PREFACE

I vividly remember sitting in my office at the Stanford Graduate School of Business in April 2003 when two men knocked on my door asking if they could have a word. By then I had done a fair amount of research on offline social networks and had written a paper on how social networks can help venture capitalists gain recognition. As a result, many newly minted (and always impeccably dressed) venture capitalists dropped in on me, looking for additional insights. I figured these two fell in the same category—except they weren't dressed as sharply.

It turned out, though, that they weren't venture capitalists at all; they wanted to talk to me about a company they were about to launch, one that involved online networking. A number of similar companies had sprung up in the area, and their founders had all secured Stanford professors who studied social networks as their advisors. As the most junior professor on campus who studied social networks, I was the only one unspoken for, and so these two gentlemen sought me out to be their sounding board.

Their site, soon to be released to the public, would let people create professional profiles to display their educational and work achievements and publicly indicate their business relationships. People could then use the online network to offer or seek consulting engagements, expertise, or financing.

The idea sounded interesting to me, but I did not believe it was going to succeed. "Why reinvent the wheel?" I thought. "We already know that networks work very well, and people already get jobs through networks." In fact, a classic sociological work by Mark Granovetter (1974) had long ago demonstrated that a significant percentage of jobs are obtained through personal networks. Clearly, offline networks do what

they are supposed to do, and have done so for centuries, so why would we need to network online? I was polite with my comments, but I was politely *negative* and we parted ways.

Later that day, as I was driving back home to San Francisco on Interstate 280, I continued to think about just how much I did not like the online networking idea. Then, as I was approaching the intersection with Route 92 that takes you to Half Moon Bay, and admiring the fog rolling over the Santa Cruz Mountains, it dawned on me that I was wrong. I remember thinking: "We have all of these theories in sociology—about how networks work, how they help us, and how they are better than markets. But what if these networks do not perform as the theory says? What if there are many social interactions that would make people happier, but these interactions simply do not happen? We have no theory that tells us when social relationships might *not* work. And if there are many missing social interactions, then there is a huge opportunity for new ventures to help people interact with one another! My visitors were right and they were onto something really big!"

By the time I got to San Francisco, I was completely convinced that I needed to contact the two men, retract most of what I had said, and ask them to meet with me again. I emailed them as soon as I got home, and the two gentlemen, Reid Hoffman and Konstantin Guericke, agreed to meet again. Just a few years later, their company, LinkedIn, had prevailed over its erstwhile competitors. Within eight years, LinkedIn reported $65 million profit on $500 million revenue and debuted on the New York Stock Exchange with one hundred million users and a $10 billion valuation. When this book was going into print, the company was valued at $25 billion. Sadly, I had nothing to do with the company's success. (In fact, I have no formal paid relationships with any of the companies discussed in this book.) But the interaction with Hoffman and Guericke changed my research trajectory for the next ten years. I document this research in this book.

LinkedIn's Critical Choice

LinkedIn's road to success was not straightforward. Indeed, in the summer of 2005, Reid Hoffman found himself facing a critical decision regarding the company's future. By then, the company had amassed five

million users, but it had very little revenue to show to investors. Furthermore, it had only five million dollars in cash reserves, which would allow it to survive for just another nine months without an infusion of cash from venture capitalists. Given about a six-month lead required to obtain financing, LinkedIn had to start generating revenue quickly, or the terms of financing would be very unfavorable.

In deciding how to generate revenue, Hoffman had to make sure that he did not undermine the basic principles that had allowed the company to attract users. For example, LinkedIn had always encouraged users to form online connections only with people they actually knew offline. It also allowed members to contact only those members who were no more than four degrees of separation, and every time someone wanted to contact someone else on the platform, the chain of friends connecting the sender and the receiver had to approve the communication. This fostered a trustworthy online environment and reduced the incidence of spam, which helped LinkedIn prevail over competitors.

The company also had to be mindful about its superusers—individuals who were so committed to the site that they used a separate computer dedicated only to their LinkedIn activities. Often referred to as "networkers," these users had established many online relationships on LinkedIn and played critical roles in connecting other users by forwarding their requests.

Hoffman and his team entertained two options. The first entailed keeping the existing free service intact, but offering a fifteen-dollar subscription for a bundle of eight new services that would help LinkedIn members search the site and manage interactions more effectively. This option garnered significant support because it helped the site's most active users, the networkers. It also offered the promise of steady cash-flow streams associated with monthly subscriptions.

The second option called for allowing members to contact each other directly, regardless of whether they were connected to each other through intermediaries. LinkedIn would charge a fee for such communication—roughly equivalent to ten dollars per message. The company had received some requests for this functionality and estimated it to be a profitable option. Many people worried, however, that pursuing this option could lead to the platform's demise. First, if anyone could contact anyone, then there would be much less need

for the networkers—the most active site members—who would probably abandon the site. Second, allowing users to contact anyone on the network would violate LinkedIn's basic premise—its commitment to privacy—potentially leading to massive user defection.

I will reveal what the company chose in a moment, but before I do, I want you to make the call yourself:

Which option would you choose?

I ask this question every time I teach the Competing with Social Networks class to Harvard Business School MBA students and to various experienced business managers in the executive education programs. And every time I do, my heart stops beating for a moment as I expect everyone in the class to pick the second option—the one that LinkedIn chose. It is so much harder to teach when all students pick the option the company chose . . . and yet it never happens!

Even eight years after the event, with lots of information on LinkedIn readily available on the Internet, 60 percent of my students vote against the second option largely because it seems to violate the privacy and trust of the people who joined the site to begin with. Many students, particularly in the executive education sessions, claim: "I would never want to be on a site like this where I can be spammed with messages." Only 15 percent of students support it. And the remaining 25 percent say that neither option offers profitability for LinkedIn.

So, *was* LinkedIn wrong to adopt the second option? Evidence suggests the contrary—the company did very well as a result. In implementing the strategy, the company opted for a subscription model rather than a fee per message, but the imputed price per message was roughly the same. And although the ability for anyone to contact anyone else on the platform for a fee did drive away the networkers, their defection did very little to curb the platform's success.

Ultimately, the second option worked well for LinkedIn because it opened up a communication channel between recruiters and people in long-term employment relationships who may be looking for new jobs. Most people in this situation face a huge normative restriction—it is often not appropriate for them to look for new jobs openly while

they are still working. Those who violate this norm can lose their jobs or be passed over for promotion. It is exactly for this reason that many people in long-term employment relationships do not put their résumés on Monster.com—a popular job-seeking website—lest their own company's HR department spot it. This normative restriction prevents these people from engaging in mutually beneficial interactions with recruiters, which in turn can prevent them from getting better jobs.

On LinkedIn, however, it *is* appropriate to list one's educational and work achievements and open oneself up to overtures from recruiters. Displaying this information on that platform does not violate the norm because the information is also used for LinkedIn's other functionality—networking with friends and business associates. Employees can use such networking activities to generate benefits for companies where they currently work and thus justify their presence on LinkedIn. So, even though company leaders know that they might lose their employees through LinkedIn, they also know that they can get a lot of benefits by having employees on that platform. As a consequence, most companies do not object to their employees being on LinkedIn.

In effect, LinkedIn overcame the norm that prevents people from going on the market while still employed. This enticed numerous employed job seekers, who in turn attracted recruiters to the site. The latter paid LinkedIn a lot of money to be able to access these employed candidates who are very hard to find in the offline world and on other online sites. To date, LinkedIn continues to generate most of its revenues this way.

Concepts Presented in This Book

LinkedIn's 2005 decision illustrates many of the central themes and concepts in this book. I'll introduce them very briefly now—putting the key concepts in italics. First, LinkedIn identified a mutually beneficial social interaction that does not take place—that between employed people and recruiters that could result in the former getting better jobs and the latter recruiting excellent candidates. I will refer to such mutually beneficial social interactions that do not take place as *social failures*. LinkedIn also recognized that the interaction it wanted to

address does not occur because of normative restrictions. Various normative restrictions that prevent us from engaging in social interactions will be of central importance throughout the book.

Second, LinkedIn developed a *social solution* that minimized the salience of this norm, and allowed people to make themselves visible to recruiters and thus engage in mutually beneficial interactions. It did so by helping people interact with business acquaintances, and leveraged that solution to give people an excuse to interact with people they did not know without violating the norm. Throughout the book, we will underscore that social solutions work best when they overcome social norms that prevent mutually beneficial interactions offline.

Third, LinkedIn's example shows us that when a firm provides a valuable social solution, it can ask the beneficiaries to do something that benefits the firm in return. In LinkedIn's case, this amounted to paying the firm money. This insight will be particularly useful in the second part of the book when we study more traditional companies, such as Nike or American Express. These companies have built their own social solutions or leveraged existing ones to help their customers interact with others. In return, these firms ask that these customers do something beneficial for the firm, such as buying more expensive products or doing customer acquisition on the firm's behalf. I will use the concept of *social strategy* to capture the idea that firms can lower their costs and/or increase their customers' willingness to pay by helping their customers develop better relationships.

Social failures, *social solutions*, and *social strategy* are the essential concepts on which this book is based. Chapter 1 explains how the book will explore and use these concepts to understand why certain social platforms have failed while others have succeeded, and how the surviving social platforms compete with each other.