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Cyworld: Creating and Capturing Value in a Social Network

In August 2008, less than a month after being appointed CEO of SK Communications (SK Comms.), Korea, Hyung-Chul Joo started reviewing the growth strategy of the company, especially its social networking business, Cyworld. SK Telecom, the \$11 billion South Korean mobile phone company, had created SK Comms. in 1999 as part of its Internet strategy. Coincidentally, the same year, Cyworld was started as an independent social networking company by a few college students. In 2003, SK Telecom acquired Cyworld, merged it with SK Comms, and managed to grow its user base from 2.5 million in 2003 to over 21 million in 2007. In 2006, SK Comms. had revenues of \$185 million and an operating profit of over \$19 million; and in 2007 even though revenues increased to \$197 million, the company had an operating loss of \$0.35 million due to its acquisition of Empas, a search portal (**Exhibit 1**). Cyworld accounted for almost 50% of the company's revenues and majority of its operating profits.

Cyworld was now reaching a mature phase. By mid-2007 it already had 21 million users in a country of 50 million people and over 90% penetration in the 20- to 29-year-old market. There were signs that its members were getting tired of buying virtual items to decorate their home pages. With almost 70% of Cyworld's revenue coming from selling these items, its current business model needed to change. The company had already started shifting its emphasis from selling items to advertising. However, advertising-based models remained uncertain, even for the major U.S. social networking sites, MySpace and Facebook. A third option was to leverage the strength of the parent company SK Telecom and focus on Mobile Cyworld. While it was possible to choose multiple options at the same time, Joo knew that he still needed to prioritize them.

The choice of revenue model could also change the way that Cyworld created value for its users. Until recently, Cyworld had stayed with its original value proposition of providing users with a free and clean community with limited advertising, and an almost exclusive focus on social networking. However, the company was beginning to provide its users with a variety of other services, including blogs and a media platform where users could upload and share videos and pictures. As a result, Cyworld was slowly morphing into a hybrid entity that combined elements of Facebook and MySpace with YouTube, Flickr, iTunes, and many other sites. Joo wondered if these new services added value for users or created confusion because of lack of focus. Did the way that Cyworld created value for its users affect its ability to capture value from this user base? As the third CEO in less than fifteen months, Joo recognized the urgency and importance of making the right decisions.

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The Evolution of Cyworld

The Early Era (1999–2003)

Cyworld was started in 1999 by a group of MBA students from the Korean Institute of Science and Technology (KAIST). Initially called People Square, it was quickly renamed Cyworld. “Cy” in Korean means “relationship,” which defined the goal of the venture. Cyworld encouraged users to invite their friends to join by offering users 500 Korean Wons (approximately \$0.5) every time they brought in a friend. The service allowed users to build a social network of friends and provided an address book for this purpose. However, initially there was not much to do once users visited the site.

At the same time, two competitors, Daum and Freechal, were creating online communities where people with similar interests could interact. While Daum was the major player, Freechal was also growing rapidly and was viewed by users as trendy. Recognizing the success of Daum and Freechal, in 1999–2000 Cyworld changed from a closed network to an open community. Soon it had hundreds of clubs. It further expanded into polling, chatting, and bulletin boards, but those areas failed.

To further differentiate itself from competitors, Cyworld positioned itself as a place “offering a small, clean community.” The “clean” service was the result of Cyworld requiring its members to use their real names, and the lack of any banner ads. Being a small company, Cyworld employees knew many users personally. Soon Cyworld started offering a “profiling” service where users could click on their friend’s name in the address book to get all of the friend’s information, and leave a message. This service got a very positive response.

Building on this success, in 2001 Cyworld developed the concept of “minihompy” (pronounced “mini-home-p”) or a mini home page where users could write diaries and invite their friends to visit and leave comments. This proved to be very popular, and Cyworld grew rapidly. At the same time the company was under pressure to create a profit model. Its promise of “clean” service ruled out advertising. Cyworld found the solution in the form of virtual gifts. Just as in the offline world where friends bought gifts for each other, Cyworld offered virtual gifts that users could buy for their friends (**Exhibit 2**). However, unlike in the offline world, receivers of virtual gifts could not use them.

Cyworld found a solution for this problem by allowing users to decorate their minihompy with these items. Soon users started buying these items to decorate their own minihompy (see **Exhibit 3** for a sample minihompy). Users created an alter ego or avatar and decorated their minihompys with virtual art, electronics, furniture, etc. A minihompy was a means of self expression, and virtual items enabled users to achieve that goal. Users could also download songs to create background music for their minihompys. These items spurred the growth of Cyworld’s user base and also created a source of revenue for the company. By 2002, its user base had grown to almost 1 million, and its item sales brought in \$3,000 a day. Thus, Cyworld was already a vibrant social networking site in Korea before MySpace was founded in 2003.

Acquisition by SK Telecom (2003)

By 2003, Cyworld was feeling growing pains. Its user base was increasing rapidly and so were its costs. Sales from virtual items were not sufficient to cover operating expenses or buy new servers to meet the growing traffic. The Internet bubble had just burst, and venture funds were not easy to get. Cyworld soon found SK Telecom as a willing partner.

SK Telecom was the leading mobile service provider in Korea, with 2007 revenue of \$11.4 billion from over 22 million subscribers. By late 1990s, it already had a high mobile penetration rate in the Korean market. Being in a fiercely competitive mobile service industry, SK Telecom had been looking

for growth opportunities. In 1999, it founded SK Comms. as part of its Internet strategy. In 2002, it acquired Lycos Korea and Let's Go, two medium-sized search and portal companies, then combined and renamed them Nate.com. In August 2003, SK Telecom acquired Cyworld with 2.5 million users for \$7.5 million.¹ SK Telecom was one of the first companies to have the vision to link mobile service with social networking.

Post Acquisition (2003–2006)

The acquisition provided the much-needed cash for Cyworld to continue growing; SK Telecom immediately invested \$10 million to improve server capacity. At the same time, Freechal was going through similar struggles to fund its growth and decided to charge users a membership fee. Users rejected Freechal's subscription model, and Cyworld gained significantly. Soon Cyworld reached a critical mass, and the network effect propelled the company to grow exponentially (**Exhibit 4**).

The growth of Cyworld was also fueled in part by a synergistic relationship with its parent company's instant messenger service, NateOn. SK Comms. had started NateOn in 2002 when Microsoft's MSN messenger was a dominant player in the Korean market. It was hard to displace a dominant global player with an entrenched position, and NateOn struggled in its early stages. The service offered up to 100 free SMS² per month from computer to mobile phone. Users found this attractive, since an SMS would normally cost about three cents. This promotion significantly improved the market position of NateOn. In 2003, NateOn leveraged Cyworld's user base by linking its buddy list with *Il-chon* (or "first-neighbor list") on users' minihompys. NateOn also displayed the Web address of friends' minihompys.³ If a friend was not online, a user could visit the friend's minihompy from NateOn with just a click, and leave a message or share a photo or video. This synergy propelled the growth of both Cyworld and NateOn. By March 2005, NateOn had surpassed MSN messenger in number of users (**Exhibit 5**).

Cyworld Users

Cyworld's target users were in their late teens and early twenties. Users in their twenties made up the largest user group for Cyworld. These users were the trendsetters, followed by the teens. Registered users were equally divided between males and females (**Exhibit 6**). While Cyworld was acquiring 10,000–15,000 new members every day, almost 5,000 members canceled their memberships daily. Byung-Hui Shin, group leader of customer service, explained, "Although there is no membership fee, young people tend to cancel their membership and re-register when they break their relationship with a close friend."

User Motivation

Many users of Cyworld spent several hours on the site every day. While adults considered this a waste of time, many young users showed fierce loyalty to Cyworld. Jong-Hyun Jeong, a 20-year-old college sophomore, explained: "I cannot keep the relationship with my friends and will be alone, if I do not use Cyworld. I like the many social network services and self-expression functions that Cyworld provides. So I use it habitually." Similar attitudes were captured in a *BusinessWeek* article:

¹ In contrast, in 2005 News Corp paid \$580 million to acquire MySpace which at the time had 19 million users, and in 2006 Yahoo reportedly made a \$1 billion offer to acquire Facebook, which then had 8.8 million users.

² "SMS" or short messaging service is a communication protocol that was initially designed for short text messages between mobile phones.

³ "First neighbor" is a friend who has a direct relationship with a user, with "one degree of separation."

For Yu-Jin Lee, an 18-year-old freshman at Osan College in South Korea, Cyworld isn't just another Web site. It's the nexus of pretty much everything she does. The graphic design student posts all of her school papers on the site. She puts up photos of her friends, her family, and her parties. She keeps a daily blog there and chats with her boyfriend via the site's instant-messaging service. She even meets new friends, when their avatars, or digital stand-ins, stop by her Cyworld site. "I simply can't do without it," says Lee. "If someone is to block Cyworld today, I'll probably have to sue the person."⁴

Interestingly, such views were not unique to Korea. Keeping in touch with friends and schoolmates was also one of the key reasons cited by U.S. users of social networking sites such as MySpace and Facebook. A Forrester survey of U.S. users found that "media and content-related activities like looking for an event, watching a video, or listening to music take a significant back seat to relationship-building."⁵ A 16-year-old high school student in Boston described his passion for Facebook:

Cell phones, text messages, and e-mails are very personal because I am talking to one person, usually with a specific purpose in mind. Blogs, on the other hand, are like broadcasting your views to the rest of the world without really knowing if anyone is listening or cares. However, writing on the wall of my Facebook friend is semi-private. I am only "talking" to my core group of friends, and yet I know my comments may be seen by friends' friends.⁶

In addition to relationship-building, Cyworld users cited many other reasons for using the website. *BusinessWeek* captured some of these reasons:

"I use Cyworld as the photo archive for my family," says Joon Kim, a 31-year-old software engineer who met his wife through a Cyworld club for virtual "families" in which he first played her husband. "My 1-year-old son will have a photo log of his life in Cyworld 20 years later."

The service's popularity has meant opportunity for some members. Hyoung-Gon Kim, 25, won Cyworld fame by posting recipes with photographs of dishes on his home page—and then won a deal to write a cookbook. Hee-Jae Kang, 31, quit her job and opened her own online shopping site after the collection of dolls and clothes she showed on her page drew 2.7 million visitors.

User Satisfaction

In spite of intense loyalty from many users, Cyworld was concerned that this loyalty was declining over time. To gauge changes in user behavior, in September 2006 Cyworld conducted a survey of 1,200 users who used the site more than once a month. Almost 64% of users had decreased their usage of Cyworld, and only 13% had increased their usage in the last six months. The top four reasons for decreased usage included "not enough time," "getting bored," "few friends," and "privacy problem." The reaction of Min-Jeong Kim, a 21-year-old female, was not uncommon:

Compared to six months ago, my usage has decreased. Initially it was really nice to create my own persona by decorating my minihompy. However, someday I realized that first-neighbor relationships are just superficial relationships, and I thought that making my minihompy public is like showing my private life to everyone. So I closed my minihompy

⁴ *BusinessWeek*, "E-Society: My World Is Cyworld," September 26, 2005, accessed April 10, 2008.

⁵ Charlene Li, "How Consumers Use Social Networks," *Forrester Report*, June 21, 2007.

⁶ Interview by the casewriter.

temporarily. Recently I started using it again, but only as a photo album, since my friends are using it. In some sense, Cyworld is unavoidable.

Consumer research by Cyworld also highlighted which aspects of the site users considered important and where they were most dissatisfied. While Cyworld was considered an easy way to communicate with friends, most users did not find any useful information in Cyworld (**Exhibit 7**).

User Segments

Not surprisingly, there were significant differences among users in their levels of activity and engagement. Of the 21 million registered users, only 5–6 million users logged in 2–3 times per week. These differences also showed up in their purchasing behavior. A large segment of users spent no money on Cyworld, while others spent hundreds of dollars each year. The top 15% of buyers accounted for over 35% of total purchases. Users also differed in the extent of their social network. Some users had many friends or “first neighbors,” while others were less connected.

Cyworld managers differed in their opinions on which aspect of consumer behavior was more critical for user segmentation. Some argued that user activity was the most critical component, since it showed their level of engagement and loyalty to Cyworld. After all, they argued, it was all about creating a powerful user experience. Others disagreed. As one manager put it, “What is the use of activity if it does not produce revenues? Wouldn’t you rather have a user who spends a lot of money buying virtual items than another who uses our site for free to chat with friends?” A third group of managers thought differently. They pointed to user networks (see **Exhibit 8** for an example) and commented:

We are a social networking site. What makes us different from Amazon and Google is that our users have a *network* of friends. We can’t lose sight of that fact. Our users take pride in having a large number of “friends,” since it gives them bragging rights and usually becomes a badge of honor for them. It is not the activity or purchases, but the number of connections that should be our main criteria. We cannot lose a user who is a *connector* and acts as the hub for his network of friends. If we do that right, revenues will follow.

To better understand this ABC segmentation (**Active users, Buyers, and Connectors**) and the relationship between them, Cyworld managers analyzed data from a sample of over 50,000 users (**Exhibit 9**). It was not immediately clear whether these data helped to resolve or intensify the debate.

Creating Value

Cyworld was facing two main challenges. First, it was reaching saturation with over 21 million users and almost 90% penetration in its target audience. Second, after several years of buying items and decorating their minihompys, users were getting tired of this activity. Cyworld needed to re-engage its users. Further, many users were becoming skeptical about paying real money for virtual items. Most Internet companies such as Google or Naver (a Korean search engine with 75% market share) were not charging users for their services, since their business model was based on advertising.

Given these challenges, Cyworld started looking for new ways to provide value to its users. Cyworld was also aware of the new trends in the industry, especially blogs and user-created content such as YouTube. These new activities were generating substantial user interest and were rapidly becoming indirect competitors for Cyworld. In 2006, Cyworld decided to embark on a new strategy based on personal media (an upgraded version of the minihompy) and a media platform (an open platform where users could share news, photos, and videos).

In March 2007 Cyworld launched its upgraded version. Ms Ji-Young Park, a group leader of the new service, described the new Cyworld:

So far we were focusing on minihompys, since they were experiencing growth. But blogs were gaining momentum. Many users visited blogs to communicate with other people with similar interests. We wanted to meet the needs of these users within Cyworld. So we created Home2 to combine the strength of blogs and minihompys. Home2 also provides more space and allows users to be more flexible and creative.

Users could continue to use minihompys or migrate to Home2. The new service was supported by MyBase, a personalized information center that would store all user data and notify them of changes in their friends' minihompys. Four months after the launch, about 80,000 Cyworld users migrated to Home2. Some users found Home2 confusing, however, because they considered minihompys and blogs two different things, and combining them resulted in something that was neither a minihompy nor a blog.

The second area of the new strategy was the creation of the media platform. Byung-Hui Shin (leader of customer service) explained:

Personal media, such as minihompys, provides a space for private conversation with one's friends. In contrast, the media platform allows users to share content beyond their personal network of friends. Users can upload videos, news, or pictures on the media platform. If a user finds interesting content on the media platform, s/he can then visit the minihompy of the person who created this content. This "plaza" already has more than 50 million video clips. Cyworld users upload about 50,000 videos and 5 million photos per day. By comparison, YouTube gets about 150,000 videos per day, and Flickr users upload about 15 million photos every day.

While these additional services were intended to create better value for users, they also had the potential to create confusion and make Cyworld lose its focus as a social networking site. Some managers wondered whether Cyworld could retain its unique position in the marketplace if it became like Facebook, YouTube, Flickr, or iTunes.

Capturing Value

CEO Joo was evaluating three options for generating revenues. Cyworld was already doing a bit of all three, but it was time to have a strategic focus and clearly prioritize these options.

Paid Items

In 2006, paid items accounted for 72% of Cyworld's \$93 million revenue (**Exhibit 10**). The two largest categories of these items were virtual (or digital) items, and music. Virtual items, which typically cost about \$1, accounted for 32% of the paid-items revenues in 2006. The launch of 3D virtual items was expected to boost item sales to \$120 million by 2010.

Music accounted for 30% of paid items in 2006. Users downloaded songs to create background music for their minihompys. When users visited a friend's minihompy, they would hear the friend's background music. Currently, the songs purchased in Cyworld could only be used for background music on minihompys. Cyworld already had over 450,000 songs in its library from all major labels (such as BMG, Universal) as well as artists from Korea. By 2006, Cyworld was selling almost 200,000 songs per day at \$0.50 per song. With less than 50% of its revenue going toward copyright and royalty fees, Cyworld found that music was a very profitable part of the business. Sales grew to

around \$38 million by 2007 and were expected to grow each year by about 10%. Encouraged by iTunes' deal in June 2007 to embed its music download service into the British networking site Bebo, Cyworld was contemplating a similar service in the near future that would allow users to download songs to play on their MP3 players.⁷

Cyworld knew there were many reasons to stay with paid items as its dominant revenue model. Users were familiar with buying virtual items, and continuing with this approach would be the least disruptive. Cyworld also had the unique advantage of being one of the few companies to adopt this model. Even Facebook had recently tried this model in a modest way. In addition, music was a dominant part of many social networking sites including MySpace, and it appealed to the site's young audience. The popularity of music downloads was best illustrated by the success of iTunes, which had the 4 billionth song downloaded by February 2008 and had estimated sales of \$1.9 billion in 2007 with a 30% profit margin.⁸

However, many executives felt that the item-based model had reached its potential. Ji-young Yun, director of Cyworld's Internet media center, expressed this view: "There is a problem in item sales. Items were successful only on Cyworld, which had to do with its unique service features. Many users have already lost interest in the existing digital items. It is hard to expect much greater profitability from item sales in the future."

Mobile Networking

Leveraging the strength of its parent company SK Telecom, Cyworld started Mobile Cyworld, where users could connect to their minihomypys by mobile phone. Revenues from this service were shared between the mobile carrier and Cyworld. By 2006, Mobile Cyworld had 1.3 million users and accounted for 15% of Cyworld's revenue (see **Exhibit 10**). In 2006, the Mobile Social Networking Service (SNS) market was \$78 million, and Mobile Cyworld had a 90% share of this market. SKC's share of this revenue was \$14 million, with the rest going to its parent company, SK Telecom.

Apart from providing additional revenues for Cyworld, Mobile Cyworld had the potential to increase customer loyalty for SK Telecom. Cox Communications, a U.S. cable company, had a similar experience when it found that the monthly churn of its customers dropped from 1.5% for consumers subscribing to only one service, to 1.1% for consumers subscribing to two services, and to 0.7% for consumers subscribing to three services. Comparable monthly churn for AT&T Broadband were 2%, 1.6%, and 1.2%, for users of one, two, and three products, respectively.⁹ With an operating margin of 19.2%, any reduction in SK Telecom's current monthly churn of 3% could have a significant impact on the lifetime value of its customers.¹⁰

Mobile networking could potentially play a significant role in the global expansion plans of both Cyworld and its parent company SK Telecom. By 2008, SK Telecom had expanded its operations in China, USA and Vietnam. Starting in 2005, Cyworld also offered its services in China, USA, Japan, Taiwan and Vietnam. Cyworld had achieved only limited success in these countries. In 2007, Cyworld started operations in Germany with a joint venture with Deutsche Telecom. However, in

⁷ Maija Palmer, "Apple to sell music through Bebo network," *Financial Times*, June 13, 2007, p. 16, accessed August 2007.

⁸ Ed Christmas, "Apple's iTunes Store Has Sold 4 Billion Tracks—But Is It Profitable?" *Billboard.biz*, March 11, 2008, http://www.billboard.biz/bbbiz/content_display/industry/e3i174d24f4a4bd6a9273308815a9663bfc, accessed March 2008.

⁹ "The Book on Bundling," *Cable World*, July 15, 2002, accessed July 31, 2007.

¹⁰ Customer lifetime value (CLV) is the present value of profits generated from a customer over the life of his business with a company. A simple and approximate estimate of CLV is given by $m*r/(1+i-r)$, where m is the profit generated from a customer per period (e.g., month), r is the retention rate (or 1-churn rate), and i is the discount rate (see Sunil Gupta and Donald Lehmann, *Managing Customers as Investments* for details).

less than a year of its launch, Cyworld decided to pull out of the German market because of poor results.

Cyworld and SK Telecom were not alone in mobile networking. In Feb 2007, Vodafone struck a similar deal with MySpace and YouTube. In March 2007, the U.K. arm of France Telecom's Orange announced that it would soon start offering its customers access to Bebo. However, experts believed it might be three to four years before mobile networking became mainstream because of the cumbersome software and poor quality of user interfaces at that time.¹¹

Advertising

By 2007, advertising represented only 16% of Cyworld's revenues but had the largest growth potential. Young-Mok Kim, division manager of Cyworld Strategy Development, explained the advertising market and Cyworld's expectations:

The online advertising market can be divided into Search and Display Advertising. In 2006, Search and Display Advertising markets in Korea were about \$490 million and \$400 million, respectively. The total market grew by 46% in 2005, 29% in 2006, and is now stabilizing at an annual growth rate of 20%, resulting in a market of over \$1 billion in 2007. We expect this growth rate to continue until 2010 when the estimated market should be almost \$2 billion.

Our advertising revenue growth of 56% in 2005, and 30% in 2006 and 2007, has exceeded industry growth rates. As we implement targeted advertising, these revenues are expected to grow even more. Depending on the success of these programs, we are expecting revenues in excess of \$50 million by 2010.

Cyworld's approach to advertising had evolved over time. Starting as a "clean community" with no ads, it had slowly introduced advertising. However, its advertising was different from that on other portals, such as Yahoo!, which advertised on Cyworld's home page. Instead, most of Cyworld's advertising was on users' minihompys. To encourage users to carry these banner ads, Cyworld started programs such as "Happy Click." This program, which was modeled after Google's AdSense, paid users for each month they displayed an ad on their minihompys. Instead of paying cash, Cyworld paid its users Cyworld money, which could be used to buy digital items from Cyworld.

Cyworld was also experimenting with brand minihompys, which were mini home pages of major brands such as Nike. Users were encouraged to visit these corporate minihompys in return for free digital items. Taking a cue from MySpace, Cyworld was also contemplating launching a Cy-TV where members could access free content in return for watching video ads. The most recent proposal was to introduce targeted advertising similar to Facebook's Beacon program. (See **Exhibits 11** and **12** for a brief description and strategies of MySpace and Facebook.)

Many Cyworld executives believed strongly that an advertising-based model would be the future of the company. Supporters pointed to the success of Naver and Google. Social networking sites such as MySpace and Facebook were also largely ad-supported. As of February 2007, MySpace generated \$25 million in advertising revenues per month worldwide in addition to its \$900 million exclusive search deal with Google.¹²

However, this option was not without its risks. Because Cyworld had started as a "clean environment" that had not offered ads on minihompys until recently, some feared that a strong push

¹¹ Kate Norton, "Mobile Telcos Rush to Social Networking," *BusinessWeek.com*, April 3, 2007, accessed August 2007.

¹² Mark Scott "How MySpace Conquered the Continent; It was late to the social-networking party in Europe, but the News Corp. site quickly overtook rivals with features designed for, and by, locals," *BusinessWeek*, July 11, 2007, accessed July 2007.

in the direction of advertising could alienate users. It would also require new skills in dealing with corporate sponsors and understanding their needs. While users might find it attractive to get free digital items by clicking on brand minihompys, Cyworld needed to prove its value to its corporate sponsors. Even MySpace and Facebook had yet to show significant revenues from advertising. In November 2007 Facebook launched a new program, dubbed Beacon, which leveraged its users' information to deliver targeted advertising. Facebook's users had a strong negative reaction to this because of privacy concerns. Soon, Facebook retreated from the program and made a public apology. Some experts believed that users were less interested in ads on social networking sites than on search sites, such as Google, since users visited Facebook or Google for very different purposes and with different mindsets. Indeed, some studies showed that the click-through rate of ads on social networking sites was 0.04%, compared with 0.2% on other types of sites.¹³ An ad-based model would also put Cyworld squarely against large competitors like Naver and Google.

Looking Ahead

Joo could certainly choose a combination of these options. The industry was witnessing a convergence of technologies as well as partnerships between companies. However, Joo needed to prioritize these options and carefully balance the benefits of trying multiple things and keeping his options open versus the benefits of specialization and focus. He needed to consider how each option would influence the customers it targeted, the services it offered, the capabilities it needed, and the competition it faced. Joo realized that his choice would also depend on his vision of what he wanted Cyworld to be in the future—the next MySpace, Google, iTunes, Amazon, or a combination of these companies? In addition, he would have to consider what role, if any, should be played by Cyworld's parent company, SK Telecom, as well as how Cyworld's global expansion plans would affect his choice.

¹³ "So Many Ads, So Few Clicks," *BusinessWeek*, November 12, 2007, accessed December 2007.

Exhibit 1 SK Communication's Income Statement (in US\$ thousands)

Revenue (by source)	FY 2006	FY 2007
- Advertisement	47,425	47,302
- e-commerce	9,665	9,086
- Product & contents	21,034	23,803
- Community service	80,385	78,731
- Others	26,211	38,351
Total revenue	184,720	197,272
Cost of Goods Sold	13,351	13,223
Gross Profit	171,368	184,049
Operating Expenses		
- General & Admin. expense	59,849	76,667
- Human resources	55,552	62,303
- Depreciation & Amortization Expense	28,038	33,929
- Marketing expense	8,632	11,501
Total Expenses	152,071	184,401
Operation Profit	19,298	-351
Non-operation Income	5,750	4,039
Non-operation Expense	16,149	33,146
Profit before tax	8,898	-29,458

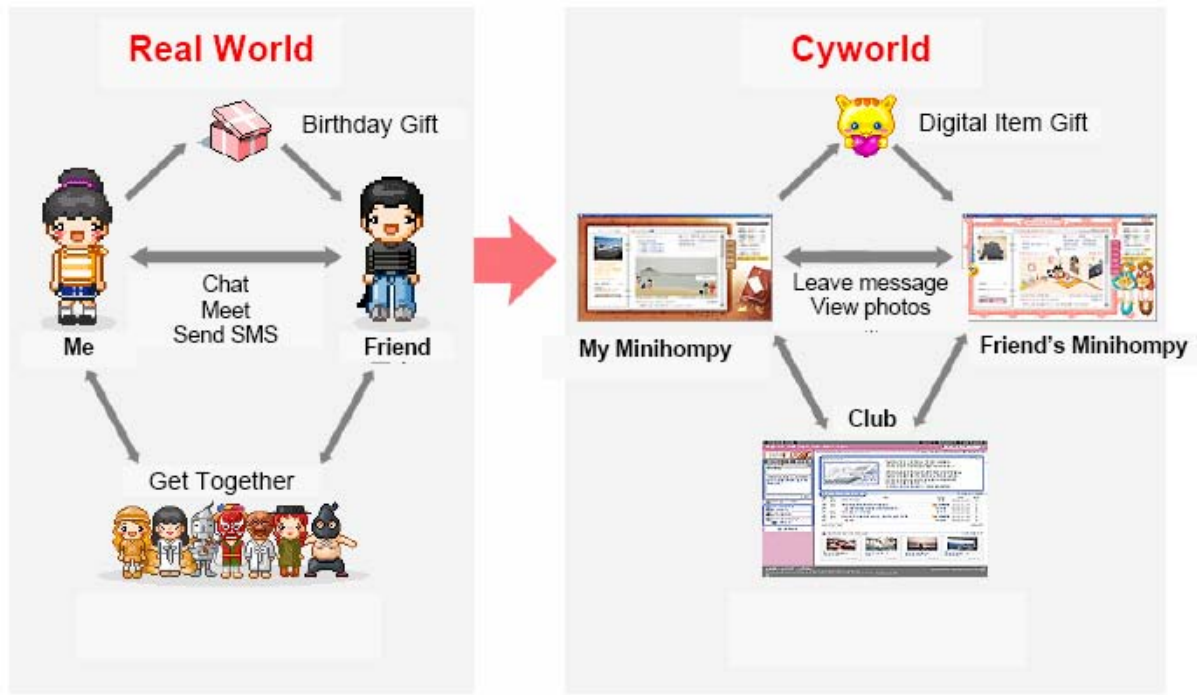
Note: Advertising revenues include Cyworld advertising as well as revenues from display and search ads.

Community service revenues include Cyworld revenues from item sales and Mobile Cyworld.

The majority of non-operating expenses were due to merger and acquisition.

Source: Company documents.

Exhibit 2 Cyworld Concept



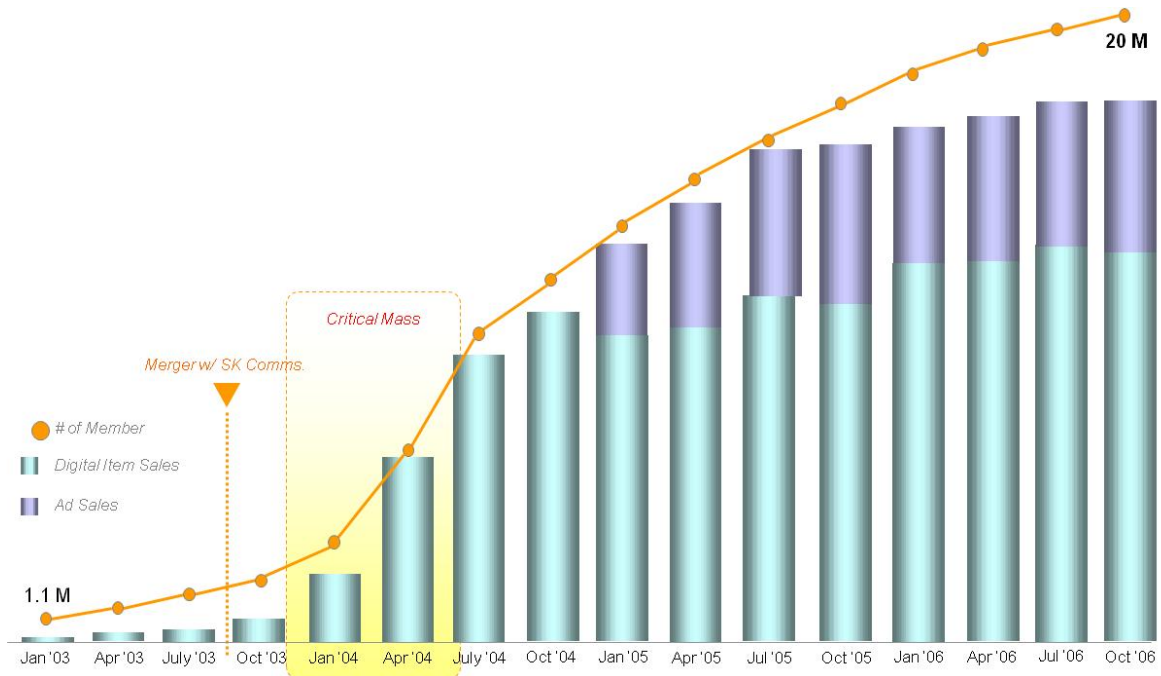
Source: Company documents.

Exhibit 3 Minihompy

The screenshot shows a Cyworld Minihompy page with five numbered callouts: 1. Buddy Link (a list of links to buddies), 2. Update News (a list of uploaded and scraped subjects), 3. BGM* Player (music bought in Gift Shop), 4. Minihompy Domain (changeable domain name), and 5. Miniroom & Storyroom (space to express myself). The page includes a profile section, a 'Today's story' section, and a 'BGM* Player' section.

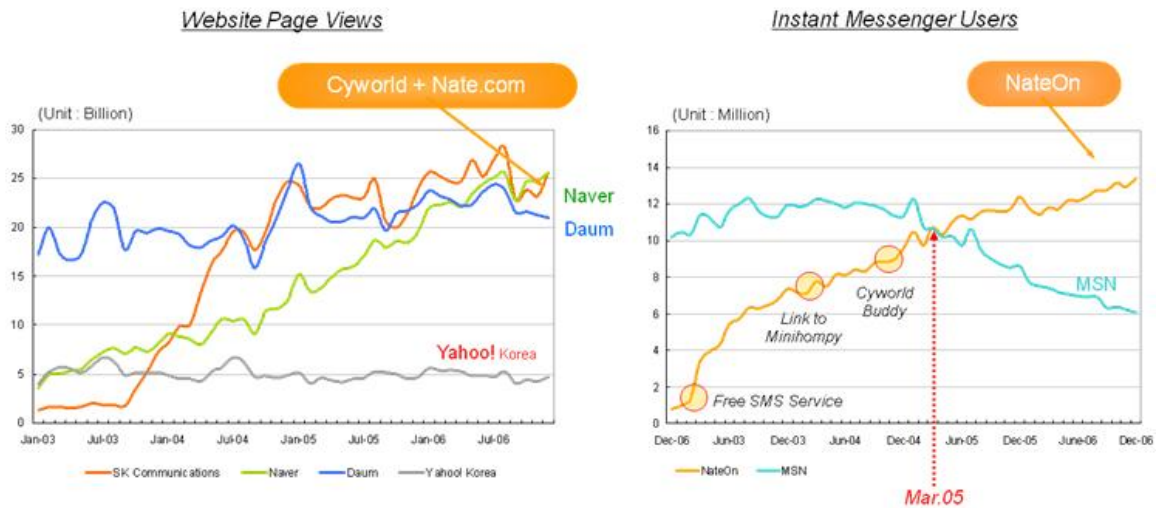
Source: Company documents.

Exhibit 4 Growth of Cyworld



Source: Company documents.

Exhibit 5 Cyworld, NateOn and Nate.com



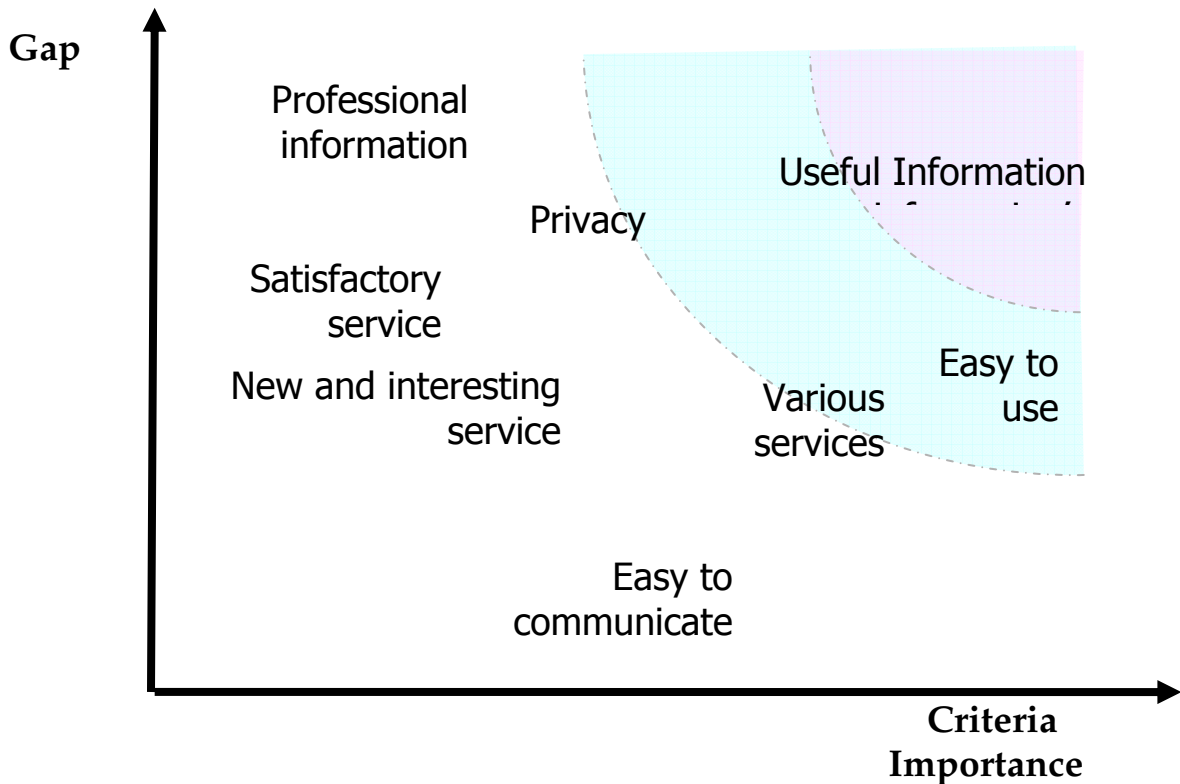
Source: Company documents.

Exhibit 6 Registered Users



Source: Company documents.

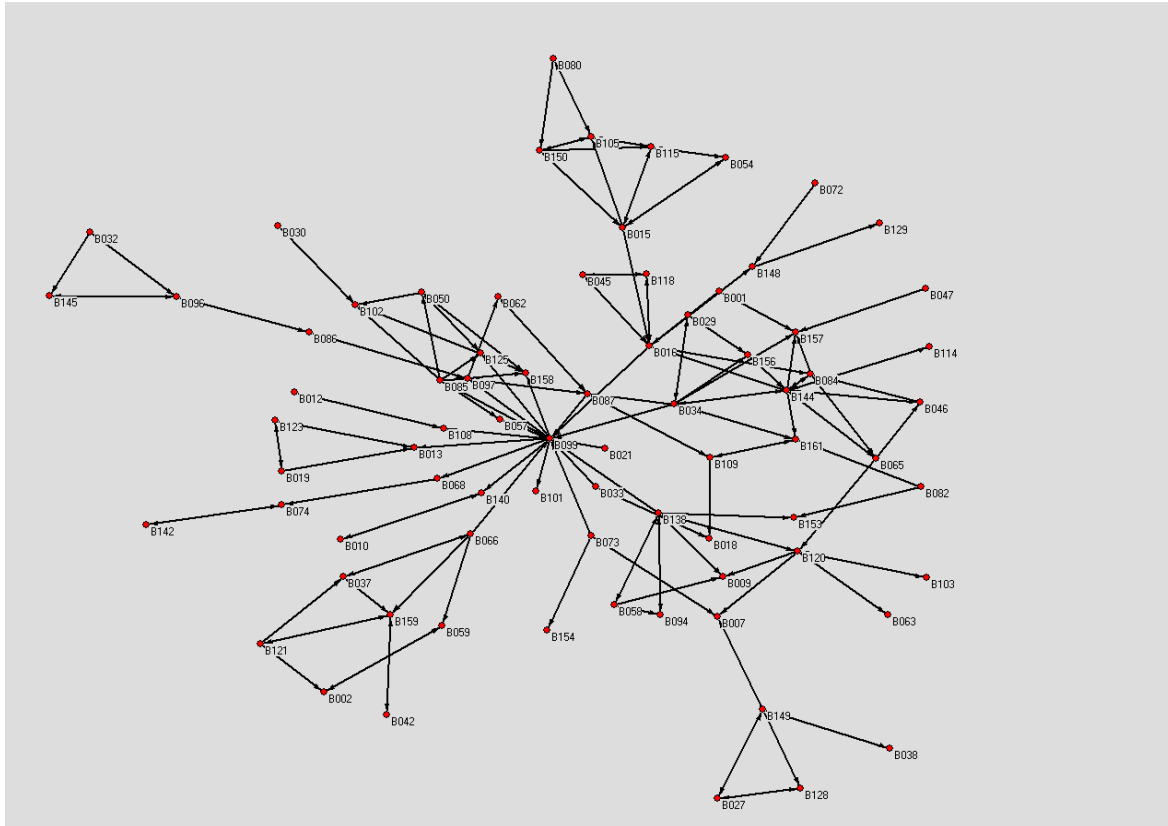
Exhibit 7 Needs Gap Analysis (N=1,200)



Gap = Importance - Satisfaction

Source: Company research.

Exhibit 8 A Sample Network of Cyworld Users



Note: Each node (e.g., B099) represents a user. A line connecting two nodes indicates social interaction (e.g., a visit to a minihompy) between two users.

Source: Company data.

Exhibit 9 User Segmentation (Sample Size N=51,177)

Activity ¹				Purchases (US \$) ²				Connections ³				
N	Mean	Min	Max	N	Mean	Min	Max	Sample Size (N)	Mean	Min	Max	
Low	26628 (52.0%)	0	0	17016 (33.3%)	2	0	6.25	Low	16892 (33.0%)	44	1	73
Med	10496 (20.5%)	1.3	1	16551 (32.3%)	13.28	6.3	22.2	Med	16682 (32.6%)	101.1	74	132
Hi	14053 (27.5%)	15.6	3	17610 (34.4%)	62.17	22.25	8,352.95	Hi	17603 (34.4%)	219.4	133	1632
Total	51177 (100%)	4.6	0	51177 (100%)	26.35	0	8,352.95	Total	51177 (100%)	122.9	1	1632

¹ Activity = number of times a user "scrapes" from a friend's minihompy in the last four months.

² Purchases = money spent in purchasing virtual items in the last four months.

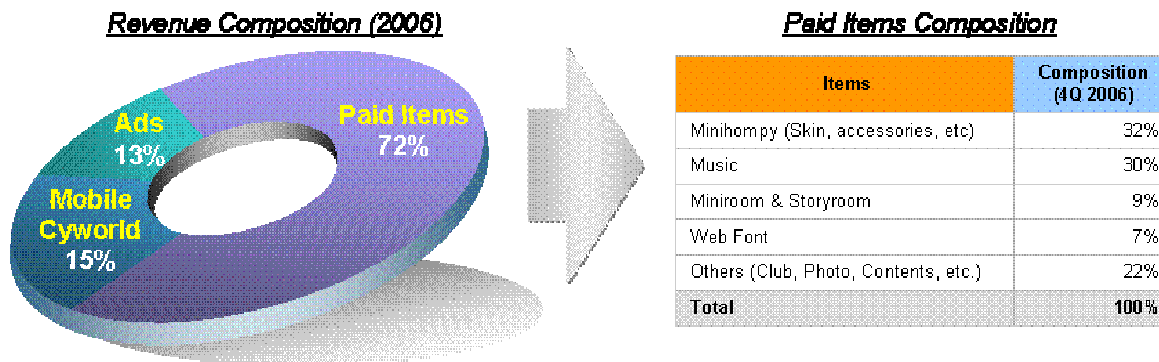
³ Connections = number of ties or relationships a user had in the last four months (ties can be formed from incoming or outgoing visits).

Activity & Purchases				Activity & Connections				Connections & Purchases			
Purchases				Connections				Purchases			
Low	Med	Hi		Low	Med	Hi		Low	Med	Hi	
**21.80	16.66	13.57	52.03	21.48	17.12	13.43	52.03	17.12	9.76	6.12	33.01
5.83	7.11	7.57	20.51	5.62	6.98	7.91	20.51	9.71	11.87	11.02	32.6
5.62	8.57	13.27	27.46	5.9	8.5	13.06	27.46	6.42	10.71	17.27	34.6
33.25	32.34	34.41	100	33.01	32.6	34.4	100	33.25	32.34	34.41	100

** To be read as "21.80% of the 51,177 in the sample had low activity and low purchases."

Source: Company data.

Exhibit 10 Composition of Cyworld's Revenues



Composition of Cyworld's Revenues in 2005–2007 (in US\$)

	2005	2006	2007
Paid Items	58 million	67 million	65 million
Mobile Cyworld	9 million	14 million	15 million
Ad	9.2 million	12 million	15 million
Total	76.2 million	93 million	95 million

Source: Company documents.

Exhibit 11 MySpace

MySpace was launched in the fall of 2003 as an online community for musicians, actors and artists. By the summer of 2007 it was the leading social networking site with over 180 million global registered users.¹⁴ In June 2007, MySpace attracted over 114 million unique users to its sites all over the world, representing a 72% increase versus a year ago. Although it had presence in many countries, over 62% of its users came from North America.¹⁵ In April 2007, MySpace had an almost 80% share of the U.S. social networking market, followed by Facebook (11.5%) and Bebo (1.3%).¹⁶

After being acquired by News Corp. for \$580 million, MySpace expanded beyond its social networking roots into a popular culture and lifestyle portal. In May 2007, MySpace announced that it would partner with a dozen entertainment companies that would provide online videos for “branded channels” for users to display on their pages. In June 2007, MySpace also announced a deal with Sony Pictures Television to show “minisodes” from its archives.¹⁷ By making professionally produced content available to its users, MySpace hoped to dramatically increase its advertising revenue.

In September 2007, MySpace was experimenting with targeted advertising. In the first phase of this program, called “interest-based targeting,” users were assigned to 10 categories based on their primary interests such as sports, fashion, finance, auto and video games. In the second phase, called “hyper targeting,” users were further subdivided into hundreds of sub categories. For example, sports fans could be divided into subgroups like basketball, college basketball, and college football. Initial results showed that these programs improved the likelihood of users clicking on an ad by 80 percent, on average. Some experts predicted that these programs could potentially increase MySpace’s revenues from its current \$40 million a month to over \$70 million a month within a year.¹⁸ This revenue was in addition to the \$900 million exclusive deal to allow Google as its search engine for four years. Jobs and classified services were other sources of potential revenue.

In spite of its rapid growth, MySpace was facing several challenges. Privacy was becoming a big issue for social networking sites as many considered them a haven for sexual predators. Privacy was likely to become even more critical with MySpace’s attempt to target ads to its users. Finally, MySpace was beginning to feel the heat of its fast growing rival, Facebook.

Source: Casewriter.

¹⁴ Patricia Sellers, “MySpace Cowboys,” *Fortune*, Sep 4, 2006, http://money.cnn.com/magazines/fortune/fortune_archive/2006/09/04/8384727/index.htm, accessed August 2007.

¹⁵ comScore, Inc., “Social Networking Goes Global,” press release July 31, 2007, <http://www.comscore.com/press/release.asp?press=1555>.

¹⁶ Data from Hitwise, “MySpace Receives 79.7% of Social Networking Visits,” press release, May 21, 2007, <http://www.hitwise.com/press-center/hitwiseHS2004/socialnets.php>, accessed August 2007.

¹⁷ “MySpace Announces Video and Sony Pictures Television Launch the Minisode Network” Business Wire, June 19, 2007, via OneSource Information Services, Inc., accessed June 2007.

¹⁸ Brad Stone, “MySpace mines data to tailor advertising,” *International Herald Tribune*, September 18, 2007.

Exhibit 12 Facebook

Facebook was the second largest social networking site in the U.S. in 2007. It was founded in February 2004 by Mark Zuckerberg, a Harvard University dropout. Facebook's started by serving college students. Later it expanded to high school students and then opened its network to anyone with an email address. By October 2007, Facebook had almost 50 million users and was doubling its user base every six months. Among the social networking sites, MySpace received 76% of U.S. traffic in the week ending October 20, 2007, compared with 15% for Facebook.¹⁹

In May 2007, Facebook opened its doors to allow thousands of developers to create applications for its "platform." New applications allowed Facebook users to listen to music, insert book reviews on their pages, play games or join charity drives, all without leaving the site. Zuckerberg's vision was to position his company as a "social operating system" just like Windows was for PCs.

Facebook was largely supported by advertising. In 2006, Microsoft agreed to pay a minimum of \$100 million per year through 2011 to broker banner ads for Facebook. However, this business model could change in the future. In a speech to more than 700 developers and journalists in May 2007, Mark Zuckerberg said, "You can build a real advertising business on Facebook. If you don't want to run ads, you can sell something. We encourage you to do both."²⁰

In October 2007, Microsoft agreed to buy a \$240 million stake in the company, which placed Facebook's market value at \$15 billion.²¹ In November 2007, Facebook launched Beacon, its targeted ad program. Beacon tracked users' activities on Facebook as well as third-party sites and showed the results to users' friends. For example, if a user rented a movie from Blockbuster, Beacon would share this information with this user's friends. Facebook hoped this program would be seen as "trusted referrals" among friends and generate more sales for advertisers and more ad revenues for Facebook.

However, the program generated a lot of controversy and a strong backlash from its users who considered it a serious breach of their privacy. Within a month, Zuckerberg apologized on Facebook's blog about mishandling this program and allowed users to "turn off" Beacon. However, in a January 2008 interview on 60 Minutes, he maintained the value of Beacon, "It might take some work for us to get this exactly right . . . [but] this is something we think is going to be a really good thing. I actually think [our ads] make [Facebook] less commercial. What would you rather see? A banner ad from Bloomingdale's or that one of your friends bought a scarf?"²²

Critics, however, were not so sure. This was the second time in 15 months that Facebook had run into privacy-related backlash from its users. In 2006 Facebook was swamped with user complaints when it introduced a news feed function that automatically informed friends of any changes in a user's profile. Skeptics worried that the third strike against Facebook might be fatal.

Source: Casewriter.

¹⁹ Jay Greene, "Microsoft and Facebook Hook Up," *BusinessWeek*, October 25, 2007, accessed November 2007.

²⁰ Brad Tone, "Facebook Expands into MySpace's Territory," *The New York Times*, May 24, 2007.

²¹ Julie Sloane, "Facebook Got Its \$15 Billion Valuation—Now What?" *Wired*, October 26, 2007, accessed November 2007.

²² Heather Havenstein, "Facebook CEO tells 60 Minutes that Beacon is 'a really good thing,'" *Computerworld.com*, January 11, 2008, accessed February 2008.