LITTLE NOTABLES EXCLUSIVE – PARI TARAPORE

WEEK 4: CREATING A BUSINESS (CREATING VALUE→CAPTURING VALUE)

THE ESSENCE OF A BUSINESS MODEL IS IN DEFINING THE MANNER BY WHICH THE ENTERPRISE DELIVERS VALUE TO CUSTOMERS, ENTICES CUSTOMERS TO PAY FOR VALUE, AND CONVERTS THOSE PAYMENTS TO PROFIT. (Teece, 2010)

BUSINESS MODELS:

WHAT IS A BUSINESS? A business is an organisation engaged in the trade of goods, services, or both to customers. The word "business" relates to being busy, doing commercially viable and profitable work.

"COMMERCIALLY VIABLE" has two meanings:

1. Customers find the firms and services valuable, they feel it is easier for them to fulfil their goals, or live their lives, if the use the firms g/s. Furthermore, customers need to prefer the companies g/s compared to the competitive alternatives in the market. → **Value creation** (a firm's ability to create value for the customer)
2. A firm needs to secure that it can capture value from the market, this value has to be captured from the customers who use the company's g/s. The most important part to value capture relates to the customers WILLINGNESS TO PAY for the g/s. The price they pay is the company's ultimate source of profit. In order to be able to sustainably make profit, companies also need to focus on long term value capture e.g. building long term relationships with customers in order to retain them for a long time, engage the customers in the development of new g/s, or getting feedback and ideas.

Balancing value capture (value to the firm) and value creation (value to the customer) is the key to success. A sustainable business relies on being able to create value and capture value. if the firm only creates value for the customers but is not able to capture any value, success will be short lived. On the other hand, customers will be dissatisfied if the opposite occurs.

WHAT IS A BUSINESS MODEL? The business model explains how the firm creates value for the customer and how it captures value from working with the customer. A BM can be described by 9 basic building blocks (these are portrayed in a business model canvas)

-Customer segments: all the people or organisations for which value is being created.
-Value propositions: bundles of products and services that create value for customers
-Channels: describe through which touch-points you are interacting with customers and delivering value.
-Customer relationships: outline the type of relationships you are establishing with your customers.
-Revenue streams: make clear through which how and through which pricing mechanisms your BM is capturing value.
-Key resources: describe the infrastructure used to create, deliver and capture value. They show which assets are indispensable to your business model.
-Key activities: show which things you really need, to be able to perform well.
-Key Partnerships: show who can help you leverage your BM since you aren't doing everything yourself
-Cost structure: after understanding your BM's infrastructure, you are also having an understanding of its cost structure.

Not all firms have the same business models, in fact most business' compete to have different business models.
e.g. the airline industry. Air NZ is a network based airline, "business model of compromise" →large airline in a small country, own 80% of the domestic market in NZ, so have to offer value proposition to customers all across the range.
LOW Price sensitive, corporate market→ HIGH price sensitive customer who has more time than money.
Have a compromise strategy; scale them to NZ's small market. Alliances help reach further markets.

THE 'FLAG CARRIER' BUSINESS MODEL	**THE 'LOW-COST CARRIER' BUSINESS MODEL**
-State owned -Serve different segments- business class important -Different value propositions -Alliances between airlines (Air NZ and Star Airlines) -Frequent flyer programmes (Airpoints)	-Focus on price-sensitive consumers -Same value-proposition-stripped down, no-frills service -Short haul flights -Lower airfares, fewer comforts Charge more for all extras (food, priority boarding)

BID FIRMS MAY HAVE SEVERAL BUSINESS MODELS simultaneously= HSBC, they have very different business models that they offer to their customer base. e.g. Online banking, customer can take care of a majority of routines by themselves. Branch network who aid customers with banking services and corporate banking which serves large corporations and a private bank which focuses on wealthy individuals.
Thus, developing business models is important for major corporations and also for small start-ups.

WHY FOCUS ON BUSINESS MODELS? In our increasingly competitive marketplace product innovation is not enough, what is needed is BM innovation when creating new products and services:

Successful companies are focusing on developing new business models and it can be argued that business models are competing against each other.

e.g. Mobile Phone industry: A mobile phone means nothing if it is not connected to series of supporting services. When an iPhone is connected to all the applications and data that you can buy in the appstore, value is added to the device. Apples total business model is being used, and this business model creates a lot of value to you.

Today there are arguably 3 BM's that COMPETE: Apples operating system vs. the Android based system produced by Google. Now we are seeing the emergence of a new op. system where Nokia and Windows have joined hands to produce a windows based BM. Eventually the winner may not be the one who has the best mobile phone, but the one with the best BM. Additionally the internet challenges all existing BM's as they have to adapt to the rapidly changing world of the internet.

-BM's today are quickly getting outdated, because the rules of the game have changed. We have transformed from consumers into producers due to the ease created by the internet to start up business' from home at zero cost.

Firms often use generic BM's: e.g 1. McDonalds and Dunkin' Donuts: as these are franchise based industries. They have standardised and defined their BM's in such a detail that they can let other company's use their successful business models, and can expand their network rapidly. For a franchisor, this is an alternative to building their own chain of stores to distribute their g/s.

2. Gilette and hp (printers): Razor and blades business model, where on item is sold at a cheap price (or even given away for free) in order to increase sales of a complementary good. e.g Razor is cheap, however blades are very expensive.

3. Google and Spotify: (internet based models: Freemium model): A product or service is provided for free but premiums are charged when you start to use advanced features or functionalities of this product or service.

-Google: "Googling" is free for consumers but advertisers have to pay. The free part supports the other part where google is able to charge a premium price.

-Spotify: Music streaming service, covering a range of major and independent record labels. It is free for 6 months by logging in with your Facebook account. Provides unlimited amounts of music as long as it is accepted that there is radio style advertisements mixed with the music. After the trial period, Spotify will make tracks unavailable once they have been played 5 times. If a subscription is paid Spotify removes the advertisements, and if a premium has been paid there is access to features such as offline access to selected music on your mobile phone.

SUSTAINABILITY: (it is important not only to society but also to businesses)

THERE'S NO ALTERNATIVE TO SUSTAINABLE DEVELOPMENT. Even so, many companies are convinced that the more environment-friendly they become, the more the effort will erode their competitiveness. They believe it will add to costs and will not deliver immediate financial benefits. Suppliers can't provide green inputs or transparency; sustainable manufacturing will demand new equipment and processes; and customers will not pay more for eco-friendly products during a recession. That's why most executives treat the need to become sustainable as a corporate social responsibility, divorced from business objectives. Becoming environment-friendly lowers costs because companies end up reducing the inputs they use. In addition, the process generates additional revenues from better products or enables companies to create new businesses. In fact, because those are the goals of corporate innovation, we find that smart companies now treat sustainability as innovation's new frontier. The key to progress, particularly in times of economic crisis, is innovation.

SUSTAINABLE DEVELOPMENT: "Sustainable development is development that meets the needs of the present without compromising the needs of future generations to meet their own needs" Bruntland (1987)

Sustainability means that things can keep going, "can sustain themselves" and continue into the future and go on forever. In a human perspective, sustainability for our planet means that it can continue to do what it was designed to do: provide fresh air, clean water, provide fresh food and allow us all to have a high quality of life forever. Non-sustainability means that it cannot, and that is where we are now.

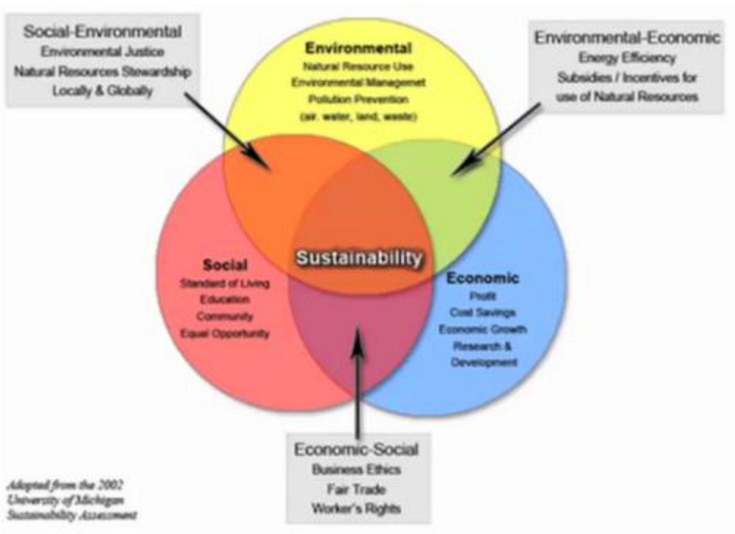
Sustainability goals: 1. Reduce our dependence on fossil fuels and heavy metals: coal, oil or natural gas. (CO_2 emissions)

2. Reduce our dependence on synthetic chemicals and other unnatural substances

3. Reduce encroachment upon nature (stop building high rises and factories where green once stood)
4. Meet human needs fairly and efficiently for people in society.

Demand for the earth's services: clean air, water, food increases as the population increases, and living standards rise, but the earth's ability to provide these services is declining because of the way we are living in or search for prosperity growth and success we are destroying the system that we as humans are completely dependent on → nature. We as humans have become a threat to our own existence. The earth is a system and everything is connected: society, environment and the economy. To live sustainably, we need to follow the 4 care instructions and apply them to everything we do at home and at work. By doing so we can all work together to be sustainable and have a better quality of life due to less pollution and waste and create more things we value in society while allowing the planet to produce the things needed in order to be sustainable.
NZ's forests can only absorb 1/3 of our CO_2 emissions into their ecosystem so a lot more trees need to be planted.

CORPORATE SOCIAL RESPONSIBILITY (CSR) is the importance of a balance between economic (making money), social (having a decent standard of living) and environmental (preventing pollution and protecting our natural resources).



Airlines are huge polluters, but sustainability plays a huge role in the strategies of Air New Zealand. Brand NZ and brand Air NZ are linked. After the global financial crisis in 2008 it was a company goal to simply SURVIVE, but today sustainability is almost a necessity. Emission's over 40 years have decreased by 70% for each km a passenger flies and this is continuously being improved. Being sustainable also improves and helps make efficient all their procedures e.g. Bio-fuel (in a way causing a WIN-WIN situation).

On the other hand, many major industries have not reacted to being sustainable. e.g CADBURY (palm-oil case): Failure to protect the natural environment has become a major public relations issue for many global brands including Cadbury and Nestle. → Well-known companies can be singled out for their business practices when they threaten the natural environment, while others are overlooked. The harvesting of palm oil is destructing the natural environments of orang-utans and many other endangered species. Social media is being used to engage people all around the world and create a public outcry against these brands. The impact of social media campaigns and worldwide news coverage has hurt the reputations of Cadbury particularly in NZ and sales have transferred to Whittaker's. Cadbury admits its actions damaged its reputation as it takes a long time to restore customer trust. **A brand is no longer what we tell people it is, it is what people tell each other it is. The result was "Cadbury" New Zealand's most trusted brand thrust to 36th place because of people's feelings about the destruction of the environment to obtain palm oil for their chocolate bars.**
-A business has to be profitable to remain in business; the challenge is how business' can prosper while developing strategies on how to remain responsible to society and the environment.

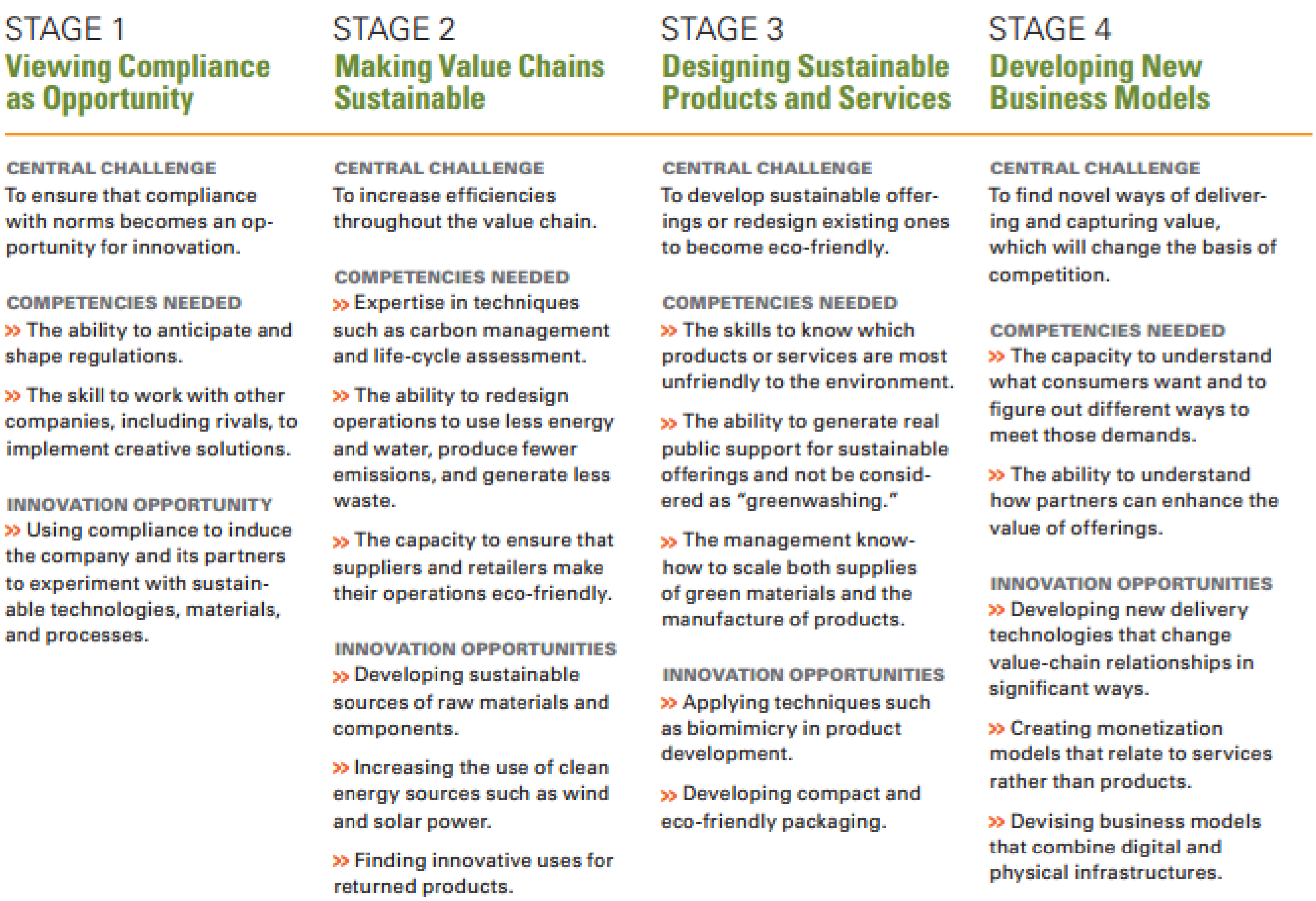
SUSTAINABILITY is now viewed as an opportunity, not a threat. (It is now the key driver of innovation)
1. Viewing compliance as opportunity (an opportunity to be more efficient, more innovative and develop new improved business models). The first steps companies must take on the long march to sustainability usually arise from the law. Compliance is complicated: Environmental regulations vary by country, by state or region, and even by city. It's tempting to adhere to the lowest environmental standards for as long as possible. However, it's smarter to comply with the most stringent rules, and to do so before they are enforced. Facets of environmental conservation which were once conventions soon become law.
2. Making value chains sustainable: Once companies have learned to keep pace with regulation, they become more proactive about environmental issues. Many then focus on reducing the consumption of nonrenewable resources

such as coal, petroleum, and natural gas along with renewable resources such as water and timber. The drive to be more efficient extends from manufacturing facilities and offices to the value chain. Most large corporations induce suppliers to become environment-conscious by offering them incentives. Operations. **Central to building a sustainable supply chain are operational innovations that lead to greater energy efficiency and reduce companies' dependence on fossil fuels.** Workplaces. **Partly because of environmental concerns, some corporations encourage employees to work from home. This leads to reductions in travel time, travel costs, and energy use.** Returns. **Concerns about cutting waste invariably spark companies' interest in product returns.**

3. Designing sustainable products and services: In order to identify product innovation priorities, enterprises have to use competencies and tools they acquired at earlier stages of their evolution. To design sustainable products, companies have to understand consumer concerns and carefully examine product life cycles. They must learn to combine marketing skills with their expertise in scaling up raw-materials supplies and distribution.

4. Developing New Business models: Most executives assume that creating a sustainable business model entails simply rethinking the customer value proposition and figuring out how to deliver a new one. Developing a new business model requires exploring alternatives to current ways of doing business as well as understanding how companies can meet customers' needs differently. Executives must learn to question existing models and to act entrepreneurially to develop new delivery mechanisms. As companies become more adept at this, the experience will lead them to the final stage of sustainable innovation, where the impact of a new product or process extends beyond a single market.

5. CREATING NEXT-PRACTICE PLATFORMS: Next practices change existing paradigms. To develop innovations that lead to next practices, executives must question the implicit assumptions behind current practices. This is exactly what led to today's industrial and services economy. Sustainability can lead to interesting next-practice platforms. One is emerging at the intersection of the internet and energy management.



STAGE 1
Viewing Compliance as Opportunity

CENTRAL CHALLENGE
To ensure that compliance with norms becomes an opportunity for innovation.

COMPETENCIES NEEDED
» The ability to anticipate and shape regulations.
» The skill to work with other companies, including rivals, to implement creative solutions.

INNOVATION OPPORTUNITY
» Using compliance to induce the company and its partners to experiment with sustainable technologies, materials, and processes.

STAGE 2
Making Value Chains Sustainable

CENTRAL CHALLENGE
To increase efficiencies throughout the value chain.

COMPETENCIES NEEDED
» Expertise in techniques such as carbon management and life-cycle assessment.
» The ability to redesign operations to use less energy and water, produce fewer emissions, and generate less waste.
» The capacity to ensure that suppliers and retailers make their operations eco-friendly.

INNOVATION OPPORTUNITIES
» Developing sustainable sources of raw materials and components.
» Increasing the use of clean energy sources such as wind and solar power.
» Finding innovative uses for returned products.

STAGE 3
Designing Sustainable Products and Services

CENTRAL CHALLENGE
To develop sustainable offerings or redesign existing ones to become eco-friendly.

COMPETENCIES NEEDED
» The skills to know which products or services are most unfriendly to the environment.
» The ability to generate real public support for sustainable offerings and not be considered as "greenwashing."
» The management know-how to scale both supplies of green materials and the manufacture of products.

INNOVATION OPPORTUNITIES
» Applying techniques such as biomimicry in product development.
» Developing compact and eco-friendly packaging.

STAGE 4
Developing New Business Models

CENTRAL CHALLENGE
To find novel ways of delivering and capturing value, which will change the basis of competition.

COMPETENCIES NEEDED
» The capacity to understand what consumers want and to figure out different ways to meet those demands.
» The ability to understand how partners can enhance the value of offerings.

INNOVATION OPPORTUNITIES
» Developing new delivery technologies that change value-chain relationships in significant ways.
» Creating monetization models that relate to services rather than products.
» Devising business models that combine digital and physical infrastructures.

Smart corporations follow these simple rules in their effort to become sustainable.

DON'T START FROM THE PRESENT. If the starting point is the current approach to business, the view of the future is likely to be an optimistic extrapolation. It's better to start from the future. Once senior managers establish a consensus about the shape of things to come, they can fold that future into the present. They should ask: What are the milestones on the path to our desired future? What steps can we take today that will enable us to get there? How will we know that we are moving in that direction?

ENSURE THAT LEARNING PRECEDES INVESTMENTS. Top management's interest in sustainability sometimes leads to investments in projects without an understanding of how to execute them. Smart companies start small, learn fast, and scale rapidly. Each step is broken into three phases: experiments and pilots, debriefing and learning, and scaling. These companies benchmark, but the goal is to develop next practices -- not merely mimic best practices.

STAY WEDDED TO THE GOAL WHILE CONSTANTLY ADJUSTING TACTICS. Smart executives accept that they will have to make many tactical adjustments along the way. A journey that takes companies through five stages -- and lasts a decade or more -- can't be completed without course corrections and major changes. Although directional consistency is important, tactical flexibility is critical.

BUILD COLLABORATIVE CAPACITY. Few innovations, be they to comply with regulations or to create a new line of products, can be developed in today's world unless companies form alliances with other businesses, nongovernmental organizations, and governments. Success often depends on executives' ability to create new mechanisms for developing products, distributing them, and sharing revenues.

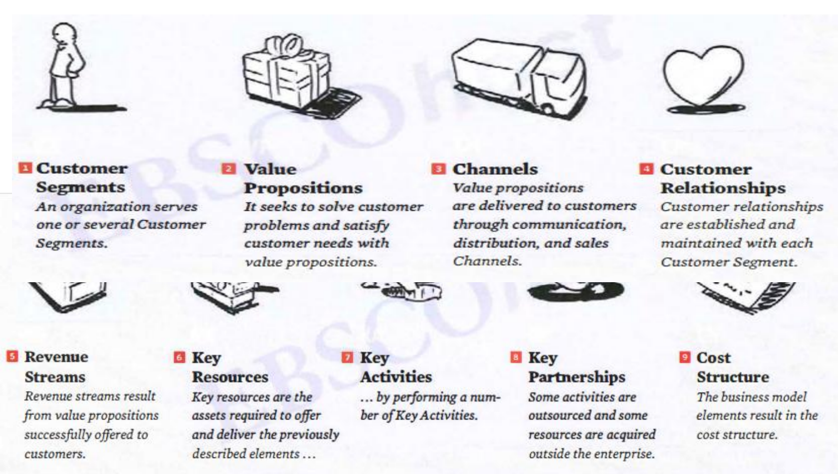
USE A GLOBAL PRESENCE TO EXPERIMENT. Multinational corporations enjoy an advantage in that they can experiment overseas as well as at home. The governments of many developing countries have become concerned about the environment and are encouraging companies to introduce sustainable products and processes, especially for those at the bottom of the pyramid. It's easier for global enterprises to foster innovation in emerging markets, where there are fewer entrenched systems or traditional mind-sets to overcome.

TRIPLE BOTTOM LINE REPORTING: is designed to capture, describe, report and measure the impact of the organisations activities on its various environments. It consists of a balanced scorecard which reports on firms financial/economic (sales, profits, ROI, taxes paid) and environmental performance (water/air quality, energy usage, waste produced) and its social performance (labour practices, community impacts) to society as a whole.
The Warehouse and Hubbards were the first two to embrace CSR and use triple bottom line reporting in New Zealand which helped form the NZ sustainable network.

AC Nielsen research (by NZ) shows that people prefer brands that support the community, i.e. charity or worthy causes. Almost 2/3rd of the population prefers a company that aligned itself with a worthy cause e.g. Ronald McDonald house charity.

NIKE and SUSTAINABILITY: (embracing transparency) Is an example of this on a global perspective. A sustainable perspective allowed Nike to turn over a new leaf and bring back its image.

A BUSINESS MODEL DESCRIBES THE RATIONALE OF HOW AN ORGANISATION CREATES, DELIVERS, AND CAPTURES VALUE. A concept must be simple, relevant, and intuitively understandable, while not oversimplifying the complexities of how enterprises function. The nine blocks cover the four main areas of a business: customers, offer, infrastructure, and financial viability. The business model is like a blueprint for a strategy to be implemented through organizational structures, processes, and systems.



The Customer Segments Building Block defines the different groups of people or organizations an enterprise aims to reach and serve. Customers comprise the heart of any business model. Without (profitable) customers, no company can survive for long. In order to better satisfy customers, a company may group them into distinct segments with common needs, common behaviours, or other attributes. Customer groups represent separate segments if:

Their needs require and justify a distinct offer
They are reached through different Distribution Channels
They require different types of relationships
• They have substantially different profitability's
• They are willing to pay for different aspects of the offer

MASS MARKETS: Business models focused on mass markets don't distinguish between different Customer Segments. Customer Relationships all focus on one large group of customers with broadly similar needs and problems.

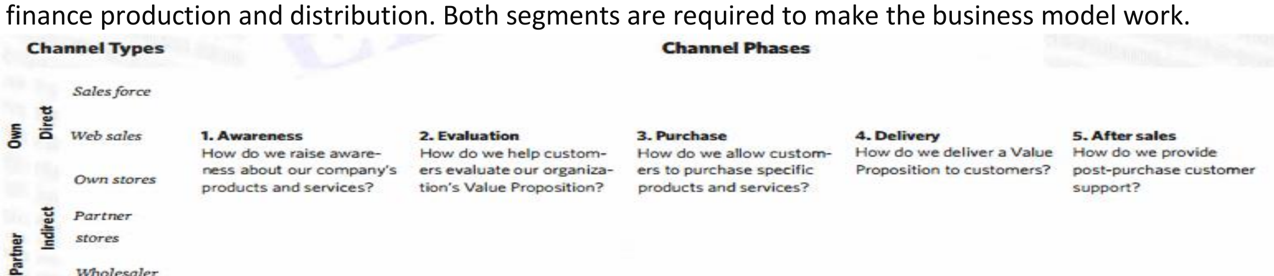
NICHE MARKETS: Business models targeting niche markets cater to specific, specialized Customer Segments. The Value Propositions, Distribution Channels, and Customer Relationships are all tailored to the specific requirements of a niche market. Such business models are often found in supplier-buyer relationships. For example, many car part manufacturers depend heavily on purchases from major automobile manufacturers.

SEGEMENTED: Some business models distinguish between market segments with slightly different needs and problems. The retail arm of a bank like Credit Suisse, for example, may distinguish between a large group of customers, each possessing assets of up to U.s. $100,000, and a smaller group of affluent clients, each of whose net worth exceeds U.S. $500,000. Both segments have similar but varying needs and problems. It serves three different Customer Segments-the watch industry, the medical industry, and the industrial automation sector-and offers each slightly different Value Propositions.

Diversified: An organization with a diversified customer business model serves two unrelated Customer Segments with very different needs and problems. For example, in 2006 Amazon.com decided to diversify its retail business by selling "cloud computing" services: online storage space and on-demand server usage. Thus it started catering to a totally different Customer Segment-Web companies-with a totally different Value Proposition. The strategic rationale behind this diversification can be found in Amazon.com's powerful IT infrastructure, which can be shared by its retail sales operations and the new cloud computing service unit.

Multi-sided platforms (or multi-sided markets)

Some organizations serve two or more interdependent Customer Segments. A credit card company, for example, needs a large base of credit card holders and a large base of merchants who accept those credit cards. Similarly, an enterprise offering a free news-paper needs a large reader base to attract advertisers. On the other hand, it also needs advertisers to finance production and distribution. Both segments are required to make the business model work.



Component	Questions
Positioning	1. Which basic customer need are we trying to fulfill? 2. How can we establish and retain a unique position in our customers' minds?
Product and service logic	3. Which products and product features are necessary to become indispensable and strengthen our positioning? 4. What is the unique product benefit we offer our customers?
Added value logic	5. How we design our value creation processes to effectively and efficiently bring our offers to the market? 6. What are our core competencies and core processes on which we focus and which allow us to create value?
Sales and marketing logic	7. How do we attract customers? 8. How do we retain customers?
Profit formula	9. Based on which economic rational are we making profits?

Product innovations no longer provide sufficient opportunities for differentiation. Ever shorter life cycles, shorter periods of imitation and increasing competition from low wage countries require new and sustained competitive advantages. Unique, non-duplicable business models are at the root of today's new business opportunities. A company's task is to find new ways to generate added value for customers and to monetize a portion of this surplus value.
A business model innovation comprises five components:
1. innovative, unique positioning;
2. a consistent product and service logic;
3. an appropriate value creation architecture;
4. an effective sales and marketing logic; and
5. a profit formula that works.