BUSINESS MODEL
DEVELOPMENT & INNOVATION

IFR
CENTURION
18 NOVEMBER 2012
BUSINESS MODEL INNOVATION
IBM STUDY 2006
Operating Margin Growth in Excess of Competitive Peers

compound annual growth rate over five years

[Source: IBM, CEOs are expanding the innovation horizon: important implications for CIOs]
Benefits Cited by Business Model Innovators

percent of respondents

- Cost reduction
- Strategic flexibility
- Focus and specialization
- Rapidly exploit new market/product opportunities
- Share or reduce risk and capital investment
- Move from fixed to variable cost

[Source: IBM, Global CEO Study 2006]
• Memeburn: Why is FNB doing this?

• Michael Jordaan: The first departure point is around the South African usage statistics for the various social media platforms. Facebook already has an impressive 6-million users in South Africa, while Twitter has around 1.5-million, LinkedIn around 1.8-million and Mxit about 10-million.

• As users are already using these platforms, often multiple times per day, FNB identified the opportunity to extend its already impressive digital footprint into this space. From this departure point, FNB had to establish what role this particular channel would play in our overall business and channel mix. Social media allows for high levels of engagement across various areas including marketing (awareness, information and discovery), sales (acquiring), support (education, feedback, advice and complaints) and transacting (social commerce and loyalty).

• Social banking or commerce is a natural extension of our digital innovation drive, which aims to provide customers with a choice of channels to engage with FNB for their banking and transactional needs. We therefore view social media as a complimentary digital channel, but with its own unique characteristics around social context. We believe social commerce in general will expand rapidly in the next few years.
MB: What value does it bring to the banking experience?

MJ: FNB views social media as a complimentary channel to our existing channels ranging from branches, call centres, online and mobile. FNB has provided its customers with another, or alternative, “always on” channel that is able to meet most needs across the various areas of marketing, sales, support and commerce. It has been a notably successful channel for new customer acquisition.

Many potential customers are choosing social media as a way to research their choice of bank with their peers, which have led to several direct and indirect sales of our products either via our online or mobile conversation channels or directly via our social media profiles. In addition to this, statistics released by the Aberdeen Group in February 2012, state that potential customers are 51% more likely to buy if they have a social connection with a brand. It has also become an important source of information to help drive communication and marketing strategy and most notably provides input into process improvement and future product development.

FNB is considered a leader in social media space by its peers in the financial services industry, as well as in various other unrelated sectors. This leadership position supports FNB’s overall positioning in the innovation space.
What is strategy about?
“The determination of the basic-long term goals and objectives of an enterprise, and the adoption of courses of action and the allocation of resources necessary for carrying out those goals”

(Chandler 1962)
DEFINITIONS OF STRATEGY

A strategy....pattern or plan that integrates....goals, policies, and action sequences into a cohesive whole.

...helps to marshal and allocate...resources into a unique and viable posture based on internal competencies and shortcomings, anticipated changes in the environment, and contingent moves by intelligent opponents.

(Quinn)
STRATEGY

A company’s strategy consists of the competitive moves and business approaches that managers employ to attract and please customers, compete successfully, grow the business, conduct operations, and achieve targeted objectives.

(Thompson, Strickland & Gamble)
STRATEGY

• Will define which battles are to be fought
• Sets out a plan to win in those areas where you choose to compete
• Will lead you to decide what not to do
• What areas of competition are beyond your reach
• or remote from the priorities which will enable you to achieve your overall vision
• The practitioner of strategy
  – Has to be practical as well as thoughtful
  – Has to be realistic as well as analytical
  – Has to be effective as well as articulate in his/her diagnosis, design, and implementation of strategy
• Only effective action and better results can justify the effort demanded by a full strategic approach
The Language of Strategy
Johnson & Scholes

• Mission – overriding purpose
  – (be healthy & fit)

• Vision (strategic intent) – desired future state
  – (ride bike race)

• Goal – general statement of aim or purpose
  – (lose weight & get fit)

• Objective – quantified/ more precise statement of the goal
  – (lose 6 kg by end December, ride the Argus in 2013)
Hedgehog Concept (Jim Collins)

What are you passionate about?  
(Mission and Core Values)

What you can be best in the world at?  
(Core/Distinctive Competencies)

What drives your resource engine?  
(Money, Time and Brand)
What is Strategy?

“a firm’s theory about how to compete successfully”
(Barney 2002)

• Theory:
  “Emphasises the imperfect information and incomplete knowledge that *always* surround implementation…”

• Compete successfully:
  “when their theory of how to compete …is consistent with the underlying economic processes …and when few other firms share this theory or are unable to act on it as completely

Outcomes:
Competitive Advantage
Competitive Parity
Competitive Disadvantage
What is Strategy? (Porter 1996)

• Competitive strategy is about being different. It means deliberately choosing a different set of activities to deliver a unique mix of value.

• Strategy is creating fit among a company's activities. The success of a strategy depends on doing many things well…and integrating them.

• E.g. S W Airlines
• E.g. Bidvest
• E.g. SABMiller
• E.g. Shoprite Group
what is a business model?
Defining Business Models

A good definition of a business model must be simple, clear and comprehensive.

• Simplicity will ensure it is easy to learn and remember.

• Clarity will ensure it is understood, and meets the intuitive “gut feel” test of experienced venture players.

• Comprehensiveness will ensure that it includes all the key elements that innovation and venture leaders need to consider in creating successful business models.
Chesbrough: the business model creates and captures value from technology. He suggests that a business model has six functions:

• To articulate the value proposition.
• To identify a market segment.
• To define the structure of the firm’s value chain, which is required to create and distribute the offering, and to determine the complementary assets needed to support the firm’s position in the chain.
• To specify the revenue generation mechanism(s) for the firm, and estimate the cost structure and target margins of producing the offering, given the value proposition and value chain structure chosen.
• To describe the firm’s position within the value network linking suppliers and customers, including identification of potential complementary firms and competitors.
• To formulate the competitive strategy by which the innovating firm will gain and hold advantage over rivals.
Gary Hamel: Leading the revolution

A business model: “a business concept that has been put into practice”. He proposes a business model framework comprising four primary elements:

• Core strategy – this includes the business mission, its product market scope and its basis for differentiation
• Strategic resources – the organization’s core skills, assets and processes that deliver the core strategy
• Customer interface – how customers interface with and experience the organization, including fulfillment / support, information / insight, relationship and pricing
• Value network – the organization’s external suppliers, partners and coalitions.
Skarzynski & Gibson: Innovation to the Core

Skarzynski and Gibson: “a conceptual framework for identifying how a company creates, delivers and extracts value”.

• Who do we serve? Includes market segments, customers, and buyers.
• What do we provide? Includes products, services, solutions, benefits.
• How do we provide it? Includes value chain, processes, skills, assets, partners, suppliers
• How do we make money? Includes pricing, revenue, costs, profits.
• How do we differentiate and sustain an advantage? Includes differences versus competitors, value to customers, sustainability based on skills and assets.
A business model: “consisting of four interlocking elements that, taken together, create and deliver value.”

- Customer value proposition: Target customer, needs (job to be done), offering
- Profit formula: revenue model, cost structure, margin model and resource velocity (asset turnover)
- Key resources, including people, technology, equipment, information, channels, partnerships and brand
- Key processes, including processes, metrics and norms.
A business model is the *core design of the business*, specifically the way it is designed to *create, deliver and capture value*.

• Thinking in terms of design is powerful. A good business model will be *simple and elegant, and it will work*.

• Its *design will be complete in every important respect*.

• Each *element will be carefully thought through and individually crafted*, and the *sum of the parts will integrate perfectly, harmoniously and effectively*.

• By contrast, a poor business model simply doesn’t work. It will either lack some critical elements, comprise the wrong elements, or comprise elements that don’t work well together.
• Markets – this consists of the markets in which the business chooses to compete, and where the business chooses to be positioned within the market’s value network. This includes the customers and needs the business chooses to address, the companies with which it competes, and the companies with which it partners.

• Products – this element is about defining the business’ offering – its value proposition – to its target customers. Think about the offering as holistically as possible. It thus includes defining and distinguishing between the core technology, platform and application features; defining the “whole” solution including third party complementary features; and defining the total customer experience and relationship. It also includes the other elements of the value proposition both to the customer (pricing and positioning) and to the business (margins and protection of IP).
• Processes – this element consists of how the business creates, markets and delivers its products and services to its customers. These three core processes – research and product development, sales and marketing, and operations and customer support – are the fundamental engine of the business. In addition, two other core processes must be defined - how the business manages (through strategic and operational planning and control), and how it supports (through HR, IT, finance, legal and other support services), these core activities. Like with the other elements, our definition of processes is holistic: it includes repeatable processes and one-off key initiatives, internal skills and assets, and external supplier and channel partners.
People – as discussed above, this element is about defining the core stakeholders in the business – the management team and key employees, investors and the board, and key strategic partners. It begins with defining which stakeholders make sense for the business, and how to attract them. It includes defining their joint vision for the business, how they work together, and how they make decisions. And it includes thinking through what they each contribute to the business, and how they each share in the value created and captured by the business.
• Economics – this element is both the result and the enabler of the other four elements. It comprises the key components of the economic model - revenue, costs, investment, funding and cash flow. Central to this element is thinking deeply about the core drivers in the other four elements, how these impact the business’ economics, how they interact with each other, and what tradeoffs must be made between different drivers. Ultimately, the overall focus of the business model is about optimizing its economics – how value can be maximized from limited resources, and how the business can capture its fair share of that value to share amongst its stakeholders.
Business Model Components: Anders Sundelin

- Value recipient - Who are we providing value for?
- Value Proposition - What values are we providing?
- Delivery - How are the values delivered?
- Assets, Capabilities & Activities - What internal and external assets, capabilities and activities are needed?
- External Relationships - What forms of external relationships are needed?
- Control Mechanisms - How is the value creation and extraction controlled?
- Benefit and Revenue Model - How are benefits and revenues generated?
- Costs and Harms - What are the costs and harms?
The profit Zone – slywotksy & morrison
<table>
<thead>
<tr>
<th>Dimension</th>
<th>Key Issue</th>
<th>Key Questions</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Customer Selection</td>
<td>Which customers do I want to serve?</td>
<td>To which customers can I add real value? Which customers will allow me to profit? Which customers do I not want to serve?</td>
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<tr>
<td>2. Value Capture</td>
<td>How do I make a profit?</td>
<td>How do I capture, as profit, a portion of the value I created for customers? What is my profit model?</td>
</tr>
<tr>
<td>3. Differentiation/ Strategic control</td>
<td>How do I protect my profit stream?</td>
<td>Why do my chosen customers buy from me? What makes my value proposition unique/differentiated vs. other competitors’? What strategic control points can counterbalance customer or competitor power?</td>
</tr>
<tr>
<td>4. Scope</td>
<td>What activities do I perform?</td>
<td>What products, services, and solutions do I want to sell? Which activities or functions do I want to perform in-house? Which ones do I want to subcontract, outsource, or work with a business partner to provide?</td>
</tr>
</tbody>
</table>
The Company Center of Gravity

The Entrepreneurial Phase

- The Company
- The Customers
- The Center of Gravity

The Growth Phase

- The Center of Gravity

The Success Phase

- The Center of Gravity

The Company
The Customers
# Strategic Control Point Index

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<td>Own the standard</td>
<td>Microsoft, Oracle</td>
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<td>9</td>
<td>Manage the value chain</td>
<td>Intel, Coke</td>
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<td>String of superdominant positions</td>
<td>Coke, internationally</td>
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<td>Own the customer relationship</td>
<td>GE, EDS</td>
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<td>Medium</td>
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<td>Brand, copyright</td>
<td>Countless</td>
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<td></td>
<td>5</td>
<td>Two-year product development lead</td>
<td>Intel</td>
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<td>Low</td>
<td>4</td>
<td>One-year product development lead</td>
<td>Few</td>
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<td></td>
<td>3</td>
<td>Commodity with 10 to 20 percent cost advantage</td>
<td>Nucor, SW Air</td>
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<tr>
<td>None</td>
<td>2</td>
<td>Commodity with cost parity</td>
<td>Countless</td>
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<tr>
<td></td>
<td>1</td>
<td>Commodity with cost disadvantage</td>
<td>Countless</td>
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</tbody>
</table>
In a product pyramid profit model, meeting customer preferences of style, colour, price, etc., is of utmost importance. It is exactly the variations in customer income and preferences that make it possible to build a product pyramid. At the base are low-price, high volume products. As the apex are high-price, low-volume products.

Most of the profit is concentrated at the top of the pyramid, but the base of the pyramid plays a critical strategic role in creating a “firewall” at the bottom. The firewall brand creates a barrier to competitors, and protects the rich profitability at the top of the structure.
Product Pyramid Profit (continued)
Switchboard Profit

Some markets are characterised by multiple sellers communicating with multiple buyers, with high costs incurred by both. In many cases, there is an opportunity to create a high-value intermediary that concentrates these multiple communication pathways through one point, one channel, by creating a switchboard. The switchboard reduces the costs to both buyers and sellers.

A powerful component of the switchboard model is that it builds on itself; the more buyers and sellers that join, the more valuable it becomes.
Switchboard Profit (continued)
Business model – gary hamel
CORE STRATEGY: HOW THE FIRM CHOOSES TO COMPETE

CORE STRATEGY

Business Mission
Product / Market Scope
Basis for Differentiation
STRATEGIC RESOURCES

Core Competencies
Strategic Assets
Core Processes
CONFIGURATION

CONFIGURATION

CORE STRATEGY

STRATEGIC RESOURCES
CUSTOMER INTERFACE

- Fulfilment & Support
- Information & Insight
- Relationship Dynamics
- Pricing Structure
VALUE NETWORK

Suppliers
Partners
Coalitions
You need a compelling story about how your business concept is going to make money. If you can’t describe how your business concept will produce above-average profits, you’re a comedian without a punch line!
Strategic architecture – ungerer et al.
In essence a business model represents the choices a firm makes on where to compete in which market space, with what products or services, by leveraging resources and capabilities for competitive benefits, to support a defined competitive position. The cumulative results of a participation, resource, and competitive strategy, is stakeholder value based on a profit strategy that benefits employees, communities and regulators.
1. Where are we going & where do we want to go?
2. What do we know?
3. What do we need to know?
4. What are we doing that works?
5. What are we doing that does not work?
6. What can we do to achieve our ambitions & overcome our problems?
7. What can we do that is new or different?
8. How do we transform these into active implementation & experimentation asap?

**SCAN & EXPLORE**
- Internal Environment
- External Environment
- Scenarios & foresight development

**FORMULATE**
- Core Aspirational Description
  - Core Strategic Philosophy
  - Vision
  - Mission
  - Values
- Participation Strategy
- Resource Strategy
- Competitive Strategy

**STRATEGY EXECUTION**
- Strategic themes/focus areas
- Strategy map: strategic goals
- BSC: strategic measures
- Improvement domains
- Portfolio of experiments & prototypes

**STRATEGY INNOVATION**
- Business model innovations
- Internal & External sense-making
- Strategic dialogues

**ENQUIRE & QUESTION**
- Business Model
- Profit Strategy
- Scenarios & foresight development

**STRAIGHT INNOVATION**
- Competitive Strategy
- Resource Strategy
- Participation Strategy
- Participation Strategy

**STRATEGIC COMPLETION**
- Internal Environment
- External Environment
- Scenarios & foresight development
READING THE BASIC BUSINESS MODEL

Internal environment context
- Financial analysis
- Internal value chain
- Core competencies & capabilities
- Product positioning analysis
- Strategic issues

Resource strengths & weaknesses

External environmental context
- Industry
- Competitors
- Customers

Market threats & opportunities

Resource Strategy

Business Model

Profit Strategy

Participation Strategy

Competitive Strategy
Support the analysis with other strategic tools & techniques, i.e. some of the **future thinking tools** and methodologies like Scenario work. The idea: use these tools and methodologies to get clear themes of how the future may look. Contrasted with this we also need a **current perspective** to contrast with our future themes, to identify strategic priorities. It is therefore beneficial to clearly **formulate both the future and the current perspectives** for each of the 3 areas.

**Main idea:** form a clear contextual understanding of the external environment in which a specific business concept should work.
A System is a perceived whole whose elements “hang together” because they continually affect each other over time, and operate towards a common purpose.

Peter Senge
Participation Strategy

Customer Selection
Product/service spread
Channel / delivery
Geography

This spells out our chosen business domain.
PROFIT MODEL

- Income Streams
- Cost Drivers
- Pricing Approach Per target market
- Cost of Capital
- Efficiency Ratio trends
Business model canvas –
osterwalder & pigneur
## BUILDING BLOCKS FOR YOUR STRATEGIC ARCHITECTURE

<table>
<thead>
<tr>
<th><strong>Partner Networks</strong></th>
<th><strong>Key Activities</strong></th>
<th><strong>Customer Value Proposition</strong></th>
<th><strong>Customer Relationships</strong></th>
<th><strong>Customer Segment</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>Who are our key partners given our offering?</td>
<td>What are our key activities, given our offering?</td>
<td>What value do we create for our customer segments?</td>
<td>How do we create a strong relationship with our customers?</td>
<td>Who do we serve? Who is our customer? What segments have we been mandated to serve?</td>
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<tr>
<td>What do we outsource and what do we insource?</td>
<td></td>
<td>What product, service, brand, image, quality do we provide?</td>
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<td>What higher order needs do we serve?</td>
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<tr>
<td><strong>Key Resources</strong></td>
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<td><strong>Distribution Channels</strong></td>
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<tr>
<td>What key resources do we need given our offering?</td>
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<td>What do we get the CVP to the Customer Segments?</td>
<td>How do we communicate?</td>
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<tr>
<td><strong>Cost Model</strong></td>
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<td><strong>Revenue Streams</strong></td>
</tr>
<tr>
<td>What are the main cost items of our business model?</td>
<td></td>
<td></td>
<td>Where do we get our money from?</td>
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<td></td>
<td></td>
<td>How do we make money?</td>
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</table>
Expanding on the Value Proposition

Could the value proposition be combined with something else?

Broader Value Proposition

Original Value Proposition

Narrower Value Proposition

Could any of the parts be valuable by itself or combined differently?
When searching for valuable assets and capabilities, it is important to not only focus on own business model and industry, but also the potential need of others:

• How can we strengthen our own value propositions?

• How can we strengthen others' value propositions?

• How can we create joint value propositions with others?
Working on the CVP

How well is the value proposition of your segment aligned with customer needs?

(-5) Value propositions and customer needs are misaligned
(+5) Value propositions and customer needs are aligned

Please evaluate the synergy between the products your segment sells and the services it offers.

(-5) There is no synergy between our products and our services
(+5) There is strong synergy between our products and services

What is your perception of our customer satisfaction levels? (How satisfied are our customers?)

(-5) We have frequent complaints
(+5) Our customers are very satisfied
Working on the Customer Segment

(-5) Our customer base is unsegmented

(-5) We have short-term client relationships with low retention rates

(-5) We are failing to acquire new clients

(+5) Our customer base is well-segmented

(+5) We have long-term client relationships with high retention rates

(+5) We are continuously acquiring new clients
Working on the DC

Are our distribution channels effective? (Adequate to accomplish a purpose; producing the intended or expected result.)

(-5) Our communication channels to customers are not effective

(+5) Our communication channels to customers are extremely effective

Are our distribution channels efficient? (Performing or functioning in the best possible manner with the least waste of time and effort)

(-5) Our distribution channels are not efficient

(+5) Our distribution channels are extremely efficient
# Working on the Resources

## Strength of key resources

<table>
<thead>
<tr>
<th>Score</th>
<th>Description</th>
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<tbody>
<tr>
<td>-5</td>
<td>Our key resources are easily replicated</td>
</tr>
<tr>
<td>-4</td>
<td>-3</td>
</tr>
<tr>
<td>-2</td>
<td>-1</td>
</tr>
<tr>
<td>+1</td>
<td>+2</td>
</tr>
<tr>
<td>+3</td>
<td>+4</td>
</tr>
<tr>
<td>+5</td>
<td>Our key resources are difficult for competitors to replicate</td>
</tr>
</tbody>
</table>

## Stability of resources

<table>
<thead>
<tr>
<th>Score</th>
<th>Description</th>
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</thead>
<tbody>
<tr>
<td>-5</td>
<td>Resource needs are unpredictable</td>
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<tr>
<td>-4</td>
<td>-3</td>
</tr>
<tr>
<td>-2</td>
<td>-1</td>
</tr>
<tr>
<td>+1</td>
<td>+2</td>
</tr>
<tr>
<td>+3</td>
<td>+4</td>
</tr>
<tr>
<td>+5</td>
<td>Resource needs are predictable</td>
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</table>

## Fit for purpose

<table>
<thead>
<tr>
<th>Score</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>-5</td>
<td>Key resources are not deployed in the correct areas and do not function</td>
</tr>
<tr>
<td>-4</td>
<td>-3</td>
</tr>
<tr>
<td>-2</td>
<td>-1</td>
</tr>
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<td>+1</td>
<td>+2</td>
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<tr>
<td>+3</td>
<td>+4</td>
</tr>
<tr>
<td>+5</td>
<td>Key resources are deployed in the correct areas and function</td>
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</table>
ACHIEVE PRODUCT-MARKET FIT WITH THE VALUE PROPOSITION CANVAS
• The Value Proposition Canvas: helps design, test, and build the Value Proposition to Customers in a more structured and thoughtful way.

• The Canvas focuses on the big picture.

• The Value Proposition Canvas zooms in on the Value Proposition and the Customer Segment, to describe them in more detail and analyze the “fit” between them.

• Companies need to get both right: the “fit” and the business model.

• The tools work best in combination. One does not replace the other.
Achieving Fit

• The goal of the Value Proposition Canvas: assist in designing great Value Propositions that match Customer’s needs and jobs-to-be-done and helps them solve their problems.

• This is what the start-up scene calls product-market fit or problem-solution fit. The Value Proposition Canvas helps you work towards this fit in a more systematic way.