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On the responsibility of experience economy: what's wrong with that Prezi is not a cure for cancer?

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This paper discusses on what the role of the experience economy would be, especially the social media and mobile applications' development in a second dot-com bubble formation. The incredible expansion of experience economy causes obvious distortions in the evaluation of the companies and it may have other effects on labour and investment markets. We also looked for answers how the government of a small and closed economy as in Hungary could steer the process towards a sustainable innovation ecosystem.

Keywords: experience economy, dot-com bubble, company valuation, investment market

1. Introduction

The customer behaviour in the society was acknowledged by several authors. Toffler (1971) has already spoken about the upcoming „experiental industry" in which the people would be willing to allocate high percentage of their incomes to live amazing experiences. Hoolbrok and Hirschmann (1982) discussed first the experiential aspects of consumption describing the amusement linked to services. A decade later, Schulze (1992) raised the idea of the „experience society" in which people changes focus from external to internal consumption. The term „experience economy" was introduced by Pine and Gilmore (1999) as the identification tag of the next economy following the most recent service economy. They argued memorable moments (the experience) of the consumption became the product itself and experience business charges for the feeling customers get by engaging it.

By the spread of the Internet and smartphones, social media has become the largest segment of experience economy, creating incredible size of populations as users' communities. As it is shown in the Table 1, if the Facebook was a country, it would have the second-highest population between China and India. Moreover, there are only four geographically determined populations among TOP10; all the rest belongs to social media users.

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The rise of web-mobile experience economy has rearranged the recruiting arena. In start-up land the social media and mobile application developer companies seem to be winning the recruiting race, and while the traditional complaint of top quality schools has been that the best talented guys go to Wall Street, a new one is developing: why do these smart, well-trained youngsters, who could help cure cancer want to work for a web-mobile amusement business?

Table 1. TOP10 populations in the world

Rank	Population	Size (million)
1.	China	1385
2.	Facebook	1280
3.	India	1211
4.	WhatsApp	450
5.	USA	315
6.	Tencent	300
7.	Google+	300
8.	LinkedIn	300
9.	Twitter	255
10.	Indonesia	251

Sources: Countries: http://worldpopulationreview.com/countries
Social media: http://expandedramblings.com/index.php/resource-how-many-people-use-the-top-social-media/#.U378MtxVhbU

As Edwards (2013) has recently pointed out, due to the extraordinary growth of web-mobile experience economy, technology market is in a bubble. Deal prices are unjustifiably high and revenues do not confirm the billion dollar valuations. Such overvaluation of social media can be demonstrated by the comparison of two recent transactions: Novartis and GlaxoSmithKline, two of the world's top drug makers reshaped their businesses by trading assets to each other in April, 2014. As a part of this deal, Novartis bought GSK's complete oncology portfolio (17 new drug candidates in 26 indications) for USD 14.5 billion plus another USD 1.5 billion that depends on the results of a trial in melanoma. Two months earlier Facebook acquired the most popular mobile messaging WhatsApp for USD 19.0 billion (grabbing it from Google who has also made an offer of USD 10 billion). WhatsApp deal is worth more than what Facebook raised in its own IPO in 2012. It is larger than any that Google, Microsoft or Apple has ever done. Considering the biggest challenges for mankind to survive, how can it be explained to the society that a free instant messenger is worth 30% more than 17 promising cancer drugs on clinical trial?

Looking at the long-term effect of the transaction above, we can conclude it contradicts with two elements of the recently spread Responsible Innovation (RI) concept: sustainability and social desirability (von Schomberg 2013). Notwithstanding both dimensions can only be evaluated in the longer term, it can easily be recognized that this exceptional growth of the experience-based market cannot be sustainable. Due to the very low interest rates (around zero) in global banking, savings are diminished and people favourably invest their money into fast growing businesses such as web-mobile experience economy, expanding the bubble. The other factor, social desirability shall be evaluated in terms of intergenerational context: the responsibility to ensure our quality of life does not compromise the chance for future generations to enjoy a comparable quality of life. This means if the very quickly inflating web-mobile experience economy diverts disproportionate resources from developments with high impact on the future of society, future generations will have less new healthcare and environmental invention with lack of chance to sustain the quality of life.

2. Results and discussion

In order to get better insight into the consequences of web-mobile business to the global economy, we examined five hypothetic statements in detail.

2.1. The market for overvalued companies has been created, which threatens with a second dot-com bubble[2]

Although the Facebook-WhatsApp deal in term of amount is totally unique, it is not a one-off case to pay USD 1 billion or more for a company without profit in experience economy. Table 2 shows some famous recent deals in web-mobile sector. Among the cases presented, the most interesting is the acquisition of Viber (which provides, similarly to WhatsApp, free messaging and – in addition – VoIP services) by Rakuten, a Japanese e-commerce platform. The deal was announced only one week after Facebook-WhatsApp acquisition was disclosed, and Facebook could have acquired Viber twenty-one times from the money spent on WhatsApp. Since

[2] Dot-com bubble is a period covering roughly 1997 – 2001. In the bloating part, millions of companies (with “e-“prefix or“.com” at the end) in the Internet business were founded and got their stock prizes seriously increased without return. The promises of future profits, stock speculations and unreal valuations by venture capital funds feed the fire of bubble. The collapse occurred during 1999 – 2001. Many companies failed completely, others lost large portion of their market value. One of the most famous examples is Broadcast.com, which was acquired by Yahoo! for USD 5.9 billion. The site no longer exists and redirects to Yahoo!’s home page.

both acquired are without profit, services are similar and Viber has advanced service by the free VoIP call, there must be some non-obvious reasons behind the deal. First should be, which is not unique at all, that WhatsApp has been growing at an incredible rate, doubling its users every year and now it has more than 450 million active users. It can be said, Facebook purchased those extremely large number of users at USD 42.22 each.[3] Second, as Gans (2014) pointed out, is the strategic compatibility. Facebook is known as a trusted social media, which means that connections between individuals are by mutual assent. Its principal pursuit is to give a tool to "stay in touch" with network members instead of "get in touch". WhatsApp is the most compatible messaging platform to this philosophy of trusted communications. In order to last relationship and avoid spams and unrequested messages, WhatsApp also grants access to people you trust. Gans (2014) suspected "there was a meeting of the minds that led to this merger".

Table 2. Some acquisitions of companies in web-mobile sector

Acquired company	Acquirer	Acquisition date	Price (million USD)
YouTube	Google	2006	1.650
Tumblr	Yahoo	2013	1.100
Instagram	Facebook	2012	1.000
Viber	Rakuten	2014	900
Sold.	Dropbox	2013	200

Source: Edited by the author

When we examine the recent acquisitions and investments, we may find three types of hardly justifiable overvaluations (Edwards 2013):

Companies with broken business models raise new investments

Typical example of this category is Fab.com. In December 2010, Fabulis.com, a social network for gay men turned into Fab.com, a flash sales site. Fab's CEO, Jason Goldberg being inspired by social networks thought he could create a new service for the gay community by Fabulis. But the growth of the daily deals business convinced him to turn the ship in another direction and create a Groupon[4]-like platform

[3] As Krantz (2014) has recently concluded "compared to the USD 141 per user valuation at Facebook, WhatsApp was cheap. In fact, the valuation paid for WhatsApp is lower than the per-user price on most other Internet darlings. Investors are paying $85 per user at professional networking firm LinkedIn, $52 per user at review site Yelp and $125 per user of online messaging service Twitter."

[4] Groupon (group coupon) is offering daily deals at restaurants, cinemas, sport events, retailers and many more service providers. It was launched in November 2008 in Chicago.

for gays. Just four months later the next pivot was done: the Fab.com became a top destination for quality-designed products at below retails prices. Notwithstanding the second pivot and the completely different challenges facing the staff with the movement from a gay-focused portal to a designed-by-customer site, Fab.com could recently raise USD 165 million in new investment last year. Goldberg was able to accomplish this even though 440 people were laid off at the last pivot.

Companies valued higher than their revenues justify

There are many well-known examples of this category. In January 2014, cloud storage and sync provider Dropbox raised about USD 250 million at an estimated company value of USD 10 billion. Dropbox revenue for 2013 was USD 800 million. Pinterest, the largest social bookmarking site where users collect and share photos of their favourite events, interests and hobbies recently raised USD 225 million in a new investment round, at a company value of USD 3.8 billion. Its revenue is estimated as a couple of 10 million in USD.

Both fictional valuations would only be based on the notion that the company could be sold or go public at that price. This trend can be observed in almost all social network companies operating with freemium (free + premium) business model. Valuations are not based on justifiable returns, but on the foretold price at next round of investment or IPO. This process results in the continuous growth of the bubble, because even the extremely huge number of early users (using the service free) does not guarantee that premium level accounts will bring the predicted revenue. But it should be finished once and if the company is unable to generate enough revenue at the end, the last investor or the owners of the shares will lose the incredible amount of money representing the distance between the real and inflated values of such companies.

Companies with no revenue at all are ridiculously valued

The most extreme example is that of Snapchat in this category. Snapchat is a self-distracting photo messaging application in which users can take photos, record videos, add text and drawings, and send them to a controlled list of recipients who can view them for a couple of seconds (adjustable limit is 10 seconds now) only. After that they will delete themselves from the recipient's device and from Snapchat's servers. Snapchat has no revenue at all, and it is hard to imagine how money can be made with a service without preserve imprint of transferred pieces.

In spite of that, Snapchat shocked the tech community late last year when it turned down a USD 3 billion acquisition offer in cash from Facebook. Many people even suspected that the founders went out of their minds, just a better offer was expected which would provide long-term gains for Spiegel and Murphy. Not much later Chinese e-commerce giant Tencent Holdings offered to lead an investment that would value the two-year-old Snapchat at USD 4 billion.

Snapchat and Tencent have perfect synergy. The Chinese company runs sort of messaging mobile applications in Asia with over 800 million active users. Tencent could also provide Snapchat with a path into China, where most US-based social media and mobile application companies have struggled in the face of competing native service-providers and strict government regulations.

2.2. Entrepreneurial frenzy overwhelms the web-mobile experience economy

The deals listed above with unrealistic valuation reinvigorated the web-mobile experience economy. New mobile applications developing companies were formed one after another to see if they will be the next acquisition targets of Google or Facebook. According to freemium model operation, users began to gather to demonstrate the viability of their business model.

However, as the recently published Quantcast (2014) report – based on web traffic data from the more than 100 million sites Quantcast monitors – shows, the explosion in the market for mobile applications is an illusion. Of the one million mobile applications for sale on both Android and iOS, Quantcast found that only 1.000 of them (just one per thousand) have more than 50.000 users, which can be considered as the minimum barrier to enter this market. According to Quantcast, 83 percent of people use less than 10 applications regularly. Accordingly it can be said the market for mobile applications is a small group of social media tools and shopping applications that we use frequently, surrounded by a shoreless ocean of trash we never get to.

2.3. Unrealistic compensation packages rearrange the labour market

Unreal company values resulted in expensive wages also. Unemployment rate in the tech sector is very low; the leading companies recruit the probably best and surely best-paid-ever key employees. As Edwards (2013) referred, Vice President of Engineering at Twitter, Chris Fry is paid more than the chairman of the company's board. Mike Schroepfer, who is in the same position at Facebook as Fry, got USD 24.4 million in shares when he joined. Start-up companies used to offer extravagant cars to lease for the coveted key employees and sign-on bonuses for creative dropouts.

The flow-chart on Figure 1 demonstrates how the absurd compensation packages resulting from the unrealistic company valuation can rearrange the labour markets.

Labour market rearranges first the vicinity of the company, because by the higher packages offered, overvalued companies drain the skilled manpower from competitors. The growth obtained from the acquired highly qualified labour force leads to two parallel processes. First, the attractive compensation packages discussed above serve as magnet to the relevant professionals working in other parts of the world and begin a flow of highly skilled labour force to the power centres of experience economy from around the world.

On the other hand, successful companies are starting the global expansion and their subsidiaries with the help of extreme compensation packages attract the local champions, rearranging thereby the labour market in the vicinity of the subsidiaries. For instance, at the Hungarian affiliation of the word leading presentation software developer, Prezi.com the newcomers' salaries are the industry average supplemented by free lunch and beverage consumption and in-house entertainments (e.g. game room).

Figure 1. Consequences of company valuation to the labour markets

Source: Edited by the author

2.4. Investors turn to the experience economy because of the lower risk and higher return

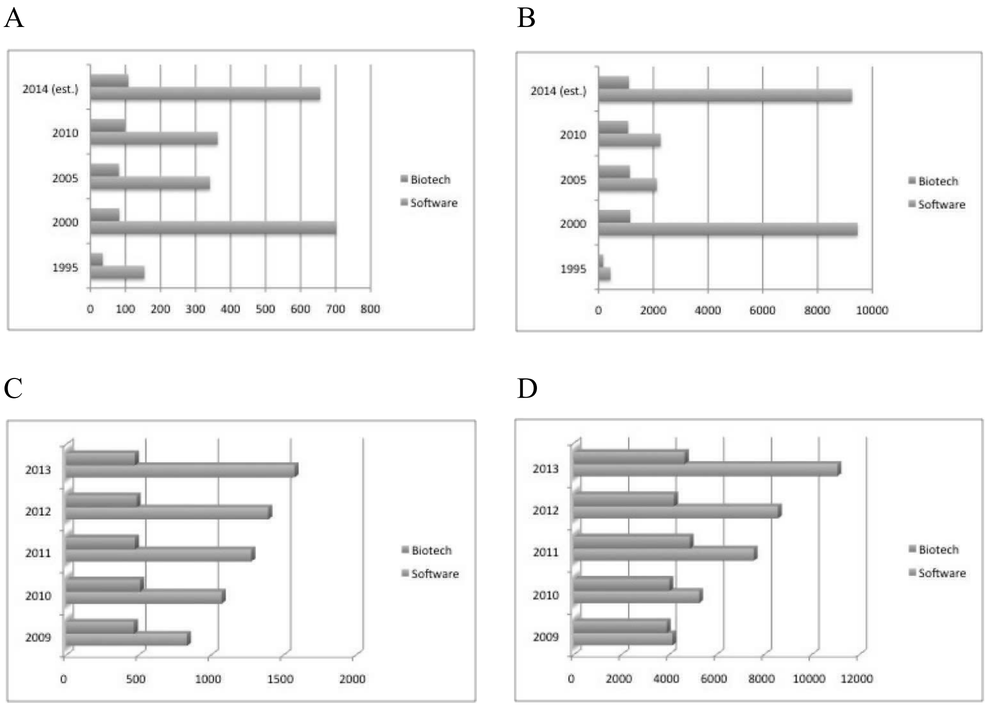
When looking at U.S. investment processes taking place in the technology regions (Figure 2), we see the following. In Silicon Valley, which has in terms of processes always been an indicator, number and volume of IT investments has reached again the state before the dotcom bubble burst.

While investment numbers of IT (and mainly web-mobile experience economy within) clearly increased, number of transactions for biotech industry slightly grew and value of the deals actually stagnated.

Considering the data were aggregated for all remarkable technology regions of the U.S., we find both number and value of investments in software industry has grown steadily over the past five years. In contrast, the biotech industry has had no significant change during this period in either term.

We can conclude that the increment of investments in U.S. high-tech industry experienced in the past years was mainly fed by the software industry and the experience economic actors within. Investors clearly prefer lower risks and their higher returns would result in unrealistic valuations discussed above. Accordingly, the biotech-healthcare sector did not get from the increment of investments experienced in recent years.

Figure 2. Number of investment in biotech and software industry (A, C) and transaction values in M USD (B, D) in the Silicon Valley from 1995 to now (A, B) and in the all major technology region of USA between 2009-2013 altogether (C, D)



Source: MoneyTree (2014)

2.5. Governments do not deliberately intervene

The economic development of a start-up ecosystem is often compared to Silicon Valley history. However, it can not be forgotten that the current situation emerged as a result of a fifty-year-long around organic development. Those were not sounding government objectives at the beginning and even later only limited state interventions were observed. In the development of Silicon Valley, U.S. military played an irreplaceable role behaving as generous "investor”: it financed the research project with huge money without claiming returns or shares of the emerging enterprises.

The emerging start-up ecosystem was stabilized by the two factors below:

- "The visible hand of capital" when it comes to venture capital funds such as Kleiner-Perkins, Sequoia and Mayfield moved from San Francisco to Menlo Park between 1972 and 1974.
- "The invisible hand of government" when the Revenue Act lowering the capital gains tax was ratified in 1978.

Besides the above there is one more important thing that many times we tend to stack up: cultural diversity also helped the emergence of Silicon Valley, because of the impact of immigrants' cultures and ideas on one another. As Wadhwa et al. (2007) pointed out, they acted as stimuli to creativity, because 52% of start-up founders in the USA were immigrants, and that immigrant-founded companies created over 450,000 jobs in 2005 only.

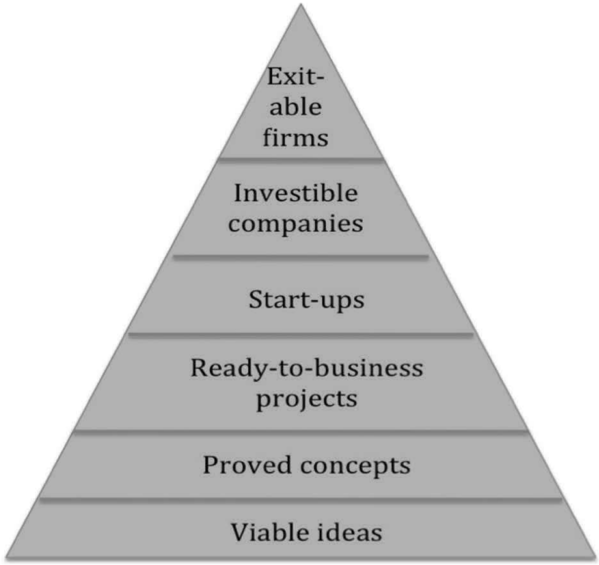
In Hungary the government has recently shown a clear interest in the start-up ecosystem. The Hungarian decision-makers have a clear objective: "... the vision that the Hungarian capital in a decade become a Central and Eastern European hub for start-ups" (Runway Budapest 2014). Let's examine how the government measures serve this purpose!

The pyramid of acceleration in Figure 3 reflects the relative proportion of survivors in each phase from concepts to the established companies with exit. In a well-functioning ecosystem, proportion of different financial instruments fits the ratio of firms in different acceleration stages. If government intervention takes place in an emerging ecosystem, it is advisable to provide the appropriate financing instruments can be derived from the proportion of companies at different stages.

In Hungary financing instruments matching with the pyramid above show a varied picture. Proof-of-concept and pre-seed funds are missing completely in the country, so this area could have obviously been the area for government intervention. However, despite the fact that the Hungarian government assisted the creation of venture capital funds with 130 billion HUF about through the EU-funded JEREMIE (Joint European Resources for Micro to Medium Enterprises) financial asset in the last 5 years, the very early-stage funds above were not among them, so this financing segment is still missing.

The situation is not much better either with seed funding. Although in the second round of the JEREMIE program above four seed funds were supported, it is only a small and pretty late step in start-up investment. The stance is similarly poor for incubator market. Under the recently launched „gazelle" scheme four accredited incubators were launched this year. Considering that the first set of JEREMIE-assisted growth funds was formed in 2010, the seed funds and incubators should have been established a few years earlier. Due to the lack of previous funding instruments, the 24 working growth funds can not find enough suitable projects and thus a considerable proportion of their capital – despite the impending deadline of December 2015 – has not yet been invested.

Figure 3. The pyramid of acceleration



Source: Edited by the author

3. Conclusions

Based on the observations, the start-up ecosystem has already been distorted even in the advanced economies. Investors have intensified the processes resulting in that the actors in experience economy (especially the web-mobile solutions' owners) are dominant among start-ups. In accordance, the biotechnology, pharmaceutical developments, human healthcare- and environmental technologies, which seek to address the most pressing problems of mankind, are overshadowed.

In a healthy functioning economy social media, mobile applications and the other elements of experience economy obviously have effective and important role. But when the enterprises behind these solutions utilizing lower risk and unrealistic recovery options drain the human and financial capital from development areas to ensure our sustainability, the question arises that there would be a need for incentives that will restore investor- and entrepreneurial attraction for healthcare and environmental businesses within a certain time limit.

If we do not find effective solution, mankind will soon be in big trouble, because the products of experience economy are entertaining, joyful and sometimes practical, but the least of the cancer patients' problems, which one to use editing presentations or sharing photos with friends.

In this progress, the responsibility of government is enormous. Instead of enjoying the quickly-came success of experience economy, they should set back the reasonable weight of healthcare- and environmental industry through appropriate incentives and awareness raising, lest the hype about experience economy results in a multi-decade setback of developments and it is too late...

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