Business Model Prospects: A requisite for the firms

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Introduction

Business Model has become the keywords in the organisations today which inspires them to innovate their existing model or build another model to aim for higher profits. It will be wrong to say that company just need a well web-based business model to get enormous profits as the factors like strategy, technological advancement and value for customers also plays a vibrant role in the growth of the company (Magretta, 2002). A business model provides the information and evidence that how a company creates value for its customers, delivers value to them, outlines the structure of inflow and outflow of revenues within the organisation and also profits associated with the business (Teece, 2009). As the concept of the business model is losing its fame just like .com appendage itself (Magretta, 2002), it is significant to realise that the core of the business model lies in the fundamental question that how a business can build a sustainable competitive advantage to make supernormal profits (Teece, 2009).

A study reveals that 7 out of 10 enterprises are involving themselves in business model innovation and 98% are modifying their existing business model to some extent (Ramon Casadesus Masanell, 2011). PwC's survey shows that 54% of the CEOs in the world are concerned about the new competitors entering their market, and also a similar number revealed that they either have started competing in the non-traditional market by themselves or have considered doing that (Clayton M. Christensen, 2016). Also, the Boston Consulting Group says in the reports that 94% of the 1,500 senior executives of the companies have engaged business model innovation to an extent (Zhenya Lindgardt, 2014). All these recent attempts at business model innovation show that the companies are trying their best to develop a successful business model to assure competitive advantage. However, imitation is easy, but it is hard to differentiate business model in the market to yield profits as the success is essentially random. For instance, Google saw an opportunity of adding Google+ into their existing products and business wherein they saw the integration of information from the social network users in a way to generate improved and personalised search results. Google's business model was that the social network allows the company to generate revenues and profitability by targeting and delivering advertisements through increased usage of its product platform, but customers did not found value from the combination of search and social networking (Clayton M. Christensen, 2016). Google's social network business model failed to attract the customers and gain momentum in the market but maintains its search business exceptionally (Eadicicco, 2015). On the contrary, Daimler recognised that car2go was a different business and started as an experiment by employees working in Ulm Germany which was far from its existing home office. Car2go design from the beginning is to fulfil Daimler's major job of providing mobility but without convincing customers to purchase the vehicle (Clayton M. Christensen, 2016). Even though car2go uses the Daimler's ownership by using the resources wherever necessary, but car2go is making profits by renting the Smart Fortwo cars on a per-minute basis by charging 38 cents per minute, and above that $35 registration fee (Gerstner, 2014).

By looking at these examples, it is clear that to achieve successful business model it is useful to create new business models rather than changing existing ones. However, Business Model is essential to every successful organisation whether it is a new venture or an established player (Magretta, 2002). Business Model Innovation can be a way to achieve competitive advantage if the model is difficult to replicate for incumbents and new entrants (Teece, 2009). There are instances where flawed business model have raised many funds, but the fault lies with its misrepresentation and misuse but not with the concept of the business model (Magretta, 2002).

What is a Business Model exactly?

It is imperative to understand Business model as it is crucial in capturing value for customers and everyone agrees that executives must know how the business model works if his or her organisation is adopting it, but then also there is little agreement on an operating definition as various people have various perspectives on it.

Henry Chesbrough and Richard S. Rosenbloom has offered a more comprehensive and operational, definition by giving the functions of the business model in an organisation (Henry Chesbrough, 2002),

- Value Proposition – The coherent value created for the users of the business model by the offerings based on the innovation in the new or existing business.
- Market Segmentation – Business model segments the market based on the purpose and usage of the technology by the customers and also specifies the revenue generation mechanism for the firm.

- Value Chain – It defines the structure of the value chain in the organisation which is required to generate and allocate the offerings and decides the assets needed to support the firm's place in the value chain.
- Cost and Profit Estimation – It evaluates the structure of cost and the potential profits of the production of the offerings.
- Positioning within Network – Business Model describes the position of the firm within the value network and identifies the possible complements and competitors.
- Competitive Advantage – It formulates the competitive strategy for the company by innovation which differentiates them over their rivals.

According to (Chatterjee, 2013), Business Models are categorised by Efficiency based, Perceived Value based and Network Value based as they are driven,

- Efficiency based – Efficiency based models depend on a human resource or capital resource to produce commodities wherein these type of business are price takers in the highly competitive market.
- Perceived Value based – The logic of this model is to position its output as a want and demand for a premium price. The value behind the "want" and be objective (drug or medical devices) or subjective/perceived (movies, music, video games, organic food and cosmetics).
- Network Value based – Value based models depend upon the loyal group of customers wherein the customers become the ambassadors that keep the network stable. For example, Microsoft's customer valued standalone desktop, and Netflix's subscribers valued movie rentals in their mailbox.

According to Joan Magretta, the Business model is defined as, "the story that explains that how the enterprise works (Magretta, 2002)." Also, A good business model recalls the Peter Drucker theory which describes it as the answers to the question: Who is the customer, what does the client's value and how to deliver that value at an appropriate cost (Magretta, 2002).

If we talk of Business Model in its simplest form then, A business model comprises of administrative choices and the consequences of those choices made by the companies which further generates virtuous cycle (**Figure 1: Virtuous Cycle of Ryanair**) that constantly reinforce the Business Model by creating dynamic network effects (Ramon Casadesus Masanell, 2011).

There are three main types of choices which the companies make while creating business models, i.e., Policy Choices, Asset Choices and Governance Choices.

- Policy Choices – administers the actions the firm takes across all its operations
- Asset Choices – relates to the physical resources a company deploys
- Governance Choices – refers to how a company poses decision-making rights over the other two choices

There are two types of consequences i.e. Flexible and Rigid

- Flexible Consequences – is the one that reacts rapidly with the change in choices
- Rigid Consequences – is the one which is difficult to emulate as company needs time

Let us understand Choices and Consequences with an example,

Ryanair moved from traditional business model to a low-cost airline in the early 1990's and eradicated all trappings by cutting the costs to the prices never heard of (Ramon Casadesus Masanell, 2011). The Choices company made as a strategy was low fares, flying out of the secondary airport, no separate class of passengers, charging for any additional service, no serving of meals in flight and short-haul trips (Carlos M. DaSilva, 2014) (Ramon Casadesus Masanell, 2011). It also made choice of utilising regular flights of Boeing 737, using non-unionised workforce, offering higher incentives to employees and operating out of a lean headquarters. The Consequences of those choices were a large volume of travellers, low variable and fixed costs, lowest air tariff charges and an aggressive management team (Ramon Casadesus Masanell, 2011) (Carlos M. DaSilva, 2014).

Figure 1: Virtuous Cycle of Ryanair

Characteristics of a Good business Model

When we talk about the business model, it is important to know that the business model is effective regarding an application in the company or not. According to (Ramon Casadesus Masanell, 2011), an excellent business model has the following characteristics,

- Alignment with the firm's goals – It is critical to design a business model where the choices should provide the consequences which are aligned with the company's goal. For example, Xerox set up Xerox PARC in the 1970's which laid technological innovations such as laser printing technology, the GUI and large scale integration of semiconductors. However, Xerox PARC was unsuccessful in laying the foundation for such new businesses and capturing value for its innovation due to the lack of alignment of the parent company's (Xerox's) goals (Henry Chesbrough, 2002) (Ramon Casadesus Masanell, 2011).
- Self-reinforcing – The choices made while developing a business model should complement the company's internal policies persistently. For example, if Ryanair a low-cost airline decides to provide a comfort in flight by reducing the number of seats and offering food and coffee, then these choices will destabilise the air carrier's low-cost structure and ruin its profits.
- Robust nature – An ideal business model should be able to sustain in the market and have an impact on customers for a longer time by resisting the threats identified by Pankaj Ghemawat (Jones, 2015).
  - Imitation – how simply and rapidly your business model can be copied?
  - Holdup – Can customers, suppliers and other players take over your value by their bargaining power?
  - Slack – Does the organisation care enough or work hard enough?
  - Substitution – Do the other product or services in the market can destroy the value of your product or services?
- Virtuous cycle – Successful business model produce a virtuous cycle that strengthens the business model by the network effects or feedback loops that are self-reinforcing. For example – Hightech companies such as Apple, Microsoft and Intel curtails fundamentally from their accumulated assets such as an installed base of iPods, Xboxes or Personal computers (Ramon Casadesus Masanell, 2011).

Elements of a Business Model

According to (Clayton M. Christensen, 2016), A business model is made up of four interdependent elements (**Figure 2: The Elements of a Business Model**), i.e., Value Proposition, Resources, Processes and Profit Formula,

- The Value Proposition – It is for customers which we will refer to as the "job to be done".
- The Resources – this is referred to the organisational resources such as human resource, finance, technology and innovation
- The Processes – this is the sequences of tasks and activities used to transform inputs into the finished goods and services that provides an integrated and dynamic picture of organisational and managerial behaviour (Garvin, 1998)
- The Profit Formula – Referred as the margin, asset velocity and measure required to achieve an eye-catching return (Mark W. Johnson, 2008)

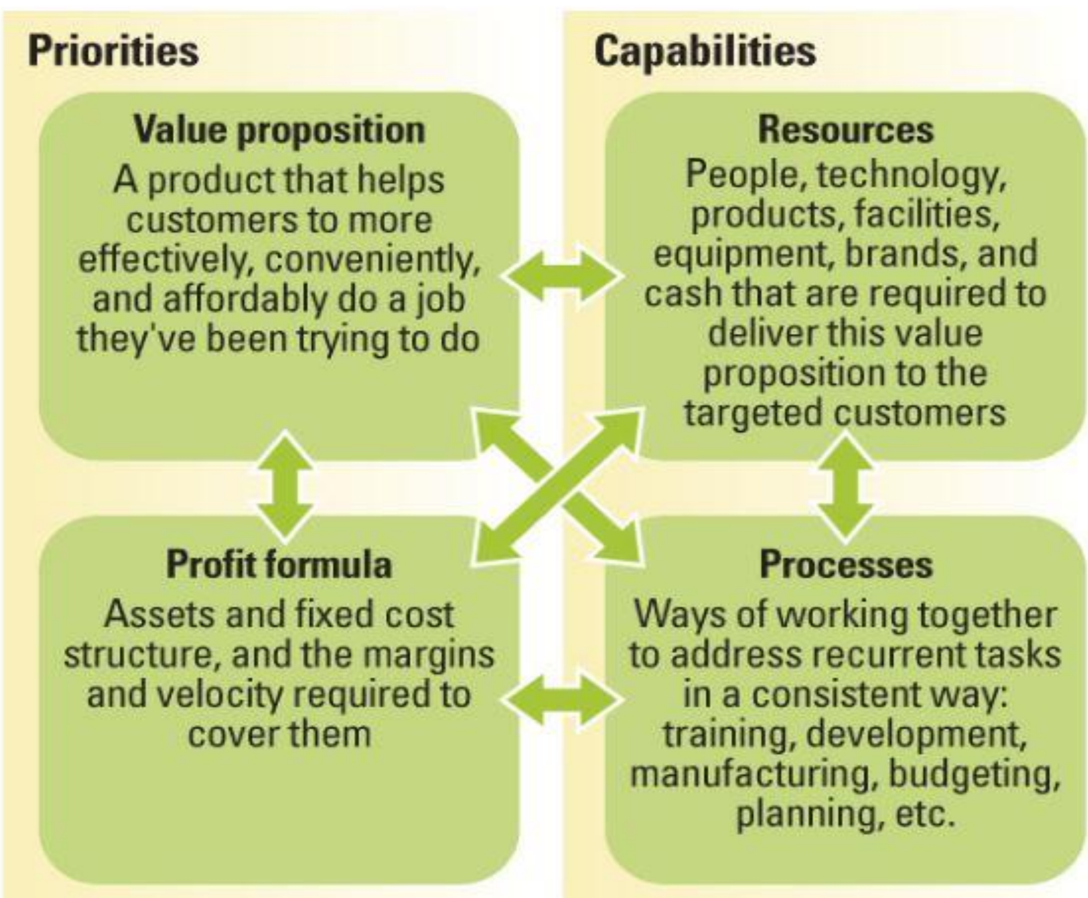

Figure 2: The Elements of a Business Model

Business Model vs. Business Strategy vs. Business Tactics

Even though the terms business model, business strategy and business tactics are used interchangeably, no three concepts can be same. If these words are used as synonyms, then it can lead to a poor decision making. Business models refer to the system where the pieces of a business fit together, but they do not influence in one of the critical aspects of performance i.e. competition (Magretta, 2002). Business Strategy refers to the provisioning of the contingencies (competitor's move or environmental shock whether it takes place or not) plan about which business model to use (Ramon Casadesus Masanell, 2011). Also, competitive strategy enlightens that how to do better or different from the rivals (Magretta, 2002). Organisations achieve superior performance when they do something unique that other business cannot duplicate (Magretta, 2002). However, every organisation does not have a strategy or a plan of action for the contingencies that may arise (Ramon Casadesus Masanell, 2011). Variation of strategic choices can be costly for the firms, but they still have a range of options to compete for that are straightforward and inexpensive to set up, and these are called Business Tactics, but the business model controls the tactics available to compete in the market (Ramon Casadesus Masanell, 2011). For example, Metro, the world's largest newspaper created an advertisement sponsored business model that says that the product and services must be free of cost and this prevents the firm from using price tactics. Now let us understand the difference and relationship between the Business Model and Business Strategy in detail,

- ***Difference between the business model and business strategy***

We have to understand the simple logic that if all the companies offer similar kind of products and services, then none of the companies will flourish and there will be one-on-one competition to gain market share which will take the prices down to points where returns are negligible (Magretta, 2002). Many young companies rushed to the market with the similar business model, but they failed as they did not have any strategies that distinguish them amongst others in the market (Magretta, 2002). The case of Walmart clearly illustrates the difference between business model and business strategy.

Arkansas, the discount retail business model, had emerged in the mid-1950's when a swing over of industry pioneers initiated to apply supermarket logic to sell the stock. Walmart came long after that in 1962 with its first store in the hamlet of Rogers when many stores were already offering lower prices than conventional stores by dropping expenses

(Magretta, 2002). Walmart took the idea of offering lower prices merchandise than competitors that was the business model, but they targetted small town and rural customers which were a different set of the market in their initial existences that were a business strategy (Richardson, 2008). Sam Walton was able to prevent competitors and dejected them from entering Walmart's territory (Magretta, 2002). Also, Walmart's value creation and delivery system were itself a strategy (Richardson, 2008). Very few like Walmart and Target have attained superior performance due to their discrete strategies and the underperformers like Kmart could not find distinctive strategies to compete (Magretta, 2002).

- ***Relationship between business model and business strategies***

To understand the connection between the business model and business strategies let us understand the story of Dell computer where unlike Sam Walton, Michael Dell was a business model pioneer. The model he generated was of selling customised computer solutions directly to the end customers at a reasonable price (Michael Morris, 2005). The elimination of the intermediaries gave the Dell the advantage to manage their inventory better than other firms in the industry (Magretta, 2002). The Dell's business model is designed for highly receptive to customers, rapid turnover of inventories, quick integration of new technologies and highly efficient procurement, manufacturing and distribution process (Michael Morris, 2005). Due to its innovative business model, Dell had consistently performed better than their rivals for more than a decade (Magretta, 2002). In the case of Dell, the business model of Dell itself operated like a strategy which made them different from others and hard to imitate. If the competitors of Dell tried to copy them, they would have damned as they would have disrupted their own distribution channels and isolated the resellers on whom they relied (Magretta, 2002). Dell was successful as they knew the clarity about their model and strategy as the fundamental business model remained the same (Magretta, 2002).

Business Model and Technology

In the age of technological era, technological development and innovation can facilitate new business models if companies understand the relationship between business model innovation and technical innovation (Charles Baden-Fuller, 2013). Various authors have a different perspective on this issue; the first say that business model and technology are interconnected, and the others say that the concept of business model and technology is different. There are researchers like (Christoph Zott, 2006) who see business model as a part of the strategy and entangled with technology where it is combined to produce an excellent effect. On the contrast, there is a researcher like (Teece, 2009) who see the business model as a separate identity from technology and strategy. To improve our understanding of business model and technology, we need to know that how innovation associates to the business model and how they interact. Also, it is important to understand how changes in business model influence technological innovation (Charles Baden-Fuller, 2013).

Technological development can facilitate new business model and also they regularly interact with each other (Charles Baden-Fuller, 2013). For example, the invention and development of steam power enabled the mass production business model. Also, if we talk about interaction, Amazon applied new technology to make a traditional business model of mail-order for delivering books in 1995. In fact, Amazon did not discover a new business model, but they applied the popular business model in the new context by applying technology and developed them (Charles Baden-Fuller, 2013). In contrast, Google's two-sided dynamic search engine was not just a technological leap, but also a business model leaps as the choices of the advertiser directly influence the search experience of users on the either side of the platform (Charles Baden-Fuller, 2013) (Tirole, 2006). The effects of business model are not different from the effects of technological innovations as both play a similar role in influencing performance (Christoph Zott, 2006). However, the business model has to change to adjust the structures of the technology that creates customer value and also that arises from the client directly (Charles Baden-Fuller, 2013).

How to know that we have a transformative business model?

The unique selling proposition of the business model is the thing that makes the firm different from the market incumbent, and also speaks of the company's platform potential which becomes dominant by leveraging a new technology which describes how a company creates and captures value for its customers (Stelios Kavadias, 2016). The features of the business models in the article define the client's value proposition and pricing mechanism (Stelios Kavadias, 2016). The industry transforms if the new entrants use the model to displace market incumbents like how Airbnb upended the hotel industry. The founders of the Airbnb realised that the new technology platform would challenge the traditional economics of the hotel business. Before the technology platform was introduced, there was no meaning to change the hotel business, but after the introduction, the dominant business model became vulnerable from anyone who could leverage that technology (Stelios Kavadias, 2016). The new business model is the interface between the wants of marketplace and fulfilment of the wants that is done by technology platform which can be analysed on six parameters given by (Stelios Kavadias, 2016). The six parameters are,

- Personalised product or service – The business model which is offered by the new entrant is better tailored to the customers individual and immediate needs.
- Closed-loop process – The trends which are booming currently in the market is of business models which are offered by the companies should have a closed loop and not direct approach.
- Asset sharing – Success as a company's innovation in the market, then it should be able to share the precious asset which is used in business. For example, Cars in Uber, homes in Airbnb.
- Usage-based pricing – It says that rather than charging customers on their buying of the products and services, charge them by usage.
- Collaborative ecosystem – New businesses are focussing on the innovation of the collaborative consumption to reduce the cost and are becoming successful.
- Agile and adaptive organisation – Innovative organisations are moving from traditional hierarchy models to real-time adaptation to changes in the decision-making process.

Conclusion and Discussion

Every company in the world that is existing or that are not existing presently had a particular business model because without business model there is no business. Even if the business model adopted by the companies were right for them or not, successful in the market or not but business models are necessary to survive in the market as it is the heart of the firm. The aim of this article is to develop a strong understanding of business model and to explore their influences on strategy, technology and decision-making process in the company. The core of the business model is that it develops customer needs and its ability to pay, and also it tempts customers to pay for the value that payment in turns becomes profits for the company in the value chain (Teece, 2009). It is essential for the existing enterprises and the new entrants in the market to understand the prospects of the business model, and also they should inculcate new technological innovations, strategies and business tactics in the model to make the value for customers higher and demanding.

Business model becomes complex due to the integration of strategy, technological competencies and process innovation in the firm (Patrick Spieth, 2014) but they also ensure that the business delivers satisfactory outputs for the customers. Equal attention must be given to designing a business model and technology as an imbalance between these can lead to a commercial failure (Teece, 2009). Even though lot of research work is done on the topic of business model by many well-known strategists such as (Chatterjee, 2013) (Henry Chesbrough, 2002) (Magretta, 2002) (Mark W. Johnson, 2008), but still business models has a potential of further research and development.

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