

# **Business Model of Facebook**

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## **Introduction**

Mark Zuckerberg, Chris Hughes, and Dustin Moskovitz, founders of the Facebook.com phenomenon, saw an existing product in need of improvement and expansion.

A facebook is a book that is made up of photographs of individuals along with their names. Facebooks are often published at the start of the academic year by the administrations of colleges and universities, with the intention of helping students, faculty, and staff to get to know each other better. A facebook may be contrasted with a yearbook, which is traditionally published at the end of the academic year and usually includes details about various aspects of the preceding year, along with the sort of content one would find in a facebook. (Wikipedia)

Facebook.com is an online database of everything the old paper facebook had and more.

Sources: 2, 6

## **The Business Model**

Business model is the mechanism by which a business intends to generate revenue and profits. It is a summary of how a company plans to serve its customers. It involves both strategy and implementation. It is the totality of:

- How it will select its customers
- How it defines and differentiates its product offerings
- How it creates utility for its customers
- How it acquires and keeps customers
- How it goes to the market (promotion strategy and distribution strategy)
- How it defines the tasks to be performed
- How it configures its resources
- How it captures profit

There are many different types of business models as some are more complex than others depending on the service. A few examples of types of business models are as follows:

- The subscription business model
- The razor and blades business model
- The pyramid scheme business model
- The multi-level marketing business model
- The network effects business model

Facebook fits into the network effects business model, which was pretty common in the dot-com boom of the late 1990s. This type of business model is based on the network effect which causes a good or service to have a value to a potential customer dependent on the number of customers already owning that good or service. Facebook fits this model because the more registered users there are on the site, the more useful the site is. In this paper I will discuss Facebook's business model using the eight criteria above.

Sources: 7

### **How it will select its customers**

Facebook's selection of customers is a very important part of the company's business model. Social networking sites have been on the rise in the last decade and many are in existence today including MySpace, Friendster, and LiveJournal. Most of these social networking sites are not very specific and have a variety of users. This fact is what makes Facebook's selection of customers so important. Zuckerberg developed a personal niche for his site in making it specifically for high school (recently), college and university communities, primarily in the United States.

### **How it defines and differentiates its product offerings**

The second aspect of a business model is how the company defines and differentiates its product offerings. One of the key elements to Facebook's success is differentiation, particularly from the social networking giant, MySpace. What makes a student with an existing MySpace account want to register with Facebook? The answer to this question lies in how Facebook sets itself apart from other social networking sites. Facebook is the only brand of these sites that is for students and students only. Also, to narrow down the potential networks even more, members are mostly restricted to viewing detailed information about students only at their school. As a result of this, more intimate communities are created based on the school. For example, when a UCSD student types [www.facebook.com](http://www.facebook.com) into their browser and logs onto the site, the real url that they are accessing is in fact <http://ucsd.facebook.com/home.php>. Facebook's features are very similar to the features of MySpace. The major features include: profile, friends, groups, messages, wall, and photos. The profile is what makes up the users' personal sites. Here they post information about themselves as well as a photo. The friends feature is one of the major ways that students are able to become connected through the site. Users can search the site and send friend requests to other users to acknowledge online friendships. The other way that the site connects students is through the groups feature. Students with particular interests, views, or hobbies are able to form and join online groups. The messages and wall features allow users to interact directly within the online community. Messaging is a private way of contacting members, almost like e-mail. Also, as an alternative to messaging, there is a "poking" feature, which is basically a way of saying "What's up." The wall acts as a sort of message board and offers more public communication between users. The recently added photos feature is part of the users

profile in which they can post photos of themselves and others for people within their college to see.

Sources: 11

### **How it creates utility for its customers**

Michael Huston from the Arizona Daily Wildcat writes, “If you’re not on Facebook.com by now, then you’re either protesting it deliberately in an attempt to avoid doing what everybody else is doing, or you’re afraid that stalkers will use it to come after you.” At first it was simply a site to connect college students but now it is becoming a staple in the college social scene. The utility that Facebook creates for its customers is essential in creating traffic. Online social networking companies like Friendster have failed in the past for being too one-dimensional and unreal. Facebook was able to recognize these mistakes and capitalized greatly in forming a very real online social network. In theory, the services provided by these two companies are very similar. The difference is what makes the individual keep coming back to the site. On Friendster you can browse through various people’s profiles and add them as friends but the likelihood of you actually meeting these online friends is very small. Facebook, on the other hand, is the opposite. With the number of participating schools and users climbing, it is not rare to see someone online prior to meeting them in person. Facebook is useful in a variety of ways including:

- Forming study groups
- Finding roommates
- Keeping in touch with friends at distant schools
- Finding others with like interests
- Keeping up with social events
- Getting information on fraternities/sororities

Sources: 8, 10

### **How it acquires and keeps customers**

Facebook is able to easily acquire and keep customers due to its increasing popularity. The statistics are almost unbelievable:

- 5M+ registered users
- coverage of 45% of US colleges (a total of 2,000 - representing 8M students)
- 80% penetration among students of colleges that are on the platform
- 10th most visited Internet site in the US
- 5.5B page/views a month (230M page/views a day)
- 8.5M unique visitors
- signing 20,000 new users a day
- repeat usage: daily 70%, weekly 85%, monthly 93%

Creating a Facebook profile is slowly being integrated into the freshman college registration process along with items like sending an official transcript, signing a housing contract, registering for classes, etc. Let's face it, going into college is a scary time socially, but Facebook makes the transition a lot easier. Incoming freshmen can "add" their roommates and even get to know them months before move-in weekend. Some freshmen are even able to build extensive friend lists (networks) before college begins. Through groups and classes one can be connected to thousands of students. Networking is very important in college and Facebook helps students to establish these with little effort on their part. Facebook acquires customers as students realize their personal need for online networking, a need that is becoming more and more necessary everyday. When students meet they often tell each other to facebook them as a means of furthering a friendship. Someone without an account misses out on this completely.

Keeping the customers is a very easy task once they are on Facebook. Users continue to visit the site to partake in one of the newest activities, "facebooking." Facebooking defined is the act of simply browsing though facebook.com with no specific purpose. More specifically, the verb "facebook" (as in "to facebook") is used across campuses for the looking up of a certain individual and a) adding him/her as a friend, b) sending him/her a message, c) 'poking' him/her, or d) writing on his/her 'wall.' These features bring about major opportunities for the communication that college students are looking for

Most new users go through a period of Facebook addiction sometime in their college career. The degree of which Facebook is used as a means of communication requires that it be checked on a daily basis. Throughout the course of the day one can get messaged, poked, or have their wall written on. Also, with the new photos feature, one can get tagged in a picture by one of their friends. There are so many places where something new to one's profile can occur, and this makes it very addicting. Has so and so sent me a message back yet? Or did so and so put those pictures up yet?

Sources: 4

## **How it goes to the market (promotion strategy and distribution strategy)**

### Distribution Strategy

Zuckerberg's distribution strategy is the key element behind his idea, the internet. Facebook provides a service that connects college students through a few clicks of the mouse. This strategy is not new as it's used by many social networking sites. In today's busy world, people don't have the time and effort to put into physical networking with others. Companies such as MySpace and Friendster use this same idea which has been proven to be successful.

### Promotion Strategy

Promotion hasn't been a major issue due to Facebook's instant success. Facebook has not funded any major advertising campaigns in order to increase awareness because the awareness was there from the start. Zuckerberg started Facebook as an online directory of Harvard students and it was an instant hit. Within a month Facebook was available at Columbia, Stanford, and Yale and by the summer it was available at about thirty different universities. The promotion of the site has been mostly by word of mouth, as current users rave to their friends about the site and its many features. Publicity in the media has also helped the company's promotion along. There have been a number of newspaper articles as well as television interviews documenting the recent success story.

Sources: 5

### **How it defines the tasks to be performed**

The tasks to be performed were very simple from the beginning in creating Facebook. Zuckerberg had a clear idea in his head of the service he wanted to provide the user with. Essentially, it would be an online directory comprised of college students for their use and benefit. Having been programming since the age of ten, Zuckerberg was able to easily accomplish this task and took a few weeks to set up a website that allowed users to interact. Through classes, groups, interests, and friends the site notifies the user how he/she is connected. This feeling of connection is very important because that's what the general population of users are seeking. Another major task that Zuckerberg was faced with was setting his social network site apart from the others. In order to demand traffic a site must be unique in one way or another. This task was performed by making the site exclusive to ones college, forming a more intimate community. Also, Zuckerberg added a variety of features that the user could utilize while on the site such as messaging and poking.

### **How it configures its resources**

The major resources of Facebook are the servers that keep the site running despite the heavy amounts of traffic. These servers are very essential because the services and operations of Facebook depend solely on the website. A down server could result in the loss of millions of page hits. With little funding at the beginning, Zuckerberg was forced to keep Facebook relatively small because only so many servers could be purchased and set up. However, the growing audience could not be contained and in the fall of 2004, former Paypal CEO, Peter Thiel, invested \$500,000 to buy servers to help support the rapid growth. (Theil noted that this particular investments was one of the best venture investments he'd ever made.)

Recently, as of November 1, 2005, Facebook signed a multi-year contract with web hosting provider and data center operator Terremark Worldwide to house over 450 of its servers at their NAP West facility in Santa Clara, California. Facebook is able to create a more secure and efficient network by co-locating its servers, which is very important in the operations of the business.

“With our increased market share, we need the NAP's state-of-the-art connectivity, security, redundancy and scalability in order to continue to service our users,” says Mark Zuckerberg, founder of Facebook. “The expansion of Facebook at the NAP West facility means that we can deliver the high quality services and guarantee uptime that our users demand.”

Sources: 1, 3

### **How it captures profit**

The big question behind Facebook and many other free online networking sites is: how do they actually make money? The answer is mainly advertising. Advertisements on Facebook are very valuable considering the amount of traffic the site is able to generate. About 70% of its five million plus users log on the site daily and these users are all between the ages of 18 and 24. The advertising prospects are just too high for big companies to ignore.

Zuckerberg offers three different ways to advertise: banner ads, sponsored groups, and text announcements. Apple has its own sponsored group called “Apple Students” where it lists the hottest items, prices, and even gives away free stuff. Electronic Arts and Geffen Records sponsor groups on the site as well. Text announcements, which are more geared toward students who want to announce a party or event, are sold regularly for \$9-\$15 and guarantee a certain number of hits. Banner ads are easily sold to many major companies including the three listed above and Tiffany’s.

Sources: 1, 2, 9

### **Conclusion**

Facebook has a very specific and strong business model that will bring the company continued success in the future. The site is growing every day in many categories and is drawing more and more attention. Major corporations are seeking out the Harvard dropouts for a possible deal, but these guys are just having fun for now. Their main concern is providing a useful service. Watch this site explode as Mark Zuckerberg, Chris Hughes, and Dustin Moskovitz continue to “have fun.”

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