

Chapter 3

Business Models

Outline

- Introduction
- Pressures forcing business changes
- Business models-definitions
- Business models-classification

Introduction

- The vertical bureaucratic structure in a firm is built on the assumption that concentrating similar activities within functions, and thus separating activities which are not similar, would result in economies of scale.
- The internet and related technologies reduce coordination costs and transaction costs.
- Traditional business models focused on creating value at the line-of-business level while the new business models focus on the customers and creating value at the relationship level across products and channels.

Pressures Forcing Business Changes

- The unprecedented challenges which businesses are facing nowadays makes competition fiercer and more global. Customers become increasingly demanding because of competing products and service offerings.
- The increasingly competition leads companies to rethink their position in the market place fundamentally.
- To have success in today's market, business networking strategies are required to provide high quality, cost-efficient products reflecting the customers need. This is made possible by the development of modern information technology.

Business Strategy Vs. Business Model

- In a company's e-business plan the business model takes a central position which consolidates its purpose and goals to outline all kinds of aspects relating to e-business including: marketing plan, competition, sales strategy, operations plan, management plan and financial plan.
- The business model must effectively address aspects such as: value proposition, revenue model, market opportunity, competitive advantage, market strategy, organizational development and management [Ghosh 98].

Business Models – types of definitions

- Definitions that relate to *participants* in a joint business venture.
- Definitions that relate to the *processes and structure* of a business organization.
- Definitions that relate to how business models are *seen from the perspective of a marketplace*.

First Type of Definition

This definition may describe business models as follows:

- Business models specify relationships between participants in a commercial venture, benefits, and costs to each and flows of revenue
- A business model describes how the enterprise produces, sells and delivers products and services, thus showing how it delivers value to the customers and how it creates wealth [Margretta 2002].
- A business model addresses a simple equation (profit = revenue – costs) [Elliot 2002]. .

Second Type of Definition

This definition describes business models as follows:

- An architecture for the product, service and information flows
- A description of the various business actors and their roles.
- A description of the potential benefits for the various actors.
- A description of the sources of revenues.

Third Type of Definition

According to this definition business models can be analyzed from various perspectives [Chaffey 2002]:

- Is the company involved in business-to-business activities, business-to-customer activities or both?
- Which position does the company have in the value chain between customers and suppliers?
- Which is its value proposition, and which are its target customers?
- Which are the specific revenue models that will generate its various income streams?
- How is it represented: by physical shops ('bricks') or online, in the virtual world ('clicks'); or even by a mixture of these two ('bricks and clicks')?

Business Strategy Vs. Business Model

- In general, business models do not indicate how the business objectives are achieved, which is different from *business strategies*.
- Business strategies specify how a business model can be applied to differentiate a company from its competitors [Elliot, 1999].
- *Marketing model* was introduced to encompass both the business model and the strategy of the enterprise [Timmers 1998]

The Important Elements When Taking the Internal Aspects of a Business Into Account:

- The *product* or *service* that a company delivers to its customers.
- The *sources of revenue*.
- The (primary, support. and physical) *activities* to deliver products or services and realize strategic objectives.
- The *organization* a company has established to realize its objectives, e.g., company structure (how tasks are allocated), processes (combination of tasks to accomplish specific outcome)

Conclusion: This Book's Definition

A business model is a descriptive representation of the planned activities of a business (sometimes referred to as business processes) that involves three integral components, which specify:

- The internal aspects of a business venture;
- The type of relationships of the enterprise with its external business environment and its effective knowledge regarding these relationships;
- How a company's information assets, e.g., information systems and effective business processes typically grouped in the customer relationship management (CRM), supply chain management (SCM) and core business operations domains, are embedded in the business venture.

Business Models – Classification

Traditional organisational structure

VS

New organisational structure

Traditional Organisational Structure

- Vertical and hierarchical
- Function-based
- Product-based
- Geography-based
- Matrix-based
- High coordination costs (costs of sending, storing and retrieving information)
- Seller- or product-driven, aiming to generate value at the of line-of -business level

New Organisational Structure

- Hierarchical, procedural and other new coordination mechanisms, which leads to network based business models.
- Team-based structure.
- Customer focused: value is generated at the relations level, across products and channels.
- Creation of Internet-based business models (5 Business models Classifications)

5 Business Models Classifications

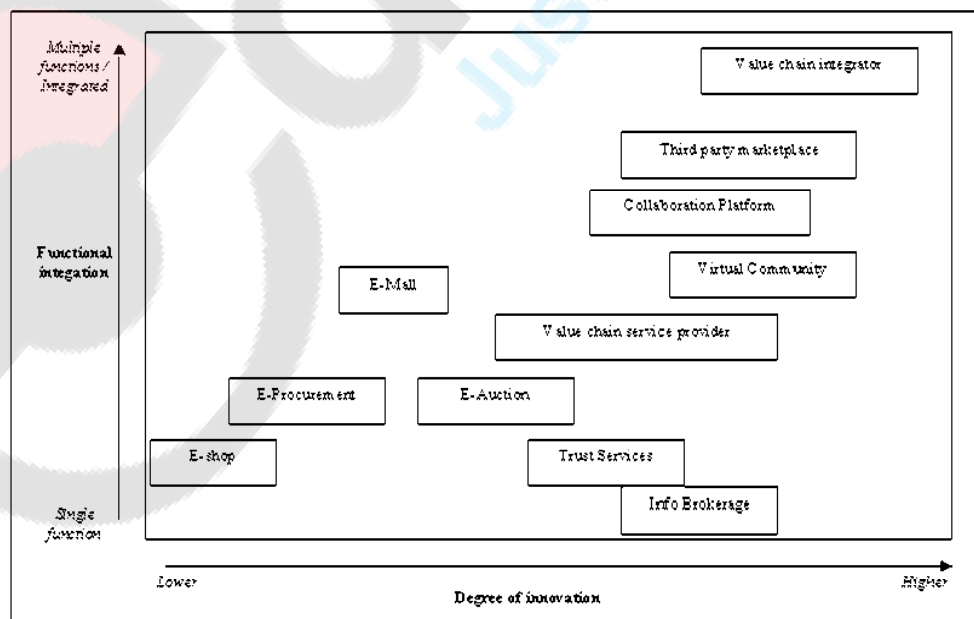
- Internet-enabled
- Value-web
- E-business enabled
- Market participant
- Cyber-intermediary

Internet Enabled Business Model

- 10 different types of business models that are facilitated by the Internet
- Based on analysis of Porter's value chain
- Internet-enabled models are classified according to the degree of innovation and functional integration involved.
- 1st dimension – Innovation: Ranges from basically applying the Internet to replace a more traditionally way of doing business to more innovative business models.
- 2nd dimension – Functional Integration: Ranges from business models that encompass one function, such as e-shop, to a business model that fully integrates multiple functions

Internet Enabled Business models

P. Timmers (1998) continued



Internet Enabled Business models

P. Timmers (1998)

- E-shop
- E-procurement
- E-auction
- E-mall
- Third party marketplace
- Virtual communities
- Value chain service provider
- Value chain integrator
- Collaboration platform
- Information brokerage, trust and other services
- Trust services

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Internet Enabled Business Model

- E-shop: Web site used by a company to give/get information for marketing purposes
- E-procurement: Process that involves purchasing goods and services through the web.
- E-mall: Collections of E-shops under 1 umbrella (special service or product types, brands etc.).
- E-auctions: Internet bidding mechanisms that can be applied to both B2B and B2C contexts.
- Third party marketplaces: Virtual marketplaces where potential suppliers and buyers interact and transact.

Internet Enabled Business Model

- Virtual Community: Offers people with a common interest, such as a profession or expertise, facilities to share information; thus they add value for their members and so become important for marketing purposes.
- Collaboration platforms: Enable companies and individuals to work together by providing an environment and a set of collaboration tools.
- Value chain integrators: Focus on integrating multiple steps of the value chain.
- Value chain service providers: Specialized in providing specific functions such as electronic payments.
- Information brokers: New, emerging information service providers working for both consumers and businesses; They provide information and help parties generate trust in one another.

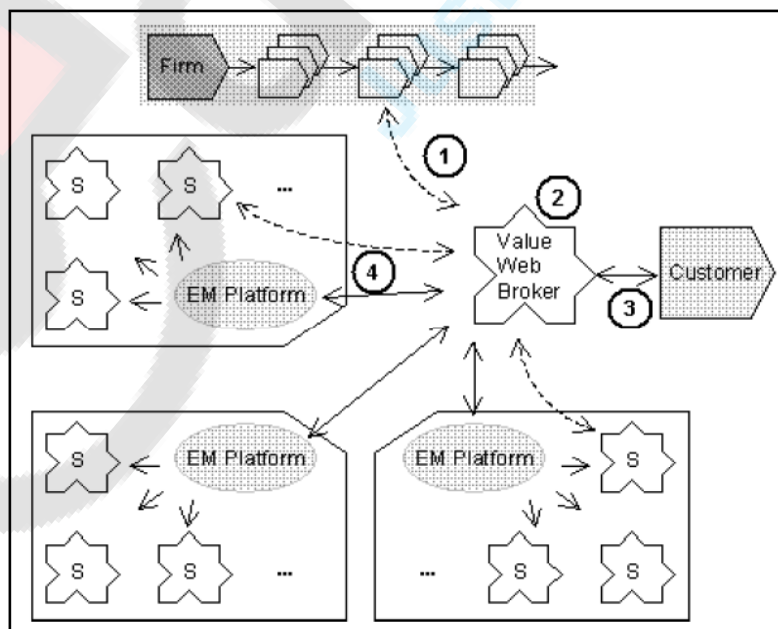
Value-web Business Model

- Value-web business model: A conception of an emerging form of a fluid and flexible organization.
- Value-web brokers: Having the central value web function of coordinator, integrator and interface.
- Consisting of several key building blocks:
 - Markets
 - Hierarchies
 - Networks
 - Information Technology
 - New-old business models

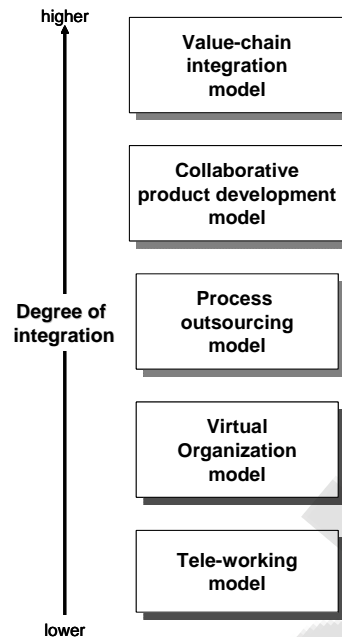
Value-web Business Model

- Markets: Purpose of markets is to bring together buyers and sellers and automate business transactions.
- Hierarchies: Traditional and inflexible bureaucratic structure.
- Networks: These arise because companies move away from the “old” ways of doing business (customer value created by 1 single organization) to the new ways of doing business (customer value created by a network of organizations). A network consists of nodes and relationships and cannot function without any missing part.
- Information Technology: Evolution of which the future is difficult to predict.
- New-old business models: They still may have value.

Value-web Business Model



The Family of e-Business Enabled Business Models



e-Business Enabled Business Models

- Classification scheme valid for B2B contexts
- Categorized based on the degree of integration between collaborating enterprises
- Low degree of integration means small no. of core business processes integration between networked organizations
- High degree means several core business processes integration in a meaningful way and can flow seamlessly between networked organizations

e-Business Enabled Business Models

- Telemarketing model: large numbers of individuals or groups collaborating using networking and communication technologies
- Example: engineers in multinational companies collaborating across the globe on the development of new products and processes

e-Business Enabled Business Models

- Virtual organization model: temporary or permanent collection of geographically dispersed individuals, groups and organizational units, linked electronically to complete a collaborative production process.
- Example: GeneralLife, an insurance company focusing on its core business product development and sales, while outsourcing all other functions to third party administrators
- Minimizes fixed costs and increases variable cost proportion
- Decreases new product time-to-market, and improves overall flexibility

e-Business Enabled Business Models

- Process outsourcing model: transferring responsibility for one or more processes to external suppliers.
- Human resources, accounting, and logistics functions are typical candidates for such transfer
- Critical condition for process outsourcing to work: smooth coordination and communication between service supplier and service recipient, meaning that transaction costs must be low
- Thus modern IT platforms are the critical factor

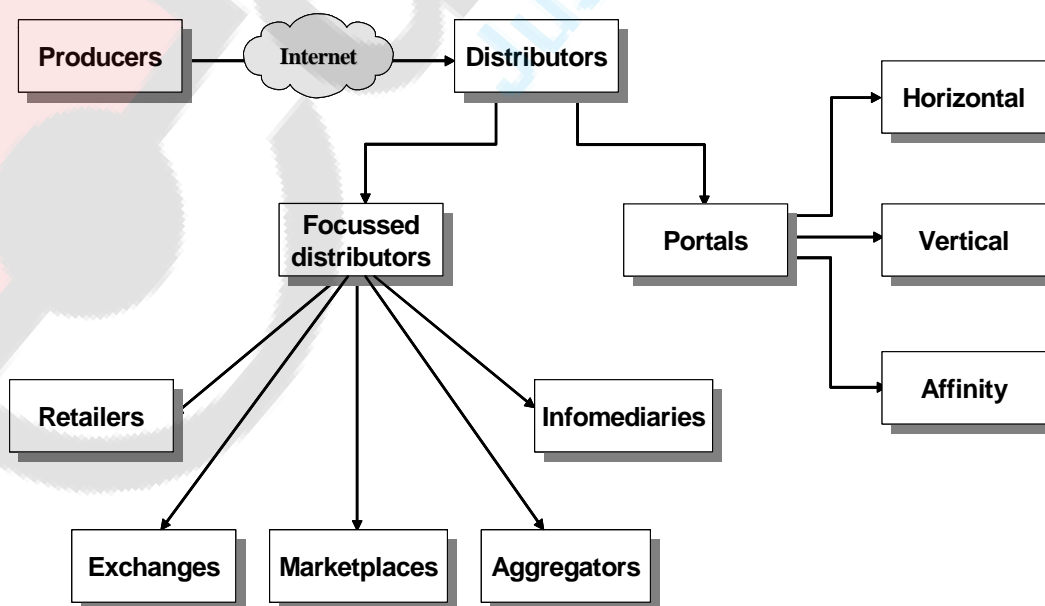
e-Business Enabled Business Models

- Collaborative product development model: concerns with the need to coordinate product development activities across multiple companies or organizational units
- Example: Ford Motor Corporation
- Called for flexible information systems and applications, making it possible to manage and transmit design documents across various Ford centers around the world.

e-Business Enabled Business Models

- Value chain integration model: when vendors must achieve effective coordination between ‘upstream’ suppliers, internal operations (e.g., manufacturing), and ‘downstream’ shippers and customers.
- Every company in the chain performs a set of activities contributing to the production of the chain’s collaborative products.

The Market Participants Business Model



Market Participant Business Models

- Two roles key: producers & distributors
- Producers (design and produce products and services)
 - Manufacturers of physical products
 - Less physical products (such as services provisioning, education and consultancy)
- Distributors (consists of focused distributors and portals)
 - Retailers (who sell inventory of which they have assumed control online)
 - Market places (without having physical control over the inventory sold)
 - Aggregators (who provide information on products or services sold by others in the channel)
 - Exchanges (who may or may not complete sales online nor assume control over inventory)
 - Infomediaries (a type of aggregator that brings together the sellers and buyers of information-based products)

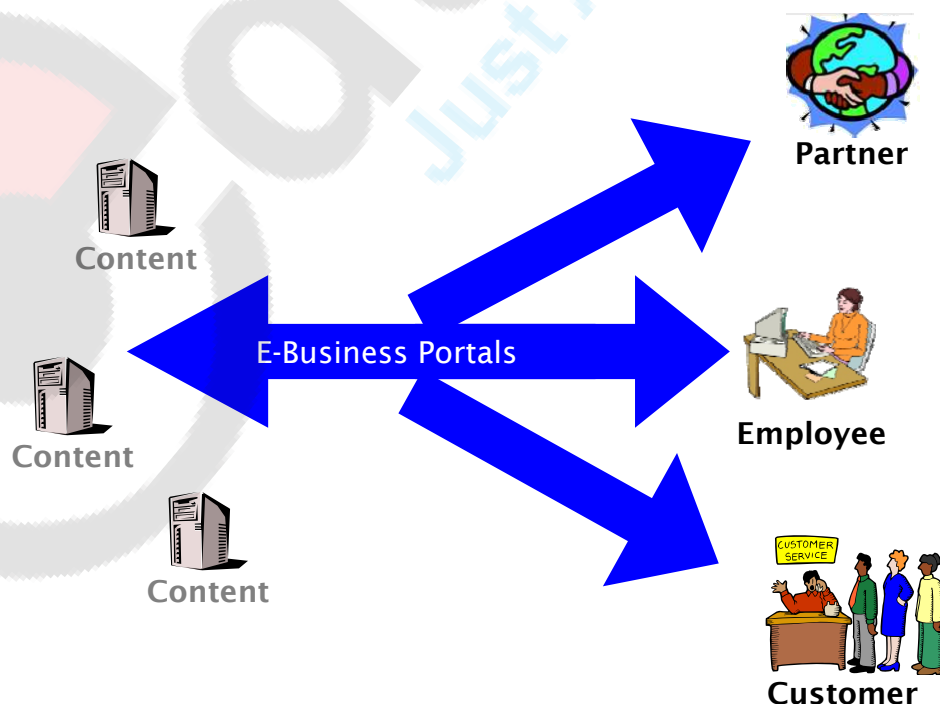
Definition of a Portal

- Portals are web sites targeted at specific audiences and communities, providing:
 - content aggregation/delivery of information relevant to the audience
 - collaboration and community services
 - services/applications access for target audiences

Definition of a Portal

- Portals offer:
 - Custom framework for presenting Web pages and components within each page and organizing info for specific customers
 - Personalization capabilities for individual users
 - Set of 'portlets' (components that integrate with data, applications, content, and resources, and present info to the portal user)
 - Single sign-on to the set of applications accessed via the portal
 - Other features, e.g., search and collaboration facilities

Role of a Portal



Portal Include Three Types:

- Horizontal Portals: Originally created to provide search engine services, these portals focus on the entirety of the Internet, not specified audiences, from various industries
- Vertical Portals: Often referred to as Vortals, these sites focus on targeted areas of interest, such as healthcare or financial services.
- Affinity Portals: Provide highly specific information, much like vertical portals but focused on specific interest groups or market segments.

Cybermediaries Business Model

- Cybermediaries: New Network-Based Intermediaries
- Definition: organizations which operate in electronic markets to facilitate exchanges between producers and consumers by meeting the needs of both producers and consumers
- Examines nature of intermediation in electronic markets and its implications for structure of electronic business
- Eleven business models are proposed based on this assumption
- Each business model is characterized by its functions

Cybermediaries Business Model

- **Directories:** Directory service intermediaries help consumers find producers by categorizing Web sites and providing structured menus to facilitate navigation.
- **Search Services:** In contrast to the directories, search sites (e.g. **Lycos** and **Infoseek**) provide users with the capabilities for conducting keyword searches of extensive databases of Web sites/pages.
- **Malls:** The term virtual mall or internet mall is often used to refer to any site that has more than two commercial sites linked to it.
- **Virtual Resellers:** The malls described above provide cyber-infrastructure, but they do not own inventory or sell products directly.
- **Web Site Evaluators:** Consumers may be directed to a producer's site via a new type of site that offers some form of evaluation, which may help to reduce some of the risk to consumers.

Cybermediaries Business Model

- **Publishers** Publisher Web sites are "traffic generators" that offer content of interest to consumers (e.g. Information Week or Wired Magazine).
- **Auditors** Auditors are not direct intermediaries, but serve the same functions as audience measurement services in traditional media.
- **Forums, Fan Clubs, and User Groups** Sites such as these are also not necessarily direct intermediaries, but can play a large role in facilitating customer-producer feedback and supporting market research.
- **Financial Intermediaries** Any form of electronic commerce will require some means of making or authorizing payments from buyer to seller.
- **Spot Market Makers** The emergency of such a service isn't surprising considering the speed with which e-networks can distribute information.
Barter Networks – Buyers and sellers exchange goods rather than pay for them with money.
- **Intelligent Agents** Intelligent agents are often discussed as the answer to user problems with navigation in the chaos of the Internet.