Strategies for business model innovation: How firms reel in migrating value

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A B S T R A C T

This paper brings together firm-level research on business models and industry-level research on value migration to examine patterns of business model innovation. We draw on qualitative data from 14 cases and 68 interviews in the computer and telecommunications industries to demonstrate how business model innovation is sensitive to industry-wide forces of value migration. Based on our analysis we conclude that when value is rapidly migrating across industries and between firms, proactively substituting key elements of the primary business model provides a better fit with the new value landscape than launching secondary business models in parallel. We suggest four underlying mechanisms that link business model innovation, value migration and subsequent outcomes. Unpacking business model innovation allows us to discuss contingencies for the main business model strategies, specifically in terms of limitations to—and opportunities of—changing the primary business model and the practice of parallel business models.

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Introduction

Only months after the ‘dotcom’ bubble burst in 2001 when countless young, promising and innovative technology ventures went bankrupt and the euphoria of the ‘new’ economy disappeared, the computer and telecommunications industries appeared to be getting back to normal again. But were they? In an article published by the Business Week in 2001, Mr. Jorma Ollila, CEO of Nokia, the world’s largest cellphone manufacturer at that time, stressed the need for the emerging “mobile Internet” to remain “under the control of the mobile industry, and not the computer makers” (Baker, 2001). Less than ten years later, his successor Olli-Pekka Kallasvuo found his firm in a peculiar situation. While still the market leader in cell phones, Nokia’s previous largest competitors had all been replaced by new players. These new competitors were a different breed. What used to be Motorola, Ericsson, and Siemens were suddenly Samsung, LG, and RIM (Gartner, 2000, 2010) without any particular track record in the mobile industry. More worrying still, revenue streams started to divert away from Nokia’s core business. To sustain their mobile handset business, Nokia was forced to partner with software giant Microsoft and appointed Microsoft executive Stephen Elop as their new CEO. Ultimately, the joint venture between the two firms was dismantled, and the business was completely taken over by Microsoft in 2013, before being written off in 2015 (Forbes, 2015). In only six years, Nokia went from being the market leader in mobile handsets to crashing out of business.

What could have caused such a dramatic result? A critical explanation is that value in the mobile industry started to migrate (Jacobides and MacDuffie, 2013; Slywotzky, 1996), amongst others, to a fast mover from Northern California that had only recently entered the industry with their iPhone product. Apple entered the mobile industry as a complete outsider and
rocked the industry by fundamentally changing the rules of the game, shifting the focus of attention away from hardware and technology towards software and content. Whereas the old business model was about selling devices, voice minutes and text messages, value started to migrate to an ecosystem of applications and mobile services. The time was ripe for a new business model that could create and capture value.

We analyze these dramatic shifts in the computer and telecommunications industries from a business model perspective (Baden-Fuller and Haefliger, 2013; Björkdahl, 2009; Chesbrough and Rosenbloom, 2002; Demil and Lecocq, 2010; Zott and Amit, 2007, 2008, 2010; Zott et al., 2011). There is a growing consensus that firms need to change, adapt and innovate their business models in order to appropriate value from technological innovation (Baden-Fuller and Haefliger, 2013; Björkdahl, 2009; Hierneth et al., 2011) and to sustain success over time (Chesbrough, 2010; Massa and Tucci, 2013; Teece, 2010). However, scholars are still debating the merits of different business model innovation strategies. One powerful stream of business model research advocates the operation of multiple, parallel, and partly even conflicting business models as a mechanism for hedging risks and opportunities (Casadesus-Masanell and Tarzijan, 2012; Markides and Charitou, 2004; Markides, 2013). An alternative view suggests changing the primary business model to align with shifting demands (Bock and George, 2014; Doz and Kosonen, 2010; Johnson et al., 2008; McGrath, 2010; Sosna et al., 2010).

To shed new light on these opposing business model innovation strategies, we marry the firm-level research on business models with industry-level research on value migration. Value migration is here defined as the shift in value-creating forces that makes value move between firms and their business models (Slywotzky, 1996). Often this happens as value moves from old business models to new business models that better meet customers’ concerns and desires. Specifically, we ask: how can firms pursue business model innovation when value is migrating across industries and between firms? More broadly, answering this question allows us to start exploring the largely neglected relationship between industry dynamics and business model innovation (see e.g. Abernathy and Utterback, 1978; Utterback, 1994a; Dosi, 1984; Carlsson, 1997 for in-depth discussions on industry forces that enable and constrain firm-level innovation).

We investigate this question through a multiple case study of 14 large and prominent firms in the converging computer and telecommunications industries. We demonstrate that when the industry is characterized by rapid value migration, firms are most successful when they take a proactive stance by substituting key elements of their primary business model in tandem with the external business environment—a practice known as ‘pivoting’ (e.g., Blank, 2013). Our results are incorporated into a wider contingency framework that allows us to contribute to the debate on the advantages and disadvantages of changing the primary business model or launching secondary business models that run in parallel (e.g., Markides, 2013).

This article is organized as follows. Section Literature review: value migration and business model innovation reviews the literature and sets the theoretical foundation for our study. Section Research design presents the research design and introduces our empirical setting. Section Findings: patterns of business model innovation presents our findings and provides a first categorization of the patterns observed. Section Discussion: explaining business model innovation in dynamic environments discusses explanations for our observations and theorizes on a set of underlying mechanisms. Section Contributions to theory and practice concludes the paper by summarizing our contributions to theory and practice.

Literature review: value migration and business model innovation

In the field of strategy, it is well established that firm-level decision making is influenced by meso- and macro-level phenomena (Brown and Eisenhardt, 1998; also see the industry lifecycle literature, e.g., Abernathy and Utterback, 1978). Indeed, it has been acknowledged that industry-level factors such as technological developments impact business models (e.g., Afuah and Tucci, 2001). Yet, business model research is relatively silent with regard to how the relationship between industry dynamics and business models can be characterized, and how the resulting strategic choices available to firms unfold. In order to develop a perspective of business model innovation that is sensitive to industry-wide phenomena, we draw on the concept of value migration (Jacobides and MacDuffie, 2013; Slywotzky, 1996). If we consider, for example, the list of Fortune 500 firms, it is easily observable that many firms that were top performers 10, 20, or 50 years ago have been replaced by new firms from either the same or new industries. Value has clearly migrated between firms as well as industries. Value migration can be understood as the shifting of value-creating forces that over time determine the profit level of firms (Jacobides and MacDuffie, 2013; Slywotzky, 1996). Value can migrate between industries and often flows between firms within the same industry (especially in industries characterized by intense competition and innovation) but can also flow between different business units or products within a firm (Slywotzky, 1996). Value can migrate from outdated business models to new ones that have a better product-market fit in relation to customers’ most important priorities (Slywotzky, 1996). While some firms may achieve value inflow (firms absorb value from other firms) due to changes in their business models, others will experience value outflow (firms lose value to other firms) because of business models that have become less competitive, or even outdated.

The business model literature has successfully developed frameworks and practices to capture the intricate interrelationship between the creation and appropriation of value (Björkdahl, 2007, 2009, 2011; Chesbrough and Rosenbloom, 2002; Osterwalder and Pigneur, 2010; Teece, 2010; Zott et al., 2011; Massa et al., 2017). Most work in the realm of business models has focused on coherence and assumed a static relationship between business model elements (see e.g.,
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