

BUSINESS STRATEGY REFLECTIONS ON BUSINESS MODEL CREATION

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Summary: *The essence of “business strategies” and “business models” has been a major area of research in strategic management throughout the past thirty years. Raising the assumption that these two managerial notions are vitally connected and sequential, this article aims to examine how business models are created under different business strategy types, therefore, analyzing the importance of each business model component to each strategy category. Regarding this concern, large amount of secondary data has been accessed and elaborated, and numerous real-life examples have been used to demonstrate the proposed connection. While theory suggests that each strategy type brings its own business model composition, results also confirmed that companies pursuing different strategy, need to put emphasis on different and specific business model components in order to reach market success.*

Keywords: *business model, business strategy, operational excellence, product leadership, customer intimacy*

1. INTRODUCTION

Understanding the concepts of “business models” and “business strategies” have continuously magnetized great interest in both literature and practice. A large body of data confirms that clearly stated strategy and a holistic and well defined business model are the heart of any company, regardless of its size, industry or operational environment [1], [2]. Perhaps one of the more significant contributions to the development of business model structure came specifically from the work of Osterwalder and Pigneur [3]. They suggested a comprehensive business model framework composed of nine business model blocks: Key partners, Key activities, Key resources, Value proposition and Cost Structure (on the left-cost side), and Channels, Customer relationship to deliver the value to the Customers and earn Revenue streams (on the right-revenue side). They are also displayed in a conceptual model illustrated by Figure 1. Furthermore, besides the legendary role of Porter in the field of strategic management, a remarkable view on this focus has also been presented by Treacy and Wiersema [4], introducing three basic business strategies: operational excellence, product leadership and customer intimacy. However, despite the importance of business models and business strategies as completely separate issues, few researches have studied their core interdependences and the importance of their mutual power when deciding on company strategy, and consequently, when composing the company business model. The question remains how the pursued business strategy shapes the business model of the company. Based on the work of Osterwalder and Wiersema, in this paper, we

provide a descriptive approach to three parallel relations: business model structure under the rules of operational excellence, product leadership and customer intimacy business strategy. The remainder of the paper is divided into three sections, carefully elaborating the three presented relations, thereby emphasizing their core influences through real-life practical illustrations.

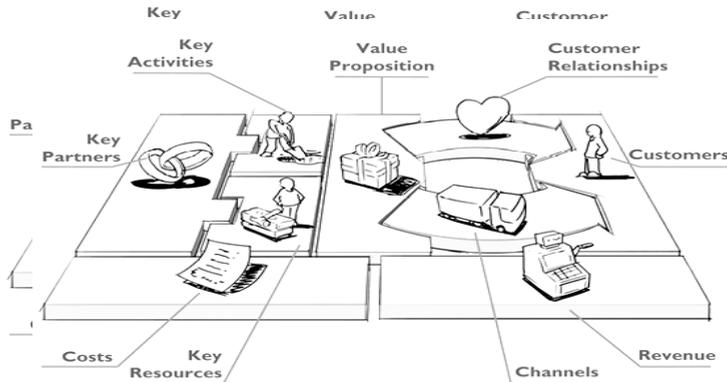


Figure 1. Osterwalder & Pigneur's Business Model Blocks

2. BUSINESS MODEL COMPONENTS PUSHED FORWARD AT OPERATIONAL EXCELLENT COMPANY

Generally, companies create business models in correspondence to their pursued business strategy. Thus, drawing on operational excellence insight, the business models at operational excellent companies, are significantly specific and modified by the core principles of the operational excellence strategy. It is noteworthy mentioning that even companies with same business strategy may establish a competitive advantage on the market by operating under a diverse business model. [5]. Regarding Osterwalder's nine building blocks operational excellent companies shed light on three basic components on its business model: 'key activities', 'distribution channels' and 'key partnerships'. Therefore, in terms of 'value proposition' operational excellent business model unhesitatingly sets 'lowest price', and in terms of 'customer segment' this business model concentrates on 'mass market'. Many business models of operational excellent companies have become legends during the recent few decades (Dell, IKEA, Wal-Mart, Southwest Airlines, and Amazon). Nevertheless, it is of high relevance to acknowledge that the key activities at this type of companies are primarily concerned with patterns and ways of cost reduction, in order to leave the competition behind in term of price and convenience.

Southwest Airlines is a company that organizing properly its 'key activities' succeeded in making the profitability of the company even more than excellent. As the value discipline suggest, the company focuses on what it perceived its customers value at most. It focused on target groups that buy ticket to get a flight, rather free food, cocktails and other additional services. Southwest Airlines focuses on its key activities including efficient operations to drive its low cost structure and exceptional delivery of customer service with low prices. Pointing to its methods of a smart cost reduction, Tomas and Kent [6] entitled the

Southwest strategy as Porter's Cost Leadership strategy. However, its culture and management's vision clearly show that the company follows a much broader concept while maintaining its operations. Thus, although the low priced flights may be achieved by using cheap equipment or paying low wages, Southwest Airline had chosen to reduce its costs by operations focused on efficiency and most important quick turnarounds of its aircraft at the gates. Southwest's culture is more than a low cost preoccupation. It is deeply settled in its core internal relationships, referring to shared values, shared goals and knowledge [7]. The discount-flight model of Southwest has been inspiration for many other airline companies, striving to achieve operational excellence through straight focus on their key activities. However, if not combined with an appropriate operational excellence culture, the results may reach much lower scale.

In addition, another success story of operational excellence business model is the experience of Dell. As Treacy and Wiersema [8] acknowledged in one of their value discipline articles, Dell chose a totally different approach to the market, while assuring its operational excellence. The young founder had realized the opportunity to outperform competitors by focusing not on prime products, but on an appreciably novel distribution channels. In fact, Dell put into use a direct business model, selling PCs directly to end users, following effortless and simple internet order. Moreover, what brought Dell to excellence are the actual elimination of intermediaries in its key activities, as well as removal of the inventory costs and sale force wages of the overall production-sale process [9]. In the work of Morris et al. [10], Dell philosophy is broadly explained as "elimination of intermediaries, systems built to order, highly responsive customer service, moderate margins, rapid inventory turnover, speedy integration of new technologies, and a highly efficient procurement, manufacturing, and distribution process" (pp.727). On the other hand, while great number of authors categorized this company as operational excellent, there is an interesting point in the literature referring that Dell's success is more greatly dependent on its Customer Intimacy elements of operations, [11]. In the relevant article exists detail explanation on the benefits derived from the information that Dell gathers in its direct communication to customers and the real-time feedback loop that Dell enjoys out of that process. The point is further supported by statistical facts, showing that Dell's intimacy factor contributes to its profitability 40% more than its low-cost, direct-distribution business model. The question whether the company is mastering on both operational excellence and customer intimacy strategies will remain issue for additional research.

While Southwest, Dell and other similar companies focus on its 'key activities' and 'distribution channels' in order to build business model that reaches operational excellence objectives, there are other companies like Wal-Mart and IKEA that rely on their 'key partnerships' components of their business model. Wal-Mart drives its path to operational excellence with incredibly sophisticated and bright partnership with its suppliers. It has created an integrated system with suppliers that enable goods to move faster from supplier's factories to Wal-Mart shelves, than between departments in other companies [4]. With the information technology as support for efficient operations within the company and "everyday low prices" approach to targeted wide group of customers, Wal-Mart calmly enjoys the fruits of operational excellent strategy, mainly based on the benefits of the 'key partnerships' business model component [12]. Another case of company relying on the benefits of its key partnerships is IKEA. Similar to Wal-Mart, IKEA uses its external relationships in order to improve its efficiency on daily basis. The company involves

its suppliers into complex and lasting upgrading projects with an objective of becoming co-producer of the initial supplying products [13]. This partnership means a fortune in terms of cost control and quality assurance. Additionally, IKEA has a unique partnership relations with its customers. More specifically, the company very wisely uses its customers as they are its own employees. For example, when people go to furniture stores there is kind staff to serve them (price included), whereas in IKEA customers serve themselves. In other stores the furniture is assembled by workers and delivered to customer's homes, but in IKEA customers turn into IKEA's employees and assemble and transport the goods by themselves [14]. Saving on staff, warehousing, transportation and many other carefully studied issues IKEA is able to deliver to its customers what they value the most-low prices for stylish furniture [15].

In light of the above mentioned, operational excellent companies that rely on their "Key Activities", "Key Partnerships" and "Distribution Channels" business model components, may easily achieve both, low cost and master position on the market.

3. BUSINESS MODEL COMPONENTS PUSHED FORWARD AT PRODUCT LEADERSHIP COMPANY

Companies pursuing product leadership strategy are victims of extreme and rule breaking innovation. Namely, the costs incurred during the process, as well the prices charged for the outcomes, are never in the center of the attention. The number of companies that have succeeded following this direction should not be disregarded. Microsoft, L'Oreal, Harley Davidson, Nike, Swatch, Apple... may all be complemented for the terrific performance in the product leadership world. The theory suggests that business strategy determines the operating business model that will work toward the achievement of the settled strategic goal. By default, the business model of product leadership strategy, sets the 'segmented market' as a group of customers to be served, and 'best product/service' as 'value proposition' to be delivered. Furthermore, product leadership companies explicitly focus on the "key resources" component of the Osterwalder's building blocks at the general business model canvas. More explicitly, product leadership companies set the financial investment (NPD, R&D and constant innovation), and the investment in human and intellectual assets (professionals, researchers, scientists), as spotlights of their success.

A remarkable example of this strategic approach is L'Oreal Company. The business model of this company is completely reliant on taking great advantage of its 'key resources', therefore focusing on enormous attention to constant innovation with huge amounts invested in research and a team of unexceptionable professionals who works on impressive products. These issues are present at any detail of L'Oreal operations. It is a company always thinking for the future, in terms of product development and improvement of the current brand portfolio. At the same time, the company shows precise attention on introducing on the market new inspiring products [16]. L'Oreal has always been making a greater financial commitment to R&D, than its competition, and this activity has always been perceived as L'Oreal's icon. The origins of its scientific passion are set at the beginning of the L'Oreal Company, and have been the basic working principal of its founder. It is the professionalism and experience of the management team always to recognize a gap on the market and invest in heavy Research and Development, to produce such an innovative product that will satisfy the uncovered market need. Therefore, it is crucial to take into

consideration that L'Oreal researchers work hard to achieve this expertise. In this regard, they work not only on creating new products for the markets, but they deeply explore the markets in multiple dimensions. Additionally, they have outsourced a team in the field of social science to explore the preferences, expectations, and negative responses of the targeted clients [17]. This outstanding position on the market in terms of leading innovative role is strongly supported with intense financial arrangements. L'Oreal is spending 3% of its annual revenues on innovation, while the industry average is below 2% [18]. The relation is more than evident-to be first in innovation, also means to be first in innovation costs. Namely, it has perfect teams of experts in the field, proven during almost a century of work, and teams that deserve trust. In 2006, the company had approximately 2.800 scientists who were working hard for L'Oreal's future. As Verviere and Revollo [19] stated in their article: "The best way to predict the future is to invent it", (p.2).

Another remarkable example of product leadership company is the unbeatable Harley Davidson Company. This company works more than a century on developing motorcycles with an extreme superior value. Their choice for following the PL strategy has shaped their entire business model as well. Regardless costs and prices, the company concentrates on continuous improvement and exploits its human and financial resources nearly to extremes. Their business model and business philosophy are entirely drawn by the product leadership strategy, with the intention to building their best bikes better. Their committed investment in product improvement has sustained the company at the top for more than 100 years. The intrinsic quality, classical design with unique performance improvements has created a brand obsession [20]. This, in fact, is the gains from the enormous investment in R&D and tireless work of company's professionals. Kotler [21], characterize this company as masterpiece of innovation and uniqueness. He stresses that with buying Harley Davidson people do not buy motorcycles, they buy lifestyle. Nevertheless, besides the necessary financial investment, Harley Davidson Corporation acknowledges the even greater importance of great people - individuals who will challenge the status quo, and who are creative, collaborative and accountable. They are committed to investing in preparing strong leaders who will live with the company's values and deliver them on a daily basis [22].

In this context, the innovative and product leadership elements contained in the Apple high-tech company's structure are remarkably evident [23]. Apple's business model is completely based on the utilization on its key resources (mainly research spending and professionals salaries). The invested amounts in R&D, innovation sessions and high-profile professionals are far over the ordinary limits. Morrison [24] retells the Apple employees' stories of the spending on costly overhauls in order to improve a tiny application on an existing product. They also indicate that other greatly sophisticated products have been completely eliminated due to their inaptitude with the existing idea. Regarding Apple employees, Muller [25] points out that they rely mostly on the cornerstones of communication, open-mindedness, collaboration and people's excitement to express ideas freely. Muller [25] also explains that the company tends to empower its innovative and creative people. In this way employees become even more passionate about every particular detail of Apple's products. The master management position leads the whole product leadership spirit of the company. Apple's CEO, Steve Jobs, who left the company in August 2011, because of serious health problems, was the genius leader of the world's top innovative company. Roya [26] evaluates his style as thinking beyond gadgets. Apple's introduction of the iPod, iTunes Store and iPhone, started writing a new technological history.

4. BUSINESS MODEL COMPONENTS PUSHED FORWARD AT CUSTOMER INTIMATE COMPANY

Happy customer at all costs is the main pillar on which customer intimacy strategy is based on. Accordingly, the business models of the companies pursuing this strategy should be completely modeled in order to satisfy this objective. In this regard, companies that have made their customers happy are: Four Season Hotel, Airborne Express, Home Depot... As far as the Osterwalder's business model components are concerned, customer intimate companies set 'niche market' as input to 'customer segment' component, and 'best total solution' as value proposition to be delivered to customers. Furthermore, customer intimate companies create their business models with a clear emphasis on the 'Customer Relationship' building block. In fact, this component of the business model crystallizes the type of relationship that company will establish with its customers. Considering this, customer intimate companies establish personal assistance, as well as dedicated personal assistance relationship with its clients. In the world of hotel industry, the Four Season Hotel and Resort, has succeeded by creating a business model completely concentrated on its personal assistance with its guests. In the work of Talbott, [27], personal assistance service at Four Seasons is explained as a source of superior profitability, reputation and growth. Furthermore, the author enlighten that the company uses the personal service as a competitive advantage against competitors, since its foundation in 1961. Spending unlimited time in explaining locations to lost customers on phone, welcoming the guests with unpretentious kindness, pronouncing their names correctly, limousines carrying forgotten item to airports and design with fine china, silver and fresh flowers, is what is perceived as warm and welcoming by Four Seasons [28]. On the other side of the 'customer relationship' business model components are the actual employees who serve the pleased customers. This company has always taken great care about its staff of all levels in the organization, recognizing the contribution to high-end service, as a merit of the manager, but doormen's as well. In their annual report of 2009, they announce:

"We depend on the continued services of key managers and employees. If we do not retain our key personnel or attract and retain other highly skilled employees, our business will suffer [29]".

Martin [30] gives a more precise details on company-employees-guests relations. According to him, company pays same level of attention to complains from its employees as to complain from the guests. Four Seasons Hotel compensates its employees with a good salary, career paths and promotions, sound retirement plans, bonuses and respect. In return, employees provide hotel's guests with a superior courtesy and personalized customer service. Respectfully, the Four Seasons Hotel, after fifty years of deep concern about the personalized service of its deferential customers, has been awarded with AAA-Five Diamond Hotels and Resorts Award for year 2011.

Home Depot is another example of a distinctive customer devoted company. With a business model based on a core relationship with customers, Home Depot has reached to become the biggest home-improvement retail store in the world. Its customer intimacy business model is based on few customer intimacy milestones. Nevertheless, this has not always been the case. In the period near 2005, the company operation has been lead by do-it-yourself philosophy and has seemingly suffered from poor customer service. However, with the change of its CEO, the business model and philosophy changed as well [31].

The new CEO, Marvin Ellison, brought back the focus on customer and mastered customer service, which showed remarkable results. Moreover, he introduced the “Customer FIRST” curriculum, which all the manager and staff had to maintain in order to ensure that their customers leave the store satisfied. Treacy and Wiersema [4] explain the Home Depot way of treating customers even earlier. They indicate that company’s clerks spend whatever time is required to solve a specific customer problem and bring best customer solution, regardless it is a 59\$ or 59 cents product. The Home Depot goal is to provide the best customer service in the industry. Therefore, management has approached simplifying tasks, so that employees have more time with customer, to give enhanced customer service. Moreover, they provide in free store expertise advice, professional onsite installation, deployment of FIRST phones (so that customer receive close attention at any meter squared in the store), personalized credit cards and interactive web site, are only a insights into the whole Home Depot-customer relations [32].

These are only few examples of match between the Treacy and Wiersema’s Customer Intimacy strategy and Osterwalder’s ‘customer relations’ business model component.

5. CONCLUSION

A large body of secondary data referring to specific business model’s components used by operational excellent, customer intimate and product leadership companies have been assessed. The business model created by each of the three strategy types radically differ. In fact, companies create different business models in order to achieve the specified position on the market. Accordingly, business models mainly focus on “Key partnerships”, “Key activities” and “Distribution channels” components when refer to companies operating under the rules of operational excellence. Moreover, in the case of product leadership companies, the greatest attention has been addressed to the “Key resources” business model component. The success of these companies deeply depends on the intensive investment in creating new products and services and designing new worlds. Besides the spending in technology and R&D processes, product leadership companies would not be able to flourish without the bright minds of their extremely innovative people. Therefore, it becomes fairly evident that firms chosen to follow product leadership strategic approach should entail the whole business model to an intense usage of financial, human and intellectual resource in order to provide the customers with constant stream of cutting-edge products and experiences. Finally, the customer intimacy business strategy is specifically more customer-attention demanding. Through brief elaboration of customer intimate company’s philosophy, we may certainly conclude that in order to reach close customers relations and to be able to offer specific rather than general solutions to customers, the business model of the company need to be focused on intense and profound attention to its targeted customers.

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