

# Chapter 4

## Business Models

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### Acknowledgment

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### The Four Components of an Online Business Model

To arrive at an online business model, senior management must define the model's four components:

- (1) a value proposition or value cluster for targeted customers
- (2) an online offering, which could be product, service, information, or all three;
- (3) a unique ,defendable resource system; and
- (4) a revenue model.

### 1. Value Propositions and Value Clusters

The first step in the articulation of an online business model.

Construction of a **value propositions** requires management to specify three things:

- (1) Target segment, (2) focal customer benefits, and (3) the key resources the business has that can help it deliver the benefit package in a significantly better way than its competitors.

When customization is applied, the firm can serve multiple groups of customers with different value propositions – for example, Amazon can serve textbook market with one value proposition, and the trade book market with a different value proposition. This means that customization can turn a value proposition into a value cluster.

#### Choice of Segments

- ✚ A careful market opportunity analysis should reveal segments in which a particular form can be competitive. While a number of classical frameworks address the segment choice decision, most reduce the analysis to the attractiveness of the market. Market attractiveness is a function of many variables, but the key decision variables are frequently reduced to the following:

- **Market size and growth rates.** The overall dollar size of the market and percentage growth rates of the market should be significant.

- *Unmet or insufficiently met customer needs.* Customers are either not being served or not being served well by existing players.
- *Weak or nonexistent competitors.* Obviously, it is best to enter markets where the competition is not evident.

## **2. The Online Offering**

The next step after value proposition is to decide on the online product, service or information offering; but in this stage we are not designing how the web site will look like but we are providing a broad description of the actual product or service that will be provided online.

The senior management team must complete 3 sequential tasks:

- 1- Identify the scope of offering.
- 2- Identify the customer decision process.
- 3- Map the offering to the customer decision process.

### **Scope of Offering:**

The scope refers to the number of categories of products & services that a firm offers; it can be anything from a firm focusing on one product category (Termed a “**Category killer**”) to a firm focusing on large number of categories.

**There are 2 specific types of scope that can be focused on:**

#### ***A- Category specific dominance:***

Refers to companies that focus exclusively on one product category (e.g. flowers)

However it’s difficult to isolate firms that are focusing on only one category!

(E.g. the online flowers category firms focus on combination of flowers, gifts & complementary goods as candy).

#### ***B- Cross category dominance:***

Refers to the extension of product offering from a single category to additional product categories (e.g. AMAZON)

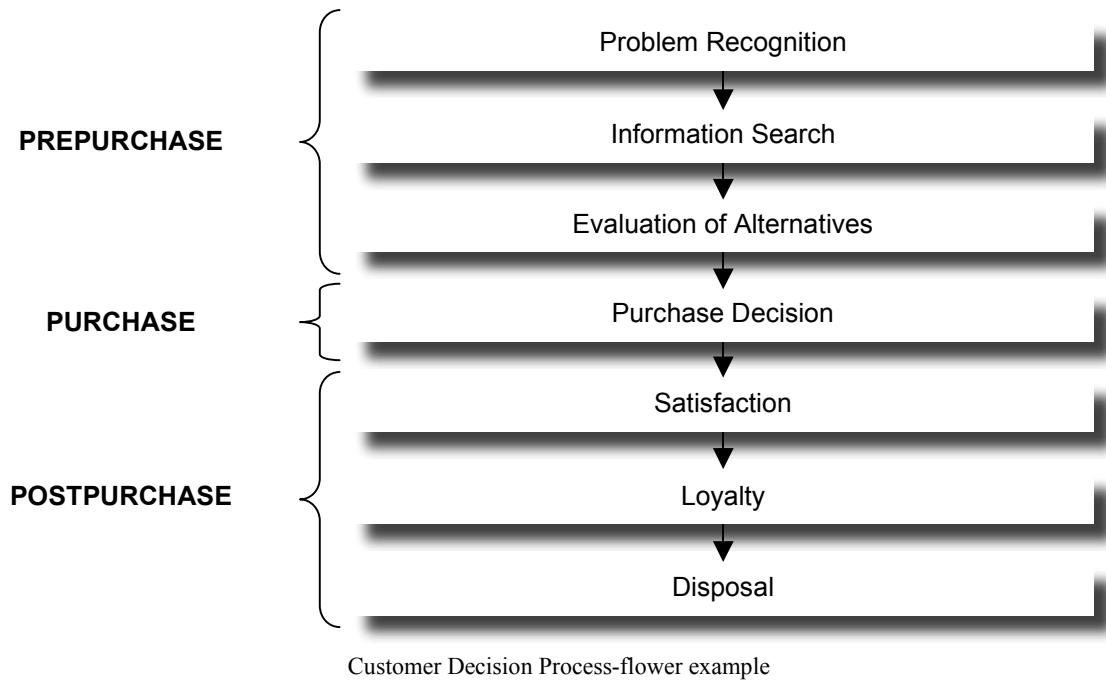
As AMAZON offers products that naturally group together from the logistics & distribution point of view.

The term “Meta Market” refer to sites that group naturally clustering categories of goods & services which are grouped according to how customers engage in activities. “Meta Markets” are then clusters of markets in the minds of customers. Also based upon the **goals** the products help customers achieve.

### **Identify the Customer Decision Process:**

The second step in the construction of online offering is articulating the customer decision process for the various product categories.

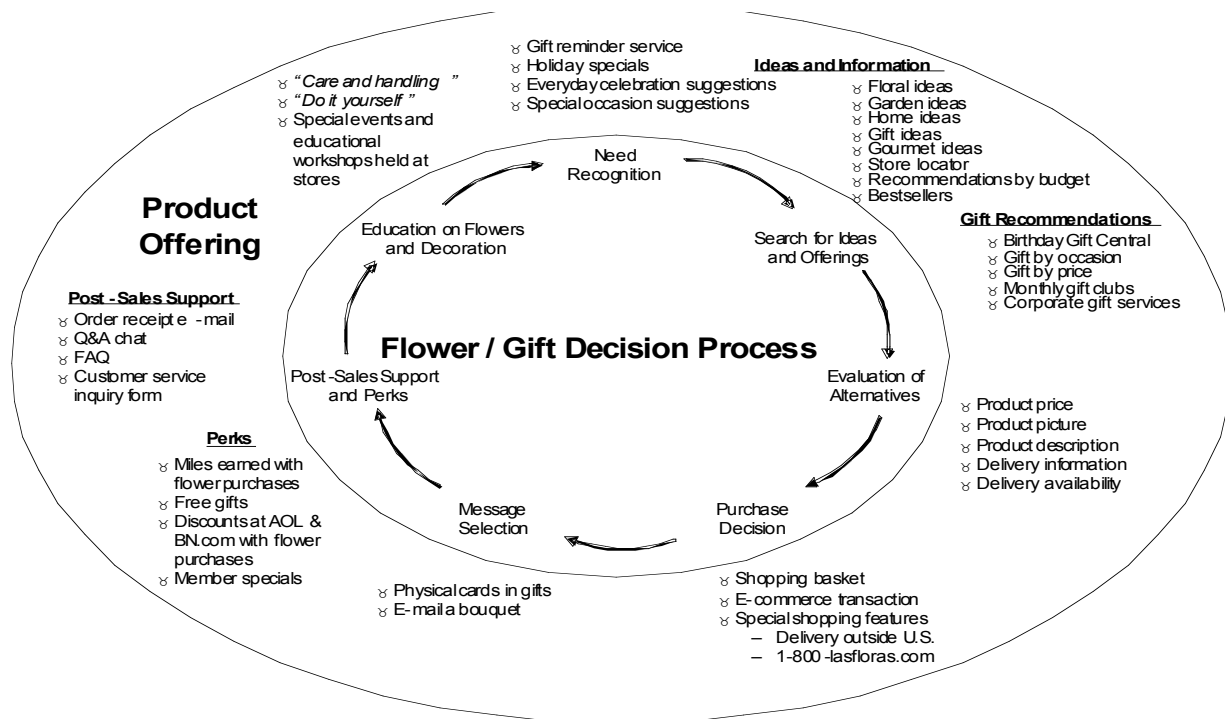
This process can be divided into 3 stages: prepurchase, purchase & post purchase.



## Map Products and Services onto the Customer Decision Process

The idea is that the website should walk the consumer through the entire purchase-decision cycle and encourage the consumer to continually revisit the cycle. This decision cycle should be repeated for each of the product categories on the site.

We refer to this process as the mapping of an egg diagram as shown



Considering the flower example, we can identify site activities that assist the consumer through each step of the decision process. To match need recognition, there might be a gift reminder service or

holiday specials for example. A site could provide ideas in various categories, a store locator, lists of favorite gifts, or list of best sellers to aid in the information search. During the evaluation of alternatives, a site could provide product price, description, availability, etc. To support the purchase decision, the site could accept credit cards over the phone or online, and show an assortment of cards and notes with appropriate messages to be delivered with the flowers.

For customer satisfaction, it could provide exceptional customer support, various free benefits or incentives.

### **3. The Resource System**

It shows how a company must select and then align its resources (either alone or with partners) to deliver the benefits of the value proposition or cluster.

#### **Specifying a Resource System:**

↳ Step One: Identify core Benefits in the Value Cluster :

##### **Example:**

1-800-Flowers.com serves the mid – to high – end market with a broad gift assortment, fresh flowers, and easy access because of its strong distribution network, product and media partnerships, and multiple contact points. Thus, its cluster of benefits includes fresh flowers, a broad assortment of gifts, and easy access.

The core benefits are identified in the construction of a value proposition or cluster.

↳ Step Two: Identify Resources That relate to Each Benefit:

To link the resources that are required to deliver a particular customer benefit. We are not concerned about whether the company has the resource; we are simply concerned about the link between the resource and the benefit

##### **Example:**

"Widespread, Easy access" is linked to four resources: popularity of website, wide reach to customers, multiple contact points, and brand name.

↳ Step Three: Identify to What Degree the Firm Can Deliver Each Benefit:

This gives a close internal look at the company (i.e. we ask ourselves: does this company contain all the necessary resources or must the company outsource or partner with others to gain missing resources?)

##### **Example:**

1-800-Flowers.com Both product and media partnerships are required in order to make the system operate effectively

↳ Step Four: Identify Partners Who Can Complete Resources:

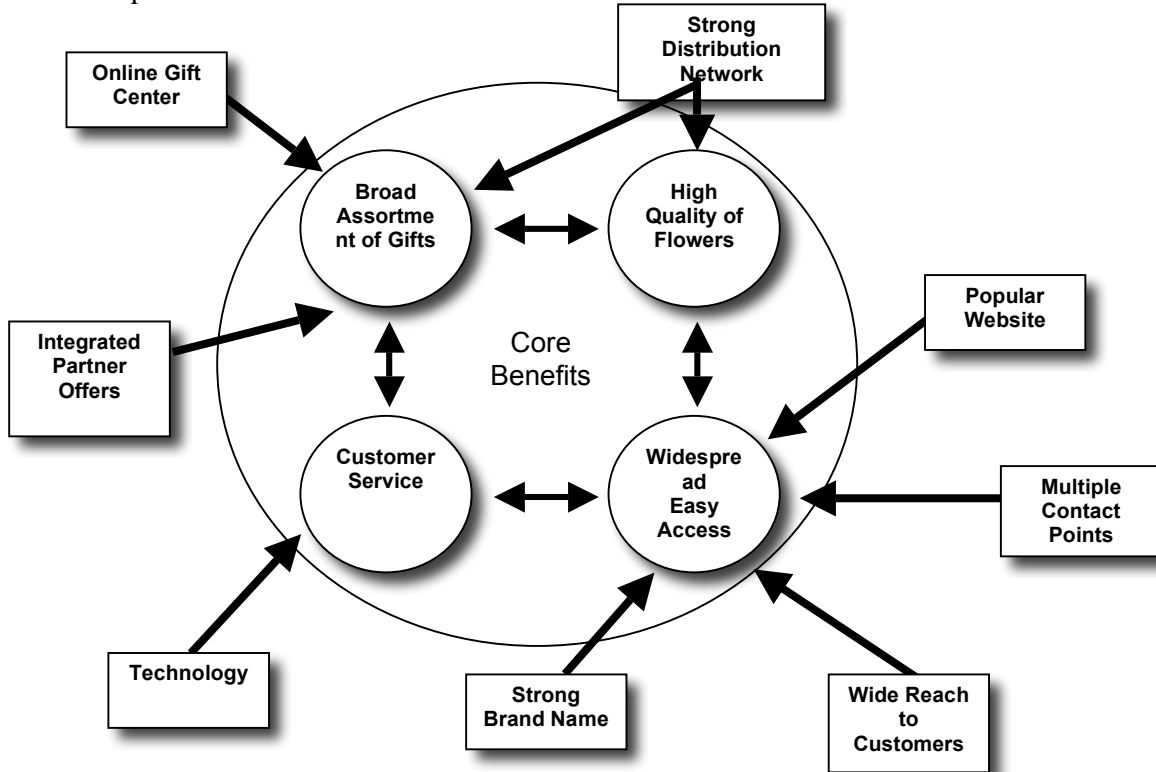
To identify key players who can complete the resources system

##### **Example:**

1-800-Flowers.com this would include product partnerships with other companies as "San Francisco Music Box" and media partnerships with major online sites such as AOL.

We would also need to adjust our resources-system model to integrate online and offline activities and assets in various combinations.

For example:



The benefit of "widespread, easy access" is supported by the resource of "wide reach to customers". This might need to be supported by online partnerships. The benefit of "multiple contact points" may need to be supported by three offline (telephone representatives, franchise-stores, catalog) and two online (affiliates, online store) assets.

**Criteria to Assess the Quality of a Resource System:**

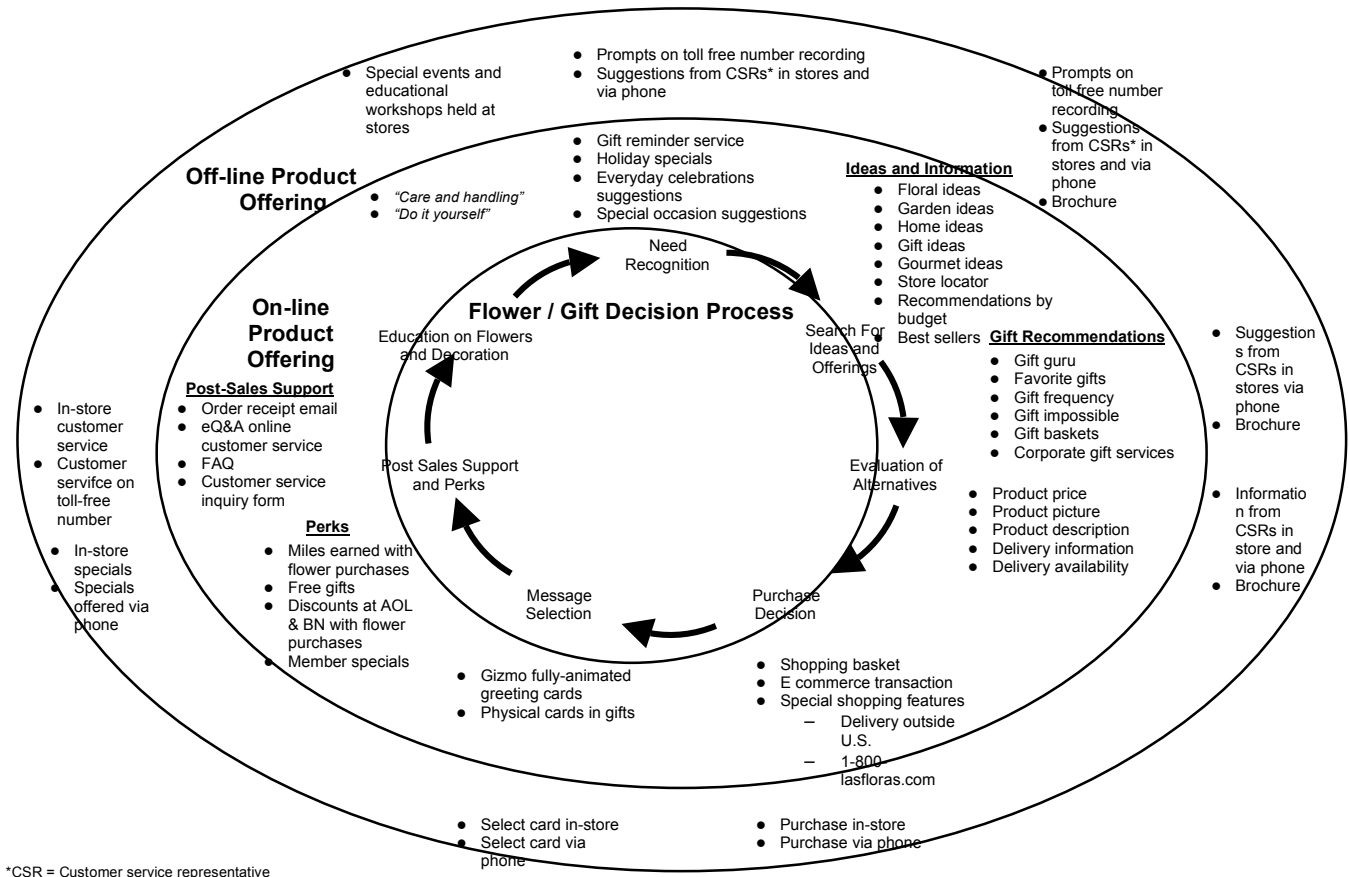
A number of criteria can be used to assess the quality of the resource system.

**1. Uniqueness of the system:**

Refers to the extent to which the organization has resources that differ from those of its competitors.

**Example:**

We could argue that the FTD.com model and 1-800-flower.com model differ at the resource level as only 1-800-flower.com partners with AOL. But the resource system of the two companies may be similar to other competitors in the market.



**2. Links Between Resources and Benefits:**

Does each resource support the delivery of a customer benefit? Is the support strong or weak?

**3. Links Among Resources in the system:**

How well do the resources complement and support one another? Are there tight linkages among the resources? Are they consistent with the overall value cluster? Are the specific resources mutually reinforcing? Are they complementary? Are they consistent with the various benefits?

**4. Links Between Virtual-World and Physical-World Business Systems:**

Does the online resource system support or conflict with the offline system.

**5. Sustainable Advantage:**

Is the resource system difficult to replicate? Possessing a unique but easily copied resource system will deliver only a fleeting advantage to a firm. Sustained high profits will come only from a sustainable competitive advantage.

The ease with which a resource system can be imitated may depend on a number of factors.

## 4. Revenue models:

- Online companies develop a new respect for deciding on a revenue model.
- While the purpose of the revenue model is relatively clear & the ways to make money are fairly straight forward, it is often difficult to align the revenue model with the company's value proposition and offering.
- Many online companies now face the challenging of figuring out what their customers are willing to pay for, and how much they are willing to pay.
- To this purpose, it is even more important to consider the value proposition, offering, and resource system when deciding how the company will make money.
- **The most frequently mentioned sources of revenue:**
  1. **Advertising:**

A particular site can earn advertising revenues through the selling of ads (banner or interstitial), site sponsorships, event underwriting, or other forms of communication.
  2. **Product, service, or information sales:**

Refers to income that is generated from the sale of goods on the site, this can include through retail sites pay-per-use information.
  3. **Transaction:**

Refers to accrues from charging a fee or taking a portion of the transaction sum for facilitating a customer-seller transaction.  
Ex: Charles, Schwab and E-bay.
  4. **subscription:**

Refers to a subscriber fees for magazine, news paper, or other information/service business.  
The online site for the wall street journal charges subscription fee.
  5. **License fee:**

Are fees generated from the licensing of content.  
Software companies often generate revenue from license fees.