Towards a Theory of Business Model Innovation

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Increasing Attention to Concept: Academia

- **First appearances:**
  - in abstract: Lang (1947)
  - in subject index: Mertes (1949)
  - in article title: Jones (1960)

- **Rising interest starting with Internet boom (Ghaziani & Ventresca, 2005):**
  - 166 articles between 1975 and 1994
  - 1,563 between 1995 and 2000

- **Deeper and wider occurrences since then:**
  Evans & Wurster, 1999; Timmers, 2000; Hamel, 2000; Mahadevan, 2000; Afuah & Tucci, 2001; Amit & Zott, 2001; European Commission, 2002; Elliot, 2002; Magretta, 2002; Mansfield & Fourie, 2004 ... 

- **Special sessions and journal issues:**
  - Session in Academy of Management 2009
  - Special Issue of *Long Range Planning* on *Business Models* (Exp Feb 2010)
Increasing Diffusion of the Concept: Examples from Business & Society at Large

• Widespread belief that BMI will be responsible for significantly larger impact on firm performance than new products / services (Pohle & Chapman, 2006)

• President Obama’s and Thomas Friedman’s comments on the automobile industry needing to change business models

• Rick Gurnon, Head of the Massachusetts Maritime Academy: "The pirates have a great business model that works for them: See ships, take ransom, make millions," he told reporters.
But

• No agreement on **definition**, leading to increased confusion (incl. in academia) about the term

• Focus on **start-ups** / new technologies

• **Confusion** between **single business** and a (multi-business) **corporation**

• No mention of **people**
Business Model ≠ Business Strategy

• Traditional Business Strategy: market (who) & product (what) & value chain (how)

• Business Model: only the how!

• BM is to be distinguished from the market (who?) and product strategies (what?) - and from technology strategies

• Having defined the 3 dimensions of the Business Strategy, one can compute the profit function (or the performance model)
Business Strategy: three “gurus”

Porter (1979, 1996):
- competitive strategy: 5 forces (HBR 1979)
- choice of activities (HBR 1996 “What is strategy?”)

Prahalad (and Hamel) (1990):
- core competences

Kim & Mauborgne (2004):
- Blue Ocean Strategy: a process for new product-market spaces

Ps: none has a mention to business model the way we define it
Business Model ≠ Start-up issue

• In fact, business model innovation has been around all the time and is hardly something new: SEARS, GM, Ford, McDonalds...

• Related mostly (exclusively) with market (who?) and the product innovation (what?)

• These are business constructs that are related to “business models” - in fact many of these start-up died b/c they had no BM
An example: the downfall of GM

• 1921: Sloan buys a chaotic GM from Durant (who had established it 13 y earlier) who “had no concept of the business” and establishes the Policy Committee (PC) and establishes the multi-divisional corporation (product-process matrix: Cadillac on top, Chevrolet at bottom, ...)

• 1924: Puts division heads on the PC (shareholders like Dupont complain) to favor collaboration that was missing - he separates PC into two: Administration and (Corporate) Executive Committees

• 1946: Drucker has full access to GM and attests to the “linking” governance virtues of the two committees

• 1958: Donner dismantles Sloan’s “participative decentralization” and removes divisional managers from the main committees (unfair process dis-engagement)

• In view of resistance from divisional managers, he takes further control and makes business decisions: removes Chevrolet from low-end segment (opening up market for smaller cars), mandates increased shared parts ... 

• 1965: creates GMA(ssembly)D dismantling the Bus Units: Vega disaster (1970)
Questions for discussion?

• **Management matters:** The Policy Committee was the key linking mechanism for GM and ensured value-adding by the corporate center on top of the value adding by the BUs (an example of **synergy in corporate strategy through management** - distinct from portfolio)

• **OM cannot be seen only as writing algorithms (routines) for optimizing physical (or information) flows:** let us be careful to consider the role of management instead of trying to optimize management away

• **Are we going to leave that terrain to others?**
  - **OB** studies organizational networks and relationships at will ... but no activities in their models, only managers
  - **Strategy:** for them business model is another term for strategy ...
  - **Entrepreneurship:** mostly concerned with start-ups (cfr. Strategy)

• **What is the opportunity for OM?**
Definition #1 : Business Model

1) A configuration of activities & their (material, informational) linkages

2) A set of organizational units that perform those activities & their (managerial) relationships (including of a governance type)

In sum: supply chain with managerial relations
A Model for Business Models
BM: what it is and what it is not

• **What it is:**
  - activities AND
  - organizational units AND
  - their relations/linkages

• **What it is not:**
  - business strategy OR
  - product or market characteristics OR
  - technology OR
  - activities (by themselves) OR
  - any combination of the above
Example 1: ZARA
Observation #1:
ZARA SUPPLY CHAIN

Step 1: Scan fashion shows

Step 2: Simplify «hits» & produce library of designs

Step 2: Shoppers (and store managers) «pull» next design (shape) & designers «adapt»

Step 3: Designers «pull» next RM batch

Step 3: Final Design of next batch

Mfg

Dist

Shopping experience
Observation #2: Management Relationships

1) Start-up of ZARA Quick Response: **CEO runs the La Coruna store and the factory**

2) “New Product Committee”: designer, supply chain manager, commercial manager co-govern operations

3) **Store managers**: fully engaged in operations
Example 2: Accor

A Multi-business corporation with central activities (real estate, new format development, financing, franchising, overseeing business leaders, ...
### Service Offer

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#### Business Processes

- **Flow line:** Inflexible
- **Job shop:** Flexible

#### ACCOR

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Example 3: Lufthansa Group

A Business Model Change that is purely a change in managerial relationships
The old Lufthansa: Functional Organization

The new Lufthansa Group: Service Holding

BMC at Lufthansa

BMC at Nissan: in the other direction
Definition #3a: Business Model Change

A reconfiguration of activities, organizational units, their linkages and relationships.

In short:
reactivating, repositioning/relocating, relinking, regoverning
A Model for BMC

- Linkages between activities: Relinking
- Regovern
- Augment
- Remove
- Set of activities

- Positioning between activities:
  - Insourcing
  - Outsource
  - Off-shore
  - On-shore

Business model Innovation

Location of activities
Definition #3b: Business Model Innovation

The definition of a business model that is new and valuable for a given product-market (or business in the SIC sense).
Implications for Practice: BU Level

• BMI offers opportunity for **lean value creation**

• BMI does not require breakthrough technologies or heavy investment in new product/market/business development

• People & relationships are as much a part of a business **model** as technology linkages & economic exchanges

• **All BMI is competency destructive** & will require transformational behavioral change

• **It takes considerable time** (and much more so than product or market innovation) - which is also why it gets little billing
Further argumentation on behalf of BM:

corporate theorizing that is distinct and new compared with the typical portfolio/synergy dichotomy
Definition #4:  
The BMI-Conducive Corporation

A corporation that maximizes the opportunity / likelihood that BMI (or BMC) will emerge from within its business units
Implications for Practice: Corporate Level

• To create BMI-Conducive Corporation, corporate executives need to engage in both structural & behavioral change

• Loose horizontal coupling combined with deep sense of organizational justice & mutual engagement (cfr. Fair process) will maximize opportunities for BMI from within $B_{UC}$

• Corporations can develop creative white space to maximize BMI exchange across $B_{UC}$
Toward the BMI-Conducive Corporation

Horizontal Coupling

Creative White Space
- High autonomy
- High cross-unit learning

Low Autonomy
- High cross-unit learning

High Autonomy
- Low cross-unit learning

Low Autonomy
- Low cross-unit learning

Organizational Justice/Mutual Engagement

High

Low
Towards a Theory of BMI: summary

- A definition of Business Model (BM) that brings in activities, their organizational units (and hence people), and their linkages and relationships
- A concept should be part of OM and elevates OM into the strategy space (in a way that supply chain design does not)
- It re-imports management into OR/OM
- It provides a unique space, next to:
  - finance (an input)
  - marketing (product-market issues)
  - entrepreneurship (not only for start-ups)
  - strategy and OB (let us add some activities)