Business Model Frameworks

A guide to creating and capturing business value

Benjamin Sommer

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Business model frameworks: A guide to creating and capturing business value
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1 What is a business model?

“Business model” as a term first appeared in management books in the 1960s. However, it is not until recently that the term was more specifically defined. Especially in the last 10 years, there has been a proliferation of business model frameworks. This eBook will on focus the most popular business model frameworks in use today. But, first of all; what is a business model?

READ THIS FIRST

Before you read on take a minute to reflect – what is a business model?
ake sure to make a note of your definition -

My definition

Business model ______________

____

____

____

____

All organizations, young, small, old, large, non-profits, governments, NGO’s and for-profits, have a business model. Organizations might not have their business model explicitly expressed, but rely on an intuitive or implicit understanding of its business model. I would argue that not having an active understanding, explicitly visualized in some format, of your organization’s business model represents a huge risk. Without it, it becomes impossible to communicate about the business model with a shared understanding. Important dependencies or relationships will become opaque in a world of blah, blah, blah. This leads to misunderstandings and missed opportunities. Without a business model perspective your company is a mere participant in an array of networks and passive entanglements. Business models take all the complexity of an organization and boil it down to a one-pager, visualized and easy to communicate.

The land of blah, blah, blah

With complex problems or challenges like business models, words don’t work that well. They simply can’t detect, describe, and defuse the multifaceted complexity of a business model. But we still try and are caught in seemingly endless meetings of words, words and words. This is the land of blah, blah, blah. I’m sure you been there many times. This book will help you avoid it!

Adopting a business model perspective will help executives and organizations purposefully structure the activity system of their companies. The purposeful design of business models is a key task for managers and entrepreneurs and is an important source of innovation. Business model thinking encourages a systemic and holistic view when considering strategy and innovation.

The term business model has especially grown in popularity since 2004–2005 and entered the everyday business language. Not surprisingly, a number of definitions of what a business model is have been introduced. However, going through different definitions they have very much in common: the business model is about value creation, customers, product or service, costs and revenue. According to University of California, Berkeley lecturer, serial-entrepreneur and angel investor Steve Blank *"A business model describes how your company creates, delivers and captures value.*
Or in English: A business model describes how your company makes money".

This is how Alexander Osterwalder defines business models: *"A business model describes the rationale of how an organization creates, delivers and captures value"*. Clayton Christensen offers a similar definition of the business model. And we could go on with many more definitions, but that wouldn't be much fun.

For the purpose of this eBook I'll define the business model as a conceptual model that represents how an organization generates and captures value.

Def_Business Model [bɪznəs mɒdl̩]

> "The business model describes how an organization generates and captures value."

The building blocks of the business model vary slightly across different frameworks. However, the business model should always include a value proposition, customer segment, profit formula (or revenue and cost), delivery channel and key resources.

A very important aspect of a business model is that it needs to be sustainable, i.e. the costs can't be higher than the revenue over time. Revenue here is defined in its widest sense and includes donations, government support as well as payments from customers. With such a wide definition of revenue, business model frameworks can also be used with success by for-profit, non-profit and government organizations.

our Def Business odel

I bet you didn't have too much trouble defining what a business model is. The surprising thing is that it's rather unlikely that your definition was the same as the person next to you, or the person next to them.

"Business model" is a term we use in everyday business language still peoplemean different things when talking about business models. This is one of the reasons why using a business model framework facilitates the understanding and communication about business models.

1.1 Business models and business plans

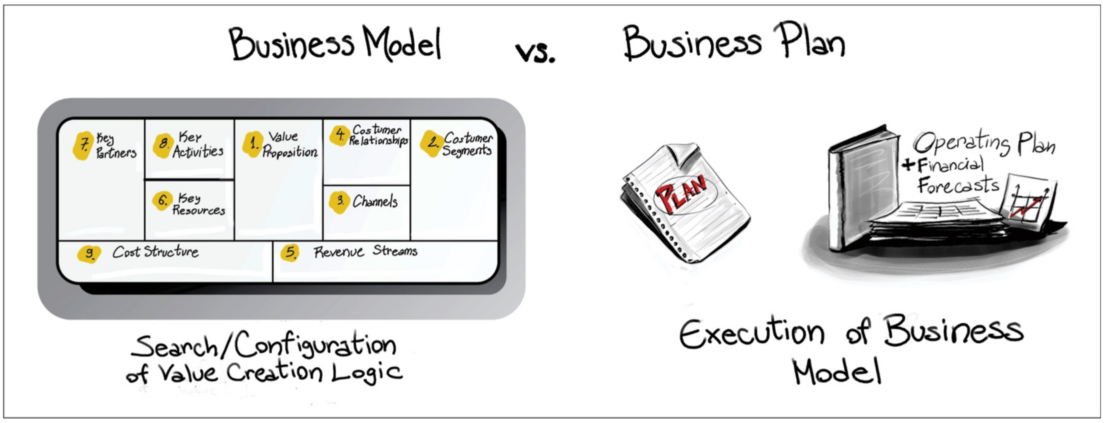
So are business models the same as business plans? This is a question I hear often. Business models do capture much of the same information as a business plan, but they are presented in very different formats than the normal 50+ page business plans. However, there is a more fundamental difference between business models and business plans. Business plans are made for execution and follow a predefined plan – the implicit assumption behind the way we used to write business plans was that we could sit behind a desk and do all the research we needed and find all the relevant information and devise the perfect plan to success. Failure was due to poor planning. We now know that no business plan survive first contact with customers. Hence, producing heavy weight business plans for execution is a waste of time and money before we have a proven business model.

The business model is a lightweight representation of all the hypotheses we need to confirm to devise a business plan. Only when we have validated our hypotheses about our business model and turned those hypotheses into facts by testing them in the market place will we go on to prepare a business plan. If through validation you have arrived at a scalable, repeatable and sustainable business model, the focus shifts from iterative testing of hypotheses to execution on a plan and company building to extract as much value as possible from the business model.

Does this mean that business model frameworks are only for new startups without a running business model? Absolutely not – business model frameworks help organizations conduct structured, tangible, and strategic conversations around new businesses or existing ones. By using a business model framework the connections, critical components and opportunities/threats in your organization's business model becomes clearer. The business model provides a holistic picture of how an organization creates and captures value.

Leading global companies like GE, P&G, Nestlé, Telenor and others use business model frameworks to manage strategy or create new growth engines. One of the main benefits of using a business model framework is that it helps companies move beyond product-centric thinking and towards business model thinking.

In summary, a business plan's main role is to plan, execute and communicate a business project and its implementation while the business model frameworks help companies to either find their right business model or innovate on their existing business model.



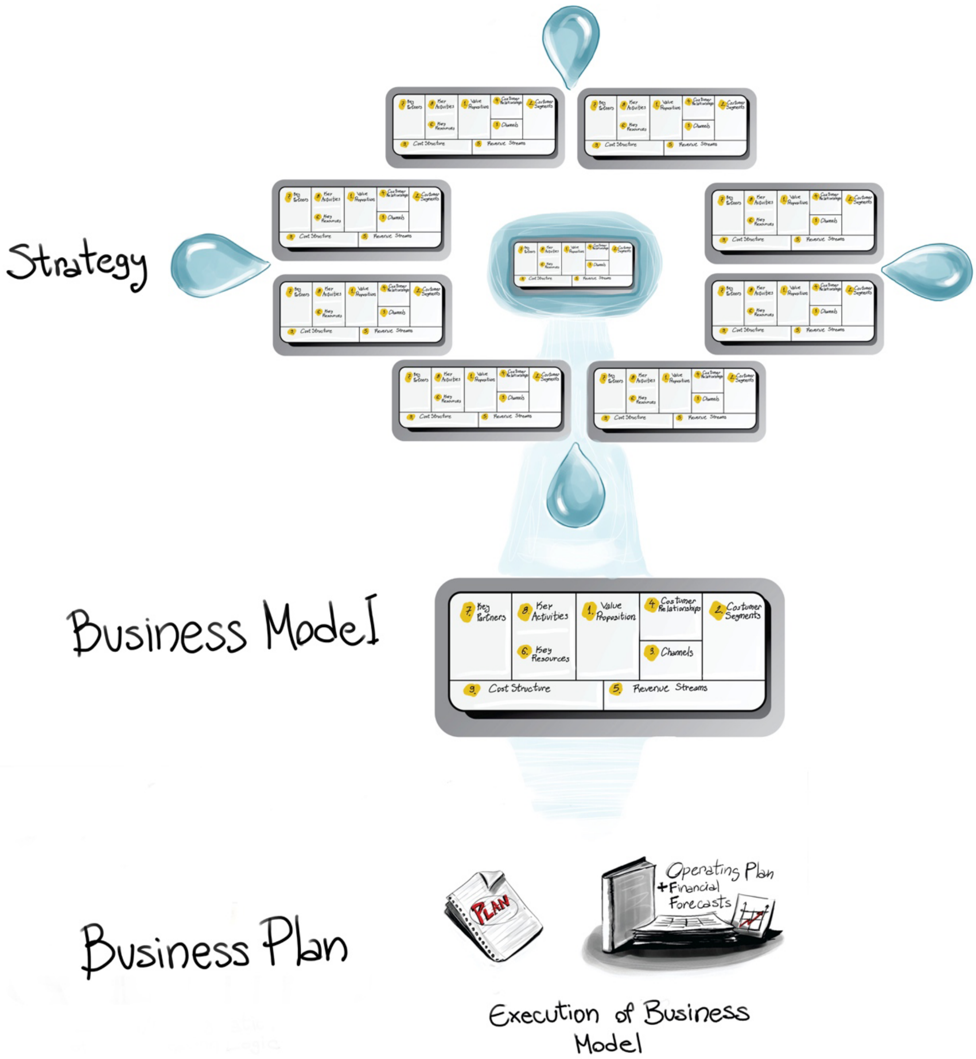
1.2 Business models and strategy

In the previous paragraph we established that business models and business plans are not the same thing. The business plan is the execution of the business model.

So are business models the same as strategy? Your business model is certainly strategic, but it is not the same as strategy. The strategy determines the position a company will have in its industry. How much of the created value an organization is able to capture is dependent on its strategic position in the industry it operates.

Value is always created in a value chain before it becomes available for the customers. The structure and strength of the actors in this value chain together with the characteristics of the industry, such as competition, substitutes etc. will determine how much of the value the organization is able to capture.

In summary, the business model describes how an organization generates and captures value, the strategy is the context in which the company operates the business model and the business plan are focused on operational execution of the business model.



! Business models should not be confused with business modeling such as business process re-engineering (BPR) or business process management (BPM).

These methods are focused on a lower level in the organization, namely the processes within and between the business model components.

Hence, a business model is different from a company's business process model. Business process models are typically modeled as flows in tools as Vision, ARIS or similar.

1.3 Business models and innovation

Innovation is an ever-important topic when it comes to sustaining the competitive advantage of an organization. Innovation is about creating something new and different that is useful for someone. Innovation can be divided into three main categories; product (or service) innovation, process innovation and business model innovation. Business model frameworks support innovation, but can also be innovative by themselves with an existing product or process.

Product innovation can be defined as the development of new products, changes in design of established products, or use of new materials or components in the manufacture of established products. Product innovation is what most people think about when talking about innovation. Product innovation can very valuable to the innovator, but the challenge with product innovation is that it is easily copied. The competitive advantage gained from product innovation is very often limited and in a short timeframe.

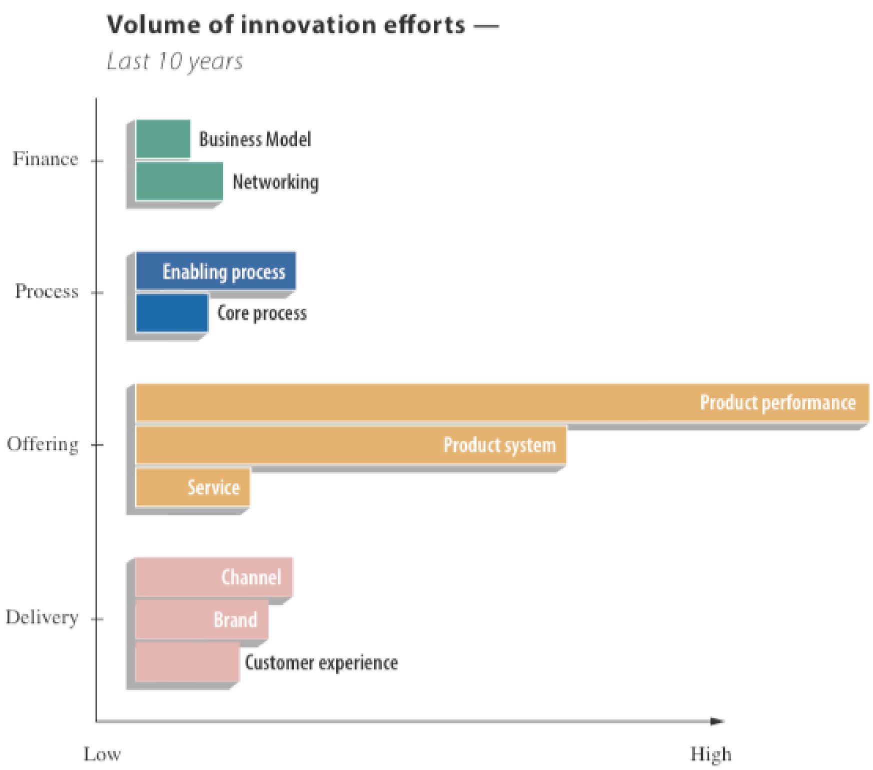
> *"Our greatest focus is on business model innovation, which is where the greatest benefits lie. It's not enough to make a difference on product quality or delivery readiness or production scale. It's important to innovate in areas where our competition does not act."*
>
> CEO, interviewed by IBM for the Global CEO report

Process innovation is the implementation of a new or significantly improved production or delivery methods (including significant changes in techniques, equipment and/or software). This type of innovation is harder to copy and requires more skill and experience, think Just-in-time production and logistics principles.

Business model innovation takes place when the assumptions or content of one of the several buildings blocks are new or significantly changed. Business model innovation is about new ways of creating, delivering and capturing value. Unlike product or process innovation, changes to the business model require changes to the foundational decisions upon which the business operates. Therefore, business model innovation will likely be radical, and in many cases, transformational. A well-designed business model has interlocking building blocks that reinforce each other.

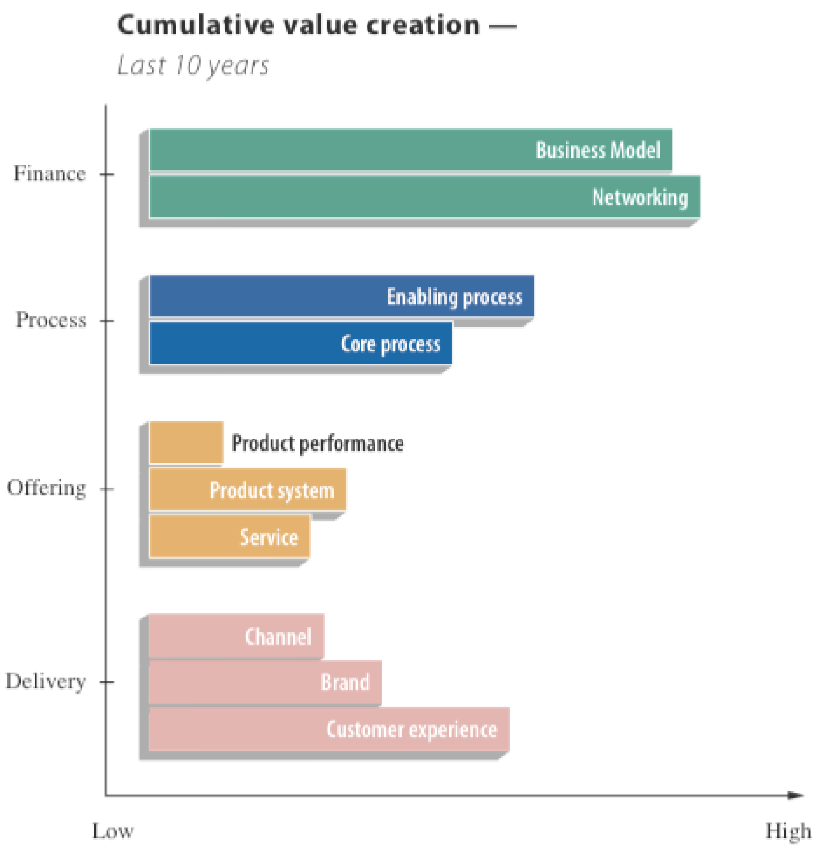
But how useful are business model innovation from a financial perspective? Why should we bother? The Doblin group conducted a thorough analysis comparing the return on investment (ROI) of different types of innovation. Evidence suggests that organizations that harness innovation prosper in the marketplace. Companies that harness innovation achieved profit margin growth of 3.4 percentage points annually since 1995, compared to 0.4 percentage for the median Standard & Poor's 1200 global company average. The group's stock price also grew by 3 percentage points higher per year over the decade compared with the S & P average.

In the analysis Doblin performed they grouped ten types of innovation into 4 group categories; Finance (business model innovation and re-configuration of the network producing the value proposition), Process, Offering (product or service) and Delivery (customer facing activities). As can be read from the illustration below most of the innovation efforts are spent in various product innovations.



Source: Doblin Inc.

It is not surprising that most of the innovation effort is spent on development of product innovation considering the traditional understanding of innovation. However, Doblin then looked at the cumulative value creation from the different innovation categories.



Source: Doblin Inc.

The data from the Doblin analysis puts the innovation effort in a different light. Considering the cumulative value creation of innovation, the effort put into product innovation is irrational from an economic standpoint. The cumulative value creation from business model innovation is in the range of 10 times that of product innovations. If we compare the innovation effort of business model innovation to product innovation, the value creation from business model innovation is close to 100 times the value creation from product innovations. The value creation from product innovation compared to the effort is a measly 1/8th.

According to Doblin Inc. less than 2% of the innovation projects produce more than 90% of the value.

This data also hints at other important parameters when considering innovation and business development – how sustainable is the innovation from a competitive advantage standpoint? As product innovations can be easily copied, the timeframe from which a company can derive extra value is short. Competitors will introduce similar product features and/or drop the price. Hence, the innovation's value is limited. Process innovations are more difficult to copy and they sustain their value for a longer time and create more value for the innovative company.
Thirdly, business model innovations are very difficult to copy as they compose the value creation logic of a company. Hence, business model innovation creates a huge amount of value and a sustainable competitive advantage for companies.

Xerox and business model innovation

In 1958 Chester Carlson, a Xerox researcher, developed a new copier using electrophotography. Electrophotography was superior to current techniques, either "wet" photographic methods or low quality dry thermal processes. The prevailing business model for both technologies was to sell the equipment just over cost and then charge a substantially higher margin for supplies and consumables. Both copier technologies required special paper and supplies, creating an aftermarket revenue stream for vendors. Typical office machines sold for $300; the average machine in use produced 15–20 copies per day and 90% were used for fewer than 100 copies per day.

Chester Carlson (1906–1968), inventor of the electrophotography process.

The 914 copier produced high quality images on plain paper, but the manufacturing cost of the machine was estimated at $2,000. Its variable costs per copy were roughly the same as the existing methods. This created a problem for commercialization of the technology. The manufacturing costs were much higher, while its supplies costs were about the same as earlier technologies. Charging an even higher premium on the supplies and consumables would drive the customer to prefer existing technologies.

How could this new technology penetrate the market, given these economics? Xerox attempted to partner with a strong marketing partner for the 914, but was rejected by Kodak, General Electric and IBM. IBM rejected the 914 after a careful and professional market analysis by Arthur D. Little (ALD). ALD concluded;
"Although it may be admirably suited for a few specialized copying applications, the Model 914 has no future in the office-copying-equipment market."

The assumptions behind this conclusion were that the 914 would be offered to the same customer segment with the same revenue model as existing copier alternatives. Joe Wilson, Xerox's president, saw the potential for massive revenues in office copying and wasn't about to give up.

In 1959, Xerox brought the 914 to market by itself, surmounting the obstacles of high cost by using an innovative business model. Instead of selling the equipment, Xerox offered their customers a lease. A customer would only to pay $95.00 per month to lease the machine, promising to pay four cents per copy beyond the first 2,000 copies each month. Xerox would provide all required service and support, and the lease could be cancelled at only 15 days' notice.

The 914 copier as introduced by Xerox to the market in 1959.

This was a huge leap of faith for Xerox, a small company in 1959 taking a risk to launch the 914 copier. Only if the 914 were to lead to greatly increased volumes of copying, would this business model pay off for Xerox. Joe Wilson bet that there was greater potential value latent in electrophotography than ADL had judged, but that its realization required a different business model.

Joe Wilson's gut feeling proved to be correct. Once installed, the appeal of the machine was intense; users averaged 2,000 copies per day (approximately a 30× increase), generating revenues far beyond Xerox's most optimistic expectations. The business model established for the 914 copier powered compound growth at an astonishing 41% rate for a dozen years, turning $30 million Xerox into a global enterprise with $2.5 billion in revenues by 1972.

Kodak and the innovator's dilemma

19th of January Kodak filed for bankruptcy. Founded in 1889, Kodak followed the "razor blade" strategy of selling cheap cameras and making money on the expensive film that consumers bought to fill the cameras. The company for decades had what strategists call a "distinctive competency" at making film with silver-halide chemicals. As recently as 1976, the company had over 90 percent of the film market. But then, digital photography happened. Did a clever and more resourceful competitor that invested in digital photography drive Kodak out of business?

NO! Kodak invented digital photography in the 1970s. However, Kodak wasn't interesting in developing digital photography further. And why should they have been – they made tons of money with their cheap cameras and expensive film business model.

However, in the digital environment Kodak's old business model of cheap cameras and expensive chemical film, or, for the high-end customer, expensive cameras and expensive film, would not work.

This is the innovator's dilemma; organizations will reject innovations based on the fact that customers cannot currently use them, and they have large investments in structures, processes etc. to support their current business model. These innovations are disruptive in that they transform a product or service that historically was so expensive and/or complicated that it was only accessible to a few select customers and make it accessible to a large set of customers (Christensen's own words). In a business model context this means that one or several of the building blocks of the business model has changed. Unless you innovate your business model to accommodate these changes the company will struggle.

Still large successful companies find this difficult given their history and the investments already made in their current business model, and they are most likely still making healthy, although shrinking, profits.

1.4 Summary – exercises

Business plans are focused on _________ while business models describe how __________ create and

Strategy is the ______________________________ in which we operate our business model.

The strategic ______________ determines how much of the created ______________
an organization ______________

CHEAT SHEET			
context	execution	position	capture
value	organizations	captures value	

How many times do you get your investment back when investing in business model innovation?

Answer: ______________ times

How many times do you get your investment back when investing in product innovation?

Answer: ______________ times

2 Business model frameworks

The business model is a conceptual model that represents how a company generates value and captures that value. But, why do we need business model frameworks?

Business models are not a management fad. The business model frameworks make it possible to simply communicate the essence of the value creation logic of an organization and how the organization captures that value. The following frameworks all have in common that they rely heavily on visualization of the business model. Visualization of business models this way has many benefits; it helps to create a shared language, dependencies are easier to understand and it facilitates seeing the whole picture and how every single building block supports the business model. Visual business model frameworks are unique in helping us organizing our thinking.

However, a business model framework is not a recipe for success. The business model stills needs to be executed and managed. There are plenty of opportunities to fail even if you mapped out your business model. In chapter 3 we will look at how you can work with business models, document your organization's business model and perform business model innovation.

Lets look into some of the frameworks that have been developed in recent years to work with and understand business models.

2.1 Business Model Canvas by Alexander Osterwalder

Business Model Canvas is probably the most popular business model framework in the world right now. Alexander Osterwalder developed the Business Model Canvas framework after publishing his Ph.D. dissertation called "The Business Model Ontology – A proposition in a design science approach" in 2004. The objective of the dissertation was to answer the question; "*How can business models be described and represented in order to build the foundation for subsequent concepts and tools, possibly computer based?*"

The business model canvas does not actually appear in the dissertation and was developed later when companies approach Osterwalder with asking for a simple tool they could use in their work with business models. Osterwalder and his Ph.D. supervisor Yves Pigneur quickly dropped "ontology" from the term, arguing it was too academic. The outcome of the request from the companies Osterwalder and Pigneur worked with was a business model framework visualized on one-page.

Canvas was added in the context of art, a clean slate to work from. Canvas can be defined as the background against which events unfold, as in a historical narrative (Farlex Dictionary). This sets the right frame of mind for the business model canvas – it's a clean slate for a new narrative, with which we can experiment.

The business model framework developed by Osterwalder and Pigenur consists of 9 interconnected building blocks. Together they constitute the business model canvas.

Value proposition: The value proposition should answer the question what are you building and for who? The value proposition describes how **a bundle of products and services create value for a specific Customer Segment. It's about solving a problem or need for a customer. What pains are you solving and what gains are you creating? If you have several Customer Segments you should have several Value Propositions.**

Customer segments; Who are my customers? The customer segments are the groups of people and/or organizations a company or organization aims to reach and create value for with a dedicated Value Proposition. Remember that your customer doesn't exist for you – you exist for them. A company should have a detailed understanding of their customers, their geographic, social characteristics, demographics and context. It's recommended that you develop archetypes or personas of your customer segments. There might be several archetypes or personas for each customer segment, especially in B2B setting where the sales process is much more complex.

Channels: How does your product or service get to your customers? Channels describe how a Value Proposition is communicated and delivered to a Customer Segment through communication, distribution, and sales channels. Will it be a physical channel, physical combined with virtual channel or purely virtual channel? Today most physical channels also have a web presence. What distribution channel a product or service will use should be one of the first questions you address.

Customer Relationships; the relationship to your customer should outline how you get customers, how customer are kept (retention) and how customers are grown over time. What type of relationship is established and maintained with each Customer Segment differs greatly from relationships spanning generations (Swiss banking) to one-time transactional ones (e.g. buying an ice-cream). Most business will try to create some type of loyalty for the customers, as keeping and growing customers generally are easier and cheaper than acquiring new customers.

Revenue Streams: The revenue stream is the result of a Value Proposition successfully offered to a Customer Segment. It is how an organization captures the value for which customers are willing to pay. In plain English – how do you make money from the product and services being sold to customer segments? What value are the customers paying for? Example of revenue streams includes transactions, subscription models, freemium, license fees, support and maintenance. Revenue model is different from pricing strategy and tactic. There will be a large set of possibilities for pricing strategy and tactics within the same revenue model. E.g. for a license model the pricing can be based on named users, concurrent users or some other component but they are still configurations of a license model.

Key Resources: What resources do you need to make your business model work? Key Resources should describe the most important assets required to produce and distributes the previously described buildings block of the business model canvas (the value proposition, customer relationship, channels and revenue stream). Do we have intellectual property we need to protect? Do we have patents or do we need to acquire patents? The focus should be on *key* resources that create value for the customer and the company and the way those elements interact. Every company also has generic resources that don't create competitive differentiation.

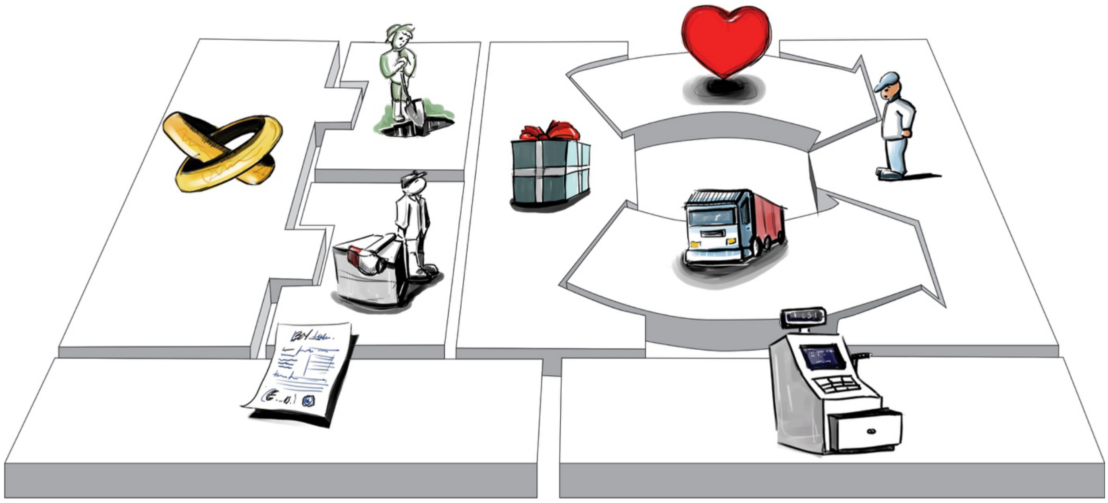
Key Activities: are the most important activities an organization needs to perform well. What activities must you do for your business to make the business model work? The key activities are instrumental for the business model to succeed and you soft of need to become an expert or have access to experts on these key activities.

Key Partnerships: What partners and suppliers do we need that have external resources and perform activities we need to make our business model work? Before going out and sign on partners we need to think through what exactly do we want from a partner and what activities to we want them to perform for us? As a business develops it probably need different kind of partners. Also consider what type of partnership you are looking for; is it a long-term supplier or buyer, a joint venture, a value added reseller or other type of strategic relationship?

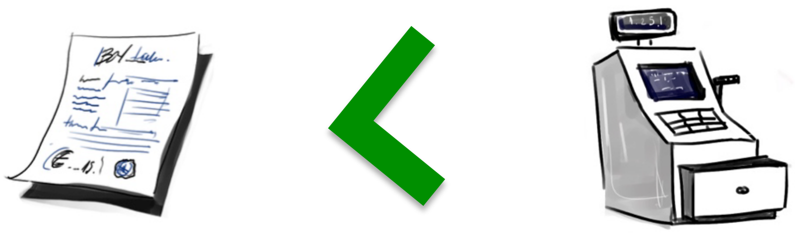
Cost Structure: Finally all the resources, activities, partnerships etc. in the business model ends up as cost in the cost structure. The cost structure describes the cost and expenses to operate the business model. Profit is calculated by subtracting the total of all costs in the Cost Structure from the total of all Revenue Streams. You need to ask yourself what are the entire costs to operate the business model. What are the most important cost you need to worry about? What are the most expensive resources you're going to need to pay for? What key activities are the most expensive?

What are fix cost? What are variable costs? Are their economies of scale? You would want to get a good picture on how much it will end up costing you to run your business.

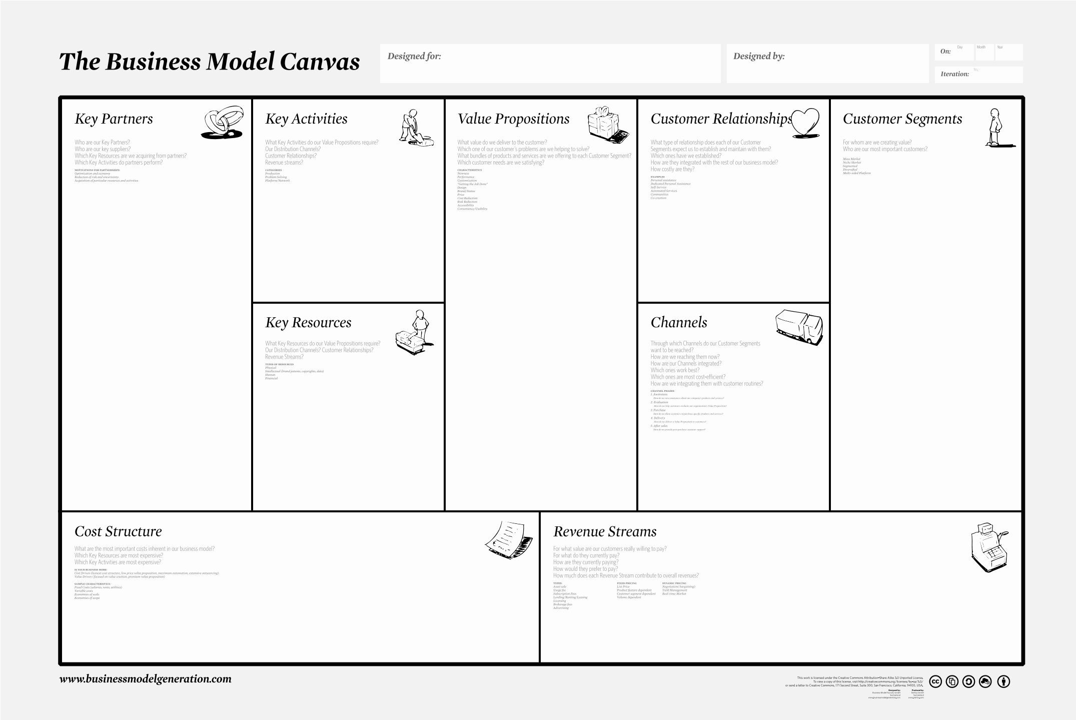
The genius of what Osterwalder and Pigneur did was to combine these 9 building blocks of the business model framework into a one-page interlocking holistic model; the Business Model Canvas. In a strong business model the building blocks reinforces each other. The business model canvas was a breakthrough in helping to organize how practitioners think about business models.



The business model canvas can also be divided into a front stage and a back stage. The right hand side (value proposition, channels, customer relationship and revenue) is the front stage. The front stage is where you interact with your customer segments and your customers can see what's going on in your business model. The front stage is what drives value and enables you collect revenue from your customers. The left side of the business model canvas equals the back stage. The back stage has everything we require to make the business model front stage possible. The back stage drives the cost of the business model. For the business model to be sustainable the revenues from the front stage must be greater than the costs of the back stage over time.



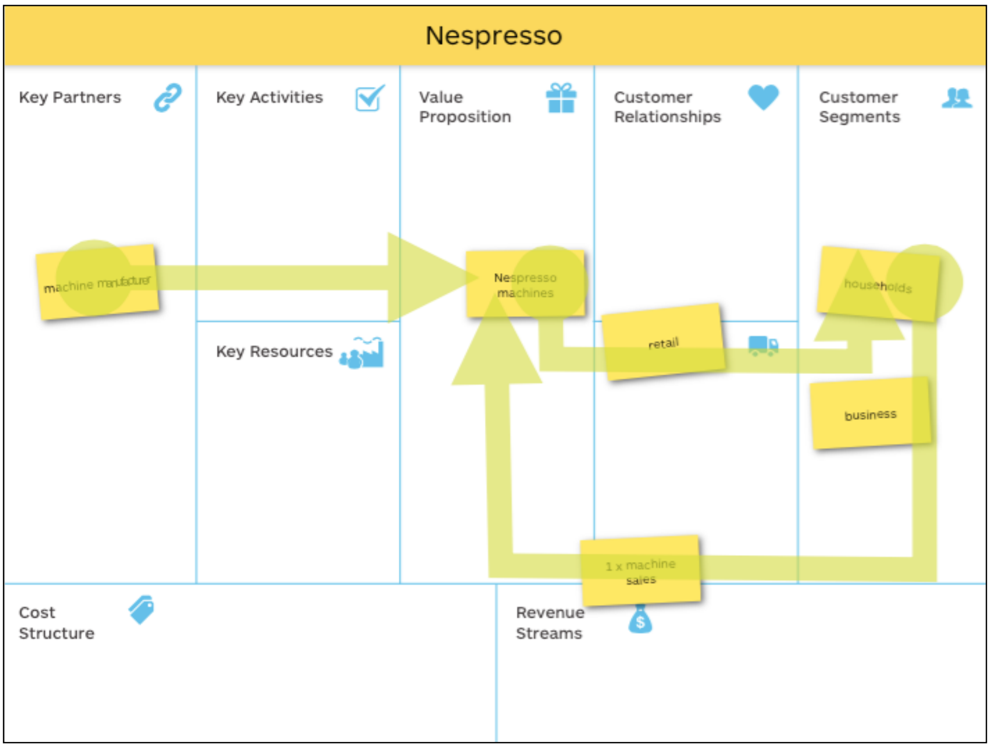
You can work with the canvas from any building block; there is no prescribed order to work in.
E.g. your company might have a patent but without a supporting business model, you could then work from the key resource the patent is and develop the canvas from this perspective. Like Xerox, your company can have existing customers and a new product but need to develop the value proposition and/or revenue streams. If you have an idea, work from the value proposition towards the customer segment and populate the canvas from this perspective.



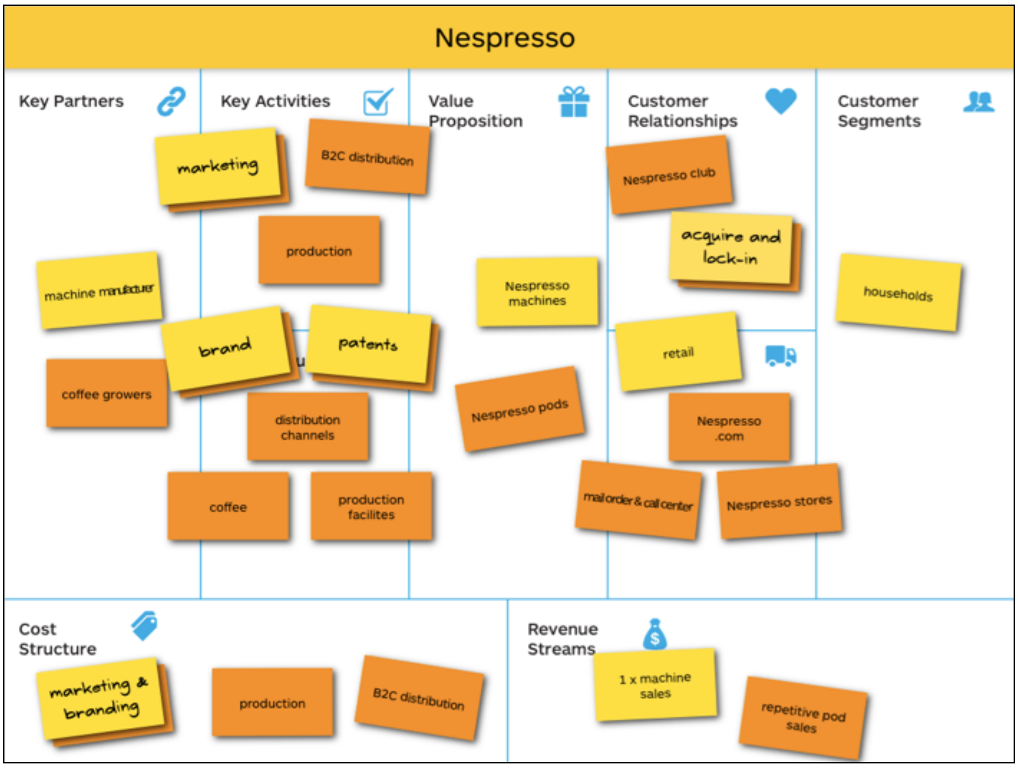
I will briefly go through the Nespresso business model canvas to showcase how Nespresso has built a very strong, self-reinforcing business model. The canvas has two different colour post-its; one representing the Nespresso machine and one representing the capsules or pods.

This example is not meant to capture every detail of the Nespresso offering, but rather shows the strategy of their business model. The Nespresso value proposition is to offer barista quality coffee in your home. Nespresso delivers on this value proposition with two products; a coffee machine and coffee pods for the machine.

The coffee machine is sold through retail stores mainly to households (more than 85%). The sale of the coffee machine generates a one-time revenue (1 × machine) that Nespresso must share with the retailers. Nespresso use key partners to produce the machines and their primary costs are marketing, branding and production of the machine.


Nespresso
Key Partners
Key Activities
Value Proposition
Customer Relationships
Customer Segments
Key Resources
Cost Structure
Revenue Streams
Nespresso machines
retail
households
business
1 x machine sales

The second part of the Nespresso business model – the pods was originally sold directly from Nespresso through mail orders, call centres and online channels. The use of the machine generates repetitive pod revenues directly to Nespresso with a high margin. But how is this possible? A margin above industry standard would normally attract a well of competitors. Nespresso had until quite recently patents protecting them from competitors producing pods for their machines. This creates a lock-in for the customers after the customer has been acquired. Lock-in are normally achieved either through patent protection and/or strong brand position. Well before their patents expired Nespresso has a clear strategy of building a high-end coffee brand. Opening of Nespresso brand stores was part of this strategy, although stores is a very costly way of distribution, for Nespresso it is an investment to protect the lock-in with their customers.



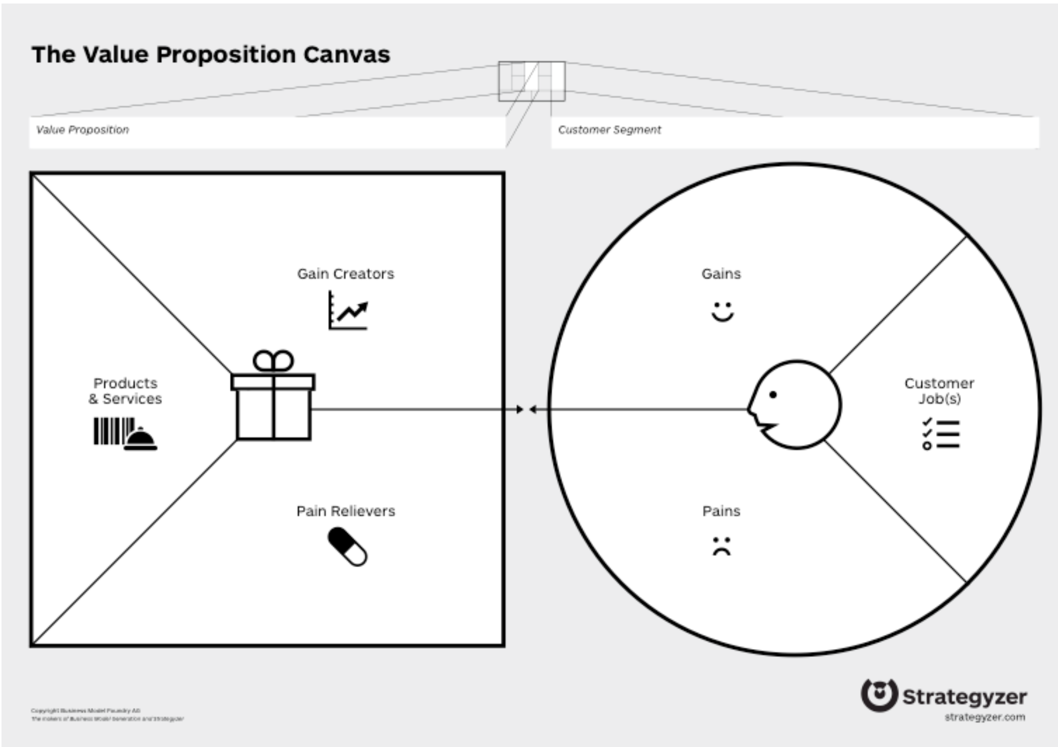
The Nespresso business model is a classical bait and hook, also commonly referred to as the razor and blades model. This business model pattern has an attractive initial offering that encourages future repetitive purchases. The razor and blade reference comes from King C. Gillette who invented the Gillette business model with cheap razor handles and more expensive blades. Gillette to this day protects their business model with a range of patents and a strong brand. This business model pattern requires strong patents or brand to secure customer lock-in for the repeat purchases.

2.1.1 Value proposition canvas – a business model canvas extension

In 2014 the Strategyzer team (led by Osterwalder and Pigneur) published the book Value Proposition Design as a sequel to Business Model Generation and an extension of the business model canvas. The value proposition canvas is zooming in on two of the buildings blocks in the business model canvas; the value proposition and the customer segment. The value proposition canvas consists of 2 sub-canvases, the customer profile and the value map canvas.

The customer profile assists you in defining more detail about your customer segment. One customer profile describes one specific segment in the business model canvas, breaking it into customer jobs, pains and gains.

The value map is a more specific description of one value proposition on the business model canvas. It describes the products and services related to the value proposition, the gains created by the products and services and the pains relieved by the products and services.



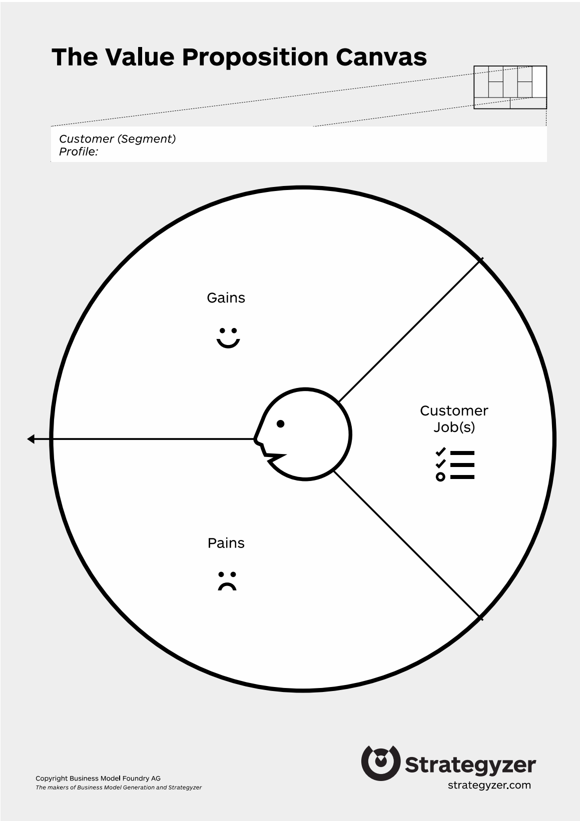
The customer profile

The customer is split into three sub-categories; customer job to be done, pains experienced before, during and after getting the job done and gains, describing the benefits the customer expects, desires and their aspirations.

Understanding the concept of job to be done is extremely important. The job the customers wants to have done is to fulfil a need (e.g. Facebook, dating site etc.) or solving a problem (enterprise software, the Xerox copier etc.).

Clayton Christensen has describes this concept in more detail in this 5 minute video, Understanding the job – http://goo.gl/NBo8OP.

Try to be as specific as possible when filling in the customer profile to clearly distinguish jobs, pains and gains.



The Customer profile side of the Value Proposition Canvas

Value map canvas

The value map consists of three parts; the products and services offered to the customer segment, the pain relievers and gain creators.

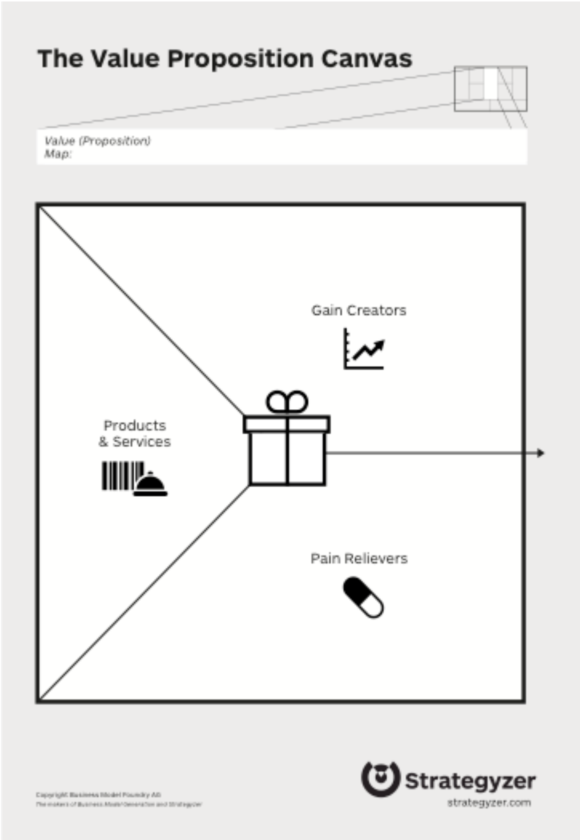
Product and services list all the products and services the value proposition for a specific customer segment is build around. The gain creators is a description of how your products and services creates gains for the customer, e.g. saves time, saves money, delight your customer in a new way compared to competition, the customer looks good (social benefit) etc.

As pain relievers you document how your products and services eases or eliminate customer pains.

The final step of the value proposition canvas is to assess the fit between the customer profile and the value map. Are you addressing the most important customer gains? Are you addressing the most painful customer pains? It's not necessary to address all pains and all gains to have fit between the customer profile and the value map, but the most important ones should be addressed. The final judge on whether you have fit or not are your customers.

You'll find the value proposition canvas on the next page. Take a few minutes and try to record what job's you are solving for your customer, which pains they have and the gains they are looking for.

Then move on to document your product and services and how those product and services creates gains and reduces pains for your customer segments.



The Value map side of the Value Proposition Canvas

How is the fit between the customers profile and your value map?

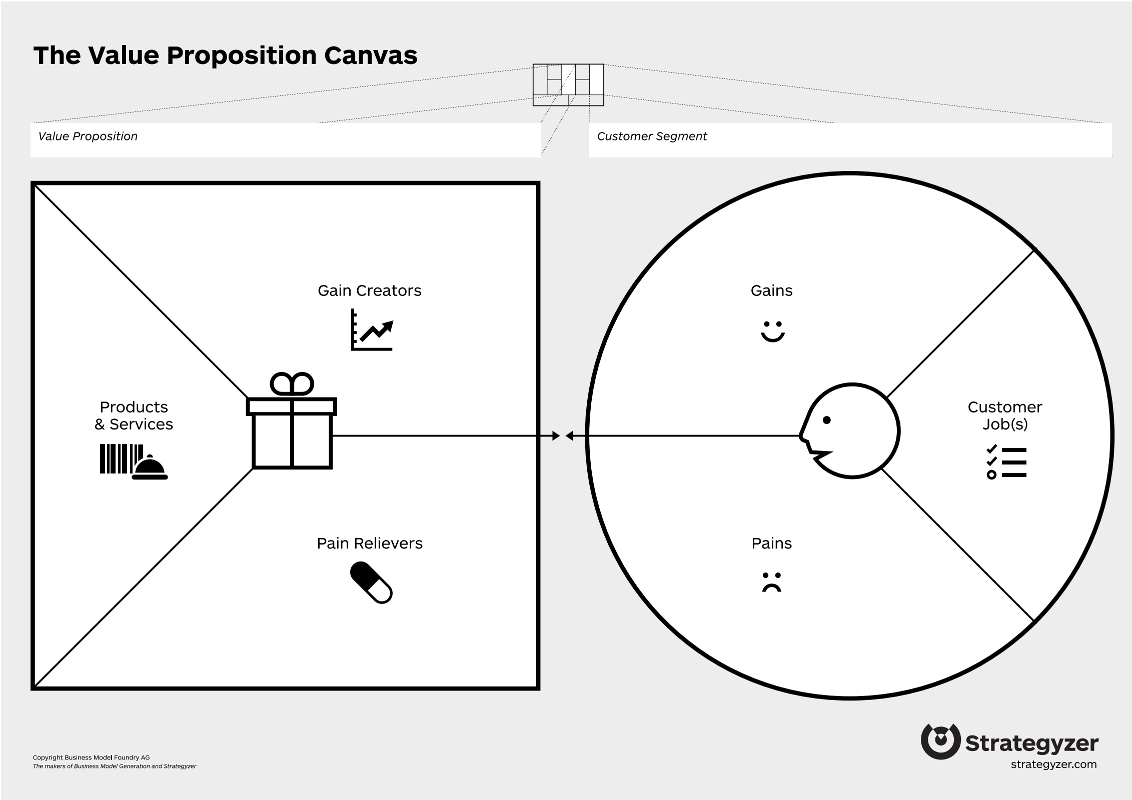
Did you get any new insights about your business model?

3 *types of fit*

1. Problem/solution fit
You have achieved problem/solution fit when you have validated that customers care about certain jobs, pains and gains, and designed a value proposition addressing these jobs, pains and gains. This is still on paper.

2. Product/launch fit
Product/launch fit when you have identified the minimum viable product you can launch to satisfy the most important jobs, pains and gains your customer segment has. You should now be learning from customers' reception of your value proposition. If you have already launched a product in the market make sure you use it to validate your problem/solution fit.

3. Product/market fit (business model fit)
You have validated that you have a scalable, repeatable and profitable business model.


The Value Proposition Canvas
Value Proposition
Customer Segment
Gain Creators
Products & Services
Pain Relievers
Gains
Customer Job(s)
Pains
Copyright Business Model Foundry AG
The makers of Business Model Generation and Strategyzer
Strategyzer
strategyzer.com

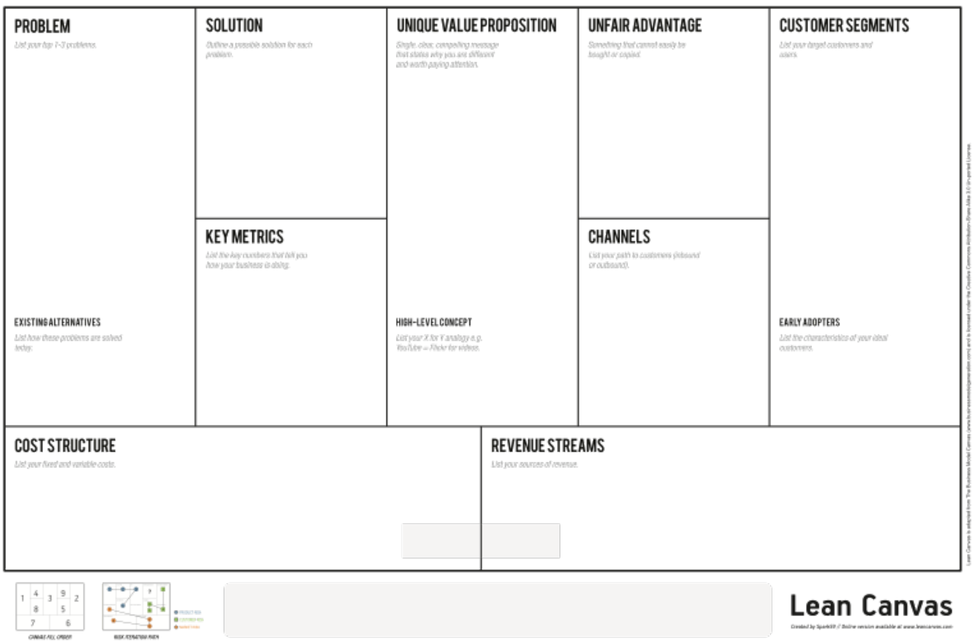
2.2 Lean Canvas by Ash Maurya

The Lean Canvas is a development / adaptation of the business model canvas as it was developed by Alexander Osterwalder. Ash Maurya is a serial-entrepreneur and blogger. His background is from software engineering (like Eric Ries who wrote Lean Startup). Maurya started to blog about his experiences and experiments as an entrepreneur that he composed into a book in 2010 called Running Lean.

Ash Maurya had been using Steve Blanks worksheets from “The Four Steps to Epiphany” as an entrepreneur and also saw how other entrepreneurs used the business model canvas to capture business model hypotheses on a single page. He started using the business model canvas and ended up with some modifications to the canvas based on his experience and testing.

His objective was to create a canvas that was specifically targeted at entrepreneurs and the context they operate in. All entrepreneurs and start-ups operate under conditions of extreme uncertainty. Maurya adapted the canvas to better accommodate the uncertainty faced by entrepreneurs. He also had a specific goal of making the canvas more action oriented. The Lean startup movement and the principles of lean development heavily influenced Ash Maurya. This background combined with the adaptation of the business model canvas resulted in the Lean Canvas.

The structure of the Lean Canvas is equal to the Business Model Canvas, consisting of 9 interlocking building blocks. However, Ash Maurya made changed four of the building blocks compared to the Business Model canvas arguing that his adaptation better captures the uncertainty and risks start-up deals with. In addition, he added sub-sections to the value proposition, customer segment and problem building block.



The four building blocks he omitted from the Business Model Canvas are;

Key Partners; the argument for dropping Key Partners was that when you are start-up without a validated product in the market search for Key Partners can be a form of waste. Most startups don't require specific key partners from the start because they deal in unknown and untested products. Hence, it would be a waste of time trying to build such relationships. Keeping lean principles in mind we do all we can to eliminate waste. Waste is all activities that don't produce value for a customer.

Key Activities and Key Resources; Both Key Activities and Key Resources helper others to see from the outside in order to understand what the start-up is doing more than it helps the entrepreneur to understand their own start-up and develop insight about the required business model.

Customer Relationship; A start-up that operates under extreme conditions of uncertainty, dealing in unknown and untested products should always have a direct relationship with their customers. In Maurya's own words *"I am an advocate of starting every product, no matter what you are building, with a direct customer relationship, through customer interviews and observation."* As such, there is no need to document the customer relationship.

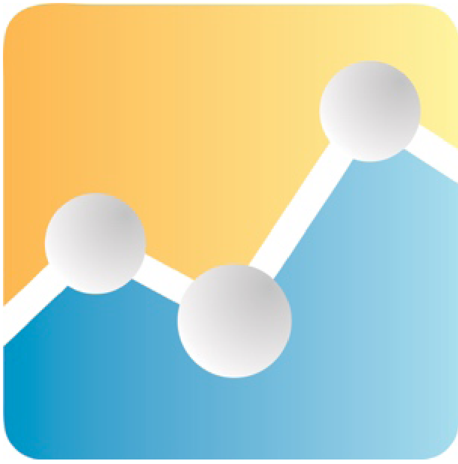
The four building blocks, problem, solution, key metrics and unfair advantage were added as an attempt to improve the Business Model Canvas.

Problem (replacing Key Partners)
Problem was introduced because most startups fail – not because they fail to build what they set out two build, but because they waste time, money, and effort building the wrong product. Maurya attributes a significant contributor to this failure to a lack of proper "problem understanding" from the start.

In the Problem building block you should list the top 3 problems that you believe you are addressing for your customer segment. This building block is similar to the jobs to be done concept in the Value Proposition Canvas that now accompanies the Business Model Canvas (the value proposition canvas was did not accompany the business model canvas when it was first released).

Solution (replacing Key Activities)
After having understood the problem to address you need a solution. Hence Maurya added a Solution building block to describe the top 3 features of your proposed solution. He also kept the physical size of the Solution building block small to enforce a focused approach. Keeping the solution box small aligns well with the concept of a "Minimum Viable Product" (MVP).

Key Metrics (replacing Key Resources)
Startups often drown in a sea of numbers in an attempt to bring order to the chaos of uncertainty. At any given point in time though, there are only a few key actions (or key macro metrics) that matter. Lean Startup innovation accounting can be a good source of meaningful metrics (also see Lean Analytics). The one metric that matters should be what you have in Key Metrics. What this metrics is, is dependent on your development stage, e.g. how much of the business model you have been able to validate.



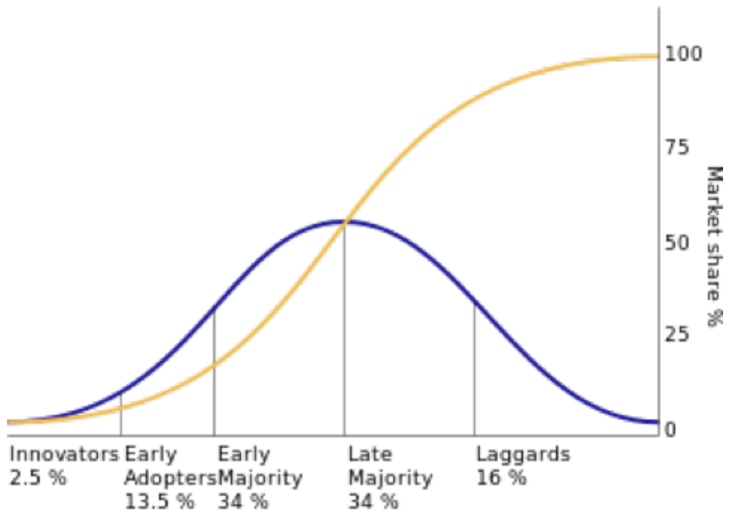
Unfair Advantage (replacing Customer relationships)
Maurya advocates starting every product (no matter what you are building) with a direct customer relationship; hence the Customer relationship is pre-defined. In comes Unfair Advantage – another name for competitive advantage or barriers to entry. A true unfair advantage is something that cannot be easily copied or bought. This overlaps with the concept of Key Resources in the Business model canvas.

In addition to altering four of the building block to create the Lean Canvas Maurya added sub-sections to customer segment, value proposition and the problem building block.

Existing alternatives (in Problem) – when document the top 3 problems, Maurya also encourages you to look at existing alternatives and list how the problems are solved today.

High-level concept (in Value proposition) – Three to four words describing your business model/value proposition in a nutshell. E.g. Spotify for music videos (vidFlow).

Early adopters (in Customer segment) – Lean canvas starting position is that of a start-up so market adoption is very relevant. Taken from the diffusion of innovation theory as an entrepreneur you should have an idea of what customer segment is most likely to be your innovators and early adopters. For more background on market adoption also see Geoffrey A. Moore's seminal Crossing the Chasm (I recommend you pick up the 3. edition from 2014, relevant updates with non-physical distribution channels and differences between B2C and B2B markets). For a short intro to the concept you can also look at http://goo.gl/FUqRXw.



Diffusion of new innovations in the market as presented by Everett M. Rogers

2.2.1 Fill-in order of the Lean Canvas

The starting point of the Lean Canvas is that of an entrepreneur. Given that most start-ups fail because they try to solve the wrong problem, there is a recommended fill-in order for the lean canvas. The book, Running Lean, which Ash Maurya published in 2010, accompanies the Lean Canvas tool. The book contains additional work steps to assist an entrepreneur in filling the canvas and validating its content.

Maurya recommends you should start by defining the customer segments and their top three corresponding problems that you will address. Then go on to create the unique value proposition. The complete filling-order of the canvas is depicted in the figure below. It's recommended that you create one Lean Canvas for each customer segment. You can also leave a building block blank at the start. In a start-up context dealing with unknowns it is impossible to have all the answers from the start. The focus should be on validating the hypotheses you have document and evolve the canvas over time.

Once you have defined your early adopters and their top three problems you should start talking to these prospective customers. The purpose of these interviews is to validate that you have a problem worth solving.

<table>
<tr><td colspan="2" rowspan="2">Problem
Top 3 problems
1</td><td colspan="2">Solution
Top 3 features
3</td><td colspan="2" rowspan="2">Unique Value Proposition
Single, clear, compelling message that states why you are different and worth buying
2</td><td colspan="2">Unfair Advantage
Can't be easily copied or bought
7</td><td colspan="2" rowspan="2">Customer Segments
Target customers
1</td></tr>
<tr><td colspan="2">Key Metrics
Key activities you measure
6</td><td colspan="2">Channels
Path to customers
4</td></tr>
<tr><td colspan="5">Cost Structure
Customer Acquisition Costs
Distribution Costs
Hosting
People, etc.
5</td><td colspan="5">Revenue Streams
Revenue Model
Life Time Value
Revenue
Gross Margin
5</td></tr>
</table>

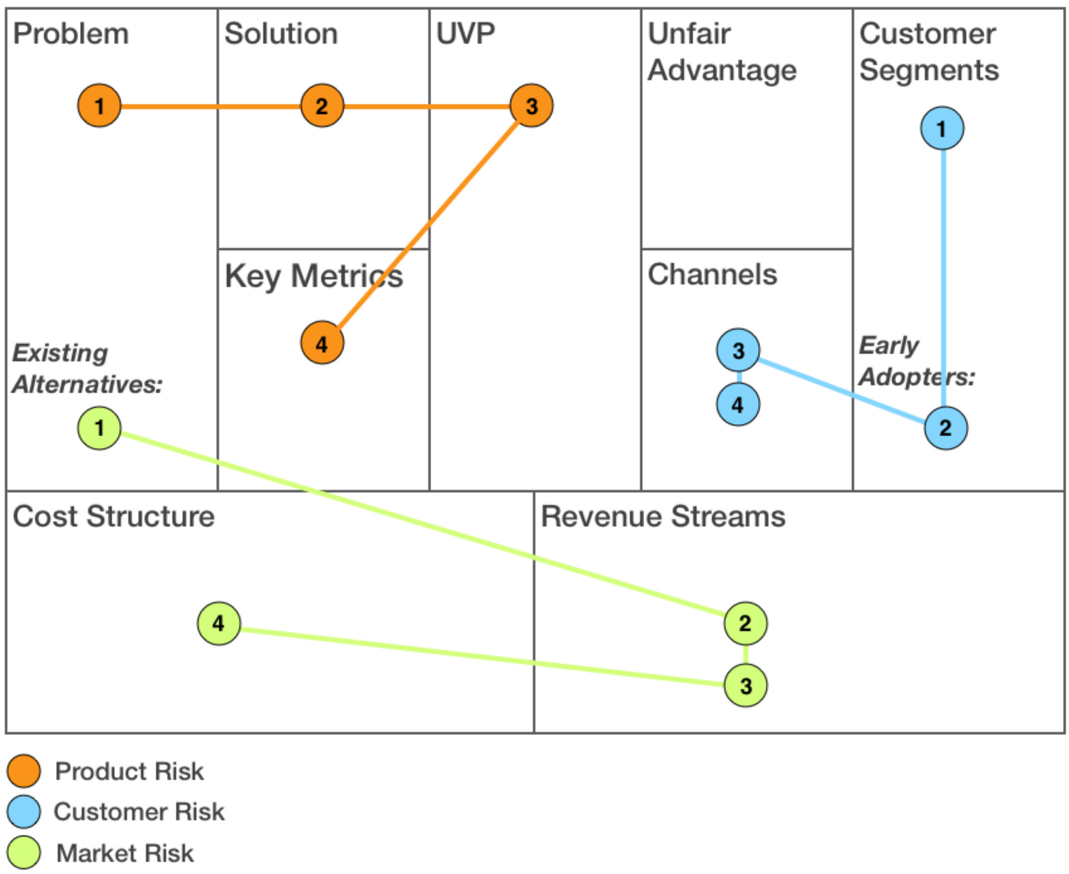
Lean Canvas is adapted from The Business Model Canvas (http://www.businessmodelgeneration.com) and is licensed under the Creative Commons Attribution-Share Alike 3.0 Un-ported License.

Having validated that you have a problem worth solving you should move on to the solution. Define the top 3 features and again talk to your prospective customer to validate that this would solve their problem. Having done so you now have problem/solution fit, comparable to the fit you will get when using the value proposition canvas.

The next steps of the Running Lean / Lean canvas approach would to build a minimum viable product or service to actually test your product or service. A minimum viable product

2.2.3 Risk categories

With the starting point that all entrepreneurs and start-ups operate under conditions of extreme uncertainty, Maurya wanted to address the riskiest assumptions about your start-up/business model as quickly as possible. He divided his canvas into three distinct risk categories;
1) product risk, 2) customer risk and 3) market risk.
The mapping of the lean canvas building block to the risk categories are shown below.



Product Risk – Getting the product right

You should first make sure you have a problem worth solving. If nobody cares about the problem (not enough potential customers, either because it isn't perceived as an important enough problem or no willingness to pay) you market will not be large enough and your current business model must be changed.

The first version of your product or service should be the smallest possible solution (MVP). *"If you are not embarrassed by the first version of your product, you've launched too late."* – Reid Hoffman, founder of LinkedIn.

Build and validate your MVP at small scale to demonstrate your unique value proposition. If it all checks out go on to verify it at large scale.

Customer Risk – Building a path to customers

Find your evangelists! That the early, early adopters that identify with the pain you are addressing. This is the group who really want your product now. They don't mind if its full of bugs, slow of doesn't work properly, and they will give you tons of feedback on what to improve.

When building your path to customers it´s okay to start with outbound channels. In the beginning you need to actively recruit customers, but you should gradually build/develop scalable inbound channels – the earlier the better.

Market Risk – Building a viable business

Make sure you know how your customer segment solves the problems you are addressing today. Identify competition through existing alternatives and pick a price for your solution. When talking to customer you should also test pricing first by measuring what customers say (verbal commitments). If you plan to charge for a product or service Maurya strongly recommend you to charge from day one. If you don't you have not validated neither the price nor the pain of the customer segment.

Develop a landing page or launch your MVP app and the measure price what your customers actually do. Adjust your price and value proposition accordingly. Remember that it is possible to increase the price, but it is generally easier to lower the price. In doubt, start with a higher price and reduce if you have to.

Finally you should optimize your cost structure to make the business model work. When you get to this point you should have arrived at a scalable, repeatable business model

You will probably have recognized how the fill-in order and the risk categories mirror each other. By addressing the highest risk factor in each risk category as soon as it is possible the Lean Canvas approach seeks to maximize value and minimize waste.

2.3 Open innovation business model by Chesbrough and Rosenbloom

Henry Chesbrough and Richard S. Rosenbloom have researched and published on open innovation business models. Both academics (Chesbrough is currently lecturing at University of Berkeley, Haas School of Business) they have a more theoretical approach to business models. Chesbrough and Rosenbloom (2002) suggest that the business model of a technology company is the construct that mediates the value creation process between the technical and economic domains, selecting and filtering technologies and packaging them into particular configurations to be offered to the market.

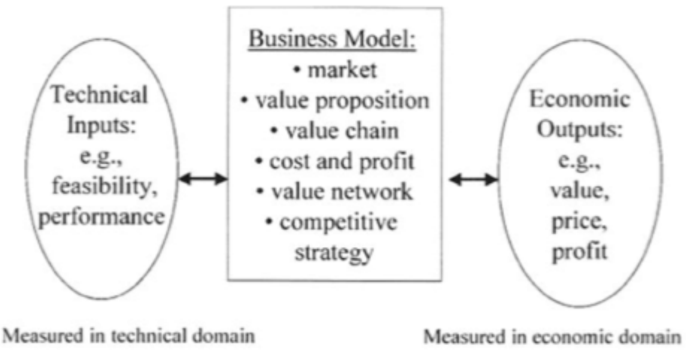


Figure 1 The business model mediates between the technical and economic domains.

Chesbrough and Rosenbloom (2002) suggest that the functions of a business model are to:

- Articulate the value proposition, that is, the value created for users by the offering based on the technology
- Identify a market segment, the users to whom the technology is useful and for what purpose
- Specify the revenue generation mechanisms for the firm
- Define the structure of the value chain within the firm required to create and distribute the offering, and determine the complementary assets needed to support the firms position in this value chain
- Estimate the cost structure and profit potential of producing the offering, given the value proposition and value chain structure chosen
- Describe the position of the firm within the value network linking suppliers and customers, including identification of potential complementors and competitors;
- Formulate the competitive strategy by which the innovating firm will gain and hold advantage over rivals

On of the key points from Chesbrough and Rosenbloom is that new innovations often require new business models. This is where the idea of business model innovation really started to gain traction.

The articulation of the value proposition and identification of the market segment are highly interdependent. The value proposition requires the articulation of the nature of the offering to the chosen market segment. This is seen as fundamental to the success of commercialization of the innovation. It means pitching the advantages of the technology, such as lower cost or new opportunities, to the appropriate market segment to generate value for the business. For many technologies there are a number of ways that a new technology can be offered to particular target market segments. Matching the two can be of critical importance. This involves developing the revenue model or how the firm is to appropriate value from the innovation (Amit and Zott 2001). Part of this process is specifying the revenue generation mechanisms best suited to the target market segment. Technologies may be packaged into products and sold, licensed to the end user or embodied into a service which is hired out involving quite different pricing regimes each with different implications for pricing.
A further task in the Chesbrough and Rosenbloom concept of the business model is to define the structure of the value chain, and determine the complementary assets needed to support the firm's position in this value chain.

The value chain displays how total value is created by the organization and consists of value activities and a margin. Chesbrough and Rosenbloom use the term 'value network' to describe the relationship between the firm and its suppliers and customers. The role of the business model is to position the firm in the value network in such a way that the firm can capture value from its innovation.

The concept of the value network developed by Christensen and Rosenbloom describes 'a nested commercial system' of firms that contribute to the production of a particular computer component or set of components. These are then sold downstream to the assemblers of these components for integration into the next stage of the product pipeline.

Chesbrough and Rosenbloom (2002) suggest that having determined what the market will bear for the new product or service, places a discipline on the costs of development and production. The development of the business model is not static but a dynamic process subject to change through learning and adaptation. For instance the process of deriving value from a technology-based offering requires a learning process of developing and adapting the technology to meet market requirements. Accordingly it may be necessary to adopt an iterative process between adjustments to product and the market segment to align the product with the cost of production.

Finally the concept of the business model includes consideration of the competitive strategy by which the innovating firm gains and holds an advantage over its rivals.

Although the approach taken by Chesbrough and Rosenbloom are more academic in style, they incorporate many of the same buildings block in their business model as Osterwalder and Pigneur and Maurya. They also emphasize the same relationships and the importance of a self-reinforcing business model.

2.4 Business model innovation by Patrick Staehler

In 2001 Patrick Staehler published his PhD called Business Models in the Digital Economy. In his thesis, he developed the concept of business model innovation. Staehler wondered if the classical units of analysis for strategy "the firm" and "the industry" were suitable for understanding the changes that could be observed in the digital economy. The answer was no, and he developed his business model concept to better understand the changes that could be observed in the digital economy. Stähler's business model consists of four building blocks;

Value proposition

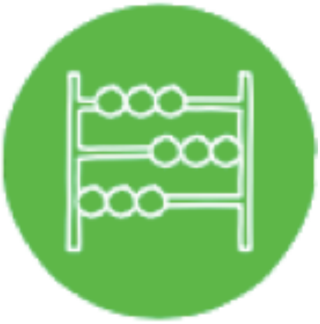
The value proposition in Staehler's business model should answer the questions; Who are our customers? What jobs do we solve for our customers? What benefit do we create for our customers and partners? The content is very similar to the business model canvas and the generic agreement on what should be covered by a value proposition.

Value architecture

The value architecture building block covers the channels used to reach customers, the customer relationship, key partners needed to produce the value proposition, key activities and key resources. The value architecture building block pretty much covers all of the back stage, everything we need to produce and deliver the value proposition to our customers. In addition it also covers how we deliver the value proposition to our customers and the type of customer relationship we want with our customer.

Revenue model

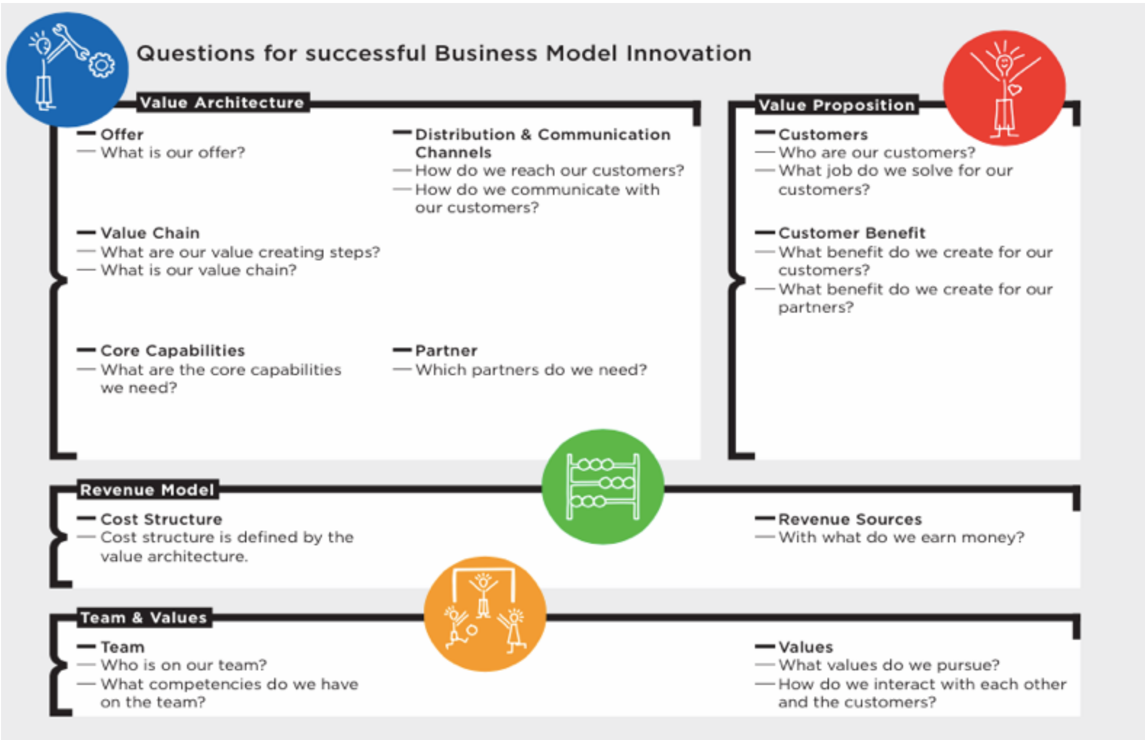
The revenue model is a straight forward profit formula; which revenue streams do we have and what cost structure do we have, as defined by the value architecture



Team & Values

Teams and values covers aspects like; who is on our team? What competencies do we have? What values do we pursue? How do we interact with each other, customers and partners? This building block does in part represent key resources and relationship, but it also represents something new when bringing in the organizational aspect to a larger extent and focus on goals and objectives. The business model must be aligned with the organization's current capabilities and objectives.

Put together on a single page the business model Staehler developed looks like a canvas with four buildings blocks;



Staehler approached business model innovation with the epicentre being one of the buildings blocks in his business model;

1. Value innovation
   Offering a better value proposition for an existing or new problem

2. Architectural innovation
   Innovating by reconfiguring the value chain so that a better value position emerges

3. Revenue model innovation
   Changing the revenue mix and thereby creating a better value proposition

4. Cultural innovation
   Change the culture to create more value, e.g. Zappos with excellent customer service

Overall, Staehler's business model rests on many of the same principles as the business model canvas. There are 11 sub-sections to Staehler's canvas, which can be easily transferred onto the buildings blocks of Osterwalder and Pigneur's business model canvas.

3 Working with business models

You now have an understanding of what a business model is and different business model frameworks. The next step is to map out your existing business model or create a business model for a new innovation or venture. Follow these steps to make a first draft;

1. Gather people from different departments, sales, marketing, product development etc. Customer facing staff is especially valuable when creating the canvas as they have insight on your customers' needs and wants. Early in the process we would like as many perspectives as possible and more participants are better than few. If more than 6–8 participants it's preferable to split into parallel groups to generate more and a wider perspective of business models.
2. Have a facilitator present the business model framework you have chosen to use to establish a shared understanding and language for the development of the business model. The vision and objective of the process should also be communicated in a simple and concise manner. Creating understanding and buy-in to the process is absolutely crucial to secure commitment to the end-results.
3. Make sure you have plenty of free wall space. Print out large versions (recommend A2 or larger) of the business model framework you are using and stich the printouts to the wall. Working in groups, go through all the buildings blocks of the business model framework. Specify what customer segments you are serving, how you are serving them (through which channels and with what kind of relationship) and so on. Populate the framework using post-its or similar, this makes it easier to experiment and change the configuration of the business model.
   A business model workshop should ideally take place in a large open space with lots of wall space. As the groups populate their business models they create a gallery of business models where the others participants can be inspired but also challenge the logic of the group.
4. Have all the groups select one business model they believe represents have you create value for your customers and how you capture that value. All groups should present their business model to the other groups for constructive feedback.
5. Working in a large group you should be able to boil down the business models from the group into one business model that represents the current business model for your organization. If you are able to arrive at one current business model: Congratulations, you're now ready to validate your baseline business model and progress on to business model innovation.
   If you're not able to arrive at one current business model – don't panic! There is a need to discuss more, do we have several different business models in our company (very possible if you're a large organization serving many customer segments), do we understand each other well enough (i.e. double check to make sure we mean the same thing by what we say) etc.

This process of going through, articulating and visualizing your business model, creates a deeper understanding of the rationale of how value is created for the customer segments you are serving and also how your organization captures some of that value. By testing and experimenting with business models (see chapter 3.3) we can validate our perceptions about how we create value. By innovating our business model (see chapter 3.2) we can create sustainable competitive advantage.

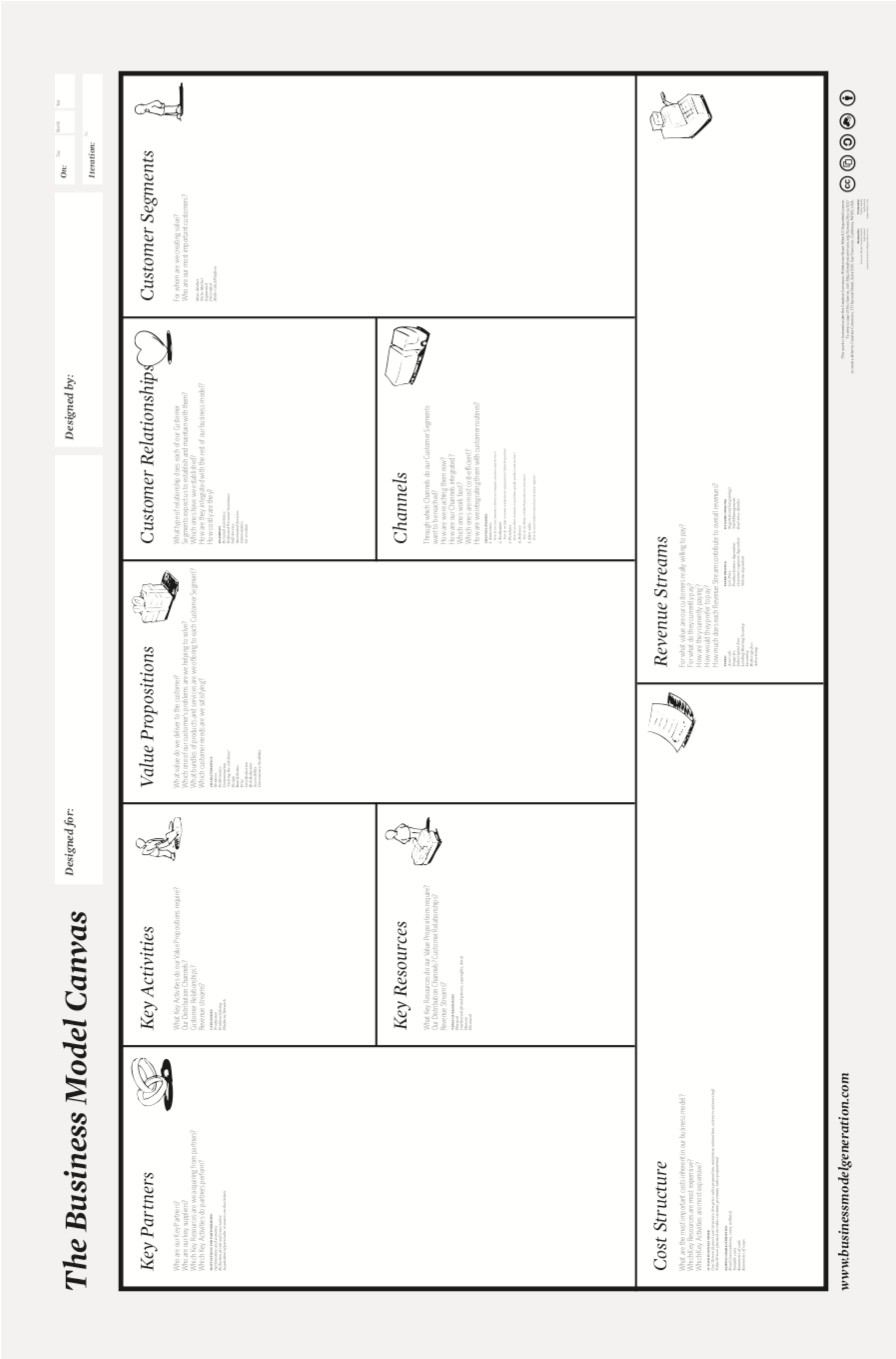
Exercise

If you're reading this on the train or you're waiting in the lounge for your flight, grab a pen and use the cheat sheet on the next page to create your initial draft of your organization's business model.

TIP

Use different color post-its as a legend to display the value creation logic of a specific customer segment

Every customer segment should have a value proposition and by using different color post-its it's easy to spot empties in the business model.


The Business Model Canvas
Designed for:
Designed by:
On:
Iteration:
Key Partners
Key Activities
Key Resources
Value Propositions
Customer Relationships
Channels
Customer Segments
Cost Structure
Revenue Streams
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3.1 What makes a business model great?

A great business model should be more than the sum of its building blocks. The individual building blocks of the business model should be self-reinforcing. The blocks should complement one another and be internally consistent. E.g. Nestle leveraged their patents on capsules when creating the Nespresso business model. The patent created a lock-in for the customers to Nespresso and you could only buy the capsules online directly from Nespresso. In this way Nespresso was able to create a closed eco-system for their business model (a platform archetype business model). A few years before their patents started to expire in 2012 Nespresso build brand stores to reinforce they luxurious feel with Nespresso and grow customer loyalty. This was an additional cost for Nespresso, but at their patents started to expire it was also an adjustment of their business model to a new competitive context.

If there's a lack of reinforcement in your business model, you should apply business model innovation to refine the business model. See section 3.2 for frameworks and tools to help the innovation process.

Is your business model robust? A good business model should be able to sustain its effectiveness over time. Firstly, it should be robust enough to fend off business model imitations; it should be hard to copy. Secondly a robust business model will defend your position in the value network (so customers, suppliers, or other players can't capture the value you create by flexing their bargaining power etc.) By establishing a key differentiator, such as customer attention or superb execution, business models build barriers to entry that protect their profit streams and your organization's position in the value chain. Thirdly the business model should offer unique value to protect from substitute products or services. Offering unique value can be in the form of a new idea, but more often it is a new combination of product and service features that offers more value (e.g. lower price for the same benefit or more benefit for the same price). Although the period of effectiveness may be shorter in the Internet age than it was before, robustness is still a critical parameter of your business model.

Successful business models are grounded in reality. This might seem as an obvious characteristic, but I often see business models that don't take reality all that seriously. A great business model should be based on validated feedback about customer behaviour. Their cost structures fit their revenue streams, day in and day out. Revenues are higher than costs over time. Obvious? Many firms, new and old, lack a clear understanding of where they make money and why customers prefer their offerings.

Completeness; the business model must be complete. Every customer segment must be accompanied by a value proposition addressing their jobs, pains and gains. The other buildings blocks of the business model must also addressed to make sure you have completeness in your business model.

Is the business model aligned with company goals? The choices made while designing a business model should deliver consequences that enable an organization to achieve its goals. This may seem obvious until you consider a counterexample. In 1970, Xerox set up Xerox PARC (Palo Alto Research Centre). PARC has been responsible for such well known and important developments as laser printing, Ethernet, the modern personal computer, graphical user interface (GUI) and desktop paradigm, object-oriented programming, ubiquitous computing, amorphous silicon (a-Si) applications, and advancing very-large-scale-integration (VLSI) for semiconductors.

Despite its huge success as a research and innovation centre for Xerox, PARC was not very successful in creating new businesses or capture value from its innovations for the parent. This has in large been attributed to a distressing lack of alignment with Xerox's goals. Most of the value from the innovations at Xerox PARC was captured by companies started by formers Xerox PARC employees that became frustrated with the failures of the parent company to create new business from the innovations.

This short list of some of the key characteristics of a great business model is by no means an attempt to be exhaustive. I'm sure you will find other characteristics that will make a business model great. However, without these five characteristics, self-reinforcing, robust, grounded in reality, complete and align with company vision and goals you will not be able to create a great business model.

3.1.1 What characterizes a great value proposition?

Value proposition is such an important part of the business model so it deserves some special attention. Without a great value proposition it will be difficult not matter how great the rest of the business model is to capture value from your customers. The next paragraphs mention only some of the most important characteristics, but you will surely find more if you search for yourself.

The first characteristic of a great value proposition is to focus on the jobs, pains, and gains that matter most to customers. Target few jobs, pains, and gains. Focus on unsatisfied jobs, unresolved pains, and unrealized gains. The best value propositions target only one or very few underserved jobs, pains and gains and but do so extremely well.

Targeting only one or very few jobs and doing them extremely well will enable you to outperform your competition substantially on at least one dimension. This will create a significant differentiation from competitors on jobs, pains, and gains that customers care about.

A great value proposition also aligns with how your customers measure success. It communicates the concrete results a customer will get from using your products and/or services in a way that resonates with the customer segment. Lastly, the value proposition should be embedded in a business model that enforces the value proposition through the other building blocks.

3.2 Creating new business models / business model innovation

It's often helpful to have a framework or tools to assist with business model innovation. Tools and framework can shift our focus enabling us to see opportunities otherwise lost and generate alternative solutions. In the following I will briefly introduce some techniques than can be used to innovate an existing business model, or create an entirely new business model. It's highly recommended to have a facilitator that's not a participant in the business model innovation to get the most effect from the tools and frameworks suggested.

Innovative business models can be created from different epicentres of the business model. Customer-driven innovations are based on customers job, pains and gains (Ash Maurya always recommend this customer-centric starting point). Finance driven innovations, created by new revenue streams, new pricing mechanisms (e.g. the Xerox case) or radically changed cost structure (e.g. Skye and Ryanair). Resource driven innovations are based on existing infrastructure and/or intellectual property (e.g. Amazon cloud services and Nespresso).

> *"Not everything we start ends up fitting with our businesses later on. Many of the ideas we work on here involve a paradigm shift in order to deliver value. So sometimes we must work particularly hard to find the "architecture of the revenues." … here at Xerox, there has been a growing appreciation for the struggle to create a value proposition for our research output, and for the fact that this struggle is as valuable as inventing the technology itself."*
>
> John Seely Brown, Chief Scientist of the Xerox Corporation and Director of the Xerox Palo Alto Research Center (from 1986 until 2002).

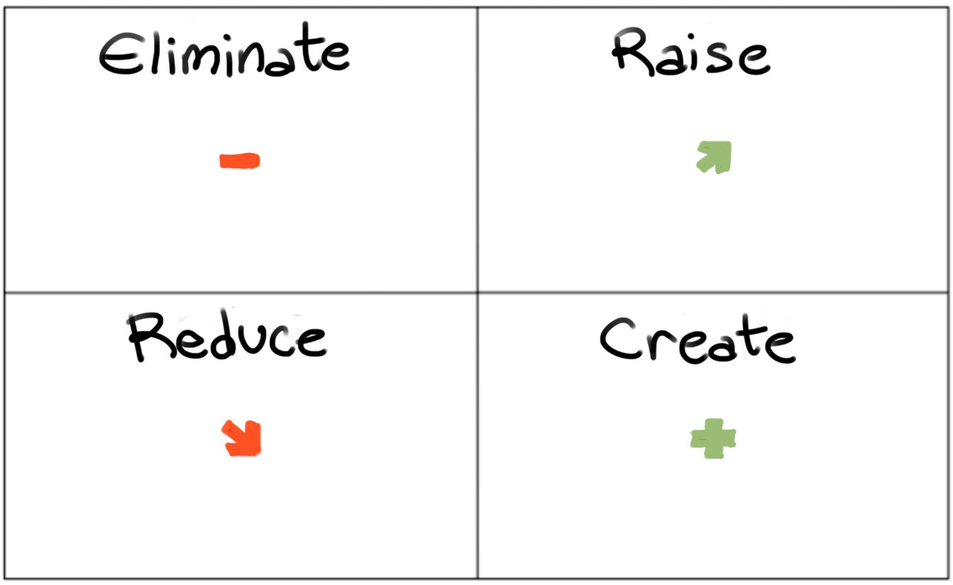
3.2.1 What if…

Open questions like "What if…" can be surprisingly powerful in generating new insights and identifying opportunities. By challenging, "the way things are done around here" we can break free from assumptions imposed by our daily context and see new opportunities. It's important that the group is open minded and not critiquing suggestions in an early stage of exploring what if's.

What if calls were free? (Skype)
What if we charged for applying for a job at our company? (RyanAir)
What if you could download 1000 songs to your pocket? (Apple)
What if you could get paid when driving somewhere by taking a passenger? (Uber)
What if our customers assembled the furniture themselves? (IKEA)
What if we gave away our product for free? (Google)

3.2.2 4 actions framework

The 4 actions framework is originally from the Blue Ocean Strategy book. It is used to reconstruct buyer value elements in crafting a new value curve. In the context of a business model we use it a conceptual tool to reflect on our business model. What can we eliminate in our business model? What should we raise or reduce? Are there things that should be added (create)?



An excellent example of elimination is Skype. Skype defined their value proposition delight to be; it should be free to make calls. This put a lot of constraints on their business model for it to be sustainable. Given this constraint Skype set out to define a new telecommunication business model;

1. First they eliminated the need for infrastructure by using the internet that customers already paid for
2. Secondly, they used your PC to code and send the calls
3. Thirdly, they used the PC's of their users as nodes to route the traffic around the world
4. Fourth, they eliminated customer service

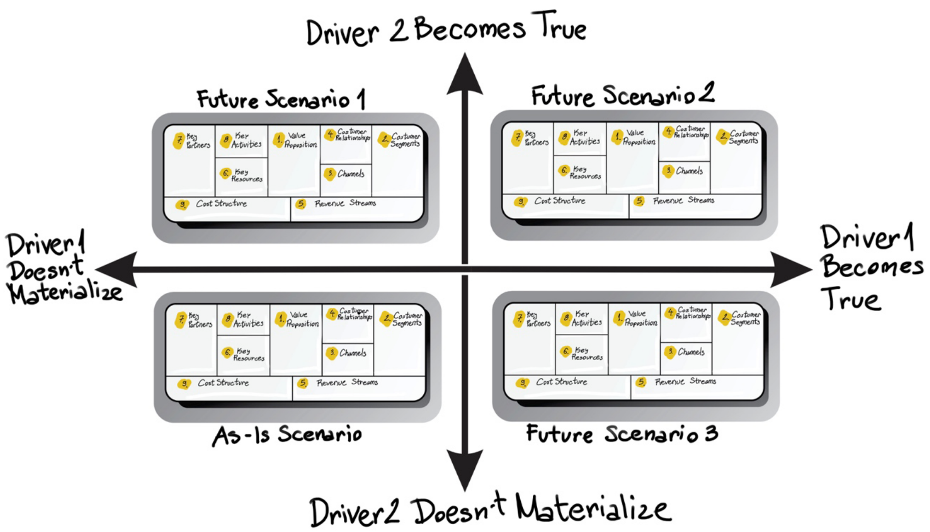
This is what Jonas Kjellberg (former CEO of Skype) calls innovating in zeros. In sum, these changes to the business model were disruptive for how we make calls. Skype has been hugely successful and demonstrated the value of business model innovation.

Try the 4 actions framework on your business model to innovate. What should you reduce or raise? Should something be eliminated? Can we add products or services that would provide additional value to our customers or make us capable to serving a new customer segment?

3.2.3 Scenario models

Scenario models is yet another technique to help us explore and innovate the business models of the future. I recommend that you develop 3–4 different future scenarios to work on your business model for the future. Having concrete scenarios with future context is often more productive than free brainstorming because the concrete description of future scenarios sets some direction.

One way of developing scenarios is to look at analysis of your industry and try to define a couple of macro-trends that could be the ones driving the market in the future. Select two drivers and map then in a 2×2 diagram like the one below.



The quadrant to the bottom left represents the as-is where none of the macro trends becomes true. The three other quadrants represent a future scenario where one or both of the macro drivers become true. This scenario framework will increase consciousness about how the context of your business model is changing and what you can do to counter or exploit those changes to your favour.

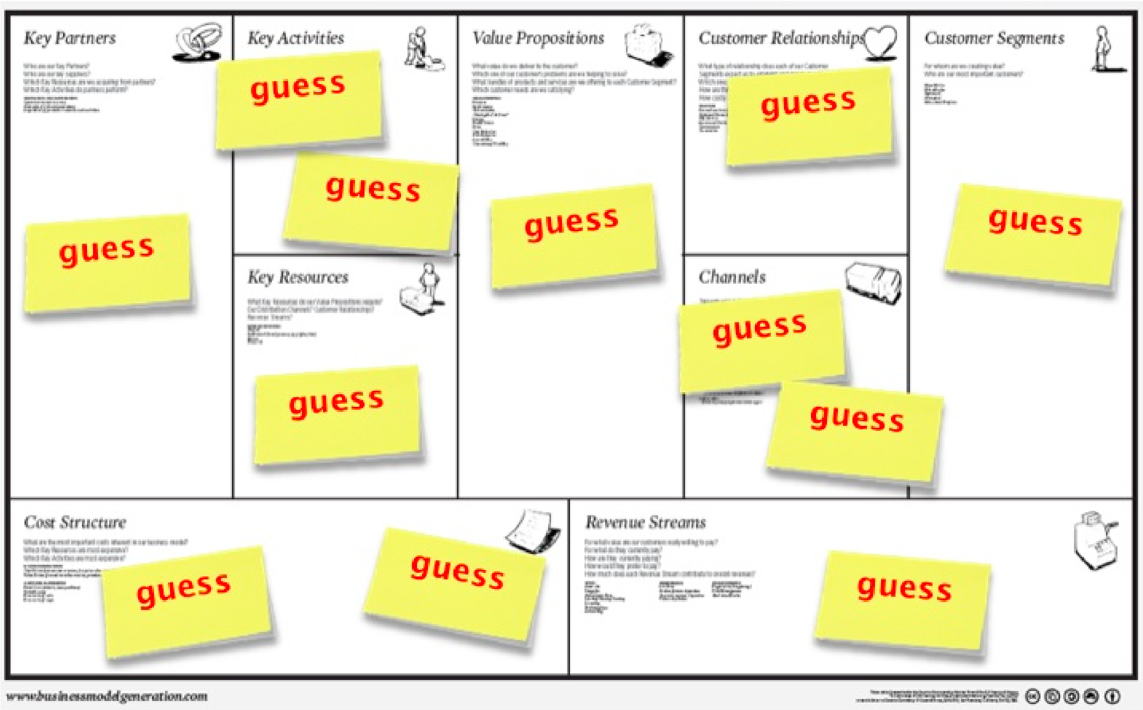
3.2.4 Impose constraints

Imposing constraints is another technique that can be very effective. If you have hard constraints in your business model already, or you expect to have so in the future you could set that constraint as a given in your business model and innovate from this fixed point.
Constraint based approaches can create novel and unexpected results in your business model.

3.3 Testing new business models

So you have gone through some hard work, participated in a few workshops and have come up with a new business model and a killer value proposition. The good news is that you have generated new insights and knowledge about your value proposition and business model. The bad news is that we now need to check whether the business model takes reality seriously.

No business plans survives first customer contact! It's the same for your business model. When documenting your current business model you have developed hypotheses not facts. Now it's time to turn the hypotheses into facts.



To validate your hypotheses you have to get out of the building and talk to actual customers. Observe and interview your customers to better understand what jobs there are trying to complete, what pains the face and the gains they experience. Talk to your customers about how you will solve their jobs, ease their pains and create gains. Use this new insight to make a new version of your business model. Iterate towards a business model that has all the characteristics of a great business model. Run experiments to validate your hypotheses after you have talked with customers. Analyse the data and use your new knowledge to align your business model even better to your customer segments.
The test you run doesn't have to be complex and with large samples, talk to just enough customers to get the insights you need (forget about statistical validity, look for trends).

You can test your hypotheses with a sub-segment of your customers to minimize the risk and make failure recovery faster. Spotify has a model for their product development where they release new functionality continuously, but only to a small set of customers to minimize their risk and exposure if something fails. Do the same for your business model – you won't regret it.

4 Business model tools

As business model frameworks have grown more and more popular there have also become available a number of tools for the different models. Most business model framework does provide a low fidelity tool like a canvas for printing (e.g. Business model canvas or Lean canvas print-outs). In addition there is a number of software-based tools that's assist in the creating, sharing and testing of business models. The tools range from simple frameworks created in Google docs to highly sophisticated software suites.

Below is a list of software-based tools and a categorization of the basic functionality. The list is by no means meant to be a complete list of business model tools.

4.1 Business model canvas tools

LauncpadCentral – https://www.launchpadcentral.com/
LaunchpadCentral was a tool original used by Steve Blank when teaching classes in entrepreneurship. From the start it had academia as their early adopters and have now later on focused more on enterprise and other customer segments. The platform integrates the customer development framework with the business model canvas. LaunchpadCentral has a regular software license model. Steve Blank is one of the investors backing the company.

LeanLaunchLab – https://www.leanlaunchlab.com/
LeanLaunchLab has a very similar approach to LaunchpadCentral. The LeanLaunchLab integrates customer development and the business model canvas to create an innovation management software. LeanLaunchLab has a freemium model with price plans starting at 9 USD. The site has also integrated banking, finance and legal advice entrepreneurs might find helpful. They even have a section on finding co-founders.

Strategyzer – http://www.businessmodelgeneration.com
Strategyzer is the company of Alexander Osterwalder and Yves Pigneur. You can find both their books and other material on the site. There are also online versions of the business model canvas and value proposition canvas. It's based on a yearly license model pr. active projects you have. You will also find other resources like videos, pdf for downloads etc. on the site.

Business Model Designer – http://bmdesigner.com/
The Business Model Designer is a simple online tool to create and share business models based on the business model canvas. You can also explore canvases made by others and share your own canvas. All content created by users on the site are shared under Creative Commons.

Canvanizer – https://canvanizer.com
Originally a StartUpWeekend project from Nurenberg in Germany the Canvanizer is an online whiteboard with lots of different canvases. Canvanizer supports both the business model canvas and the lean canvas. Canvanizer is currently upgrading expecting to release their 2.0 version of the product in early 2015.

REMEMBER

Business models should not be confused with business modeling such as business process re-engineering (BPR) or business process management (BPM).

4.2 Lean Canvas tools

Lean Stack – http://leanstack.com/
Lean Stack is part of Spark59, Ash Maurya's company. The Lean Stack tool support the lean canvas and also has a kind of workflow taking you through the validation of the hypotheses towards a scalable, repeatable business mode. Lean Stack has a freemium model.

Tuzzit – https://www.tuzzit.com
Tuzzit is an online whiteboard collaboration tool with lots of different canvases. It supports both the business model canvas and lean canvas. Tuzzit offers a free version and you can even upload your own canvas. With a pro solution you will get more features and customization of your canvases.

RealtimeBoard – https://realtimeboard.com
RealtimeBoard is an endless online whiteboard where you can organize your workflow, brainstorm and manage your tasks in a highly visual way. Lean Canvas is only one of the many kinds of whiteboards supported by RealtimeBoard. RealtimeBoard have a freemimum business model with premium features starting at 8 USD.

5 Suggestions for further reading / References

5.1 Books

Blank, Steve: The Four Steps to Epiphany. K&S Ranch; 2nd edition, 2013.

Blank, Steve and Dorf, Bob: The Startup Owner's Manual: The Step-By-Step Guide for Building a Great Company. K & S Ranch, 2012.

Maurya, Ash: Running Lean: Iterate from Plan A to a Plan That Works. O'Reilly Media; 2 edition, 2012.

Moore, Geoffrey A.; Crossing the Chasm. HarperBusiness; 3 edition, 2014.

Osterwalder, Alexander: The business model ontology, A proposition in a design science approach. University of Lausanne, 2004.

Osterwalder, Alexander and Pigneur, Yves: Business Model Generation: A Handbook for Visionaries, Game Changers, and Challengers. John Wiley and Sons, 2010.

Osterwalder, Alexander, Pigneur, Yves and Bernarda, Gregory: Value Proposition Design: How to Create Products and Services Customers Want. Wiley, 2014.

Ries, Eric; The Lean Startup: How Today's Entrepreneurs Use Continuous Innovation to Create Radically Successful Businesses. Crown Business, 2011.

Roam, Dan; Blah Blah Blah: What To Do When Words Don't Work. Portfolio Hardcover 2011.

5.2 Blogs / groups

Steve Blank – http://steveblank.com
Steve Blank's blog on startups, customer development, lean startup and agile development.

Practice Trumps Theory – http://practicetrumpstheory.com
Ash Maurya's blog on business models, lean startup and actionable metrics.

The Startup Tool Kit – http://thestartuptoolkit.com
Rob Fitzpatrick's blog on lean startup and a lot of other stuff…

Alexander Osterwalder – http://businessmodelalchemist.com/
Alexander Osterwalder's personal blog on business model canvas, value proposition design and business model generation.

Business Model Innovation – http://blog.business-model-innovation.com/
Patrick Stähler's blog on business models, innovation and business agility.

Strategyzer – http://blog.strategyzer.com/
Strategyzer is a company founded by Alexander Osterwalder.

Dan Roam – http://www.danroam.com
Visual thinking for the business world

Business Model Innovation Hub – http://businessmodelhub.com/
…where visionaries, game changers, and challengers discuss business models

Meetup.com – http://www.meetup.com/
Lots of relevant groups in your city getting together to learn something, do something, share something…