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VENTURE CAPITAL INVESTMENTS IN SOCIAL MEDIA

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Abstract

The purpose of this thesis is to analyze business model innovation in the social media industry. This industry of extraordinary growth and continuous technological development is driven by high level of investment from venture capitalists in their quest to find the next Facebook or the next Instagram. By conducting case studies on seven successful venture capital founded social media companies we want to map key similarities and differences in their business models. By creating a theoretical framework; the 7 Factor Model and combining it to the Business Model Canvas we identify scalability, uniqueness, loyalty, profitability, sustainability, mobility and inimitability as key value drivers. Based on our findings from the case studies we conclude that the design of business model influences the success of a social media start-up company and state that business model innovation is an important issue for these companies to react and gain competitive advantage in a world of constantly changing condition.

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1. Introduction

1.1. Foreword

Social media shapes events and culture all around the world. From the Arab spring to the international Occupy movement, citizens of all countries are now more able than ever before to affect the society. By communicating their message through social media, individuals have rallied crowds of millions, generated massive views and overthrown political administration. The social media and mobile technologies have grown faster than anyone could have anticipated. To observe these two technologies one only has to walk down a street and see where people are looking. Most likely it is on their smartphone checking out a mobile social media application. The business environment has also changed due to social media. Businesses have new social strategies, all information is easily accessible, customers are more engaged and the power of word of mouth can make or break a business in just few days. Something that did not exist last year, people are taking for granted this year. That is the speed of social.

1.2. Problem formulation

One of the most powerful forces that have helped establish the social media industry is the venture capitalists that have supported the high-risk, potentially high-reward start-up companies with both financial and operational contributions until they have reached a sufficient size so that they can be exited with a satisfying return on investment.

Given that most of these start-up companies share certain characteristics at their early stage that make them strikingly similar, the critical challenge for venture capitalists is to select the companies with the highest growth prospects to invest in. In many cases the only differentiator is how these companies generate revenue through their business model. As Chesbrough (2007) put it: “It is not just about technology anymore. Today's innovation must include business model as a better business model will often beat a better idea or technology.”

As the social media industry is still naive, the need for business model innovation is high as most of the start-up companies are still seeking ways to become successful in the virtual world. Thus, they all employ different kinds of business models that capture the logic of how they do business, with diverse success.

Therefore, the interesting overall research question arises of:

How does the design of business model influence the success of a social media start-up company?

In this thesis, we seek to answer the above question by studying business model innovation in successful social media start-up companies. The purpose of this thesis is to map key similarities and differences from these success stories and learn from their experiences. This knowledge of what characterizes a successful business model in social media can then be contributed to the investment criteria that venture capitalists apply when screening potential candidates for investment.

1.3. Thesis approach

Research on business model innovation in start-up companies and investment criteria of venture capitalists is by no means untouched as of this date, since many articles and academic studies have discussed the subjects for years.

However we find that most of these studies focus on business model innovation in a more general setting and articles found on venture capital concentrate on the venture capital industry performance by looking at the venture capital fund overall strategies and returns. Moreover, studies that focuses explicitly on business model innovation in social media or other virtual industries concentrate mainly on the monetary element of a business model rather than looking at the different value drivers as a whole. In addition, scientific evidence of how business models should be evaluated and how they should influence the investment criteria of venture capitalists is rare.

Because of this research gap, we recognized the opportunity to gather all the secondary data available on these subjects into this thesis and to complement it with our own building of theoretical framework and analysis. The thesis will take a case based approach by analyzing business models in some of the best known venture capital founded social media companies in the world. Due to this approach, the academic foundation of this thesis does not use a deep theoretical framework. Instead it is motivated by a practical application of the theoretical framework.

Our findings should therefore be highly interesting for parties, such as venture capitalists, start-up companies and academics interested in business model innovation and how venture capitalists can screen for successful business models in social media.

1.4. Research strategy

Our research strategy consists of building theoretical framework, performing comprehensive analysis and conducting case studies.

Building a theoretical framework requires a qualitative research that covers the academic literature that is available on the investment criteria of venture capitalists. Our study is focused towards the business model due diligence to identify factors that venture capitalists value when assessing business models.

When assessing social media start-up companies, we find it essential to identify the different value drivers that influence the business models, as we consider these factors to have interconnected effect on the success or failure of these companies. We then introduce a 7 Factor Model that has been put together for this very purpose and combine it to the Business Model Canvas framework. The purpose of this application is to create a practical evaluation tool to use for business model analysis of the thesis case subjects.

This is followed by a comprehensive analysis of the dynamics in the venture capital industry and discussion of why social media has become such popular phenomenon for consumers and such attractive investments for venture capitalists. We will then study business model innovation in social media in more detail and provide an overview of the main monetization models that are present in the industry today.

Our aim is to provide a summary of the following:

- Why do venture capitalists invest in social media?
- Why is there a need for business model innovation in social media?
- How do the business models in social media differ from each other?

Based on our findings, we conduct case studies on companies that have all received venture capital financing. Overall rating of these business models and key learning from each case is consolidated in a sub conclusion that will seek to summarize the following:

- How interconnected are the different value drivers in the business models?
- Why is there usually only one winner in each market segment in social media?

There we should have answered the overall research question of how the design of business model influences the success of a social media start-up company.

The last part of this thesis aims to give an outlook concerning the future status of the case subjects in the social media industry and a conclusion on how our findings can contribute to the investment criteria of venture capitalists.

1.5. Case study design

There are many ways of conducting research and case studies are just one of them. Case studies are the preferred strategy when *how* or *why* questions are being answered, when the investigator has little control over events, when the focus is on a contemporary phenomenon within its real-life context and when multiply sources of evidence are used (Yin, 2003).

As how and why events took place are important questions in our research, we decided to use case studies as they are ideal for our research strategy to contribute to our analysis of business models in social media companies.

The companies selected for the case studies, represent a pre-defined market segment in social media. These market segments and companies are analyzed in the following order, based on the date of establishment:

- Professional Network: **LinkedIn**
- Social Network: **Facebook**
- Video Sharing: **YouTube**
- Micro-blogging: **Twitter**
- Blogging: **Tumblr**
- Photo sharing: **Pinterest**
- Mobile photo sharing: **Instagram**

We conducted our analysis of these seven companies by looking at their business models systematically, collecting data, analyzing the data using our theoretical framework and interpreting the findings (Yin, 2003). As seen in Figure 1, the companies are present at different stages of their lifecycle and thus the event window is in real time to reflect on the business models at their current stage.

Case company	Founded	Current stage
LinkedIn	2002	Public as of IPO in 2011
Facebook	2004	Public as of IPO in 2012
YouTube	2005	Acquired by Google in 2006
Twitter	2006	In late stage financing
Tumblr	2007	In late stage financing
Pinterest	2010	In early stage financing
Instagram	2010	Acquired by Facebook in 2012

Figure 1: Case companies and event window for analysis

1.6. Validity and Generalization

Independent scientific knowledge on the social media industry is difficult to discover. Most of the accessible information is either in the form of newspaper articles and online blogs or enclosed in the company's financial statements and investor memorandums. Consequently, great deals of the secondary data sources that are used for this thesis are not scientifically reviewed. We have strived to use as credible data sources from as much acknowledged sources as possible but recognize the fact that some data could be biased towards the people, organizations, and companies in question and thus limits the validity of this data.

Multiple case studies give us an opportunity to get a more holistic and more dynamic picture of business models in social media. We believe that the selection of the seven companies used in the case studies are appropriate for generalization as each of them represents a particular market segment in social media. We strived to study and learn from the companies that succeeded in the industry. Learning can then be used across market segments and for new companies that will enter the social media industry. However we are aware that a larger sample might give a more significant conclusion.

1.7. Delimitation

The lack of primary data limits the scope of this project. We only use secondary data because primary data for analyzing the case subjects are greatly out of reach. We also decided not to speak to venture capitalists as this would be beyond the scope of this project. This is the first step to building the tool. Next step would be to take it to work and involve venture capitalists.

We reckon that there can be many factors that contribute to the success of social media start-ups and the business model is just one of them. We however show that a business model can be a decisive factor for start-up companies as the other factors can be quite similar. Thus, to focus on the particular importance of the business model, other factors will only be taken into consideration where relevant for the purpose of this thesis.

Statistical testing of the model was not carried through, as it would have required a larger data set, which was unattainable. Tax issues, legal issues and society matters are also out of the scope of the thesis.

1.8. Thesis structure

Figure 2 demonstrates how this thesis is organized:

Figure 2: Thesis structure

2. Theoretical framework

2.1. Empirical evidence

Investment criteria have been studied extensively over the years as well as their relative importance in the eyes of venture capitalists. Most sources indicate management team as the criteria venture capitalists place particular importance on (Franke, Gruber, Harhoff & Henkel, 2008). Many sources also state the importance of market drivers (Suarez & Lanzolla, 2007), product service offering (Mason & Stark, 2004) and the financial returns to be expected (Franke et al., 2008). Weiss (2010) pointed out that there is not sufficient research available on business models as source of information for investment decision-making. However his investigation found that business models are indeed analyzed in business practice, just not explicitly or as a structured process but rather in a way that connects with other units of analysis.

Hamel (2000) was one of the first academics to create an evaluation approach for business models. According to his research a business model consists of four key elements; customer interface, core strategy, strategic resources and value network. The quality of business models can then be measured by applying the following criteria; efficiency, uniqueness, fit and profit boosters.

Amit & Zott (2001) took this approach one step further. Their findings imply that the business model describes the content, structure and governance of transactions designed so as to create value through the exploitation of business opportunities. They identify four sources of value creation; novelty, lock-in, complementarities and efficiency. Moreover, in a later research Zott & Amit (2007) find that novelty-centered and efficiency-centered business models have a positive impact on entrepreneurial firms.

Morris, Schindehutte, Richardson & Allen (2006) state in their research: “Limited progress has been made in establishing criteria for evaluating models or their underlying components.” Subsequently they suggest the following criteria for evaluating the overall business model: uniqueness, profit potential, internal consistency, comprehensiveness, inimitability, robustness, adaptability and sustainability.

Weiss (2010), developed an evaluation instrument that would facilitate business model due diligence during venture appraisal. His framework is equipped with evaluation criteria that has been put together resulting from literature review; lock-in, uniqueness, efficiency, profitability, inimitability, adaptability, fit, novelty, robustness and complementarities, and complemented by criteria attained from interviews with venture capitalists; scalability, patentability, plausibility and completeness. His evaluation framework was then tested on a German venture capital fund that ranked the criteria based on importance and relevance.

2.2. Business Model Canvas

Osterwalder and Pigneur (2010) define a business model as a conceptual tool that describes the rationale of how an organization creates, delivers and captures value. The Business Model Canvas is a tool to evaluate both the business model environment on the one side and the business model itself on the other side. Moreover, in a complementary two-fold approach, a SWOT analysis is applied to the business model as a whole.

The Business Model Canvas is described with nine basic building blocks that show how the organization plans to make money. These building blocks cover the four main areas of a business, namely: customers, offer, infrastructure and financial viability.

Customers

- **Customer Segments:** The customer segments define the customer that the business is planning to reach and serve. There are many possible types of segments:

  Mass market: The business focus on one large group of customers with no distinguishes.

  Niche Market: The business model targets specific customers with specific characteristics.

  Segmented: Some models add additional segments to their customer segments e.g. based on income, gender or age.

  Diversify: A business that uses diversified customer business model targets more than one specialized segment with different needs.

  Multi-sided platform: A business serves two or more independent from the same customer segment

- **Customer Relationships:** Identify the type of relationship a business wants to establish with their customer segments. Customer relationships can include personal assistance, dedicated personal assistance, self-service, automated, communities or co-creation.
- **Channels:** Describe how the business communicates and delivers their value propositions to their target customers.

Offer

- **Value propositions:** Includes business' products and services that create value for its customers and pleases their needs. The value propositions are what differentiate the business from its rivals. Values may be quantitative, e.g. price and speed of service or qualitative, e.g. design or customer experience. Elements that can create value for customers are e.g. newness, performance, customization, getting the job done, design, brand, price, cost reduction, risk reduction, accessibility and usability.

Infrastructure

- **Key resources:** Every business needs key resources to be able to create and offer value propositions to their customers. These key resources can be physical, financial, intellectual or human.
- **Key activities:** Are the most important activities of businesses to operate effectively. These activities can be production, problem solving and platform/network.
- **Key partnerships**: Network of suppliers and partners that optimizes the business model and reduces risks and uncertainties. This can for instance be through joint venture and strategic alliances.

Financial viability

- **Revenue streams:** Shows how the business plans to make an income from the different customer segments. There are few possible ways to generate revenue streams, which might have a different pricing mechanism. These include: asset sale, usage sale, subscriptions fees, lending/renting/leasing, licensing, brokerage fees and advertising.

- **Cost structure:** Describes the most important costs in the business model. Costs can be cost driven or value driven. It features fixed costs, variable costs, economics of scale and economics of scope.

The Business Model Canvas Template is demonstrated in Figure 3 where customers are highlighted with green color, offer with blue color, and infrastructure with orange color and financial viability with purple color.

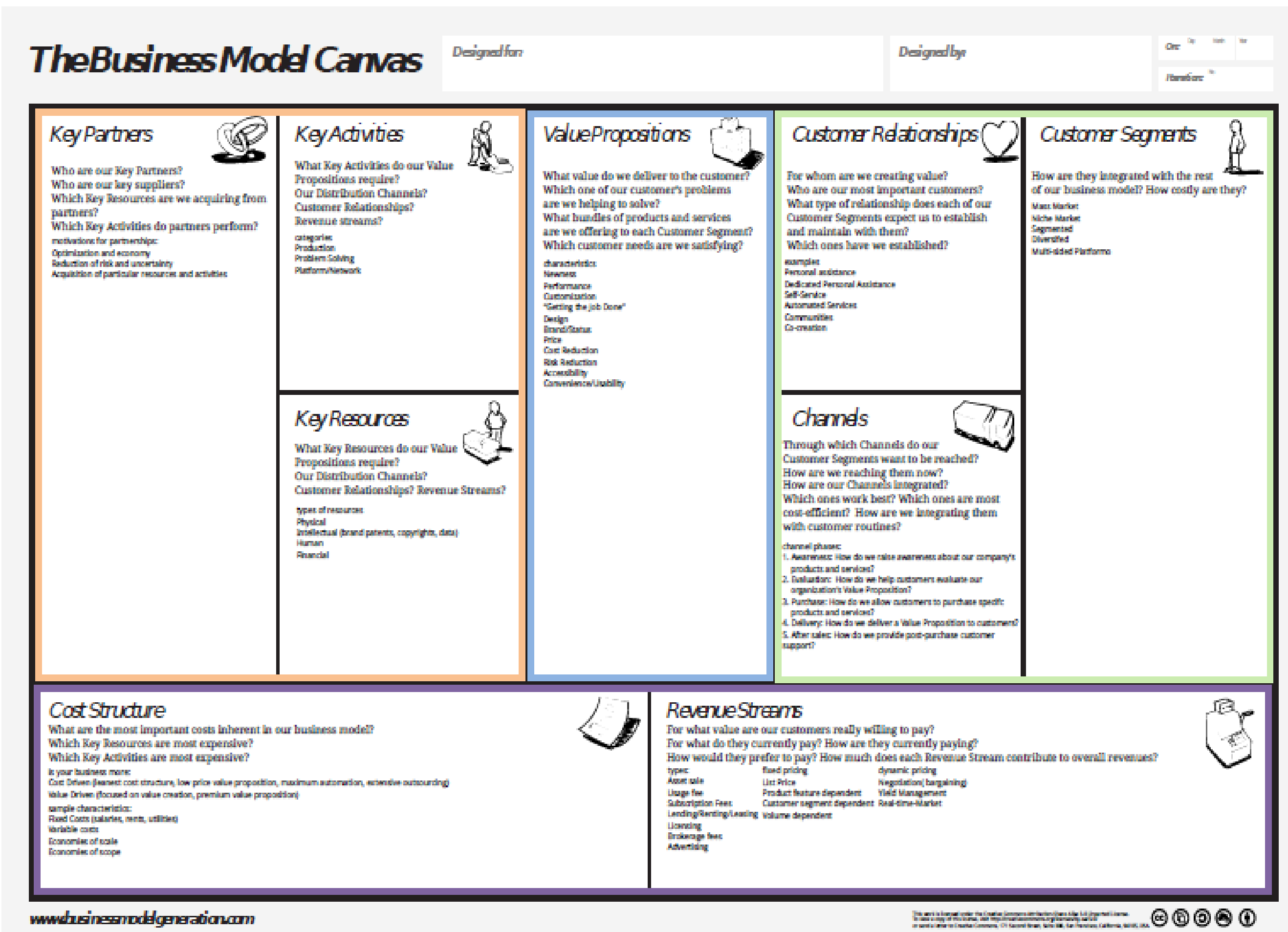

Figure 3: Business Model Canvas Template

2.3. The 7 Factor Model

Inspired by existing framework we want to combine the most notable criteria in a practical evaluation instrument.

Results from Weiss's (2010) testing on a German venture capital fund, showed that the criteria that venture capitalists put the highest *importance* and *relevance* on are scalability, lock-in, uniqueness, efficiency and profitability. But the other tested factors also got their share of attention. We noted that some of the tested factors share certain characteristics that make them difficult to distinguish and thus needed alternation.

After a thorough analysis of all tested factors we have identified the following seven factors that we believe are the most relevant in a venture capitalist assessment of social media start-up companies. These factors are summarized in Figure 4:

7 Factor Model	Weight	Inspired by existing framework	Research Source
Scalability	25%	Scalability, Fit	Weiss (2010), Hamel (2000)
Uniqueness	20%	Uniqueness, Novelty	Hamel (2000)/ Morris et al. (2006), Amit & Zott (2011)
Loyalty	15%	Lock-in, Complementarities	Amit & Zott (2011)
Profitability	15%	Profitability	Hamel (2000)/ Morris et al. (2006)
Sustainability	10%	Efficiency, Plausibility	Hamel (2000)/ Amit & Zott (2011), Weiss (2010)
Mobility	10%	Adaptability	Morris et al. (2006)
Inimitability	5%	Inimitability, Robustness, Patentability	Morris et al. (2006), Weiss (2010)

Figure 4: The 7 Factor Model

For the purpose of this thesis, the weight of each factor in the 7 Factor Model has been determined by looking at Weiss's (2010) results and by adjusting their mutual importance and relevance so they will reflect better, our own perception, on the social media industry. Hence we perceive some of the factors to be more important than others, therefore it would not be fair to put the same weight on all factors.

To transform the 7 Factor Model into a practical evaluation instrument we combine it to the Business Model Canvas. This framework was chosen as it is the most recent framework available in the business model innovation landscape. Published in 2010 it has been very well received in the business community and is already widely used by organizations. Moreover, we find the design and purpose of the model well fitted for analysis of social media start-up companies as these companies are constantly evolving as they grow.

The following subsections will describe each factor in the 7 Factor Model in more detail, explain how they have been linked to the Business Model Canvas as well as their individual importance and relevance in a venture capital setting.

2.3.1. Scalability

Venture capitalists will want to invest in solutions for significantly large target markets. Scalable infrastructure supports the possibility to enlarge customer base by expanding into new customer segments or new geographical regions. So the company can grow quickly and manage the scale necessary to maximize the size of its market opportunity, there must be high internal consistency between the company's key resources, key activities and key partners that fit well together and reinforce each other.

2.3.2. Uniqueness

Something in the company's value proposition is new or distinctive in ways that are valued by customers. Venture capitalists prefer to invest in first of a kind new idea that have these proprietary features that distinguish them from competitors and gives them competitive advantage in their market segment.

2.3.3. Loyalty

Customers stay loyal because they love the product or service offered or because it is difficult or painful to leave or switch. The company has efficiently segmented its customer base and provided each segment with appropriate customer relationships that meet the needs and wants of customers. Companies that are able to execute this well are favored by venture capitalists.

2.3.4. Profitability

Financial viability is in place as company is generating revenues, or is expected to be generating future revenues, that are greater than costs. Venture capital investment is dependent on the company's ability to exceed financial indicators.

2.3.5. Sustainability

Company is efficient as it offers customers products and services that are cheaper, faster, of better quality and on average simpler. Moreover, the company is built on a strong foundation and forecasts for the future are plausible and well supported with reliable data. Consequently the company has promising operational strategy in place that shows specific steps it will take to achieve a successful exit for the venture capital. Thus venture capitalists perceive the company as sustainable.

2.3.6. Mobility

Company is flexible as it allows adaption of business model if required due to changes in its environment, such as if technology advances. That includes the possibility of increasing business productivity by reaching out to customers through different channels than originally intended. Venture capitalists desire to invest in a proven and verifiable technology that makes this possible.

2.3.7. Inimitability

Infrastructure is difficult to imitate, because of resources, activities, partnerships, patents and reputation. This motivates venture capital investments as the company is robust and able to fend off threats well. Consequently, there are high barriers of entry into the given market segment.

2.3.8. The 7 Factor Model Score

The strength of the factors in the 7 Factor Model can be assessed by applying the following numerical scale:

1 *Poor or nonexistent*, **2** *Fair*, **3** *Good*, **4** *Very good*, **5** *Excellent*

Assessment will be based on interpretation of our findings in the case studies.

2.4. Combined evaluation framework

The combined 7 Factor Model and Business Model Canvas framework is illustrated in Figure 5 below:

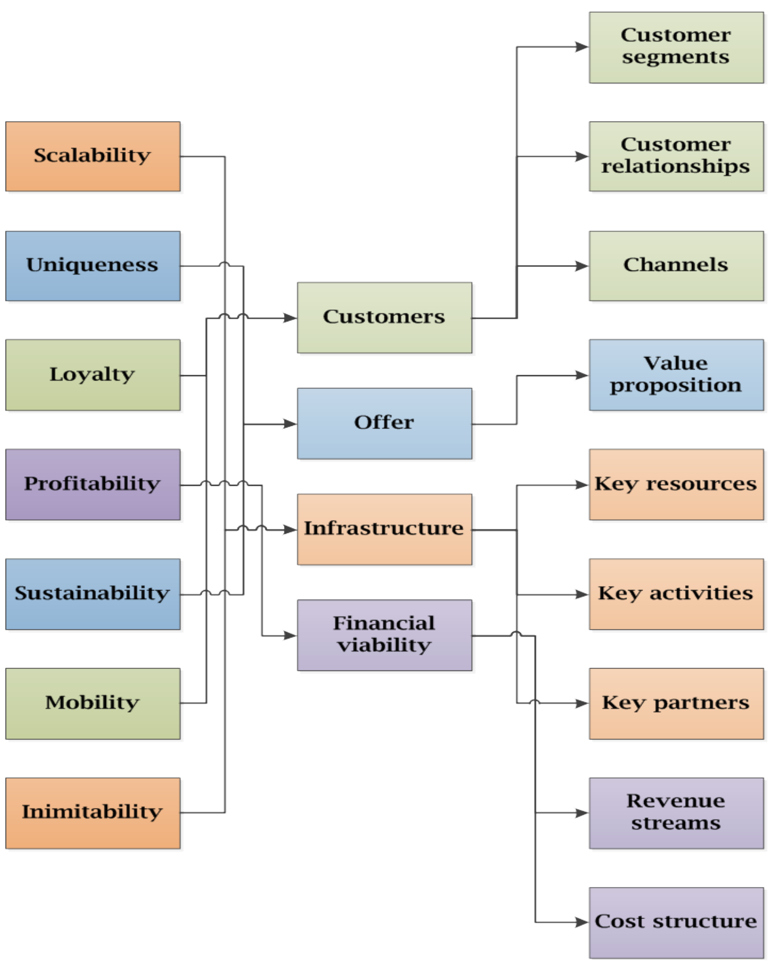

Figure 5: Combined evaluation framework of Business Model Canvas and the 7 Factor Model

3. Venture Capital

3.1. What is venture capital?

Venture capital is as an important intermediary in financial markets, providing capital for start-up companies that might otherwise struggle attracting financing. It can be defined as professionally managed capital that is provided to high risk start-ups with perceived long-term growth potential (Investopedia, 2012). These companies are usually small and young, with high level of uncertainty, possess few fixed assets and operate in market segments that change very rapidly. Venture capital funds finance these high-risk, high-growth companies, by purchasing equity or equity-linked stakes while the companies are still privately held (Gompers and Lerner, 2001).

3.2. Industry dynamics

The venture capital industry can be described as a nexus of entrepreneurs who need funding, capital providers who want high returns, investment bankers who need companies to sell and venture capitalists who make money for themselves by making a market for the other three (Zider, 1998).

The market for venture capitalists exists because of the structure and rules of capital markets. An entrepreneur with a new idea does usually not have anyone else to turn to. The law limits the interest rates that banks can charge on loans and the risks inherent in start-ups usually justify higher rates than allowed by law. Furthermore, investment banks and public equity are constrained by regulations meant to protect the public investor. Although the IPO threshold has been lowered in many countries through the issuance of development stage company stocks, the financing window is still closed to the entrepreneur (Zider, 1998).

The typical venture capital fund is organized as a limited partnership, with the venture capitalists acting as general partners of the fund and the capital providers acting as limited partners (Black & Gilson, 1998). The limited partnership agreement sets a maximum term for the partnership after which the partnership must be liquidated and the proceeds distributed to the limited partners (Sahlman, 1990). The explicit contract between the general partners and the limited partners requiring liquidation of each limited partnership is complemented by an implicit contract in which capital providers are expected to reinvest in future limited partnerships sponsored by successful venture capitalists (Black & Gilson, 1998).

The capital providers include large institutions such as pension funds, banks, insurance companies and university endowments. These institutions invest a small percentage of their total funds into venture capital and expect a high return over the lifetime of an investment. What lead these institutions to invest in a fund are not the specific investments but the venture capital fund's overall track record, the fund's reputation and their confidence in the general partners themselves (Zider, 1998). Other types of venture capital funds include incorporated venture capital funds, publicly traded closed end funds, and independent small business investment companies (Sahlman, 1990).

Once a venture capital fund is raised, the venture capitalists must define their investment strategy, identify investment opportunities, structure and execute deals, monitor investments and ultimately generate high returns.

3.3. Investment strategy

3.3.1. Industry choice

Most venture capital funds tend to specialize by industry. The choice of in which industry to specialize in is often dependent on how attractive a specific industry is at the current time, as picking the wrong industry or betting on a technology risk in an unproven market segment can proof to be disastrous for the fund. Thus, venture capitalists tend to focus on industries or market segments where most companies are likely to prosper in the near term as these industries tend to be more competitively forgiving than the market as a whole (Zider, 1998).

3.3.2. Stage of investment

Many venture capital funds will also specialize by stage of investment. Some will invest only in early-stage deals while others will concentrate on later-stage financing. Moreover, many funds limit their geographic scope.

It has been argued that venture capital only plays a minor role in funding basic innovation. That is because only a small amount of venture capital goes to seed investments that take a company through research and development. The majority of the venture capital goes to follow-on funding for companies already developed through the far greater expenditures of seed capital providers (Zider, 1998). Thus, venture capital plays an important role in the next stage of the innovation life cycle that is, when the company has evolved past the need for seed capital, has several years of operating history, has a management team in place and is able to commercialize its innovation. In other words, venture capitalists focus on the adolescent phase of the classic start-up financing cycle S-curve, as can be seen in Figure 6 (Wikipedia, 2012):

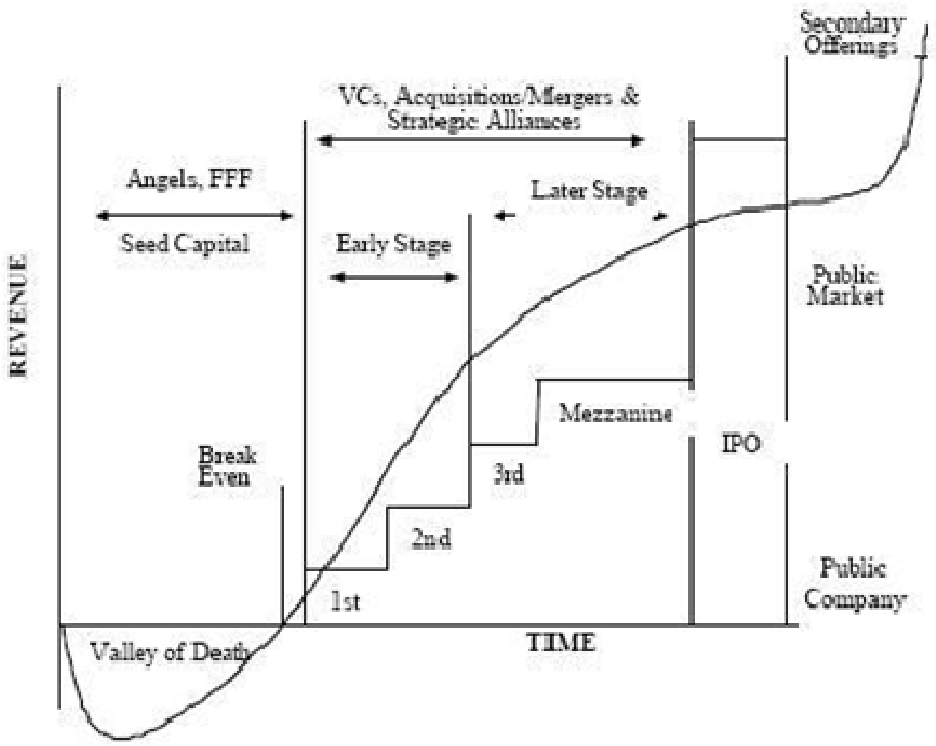

Figure 6: Start-up financing cycle

Seed stage

Most newly established companies start up by receiving seed capital from companies, universities, business angels, and the government or from friends and family. Seed capital is a small amount of funding provided to an entrepreneur to determine whether an idea deserves further consideration and further investment (Plummer & Walker, 1987). Seed capital is sometimes referred to as *soft money* as it typically involves supporting the entrepreneur with a salary and research facilities so that he can dedicate his efforts to research and development.

Venture capitalists are generally not interested in investing at this stage because of the high technology risks and market uncertainties that make the companies most volatile at this stage. Indeed, most of these companies will not end up having a product or service to offer to the market and will seize to exist.

Start-up stage

Companies showing potential will move on to the start-up stage of new business development. Typically, this requires that a company has been able to satisfy the *proof of concept*. Proof of concept is simply the proof that a company can develop a working prototype that will serve a market need. This could for instance be the development of a simple software program. The program will then determine whether the anticipated design will meet intended functionality.

At this stage, the companies are usually still being financed by the same parties that provided the seed capital. The problem is that these parties are usually better at helping entrepreneurs find new ideas than at turning them into successful businesses. This is where venture capital funds step in and provide start-up capital.

Venture capitalists are interested in investing at this stage because they can effectively evaluate the prospects of a new business and reasonably estimate a timeline for their involvement so that their funding, reputation and advice will add the most value.

Second stage

Companies proceed to the second stage only if the prototype looks good enough so that further technical risks are considered minimal. Likewise, the market studies must be promising so that management team is comfortable transforming the prototype into a commercialized product (Plummer & Walker, 1987).

If the company has entered into an unexplored market segment the level of demand is most likely benefitting from first mover advantage. But if the market is highly competitive the company will have to fight to get market share. The company may not know quantitatively what its ultimate market penetration will be, but it may know the qualitative factors that will determine the speed and limits of its penetration (Plummer & Walker, 1987).

Third stage

Third stage companies should be able to determine *proof of scale*. Proof of scale proves that the business can scale the product or service offered to satisfy the market need at a profit.

To get the functional infrastructure required to sustain scalable growth, the companies will seek more capital. As the companies are successful and stable enough so that the risk to outside investors is much reduced, the companies may prefer to use debt financing to limit equity dilution. That is, if commercial banks are willing to supply the credit needed. Typically, the cash-out point for venture capitalists is thought to be within a couple of years, but the form of exit and timing of cash-out is still uncertain (Plummer & Walker, 1987).

Bridge stage

The bridge stage or *mezzanine financing* is generally the last stage of the venture capital financing process. The company may have some idea which form of exit is most likely and even know the approximate timing, but it still needs more capital to run its operations in the meantime. A bridge financing may also correspond to the exit of early investors, replacement of management team or restructuring of positions among venture capital funds. Thus, this type of financing is typically in form of subordinated debt with some additional equity participation in the form of options to buy common stock (Plummer & Walker, 1987).

3.4. Exit opportunities

A well-developed stock market that allows venture capitalists to maximize financial returns by exiting successful investments is critical to the existence of an efficient venture capital market (Black & Gilson, 1998). Due to the limited partnership agreement, venture capital funds have a contractual obligation to return capital to their capital providers. Consequently venture capitalists have a strong incentive to exit from their investments when feasible and even well before the end of the partnership period. This is because a fund's performance record is based on completed investments and is the fund's principal tool for attracting capital providers to invest additional funds into new limited partnerships (Black & Gilson, 1998).

There are many different ways for venture capitalists to exit a company, determined by the market, the company and other external factors. These exit opportunities can be limited to:

Initial public offering (IPO): where company is introduced to stock markets, where public equity will step in to provide liquidity.

Industrial sale: where company is sold to a competitor or industrial partner.

Stock repurchasing: where company is leveraged so it can repurchase the venture capitalist stake.

Bankruptcy: where the company fails and the venture capital fund is most likely given first claim to the company's assets and technology due to contractual obligation.

Typically the most profitable exit opportunity is an IPO (Gompers & Lempers, 2001). However, depending on how the general stock market is doing, the IPO window can open and close in very unpredictable ways. Likewise, in cases where exit through industrial sale is the most efficient form of exit, the level of interest rates and the availability of commercial credit can influence the timing and feasibility (Plummer & Walker, 1987). Exit through stock repurchasing or bankruptcy is obviously not ideal.

3.5. Investment process

Each year venture capitalists spend a significant amount of time and effort screening and evaluating investment opportunities before deciding on which companies to support. Typically they screen hundreds of ventures looking for financing out of which a few dozen may be worthy of detailed attention, and fewer still will succeed in receiving investment (Kaplan & Strömberg, 2001).

3.5.1. Screening

In the initial screening, venture capitalists must make inferences about new ventures based on the limited information that is voluntarily disclosed in the investment proposals submitted by the entrepreneurs. The investment proposal is usually in a form of a business plan or an executive summary that gives a comprehensive description of the company. The most important quality of a business plan is to identify the weakness of the idea which helps the entrepreneur to know if it is worth committing to or not. Venture capitalists look at the business plan to understand how the entrepreneur is going to take their idea from opportunity to reality.

Based on the business plan venture capitalists screens the company based on the investment strategy and the investment criteria of the fund. The investment criteria vary in terms of industry and start-up stage but usually consist of both financial and operational factors. These criteria will be explained in more detail in section 5.3.: *Investment Criteria*.

3.5.2. Evaluation

Companies that meet all or most of the investment criteria of the venture capital fund are then evaluated closely. To help the venture capital partnership evaluate a venture it is common for the individual venture capitalist that is sponsoring the investment to perform a standard due diligence analysis and to prepare a detailed memorandum for the other partners (Kaplan and Strömberg, 2001). A due diligence analysis is a *360 degree* view of a company where venture capitalists scrutinize the company in regards to the investment criteria. It is usually based on the submitted business plan and interaction between the venture capitalists and the entrepreneur.

Based on Kaplan and Strömberg (2001) findings the memorandum explicitly considers the attractiveness of the opportunity that is; the market size, the strategy, the technology, customer adoption and competition in addition to the management team and the contract terms. Venture capitalists assess individual information cues as well as whether the information cues are consistent with that they would expect within the context of the other information provided in the disclosure. The memorandum also describes the risks in the given investment. The most common sources of uncertainties are usually for the technology or for the management. As a result it is common for venture capitalists to decide to complete the management team with experienced executives.

3.5.3. Investment

At the investment stage there are only few companies left in the process. Venture capitalists are interested in making an investment but it is not yet clear whether or not the companies will receive an official investment proposal. The investment proposal is dependent on a successful negotiation phase where both parties must end up agreeing on a term sheet. The term sheet is a piece of paper outlining the terms and conditions of a business agreement. It typically includes key terms such as amount raised, price per share, pre-money valuation, liquidation preference, voting rights, anti-dilution provisions and registration rights (Kaplan & Strömberg, 2001).

In a typical investment deal the venture capital fund will invest money in exchange for a convertible debt- or a convertible preferred equity ownership position based on the valuation of the company. The position typically carries board representation and disproportional voting rights that enable the venture capitalist to have power over significant operating decisions by the company.

3.6. The logic of the deal

Once investment decisions are made and deals consummated, venture capitalists need to manage their investments, monitor progress and evaluate performance. As this can often proof to be challenging, venture capitalists preserve mechanisms to ensure that the companies will succeed to the exit point.

3.6.1. Control mechanisms

The most important control mechanism that venture capitalists can apply is staging the infusion of capital (Sahlman, 1990). As the initial investment is usually insufficient to allow the company to carry out its business plan, the venture capitalists are able to keep the entrepreneur in tight control and thus reduce potential losses from bad decisions.

Venture capitalists will want to provide sufficient financing for a company to reach a pre-defined milestone that fits the stage in its development. At each milestone the parties can return to the negotiation table with some new information. If the company is doing well venture capitalists will enjoy upside provisions giving them the right to put additional funding into the company at a predetermined price. But if the performance milestones are not met, the venture capitalists can choose not to invest additional funds into the company and limit their losses (Gompers & Lerner, 2001).

Each financing event is known as a round, so the first time a company receives financing is known as *series A*, the second time as *series B* and so forth. As the company moves up in the development path and becomes better established, the venture capitalists can increase the duration of funding and reduce the frequency of re-evaluation. After all, unless the company is exited successfully there is little actual value. Venture capital is a long-term investment.

3.6.2. Incentive mechanisms

Another mechanisms utilized by venture capitalists is to provide entrepreneurs with appropriate incentives, so the interests of both parties are aligned. This can for instance be to design compensation schemes that encourage the entrepreneur to perform within a limited time span. If a substantial fraction of the entrepreneur's compensation is in the form of equity or options, this would give a great mean of motivation for the entrepreneur to develop the company and ensure that the company will succeed (Gompers & Lerner, 2001).

3.6.3. Monitoring mechanisms

The venture capitalists become actively involved in managing the companies they are supporting. Therefore a seat on the board of directors is a key mechanism for venture capitalists. Indeed, a venture capitalist spends a substantial fraction of his time as a board member (Metrick and Yasuda, 2010). In this role, venture capitalists add value to the companies by providing management assistance and reputational capital.

Management assistance

With respect to learning-curve effects, venture capitalists become repositories of useful institutional knowledge. Consequently, the venture capitalists can assist the companies, based on prior experience, in tasks such as strategic planning, finance and accounting, marketing, locating and recruiting key personnel or in other challenges that they might face when moving up the development path (Black and Gilson, 1998). Moreover, venture capitalists tend to professionalize these companies. They set up board meetings, take meeting minutes, build up processes and help with legal advice. They also force the entrepreneur to think about the long-term strategy of the company including its preferred exit strategy (Metrick & Yasuda, 2010).

Reputational capital

Venture capitalists will often use their contacts and reputation to make introductions that can lead to new partnerships, customers and suppliers that would not otherwise be possible (Metrick and Yasuda, 2010). Venture capital financing enhances the company's credibility with third parties whose contributions will be crucial to the company's success. Talented managers are more likely to invest their human capital in a company financed by a respected venture capital fund, because the venture capital participation provides a credible signal about the company's likelihood of success. Moreover, suppliers will be more willing to commit to the company and customers will take more seriously the company's promise of future product delivery. Later on the venture capitalists reputation helps to attract a high quality investment banker for an IPO or an industrial sale of the company's stock (Black and Gilson, 1998).

Like staged capital infusion, the provision of management assistance and reputational capital can also be staged, informally. A venture capitalist can choose not to make or return inquiries to or from a company or not utilize its reputation for getting in touch with potential suppliers, customers or employees. This reinforces his incentive and power to monitor (Black and Gilson, 1998).

3.6.4. Liquidity mechanisms

Venture capitalists preserve mechanisms to make investments liquid. They will for instance often try to bring in other venture capital funds. Typically there will be a lead investor and several followers. Such syndication of investment serves multiply purposes. Each venture capital fund is able to invest in more companies and thus largely diversify away firm specific risk. The involvement of other venture capitalists also provides a second opinion on the company, which limits the risk of bad deals getting funded. Moreover the presence of several venture capital funds adds credibility. Indeed, most high growth companies are backed by multiply venture capital funds (Gompers & Lerner, 2001).

4. Social Media

4.1. What is social media?

Social media can be defined as a media for social interaction. In more detail one can say it is the creation of dialogue through web and mobile-based technologies. Kaplan and Haenlein (2010) define social media as: "A group of internet-based applications that build on the ideological and technological foundations of web 2.0, and allow the creation and exchange of User Generated Content."

Social media is similar to media such as radio, TV, etc. in a way that it is an instrument of communication. However, contrary to media, which deals with information through one-way communication, social media encourages two-way communication in the form of feedback, debate, information sharing etc. By that, it is a *computer-mediated communication (CMC)* facilitating conversations and interactions between groups of people. Social media blurs the line between audience and media, and this interaction is what creates the social aspect of the media.

On the basis of this, social media comes in many forms, including social networks, blogs, photo sharing, video sharing, micro blogging etc. (Mayfield, 2008). Probably the most well known social media today is Facebook. Facebook is primarily a social network; however, it also covers several of the other types of social media simultaneously, as opposed to only one of the categories.

4.2. The purpose of social media

When studying social media, a very interesting question, of why social media is indeed so popular, arises. Given the success of Facebook and social media in general, social media must serve a purpose for the individual user. Identifying this purpose, and hence the value that the social media adds for the consumer, will help clarify where businesses will need to focus their strategic efforts.

In the business world, it can be claimed that social media enable the creation of virtual customer environments, where consumer preferences become clear and communities form around different brands or products. This kind of public information is highly applicable for marketing strategies and opportunities for many businesses, both due to the increased knowledge and the easy access to target segments.

However, the users of social media hardly engage in the usage of social media to provide this information to companies. Therefore this is not directly a purpose of social media, but rather a bonus opportunity for the companies and a reason for the business world to wish to maintain the current trend of using social media.

The growing amount of time that individuals spend in front of a computer might indicate that the purpose of social media is to substitute real life interaction to computer based communication, saving time and effort in a stressful day. Several studies on whether social networks are used as a substitute for face-to-face communication or as an extension of this have been carried out over the last years. Studies can be found, stating that the use of social media has a negative effect on a person's offline social life and hence increases factors such as isolation and loneliness. However similar studies with the exact opposite state that the use of social media is an extension of existing networks, that helps strengthen a person's offline relationships, and helps maintain offline relationships that would otherwise have disappeared. Recent study by Kujath (2011) indicates that users of social media rarely make use of sites to create new friendships, but as a way of maintaining existing ones, and rarely communicate with people they have not interacted with in real life.

4.3. The need for social media

No matter why people use social media the question comes up of whether there is an actual demand for it, or if it is merely a trend. With increased usage of internet it is fair to assume that there is a real demand for internet communication and social media, since there has been a shift in where people put down their time. At the moment social media is a place where you meet up and chat with people, share your life and plan events.

4.4. Smartphones, tablets and mobile applications

When Apple Inc., introduced the iPhone in 2007 it started a wave of smartphone creation and a whole new business of mobile applications because the operating system supported a third party web 2.0 applications. A smartphone is a multifunctional device that not only communicates, but also helps learn, earn and entertain. Users can choose between Apple iPhone, Google Android, Blackberry smartphones and many more. These smartphones all include Internet access, GPS, sensors and numerous applications.

Following the success of smartphones, Apple introduced the iPad in 2010 that became the first mobile computer tablet to get commercial success in the world. The tablets uses the operating system and touch screen technology similar to iPhone and is much smaller, lighter and have better battery life then a computer laptop. The use of tablets exploded and according to Online Publishes Association 31% of internet users in USA use them in 2012 and is expecting to grow to 47% in 2013 (Loechner, 2012).

The smartphones and tablets have changed the way people consume published content such as news and video. It also offer new ways to play games, download music, capture and edit photos and videos, do business and manage their health. Everything is made possible by the development of mobile applications. A mobile application or an *app* is a small bundle of codes designed and developed for use on smartphones or tablets to provide additional functionalities and utilities that increase the usability and entertainment features of the device.

For many businesses mobile apps are becoming a powerful tool and able to make a big difference. This business tool can strengthen brand value, improve customer engagement and offer better customer service and therefore has become a high priority for companies that want to bring in more customers.

This segment of apps has expanded enormously in recent years with the popularity of smartphone and tablets. The Apple App store has reached 25 billion apps downloads and Google Android has around 15 billion downloads. The app industry is predicted to be $ 36.7 billion market in 2015 and is standalone creating hundreds of thousand jobs worldwide (Racoma, 2011).

4.5. Market segments in social media

The social media industry can be segmented into different markets based on their purposes:

Professional Network

Where users can upload their resume to their own profile, use it to exchange information, ideas, opportunities, find jobs and business networking. LinkedIn is the largest professional networking social media and the largest of its kind to focus on interactions and relationships of business nature. Other known professional networks include BranchOut, Viadeo, Monster, Plaxo and XING.

Social Network

Companies like Facebook and MySpace, focus on building relationships among people. It is a social media platform where users share thoughts, photos, and videos and participate in groups.

Video Sharing

Allows users to easily upload and share video content across the internet through websites and mobile devices and leave comment on other videos. YouTube is the best known video sharing website, but Vimeo and Dailymotion are also widely used.

Micro-blogging

Is first and foremost Twitter. It is a social media tool that is supposed to answer the question, *what are you doing* in 140 characters or less, with a photo or a video link.

Blog

Is a website created by an individual that often serves as a publicly accessible journal with entries of commentaries, thoughts, descriptions of events or photos and videos. Readers can leave comments, which can lead to discussions. Most popular blogging platforms today are Blogger, Tumblr and Wordpress.

Photo sharing

Where users can upload photos, share them with others and comment on photos. Examples are Flickr, Picasa, PhotoBucket and Pinterest.

Mobile photo sharing

Where users can take photos on smartphones, apply filters and share the photos with other users. This market segment includes e.g. Hipstamatic and Instagram.

Certainly there are other social media categories as, games, podcast, RSS feeds, chat rooms and social bookmarking, which could be included but we define these seven segments as the key segments of the industry. Therefore we concentrate on them in our research.

5. Venture Capital Investments in Social Media

5.1. Why invest in social media?

As the social media industry continues to grow, providing new ways for people to connect, share, shop, create and network, it will continue to attract venture capital financing. The factors that influence the growth of the industry can be summarized as following.

Internet penetration: the proportion of the world population with access to internet is increasing. From the year 2000 to 2012, the number of people who use the internet has increased with 528%, and at the moment 33% of the world population makes regular use of the internet. This number is however highly tainted by countries such as the USA (78%), UK (90%) and Australia (80%) as well as the European Union (72%) (Internet World Stats, 2012). Moreover, just over 10 years ago, internet usage was almost non-existent in emerging markets. Today, it is estimated that the number of internet users in China, India and Brazil combined will exceed 1 billion by 2015 (Ernst&Young, 2012).

Global social media users: social media is the most popular and time consuming destination online. Approximately two-thirds of global internet users said that they use a social networking site. That is more than double the percentage that reported social network usage in 2008 (Nielsen, 2011).

Time online: according to Mindjumpers (2012) global time online is mostly spent on social media (22%) followed by search engine (21%) and e-mail (19%).

Fast growth of mobile networks: increase in mobile phone usage has propelled social media, with nearly 40% of social media users accessing content directly from their mobile phone (Nielsen, 2011). With smartphones and tablets, a variety of content can be more easily distributed, such as music, video, books and games (Ernst&Young, 2012).

Social networking and commerce intersects: social media enables businesses to connect directly with customers, a potentially valuable tool that is contributing to the increase in social media advertising (Nielsen, 2011). Moreover, as social media evolves it facilitates information sharing to the world at a lower cost and of higher quality than other media, which have been monopolizing until now. Likewise it also enables companies to collect information from the world (Ernst&Young, 2012).

5.2. Investment activity

According to the latest PWC Money Tree Report that is co-created with the National Venture Capital Association (PricewaterhouseCoopers, 2012), the software industry received the highest level of venture capital funding of all industries with $2.3 billion invested during the second quarter of 2012, as can be seen in Figure 7. This is the highest investment total for the sector since 2001 when the IT bubble burst. The software industry also had the most deals completed in the quarter. Internet specific software companies, that include social media, accounted for 78% of the investment total.

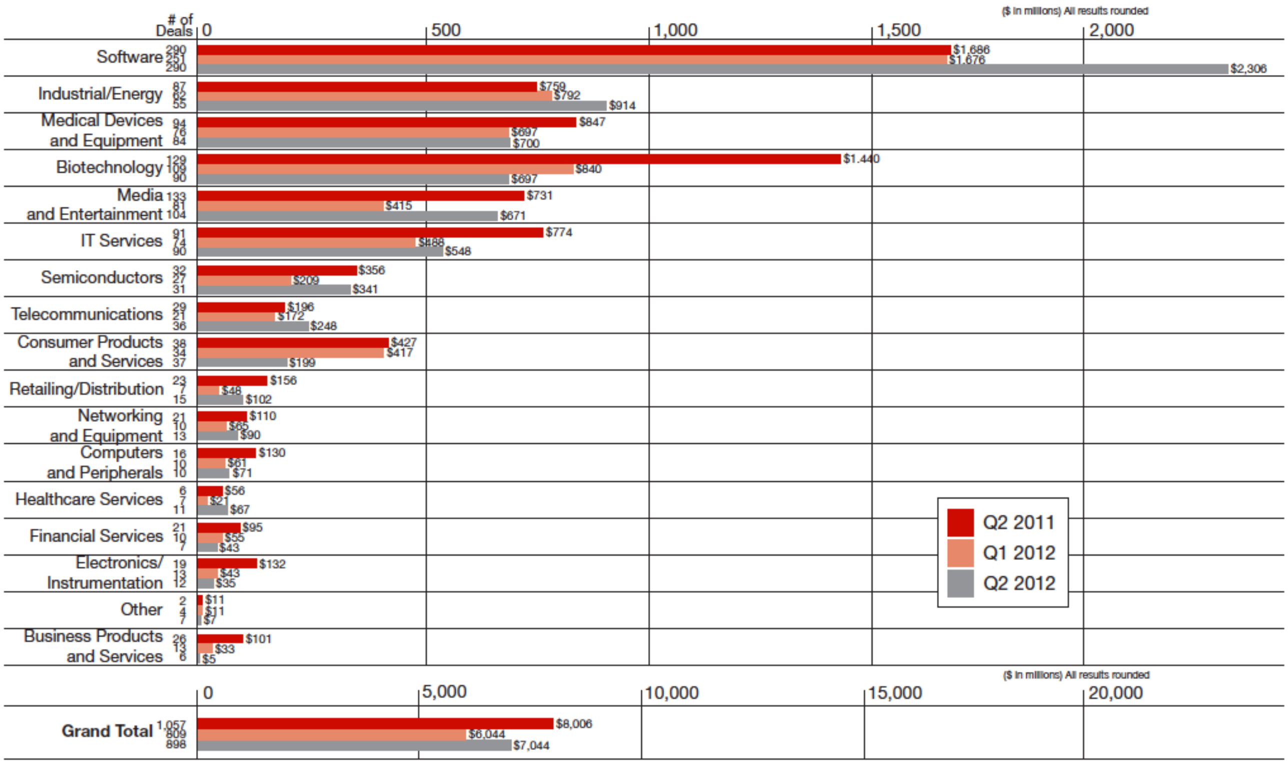

Figure 7: Investment activity by industry

Since 2010, more than 800 venture capital financing deals have been announced in social media representing aggregate value of $8.3 billion. Interestingly, over 40% is classified as seed capital or series A financing which implies that venture capitalists are willing to invest earlier and thus with higher risks than when dealing with other industries like life-science and clean-tech where most deals are achieved at later stages. This may be caused by the continuous rivalry between venture capitalists in the race to discover the next big thing in social media. Consequently promising social media start-up companies can often choose between venture capitalists that drive up the value of the companies.

More than 80% of these investments have been invested in US based companies, where far most are located in the Silicon Valley. Among the most prominent venture capital funds investing in social media today are Andreessen Horowitz, Sequoia Capital, Accel Partners, Benchmark Capital, Union Square Ventures, Greylock Partners and European Founders Fund.

5.3. Investment criteria

In the adolescent phase of a company's life cycle where there is high and accelerating growth it can be hard for venture capitalists to distinguish the eventual winners from the losers because the respective financial performances and growth rates look strikingly similar (Zider, 1998). Consequently when screening for investment opportunities, venture capitalists assess the candidates based on investment criteria that should be designed to support their decision.

In a recent study by Visagie (2012), the criteria that venture capitalists put the highest weight on can be limited to people, money and technology. These criteria can then be adapted to start-up companies in social media as the following:

People

Venture capitalists will invest in competent management with high aspirations and the will to succeed. Social media entrepreneurs with prior experience and success in the industry or a track record of leadership and performance are usually the most important factor for creating value.

Money

Management that is able to demonstrate a thorough understanding of market dynamics and competitive landscape in the social media industry is important for generating revenue. Venture capitalists will generally prefer a large penetrable market segment or a highly profitable niche market, customer involvement at early stage, modest competition and fair barriers to entry. Management also needs to recognize the financial dynamics of the business and the industry. Appropriate sales models, reasonable financial projections and high technology adoption rates all support for a high valuation.

Technology

Venture capitalists consider companies with strong innovation in product or service offering. Social media companies are most likely to create product differentiation through the use of technology and utilize it for the best quality and function.

Social media companies roll out their products or services through the creation of a platform. The most important function of such a platform is to attract and protect network. Therefore, companies with successful platforms enjoy strong network effects and can maintain stable profits. These platforms are often based on a free product and therefore it is crucial to offer a product effectively differentiated. The quality of the product thus determines the size of the market opportunity.

5.4. Business model as a key differentiator

The problem with people, money and technology is that these criteria tend to give similar result when assessing social media companies as most of them have management with strong technical background, address the same customer need and pursue similar product market strategies. What differentiates each social media company is therefore how they exercise their business models to enhance people, money and technology.

As a result, venture capitalists need to identify the most competitive business models as well. Their challenge is to identify the best business models as investing in a company with a weak business model could harm their business and reputation. Venture capitalists must compare business models to spot strategic differences that may impart a competitive advantage. Thus, they need to seek business model innovation (Osterwalder & Pigneur, 2010).

5.5. Business model innovation in social media

Social media has demonstrated that the development process can go from many years to only few months, making it a unique investment for the venture capitalist. It is not about developing a product for years and coming out with the amazing product and protecting it with intellectual property rights. Instead, it's more about rolling the product out whenever the company has something that interests users and can then later be altered and improved.

Social media companies employ virtual business models. In short, this means that the business model is fundamentally dependent on the Internet, regardless of the company's primary market segment. Robust business models combine hardware, software and service in an innovative way and create value for the user. The virtual model offers management the potential to create a highly flexible company capable of expanding or narrowing the scope of product development in a very short period of time.

This makes companies in social media constantly engage in business model innovation. Innovation becomes business model innovation when two or more elements of a business model are reinvented to deliver value in a new way (Zott, Amit & Massa, 2011). As this involves a multidimensional and orchestrated set of activities, business model innovation is both challenging to execute and difficult to imitate. Therefore at a given time there will always be a frontrunner in each market segment that deploys this best. How long the company stays in front in dependent on its ability to evolve. Consequently market segments in social media tend to have only one dominant player and few followers at a time.

A special concern has been the monetization of these business models. Pauwels and Weiss (2008) examine fee and free business models for providing digital content on the Internet. Their work focuses on the firm performance implications of a shift from the free to the fee model and empirically analyzes the role that marketing actions can play in accommodating this shift. The models are countless but some of the most used are introduced in the following subsections.

5.5.1. Advertising model

The advertising model is when a web site or other broadcaster provides content or service mixed with advertising messages. The broadcaster may be a content creator or a distributor for others and the *ad* may be the major or only source of revenue for the business. The advertising model works best when the web traffic is large or highly specialized (Rappa, 2010).

There are many revenue models for web advertising. The main models are CPM (cost for impression), CPC (cost per click) and CPA (cost per action). The main difference between these models is that CPM is where company is paid for showing a number of ads, CPC is where company is paid each time a user clicks on an ad and CPA where company is paid each time a user completes a particular action.

5.5.2. Affiliate model

Affiliate model is an e-commerce model where the affiliate, that is a particular user site, promotes other businesses products or services for a commission. For start-ups it has low costs, easy to set up, can create a multiple income stream and lets the business focus on its core skills.

There are three main methods of financial incentive offered by the affiliation model (Rappa, 2010).

Pay-per-click: Where businesses pays affiliate for user click-through.

Ads exchange: Where businesses place ads on affiliated sites to increase exposure.

Revenue sharing techniques: Where businesses offer affiliates a percentage of sale commission based on a user click-through in which the user subsequently purchases a product. More modern way of revenue sharing is when a host company (e.g. YouTube) rewards a user of their network for generating traffic to the site and encourage him to stay with the company instead of developing his own independent site (Wikidot, 2012).

5.5.3. Crowdsourcing model

Crowdsourcing model is the act of a business taking a function once performed by employees and outsourcing it to a generally large network of people in the form of an open call (Howe, 2006).

When using the crowdsourcing model it is needed to distinguish between value creation and value capture. When activity of a business is based completely on crowdsourcing, users perform the value creation using open source software, while the value capture should be made within the business model. Open source projects permits online users to communicate in decentralized way and to work together in order to reach project goals with more efficiency and better solutions.

5.5.4. Freemium model

Freemium, made from the words, *free* and *premium*, is a business model where businesses give a core product away for free and then sell premium products. As the service is given away for free the company can acquire many customers very efficiently through word of mouth, referral networks and organic search marketing. Then businesses offer premium priced value added services or an enhanced version of the service to their customers (Wilson, 2006).

For successful freemium model it is vital to have quality product, with large reach because with increasing supply for the product the demand for the complementary product also increases. The generous nature of freemium fits well with social media; the product can be duplicated digitally with very low cost and reach a lot of users online.

Freemium model demands millions of users with high loyalty. The value of the product increases over time, with growing user base but freemium business model can take a long take to reach breakeven point. Therefore to bridge this gap these businesses often need higher equity financing from venture capitalists (Gobry, 2011).

5.5.5. Merchant model

Merchant model is primarily used by wholesalers and retailers of goods and services. Sales can be made based on list prices or through auctions. There are two main types of this model:

Virtual Merchant: is a retail merchant that operates exclusively over the web, like Amazon.

Bit Vendor: are on the other hand merchants that deals strictly in digital products, like Apple iTunes store and conducts both sales and distribution over the internet (Rappa, 2010).

5.5.6. Subscription model

The subscription model is where users pay a fee (generally monthly or yearly) to access a product or service. Often this is a combination of free content, with option of premium content for subscription only. Subscription fee is most often based on a fixed fee regardless of usage (Rappa, 2010). This model was established by newspapers and magazines but is now used by many websites and businesses.

5.5.7. Virtual goods model

Virtual goods model is used for selling virtual goods. Virtual goods refer to objects such as characters, items, currencies and symbols that exist inside various online games, mobile application and social media. Three defining attributes for virtual goods are rivalrousness which refers to the unusual nature of virtual goods, persistence as virtual goods are persistent and interconnectedness as the goods can be interactive among multiple actors (Fairfield, 2005). The advantage of virtual goods is that the margin is very high. Goods only cost as much as the bandwidth required serving them, which usually is close to zero. On the other hand the biggest hindrance for these companies to create something that the users want and is relevant to the community.

5.6. Summary

We argue that venture capitalists are interested in investing in social media start-up companies and that business model innovation plays a large part in helping businesses adapt and succeed in this competitive industry. Therefore it should not be neglected in the investment criteria of venture capitalists. But to understand precisely how business model design influences the success of a social media start-up company, so venture capitalists will know what to look for, we will conduct case studies based on our proposed theoretical framework in the following section.

6. Case studies

The case studies will be conducted in the following order:

- 6.1. LinkedIn
- 6.2. Facebook
- 6.3. YouTube
- 6.4. Twitter
- 6.5. Tumblr
- 6.6. Pinterest
- 6.7. Instagram

6.1. LinkedIn

LinkedIn is the world's largest professional social network with over 175 million users in more than 200 countries. The company was founded by Reid Hoffman and his team Allen Blue, Konstantin Guericke, Eric Ly and Jean-Luc Valliant in Hoffman's living room in 2002. Their aim was and is still today to connect the world's professionals to make them more productive and successful. LinkedIn has shown how social media can impact the executive and job field. Users can create their own professional profile, find business contacts or prospective clients, and search for jobs and access knowledge. LinkedIn currently ranks nr. 12 on the Alexa list over the most popular global websites in the world (Alexa, 2012).

6.1.1. Business Model Canvas

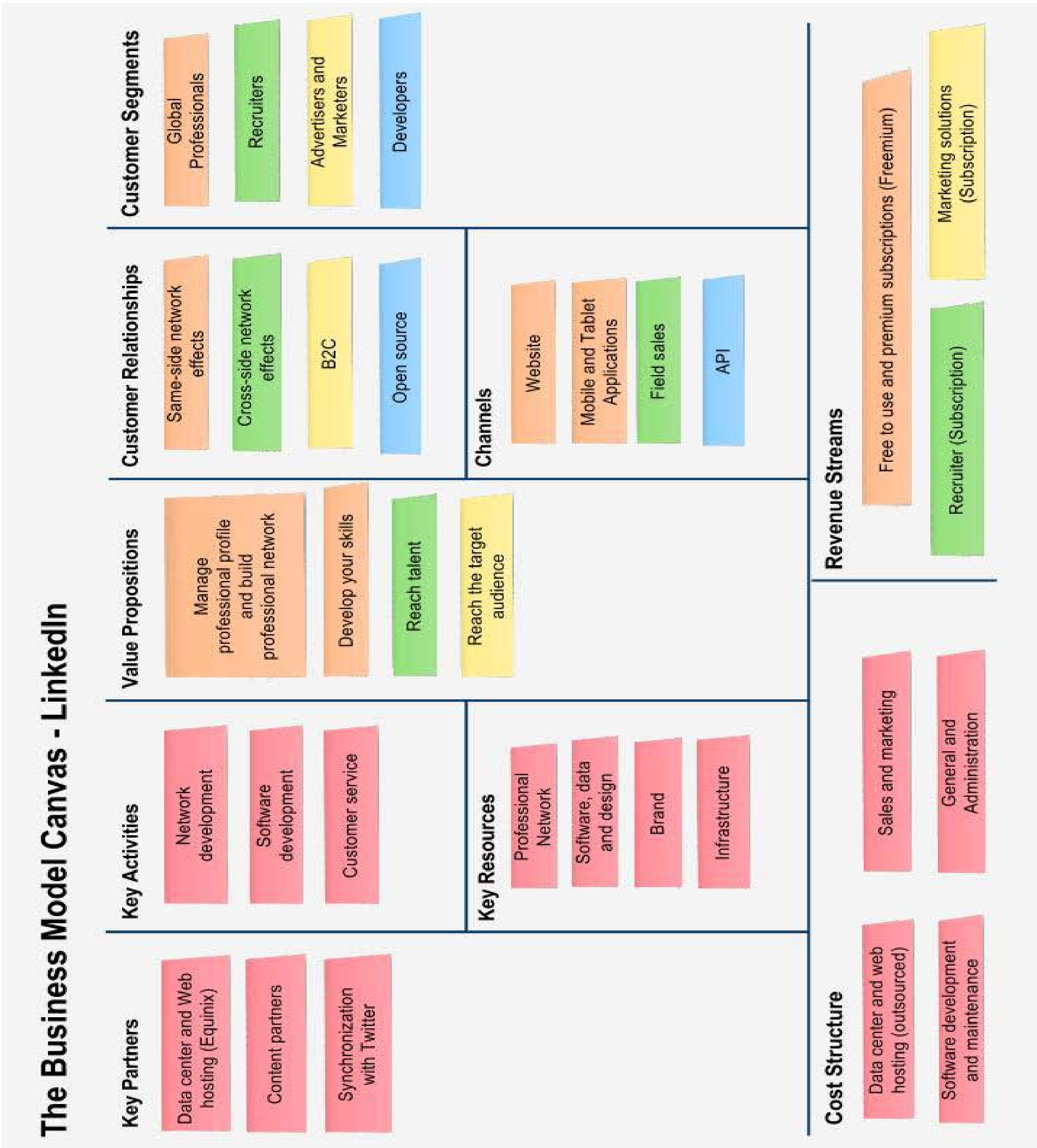

Figure 8: Business Model Canvas - LinkedIn

6.1.2. Venture capital funding

LinkedIn has in total received venture capital investment of $103.7 million both from independent- and incorporated venture capital funds, demonstrated in Figure 9. The company has proofed to be a very successful investment for these funds as it accounted for a valuation of $9.31 billion at the time of exit. LinkedIn entered the New York Stock Exchange (NYSE) in May 2011, generating great returns to the venture capitalists that supported the company (Crunchbase, 2012).

Type	Date	Investor	Funding
Series A	Nov 2003	Josh Kopelman and Sequoia Capital	$4,7 M
Series B	Oct 2004	Greylock Partners	$10 M
Series C	Jan 2007	Bessemer Venture Partners and European Founders Fund	$12 M
Series D	Jun 2008	Bain Capital Ventures, Sequoia Capital, Greylock Partners and Bessemer Venture Partners	$53 M
Series E	Oct 2008	Bessemer Venture Partners, SAP Ventures, Goldman Sachs and McGraw-Hill Companies	$22 M
Exit	May 2011	IPO: NYSE *LNKD*	Valuation: $9.31 B

Figure 9: Venture capital funding – LinkedIn

6.1.3. Assessment of business model

6.1.3.1. Scalability

LinkedIn has implemented a multi-side platform, like most other social media companies, which offers different solutions to different categories of users. The platform benefits from same-side network effects among its members because it is still growing via word of mouth and connection requests. While the user base grows the network improves and becomes more appealing to users on the opposite end of the platform; the recruiters, advertisers, marketers and developers.

LinkedIn seeks to be dominant in a niche market and with over 600 million white-collars workers worldwide it has only realized a fraction of its market potential. The company has many ways to grow and expand its network. For instance, they can try to get users more engaged and offer LinkedIn versions in as many languages they can reach and involve more powerful people and businesses to the network. International expansion is going to be a key strategy as in first half of 2012 about 70% of new members came from outside the U.S. (Bort, 2012).

To deal with the scalability challenges of this growth, LinkedIn's technology infrastructure consists of professional graph, search, customized content, matching, targeting and recommendations, ad targeting platform and open source technologies that have been developed with the goal of maximizing the availability of the platform to the users. Interestingly, LinkedIn's data center and web hosting activities are outsourced to third party service provider for more cost efficiency.

6.1.3.2. Uniqueness

LinkedIn has a strong value proposition as it allows users to manage professional profile and built professional network with millions of users worldwide. Moreover, LinkedIn counts executives from all 2012 Fortune 500 companies as members and its recruitment solutions are used by 85 of the Fortune 100 companies, making it a highly attractive network for global professionals and recruiters to be part of today (LinkedIn, Nov. 3, 2012). Moreover LinkedIn represents a valuable demographic for advertisers and marketers to reach their target audience.

6.1.3.3. Loyalty

LinkedIn benefits from being the largest professional social network in the world today. The users however do not keep a lot of personal information on the network e.g. compared to Facebook and are therefore likely to switch networks if something better comes along, with more recruitment solutions and career options. Recruiters, advertisers and marketers will then be where the talent is and stop investing in the LinkedIn platform.

6.1.3.4. Profitability

Diversifying its revenue stream to better match the needs of its different customer segments has worked well for LinkedIn. For the third quarter of 2012, margins were up and the company's total revenue of $252 million resulted from three key revenue streams (LinkedIn, Nov. 8, 2012):

- Hiring solutions: 55%
- Marketing solutions: 25%
- Premium subscriptions: 20%

LinkedIn monetizes its Hiring solutions and Marketing solutions by utilizing the *subscription* revenue model. Its flagship product, Recruiter, has been a success and attracted around 12.000 enterprise subscriptions and over 2 million company profiles, spending from $25 to millions of dollars a year (Bort, 2012).

For Premium subscriptions, LinkedIn uses the traditional *freemium* revenue model. While the core offering is free for its network members, premium membership with increased benefits is available for a price.

6.1.3.5. Sustainability

The company has growing efficiency in regards to having users spend more time on its platform. Offering members better tools with new features and design to share their professional skills and insights, providing more efficient hiring solutions and by making their marketing solutions more relevant by significantly investing in targeting capabilities and analytics will help to sustain this.

LinkedIn also intends to leverage its business model to further monetize its platform while adding value to its members on a global basis. Strikingly, while 63% of current LinkedIn members are international, only about the third of its revenues is coming from there. The company has therefore an untapped revenue potential in activating this pool.

Moreover, the market for recruiting tools and solutions is big and the company wants to become the leading force there. LinkedIn's CEO Jeff Weiner said, in September 2012, that he wants to grow revenue by getting more members, instead of raising prices for existing members, at least for the Recruiter (Bort, 2012).

6.1.3.6. Mobility

Given the nature of LinkedIn's business as a professional social network, the company is strongly affected by the state of the job market. Low unemployment rate means prosperous job market and therefore many using the network seeking better job opportunities. While, high unemployment rate could mean further activity in job haunting but that could also mean cost cutting, laying-off employees and reduction in usage on recruitment solutions. Thus, in this challenging environment it is important for LinkedIn to be able to adopt well to change and to diversify away any product-specific risk that might harm the company.

LinkedIn has responded well to the mobile evolution and is now able to reach users both through its website and mobile applications ranging from Blackberry to iPhone. In early 2012, the company introduced new and improved mobile application and unique visitors grew instantly from 10% to 23% (Bort, 2012). However, this is merely perceived as an additional service to users rather than a revenue opportunity. The company is not reliant on revenues from the mobile platforms and it does not matter much how users access the service.

6.1.3.7. Inimitability

The market segment of professional networks, recruiting- and marketing solutions is highly competitive. Professionals around the world are therefore most likely willing to use the network that provides the highest benefit. With growing number of members, better service and sustained growth in revenues, LinkedIn currently has all the advantage. But the company will have to fight off fierce competition, from companies like Viadeo, Monster Worldwide and BranchOut, which also offer services for finding jobs and recruiting employees.

6.1.4. Overall rating and Key learning

Figure 10 is the overall rating of LinkedIn according to the 7 Factor Model and key learning in regards to each factor:

LinkedIn	**Overall rating**	**Key learning**
Scalability (25%)	2	Niche market
Uniqueness (20%)	3	Fortune 500 Professional network
Loyalty (15%)	3	Low switching costs
Profitability (15%)	4	Profitable Diversified revenue stream Flagship product enhances value
Sustainability (10%)	3	Growing efficiency Plausible plans for the future
Mobility (10%)	2	Reaching out to users through different channels
Inimitability (5%)	2	Competitive market
Score	**2.8**	**Rank #5 of 7**

Figure 10: Overall rating and Key learning – LinkedIn

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6.2. Facebook

Facebook was founded by Harvard student, Mark Zuckerberg, in February 2004. With help from his college roommates Eduardo Saverin, Dustin Moskovitz and Chris Hughes he created a social network site for the Harvard student society. In less than a month the site expanded to other Ivy League schools and in a few months most universities in USA and Canada had access to the network. Zuckerberg teamed up with Sean Parker, entrepreneur and founder of Napster, who soon became President of Facebook and quickly managed to find investors for the project. In September 2005 high-school students all across the USA were able to join, and later employees of numerous companies including Apple and Microsoft were joining the network. Subsequently, in September 2006, Facebook was made open for anybody over the age of 13 with an acceptable e-mail address. Since then Facebook has become the biggest social media network in the world with more than 1 billion active users. Facebook currently ranks nr. 2 on the Alexa list over the most popular global websites in the world (Alexa, 2012).

6.2.1. Business Model Canvas

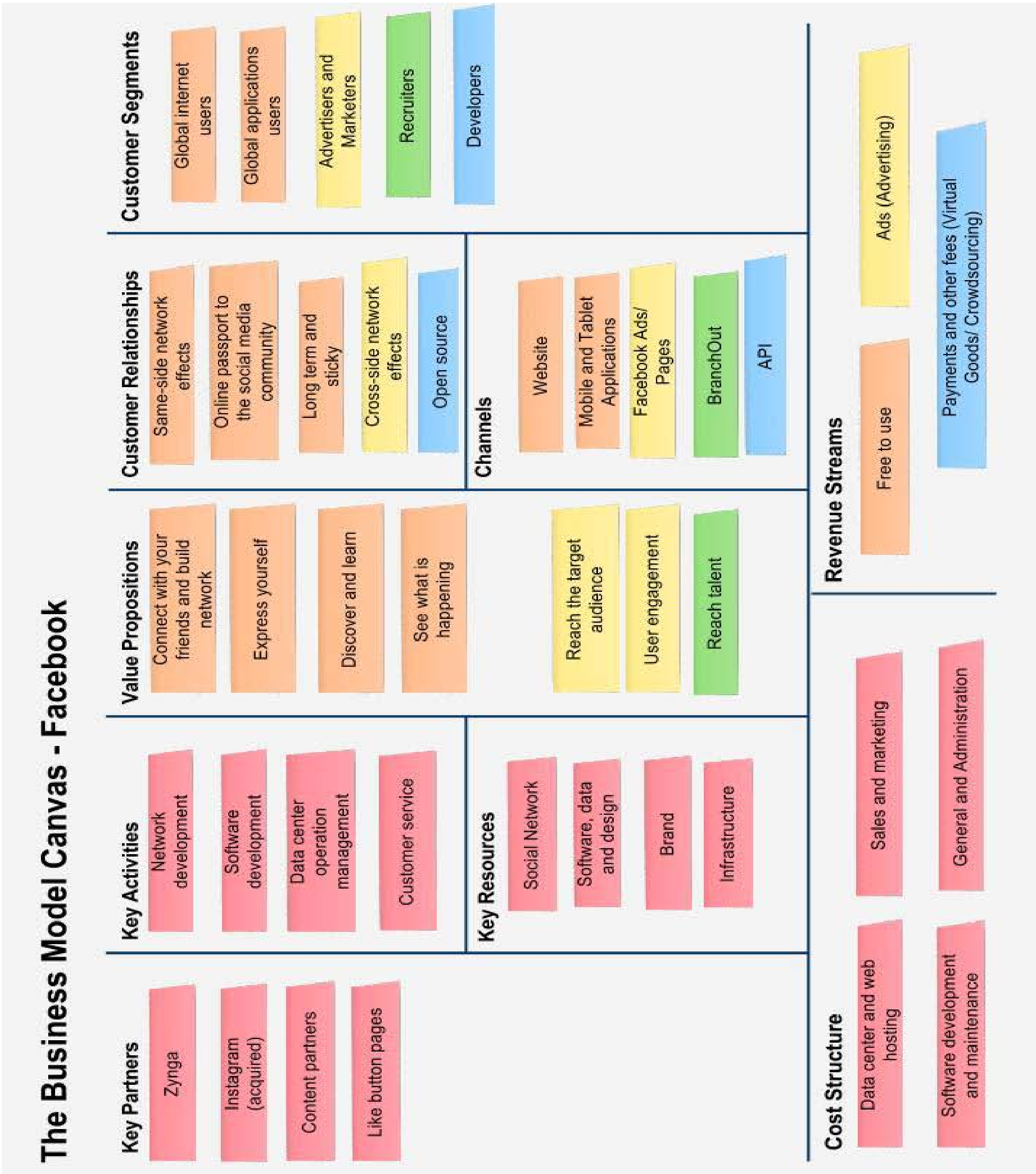

Figure 11: Business Model Canvas – Facebook

6.2.2. Venture capital funding

After receiving seed investment, Facebook managed to raise $2.2 billion in venture capital from both independent- and incorporated venture capital funds, as demonstrated in Figure 12. The company did also secure a debt round of $100 million for their late stage development. Thus, total funding raised amounts up to $2.3 billion. After a lot of speculation for several years, Facebook finally went public in May 2012. The IPO valued the company at $104 billion, which made Facebook the highest valuation for newly listed public company ever (Crunchbase, 2012).

Type	**Date**	**Investor**	**Funding**
Angel	Sept 2004	Peter Thiel and Reid Hoffman	$500k
Series A	May 2005	Accel Partners, Mark Pincus and Reid Hoffman	$12 M
Series B	Apr 2006	Greylock Partners, Meritech Capital Partners and The Founders Fund	$27 M
Series C	Oct 2007	Microsoft	$240 M
	Jan 2008	European Founders Fund	$15 M
	March 2008	Li Ka-shing	$60 M
Debt round	May 2008	TriplePoint Capital	$100 M
Series D	May 2009	Digital Sky Technologies	$200 M
Venture Round	Jun 2010	Elevation Partners	$120 M
	Jan 2011	Goldman Sachs and Digital Sky Technologies	$1,5 B
Exit	May 2012	IPO: Nasdaq *FB*	Valuation: $104 B

Figure 12: Venture capital funding – Facebook

6.2.3. Assessment of business model

6.2.3.1. Scalability

Facebook's greatest resource is its network. As of September 2012 Facebook has more than 1 billion active users from all over the world, and if Facebook were a nation, it would be the third largest country in the world after China and India (Facebook, Nov 3, 2012).

Despite this impressive number of users, Facebook is far from reaching its full market potential as its mission is to connect the entire world. With increased proportion of the world population gaining access to internet, especially in emerging markets, Facebook can keep growing its network rapidly in the years to come.

Seeking mass market has its challenges, as the billions of minutes spent and billions of photos and content shared on the platform must be matched with a scalable infrastructure that can serve this information quickly and without problems. Facebook has addressed this by having a very strong technology infrastructure and engineering culture, which is constantly growing and innovating. All this data is stored in multiple data centers, owned by Facebook, all over the world, with strong backup that prevent data loss, so nothing happens if one server brakes down (Gedda, 2010).

6.2.3.2. Uniqueness

Facebook defines its service as: "A social utility that helps people communicate more efficiently with their friends, family and co-workers. The company develops technologies that facilitate the sharing of information through the social graph, the digital mapping of people's real-world social connections. Anyone can sign up for Facebook and interact with the people they know in a trusted environment." (Facebook, Aug 10, 2012).

Thus, Facebook is amazing because it can put everything the user does on the internet into a social framework. The service itself is very unique as the company dares to continuously challenge the status quoi and keep re-inventing itself. The company is known for constant improvement of design and user interfaces and has formed many partnerships and acquired countless companies to add to their user experience. For instance, their most recent acquisition, Instagram should enhance the company's photo product offering. But Facebook must be considerate when choosing its partnerships as they could along with other

Facebook platforms reduces user activity on Facebook by making it easier for users to interact and share on third-party websites.

6.2.3.3. Loyalty

Facebook core is the user’s online relationships which reflect their real personal life. No wonder why internet users spend more time on Facebook than any other web brand (Nielsen, 2011) as using the service gives them the good feeling of being *liked* and the opportunity to embrace content shared by their friends.

For millions of people, having a Facebook account is like having a social media passport and a diary of life. Many other social media sites and mobile applications even require a Facebook login for admission. Consequently the switching costs for the users are high and make it difficult for them to leave.

Facebook owns all data that is voluntary disclosed by their users. This gives them complete knowledge about their users that they can utilize both in relation to predicting their user needs and for beneficiary use in relation with marketers and advertisers. The growing number of users makes the network an attractive place to reach maximum audience.

6.2.3.4. Profitability

Facebook's main goal has always been to make a great product rather than generating revenue. Zuckerberg has said about Facebook: “We don´t build service to make money, we make money to build better service.” (Magid, 2012). So when Facebook filed for IPO it gave a significant look into its financial statement. It showed that the social network is a strong company with growing revenues of $3.7 billion in 2011, which is more than 450 percent of 2009 revenue and almost double of those in 2010 (Sherman, 2012).

As can be seen below, Facebook relies heavily on the *advertising* model (Facebook Inc., 2012):

- Advertising: 84%
- Payments and other fees (mostly from Zynga): 16%

For payments and other fees, Facebook utilizes the *virtual goods model* and the *crowdsourcing* model.

The company has been criticized for relying too much on traditional advertisements as their key revenue source, as these can be highly unpredictable and unreliable. It has responded to this criticism by introducing a number of new methods that should play an important part in diversifying their revenue stream in the future. For instance, the company introduced sponsored stories on its mobile application in early 2012 aiming at generating revenues on other platforms than the web. Sponsored stories let advertisers take advantage of word-of-mouth recommendations and promote them. In this way they give a way for application developers, page owners and place owners to be able to promote their content that's as core to the user experience as the news feed (Facebook Inc., 2012).

6.2.3.5. Sustainability

Constant development and re-inventing of the Facebook platform has managed to keep the users interested in the product and build a good reputation. By focusing on hardware efficiency, information security, building new servers and creating the Facebook Immune system, the company has lowered the possibility of hacker parties exploiting its information. Thanks to this, less than 0.5% of users experience spam each day (Constine, 2011).

6.2.3.6. Mobility

By allowing open source technology development from partners and developers, the software and network is able to grow at enormous speed. Open source allows Facebook to innovate with others, build on top on things other have released, use it to solve problems and then release it again for others to build on.

As most other social media companies that were built on the 2.0 technology Facebook has struggled to develop agile mobile applications that would enhance the user experience the same way it does on the Web. This imposes a threat to the company’s business as changes in user sentiment about the quality or usefulness of the products offered can harm the company’s reputation and thus it could risk missing out on a potentially huge market segment.

But the costs of pursuing this market segment could also be high as the channels must complement each other. As can be seen in Figure 13, growing number of users are now accessing Facebook via mobile applications where the company does not yet generate any meaningful revenue (Facebook Inc., 2012).

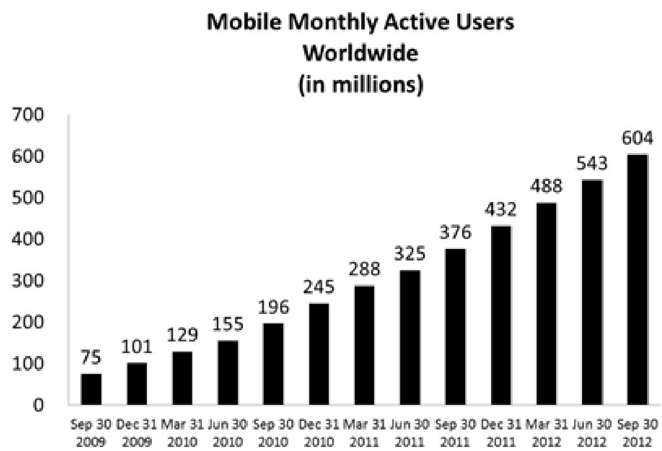

Figure 13: Mobile Monthly Active Users Worldwide - Facebook

Increased mobile access could thus harm the company's profitability as it substitutes Facebook usage on personal computers where it has much greater opportunities to monetize usage by displaying ads and other commercial content.

6.2.3.7. Inimitability

The size of the social network and information database is unique in the world and impossible to imitate. The reputation, experience in the social network world and a leader in Zuckerberg, which it seems is driven only by the motivation to expand and improve the network, Facebook will be hard to match.

6.2.4. Overall rating and Key learning

Figure 14 is the overall rating of Facebook according to the 7 Factor Model and key learning in regards to each factor:

Facebook	**Overall rating**	**Key learning**
Scalability (25%)	4	Mass market
Uniqueness (20%)	5	Connects the world
Loyalty (15%)	5	Passport to all social media
Profitability (15%)	2	Profitable Dependent on one key revenue source Failure to monetize mobile application
Sustainability (10%)	4	Constant re-inventing of user experience
Mobility (10%)	3	Channels complement each other
Inimitability (5%)	5	Impossible to imitate
Score	**4.0**	**Rank #1 of 7**

Figure 14: Overall rating and Key learning - Facebook

6.3. YouTube

YouTube unites the world through video. The company was founded in February 2005 by three PayPal employees; Chad Hurley, Steve Chen and Jawed Karim, after the former two had experienced difficulty sharing a personal video with the third over the internet. YouTube now enables billions of people to discover, watch and share originally created videos online. The site provides a medium for people to connect, inform and inspire others across the globe and acts as a distribution platform for original content creators and advertisers. YouTube currently ranks nr. 3 on the Alexa list over the most popular global websites in the world (Alexa, 2012).

6.3.1. Business Model Canvas

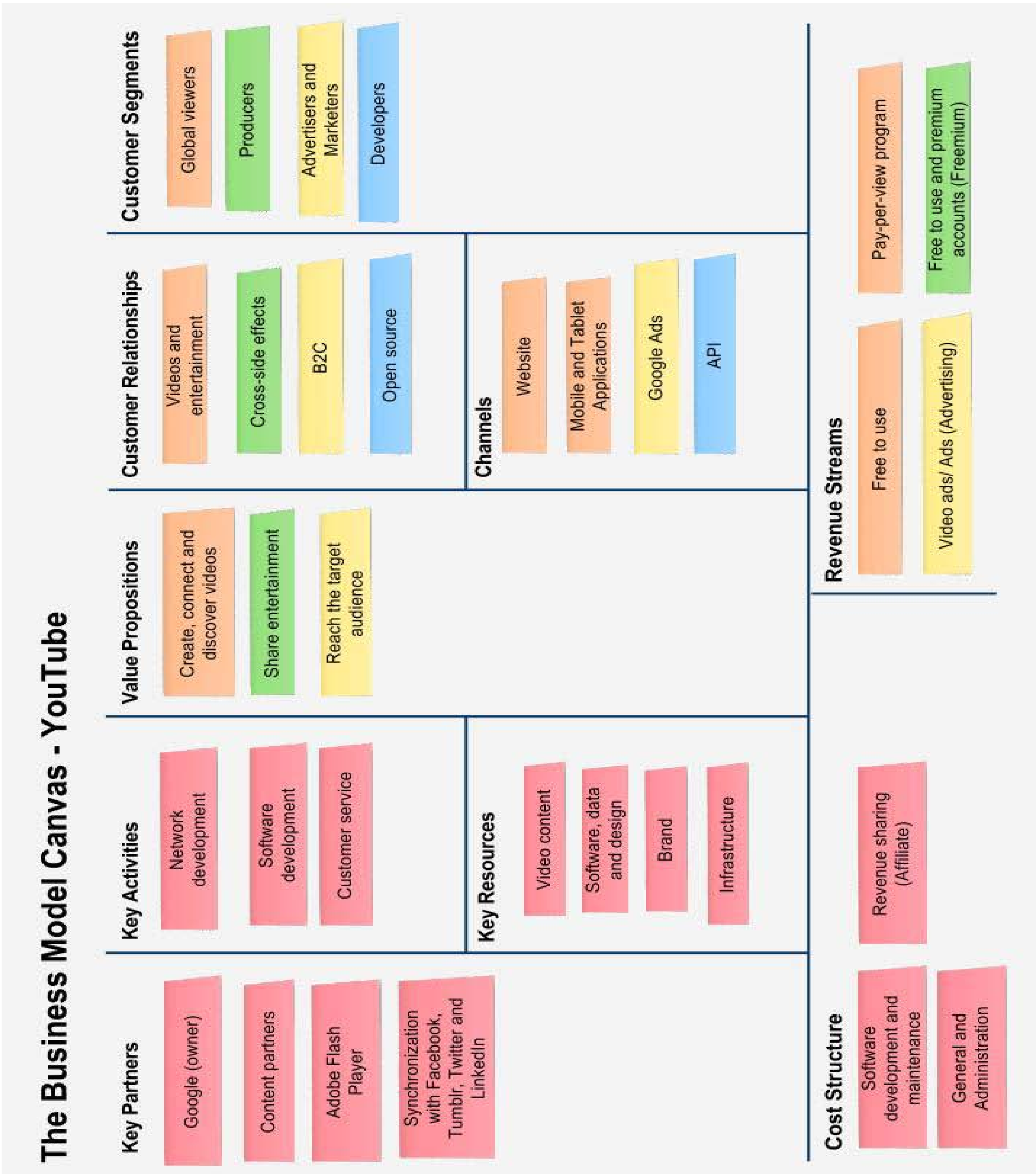

Figure 15: Business Model Canvas – YouTube

6.3.2. Venture capital funding

It did not take long for Google Inc. to realize the hidden value that lied within YouTube. Still in its early stage development and after only receiving $11.5 million in venture capital from Sequoia Capital, the company was acquired by Google in November 2006 for $1.65 billion (Crunchbase, 2012). Demonstrated in Figure 16:

Type	Date	Investor	Funding
Series A	Nov 2005	Sequoia Capital	$3.5 M
Series B	April 2006	Sequoia Capital	$8 M
Industry sale	Nov 2006	Google Inc.	Valuation: $1.65 B

Figure 16: Venture capital funding – YouTube

6.3.3. Assessment of business model

6.3.3.1. Scalability

YouTube uses a peer-to-peer file sharing network geared specifically towards video technology. It made generate video clips easy and now with the smartphone and tablets revolution and easy synchronization with all the largest social media, it is not surprising that YouTube is so successful.

The company recently redesigned its platform around its hundreds of millions of niche channels. It is now focusing on becoming a platform that could host hundreds of hyper-specialized channels that would appeal to the most specific of interests. This includes partners from major movie studios, record labels, web original creators, celebrities and ordinary people (Swift, 2011). Users don't need to be registered to view the majority of the content on YouTube but they have to have an account to share content and subscribe to channels.

Being part of the Google conglomerate, YouTube benefits from in-house built software and network infrastructure such as Google Search, Google Cloud and Google Ads that have strengthen the scalability of the company. For instance, Google Cloud has proven to reduce the amount of upload time and streaming for users (Hickins, 2011).

6.3.3.2. Uniqueness

YouTube is perceived one of the most important social media tools in the world. Being able to generate millions upon millions of video views per day, it presents a fantastic opportunity for people, brands and businesses to have their content seen by a large audience (Simplyzesty, 2012).

Given the enormous number of views, YouTube is an ideal platform for using video advertisements. The more of a video someone watches on average, the greater the value of the video. As the average viewing time grows, YouTube will be able to provide advertisers with a greater reach than comparable TV ad spots (Rigsby, 2012).

YouTube's unique features have helped people to get attention on the internet. This YouTube sensation enables creative users to develop a strong following and their fame will grow with the number of views on their videos.

6.3.3.3. Loyalty

Google Ads services enable YouTube to provide advertisers with customized solutions that enhance customer loyalty. Advertisers pay only when the viewer chooses to watch their ad, which is similar to the pay-per-click pricing with search ads. The only downside is that with billions of videos on the site, getting attention is not easy. YouTube provides innovative ad formats and comprehensive targeting to make it easier for advertisers to find both popular and hard-to-reach audiences. Advertisers do also get video insights, viewer statistics and other tools they need to create and manage their video ads (YouTube, Nov 3, 2012).

YouTube has launched a premium channel initiative for its video content producers to reward these producers for their successes with their channels and to avoid that they will take their popular content elsewhere.

6.3.3.4. Profitability

When Google purchased YouTube, many questioned its ability to monetize the site. Being highly unprofitable at the time, YouTube has managed to turn things around and says it has finally found a business model that works (Lawlers, 2012).

YouTube is predominantly ad-supported platform that account for the majority of their revenues. YouTube has been working to capture metrics that demonstrate that advertising on the site has a higher ROI for brand advertisers than traditional TV ads. With commitments from advertisers such as American Express, AT&T and Unilever, this strategy seems to be paying off (Lawlers, 2012).

To start diversifying its revenue stream, their most recent initiative was to introduce its first incursion into the business of charging users to stream full length feature films. YouTube's first step into this market included films tied to the Sundance Film Festival available for ten days at $3.99 per rental. With 2.684 views the company generated a profit of around $10.000 dollars (Weboart, 2010). This was just the beginning of a pay-per-view program for a growing number of television shows and movie titles.

6.3.3.5. Sustainability

As the Web evolves, it enables YouTube to build the kinds of channels that wouldn't have made sense for cable TV, in the same way cable TV enabled companies to built content that wouldn't have made sense for broadcast. Looking towards the future YouTube plans to introduce a host of new niche channels that offer a broader array of programming, such as live TV and 3D videos and thus become competitive with the three big networks in the USA; ABC, CBS and NBC (Swift, 2011).

6.3.3.6. Mobility

YouTube's mobile version is the #2 video-viewing website in the world (right after YouTube itself) with more than 400 million videos watched on mobile devices every day. That is more than 20% of global YouTube views (YouTube, Nov 2 2012). YouTube works on tablets, Androids, iPhones, Blackberries and other kind of mobile device.

The company has succeeded in monetizing its mobile platform as viewers are able to stream content. Producers are able to share videos and advertisers are able to get maximum reach. As long as YouTube is able to attract the newest content from movies, music and other artwork the viewing will continue.

6.3.3.7. Inimitability

Other players in this market segment include Vimeo and Hulu that have also been very successful. However, YouTube has become dominant in the marketplace due to its partnership with Google.

6.3.4. Overall rating and Key learning

Figure 17 is the overall rating of YouTube according to the 7 Factor Model and key learning in regards to each factor:

YouTube	**Overall rating**	**Key learning**
Scalability (25%)	4	Mass market Promising clash of future niche channels
Uniqueness (20%)	3	Large audience
Loyalty (15%)	3	Diversified customer relationships Affiliate model enhances user engagement
Profitability (15%)	2	Dependent on one key revenue source
Sustainability (10%)	4	Think big towards the future
Mobility (10%)	5	Take advantage of mobile technology evolvements
Inimitability (5%)	3	Competitive market Syndication with Google
Score	**3.4**	**Rank #3 of 7**

Figure 17: Overall rating and Key learning - YouTube

6.4. Twitter

Twitter is a micro blogging service and a social network where users share tweets, photos, and videos with their friends and followers. A tweet is a message supposed to answer the question, *what are you doing* in 140 characters or less. Jack Dorsey created it in March 2006 based on his idea to use SMS service to tell small groups what you are doing. Since then Twitter has become successful worldwide and is one of the top 10 most visited websites in the world with over 500 million users and more than 400 million tweets per day. It is used by people, Medias, and businesses to share information and connect them in real time. Twitter currently ranks nr. 9 on the Alexa list over the most popular global websites in the world (Alexa, 2012).

6.4.1. Business Model Canvas

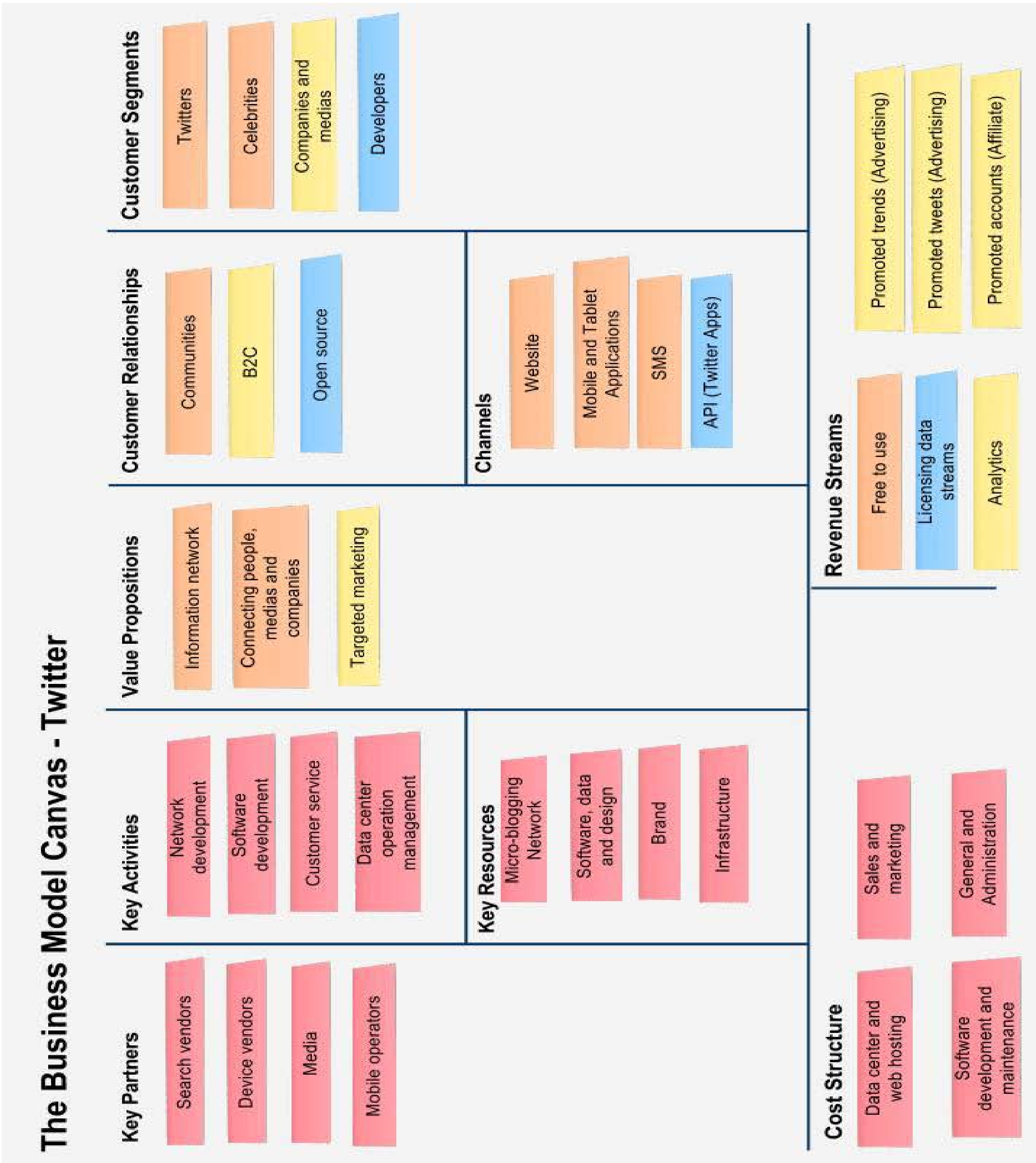

Figure 18: Business Model Canvas – Twitter

6.4.2. Venture capital funding

As demonstrated in Figure 19, Twitter has secured $1.1 billion in eight rounds of venture capital financing from various independent- and incorporated venture capital funds around the globe. Interestingly, each round has been relatively small e.g. compared to Facebook that demonstrates the differences in their vast businesses. A lot of speculation of a potential Twitter IPO has emerged in the last couple of years but the company does not seem to be in any rush of going public. Most likely the company is waiting to see how Facebook's recent IPO will develop so they can learn from their experience (Crunchbase, 2012).

Type	**Date**	**Investor**	**Funding**
Series A	July 2007	Charkes River Ventures, Union Square Ventures, Marc Andreessen, Dick Costolo, Navai Ravikant, Ron Conway, Chris Sacca, Greg Yaitanes and Brian Pokorny	$5 M
Series B	May 2008	Union Square Ventures, Bezos Expeditions, Spark Capital, Digital Garage, Kevin Rose and Timothy Ferriss	$15 M
Series C	Feb 2009	Benchmark Capital, Institutional Venture Partners, Spark Capital, Union Square Ventures, Charles River Ventures and Digital Garage	$35 M
Series D	Sep 2009	Insight Venture Partners, T. Rowe Price, Spark Capital, Benchmark Capital, Institutional Venture Partners and Morgan Stanley	$100 M
Series E	Jan 2010	Not disclosed	$5.17 M
Series F	Jan 2010	Kleiner Perkins and Caufield & Byers	$200 M
Series G	Sep 2011	DST Global	$400 M
Unattributed	Dec 2011	Alwaleed Bin Talal	$300 M

Figure 19: Venture capital funding - Twitter

6.4.3. Assessment of business model

6.4.3.1. Scalability

Twitter has found a way to be present in many diversified niche markets. Twitter is still growing steady in users and numbers of tweets per day. The media is using it increasingly to deliver news, sport brands are reaching out to fans and more celebrities are tweeting. Overall the popularity and brand value of the network is increasing. Furthermore, Twitter uses asynchronous follow model, meaning that a user can follow another user but does not necessary have to be followed back by that user.

Agile technology infrastructure as well as partnerships with search vendors, like Google and Microsoft and device vendors like Apple enable strong linking with operating systems and help media companies to deliver Twitter integration to business and brands more easily. These partnerships are not a large source of revenue but help in expanding user base and drive further scalability for Twitter. The goal has always been to increase number of users that will help attract more advertisers without ruining the ad-free experience of the network.

6.4.3.2. Uniqueness

Twitter key resource is their platform and high brand value. Having all these people sharing the platform with businesses, news media and most of all celebrities is unique. For ordinary people to have the opportunity to interact directly and convincingly to influential people they idolized has been hugely successful for Twitter. Furthermore, Twitter has change the way people consume news by offer live feeds for constant news updates. This instructiveness has strengthened relationships between people, businesses and markets from different parts of the world, connected players beyond size, abilities and market positions.

6.4.3.3. Loyalty

The reputation of Twitter results from the millions of users that count on the service to deliver them news from their friends, the world and their idols. In their early years, Twitter experienced relatively low retention rate of 40% but the growing amount of users and usefulness of the network have let this number and loyalty to grow and made the platform into a community (Nielsen, 2009).

6.4.3.4. Profitability

Interestingly, Twitter has never been under pressure from their investors to turn profit. The real urgency is to protect the long-term value of the platform and protect the user experience. Twitter only started using advertisements on the platform in 2010, after four years of almost no effort in making money from the site. Founder Jack Dorsey explains: “We think of revenue as not a destination but as oxygen that feed the model and vice versa. You can´t build a product without revenue, but can´t focus on revenue without having a product either” (Barnett, 2012).

Contrasting to most other social media sites, Twitter does not display ads on its platform but instead provides advertisers with modern ways to reach customers with promoted accounts, promoted tweets and promoted trends (Twitter, 2012):

Promoted accounts: are offered through Cost-Per-Followers, where business is charged when a user converts into follower. These accounts appear in search results and who-to-follow section.

Promoted tweets: are cost-per-engagement auction. Businesses can promote messages to followers and non-followers.

Promoted trends: Business can benefit from Promoted trends, product to scale conversations and build mass awareness. Promoted trends appear at top hottest topics of discussion next to user’s timeline.

Twitter uses the *affiliate* model for promoted accounts and the *advertising* model for promoted tweets and promoted trends.

6.4.3.5. Sustainability

The company is still some years from fully monetizing its platform. Twitter is reported to have made around $45 million in 2010 and between $140 and $165 million in 2011. This revenue is projected to grow significantly when the promoted products are fully operational and could hit $1 billion in 2016. Twitter was in 2011 valuated around $8 billion (O´Dell, 2011).

Open source projects supports this strategy by constantly improving the platform and satisfying the needs of growing amounts of users and their engagement.

6.4.3.6. Mobility

According to Twitter's CEO, Dick Costolo, the majority of Twitter users are mobile and those users are more active and have higher level of engagement than non-mobile counterparts. (Farber, 2012)

Tweets are 140 characters and the platform is suited for mobile usage. Moreover, the advertisement platform is designed to make revenue from mobile that gives Twitter great competitive advantage for the future. Twitter´s growth has been driven through Twitter API and thousands of software developers that could now be a threat to Twitter's commercial success because to effectively monetize their platform they need to own the entire user experience.

6.4.3.7. Inimitability

Twitter is currently monopolizing the micro-blogging market segment. The only direct competition is from social media companies in other market segments in regards to user time spent online.

6.4.4. Overall rating and Key learning

Figure 20 is the overall rating of Twitter according to the 7 Factor Model and key learning in regards to each factor:

Twitter	Overall rating	Key learning
Scalability (25%)	2	Diversified niche market Asynchronous follow model Synchronization
Uniqueness (20%)	4	Attract interesting people
Loyalty (15%)	3	Usefulness of network
Profitability (15%)	4	Profitable Modern ways to reach customers Ability to monetize mobile application
Sustainability (10%)	4	Promising operational strategy in place
Mobility (10%)	5	API enhances platform development High level of mobile user engagement
Inimitability (5%)	4	Monopolizing the market segment
Score	**3.5**	**Rank #2 of 7**

Figure 20: Overall rating and Key learning - Twitter

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6.5. Tumblr

Tumblr is a blogging platform and a social networking website that lets users post text, photos, quotes, links, music and videos through their server. Users can customize their blogs, from colors to content. Tumblr was founded in February 2007 by David Karp from his bedroom in his mother's apartment in New York and quickly became popular amongst bloggers and artists that found the site refreshing. The site gained 75.000 users in the first fortnight and now hosts more than 81 million blogs, ranging from people, pets to politics. Tumblr currently ranks nr. 36 on the Alexa list over the most popular global websites in the world (Alexa, 2012).

6.5.1. Business Model Canvas

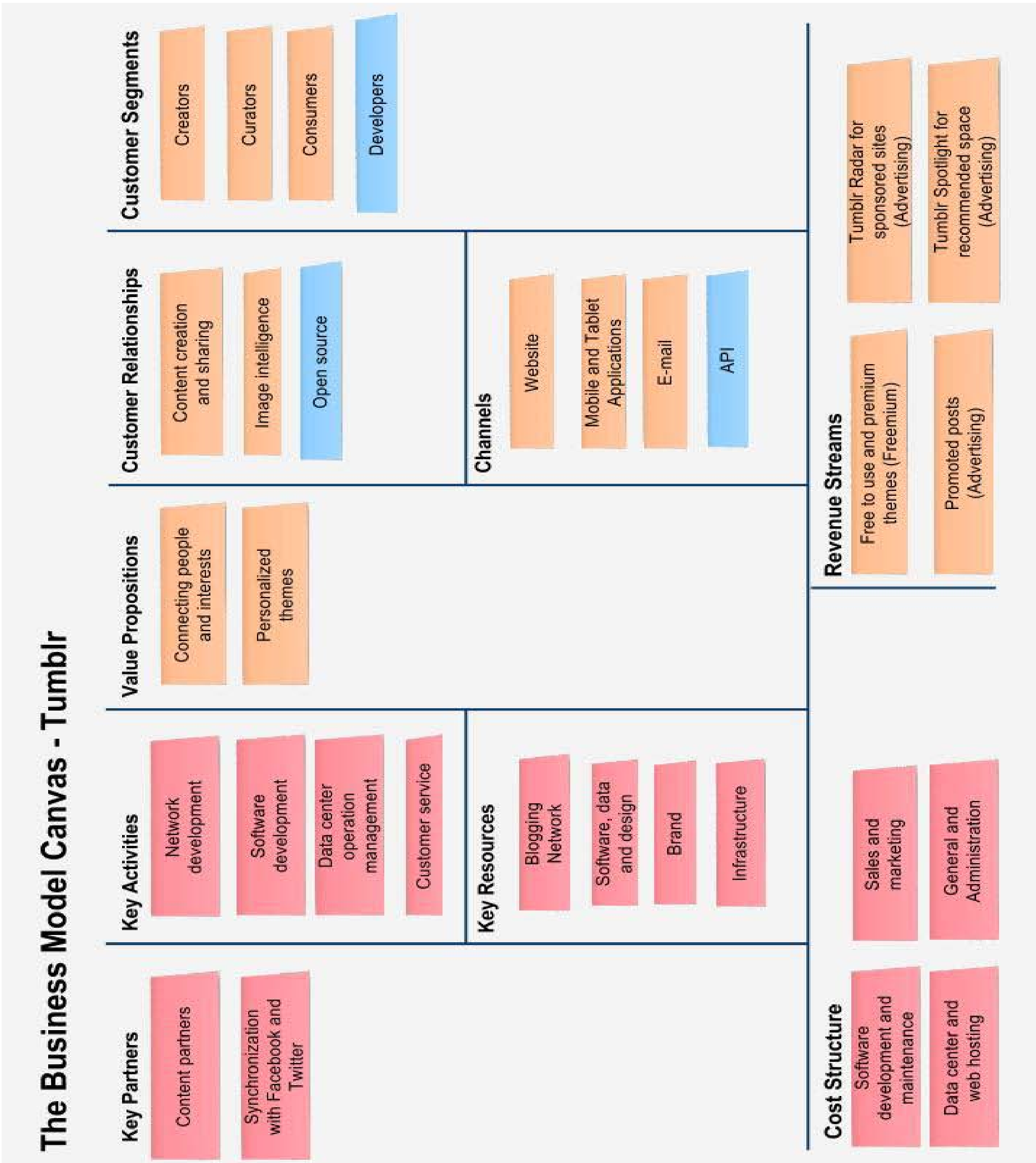

Figure 21: Business Model Canvas – Tumblr

6.5.2. Venture capital funding

Tumblr has managed to raise $125 million in five rounds of financing from major venture capital funds as well as from the philanthropist Sir Richard Branson, as demonstrated in Figure 22. As the company is still in late stage development it has not yet reached its exit point and moreover it is not yet clear what the preferred exit strategy will be (Crunchbase, 2012).

Type	**Date**	**Investor**	**Funding**
Series A	Oct 2007	Spark Capital and Union Square Ventures	$750 K
Series B:	Dec 2008	Union Square Ventures and Spark Capital	$4.5 M
Series C:	April 2010	Union Square Ventures and Spark Capital	$5 M
Series D:	Nov 2010	Union Square Ventures, Spark Capital and Sequoia Capital	$30 M
Unattributed	Sep 2011	Greylock Partners, Insight Venture Partners, Chernin Group, Richard Branson, Spark Capital, Union Square Ventures and Sequoia Capital	$85 M

Figure 22: Venture capital funding - Tumblr

6.5.3. Business model assessment

6.5.3.1. Scalability

Tumblr has implemented a multi-side platform for content, creation and sharing as well as an asynchronous follow model for maximum reach. Tumblr divides its users into three niche categories (Walker, 2012):

- **Creators:** producing the bulk of original content
- **Curators:** who harvest the best work content and re-blog for larger audiences
- **Consumers:** that are the largest user base on Tumblr

The company is growing around 30% in numbers of users per month and has over 500 million page views a day. Despite this incredible growth, Tumblr needs to attract hundreds of millions more subscribers on its route to profitability (Ante, 2011). Luckily for the company, the blogging platform may be recent but nerdy obsessions with stuff are as timeless as ever (Leach, 2011).

Tumblr's growth has not been without challenges. The company is still building up its technology infrastructure to support its growing demand. The direction Tumblr is currently moving is towards a distributed services model and intriguing cell based in-house architecture for powering their platform. This should allow Tumblr to extrapolate transition at massive scale (High Scalability, Nov 3, 2012). Their focus for the future will be simplifying the way people share their content through open source development.

6.5.3.2. Uniqueness

For years, blogs with beautiful themes, style and content were only available from design studios and art institutions, until Tumblr. David Karp's vision to allow anyone to easily implement a high-art template, source quality content and share virally has changed the way people think about blogs, which is unique (Aten, 2012).

6.5.3.3. Loyalty

There is little to no learning curve involved in using Tumblr. Features are intuitive and quick to establish. Subscribers simply sign up and begin posting in a minute. Consequently the company is able to sustain a high retention rate. People write in-depth content that's worth reading so people stay for hours (Dannen, 2009).

6.5.3.4. Profitability

The venture capitalists that have put money into the company are losing patience with Tumblr's lack of successful business model and revenue. The company's lack of revenue even prevented some venture capital funds from participating in the latest funding round (Ante, 2011).

The company has build their advertising products around creative brands and what the advertisers to try to create intent rather than to capture it. So far, the company has no proven revenue model but has tested revenue plans like the *freemium* model for premium themes and the *advertising* model for sponsor products and promoted posts (Tumblr, 2012):

Premium themes: that allows designers to create premium themes and sell to users.

Sponsor products: that highlights content from advertisers or sponsors. Tumblr Radar is meant to showcase the most creative and interesting media on the Tumblr network and advertisers will get a dedicated share of attention with the opportunity to gain thousands of new followers, likes and reblogs. Then, Tumblr Spotlight features a sample of the most talented creators on Tumblr that are featured front-and-center on a recommended space

Promoted posts: where users can highlight single posts for a dollar price which then puts a sticker on the post that lets people know it is extra important.

However, these efforts have not yet paid off. The company will therefore continue in its efforts to proof to investors and its subscribers that it can become profitable.

6.5.3.5. Sustainability

People will always look for opportunities to share high quality content. But this is a highly competitive market in all directions. Tumblr has sometimes been describes as Twitter meets YouTube and Wordpress. Tumblr will therefore need to focus on finding its identity to sustain its customer loyalty and stay relevant in the social media eco system.

6.5.3.6. Mobility

Tumblr's mobile version is simple and convenient because Tumblr users can capture photos and write messages with their mobile phones and immediately upload on their blogs. However, Tumblr's mobile platform reformats the user blogs by removing themes, background images and other Flash content, resizes images and changes text to black on a white background. Consequently it removes a great deal out of their user experience and makes it difficult for users to differentiate themselves.

6.5.3.7. Inimitability

Users create content and have access to other people's content hundreds of pages back into the platform. Other social media are mostly live streams of current events that the users sample while Tumblr is more knowledge bound.

6.5.4. Overall rating and Key learning

Figure 23 is the overall rating of Tumblr according to the 7 Factor Model and key learning in regards to each factor:

Tumblr	**Overall rating**	**Key learning**
Scalability (25%)	3	Diversified niche market Asynchronous follow model Synchronization
Uniqueness (20%)	2	Beautiful designs attract users
Loyalty (15%)	3	High retention rate Easy to use
Profitability (15%)	1	Unprofitable business models cannot last forever
Sustainability (10%)	3	Lack of focus
Mobility (10%)	3	Simple mobile platform
Inimitability (5%)	3	Competitive market Accessibility to mass content
Score	**2.5**	**Rank #7 of 7**

Figure 23: Overall rating and Key learning - Tumblr

6.6. Pinterest

Pinterest is a virtual pinboard that allows its users to collect their online memories and share them on the web by using pins. A *pin* is an image added to Pinterest. Pinterest was founded in March 2010 by Ben Silbermann, Paul Sciarra and Evan Sharp. Ben Silbermann got the idea when planning for his own wedding and trying to gather his inspirations from all around the web. He wanted to create a platform where users could discover new things and get inspiration from people who share their interests. The first prototype was only available to a small group of colleagues and family members but quickly developed into one of the fastest growing social media sites in the history of the web. The site now tracks more than 25 million unique visitors per month. Pinterest currently ranks nr. 38 on the Alexa list over the most popular global websites in the world (Alexa, 2012).

6.6.1. Business Model Canvas

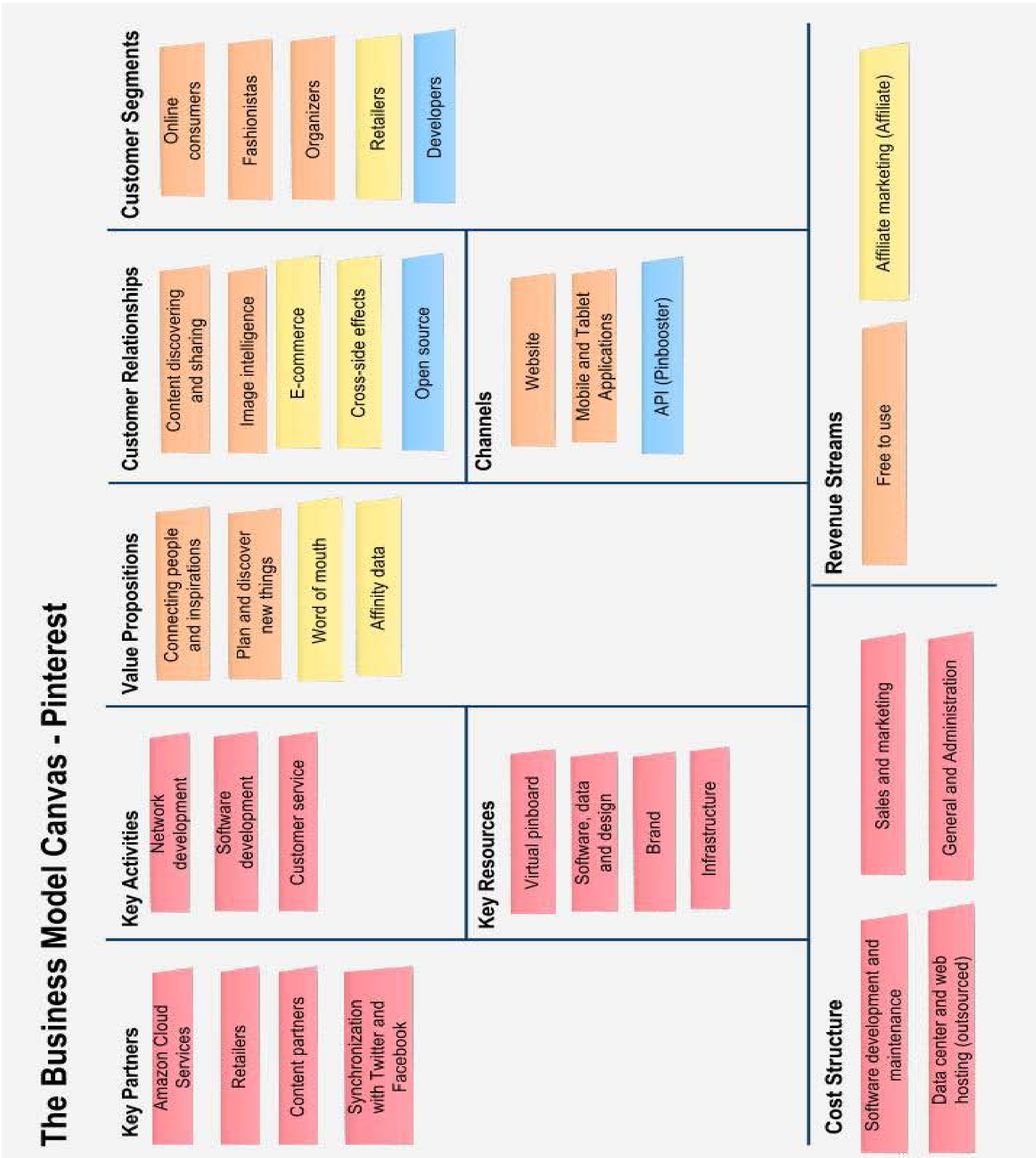

Figure 24: Business Model Canvas – Pinterest

6.6.2. Venture capital funding

Pinterest is the fastest company to raise $100 million in venture capital financing ever. As demonstrated in Figure 25, the company has secured $137 million from various venture capital funds. Many have questioned why venture capitalists would want to invest in a company with niche market potential, no revenue model and limited users. The possible answer is that these funds believe that the company has a promising future as a leading e-commerce platform that will sustain its growth and valuation. As the company is still in early development it is difficult to speculate on exit but as it seems now the company would make an ideal acquisition for a larger company wanting to gain influence in this market segment (Crunchbase, 2012).

Type	Date	Investor	Funding
Angel	Jan 2010	Jack Abraham, Michael Birch, Scott Belsky, Shana Fisher, Kevin Hartz, Jeremy Stoppelman, Brian Cohen, Fritz Lanman, Hank Vigil and FirstMark Capital	$500 K
Series A	May 2011	Bessemer Venture Partners, Kevin Hartz, Max Levchin, Jack Abraham, Michael Birch, Ron Conway and FirstMark Capital	$10 M
Series B	October 2011	Andreessen Horowitz, Bessemer Venture Partners and FirstMark Capital	$27 M
Venture round	May 2012	Rakuten, Andreessen Horowitz, FirstMark Capital and Bessemer Venture Partners	$100 M

Figure 25: Venture capital funding - Pinterest

6.6.3. Assessment of business model

6.6.3.1. Scalability

Pinterest is a multi-side platform bringing consumers and businesses together. It utilizes asynchronous follow model and synchronization with Facebook and Twitter to enable new users to instantly connect to their friends of other platforms. This setup boosts the size of every individual network and thus empowers the entire Pinterest network.

Pinterest focus is on growing its platform and making it more valuable. By outsourcing a large deal of their technology infrastructure to the Amazon Web Services, the company has been able to be more efficient and try out new experiments at low costs while maintaining a very small team (High Scalability, Nov 5, 2012).

6.6.3.2. Uniqueness

Pinterest has a strong position in the social media marketplace as virtual storefront driving customers to businesses. Many retailers and small brands are taken advantage of Pinterest to get traffic on their websites and buzz around their products. One of Pinterest's key assets is its web design that provides an ideal layout for style conscious retailers where products can easily be visualized within a consumer context. These retailers are using Pinterest as an affiliate for online referrals that link users with similar interests to a company (Brave, 2012).

Consumers seek product info via social media to determine best price, value and quality offering. Pinterest is special because of the people who use it. Expressing passion for an interest is just as easy as browsing for the customer's next purchase. Even more addictive is that Pinterest is just as much about the users as it is about what they have posted (Kessler, 2011).

6.6.3.3. Loyalty

Pinterest makes all the best images on the web available on one platform and gives its users the chance to easily express themselves using these images. A user can add a pin from a website using the *Pin It* button or by uploading images from their computers. Each pin added links back to the site it is originated from. Users can then organize their set of pins into boards that can be created on any topic of interest. Consequently Pinterest is able to maintain a high user engagement.

6.6.3.4. Profitability

Pinterest is completely free to use. Pinterest has tested a few different approaches to making money, like testing the *affiliate* model, but did not succeed and still remains unprofitable. Pinterest states: "Even though making money isn't our top priority right now, it is a long term goal. After all, we want Pinterest to be here to stay" (Pinterest, 2012).

6.6.3.5. Sustainability

Pinterest is dependent on the future growth of e-commerce. Pinterest value is derived from the company's ability to drive traffic to retail sites. Therefore, the company's largest business opportunity is to become a promising marketing platform that collects data for retail companies and marketing strategists. Mining information about interests and affinities of users could be priceless as such affinity data reveals valuable relationships between consumer behaviors, products and content that can then be used to create more targeted marketing (Brave, 2012).

Most of the content on Pinterest is actually posted in violation of both the law as well as Pinterest's own terms of service. However these violations don't seem to hurt any constituency bad enough to bring pressure that could break the company (Poletti, 2012).

6.6.3.6. Mobility

Pinterest's mobility is enhanced with the custom-designed mobile- and tablet applications that give the users a new way to engage with pins. One could say that Pinterest's browser experience is ideal for the small attention spans of web readers as there is almost no text, almost all pictures. This differentiates Pinterest from other social media companies as adding a pin to a list from anywhere is much easier than writing a blog post or uploading an image to a photo-sharing service. However, Pinterest still needs to improve its customer interface with mobile applications, as it is currently problematic for users to pin content in the mobile web application. The experience is therefore limited to the Pinterest application, unlike when browsing on a desktop counterpart.

6.6.3.7. Inimitability

The market for photo sharing is competitive and given the nature of these companies they can be easily imitated. If Pinterest succeeds in becoming a leading marketing platform in social media it will benefit from having all the necessary partnerships that will sustain their brand and reputation

6.6.4. Overall rating and Key learning

Figure 26 is the overall rating of Pinterest according to the 7 Factor Model and key learning in regards to each factor:

Pinterest	**Overall rating**	**Key learning**
Scalability (25%)	4	Segmented niche Market Asynchronous follow model Synchronization Amazon Cloud Scalability
Uniqueness (20%)	2	Bringing social media and e-commerce together
Loyalty (15%)	2	Availability of pictures in one place High user engagement
Profitability (15%)	1	Not profitable yet
Sustainability (10%)	3	Promising marketing platform for affinity data Dependent on future growth of e-commerce
Mobility (10%)	4	Pictures work well with mobile
Inimitability (5%)	1	Competitive market
Score	**2.6**	**Rank #6 of 7**

Figure 26: Overall rating and Key learning - Pinterest

6.7. Instagram

Instagram is a free mobile photo sharing application and social network. Entrepreneurs, software designers and Stanford graduates, Kevin Systrom and Mike Krieger, launched it in October 2010. Only 18 months later, Facebook acquired Instagram for $1 billion, making everybody involved multimillionaires. Originally built as a mobile application for Apple´s iPhone 4, Instagram exploits the high-resolution camera for taking a picture, tweak it, write a caption and share it with the world. For the first 24 hours, 25.000 users signed up, after three months they were 1 million and in April 2012, there were over 30 million accounts. Instagram currently ranks nr. 92 on the Alexa list over the most popular global websites in the world (Alexa, 2012).

6.7.1. Business Model Canvas

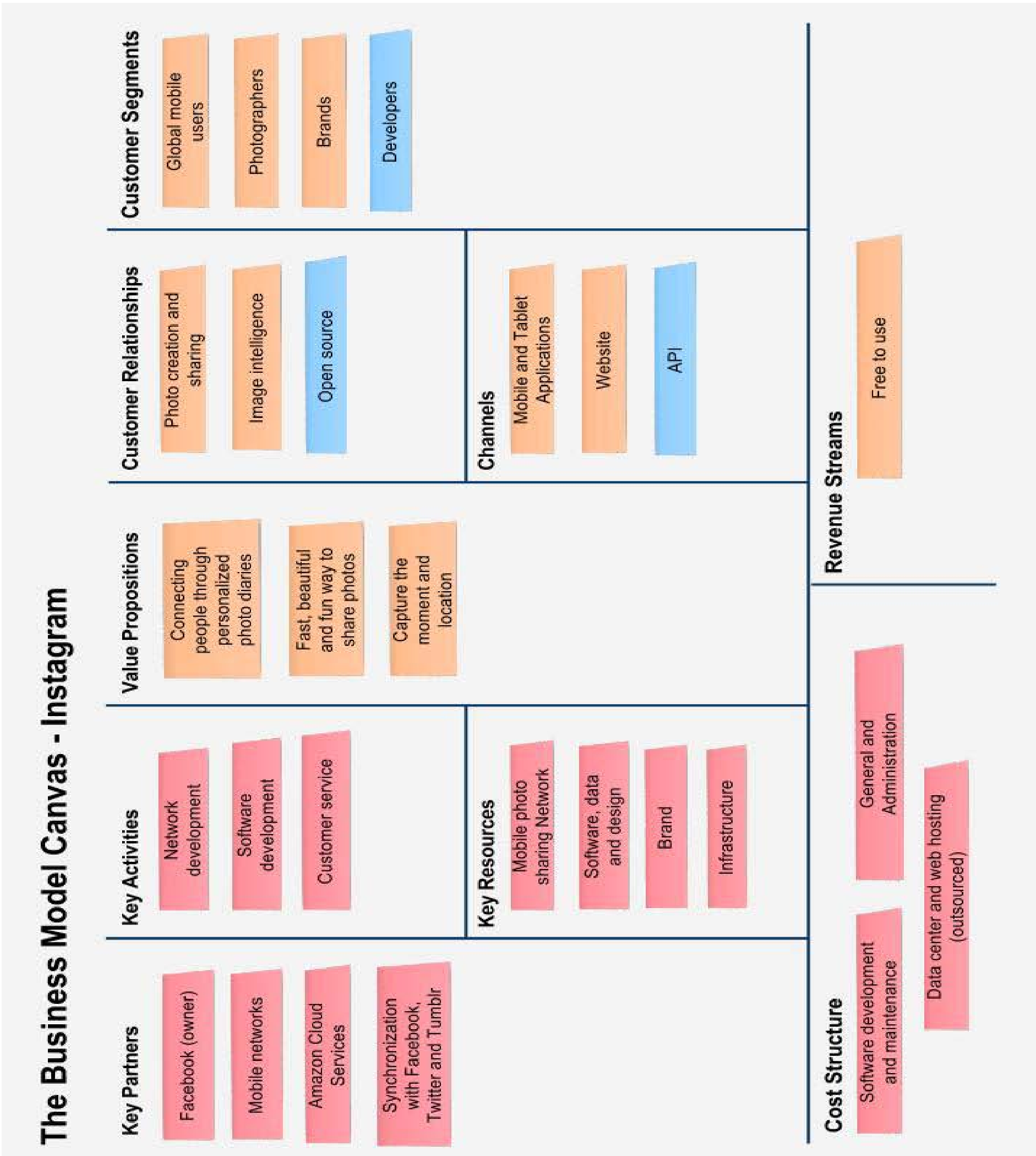

Figure 27: Business Model Canvas – Instagram

6.7.2. Venture capital funding

The $1 billion acquisition by Facebook has become inspiration to many start-ups on why making money is not necessarily so urgent. Instagram has always been completely free to use and the only financing has been from venture capitalists that provided $57.5 million in total of seed- and start-up investment needed to develop the company, as demonstrated in Figure 28 (Crunchbase, 2012). Today this strategy of having millions of users with zero revenue is often referred to as the *Instagram business model*.

Type	**Date**	**Investor**	**Funding**
Seed	March 2010	Andreessen Horowitz and Baseline Ventures	$500 K
Series A	February 2011	Adam D'Angelo, Jack Dorsey, Chris Sacca, Baseline Ventures and Benchmark Capital	$7 M
Series B	April 2012	Sequola Capital, Thrive Capital, Greylock Partners, Benchmark Ventures and Baselines Ventures	$50 M
Industry sale	April 2012	Facebook	Valuation: $1 B

Figure 28: Venture capital funding - Instagram

6.7.3. Assessment of business model

6.7.3.1. Scalability

Instagram has a simple platform with simple purpose as it is based on mobile technology for mobile usage only. Essential to the quick success of Instagram was the free subscription (compared to their early competitor, Hipstamatic which cost $1.99 in Apple store) and syndication with Facebook and Twitter. This syndication creates buzz and Instagram is still growing because of their asynchronous follow model, word of mouth and network effects.

Instagram targets mass market which fits well with its integration with Facebook. Now it has 100 million users, up from 30 million users since Facebook acquisitions in April 2012 (Taylor, 2012). For handling such a rapid growth the company uses open source projects, building the service by exposing API and external service. The growth has been very fast but the company has been able to keep it small with only three engineers to run the service because it is using Amazon cloud services.

After the Facebook acquisition it looks like Instagram has all the possibility for further scalability. With connection to Facebook's 1 billion users, back up from their enormous data center and prompt growth in smartphone and tablets usage worldwide, indicate a promising future for Instagram.

6.7.3.2. Uniqueness

Instagram has succeeded in influencing its users to feel creative and more importantly appear creative to others. Snapping a photo with Instagram and personalize it makes that photo seem inspired. When users hit the button to share with friends there is a satisfying feeling of anticipation that others will be impressed by the user's creation.

6.7.3.3. Loyalty

Users have made their personalized photo diary photos and a network with their friends on Instagram. This can create a lock-in for the user because he is not willing to give that up for something else. This profile and a strong connection to the user's Facebook profile, which has extremely high loyalty, make also high customer loyalty for Instagram.

Brands have also taken the opportunity to reach out to customers to create a buzz around their products.

6.7.3.4. Profitability

Before the $1 billon acquisition by Facebook, Instagram had zero revenue and no business model. For young start-up like Instagram, revenues are maybe not the best indicator for price valuation. The value was in acquiring talented team of designers, the best mobile photo application, fastest growing social network, tens of millions of users and endless additional mobile engagement.

According to CEO Kevin Systrom Instagram has considered various means of making money but nothing came out of it (Thomas, 2012).

6.7.3.5. Sustainability

Instagram has proved to be the best mobile photo sharing application on the market and has grown even stronger because of network effects. They have shown that focusing on keeping everything simple can be very efficient to sustain customer satisfaction. For them to stay on top they need to enrich their value propositions and continue to let people curate their own user experience. Popularity of Instagram was demonstrated when distinguished newspaper New York Times started using a Instagram column on their website to cover both news of the USA presidential election and hurricane Sandy in November 2012

6.7.3.6. Mobility

In November 2012, Instagram introduced a website service, making the network for the first time available to others than mobile app users. This interface should secure Instagram as an independent social media. Taking photos, progress them and share them with friends is just going to increase with growing smartphone engagement.

6.7.3.7. Inimitability

There are lots of mobile applications with similar usage to Instagram but none of them have come close to their success. The high profile brand name and close syndication to Facebook, the largest social network and millions of users who already have created their own photo album profile on the network will be hard to win over for rivals.

6.7.4. Overall rating and Key learning

Figure 29 is the overall rating of Instagram according to the 7 Factor Model and key learning in regards to each factor:

Instagram	**Overall rating**	**Key learning**
Scalability (25%)	5	Mass market Completely free for all Asynchronous follow model Synchronization Amazon Cloud Scalability
Uniqueness (20%)	2	A picture is worth a thousand words
Loyalty (15%)	3	Let people curate their user experience
Profitability (15%)	1	Product first, money later
Sustainability (10%)	4	Independent mobile applications can succeed
Mobility (10%)	3	Keep it simple
Inimitability (5%)	3	Competitive market Syndication with Facebook
Score	**3.1**	**Rank #4 of 7**

Figure 29: Overall rating and Key learning - Instagram

6.8. Sub Conclusion

The overall rating from each case study is summarized in the Radar Chart in Figure 30 below:

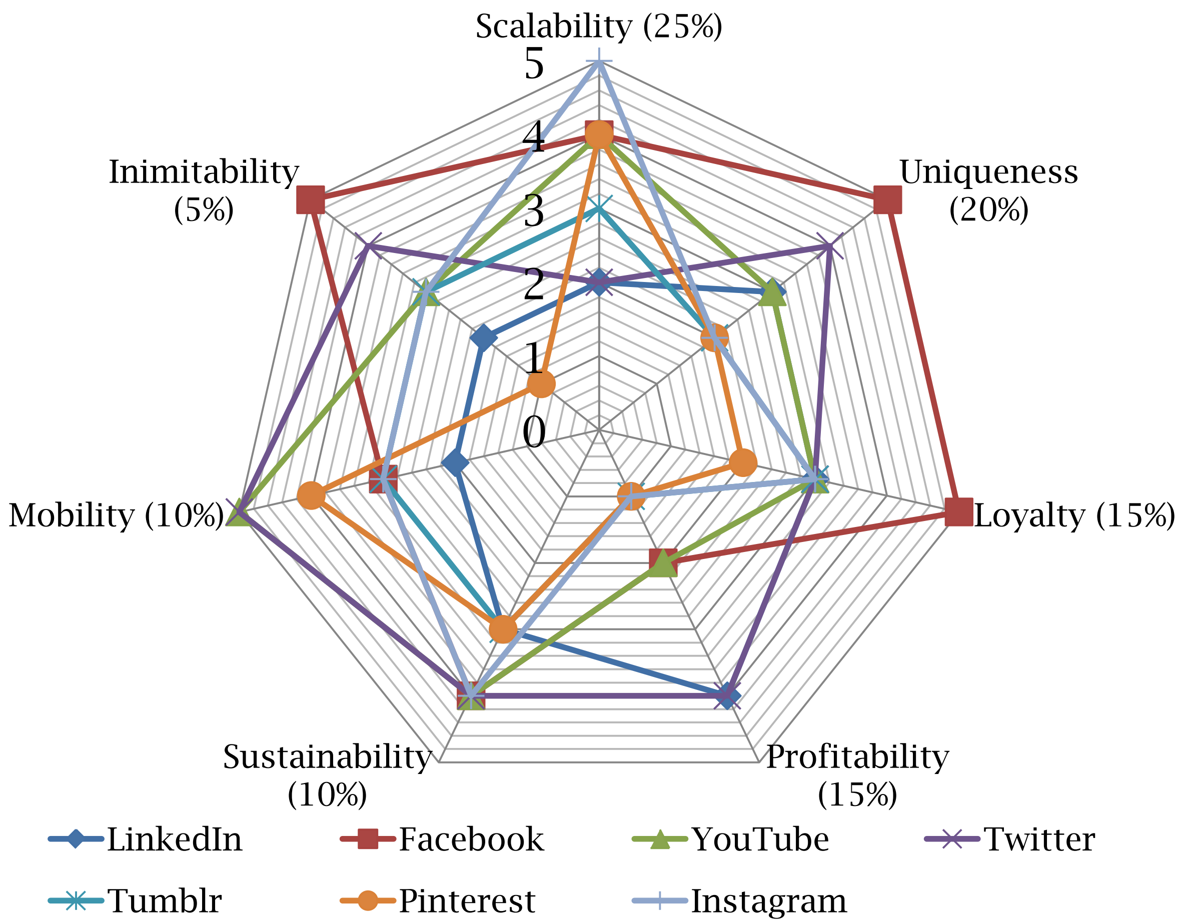

Figure 30: Radar Chart - Overall rating

While there remain clear differences between the seven cases, there are also a number of important similarities. The most notable similarities that can be derived from the chart above are that companies that have high *scalability* usually have low *profitability* and vice versa. Moreover, companies that have high *uniqueness* and *loyalty* usually have high *inimitability* and vice versa. Likewise companies that have high *mobility* have high *sustainability* and vice versa.

Interestingly high scalability seems to be at the cost of low profitability. Instagram and Pinterest that are highly focused on the *product first, money later* philosophy have shown that enormous growth is possible in a short period of time without generating any real revenue. By allowing synchronization with other social media and asynchronous follow model, the companies have been able to boost individual network growth. For more efficiency, the use of external cloud services allows these companies to try out new experiments at a low cost while maintaining a small team. This scalability compensates for the high valuation that the companies have received without having shown any sign of future revenue streams. However, Tumblr that is farther in the lifecycle has demonstrated that being unprofitable cannot last forever as venture capitalists feel the urge to monetize more now because the economic environment has changed. Instagram has already been acquired by Facebook. But how long Pinterest can focus only on scalability without venture capitalists losing its patience is yet to be seen.

For the more established companies, it is interesting to see that Facebook and YouTube have so far not been able to fully monetize their platforms. In a constantly evolving social media industry they are too dependent on one revenue source; the advertising model. Twitter and LinkedIn that are using more diversified and innovative revenue models are proofing to be more profitable.

Facebook and Twitter were found to employ the most unique business models. Their ability to activate their multi-side platforms and constantly develop their product and service offering allows them to attract businesses and interesting people. Knowing what users want, before users realize what they want makes their value propositions unique. Consequently users stay loyal to the services because they love the product but also because leaving would hurt their social media identity. As the companies have made themselves indispensable in the eye of the users they are difficult to imitate which makes the barriers of entry high in their respective market segments. On the contrary, Tumblr's, LinkedIn's and Pinterest's inability to create a convincing sentimental value for its users makes their business model less unique and reduces customer loyalty. Consequently the barriers of entry are lower for their market segments.

Companies that were found to have responded most efficiently to technology evolvements and thus have the highest level of mobility are YouTube and Twitter. These companies are able to show high level of mobile user engagement while being able to monetize their mobile platforms, counter to e.g. Facebook and LinkedIn. Successful mobility has ensured their sustainability in the growing mobile world that allows them to think big towards the future. Likewise Pinterest, Instagram and Tumblr show that pictures work well with mobile technology and simple applications are more likely to succeed. By acquiring Instagram, Facebook has taken a step towards improving its photo product offering and to increase their user's level of mobile engagement. Enhancing mobility boosts sustainability as the companies are striving to stay relevant in a competitive and creative environment.

As a result the companies are ranked in the following order in regards to the 7 Factor Model:

- #1 Facebook
- #2 Twitter
- #3 YouTube
- #4 Instagram
- #5 LinkedIn
- #6 Pinterest
- #7 Tumblr

7. Outlook

Social media is not going anywhere. The industry is a market of 2 billion users that has an unprecedented level of opportunity. Speculation of social media bubble, similar to the IT bubble that burst in 2001, has emerged. However it is interesting to look at the different level of historical investment activity that has been in the software industry to determine if this really is a bubble. As can be seen in Figure 31, there is a significant difference in the level of investment today as compared to the millennium where the industry peaked (PricewaterhouseCoopers, 2012) making it more of a wave than a bubble.

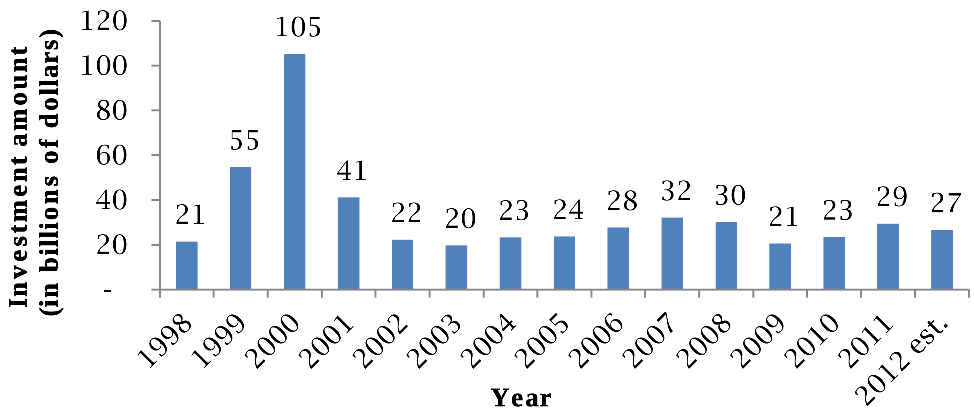

Figure 31: Historical Venture Capital Investments in the Software Industry

History of venture capital investments tells us that the social media wave will run its course and a new wave of innovation will follow. As investors will start moving more money into mobile and other emerging technologies it is apparent that investments into social media will follow as the industry is tightly connected to the future of these other technologies. The first wave of social media may be over but the industry is just beginning to deliver on their value potential. Untapped potential in social media is estimated to reach $1 trillion in the near future (McKinsey & Company, 2012).

At the moment, LinkedIn, Facebook, YouTube, Twitter, Tumblr, Pinterest and Instagram are perceived market leaders in *winner takes it all* market segments. To sustain their position in the future the companies need to figure out how to best leverage their position in the industry or risk missing out of the untapped potential.

We have examined what paths might exist for these companies and how business model innovation can help them evolve.

Social shopping

It is believed that share of consumer spending could be influenced by social shopping. It is still early but no company has been able to connect e-commerce efficiently to social media yet, but with Pinterest there is now a real opportunity for intense engagement of users on social platforms for shopping.

If Pinterest could find a way to enhance social shopping or try to create a way where their user's social information would give businesses more targeting information, it could become a leading marketing platform. This could be a very interesting business because it allows companies to gain priceless information about their customers and their affinities towards their products.

Venture capitalists are funding a lot of new and innovative social shopping concepts, like Sugar, Moguji, Blippy, Svpply and Endorse, that will fight hard to beat Pinterest. Pinterest will therefore have to speed up its business model development to make sure to come out first.

Communication and Collaboration

The latest successful platforms are more about distribution than content. Twitter, Tumblr, YouTube, LinkedIn and Facebook are distribution platforms for content. But the content itself can be a valuable area. The ability of social media to influence communication and collaboration enable societies to work more efficiently together. One or more of these companies could utilize its business model to keep changing the way people consume news, education and knowledge. For instance they could provide students all over the world with Ivy League education online, businesses with collaboration projects between continents, viewers with niche channels that offer a broad array of programming, patients with healthcare service and lead to more participatory governance processes and more responsive governments.

Video mobile sharing

With the success of Instagram in mobile photo sharing, the simplicity and how well they utilized the mobile phone technology it is not long to wait until mobile video sharing will come along. With 4G technology users will be able to post clips from their real life building on the same model that has worked well for Instagram. In the race towards building up technology which allows live video sharing directly from the user's mobile phones, Instagram and indeed YouTube will face fierce competition from new venture capital backed start-ups, such as Color, Socialcam and Viddy.

Social shopping, communication and collaboration and video mobile sharing are only a fraction of the opportunities that lie within the future of social media. These are simply the ones we find to be most suitable for our case companies and their future business model innovation.

8. Conclusion

Taking part in creating new industry and a new present for people around the world has led social media start-up companies to engage in business model innovation. At first glance these companies look pretty similar but when taking a closer look one will note that they are indeed very different and that the business model is the main facilitator for creating these distinctive features. Employing a strong business model allows these businesses to adopt in constantly moving business environment and thus can have a significant effect on the success or failure of the company.

The social media industry growth is accelerating as a result of continuous improvement in social and mobile technology causing more time being consumed online and creating higher user engagement. Social media is a leading force in time spent online as it appeals to the most basic human behavior, forming groups, entertain and communicating exciting content and providing a place for users to tell their stories. Continued success of social media companies will therefore depend on their ability to adjust their business model to travel on the speed of social.

The growth of social media would not have been possible without the involvement of venture capitalists that have favored investments in social media with billions of dollars and minutes spent on these companies. The quest for the next big thing in networking, sharing, content creation, shopping and more has put both high valuation and hope on this industry. However, only a small amount of these investments succeed.

We believe that standardizing the process for venture capital can be helpful as they receive thousands of investment requests and often operate according to the four eye principle. The process is therefore frequently based on personal judgment and experience. Standardized process should help certify that no important aspects are ignored, increase the efficiency of the investment criteria for social media start-up companies and thus increase the likelihood of venture capitalists selecting the future winners in a particular market segment.

For this purpose we created the 7 Factor Model; a practical evaluation tool, to assess business models in social media. The factors in the model are scalability, uniqueness, loyalty, profitability, sustainability, mobility and inimitability. This we combine to the

Business Model Canvas to conduct case studies on seven successful venture capital founded social media companies. We have mapped key similarities and differences from these companies to gain valuable insights and learn from their experiences.

From the case studies, interesting findings can be derived from the result of the 7 Factor Model. Facebook and then Twitter received the highest score, within the sample, and are as a result perceived to be operating the best business models in the social media industry today. Both companies have unique features to activate all aspects of their business, causing high loyalty and constantly growing user engagement. The results show clear similarities between uniqueness, loyalty and inimitability and also between mobility and sustainability. Most interestingly it shows strong connection between high scalability and low profitability. The product first, money later mindset appear to be presiding as the two early stage companies, Pinterest and Instagram, both have tremendous user growth but no real revenue model. High market valuation on these companies, therefore only seem to come from their high growth and future revenue prospects.

It is apparent that revenue models are a driving factor in the long term success of a social media start-up companies. However as we mentioned, many early stage social media companies have proven to be successful without having any source of revenue and therefore other factors need to be considered when analyzing these companies. All these companies have different profiles and therefore it is not possible to find one right way that fits all companies but instead it is important to evaluate the companies individually and in regards to their distinctive characteristics. One thing is certain; which company will stay on top will be a constant struggle of the survival of the fittest.

Therefore, implication for further research is to take the 7 Factor Model to work and involve venture capitalists in further development of the tool. We reckon that our results would be more significant if a larger sample had been used. Thus, the 7 Factor model would preferably be build into a program that would facilitate statistical testing on the factors in regards to the Business Model Canvas and tested on a larger sample of social media start–up companies that are present on various investment stages and across market segments.

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