) Mr. Dorsey is seen as a leader and is well respected inside and outside of Twitter; 2) He has been running the company since July and we’ve already seen his fingerprints in faster product rollout (Commerce via DM, instant articles, etc.); 3) We think some senior execs would only work for him vs an outsider; and 4) We think Mr Dorsey as CEO is expected and supported by shareholders at this point.

Pressure Building on Board. We think it’s inevitable that once the new CEO is established, the board will be rejiggered for several reasons: the sudden CEO departure; the lengthy search process; and initial delays in product roll out. We think active involvement and stock ownership by these directors is critical (see table). Based on this, we think 2 of the 8 board members, are more likely to move on: Peter Currie (leading the CEO search, low ownership & activity) and Marjorie Scardino (low ownership & activity). We would look for the company to put more expertise on the board in media, tech, and operations.

Basis of Our Buy Recommendation. We upgraded TWTR to Buy from Neutral on August 31st, based on the washed out sentiment, combined with a series of expected positive catalysts. Importantly, our upgrade was predicated on a quick mgmt. clarification and execution — this remains critical and timely. Our $38 PT is ~5.5x EV/revenues and ~18x EBITDA, vs. growth rates of ~40% and ~55%.
BOARD ACTIVITY AND OWNERSHIP

We think that given the company's turnaround position, it is imperative that the board members show engagement in the product (i.e. activity) as well as have some “skin in the game” in the form of equity ownership. Below we look at 2 main metrics: 1) the number of lifetime tweets of each board member (as a proxy for engagement); and 2) total equity ownership. While we know that tweets are not a perfect representation of engagement, we do think it is a fair analog and is instrumental in not only understanding the current product but also understanding where the product needs to evolve. For stock ownership, we always like to see management and directors have equity exposure in kind with investors to underscore alignment of interests. Further, directors buying sizable positions would be comforting for investors in their confidence in the future. Based on this table, we think the directors with the least activity and exposure are more susceptible to move on after a CEO is chosen.

<table>
<thead>
<tr>
<th>Board Member</th>
<th>Lifetime Tweets</th>
<th>Fully Diluted Shares</th>
<th>Direct Shares</th>
<th>Options / Indirect Shares</th>
<th>% O/S</th>
</tr>
</thead>
<tbody>
<tr>
<td>Peter Currie</td>
<td>98</td>
<td>383,581</td>
<td>23,581</td>
<td>360,000</td>
<td>0.003%</td>
</tr>
<tr>
<td>Peter Fenton</td>
<td>1,026</td>
<td>1,008,038</td>
<td>1,008,038</td>
<td>-</td>
<td>0.149%</td>
</tr>
<tr>
<td>Ev Williams</td>
<td>7,744</td>
<td>46,560,601</td>
<td>46,560,601</td>
<td>-</td>
<td>6.885%</td>
</tr>
<tr>
<td>Jack Dorsey</td>
<td>17,300</td>
<td>23,856,513</td>
<td>21,856,513</td>
<td>2,000,000</td>
<td>3.232%</td>
</tr>
<tr>
<td>Dick Costolo</td>
<td>9,403</td>
<td>8,131,529</td>
<td>436,634</td>
<td>7,694,895</td>
<td>0.065%</td>
</tr>
<tr>
<td>David Rosenblatt</td>
<td>265</td>
<td>377,625</td>
<td>27,625</td>
<td>350,000</td>
<td>0.004%</td>
</tr>
<tr>
<td>Marjorie Scardino</td>
<td>8</td>
<td>14,352</td>
<td>14,352</td>
<td>-</td>
<td>0.002%</td>
</tr>
<tr>
<td>Peter Chernin</td>
<td>527</td>
<td>200,000</td>
<td>200,000</td>
<td>-</td>
<td>0.030%</td>
</tr>
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Search Committee

Source: FactSet; Company Reports; STRH
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Legend for Rating and Price Target History Charts:

D = drop coverage
I = initiate coverage
T = transfer coverage
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<tr>
<th>Coverage Universe</th>
<th>Investment Banking Clients Past 12 Months</th>
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<tr>
<td>Rating</td>
<td>Count</td>
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<tr>
<td>Buy</td>
<td>326</td>
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<tr>
<td>Neutral</td>
<td>245</td>
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<tr>
<td>Sell/Reduce</td>
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