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What can Strategy Learn from the Business Model Approach?

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ABSTRACT The use of the business model concept has grown dramatically over the past several years, yet it remains difficult to distinguish the concept from conventional strategy. Despite a lack of consensus on a definition of business model, proponents of the concept assert that it is quite different from strategy. We generate alternative definitions of the business model concept and compare these to the received strategy literature to determine where/if potential theoretical or empirical advances might be likely. We identify opportunities for business model concepts to yield theoretical contributions and highlight why the concept may be so attractive to entrepreneurs and managers.

Keywords: business model, firm performance, resource based view, strategy

INTRODUCTION

So, what can strategy scholars learn about strategy from the business model approach? It's clear that the amount of research devoted to business models has increased over the past decade, but we wonder: is the business model approach different than conventional strategy, or is this just 'new wine in old bottles?'. There is no denying that the use of the term 'business model' has grown dramatically over the last several years – and not just among practitioners, but among academics as well. In one way this is very surprising, since to date there is no widely accepted definition of this term.

Despite this lack of consensus as to what constitutes a business model, a vocal and dedicated cadre of researchers vehemently assert that the term business model represents a new and unique concept and is not equivalent to strategy (Amit and Zott, 2001; Casadesus-Masanell and Ricart, 2010; Zott and Amit, 2007, 2008). These authors readily concede the lack of consensus on a definition, arguing that this is fuelled by the

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relatively early stage of theoretical development as well as the rapid dissemination of the term across interest areas (Zott et al., 2011). Nevertheless, they remain certain that business models are distinct from strategy and that they do indeed contribute to the performance of firms, both new ventures and extant firms seeking to respond effectively to changes in the competitive landscape or to revitalize moribund strategic plans.

We posit that ultimately the business model approach, given its emphasis on interdependencies and multi-lateral connections, may provide more insight to managers and entrepreneurs who are grappling with the complexity of an increasingly interdependent environment in which to compete. While such complexity makes theory building difficult, it reflects the exigencies of individuals seeking to create and capture value for their firm. We note that this view is consistent with Lanzolla and Markides (2020) who provide the counterpoint article paired with our paper.

We review several definitions of business model and as we describe below, we then compare these definitions to extant strategy research. Doing so, we assert that there is a limited amount of theorizing that has not already been addressed in the various segments of the strategy field. However, through this process of carefully comparing strategy theory to the business model approach, we observe areas of inquiry that could be illuminated through the adoption of a business model lens.

For example, the business model, more than conventional strategy, adopts an individual decision-maker perspective. As such, we would look for possible contributions to flow from this, given advances in the micro-foundations of strategy (Barney and Felin, 2013; Felin et al., 2012) and cognitive framing (Kaplan, 2008; Kaplan and Orlikowski, 2013).

Finally, we acknowledge that given its popularity among practitioners, the business model approach may have a more lasting impact in strategy and entrepreneurship education. It may represent a more accessible vector for conveying fundamental strategy principles to students, entrepreneurs, and managers.

Is it possible to identify the distinctiveness of the business model concept from existing theories of strategy? One approach to answering this question is to identify alternative definitions of the business model concept currently in the literature, and then, consider whether or not these alternative definitions suggest important new avenues of theoretical and empirical research compared to the received strategy literature.

Definition One: Business model as a Firm's Theory of Value Creation

For example, business model may mean a firm's theory of how to generate and appropriate economic value. However, this is currently the most popular definition of strategy, so just substituting the words business model for the word strategy does not seem likely to be particularly fruitful theoretically or empirically.

Johnson et al. (2008) illustrate this approach to defining the concept of a business model. The four interactive elements of their business model concept are i) the customer value proposition, ii) the profit formula and iii) the necessary resources and iv) processes to implement the value proposition in an economically viable manner. To illustrate this definition of business model, they highlight an example of how a large manufacturing firm – Tata – overhauled its business model in order to enter a new segment of the market.

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Tata Group managers noted that the growing Indian middle class would gladly trade-up from a scooter to a sedan if one were available at a price point that was 50 per cent lower than current sedan prices. The challenge was to design and build a product that could meet that price point and still generate a profit.

Johnson et al. (2008) note that this meant the firm needed to start from scratch as they sought solutions to the problem of generating value for the customer as well as the firm. Using their four-factor definition of a business model these authors' highlight the steps it took to identify the customer value proposition- in this case the sight of middle class families attempting to navigate the crowded streets of India during a rainstorm on a scooter prompted a senior manager to recognize a problem for this growing and underserved group of customers. Next Tata leveraged its industrial design and manufacturing capabilities to create a product that could be offered at the lower price point and still generate a profit. This meant greater reliance on a small set of suppliers for components which Tata had not used before in any of its other vehicles. Such a business model innovation, the authors imply, led to the launch of a product that would not have materialized by relying on conventional strategic analysis.

However, this business model approach combines strategy insights from the work of Nickerson and Zenger (2004) in their identification of the problem as the unit of analysis, Porter (1996) in his thesis on competitive advantage and Barney (1991, 1996, 2001) on the identification and utilization of costly to imitate resources and capabilities.

Beginning with the identification of problem to be solved is common to both Nickerson and Zenger (2004) as well as Christensen and Raynor (2003). Both indicate that problems are chosen such that the firm will be able to capture value- either indirectly through capability development or directly through profit-generating solutions, or both. Yet the problem-solving perspective of Nickerson and Zenger (2004), Nickerson et al. (2007) and others does not disengage from strategy. This work uses the problem as the unit of analysis in order to connect with other core strategy areas such as governance, boundary of the firm, and value creation-value capture. This line of research does not invoke the term business model, yet it bears striking similarities to the work of Christensen and his colleagues.

Returning to the Johnson et al. (2008) illustration of their business model using the development of the Nano, these authors emphasize the ability of Tata to draw on the capabilities embedded within the firm to 'reinvent' their business model. The firm relies on a combination of in-house design capabilities, manufacturing experience and supplier management to create this novel product. These are also textbook examples of the resources and capabilities that form the central insights of the resource-based view (RBV) (Barney, 1991, 1996, 2001). As demonstrated in later work, (e.g., Helfat and Peteraf, 2003; Helfat and Raubitschek, 2000 and others) these resources and capabilities generate unique firm advantages which develop over time and can be strategically deployed by managers.

Further, the interdependencies which strengthen Tata's ability to manage the business model innovation reflect the same dynamics of the activity system described in Porter (1985). His work articulates the ability of firms to reinforce and extend capabilities through consistent investments that complement one another. By combining activities and functions in a manner that is consistent with the firm's strategy, Porter demonstrates

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that firms can build competitive advantage. Thus, the business model as illustrated in the Tata new product example seems to be replete with concepts from strategy.

Definition Two: Business Models as Strategy Implementation

This same overlap between business model and strategy appears in Girotra and Netessine (2014). These authors describe a business model as 'essentially a set of key decisions that collectively determine how a business earns its revenue, incurs its costs, and manages its risks' (p. 98). Echoing the overlap, Casadesus-Masanell and Ricart (2011) explain 'Whereas business models refer to the logic of the company – how it operates and creates and captures value for stakeholders in a competitive marketplace- strategy is the plan to create a unique and valuable position involving a distinctive set of activities' (p. 107). These definitions recall Porter: 'Strategy is making trade-offs in competing. The essence of strategy is choosing what *not* to do… strategy is about combining activities' (1996, p. 10).

Comparing these statements it may be that business model proponents are trying to make the case that business models encompass action or implementation, while strategy is concerned just with planning or formulation. Of course, it is widely known that such distinctions are artificial and the connection between formulating and implementing strategy has been explored within the resource orchestration literature (e.g., Sirmon et al., 2011). Business model might be considered a stream-lined reconceptualization of strategy, and may therefore be useful to a practitioner audience, as the proliferation of these above cited business model articles within practitioner-oriented journals suggests. However, this conceptualization of a business model as one which is strikingly similar to strategy is less likely to be a source of new theoretical or empirical research among academics.

Definition Three: Business Models Focus on Monetization

Alternatively, business model might mean how a firm plans on monetizing the economic consequences of its strategy. Much of the business model literature which focuses on e-commerce and internet-based business relies on this monetization concept of the business model. Mahadevan (2000) for example, describes multiple methods for generating revenue streams derived from internet-derived access to information, reduction in search costs, real-time connection to suppliers and customers. Similarly, Stewart and Zhao (2000) describe the manner in which internet-based businesses are able to generate returns that are unique to other forms of economic exchange, such as providing services for free, with an expected pay-off predicted in the future.

Expectations of frictionless markets may have been over-emphasized given the time period in which these papers were written (i.e., the height of the dot-com bubble). In hindsight, many of these methods of monetization failed to deliver. This, of course, is an important issue, but an issue that seems to be incorporated in the 'appropriate economic value' part of the generally accepted definition of strategy.

Indeed, in their distillation of strategy research Ghemawat and Rivkin (1998) provide an excellent summary of the fundamental economic problem articulated in Brandenburger and Stuart (1996). They highlight the difference between the cost of producing a good or service and the price for that good or service. Firms can capture value either by reducing costs and engaging in tactics to manage suppliers or through finding methods

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of increasing customers' willingness to pay. Ultimately the value captured by the firm depends on managers' ability to successfully maximize gains from both approaches.

In their discussion of value creation vs value capture Nickerson et al. (2007) make the argument that, in fact, the vast majority of empirical strategy research has focused on value capture. As a result, we know a great deal about the role of capturing value from a wide-range of sources including formal intellectual property rights (Barzel, 1997; Grindley and Teece, 1997; Hart and Moore, 1990; Pisano and Teece, 2007); network position (Ryall and Sorenson, 2007); buyer-suppliers (Chatain, 2011; Chatain and Zemsky, 2011) and the scope of R&D (Cohen and Leventhal, 1990; Ethiraj, 2007). Thus, the business model as mechanism for monetizing strategy may not provide new insights or approaches for researchers or practitioners.

Definition Four: Business Models Focus on Organizing

Fourth, business model might mean how a firm organizes itself – through its structure, control processes, and compensation policy – to implement its strategy. This definition focuses on strategy implementation – an important but sometimes neglected part of the field of strategic management. Arguably, this too is an underdeveloped area of the business model literature. Timmers (1998); Hedman and Kalling (2003) and Morris et al. (2005) devote more attention to the internal mechanisms which might reveal greater opportunities for value creation through business model (particularly e-commerce business model) innovation. But the argument for the role of organizational factors is muted. It may be that this is due to the complexity of mapping and understanding organizational structure. Such complexity has stymied two of the most important theories in strategy: the RBV and transaction cost economics (TCE).

Indeed, one of the criticisms of the resource-based view is that it is relatively lacking in a detailed explanation of the link between value creation and value capture (Foss and Foss, 2004). Arguably, internal organizational features are mechanisms for supporting the maximization of value creation activities and value capture, but the theoretical and empirical RBV literature has largely focused on the former. Within the VRIO framework, the power of firm analysis resides in the accumulation of valuable, rare and costly to imitate assets and capabilities, with the proviso that the firm organizes in such a way as to capture the value created. But the details of how to evaluate the organization generally end there.

Within the strategy field, transaction cost economics comes close to addressing concerns of organization writ large through the comparative trade-off of governance structures with their attendant incentive and control features. A central insight invokes a discriminating alignment hypothesis, matching transaction characteristics to a form of exchange (Williamson, 1985, 1996). The trade-offs of market, hybrid and internal exchange are well-understood in terms of their ability to economize on transaction costs. Performance consequences have been empirically tested (Argyres and Bigelow, 2007; Nickerson and Silverman, 2003) providing significant headway in understanding how firms should structure inter-firm exchange but here again, far less attention has been paid to intrafirm tests of optimal organization.

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If reduced to their theoretical atomic structure, the RBV relies on inimitability and TCE relies on asset specificity. While this provides formidable empirical and theoretical power, it also constricts the application of these theories to internal organizational matters. The business model approach, however, is unfettered to such fixed theoretical markers. As such it has the capacity to develop theory about the potential factors that drive the internal organization of the business model in ways that could enlighten strategy research on value creation and capture.

While the business model approach has the potential to better explore organizational issues compared to TCE and the RBV, we perceive an important caveat. From our reading of the literature, the business model approach fails to separate implementation issues from organization structure. This is not to say that the business model approach assumes that simply specifying the organizational structure of a business model assures successful implementation. But it does seem to imply that the two are intertwined by design given the holistic view of the business model approach. The lack of consensus on definitions within the business model literature complicates determining a consensus on assumptions of temporal order. Does organization precede business model design or the opposite? Does this vary across de novo and de alio firms? Does implementation occur simultaneously, sequentially, or iteratively with business model design or organizational structure? Perhaps the myriad possible antecedents of strategy implementation and organizational success or failure may be beyond the scope of any strategy or business model framework.

Definition Five: Business Models as 'All of the Above'

Finally, business model might mean how a firm combines its strategy, its monetization plans, and its approach to strategy implementation in a way that generates and appropriates economic profits. This last definition combines the elements of the first four. It does have the benefit of reminding us that economic profits and their appropriation can stem from a firm's strategy, its creative monetization process, or through its efficient organization. Thus, for example, a firm may not have a special strategy or approach to monetization, but may be more efficiently organized, and still generate and appropriate economic profits. Or, a firm may not have a special strategy, or unusual strategy implementation skills, but still be able to generate and appropriate economic profits because of its unique approach to monetization. Or finally, a firm may not have special monetization or implementation skills, but have a unique strategy that generates economic profits. Amit and Zott indicate that '… competitors might find it more difficult to imitate or replicate and entire novel activity system than a single novel product or process.' (Amit and Zott, 2012, p. 42). Indeed, this definition is also reflected in Porter's discussion of the need for firms to build activity systems (Porter, 1996) and the resource-based view's proposition that firms can achieve sustained competitive advantage through leveraging and managing an expanded portfolio of resources and capabilities (Barney, 1991, 2001).

The difficulty of separating these mechanisms complicates analysis. In the Tata example, was the success of the new product a function of the firm's strategy, identification of the right problem, an ability to appropriate value from suppliers, or was it differential access to under-served customers? It's conceivable that such differential access to customers triggered an articulation of a problem that rivals didn't identify. Or its relationship

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with suppliers enabled the production of new lower-priced products. What is important is to recognize that each of these elements can be more formally studied using existing concepts from strategy. Indeed, many business model proponents admit as much (e.g., Hedman and Kalling, 2003).[1]

Nevertheless, one of the themes that emerges from the authors who support the notion that business models are distinct from strategy revolves around the holistic, systems approach embedded in the concept. Business models are boundary-spanning, networks of connection across firms and across industries. Business models provide a reminder of the importance of considering multi-lateral arrangements which have indeed been difficult to build theory around. Difficult but not impossible- such business model research might be considered analogous to research on platforms, networks and ecosystems.

But even emphasizing the connections and complexity of this systems approach found in business model research fails to completely distinguish it from prior strategy research, such as the work on resource orchestration in the RBV literature.

Sirmon et al. (2007) address the acknowledged gap in the details of combining resources in order to generate competitive advantage. By sketching a model that includes three stages of structuring, bundling and then, leveraging resources, the authors fill in many aspects of managerial action that are also included in the business model literature. Much as Zott, Amit, and Massa (2011) describe the business model as identifying and structuring interdependent activities that create value for the firm, its customers and other stakeholders, Sirmon et al. (2007) emphasize that simply accumulating resources is not enough. Value creation is a function of combining and structuring these resources so that the firm can take advantage of market opportunities. They elaborate on the processes involved in each stage. Structuring involves both acquiring and divesting resources. Bundling is identified as a set of processes that build current and future capabilities through both enriching and pioneering activities. Leveraging involves mobilizing, coordinating and deploying resources and capabilities.

In contrast, the empirical work of Zott and Amit, 2007 which claims to be the first test of whether or not a firm's business model generates value, provides a test of a set of line items from a survey, but it is not unequivocally a test of the impact of the complexity or interrelatedness of the business model on firm performance. In later work, Zott and Amit (2008) extend their business model logic and argue that there are real distinctions between business models and product market strategy. The authors generously share many of the line items used in their analysis of the survey data employed in their research. Once again, however, it is difficult to know precisely how the managers and entrepreneurs completing these surveys think about these concepts. While Zott and Amit argue that these are distinct concepts, if the coding is relying on the public statements of small firms who are on the brink of going public in the midst of the largest (to-date) tech bubble, it may be possible that some statements from both the firm and the analysts who cover them may reflect intent rather than verified performance.

In later work, Sirmon et al. (2011) delve deeper into the processes and decisions that determine the scope and depth of the firm's resource mix. They combine insights from prior resource management research (Sirmon et al., 2007) with asset orchestration research (Helfat et al., 2009). One benefit of combining these lines of research is that the asset orchestration research devotes more attention to the details of how to select and

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configure assets across organizational boundaries (i.e., amongst strategic alliance partners, suppliers, customers) echoing the business model mandate to look beyond the firm when creating and capturing value. Interestingly, one aspect of the asset orchestration framework is that business models are embedded in the process of selecting and investing in assets.

The resource orchestration approach also adds evolutionary forces by describing differences in how resources may be combined and re-deployed depending on the stage of the industry lifecycle. For example Sirmon et al. (2011) note that in the early stages of the life cycle, pressures for flexibility dominate and managers may engage in efforts to be responsive. As the industry matures, efficiency pressures dominate, and managers contend with the tension of maintaining growth through innovation while also monitoring costs. As an industry declines, the decision to focus on the conservation of resources dominates. Throughout, the orchestration of resources is at the center of how managers navigate over time. By incorporating aspects of the industry life cycle, this resource orchestration approach provides guidance and, arguably, rebuttable, testable strategic propositions for potential changes in competitive position over time. Similarly, the business model literature notes that managers will likely need to adjust their business models over time. But unlike strategy, it is not evident that the business model approach can provide guidance beyond ad hoc postulations. Indeed Zott and Amit (2013) conclude in their discussion of the state of the business model literature that work on the dynamics of business models and the how they coevolve with the organizational structure over time is an important area for future research. Perhaps then, including insights from strategy as a guide for how and when to transition from one business model to another could be a fruitful avenue for advancing the business model framework.

Other Possible Distinctions between Business Models and Strategy

While the resource orchestration branch of the RBV literature makes progress in addressing the role of the manager and managerial decision-making in anticipating and responding to changes in the environment it still lacks the managerial-centric tone of the business model literature. Perhaps because the notion that resources are still at the heart of this conceptualization, it has not entirely resolved the concern of developing the role of the manager or entrepreneur as the central element in generating performance. In simple terms, the resource orchestration research still emphasizes the combination of musical instruments rather than the role of the orchestra conductor. However, recent extensions of resource-based theory into a stakeholder perspective have begun to address this issue (Barney, 2018).

In contrast, current business model research takes a decision-maker perspective. Zott and Amit (2007, 2013) repeatedly and explicitly invoke managerial decision making writing, for example, that a business model 'is crafted by a focal firm's managers (2013, p. 404), that the development of the business model is 'a key task for entrepreneurial leaders' and that designing and re-designing these models is incumbent upon 'entrepreneurs and senior executives throughout the world' (2013, p. 404). Despite the similarities between what Sirmon et al. (2011) describe as resource orchestration and what Zott and Amit (2013) label the activity system, the emphasis on managerial decision-making is a

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possible point of separation between the two streams of research. This may be another reason why it resonates more strongly with managers and entrepreneurs. Given advances in the microfoundations of strategy research area (Barney and Felin, 2013; Felin et al., 2012) as well as cognitive framing (Kaplan, 2008; Kaplan and Orlikowski, 2013) researchers in the business model approach could make strides in better understanding how decision makers construct, choose and adopt business models.

One final distinction between the business model approach and recent work in the entrepreneurship literature regarding value creation opportunities may be relevant to the business model- strategy distinction. Alvarez and Barney (2007) have questioned the assumption that opportunities exist exogenously in the environment, like diamonds in a seam of rock, just waiting to be discovered. They make the argument that entrepreneurs engage in efforts to shape the environment in ways that generate opportunities that would not have materialized otherwise. They further divide such value creation strategies into two types, dependent on the context in which the entrepreneur operates. Utilizing a distinction between uncertainty and risk, they contend that different strategies, financing arrangements and marketing efforts will be deployed depending on the nature of the context, that is, be it one of discovery or creation.

This work on the nature of value creation opportunities has continued to be developed in the entrepreneurship literature (e.g., Alvarez et al., 2014; McBride et al., 2013). It illustrates a fundamental distinction between the assumptions of the business model approach and that of conventional strategy. In the former, an implicit assumption of exogeneity in value creation dominates, while the strategy literature is willing to grapple with the likelihood of endogenous value creation. Going forward, the articulation of assumptions regarding value creation opportunities may be more explicitly addressed in the business model literature.

Practical Appeal of the Expanded Definition

Despite shortfalls in providing rebuttable hypotheses and avoiding redundancy with theories of strategy, the business model has clearly gained traction with practitioners. The success of *Business Model Canvas* (Osterwalder and Pigneur, 2010) and the various iterations which have emerged subsequently (e.g., Lean Business Model Canvas, on-line videos, printed templates, etc.) demonstrate the power of its appeal to a broad audience that may not have the time or desire to wade through academic articles. While the nine components of the basic template of the Business Model Canvas reflect primary aspects of strategy fundamentals, the simple explanations and the stream-lined and colorful graphics provide students, entrepreneurs and managers with immediate insight. The holistic and simplified approach of the business model – and Business Model Canvas in particular- connects with practitioners. Moreover, academics spend a great deal of time and energy focusing on a specific sliver of expertise, utilize complex econometric techniques to test their theories and communicate in a language that is often unintelligible to non-academics. It should not be surprising that the business community has been drawn to an approach which is much more accessible.

Another factor that may amplify the appeal of the business model concept for practitioners is its malleability. While academics are quick to acknowledge boundary conditions

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for their theories, the business model concept – untethered to a specific definition or objective – is ready to be deployed across multiple settings and problems. In fact, managers who often face internal political headwinds when suggesting a strategic initiative or entrepreneurs who must embrace the inevitable pivot as they develop their venture, likely rely on the business model concept as a facilitator of change. These practitioners may need to maneuver away from initial strategic choices, and having a framework which easily adapts to change, offers limited predictions about the risks of change, could be expedient. In contrast, strategic theories are liable to stymie such maneuvering through pointing out the inevitable risks of change and the potential economic consequences of eschewing first-best solutions for political purposes.

So What Strategy Research Questions Might be Informed Through the Business Model Lens?

These observations suggest that while the business model concept remains, in our view, significantly similar to strategy, its appeal to managers and entrepreneurs cannot be dismissed. While we believe it will continue to have an important impact on how strategy is taught, potentially providing a better vector for communicating strategy fundamentals, there are also potential research contributions from utilizing the business model lens.

We posit that the business model approach highlights the centrality of the manager or entrepreneur as decision-maker. As such, the business model literature could be uniquely positioned to integrate insights from the microfoundations of strategy (e.g., Felin et al., 2012) as well as cognitive framing (e.g., Kaplan, 2008) literatures to make progress in addressing questions related to how decision makers construct, choose and adopt business models. We also suggest that the business model approach focuses on the interdependencies within firms, emphasizing these connections as empirically amenable to analysis on the heterogeneity in firm performance. The internal organization of the firm is often given limited attention in the strategy literature, yet recent work on stakeholder theory (Barney, 2018) as well as managerial processes (Bloom et al., 2012) suggest that this is an area of great interest to strategy scholars. In particular, renewed interest in how firms utilize incentives to ensure cooperation with key stakeholders in creating value is entirely consistent with the detailed interdependencies at the heart of the business model approach, suggesting that business model approaches could contribute to stakeholder theory.

In sum, there may be new avenues for research in the business model approach which could contribute to long-standing challenges in the strategy literature. The overwhelming popularity of the business model approach among non-academics may have value in reminding and enabling practitioners to engage in strategy fundamentals when making decisions in complex and quickly changing circumstances. That alone may make it worthwhile to study this concept.

NOTE

[1] It should be noted that the evaluation of the Tata 'Nano' as a successful business model innovation was premature. Over the course of its 10-year existence, sales were estimated to be less than 1,000 units annually, and this year (2018) Tata retired the model. Reasons for the failure include an initial sub-optimal

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solution to the problem of providing a car for the middle class, over-extended supplier relationships, and a shifting marketing strategy. Given a lack of information, it's impossible to determine which of these elements of the business model failed, but a tantalizing clue from Johnson et al. (2008) suggests that a conventional TCE approach would have diagnosed potential and significant hazards in that managers increased the level of asset specificity among components while increasing reliance on suppliers.

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