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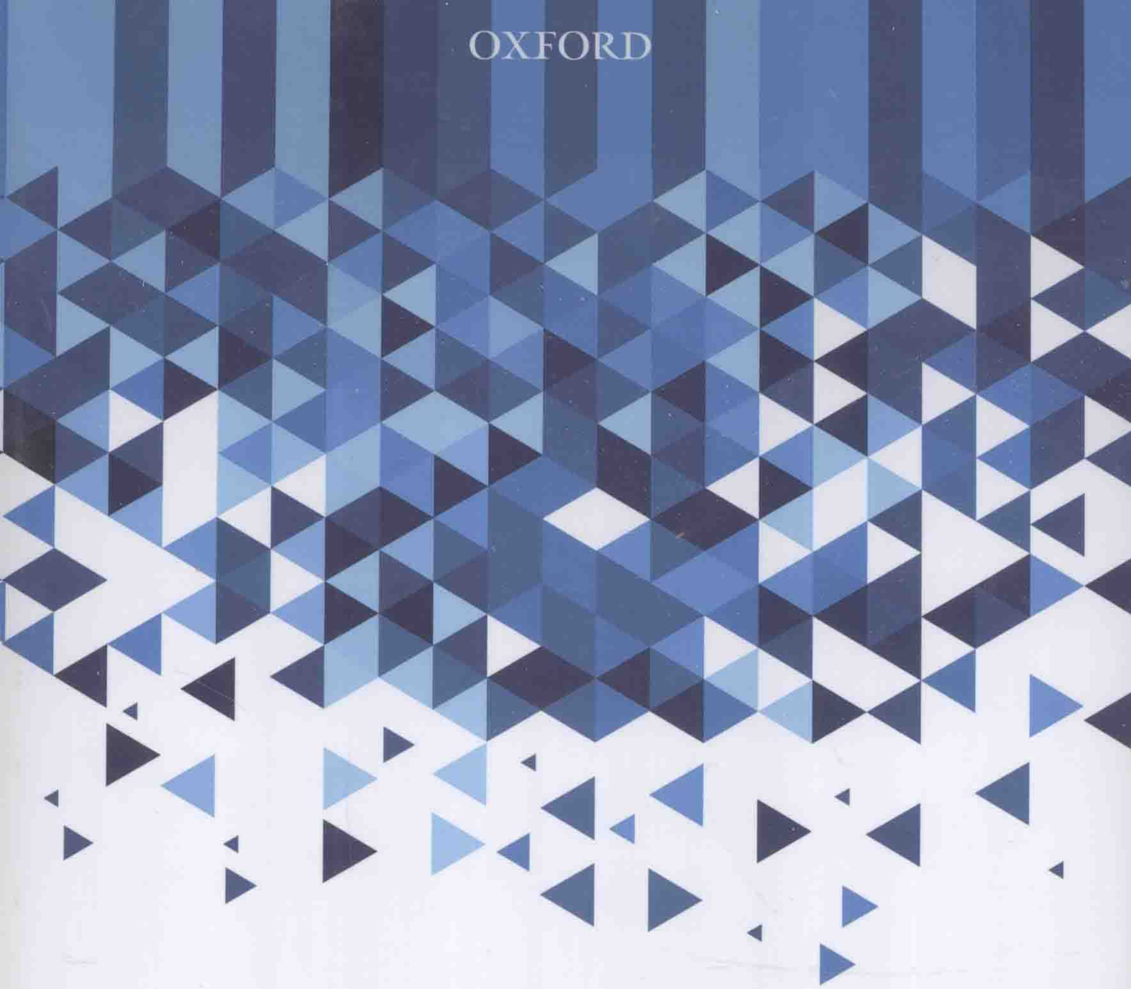

# BUSINESS MODEL INNOVATION

*the organizational dimension*

EDITED BY
NICOLAI J. FOSS & TINA SAEBI

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## The Organizational Dimension

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# Business Model Innovation

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# 1 Business Models and Business Model Innovation

## *Bringing Organization into the Discussion*

NICOLAI J. FOSS AND TINA SAEBI*

## Introduction

The notion that companies have "business models" has become extremely influential, although perhaps still more so in the communication of business people and in the business press than in the management research literature. And yet, the latter literature has most definitely taken off within the last decade. With over 1,200 articles published in peer-reviewed academic journals between 1995 and 2010 addressing the notion of business models since (Zott, Amit, and Massa, 2011), the business model construct has gained substantial currency across strategy, entrepreneurship, and innovation literatures. There is little doubt that the construct resonates within several, overlapping communities, both practice-oriented and scholarly.

Much of the attraction of the business model construct arguably lies in its holistic approach. Thus, business models are sometimes characterized as mental constructs—presumably mainly residing in the upper managerial echelons of a company—that define the structure of the interlocking activities associated with key strategic choices. The relevant strategic choices relate to the firm's fundamental value proposition(s), the markets and market segments it addresses, the structure of the value chain which is required for realizing the relevant value proposition, and the mechanisms of value capture that the firm deploys, including its competitive strategy. Teece (2010: 172) summarizes this by stating that 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."

* We gratefully acknowledge support from the Center for Service Innovation at the Norwegian School of Economics, where Tina Saebi has been employed as a Post-doctoral Research Fellow. We also thank Anders Pico for efficient editorial work.

It is intuitive that this "manner" can be highly firm-specific and may thus serve to differentiate the firm in the marketplace. It is similarly intuitive that because of this firm-specificity and the underlying complexity that a business model contains, advantages associated with such differentiation may be hard to eliminate (e.g., by imitation) by the competition. Along similar lines, the firm that possesses a successful model may also be in a privileged position to change, renew, and even innovate that model. Such thinking has not been lost on the business community: Surveying more than 4,000 senior managers, a global survey conducted by the Economist Intelligence Unit (2005) found that the majority of managers preferred new business models over new products and services as a source of future competitive advantage. Similarly, an IBM survey (IBM Global Business Services, 2006) confirmed that managers increasingly perceive innovative business models as the key to sustained competitive advantage (Amit and Zott, 2012).

However, in spite of such massive resonance, in the academic as well as the practitioner community, much, and perhaps most, of the extant literature on business models and the innovation thereof suffers from deep-seated conceptual problems, little cumulative theorizing, and a lack of a sustained data collection and analysis. Thus, definitions of the core construct proliferate (in fact, there is some definitional variation across the chapters in this book), scholars do not scrupulously cite each other, and single-firm cases dominate empirical inquiry. By most standards, this seems problematic. However, these are typical characteristics of an emerging field rather than characteristics of bad research, and there are reasons to optimistically expect that these characteristics will gradually disappear as research in business models becomes increasingly cumulative.

In any case, it may seem to be something of a stretch to add more complexity to an influential, yet emerging and complex discourse, as we do in this volume, pressing the argument that the literatures on business models and business model innovation need to embrace organizational theory (in a broad sense). And yet, we argue that bringing organizational considerations into the discourse has the potential to clarify and align rather than confuse. Consider again the notion of a "model." On one understanding of this notion, namely the one that engineers and social scientists (notably economists) ascribe to, a model is fundamentally a set of relations between variables designed to capture reality in an essential way. Note that those who think of a business model in terms of managerial cognition hold a similar view: The mental model represents the key relations between the key elements of the firm's business. The point here, however, is that a model goes beyond the mere elements or variables; it also includes the *relations* between those elements or variables. In a nutshell, *our key argument is that in the context of a company, these relations are fundamentally organizational.*

Relations are organizational in a trivial sense—namely, these relations are embedded in the firm. However, more substantively they are organizational in the sense that they involve decision processes and outcomes, communication, interdependencies, decision authority, performance assessment and key performance indicators (KPIs), rewards, job descriptions, implicit and explicit contracts, and so on. This is the stuff from which organizational structure and control are made. Indeed, some notions of business models (and, per implication, business model innovation) make this point implicitly. For example, Zott and Amit (2010) place organization centrally, namely as part of the very definition of a business model. Thus, they argue that business models can be understood in terms of transaction content (i.e., value propositions), transaction structure—and transaction *governance*. Of course, the governance part directly links to the organizational dimension (Williamson, 1996).

Teece (2010) argues that the "architecture" of the firm's value creation and appropriation mechanisms is the hallmark of a business model. Although Teece does not specify this, an important part of an architecture is the organizational structure and control that supports the activities that allow the company to make its value proposition to the marketplace and embed the human and social capital that, with other resources, add value in those activities. In this volume, Santos, Spector, and Van der Heyden (chapter 3) argue that business models are all about "How is it being done?" rather than "What is being done?," "What is the segment being addressed?," and "How is revenue being captured?" The underlying argument is that business models uniquely address "how" issues, whereas the other issues are treated in the extant body of literature on marketing and competitive strategy. In such an interpretation, business models are fundamentally about the activities under the control of the firm that allow it to exploit an identified opportunity in the marketplace, and therefore also the structures and relations between the firm and its multiple stakeholders that support the value creation and value-capturing processes of the firm. Similarly, George and Bock (2011: 99) note that a "business model is the design of organizational structures to enact a commercial opportunity." In this volume, Birkinshaw and Ansari (chapter 5) even coin a new term for this organizational dimension of the business model, namely the "management model": "A firm's management model is the choices it makes about *how* work gets done—how activities are coordinated, how decisions are made, how objectives are set, and how employees are motivated."

Another fundamental organizational issue relates to the question at what level in the organization a business model exists. The literature does not provide any clear-cut answer to this. In this volume, Casadesus-Masanell, Ricart, and Tarziján (chapter 4) argue that business models exist at the level of business units. They may, however, reflect overarching corporate models.

In sum, scratching the surface of the business model construct immediately raises all sorts of fundamentally organizational concerns. In the remainder of this introductory chapter we discuss why it is important to link business models and business model innovation to the "organizational dimension," and we discuss the role of organization as an antecedent and moderator of business model innovation. We end by surveying the various ways in which