

# The ABC of Business Models

What is it? How to use it? How to  
control it?



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control it?

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To Kathleen: for the love, support, inspiration and just being there

&

To the elephants in the world: for inspiring me since my childhood



"Hefner" by Johan Durwael (2015)

## **About the author**

Michel Schelkens studied, a.o., at University Antwerp (Belgium)/Georgetown University Washington DC (United States), where he obtained the master's degree in Applied Economic Sciences. He also studied at Vlerick Leuven Ghent Management School (Belgium) and the School of Business and Economics (Maastricht University, The Netherlands), where he obtained an Executive Mastership in Finance & Control and the title of Register Controller.

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Supported a.o. UNILEVER, VOLKSWAGEN, LANXESS and SABIC

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## Preface

Human beings and organizations hold a lot in common. One commonality is that they all cease to exist at one point of time. The quest for immortality for humans is going on for centuries and we seem to make progress on that complex topic. Meanwhile, organizations die not only younger on average than humans, the lifecycle seems to become even shorter. Apparently, it is easier to work on the immortality of human beings. Nevertheless, numerous instruments have been developed to assure long-term success for organizations. One of them is now active for approximately 40 years, namely the mission, vision and strategy deployment. I can hear you thinking “we have been there” and “those instruments were and are very successful, but especially for the consultants billing every hour they worked on this topic”. That was at least what I thought when start reading this book. Although, when you know Michel – I have taught Michel at the Maastricht University in the context of the “Executive Master of Finance and Control”-program – something new should and will pop up.

When I began working for a big multinational back in the nineties, there was a big poster hanging everywhere in our offices. After a couple of weeks, I took the time to read the poster. It was packed with characters, but not the small kind, which you are not supposed to read until after you have bought something, but really large alphabetic characters. Together they formed a sentence, which I was not able to pronounce at once. But after some practicing, I could read it loudly. Subsequently, I continued my day in business meetings, answering mails, working on spreadsheets, creating and listening to presentations and making decisions, etc. Except for the two minutes I spend trying to read it, the poster never ever changed anything I did for that organization. Since I already was in the top 2% - I assume that 98% of the colleagues never invested the two minutes in decrypting the strange sentence - I dare to state that the mission statement, which was the sentence on the poster, never ever affected our products, logistics or customer service. Of course, it had impacted our P&L on the cost side, since somebody had

taken the time to develop it, to discuss that mission statement on executive level, to print the posters and to hang them up. It most certainly did not prolong the success of the organization.

The clearness of that mission statement is not my main message. What I actually want to indicate, is that it never influenced the way of working in the organization. This book will help you on the latter. Michel makes clear what a Business Model really is, how it should be positioned versus strategy management and how it could create value. Moreover, by introducing a new and improved tool, he does not only improve the current knowledge of this rather young notion, but for the first time, somebody makes clear how the CFO and controllers should align their way of managing with their Business Model(s). Differently stated, this book shows how to integrate the mission, vision and strategy in the organizational processes and how the controllers can contribute to this process. I think that this combination is key to the success of steering your company towards a long and prosperous life, and especially in these disruptive times of the digital transformation.

Mark van der Pas

Lecturer Maastricht University  
Managing Director European Center for Digital Transformation

# 1 Introduction

Have you noticed as well how many times your CEO, your boss and your colleagues are using the term “Business Models”? You hear this term frequently in presentations and in every management article it is mentioned at least a few times. Perhaps you do it yourself as well. Have you already wondered what it actually means? How a Business Model can be positioned versus the mission, vision and strategy? How you could use it? Has it really an advantage and last, but not least, how should you control it?

This is exactly the point I want to make. Since the late nineties of the last century, the business started to use the term “Business Model” and authors began to analyze the phenomenon and created Business Model concepts. Anyhow, regardless of the fact that this buzzword emerges everywhere, still dissension exists concerning the definition. Multiple Business Model concepts exist, but are not actively used in daily business life and the bridge to controlling is never made.

In this book, I want to answer three questions: What is it? How to use it? And how to control it? By doing this, I will make specific choices, improve the current knowledge and will introduce the link towards controlling. In fact, I revise what exists and go on where other books stopped. This way, I want to deliver a humble contribution to the intellectual home of management in general and to Business Models in particular in the hope Business Models will not only be actively understood, but also actually used to manage the challenging future of business and to support controllers and managers to steer their businesses.

Before discussing the ins and outs of Business Models, I first would like to welcome the reader and prepare him or her. Therefore, I will introduce you, the reader, in a nutshell in my view of the business of today and in the coming decade(s). Furthermore, I want to use this

introduction to present my motivations and goals to write this book. Finally, I show the reader the roadmap of this book towards the fulfillment of these goals.

## ***1.1 Situation: three clear ascertainments***

When beholding the contemporary society in general and the economic activities and trends more in particular, three significant issues strike me the most. I will guide you through my findings.

### **1.1.1 Increasing importance of strategy and Business Models to support answering the upcoming disruptive shocks**

First and foremost, the dynamism and format of the current economy and – in a broad sense – society is created by a series of revolutionary developments over the last two decades. The not-exhaustive list of major trends could be summarized in the following not exhaustive lists:

- New communication technology, like e-mail, social media, Electronic Data Interchange (E.D.I.), Radio Frequency Identification (R.F.ID.), etc.<sup>1</sup>
- New computing technology and applications, such as internet, cloud computing, virtualization, Enterprise Resource Planning (E.R.P.), Service Oriented Architecture (S.O.A.), Customer Relationship Management technology (C.R.M.), Electronic Funds Transfer (E.F.T.), Global Positioning System (G.P.S.), apps, cloud computing, Software as a Service (SaaS), Platform as a Service (PaaS), Infrastructure as a Service (IaaS), Really Simple Syndication (R.S.S.), Enterprise 2.0<sup>a</sup>, multitenancy software<sup>b</sup>,

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<sup>a</sup> Enterprise 2.0 includes interactive applications concerning knowledge

NoSQL databases<sup>c</sup>, algorithmic personality recognition, bots, golden backdoors, quantum computers, etc.<sup>23</sup>

- Cheap information technology, bandwidth and communication possibilities<sup>4</sup>
- Big data and information avalanche<sup>5</sup>
- Other technological breakthroughs, like Internet of Things (IoT), drones, autonomous cars, innovative applications like smart materials, 3D printing or additive manufacturing, grapheme for application of recovering of hydrogen fuel from air, development of other new energies, blockchain, augmented knowledge<sup>6</sup>, etc.
- Globalization and deregulation. In the last decades many global trading regimes are established a more globalized and deregulated economy. Examples are the economic and monetary unions, like EU; customs and monetary unions, like CEMAC; common markets, like CIS; customs unions, like MERCOSUR and multilateral free trade areas, like NAFTA and SAFTA.
- Social and environmental events<sup>7</sup>: new global middle class, overpopulation, ageing, Western shrinkage of population, obesity, urbanization, terrorism, concern for global warming, sustainability, financial integrity and transparency, etc.
- More outsourcing, off-shoring and on-shoring
- Etc., etc., etc. ...

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management within organizations.

<sup>b</sup> Software multitenancy: a software architecture in which a single instance of a software runs on a server and serves multiple tenants or groups of users.

<sup>c</sup> NoSQL databases: database with a data storage and data retrieval mechanism other than the tabular relations used in relational databases. Used for big data and real-time web applications.

Due to many of those major breakthroughs, a shift of power can be observed towards the customer. This can be explained by the increased possibilities for customers to express wishes; the access to all markets and by consequence all products for all customers; the origination of global markets; the growth of transparency and knowledge, which makes it easier to compare between alternative products and services; and finally more and improved products and services.<sup>8</sup>

This increased customer-centric business attitude supplicates for innovation and will have major impact on the strategy management of companies and on the fulfillment of the organization of creating and delivering value for the customer and still capturing value for the own enterprise.<sup>9</sup> Or stated in another way, how does a company model his business to create and deliver value for the customer and itself in a world with those economic developments?<sup>10</sup>

Also Grasl argues that Business Models and strategic management are essential to every company, since it makes clear what the position is of the firm in its value network, in the interactions with their stakeholders, in relation with the exchanged output and the economic logic that defines how the firm creates value.<sup>11</sup> It is by consequence not surprising that those earlier-mentioned trends just seem to invigorate and accelerate the importance and focus of Business Models.

That mentioned necessity for innovation will lead to the following evolutions or even revolutions in the business of tomorrow and, like stated before, will have disruptive consequences for strategies and business models. I expect the following five business (r)evolutions:

1. Less physical capital is needed.

21<sup>st</sup> century-companies will optimize their capital in such way that even virtually no physical capital is needed to compete capital-heavy 20<sup>th</sup> century-corporations. Alibaba for example is the world's most valuable retailer and it holds no stock. Although that Airbnb is the world's largest provider of accommodations, no real estate is on the balance sheet. The

world's largest car service of today is managed under the name "Uber" without even owning cars. Those mentioned companies and the other leading companies in the 21<sup>st</sup> century have found ingenious ways to take friction out of its industry, connecting buyers and sellers directly and conveniently, enabling new, nearly capital-free Business Models. Those 21st-century corporations will increasingly be based on out-of-the-box ideas that consume lots of brainpower and this in every possible industry. Based on research findings of McKinsey "asset-light, idea-intensive sectors" generated 17% of Western companies' profits in 1999 while they already generate 31% today.<sup>12</sup>

2. Creative and flexible human capital will matter more than ever.

Since innovative ideas and the transformation of those ideas in commercial successes can be generated with less physical capital, employees become more important. That human capital creates intellectual capital in the form of software, patents, copyrights, brands, and other knowledge; and customer capital in the form of relationships with buyers; etc.<sup>13</sup> This expectation will be positive for the creative and well-educated part of the population. Meanwhile, do not fool yourself, the standard jobs will disappear more and more by the digital revolution, like the bitcoin with its blockchain technology. Differently stated, you need to identify the people critical to the company, and recognize that increasingly, they are the company. I dare to predict that companies will have almost no employees anymore and the ones that are there, will only be there because they generate real added value. Also they will only be temporarily employed by the same company. Almost each staff member will be a company on his or her own, delivering service to other companies as long as it pays off. Former Cisco CEO John Chambers mentioned that "soon you'll see huge companies with just two employees – the CEO and the CIO."<sup>14</sup> OK, exaggerated, but he indicates the future in rough lines. It is clear that this will have huge social impact and as society, we all need start

thinking about how to manage this. Finland and the Netherlands are already anticipating by testing the “basic income” idea.<sup>15</sup>

3. Winners will win bigger, and the rest will fight harder for the remains.

“New Business Models often make fortunes for their creators and destroy whole industries in the process.”<sup>16</sup> Logically, this phenomenon is especially frightening for established category leaders, because even if they switch to new, low-friction Business Models, they could still end up smaller and less profitable than they were. That’s because “some tech and tech-enabled firms destroy more value for incumbents than they create for themselves” says the McKinsey Global Institute. For example, Microsoft’s Skype service brought in some \$2 billion in 2013, but in that year, Skype transferred \$37 billion away from old-guard telecom firms to consumers by giving them free or low-cost calls, according to the calculations of McKinsey.<sup>17</sup>

4. Increasing company sizes.

Regardless of the pressure on the number of staff, 21<sup>st</sup> century corporations will be bigger than their 20<sup>th</sup> century predecessors and even bigger than nations. Geoff Colvin gave in his article in Fortune magazine some striking examples. Via Google billions of searches a day are conducted. This generates better real-time knowledge of what’s going on in the world than any government knows. With this information disease outbreaks and stock market movements could be predicted. Also elections everywhere in the world could be influenced, if Google wants to. Facebook, with its 1.5 billion users, has a bigger population than China and can predict their success in work and romance based on the gathered information posted by those users. On any given day, Apple probably has more cash on hand than the U.S. Treasury.<sup>18</sup>



## 5. Businesses will retire very fast.

Corporations will have a significantly shorter life cycle. The average life span of companies in the S&P 500 has already fallen from 61 years in 1958 to 20 years today. It will fall further. Also this is a logical evolution of the fast changing technology and its possibilities. I even expect that “pop-up”/“pop-in<sup>d</sup>” companies and “pop-up” brands will appear increasingly with repercussions on the shelf life of strategies and business models.

To conclude, the importance of the (re-)design and management of strategy and Business Models is increasing due to revolutionary and especially technological developments.

Very important to mention is that I do not see the above-mentioned trends, breakthroughs and the increasing complexity of society as the beginning of the end of the current period of prosperity. On the contrary, this will be the beginning of the next era of growth and new possibilities. Only one condition, the management of business and society has to be optimized and professionalized.<sup>19</sup> Business Models will contribute in this framework as well.

### **1.1.2 Too little attention for strategy formulation and strategy implementation.**

Although the strategy and the Business Models become more and more important, it is striking to see that the strategy analysis and strategy formulation do not get sufficient professional attention. But also the next step in the strategy process, the strategy implementation, is step motherly managed. A study of the Strategos Institute showed that the most profitable companies over multiple years were strong in strategy and in strategy implementation.<sup>20</sup> The mainstream in most organizations

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<sup>d</sup> “Pop-in” companies are companies and activities popping up temporarily in an existing business. E.g. specialized chocolatiers in an eating house during Easter.

shows however a different picture: 52% of the business leaders should be effective in strategy development and only 50% excel in strategy execution.<sup>21</sup> This remarkable statement and outcome of that research could be vouched by the “Strategy Execution Barometer”. Since the importance of strategy to overcome the disruptive shocks and the close link to Business Models, I would like to present some conclusions of this survey of 20.000 managers of more than 1.100 companies in 36 countries and 29 industries.<sup>22</sup> The most striking inferences were:

- Too little alignment between executives and mid management levels was ascertained. This resulted in 33% of all managers that were actually never asked the question if they understand the strategy.
- Managers lack information of their colleagues’ goals.
- 24% of the managers do not have a clue of the strategic projects of their colleagues.

Managers, independent of the level, should not only know and understand the strategy, but they also should have the aligned vision and priority to implement the strategy. Approximately one third of the participating managers lacks the insight and knowledge of what is needed to actually implement. This results in the fact that the major part of the business strategy (40 to 60%) is not executed due to failing implementation<sup>23</sup>. Furthermore:

- 1 on 5 projects fail to support the strategy
- 85% of the managers state that there is a mismatch between project portfolio and strategy
- 49% of the strategic initiatives are poorly budgeted and staffed
- 92% of all managers are unhappy with resource allocation of the so-called strategic projects

- 79% of all managers find the project accountabilities unclear

To conclude, although the increasing importance of proper strategy formulation and Business Model development, strategy management needs a boost in professionalization.

### **1.1.3 The home of Business Models is not yet complete**

Finally, it stands out that, although due to a series of revolutionary developments in our society, the importance of Business Models increase, still no common understanding exists concerning Business Models in the academic and business world, like mentioned in the beginning of this introduction. Magretta stated once that, “like the term strategy, the term Business Model is used sloppily, being stretched to mean everything and ending up meaning nothing”<sup>24</sup>. She even went further in the same article in the “Harvard Business Review” where she indicated that the term Business Model is just a buzzword. According to Magretta however, this is a “shame”, since a Business Model is essential to every organization looking for success. Although many books have been written about marketing, production methods, supply chain solutions, customer service issues and strategy and the fact that nowadays the notion “Business Model” is frequently employed in the last decade, David Teece mooted that the concept of Business Models has been neglected too long in economics and business studies. Economic theory and by consequence textbooks of economics make the assumptions too easily that inventions lead almost automatically to value creation for the customer who will undoubtedly pay for it. If the value proposition is attracting customers, Teece argued that we suppose that it is a matter of course that value is captured by the companies by selling their innovative products to already existing markets and that patents always guarantee sufficient protection. According to the same author, the design of a business is not questioned and too much assumed as a given fact. To put it in his words, “the study of Business Models lacks an intellectual home in the social sciences or business studies”.<sup>25</sup>