What sources of finance might Pinterest acquire in order to grow and compete with other social networking sites?

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Introduction

Pinterest is a fast-growing social networking website that was founded in 2009 by Yale graduate, Ben Silbermann (Bing Booster Team). Pinterest is a virtual pinboard, allowing its users to view pictures ranging from home décor ideas to funny animals. The website is very simplistic with the pictures set up in a grid with a caption underneath it. Users can then pin these pictures onto their various boards with titles such as “Recipes to Try.” When a user clicks on the picture, it takes them to website where the picture was originally from. They can then read about how the recipe or craft was made, or order the item online. This website has become popular with many women throughout the world, mainly from the Midwest.

Although the website was launched in 2010, it didn’t really take off until late in 2011. In November 2011, Pinterest had 4.9 monthly viewers which more than doubled to reach 11.7 million in January 2012. In February 2012, there were 17.8 monthly viewers, a 52% increase from the month before (Ortutay). Pinterest’s team has also grown as their users have increased. The team now consists of eight people, including Silbermann and his two co-founders. Andreessen Horowitz and Jeremy Stoppelman are both prominent investors in the company (Needleman). Since Pinterest is privately held, they are not required to release financial information. Their website does not have any advertisements, and even though Pinterest has many users each month they claim to not bring in revenue (Needleman). What sources of finance might Pinterest acquire in order to grow and compete with other social networking sites?

Commentary

Pinterest is internally financed by main investors Andreessen Horowitz and Jeremy Stoppleman. Pinterest has become extremely popular over the past few months but they are having difficulties figuring out how to make money off of their popularity. Jeremy Levine, a board member of Pinterest, comments on the money making problems and claims they have many ideas but no execution yet. Since Pinterest is a fairly new social networking website, they are not interesting in going public yet. The board of Pinterest would rather develop their ideas more before they give up part of their control by going public (Yarow). However, once Pinterest does develop their ideas an IPO would draw in share capital which could then be their main source of finance. The board of Pinterest could buy a majority of the shares to keep control of the company, and sell the remaining shares in order to bring in some revenue.

Pinterest also claims they have done an API, application programming interface, but are hesitant to release it to the public. If they release the API, it will allow developers to create applications using data from Pinterest (Yarow). They have not released the API yet because they are worried that they will have the same problem Twitter did. When Twitter released their API, they were still a developing business. The other developers built applications with features Twitter was missing, but as Twitter developed they added these features and developed their own mobile phone applications more. Twitter's own developments hurt the other applications that had been created which caused the developing community to turn against Twitter (Yarow). Since Pinterest is a young company, like Twitter was when they released their API, waiting to release their API after they have developed more would be a better option. If their API is utilized in the right way, it could become another source of finance.

Many social media websites run into the same problems as Pinterest. They have the users, but they don't have a plan to generate revenue. Facebook was in a similar situation, but the company went public and shows advertisements to deal with the revenue problem. Since Pinterest would want to make improvements before going public, advertising would be another source of finance for the new company. If the company could design a new format for the website so that advertisements would not interfere with the simplicity of the website, then advertisements wouldn't take away from the user's experience.

Although Pinterest claims to be unprofitable, there is some information that contradicts this. Pinterest has been using a service called SkimLinks which is the company's sole source of revenue. The program ensures that Pinterest receives credit for sales referrals (Madrigal). For example, if a woman were looking at the clothing section on Pinterest and decided she wanted to purchase a shirt, she would simply click the picture. This would lead her to the website selling the shirt. When she buys this shirt, Pinterest receives a small percentage of the sale since they referred her to the website. SkimLinks simply ensures that Pinterest receives credit for and data from the sale. Perhaps Pinterest is claiming to be unprofitable, but they have been making and using money from SkimLinks for the past two years. Since Pinterest has survived solely from this revenue and private investments, further sources of funds many not be necessary. If Pinterest is interested in becoming a large, high profit company then alternate sources of funds would be necessary since they are supposedly unprofitable (Madrigal). Their current plan using SkimLinks is profitable and ideal for users since advertisements don't clutter the simple setup of the website.

Pinterest many also need to be comfortable making less revenue since more revenue could lead to legal problems. The website displays pictures, but the images technically don't belong to them (Taylor). As soon as Pinterest starts making their own money, intellectual property owners have the right to ask Pinterest to pay them or delete their images. Some believe that similar social media websites such as Tumblr and YouTube faced the same problem, which is why it took so long for both websites to start making money (Taylor). For now, Pinterest's best solution to this problem would be to develop a plan to deal with the copyright problems before they attempt to generate revenue.

Youtube faced similar copyright problems after the website was founded and became popular. Instead of dealing with the threats internally, the founders and investors of Youtube decided to cash in and sell to Google. Youtube was not originally interested in selling at such an early stage of development, but they had the looming copyright threats and increasing server costs as the website grew rapidly (Blodget). Google was also willing to offer a large amount of money to Youtube. Pinterest is in almost the same situation as Youtube when they sold to Google. They have looming copyright threats, and their server costs are increasing (Blodget). If Google were willing to let the current Pinterest board stay in charge of the development of the website while Google would simply own the company and deal with the legal matters, Pinterest could become a huge success. The Pinterest board would still be in charge of developments, which is what they wanted, and Google would own successful social networking site, which would only help after the bomb, Google + (Blodget).

Conclusion

Pinterest is a popular social networking website with a problem similar to many young socially based websites. Over the past two years, Pinterest has built up its user base, and now is unable to create a plan to make money. There are many optional sources of funds for the company, including both internally and externally financed options. Before Pinterest is able to execute their plan, they must deal with their looming legal problems. Since Pinterest is facing these copyright problems, selling their company may be a realistic solution for them. If they are able to come up with a plan to deal with these copyright issues, then Pinterest has many potential sources of finance. If the company were willing to give up some control then going public or releasing an API would draw in revenue. If they weren't willing to make this sacrifice then advertisements on the website would also bring money to the company. Although Pinterest claims to be unprofitable, other sources claim they are getting a percent of sales for the referrals made through the website. Since this may be the case, then Pinterest could continue to use their program SkimLinks to receive money for these sales. Since Pinterest is still a developing company, making money is an issue they are still dealing with. I am confident that with time Pinterest will solve their financial problems, perhaps through one of the methods described, and become a main social networking website in the future.

Appendix

Document 1:

Yarow, Jay. "Pinterest Is Scared Of Having A 'Twitter Problem'" *Yahoo! Finance*. Business Insider, 26 Mar. 2012. Web. 29 Mar. 2012. <http://finance.yahoo.com/news/pinterest-scared-having-twitter-problem-140712764.html>.

Pinterest Is Scared Of Having A 'Twitter Problem'

By Jay Yarow | Business Insider – *Mon, Mar 26, 2012 10:07 AM EDT*

Pinterest has an API done and ready for developers, but it hasn't released it to the public yet.

And it might not release it for a while, says an industry source familiar with Pinterest's plans. This source says that Pinterest fears having a "Twitter problem."

An API, or application programming interface, allows developers to build apps using Pinterest data.

Twitter released its API when it was still an immature company, allowing developers to build applications with features that it was missing. When Twitter matured, and it wanted to control its platform, it began adding those features, thus damaging those developers.

For instance, Twitpic, which built a way to share photos is now threatened because Twitter added native photo sharing. HootSuite, and Twitterrific, which build great mobile apps were crushed when Twitter started putting more effort into its own mobile apps.

As Twitter began competing with its developers, the developer community turned against Twitter. It didn't really trust Twitter.

Pinterest doesn't want that to happen. It's a very young company and it's just getting started, says our source. It doesn't want developers to build features/applications that it plans on building, and then alienate those developers by building similar features.

Also, our source says Pinterest is, "more Apple than Google." It believes in design and control and doesn't want other people mucking with the look and feel of what it's building.

This is important because if Pinterest is going to make the leap, and become a $5 billion company like VCs think, it has to become a platform. That's how web companies become big.

It's also important because VCs are excited to fund a wave of startups that build on the Pinterest platform.

For now, those VCs and startups have to sit tight. Pinterest is staying closed for a while longer.

Document 2:

Madrigal, Alexis. "Why Pinterest Is Playing Dumb About Making Money." *Yahoo! Finance*. The Atlantic, 17 Feb. 2012. Web. 26 Mar. 2012. <http://finance.yahoo.com/news/why-pinterest-playing-dumb-making-192501616.html>.

Why Pinterest Is Playing Dumb About Making Money

the Atlantic *By* contributors@theatlantic.com (Alexis Madrigal) | The Atlantic – *Fri, Feb 17, 2012 2:25 PM EST*

Despite the company's protests to the contrary, Pinterest already knows how to make money, and may already have a model that would work for users, retailers, and itself.

Over the past few weeks, we've seen Pinterest rise out of the pack of next-next-next-gen social networks after humming along in relative obscurity for a couple of years. We presented our take on the visual bookmarking site a few days ago. Along with the explosion of interest, the company's sole source of revenue came into the spotlight: affiliate links. Pinterest had been using a service calledSkimLinks, which is helmed by Australian native, Alicia Navarro, and which, has been in business itself for several years without a bunch of hoopla. SkimLinks' software looks at links users post to websites, determines if there is an affiliate program to which they can be linked, and appends a code that ensures Pinterest gets credit for (and data from) the referral.

To be honest, I don't see much wrong with this practice. The only people it could possibly hurt are merchants who are posting things to Pinterest and then having people click through the site, picking up an affiliate code that costs them a small percentage of the sale. For the average user, it's a non-invasive way to generate revenue for a site they like that doesn't require putting up with advertising.

Nonetheless, once the story broke that Pinterest was quietly making money off its users (the horror!), the company started to backpeddle on its practices. That reached full bloom in a Wall Street Journal article yesterday in which various Pinterest parties (CEO, board member) fell all over themselves to declaim that the company knew anything about making money.

"Pinterest's monetization strategy isn't in the oven and it's not even off the baking table. We have one hundred ideas but no execution as of yet," Jeremy Levine, a board member of Pinterest and a venture capitalist at Bessemer Venture Partners, told the WSJ.

Ben Silberman, Pinterest's CEO, struck the same "Money, well, golly?!" chord. "My hope is that if we build a service that a lot of people use to plan and discover things, that will be really valuable," Silberman said.

Now, all of this is pretty standard Silicon Valley speak. They pretend that they don't care about making money off of users and we users pretend that we aren't the product. It's all about "building value" and "creating a better experience" and all that. Which is fine and good. I find the Valley's deep and starry-eyed belief that money flows to all the right people to be very endearing.

But let's get real here: **Silberman's company had been happily using and money with SkimLinks for 2 YEARS**. Then, suddenly, $37 million of venture capital falls into their hands and suddenly all they care about is building that "a lot of people use to plan and discover things."

An anonymous source also told the WSJ that the company, VC-valued at $200 million, "isn't yet making much revenue and is unprofitable" and furthermore, "affiliate marketing isn't a major part of Pinterest's business model right now, according to the company and its venture capitalists."

This is a bit strange because:

1)We know Pinterest is driving truly massive traffic to retail sites, by some accounts more than YouTube, LinkedIn, and Google+ combined. It is, after all, a platform that's perfect for shopping!
2) We know Pinterest used SkimLinks to add affiliate links.
3) Affiliate links generate revenue.

Should this add up to chump change? Let's do the math just to get an order of magnitude estimate.

Commissions on sales for affiliate links vary widely, but they average around 5 percent. After SkimLinks cut, that'd be 3.75 percent (although SkimLinks says they can sometimes negotiate deals that would keep the percentage closer to the original number).

So, Pinterest has 10 million users. Let's say that the average across all of them is that they buy items valued at $10 in a month through affiliate links on Pinterest. That's $100,000,000 of sales for which Pinterest would get credit. That's $3.75 million in monthly revenue, or $45 million of annual revenue.

Is that going to make you the next Facebook? It doesn't look like it when your user base is 10 million. But what about when the site has 100 million users? Assuming revenue scales linearly,affiliate revenue would stand at $450 million. And if the site had 800 million users like Facebook? That revenue would go to $3.6 billion, just $100 million less than Facebook's 2011 haul.

These numbers are far from exact, but they aren't totally out there, either. The key to this model here is the Superman III principle: they are making pennies on a retail shopping market that is truly gigantic, and they are taking their cut from the top-line. Forrester estimates that the online retail market, in the US alone, will total $279 billion in 2015.

And really, what a win for everyone. Users get a great service and don't have to look at advertising. Retailers get a new outlet for marketing. Pinterest connects all these buyers and sellers.

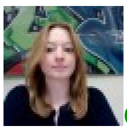
I don't know Pinterest's financials, but I can't think of a time when a company has run harder away from what seems like a good business model that I don't think its users would object to.

What I think is going on here is that Pinterest's backers don't want the company's revenue engine (i.e. SkimLinks) to be located outside the company. Because while there's no doubt Pinterest is a viral product, the actual IP for generating data and affiliate income was located in Navarro's, not Silberman's.

Document 3:

Taylor, Colleen. "For Pinterest, Revenue Will Turn Copyright Questions Into Real Problems." *TechCrunch*. 22 Mar. 2012. Web. 26 Mar. 2012. <http://techcrunch.com/2012/03/22/for-pinterest-revenue-will-turn-copyright-questions-into-problems/>.

For Pinterest, Revenue Will Turn Copyright Questions Into Real Problems


COLLEEN TAYLOR

Thursday, March 22nd, 2012

It's a bit surprising to hear Jonathan Klein talk about photo sharing on the Internet. As co-founder and CEO of stock photo agency **Getty Images**, he is focused on protecting the photographs that belong to his company — and making sure that Getty and its affiliated photographers get paid.

But he hasn't eliminated the ability to right-click on a Getty photo and save it to your computer. Anyone with the most basic of Photoshop skills could easily get rid of the Getty watermark within minutes. That's because he's not concerned about people playing with Getty photos, teenagers using them for school projects, and folks putting them up on their personal blogs — or, at the moment, even**Pinterest**.

So when *does* Getty snap into action? The moment that a website starts running ads alongside those images. As Klein told me in the interview embedded above:

"We're comfortable with people using our images to build traffic. The point in time when they have a business model, they have to have some sort of license."

That is why Pinterest has a big problem on its hands at the moment. The site has certainly **built immense traffic** by allowing people to share and collect as many photos as they want — many of which **inevitably don't belong to them**, in the legal sense. And as Fortune's Jessi Hempel reported**today**, each week the site has to write a big check to keep its servers running to handle its ever-increasing visitor load. This, of course, means that making its own money is an increasingly big priority for Pinterest — and the company has **just hired** Tim Kendall, a big-name monetization executive, to that end.

But: The second that Pinterest starts making money of its own, intellectual property owners such as Getty Images will have the right to ask that Pinterest pay up — or start deleting pinboards.

It's not a completely unprecedented problem, but it is a very expensive one. Some people say it's why Tumblr has still **not started** to make real money yet. It took YouTube years to **even come close** to making self-sustaining revenue — and that is in the arms of a ridiculously profitable parent company, Google. When you are a popular online repository for user-generated content, policing what media belongs to whom can literally be a full-time job for entire teams of people. That does not come cheap.

And, perhaps most importantly, your users really don't like it when you take down the content they've shared. Pinterest has built up a ton of goodwill with its community, but nowadays on the web even the most enthusiastic of users can be **very fickle**.

Now, this is certainly a problem that Pinterest is aware of. And with **$37.5 million in funding** from some of the Valley's savviest investors, they are no doubt working on a smart solution. If they come up with one, it will be great news for Pinterest and scores of other innovative sharing-based web companies that would be born in its wake. But for right now, all those question marks surrounding Pinterest's copyright situation are poised to turn into very big problems — once dollar signs enter the equation.

Document 4:

Blodget, Henry. "Okay, Google, It's Time To Suck It Up And Buy Pinterest For $2 Billion."*Business Insider*. 8 Mar. 2012. Web. 26 Mar. 2012. <http://www.businessinsider.com/google-buy-pinterest-2012-3>.

Okay, Google, It's Time To Suck It Up And Buy Pinterest For $2 Billion

Henry Blodget | Mar. 8, 2012, 12:54 PM | 13,820 | 33

At a conference recently, an industry guru made an impassioned argument that Google should immediately buy Pinterest, the photo-pinning social site that has taken the world by storm.

The argument was persuasive.

Here, in a nutshell, are the guru's key points:

- **Google sucks at social and will always suck at social.** Despite its humongous user numbers, the guru says, Google + is a bomb. It's a bomb because, once again, Google is playing catch-up and because Google just doesn't know how to build good social products.

- **Wayne Gretsky's famous secret to success in hockey was to skate to where the puck is *going*, not where it is, and Google is skating to where the puck is.** Facebook has the puck, the guru says, and there's no way Google will catch up if it keeps chasing Facebook. Google needs to skate to where the puck is going.

- **Pinterest is where the puck is going, because web navigation is shifting from search to social and from "streams" towards "grids."** As Pinterest's success demonstrates, the guru argues, the web is becoming more and more of a visual medium. In this new web, users prefer to browse content and follow each other in visually-appealing "grids," rather than chronological streams. Google + is following the tired "streams" convention, the guru says. Meanwhile, the puck is headed toward "grids." [I don't agree with the guru that "grids" will entirely displace "streams"--sometimes chronology is helpful--but I think I certainly think you'll see a lot more grids.]

- **One of the few home-run acquisitions Google has ever made is YouTube--and that's because Google acted aggressively and boldly to buy it early and then didn't screw it up.** Google, you will recall, bought YouTube for $1.7 billion back in 2006. This acquisition was ridiculed at the time--by smug pundits who didn't realize that $1.7 billion was chump-change to Google and that a site with an opportunity as big as YouTube's was worth making a big bet on. The YouTube acquisition is not ridiculed anymore.

- **Google will be able to marry its amazing algorithmic revenue engine--one of Google's core strengths--to Pinterest's new social distribution engine**. For some forms of content and commerce, "social" is becoming a critical distribution channel. Sites that once optimized for search are now optimizing for social. This trend hurts Google, which is still completely dependent on search. Google hopes to forestall this trend by making search more social, but it's still playing defense, not offense. To play offense, the guru argues, Google needs to embrace the *next* form of social--and then combine it with its existing revenue engine. (Pinterest is already making money using links, which are close to Google's AdWords product).

- **Google can afford to write a check for whatever it takes.** No, Pinterest is not "for sale." But everything's for sale at the right price. And Google has the resources to pay that price.

  The guru added that Google would have to go out of its way to make sure that it doesn't wreck Pinterest the moment it buys it, the way it has so many other acquisitions.

  The secret to Google's not wrecking Pinterest, the guru said, is for Google to leave it alone.

  Larry Page would personally have to commit to Ben Silbermann and the rest of Pinterest's leadership that Pinterest would be free to do its own thing without being assimilated into the Google Borg. Page's pitch could be that Google could handle monetization while Pinterest focused on the product and audience.
  But would Pinterest ever sell to Google?

  Pinterest is not for sale and probably has no intention of selling. But just about everything is for sale at the right price.

  And, in recent weeks, a threat to Pinterest's future has appeared that might well make Pinterest more likely to sell than it otherwise would have been:

  The threat of copyright theft.

  Pinterest allows users to "pin" photos from other sites to personal pinboards.

  Another way of saying this is that Pinterest allows users to easily steal and display photos.

Pinterest's Terms of Use prohibit users from posting photos they don't have rights to, but just as YouTube used to be a garden of stolen videos, Pinterest probably has many more copyrighted photos posted on the site than it would ever be able to police.

(Some observers argue that Pinterest's pin boards constitute "fair use" of photos, but if Pinterest were really confident about that, it probably wouldn't have made posting copyrighted photos against its terms of service. And lawyers wouldn't be fleeing Pinterest in fear of being sued.)

In other words, Pinterest may have a huge, looming legal problem, one that will only grow bigger as the company gets more successful.

The story behind YouTube's decision to sell to Google at such an early stage of development is that three factors played a role:

- The looming legal threat to YouTube
- The rapidly increasing costs of storage and streaming as the site's growth exploded
- The vast check that Google was willing to write

By selling to Google, YouTube's founders and investors neutralized these risks and cashed in. They might have made less than they otherwise would have gotten if they had developed YouTube into a huge, successful standalone site, but they also removed the risk that they would be sued into oblivion--the way, say, Napster was.
Pinterest's situation is not directly analogous to YouTube's, but it has some elements in common.

Specifically, Pinterest has potential large and looming legal risks. And Google has the ability to write an absolutely humongous check to induce the founders and investors to take these risks off the table.

How much would Google have to pay to get Pinterest to sell?

Right now, it would probably take $2 billion.

$2 billion is chump change to Google, which has $45 billion in the bank. If Pinterest implodes and the $2 billion goes "poof," Google and its shareholders will barely notice. Google's vast wealth would make the Pinterest gamble a much smaller risk for Google than it might seem. Google earns $2 billion every couple of months.

To Pinterest and its investors, meanwhile, $2 billion is a lot of money.

Pinterest, after all, is less than two years old.

And $2 billion for a year and a half of work is pretty fair compensation.

Yes, if they sold to Google, Pinterest's founders and investors would have to give up a dream of building a company worth tens or hundreds of billions of dollars.

But they would also eliminate the risk that Pinterest might end up being worth nothing.

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