Monetising social networks

Tweeting all the way to the bank

Jul 23rd 2009 | SAN FRANCISCO
From The Economist print edition

Can virtual communities make billions of dollars from their millions of connections?

Illustration by Claudio Munoz

WHENEVER the founders of Twitter, a social-networking service, have been asked about how much revenue they expect to generate from their creation, they have politely deflected the question. So when a hacker recently leaked documents after gaining access to the private e-mail accounts of a Twitter employee and the wife of one of its founders, the blogosphere was abuzz. The haul included a spreadsheet showing revenues reaching $140m by the end of 2010, up from $4.4m this year. Twitter dismissed the document as out of date, but it showed the firm's owners believe it has the potential to mint serious money.

Their confidence is not surprising: Twitter is now thought to have around 23m users. Other social networks have also been piling on members. Facebook, one of the biggest networks along with News Corporation's MySpace, has seen membership leap from 100m in August 2008 to some 250m today. With the number of people online worldwide expected to go from 1.5 billion today to 2.2 billion by 2013, according to Forrester Research, many of these networks will grow like Topsy.

They will also have a profound influence on consumer behaviour, prompting firms to shift a hefty chunk of their marketing budgets in their direction. That prospect has investors salivating. Marc Andreessen, a well-known Silicon Valley figure with stakes in both Twitter and Facebook, believes Facebook's revenues will amount to billions of dollars in five years' time, up from about $500m this year. A recent investment in Facebook by a Russian firm valued it at $6.5 billion. Other venture capitalists have been ladling cash into start-ups developing software applications for these online communities.

Yet some experts point out that although social networks have captured the popular imagination, the managers running them face a delicate balancing act. They need to reconcile a desire to drive up membership as fast as possible—which increases the value of a network to both existing and potential members—with the need to experiment with ways of raising money to fund long-term growth. If they push too hard for revenue in the short term, they might drive away users, undermining a network. Leave it too late to monetise and the business could collapse.

MySpace, which was bought by News Corp in 2005, offers a cautionary tale. It grew rapidly from its origins as a site focused on members' musical interests into a more eclectic network. But as it expanded, it spent too much time chasing revenue and too little improving its online offerings. Now it is bleeding users and advertising: eMarketer, a research firm, estimates that MySpace will bring in $495m of ad revenue from America this year, 15% less than in 2008. In June Owen Van Natta, the site's new boss, announced plans to cut hundreds of jobs at the bloated operation. He is widely expected to return MySpace to its roots in entertainment.

Executives at other networks stress that their priority is keeping users happy. But they acknowledge that the recession has sharpened interest in generating revenue. Some sites, such as LinkedIn, a professional network that helps its members further their careers, already boast healthy revenue streams. As well as selling job advertising, the site charges users a premium for some career-related services and firms for the use of proprietary software that helps them identify promising candidates. To LinkedIn the downturn is an opportunity to pinch business from weaker rivals, explains Steve Sordello, the chief financial officer of the company, which has been profitable since 2007.

Broader-based social networks such as Facebook and Twitter are reluctant to charge users fees. Instead Facebook is focusing its attention on driving many more marketing dollars to its site. There is a big opportunity here. After all, only a small fraction of marketing budgets are dedicated to social networks today. The networks also have plenty of useful data about their users' likes and dislikes.

But they have one big drawback. Users typically want to hang out with their pals when they are online and so tend to ignore advertisements pushed at them while they are gossiping. The social networks are therefore considered less effective marketing vehicles than search engines such as Google, whose users are seeking information on specific subjects and are more likely to click on ads relevant to their interests. This helps to explain why advertisers will only pay a pittance for page views on many social networks.

To address this issue, Facebook is experimenting with a host of ad formats that enable firms to strike up online conversations within social networks—without tarnishing users' experience, it hopes. Facebook is also targeting e-commerce revenues. These are already a big source of income for some Asian social networks, which take a cut on deals for everything from electronic greeting cards to digital games. In June Facebook launched a

stored-credit system that allows users to pay easily for digital goods and services on the site, which pockets a small commission on each transaction. Sheryl Sandberg, Facebook's chief operating officer, says that thanks to its advertising and e-commerce initiatives the social network is on track to increase revenue by 70% this year.

What about Twitter? Embedding advertisements in "tweets", short text messages that can be up to 140 characters long, is unlikely to appeal to users. A better bet would be for the firm to charge corporate users for premium services. For example, it could pocket a fee from businesses for verifying their Twitter accounts, so that users following their postings would know the firms' tweets are genuine. It could also develop a statistical toolkit that measures the effectiveness of tweets in generating sales.

Some analysts have warned that if social networks do not get smarter at generating revenue themselves, they risk seeing the best money-spinning opportunities siphoned off by those venture-backed start-ups. By some estimates, developers working on Facebook applications may pull in as much revenue this year as the site itself. In a report published in May, ContentNext Media, a research firm, concluded that Facebook should think of itself as a shopping mall and start charging developers "rent" to be on its platform. Twitter might ultimately want to follow suit. Such a move could bring in plenty of cash, even if it does appear a bit, er, anti-social.

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