REINVENT YOUR BUSINESS MODEL

New game.  
New field.  
New playbook.
New Business Models Aren’t Just for Startups

Once upon a time, new business models were considered the domain of startups that would disrupt incumbents.

New entrants such as Amazon, Google, and Facebook, as well as Starbucks, CarMax, Amgen, Tesla, Netflix and Salesforce all came into being largely by discovering new ways to generate value.

One study shows that the majority of companies to enter the Fortune 500 in recent decades did so through business model innovation.

In retail, discounters that, like Target, Walmart, and Amazon, entered the market with innovative business models accounted for 93 percent of the total industry market capitalization by 2016, having seized more than $300 billion of value from their old-line competitors.
INCUMBENTS CAN BE BUILT TO TRANSFORM

Established corporations can conceive, implement, test, and roll out world-changing products and services just as well as or even better than startups can.

Amazon itself is a prime example.
No longer a startup, the “everything store” company has continually created new business models for new growth markets—from e-books, to cloud services, to streaming media, to robotics, to its more recent foray into healthcare.
If you want to continuously revitalize the service that you offer to your customers, you cannot stop at what you are good at. You’d have to keep asking what your customers need and want, and then, no matter how hard it is, you’d better get good at those things.”

JEFF BEZOS, CEO, AMAZON.COM
Where is the White Space?

The term *white space* means uncharted territory or an underserved market. Serving a new customer an existing one in a radically new way. Creating an entirely new market—or significantly transforming an existing one.

The white space involves the range of potential activities not defined or addressed by the company’s current business model—the opportunities that exist outside its core that require a different business model to exploit.

The chance to seize white space presents a tantalizing opportunity. But it’s also an area where assumptions are high and knowledge is low—the opposite of conditions in the company’s core space.
Lockheed Martin Takes Off into Its White Space

Seeking new growth markets, Lockheed Martin has invested over $100 million to build a helium-filled “hybrid airship” unlike anything ever before built. The airship can take off and land in small, unimproved spaces and carry a very large payload.

After successful test flights, management understood that the airship could generate substantial new growth. But not in the traditional way—or by targeting the traditional customer—that had made Lockheed so successful.

After all, Lockheed was optimized to excel in the relatively low-volume, high-margin world of multibillion-dollar fighter aircraft, missiles, and space satellites. It served one primary customer—the U.S. government—and its core was built on delivering complex solutions in a highly structured way, with margins defined in advance.

The hybrid airship would require a foray into the white space – and a very different business model that addressed:

- Who will be our customers?
- What problems do they face?
- How do we charge for the airship and turn a profit?
- What kinds of resources and processes will it take?
After a decade of development,

Lockheed has created a new business model targeting an entirely new customer—mining companies, freight companies, and others who need to transport huge payloads of cargo. It launched a new division, Hybrid Enterprises, with the new sales and distribution capabilities needed to sell the $40 million dollar airship.
The Four-Box Business Model

A business model is a representation of how a business creates and delivers value for a customer while also capturing value for itself, doing so in a repeatable way.

When you deconstruct any business model, you can see four distinct yet interdependent elements:

1. **The Customer Value Proposition (CVP).** A customer value proposition helps customers more effectively, reliably, conveniently, or affordably solve an important problem (or satisfy a job-to-be-done) at a given price.

2. **Key Resources.** The people, technology, facilities, equipment, funding, branding, and raw materials required to create the product or service and deliver it.

3. **Key Processes.** The means that people in organizations develop to produce and deliver products in repeatable, scalable, and sustainable ways.

4. **The Profit Formula.** How the company creates value for itself and its shareholders. It includes a revenue model, a cost structure, a target unit margin, and resource velocity.
Successful businesses devise a relatively stable system in which these elements interact in consistent and complementary ways. A change to any one of the four affects all the others and the system as a whole.
Medtronic Unlocks an Emerging Growth Market

India, which makes up 16 percent of the world's population, accounts for more than half the globe’s heart disease. But there were steep barriers in the way of Medtronic selling pacemakers and other life-saving heart products in the country:

- Lack of awareness of heart health and solutions.
- Lack of health insurance or reliable care pathways.
- Lack of access to proper diagnostics.
- Lack of affordability.

To blueprint a new business model for India, Medtronic relied on four building blocks to build a new venture called “Healthy Heart for All”:

- **Go direct-to-patient**: reach out through a toll-free hotline posted on billboards, ads on trucks, in social media and text messaging, inviting patients to free diagnostic events.
- **Engage the ecosystem**: work with industry stakeholders to raise awareness and drive participation in the program.
- **Manage the pipeline**: set up screening camps with telemedicine technologies such as wireless relay of ECG results and other tools that directly identify patients.
- **Ensure affordability**: create the first-ever consumer financing plan for pacemakers.
The linkage between these four elements is what created our business model. We’re scaling it up very rapidly, to the point where this becomes the default business model, the standard of how we deploy cardiac therapies in India. This will be fundamental to our growth in the future.”

Omar Ishrak, CEO, Medtronic
A powerful, focused CVP is the keystone of all successful business models. A great CVP:

1. identifies an important, unsatisfied consumer problem, or “job to be done,” and then
2. proposes a focused product or service (or combination) that delivers it in the right way at a given price. Before you can design a great CVP, you must first thoroughly understand your target customer’s job-to-be-done.

Whole Foods reached out from its crunchy-granola core to serve a customer looking for a new focused job-to-be-done:

“Give me full and pleasurable access to a variety of foods and products that meet my high standards for quality and honor my interests in health, organics, and protecting the environment.”
Whole Foods Market

From its start as a single store in Austin, Whole Foods has targeted the job of “I want to eat healthier,” attracting customers willing to pay higher prices for higher-quality, often organic, fresh vegetables, meats, fish, and prepared foods.

To deliver its game-changing CVP, Whole Foods had to build a supply-chain system unlike any that then existed in the grocery business.

Essentially, Whole Foods inverted the established supermarket model. It relies not on volume but on higher prices and higher margins on the perishables, which its customers buy in large quantities.

By considering the customer experience an integral part of its CVP and devising the appropriate profit formula to satisfy it, Whole Foods commands the higher margins it needs to satisfy its customers’ job-to-be-done.

How has the Whole Foods model changed since the acquisition by Amazon.com in 2017 for $14 billion? One way involves marrying the delivery resource to the CVP: Amazon announced it will offer free two-hour delivery of Whole Foods groceries in four U.S. cities. The plan is to expand same-day delivery nationwide.
FOCUS ON
The Profit Formula

This is the economic blueprint that defines how the company will create value for itself and its shareholders. It in specifies the assets and fixed cost structure, as well as the margins, volume, and velocity that are required to cover them.

Discount retailers generate profits despite discounted pricing by turning inventory even faster. Amazon has taken this to a new level. Combining digital technologies with just-in-time supply-chain management, the company dramatically reduced the time held a book in inventory, from an industry average of 168 days to 17 days at Amazon. This maximized the return from its working capital.
Disruptive startups are attracting your least profitable customers with a simpler solution.

Increased competition is causing margins to shrink or revenue to decline.

Consumer behavior is changing, causing shifts in market demand.

Discontinuous new technology is enabling a new way of creating and delivery products and services.

Dramatic shifts in regulatory policy changes the rules of the playing field.

You want to preempt any of the above from taking root, so you seek to disrupt your own markets before others do.
Artificial intelligence, robotics, 3-D printing, drones, and big-data analytics...

THE DIGITAL TRANSFORMATION IS CHANGING OUR WORLD.

But while technology is a great enabler of transformative business growth, it cannot create it on its own.

Amazon and Netflix wouldn’t exist without digital technology, but what has driven their success is its willingness to venture into all its white spaces—between, within, and beyond—and explore new business models. Companies as varied as Microsoft and GE are venturing into their own white spaces.
HOW DIGITAL TECHNOLOGIES CAPTURE VALUE

While any technology without a viable business model can lead to a commercial dead end, digital technologies can drive the creation of value in bold new ways. These models fall under four broad categories:

- **E-commerce.** This category includes everything from Warby Parker selling designer eyeglasses to online consumers to Dow Corning’s Xiameter, which sells silicone to manufacturers.

- **Digital platforms** enable value-creating interactions between producers and consumers. Airbnb connects people who have spare rooms with people who are looking for a place to stay. In B2B, Salesforce.com, Adobe, and Microsoft stream applications to subscribers via the cloud.

- **Models that turn data into assets** use data management and analysis to derive value from access to, or ownership of, large volumes of proprietary data. Think of Google’s targeted advertising; the Weather Company (now part of IBM) delivers 26 billion weather forecasts a day to its subscribers.

- **Automation-enabled services** harness software to perform tasks formerly carried out by people—everything from the robots that pick and pack in Amazon’s warehouses to the autonomous vehicles from Uber or Google.
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Key Resources and Processes

The synergy between the key resources and key processes is as critical to the success of an enterprise as the key resources and processes are themselves.

**Key resources:** unique people, technology, products, facilities, equipment, funding, and brand required to deliver the value proposition to the customer.

**Key processes:** the recurrent, critical tasks—such as manufacturing, sales, service, training, development, budgeting, and planning—that must be delivered consistently.

The ability of Irish airline Ryanair It’s ability to provide a low-cost value proposition hinges on choices about its resources and processes:

- To service secondary airports
- employ a nonunionized workforce
- fly a standardized fleet
- maintain a spartan headquarters

This potent combination of resources and processes work together harmoniously to support Ryanair’s business model—a CVP of delivering radically discounted travel to customers through a profit formula reliant on high resource velocity and a low cost structure.
Dow Corning

When Dow Corning introduced a disruptive new business model aimed at selling its silicone products to customers online instead of through its high-touch sales force, it recognized the shift in the job-to-be-done of some of its existing customers before it could be disrupted by competitors or new entrants. It called the new business Xiameter.

Dow Corning was wholly acquired by The Dow Chemical Company in June 2016, and Xiameter is now poised for its biggest expansion yet, as it prepares to introduce a no-frills, web-order platform for all Dow Chemical brands. Xiameter will no longer be synonymous with silicone, but will advance its business model—one that has yet to be successfully replicated in its industry. Now called Consumer.Dow, its key strength remains its real-time inventory system and instant auto-confirmation.

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<tr>
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<th>Dow Corning</th>
<th>Xiameter</th>
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<tr>
<td><strong>Customer value proposition</strong></td>
<td>Customized solutions, negotiated contracts</td>
<td>No frills, bulk prices, sold through the internet</td>
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<tr>
<td><strong>Profit formula</strong></td>
<td>Negotiated prices, high overhead, high margin</td>
<td>Spot-market pricing, low overhead, lower margins, high throughput</td>
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<tr>
<td><strong>Key resources and processes</strong></td>
<td>• R&amp;D • Sales • Service orientation</td>
<td>• IT system • Lowest cost processes • Maximum automation</td>
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Successful Incumbents Face Particular Challenges...

The business rules, behavior norms, and success metrics that help to make an existing business model so successful can be poison to new business models. That’s because they act as invisible guardians of the current model. This can include:

- Limiting how far a project team will venture from traditional offerings, precluding new approaches to what can be sold (such as moving from a product to a service) or how an offering can be sold (such as moving from physical stores to the internet).
- Creating an organizational urge to “cram” new opportunities into the existing business model
- Impatience for growth at the pace and on the scale of the traditional core—growth initiatives—and the risk of prematurely killing nascent new ventures
- Rigged adherence to the current profit formula—for example, expected margins of the core enterprise can lead executives to reject out of hand the possibility of reinventing a business model with different margins
... But They Can be Overcome

- Top leaders must learn to recognize and overcome the influence of existing core business models in the pursuit of their corporation’s white spaces.
- Create dedicated teams to create new models and then protect and nurture them. Such teams should not be large, but they do have to be focused mainly on the new
- Empower these teams to create new rules and metrics, especially financial metrics.
- Create a strategy development process that is unfettered from the assumptions that drive its core.
- Resist the doctrine of marginal costs.
MAKING BUSINESS MODEL INNOVATION A REPEATABLE CAPABILITY

A company venturing into its white space without a clear framework for business model innovation is like a contractor trying to build a house with no blueprint.

How do you know if your new CVP requires a venture into your white space? You need a new model when you are faced with fulfilling a new customer value proposition. Only then are you ready for these three essential steps:

1. **Finding the Job to Be Done**
   To become truly customer-centric, you must stop asking your customers, “What do you need?” and start asking them, “What are you trying to get done?” This is the question that will set you down the road to a jobs-based approach.

2. **Blueprinting the business model**
   Having identified an important job-to-be-done for a customer, you then need to create a blueprint of the business model that will satisfy it, as we’ve discussed.

3. **Incubating and testing the model**
   To successfully incubate a new business, you must identify a foothold market, a small geographic region or customer group that will serve as the low-cost laboratory, representing the larger target market.

Most critically, you must keep the incubation effort free of interference from the core and the way it operates.
Business model innovation is most successful...

- In cultures of inquiry, environments in which new value propositions and ideas for new business models are met with interest and encouragement
- When managers recognize that a nascent business opportunity, no matter how different from the core it is, might be the key to the next big thing
- Where thinking big about ambitious opportunities is balanced by starting small and slowly incubating new ventures, testing assumptions, and making adjustments
- With a structured approach that embraces the high degree of uncertainty but minimizes the risk

Seizing the white space begins with a simple four-box business model framework.

But it leads to far-reaching implications for every organization that is navigating accelerating disruptive change.
ABOUT THE AUTHOR


ABOUT INNOSIGHT

The strategy and innovation practice of global professional services firm Huron, Innosight helps organizations design and create the future, instead of being disrupted by it. The leading authority on disruptive innovation and strategic transformation, the firm collaborates with clients across a range of industries to identify new growth opportunities, build new ventures and capabilities, and accelerate organizational change.

To learn how we help organizations unlock the power of business model innovation, get in touch with us at inquiries@innosight.com.

For additional insight and materials, please visit www.reinventyourbusinessmodel.com. Mark Johnson is available to talk with the press and organizations.
