

MYSFACE: THE ONLINE REALITY SHOW

In the fall of 2006, Chris DeWolfe found himself stepping back in time as he stood before a crowd of alums and current students from the Lloyd Greif Center for Entrepreneurial Studies at the Marshall School of Business of the University of Southern California. He was there to receive an award as the Alumni Entrepreneur of the Year for co-founding the second largest site on the Internet, MySpace, the social networking phenomenon. But more than that, he was there to remember his roots and to tell an eager audience of entrepreneur hopefuls what to watch out for. "Technology does not drive demand," he cautioned the students. "MySpace has always taken a sociological viewpoint—How do people do things? What do they like to do? Then the MySpace team figures out how they can enable their users to do what they want." Asked what he would have done differently, DeWolfe doesn't miss a beat—"I would have started it sooner." He would have expanded aggressively and hired more developers in the early days, because "speed to market is important."

DeWolfe was looking back at the launch of the company he co-founded with Tom Anderson from a new position in that fall of 2006. MySpace had recently been acquired by Rupert Murdoch's News Corporation (News Corp) as part of a \$580 million package deal for InterMix Media, MySpace's parent company. With the enormous resources of News Corp behind it, MySpace was taking on an astounding number of new projects: a new Google agreement for text ads, a MySpace records label, a VoIP feature so their users could call one another, international sites, and another 20 products in various stages of development in the pipeline. How did MySpace go from launch in late 2003 to online media giant by 2007?

In the Beginning

Chris DeWolfe hails from Portland, Oregon; both parents were teachers. So it was a bit of a break from tradition when he decided to major in business at the University of Washington. Upon graduation he took a job, but two years into it, he began to have some doubts.

I looked to my left and looked to my right and saw that my colleagues were twenty years older than me, and it was almost like looking into the future. And I was scared because that wasn't something that I wanted to do. I wanted to create my own business; I wanted to do my own thing; I wanted to innovate.

Frustrated, he decided to further his education by getting an MBA. His friends told him that he had to have a plan to get into a good business school. He had to know whether he wanted to be a consultant, an investment banker, or a marketing manager. Again, DeWolfe sidestepped the traditional route—"My plan is, I'm going to figure out a plan when I get there." He was accepted into the Marshall School of Business at the University of Southern California (USC), and for the first year he immersed himself in the Internet, which in 1995 was just beginning to gain some ground as a commercial channel. Netscape and Yahoo! had gone public and things were getting interesting. In the second year of his MBA, he took a class in the Lloyd Greif Center for Entrepreneurial Studies and was hooked. He knew what he wanted to be—an Internet entrepreneur—that was his passion.

After graduation, DeWolfe and three of his USC Marshall friends took jobs at an Internet data-storage

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company, Xdrive; DeWolfe became the company's head of sales and marketing. It was in that capacity that he met one of his future partners, Tom Anderson, in 2000. Anderson, a frustrated English major at UC Berkeley and then film school major, responded to an ad to earn \$20 for testing an Xdrive product. Although Anderson disliked the product immensely, DeWolfe liked him so much that he offered him a full-time job. Xdrive was not a success, however. It was the typical dot com company of the day, raising \$120 million and spending it foolishly on parties, excess advertising, and hiring people it didn't need. That experience told DeWolfe that it was time to start his own company, so he and Anderson left the firm (in bankruptcy) in 2001 and launched an Internet direct-marketing firm called Response Base. They sold that business for several million dollars in late 2002 to eUniverse, a holder of multiple Internet assets. Both joined the company, but just six months later, DeWolfe and Anderson were asking themselves, "What's next?"

A Brief History of the Internet

Although the Internet didn't become the focus of consumer attention until about 1995, its history actually dates back to August 1962, when MIT's J.C.R. Licklider began discussing what he called the "galactic network," a "globally interconnected set of computers," which would enable anyone in the network to access data and programs from any site. While serving as the first head of the computer research program at DARPA, he convinced his colleagues of the significance of his concept. By late 1966, MIT researcher Lawrence Roberts had created a plan to build the ARPANET and by 1969, the first node was installed at UCLA. Within a month, two additional nodes were added at UC Santa Barbara and the University of Utah, and by the end of 1969, there were four host computers connected on ARPANET. Nevertheless, it took until October 1972 to demonstrate ARPANET's capability to the public at an international conference and to introduce its newest application, electronic mail.

ARPANET was the first of what would become many networks linked by an open architecture networking called the Internet. In open architecture

each network could have its own design and user interface, yet they would all be connected seamlessly to the Internet. The 1980s saw the rapid development of LANs (local area networks), PCs, and workstations, which contributed to the swift expansion of the Internet that was now serving a broad base of researchers and developers.

In 1991, the first user-friendly interface was developed at the University of Minnesota. *Gopher*, as it was named after the university's mascot, quickly expanded to over 10,000 systems around the world while other universities developed enhancements to it, such as a searchable index of gopher menus and a spider that crawled gopher menus to collect links and place them in the index. But it was the development in 1993 of Mosaic, a graphical user interface, by Marc Andreessen and his team at the National Center for Supercomputing Applications that became the catalyst for the commercial Internet as we know it today. With the launch of Delphi, the first national commercial online service that offered Internet access to subscribers in 1992, the commercial Internet could not be stopped. In 1995, the National Science Foundation halted funding of the Internet backbone, and commercial networks like AOL and CompuServe were born.

Until 1998, when Microsoft released Windows 98 with a full-scale browser incorporated, Netscape's browser, which was free, was the most popular browser on the market. At this point, there was no stopping the proliferation of Internet sites as more and more companies tried to find business models that would enable them to make money through this exciting new channel. The highly speculative period between 1995 and 2001 has been called the "dot com bubble," because stock markets saw their value explode to unprecedented levels from the growth in Internet companies and related sectors only to crash in the spring of 2000 because these same companies couldn't deliver business models that made sense or contributed to realistic valuations. The dot com bubble was not a unique event. History has witnessed other booms and busts: radio in the 1920s, transistor electronics in the 1950s, and home computers in the early 1980s. Some of the more notable dot com failures were Webvan, the online grocer; Pets.com; and eToys.com.

Today many pundits question whether we are heading into another dot com bubble—the sequel—with the recent acquisitions of MySpace and YouTube at extremely high valuations. These social networking sites depend a good deal on content that their users create and on their users' ability to build large networks among their friends and associates. There are no fees charged to the users, so the sites rely on advertising revenue and sponsorships and often have no proprietary technology. However, if MySpace is the model for the current Internet venture, then we will see more acquisitions by large corporations instead of IPOs by unprofitable Internet companies.

The Birth of MySpace

Ready to start another business, DeWolfe and Anderson surveyed the Internet landscape and recognized a "perfect storm" of activities that seemed to suggest a space to do something that wasn't being done. In late 2002, the term *social networking* was getting some play due to the emergence of Friendster (a dating site), Tribe (a classifieds and local information guide), and Facebook (social networking for college students). DeWolfe and Anderson noticed that they were receiving a constant stream of requests through their e-mail to join these networks, so they began to do some research and quickly determined that these were niche players without a lot of potential to become huge. The two had bigger plans in mind, specifically a portal that would bring all of the niche functions together and let users do whatever they do offline in a more product way: express themselves, send out invitations, blog, discover music, share photos, and play games. DeWolfe's mantra has always been "once you've done the research, stop strategizing and jump off the cliff." So he and Anderson made the leap to start the company. They pitched the idea to eUniverse and took a seed round of financing for 66 percent of their equity. They also purchased the myspace.com domain name from a data-storage company no longer in existence.

It took three months to build the site, and they launched at the end of 2003. However, the day after launch the site blew up—in other words, it stopped

working. DeWolfe quickly consulted with his developer and learned that the system they had built couldn't survive an assault by more than 200 people at the same time. Realizing the mistake that had been made, DeWolfe instructed the developer to build the site to hold millions of people at the same time. Shortly thereafter they were back in business. Growth did not come quickly for this social networking portal; in fact, the company didn't start to see success for at least six to nine months. At first they attracted their users by inviting bands and club owners in Los Angeles to create pages and then invite others to "become their friends." Because the bands and clubs could use MySpace as their promotional platform, they very willingly invited others onto the site. And everyone came, because MySpace allowed them to do and post what they wanted, whereas rival Friendster made sure that its site did not contain anything that didn't fit its core proposition, which at the time was essentially Internet dating. MySpace also succeeded in correcting many of the problems that users had with Friendster, such as speed of access to the site. Giving bands an outlet to let users sample and share songs as well as communicate with the bands was the secret sauce that catalyzed MySpace's growth. By 2004, more than 350,000 bands and solo artists, both unknown and famous, had set up pages on the site and invited their friends to join, creating a viral effect. In September 2004, R.E.M. became the first band from a major record label to stream its latest album on MySpace before its release.

The *New York Times* wrote of MySpace:

Even with many users in their 20s MySpace has the personality of an online version of a teenager's bedroom, a place where the walls are papered with posters and photographs, the music is loud, and grownups are an alien species.

And that's just what DeWolfe and Anderson intended. Users are able to customize the look of their pages, add personal photographs, and create a network of friends who must receive permission before being added to someone's site. The biggest celebrity on MySpace is co-founder Tom Anderson because it is his face that pops up when a new member registers, so his list of friends was running over 46 million as of

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In July 2006, InterMix Media's Richard Rosenthal, who in 1999 raised \$565 million for a struggling company, was under SEC investigation for nearly four quarters of financial reporting on NASDAQ, a various class of securities. These problems were soon cleared up, supporting the growing asset structure of the capitalist MySpace company. The team, and the But Redpoint understand the December 2006 InterMix Media common stock 150,000 shares. The ink on the Redpoint Venture \$11.5 million. The newly formed mix, MySpace held a 53 percent stake. DeWolfe served year term the

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2006. Of the two founders, Anderson, who came out of music and film, is the most gregarious and creative while the quieter DeWolfe manages MySpace's finances and keeps a lower profile. In fact, it was DeWolfe who shielded Anderson from much of the turmoil surrounding the later acquisition of MySpace.

In July 2004, eUniverse changed its name to InterMix Media (IMIX) and brought on a new CEO, Richard Rosenblatt, a successful Internet pioneer who in 1999 had sold his company iMall for \$565 million. His challenge was to turn around the struggling company, which had gone through an SEC investigation, had its stock halted from trading for nearly four months, had to restate the first three quarters of fiscal year 2003, had been delisted from NASDAQ, and was being sued by its shareholders in various class-action and derivative lawsuits. All of these problems cost the company a lot of money, so it was soon clear that the company needed more funding to support its rapid growth and that of its fastest growing asset, MySpace. This meant talking to venture capitalists, most of whom didn't understand the MySpace concept, didn't know the management team, and thought they were trying to do too much. But Redpoint Ventures, a Silicon Valley firm, did understand the technology-entertainment mix. In December 2004, they agreed to invest \$4 million in InterMix Media, Inc., for one million shares of its common stock and a five-year warrant to purchase 150,000 shares of common stock at \$4/share. With the ink on that deal still drying, in February 2005, Redpoint Ventures again invested, this time a total of \$11.5 million for a minority stake of 25 percent in the newly formed independent subsidiary of InterMix, MySpace, Inc. As of February 2005, InterMix held a 53 percent equity interest in MySpace, Inc. DeWolfe served as chief executive officer for a three-year term that ended in October 2007.

The Acquisition of InterMix and MySpace

In 2005, a number of large media companies began approaching Richard Rosenblatt, CEO of InterMix and chairman of MySpace, about acquiring InterMix and its three main assets: MySpace, Alena (marketing

analytics and e-commerce), and its media network, which consisted of about 30 different websites. At the time, MySpace was supporting approximately 18 million unique visitors and was the fastest growing part of InterMix. DeWolfe was very nervous when News Corp's Rupert Murdoch, the media icon, approached them about an acquisition, because he did not want to risk losing the no-rules culture they were known for and become buried in a huge conservative conglomerate; however, they needed the money to support their blistering growth, and their board approved the sale. In approximately 18 months from the time he had become CEO of InterMix, Rosenblatt had turned the company around and sold it and its highly successful subsidiary MySpace for a premium, \$580 million in cash, to News Corp to become part of its Fox Interactive Media, Inc. Rosenblatt remained a consultant to News Corp to help grow the InterMix properties until he launched Demand Media in 2006, raised \$220 million in investment capital, and bought back the non-MySpace assets of InterMix Network LLC from News Corp.

Prior to the acquisition, Murdoch had assured DeWolfe and Anderson that he would not interfere with the running of MySpace; however, shortly after the acquisition of InterMix in July 2005, News Corp decided to move MySpace from its laid-back office a block from the beach in Santa Monica to Beverly Hills, where all of News Corp's Internet companies were based. It was at that point that DeWolfe and Anderson first realized that they no longer really owned MySpace. They soon found that other things had changed as well. Decisions took a lot longer now with all the big corporate processes and the culture was not as casual. The upside, though, was that MySpace had significantly more resources at its disposal to launch multiple projects and products simultaneously.

DeWolfe believes that MySpace is at the nascent stage of where it can potentially go. As the number two Internet site in terms of page views, the duo needs to make sure that they continue to listen to the market, not the experts, and not "follow the pack." DeWolfe attributes the success of MySpace to several factors: (1) an experienced management team that had worked together for 8 years; (2) great timing on the launch of the site, with social networking taking

off and advertising revenues returning to Internet companies; (3) features on the site that were compelling to their users—they provided a solution that made sense and that users couldn't find on other sites; and (4) the use of influencers from entertainment to drive interest in the site. As long as DeWolfe and Anderson remain with the company, the intent is to make sure that users control the site and users dictate the features that MySpace offers. That philosophy often presents problems, with the less desirable elements of society easily setting up shop in MySpace and preying on other users. "We take safety very seriously and we make huge investments in it," asserts DeWolfe. Monitoring the site while still giving users freedom is a real balancing act, but it has to happen for MySpace to be able to attract national advertisers like Coca-Cola and Procter & Gamble, who will not risk their brands by having them associated with off-color or inappropriate content. These "sponsors" supply significant revenue for a company that depends primarily on ads in its business model. In December 2006, with the resources of News Corp at its disposal, MySpace went mobile on a grand scale with a service that enables Cingular Wireless subscribers to use many of the social networking features of MySpace on their cell phones for a \$2.99 per month premium. This was a way to diversify its business model and again meet one of the requested needs of its users.

In the spring of 2007, with their contract end date looming in October, DeWolfe and Anderson were again faced with the question, "What's next?"

Sources: "A Brief History of the Internet." *Internet Society*, <http://www.isoc.org>, accessed May 29, 2007; Interview with Chris DeWolfe, Alumni Entrepreneur of the Year Event, November 2006, University of Southern California; "Dot-Com Bubble, Part II: Why It's So Hard to Value Social Networking Sites." *Knowledge@Wharton*, <http://knowledge.wharton.upenn.edu>, accessed October 4, 2006; Sellers, P. (2006). "MySpace Cowboys." *Fortune* (September 4): 67; "Interview with Richard Rosenblatt, Intermix and MySpace." *Socal Tech* (January 30, 2006), <http://www.socaltech.com>; Williams, A. (August 28, 2005). "Do You MySpace?" *New York Times*, <http://www.nytimes.com>; Weintraub, J. (July 25, 2005). "A, B, C, D, eUniverse." *DM Confidential*, <http://www.adaastro.com>; "Entry Material Agreement, Other Events, Financial Statements and Exhibits." Form 8-K for Intermix Media, Inc., published February 17, 2005; Exhibit 99.1, eUniverse Issues Open Letter to eUniverse Stockholders, January 7, 2004, <http://sec.edgar-online.com>.

Discussion Questions

1. How did DeWolfe and Anderson recognize the opportunity for MySpace?
2. What mistakes were made with Xdrive that ultimately made MySpace go more smoothly?
3. How did MySpace differentiate itself from the competition?
4. Should DeWolfe and Anderson have given up so much equity (66%) in the beginning to eUniverse? Was there an alternative strategy available?
5. Evaluate the acquisition of MySpace as part of the Intermix package. Would you have made that decision? Why or why not?

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