

Twitter Overview

Twitter is a social networking service that launched in 2006, which was around the same time smartphones began to penetrate the U.S. consumer market. Unlike other social networking sites at the time, Twitter restricted users to sending short 140-character messages, called “tweets”, using SMS or the internet. Initially catering to technology enthusiasts and pundits, Twitter’s popularity rose when the founders advertised the service at SXSWi, a film and music conference filled with celebrities and prominent journalists.¹ Explosive growth followed, leading the company to go public in 2013. As of July 2014, Twitter has approximately 275 million users and is still in the growth stage of the industry life cycle.²

1) Risk of Entry by Potential Competitors

Economies of Scale

Twitter is a web service, and it is powered by thousands of servers that allow millions of devices to send and pull requests for content, which in Twitter’s case is tweets that may include either text, images, or videos. While the details of the company’s server and web hosting costs are not public information, it is highly likely that the company has achieved economies of scale on their web infrastructure. Because of their immense web traffic, the company probably has deals with server, web hosting, and other internet infrastructure vendors for quantity discounts. It is unlikely potential competitors would be able to strike such deals, as their traffic would not be near Twitter levels when they launch, thereby reducing the risk of entry by potential competitors.

¹ For a fascinating account on how Twitter started, a reading of Hatching Twitter by Nick Bilton is highly recommended.

² <https://investor.twitterinc.com/releasedetail.cfm?ReleaseID=862505>

Brand Loyalty

In addition to achieving economies of scale, Twitter also possesses a lot of brand loyalty. The Twitter logo is found on many company advertisements on television, sports commentators ask viewers to follow them on Twitter, as do celebrities and notable politicians. Most notably, this is often done voluntarily without the need for Twitter to advertise or solicit for their logo to be placed on the adverts. As a result, it would be extremely difficult for a competitor to come along and sweep Twitter users away, as the service is favored immensely by the community. This loyalty will reduce the risk of entry by potential competitors.

Absolute Cost Advantages

In November 2013, Twitter went public on the NYSE with a market capitalization of \$24.5 billion (is it worth \$32 billion as of 09/14/14).³ As a public company, Twitter has access to cheaper funds, and is able to finance more Research and Development and Sales and Marketing spending.⁴ In addition, the company can invest more money into its infrastructure and mobile applications, making it even harder for competitors to match Twitter's absolute cost advantages. For this reason, the risk of entry by potential competitors is further lowered.

Customer Switching Costs

Twitter is infamous for severely restricting access to its service and API to other application makers, making it very difficult to switch to another service or application.⁵ In fact, until recently, users of the service could not export their tweets even for archival purposes. Thus, it would be difficult for a Twitter user to import their past tweets into a competitor's service due to the restrictions the company places on your content. Users

³ <http://finance.yahoo.com/q?s=TWTR>

⁴ Access to cheaper funds is one of the elements of absolute cost advantages, according to *Strategic Management: An Integrated Approach 10E*, pg. 52.

⁵ This is just one example of Twitter's API restrictions: <http://www.theguardian.com/technology/appsblog/2013/feb/27/twitter-token-limit-falcon-pro>

of Twitter would also be hesitant to abandon the service after using it for years, as they have accumulated many followers and tweets on it, making it a powerful entry barrier to competitors.

Summary for Risk of Entry by Competitors

With respect to Porter's Five Forces Model, it is our conclusion that Twitter faces a low risk of entry by potential competitors due to the aforementioned barriers. These barriers could not be overcome by App.net for example - a Twitter competitor that could not gain the traction to compete in any considerable way.⁶ It is also worth noting that the risk of competition is higher for Twitter from well established competitors, as they have the economies of scale and financial capital to compete with Twitter.

2) Rivalry Among Competitors

Industry Competitive Structure

The social network industry has been incredibly competitive in the last decade, with the rise of Myspace, Facebook, and now Twitter.⁷ In addition to these three technological behemoths, virtually thousands of other social networks have sprouted to compete in the arena for user attention. And yet, while the social media industry is extremely fragmented, Twitter has not yet faced any worthy competition in the last eight years of its existence. This is thanks to the above entry barriers that the company commands.⁸

Industry Demand

The user demand for social networks is a difficult topic to tackle, since the definition of a social network is not entirely clear. For example, users are given the

⁶ <http://www.theverge.com/2014/5/6/5688014/app-net-cant-pay-employees-but-promises-to-carry-on>

⁷ Myspace is just a shell of what it once was, after being overtaken by Facebook.

⁸ Not all of these barriers were erected by Twitter.

option to make their Twitter accounts private, essentially turning the social network into an antisocial one. That said, as a whole, as more people all over the world are purchasing mobile devices with internet access, the amount of users social networks such as Facebook and Twitter are gaining is steadily increasing every year. For this reason, we believe that this growing industry demand somewhat offsets the rivalry between the various social networks, lowering the risk of competitor rivalry.

Cost Conditions

Cost conditions for Twitter are based in majority on fixed costs, since each additional user requires a negligible amount of server load. Given that Twitter is a free service that is monetized by ad revenue, the company makes more money with more volume, spreading the fixed costs over a larger user base.⁹ Competitors that would like to enter the tweeting space, as a result lower user counts, would have higher fixed costs per user and thus not be as profitable. This further lowers the risk of competitor rivalry for Twitter.

3) Bargaining Power of Buyers

In Twitter's case, the buyers are companies and individuals who purchase ads on Twitter. Because the quantity of social networks and internet advertising placements is so large, the bargaining power of buyers is high, since they can switch to any other service such as Facebook, or Google AdWords.¹⁰ This can heavily reduce Twitter's revenues, making it an extremely high risk element.

⁹ More user impressions allow Twitter to charge higher amounts for ads.

¹⁰ An interesting article on digital advertising spending: <http://www.theatlantic.com/business/archive/2014/03/facebook-and-google-own-the-future-of-advertising-in-2-charts/359568/>

4) Bargaining Power of Suppliers

Twitter's suppliers are its users, who can switch to any substitute service (see analysis below) for free, but that switch brings with it intangible switching costs such as lost followers and prior tweets¹¹. That is, Twitter is dependent entirely on its suppliers, since they supply both the content and the impressions, which is how Twitter generates ad revenue. Because of this, the bargaining power of suppliers poses a high risk.

5) Substitute Products

In the social networking space, there is almost no limit for substitutes. Facebook, Instagram (now part of Facebook), Snapchat, App.net, Tumblr, LinkedIn, Quora, Foursquare, and Twitter all compete for user attention, but in different ways. Probably Twitter's main competitor, Facebook allows users to post "statuses", which are similar to tweets except they have no character limit and allow for more features. At the end of the day, the limiting factor is the users' time, since a user can give only a certain number of hours per day for social networking, making the risk of substitute products very high for Twitter, unless it is able to distinctly differentiate its product.

6) Complementary Products

Complementary to Twitter are 3rd-party mobile applications such as Tweetbot, Tweetdeck, and various other services that add to Twitter's features.¹² These complementors add value to Twitter, and by proxy, Twitter's users. Most competitors to Twitter do not provide such an extensive API for 3rd-party's to work with, making the risk from complementors weak for complementary products.

¹¹ This is an example of an exit barrier for Twitter users.

¹² An exhaustive list of Twitter complementary products and services is listed here: http://en.wikipedia.org/wiki/List_of_Twitter_services_and_applications

Macroeconomic Forces

There is a slew of macroeconomic forces that affect Twitter, namely privacy and government regulations. With the recent NSA leaks, user privacy has been on the forefront of tech news. How Twitter reacts to government data requests and how secure it keeps user data are important given the public demand for privacy. Twitter must walk a fine line between government requests and user demand for privacy.

Conclusion

In the past, Twitter has been very accommodating to the demands of users, and much less so to the demands from government.¹³ While this is great news for users, it's worth questioning whether the political forces will impose stricter regulations on Twitter, thereby upsetting users and profitability.¹⁴ It will also be vital for Twitter to handle user privacy with the utmost privilege, given the amount of data leaks and hacks in the past months.¹⁵ This is because in the last few years, security and user privacy has been on the social radar, demanding internet services to fortify themselves against breaches. How Twitter handles these demands will be a powerful asset, or a destructive liability, for the company.

¹³ Twitter must be commended for its transparency regarding government and third party information requests. This data is available to the public at the following link: <https://transparency.twitter.com/information-requests/>

¹⁴ Twitter is blocked in China, among many other countries, due to government censorship. This can severely limit Twitter's future growth. <http://thenextweb.com/asia/2012/09/26/surprise-twitters-active-country-china-where-blocked/>

¹⁵ A major iCloud security breach was made just a few weeks ago, among others that attacked many other companies. http://bits.blogs.nytimes.com/2014/09/04/apple-says-it-will-add-new-security-measures-after-celebrity-hack/?_php=true&_type=blogs&_r=0