Online Networks

Microsoft has recently paid $240m for 1.6% of Facebook, a stake which values the company at $15bn, a value which experts and non-experts think is mad.

Perhaps it is not a case of what Facebook is worth as a company, but more a recognition of what Facebook is worth to Microsoft. The days of making huge profits from software licence fees maybe over for Microsoft. The likes of packages such as Linux have already been adopted by IT savvy staff, who are happy to trade less technical backup, for a free software package – especially when some think the software it better designed than many commercial packages.

At the other end of the scale, personal PC users are less willing to adopt new standards in operating systems. Why spend money on MS Vista, when XP works well? In fact the preferences of computer users are changing. The basics such as computers and software are now reliable and cheap. Users are moving their time, effort and money into the experiences to be had online, where social network sites are currently popular.

The business model has followed the customers. So where traffic flows, adverts follow. Google has made masses of money from attracting search traffic and coupling the results with search specific adverts. Microsoft has been slow to tap into this revenue stream.

Adstream is Microsoft's answer but needs more networks in order to generate more traffic and more ad revenue. But so too does Google. Thus it was Google, not Microsoft, which got a stake in AOL, the internet arm of Time Warner. Google also won the deal to supply advertisements on MySpace, the world's largest social network. It bought YouTube, the most popular video site, and most recently acquired DoubleClick, an online-advertising firm. As the number of potential partners dwindled, Microsoft got desperate.

aQuantive, an online-advertising agency, was purchased by Microsoft for $6 billion and Facebook now has a price tag which will hopefully make Google think long and hard before trying to buy it.

Adstream is now Facebook's lead supplier of online adverts and in return Facebook receives guaranteed revenues from Microsoft's Adstream. Since Google leads this new business model it is not unduly affected by the deal. Yahoo, however, is. It is losing search and advertising revenue to Google; and it recently closed its social network Yahoo 360.

Questions

1. E-business is often characterized by high fixed costs and low variable costs. Does this apply to social networks?

2. Why do Microsoft and Google need to grow their collection of networks?