

BUSINESS MODELS

NEW PRODUCT INNOVATION

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Why You Need
to Use a
Business
Model for
Innovation

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Firms working in new product development (NPD) recognize that the strategy drives decisions with long-term impacts for customers, revenues, and sustainability. While strategy is an overarching guide describing the values and vision of a firm, detailed execution of a strategy is accomplished via the firm's business model. Yet, many companies are challenged to articulate their business model and face inherent obstacles to revise and renovate an established, but aging, business model.

What is a Business Model?

First, we have to define a **business model** and explain how it is different than the strategy or mission of a firm. At the highest level, a firm's strategy describes why it is in business, who its competitors are, and what it envisions for the future. Strategies, while not set in stone, do not readily change because they provide a guiding light for the company over a long period of time, often aligned with the vision and mission of its leadership team.

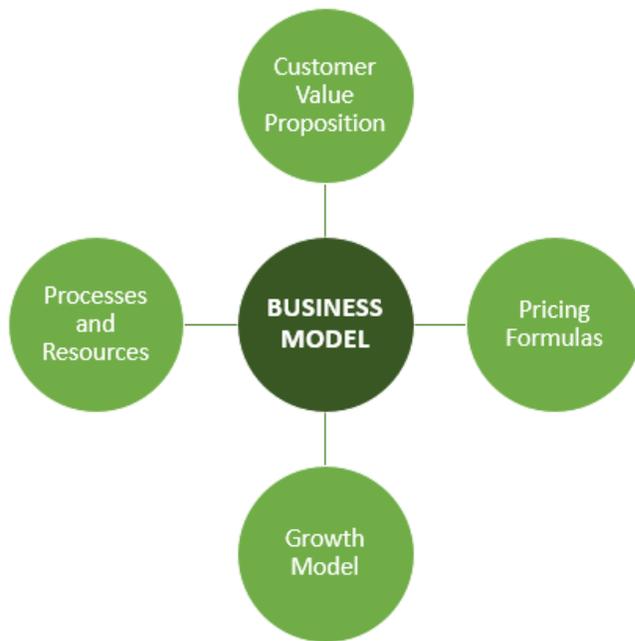
A firm's vision illustrates how, where, and what the company will do in the future and with whom. Vision statements are often very long-term in nature, looking 10 to 20 years into an unpredictable future. Yet, the vision statement can frame key strategic decisions that guide product development actions for the better or the worse.

In contrast, a firm's mission describes the products and service it will offer in the near term to accomplish the stated strategic goals. For instance, a mission statement may note expansion of product sales into a new geographic region in order to satisfy a strategic growth goal. In turn, that objective supports the vision of being a global provider.

Components of a Business Model

On the other hand, a business model describes how a firm operates *today*. Business models focus on several key components such as the customer value proposition, pricing and revenue models, growth models, and key resources and processes. Of course, all of these elements support strategic goals and the mission of the firm; however, business model components are fairly specific and may be revised frequently to take advantage of market trends and transformations.

The *customer value proposition* defines how a customer or user of the product or service benefits.



NPD practitioners often take a limited perspective of the customer value proposition. Increased functionality and product sophistication are the bailiwick of technical designers who may assume customers want more and better. Yet a careful analysis of the customer value proposition may reveal a desire for simplicity, ease-of-use, and reliability instead. Consumers often purchase products and services to accomplish specific tasks looking for the solution to a given problem, not seeking the new

product or service itself.

For instance, in the so-called “sharing economy,” customers are seeking comfortable, low-cost lodging that is readily available. The customer value proposition does not include marble-tiled lobbies, room service, or loyalty programs. Traditional hotels offer these features to a different set of customers with a different set of beliefs and values.

It is not surprising, then, that the customer value proposition is tightly linked to the pricing formula in a business model. Prices must be set to reflect a number of variables, including the value that a customer believes s/he is getting out of the transaction. Companies risk alienating customers when pricing too high and risk revenue loss when pricing too low. Consumers expect to gain a benefit *above* the price paid for a given product or service; although, this benefit is often intangible and difficult to monetize.

A business model also must include a path for future growth. After all, the business model is supporting strategic goals for the firm. Growth models may include access to new geographical markets or new market segments. A popular growth model tends to add features to a basic

product or service and offer a luxury or premium product or service. Companies can easily plan and develop new products and services with additional features over the life cycle of the innovation using this business model.

Finally, business models incorporate the culture of the firm – what business processes and resources are critical for success? Too often we see business processes that conflict with strategic goals. Stripping away burdensome procedures can open the firm to new ideas and growth opportunities.

For example, consider a large manufacturing company with strategic growth goals to increase the product portfolio via new product development. The company also introduced a three-page template with required approvals of a department manager, division manager, and R&D executive in order to begin experimentation on any new idea. The burdensome form sent an indirect message to designers and developers: *“We really don’t want your ideas!”*

Key resources, along with business practices and policies, also define the business model. Refineries are often vertically integrated in an oil company to give them access to feedstock and to convert byproducts to valuable chemicals sought by downstream manufacturers. In this case, oil field and plant, property, and equipment make up the firm’s key resources.

Why Use a Business Model?

Thus, a business model is comprised of a firm’s specific approach to the customer value proposition, pricing and revenue formulas, growth models, and key processes and resources. But, if a firm already has a strategy in place, why should they pursue business model innovation?

Markets change and technologies advance. Customers’ needs evolve over time. Business models are a vehicle to address market forces and trends while still adhering to the vision and strategy. The business model allows for adjustments in a particular product, service, or program to keep pace with market trends yet still provides focus for the business to accomplish strategic goals.

As an example, consider a company with an existing product with good sales. The firm has a strategic growth target to increase sales by 15% over the prior year. You can either sell more

product or sell the same number of units at a higher price to increase revenues. Going to the business model can shed light on which decision is more effective for the product in light of industry and market trends. You may be able to increase the number of units sold by selling more to existing customers (increase consumption) or by selling product to consumers who were previously non-users. Alternatively, you can sell more auxiliary and ancillary products to drive consumption within the overall product line.

Such decisions require market insights and an understanding of what customers value about the product – the customer value proposition. Moreover, increasing sales by increasing revenue through a price change requires understanding of elastic supply and demand curves, competitor responses, and changing technologies. All of these are first identified within the business model framework.

Business models also drive decisions by focusing on the right questions at the right time. A business model will address three key questions.

1. What mix of products and service should we offer to our target customers and markets?
2. What is the timing of decisions to invest in innovation?
3. Who is the best party to make our business decisions?

Of course, it is a basic tenet for all strategies to address which customers to serve and which to not serve. However, Question #1 digs deeper into the mission statement to clarify products, services, auxiliaries, and capabilities thereof. It also focuses the decisions on which customers, in which markets, and in which industries to participate. Decisions within the business model framework should be consistent with the firm's overall strategic thrust.

Question #2 is relevant to NPD practitioners. Investments are often made late in the game in order for a firm to catch up with competitors. This results primarily in copy-cat innovations. Using a business model framework can help decision-makers focus on future trends and emerging technologies instead. Insights from market research studies will drive NPD to not only stay ahead of competitors but to clearly address customer needs with a specific solution that delivers value to all parties.

Finally, a firm must come to terms with its own culture via decision-making authority within its business practices (Question #3). Employee engagement and empowerment mean that the front-line staff are able to take decisions based on their intimate knowledge of their customers. Senior management should encourage *design thinking* as a means to gain deeper insights to customer needs and values. In fact, successful companies encourage senior management to visit and work in retail positions weekly or monthly to maintain an understanding of consumer needs and employee challenges.

Trust is required to build close customer relationships and it is through such relationships that a firm will gain deeper market insights. Close customer relationships will help a company determine what customers need, what they value, what prices they will pay for products and services, and what resources are necessary to execute a given strategy. All of these components are the focus of a business model framework that addresses technology and market transitions for existing and new customers, products, and services.

Emerging Trends for Business Model Innovation

In recent years, technology advances have begun impacting how companies do business and how strategies are implemented. Of course, new business approaches via technology are manifested through a firm's business model. Yet, technology by itself does not transform a business model.

Because business models describe how the complex parts of a business interact to determine the degree of success of a firm, technology disruptions will indeed allow new entrants opportunities to displace incumbent firms. However, it is normally the *application* and *integration* of a technology that creates the market disruption. That is, technology *assists* in designing a new customer value proposition, pricing formula, growth model, and utilization of key processes and resources. A successful business model will take advantage of the interface of technology enablers and customer needs.

Kavadias and co-authors (Harvard Business Review, October 2016) have identified six elements tying technology to transformative business models. In their study, they found that three or more

elements were necessary to introduce a disruptive business model. Likewise, the more features present, the more impact was realized in the marketplace. These six components are:

- Personalized product or service,
- Closed loop process,
- Asset sharing,
- User-based pricing,
- Supply chain collaboration, and
- Adaptive organizations.

For example, Etsy (an online craft clearinghouse similar to eBay) allows personalization of products but is not considered to be a disruptive business model. One feature taking advantage of technology is not enough to create a transformative new business model according to Kavadias, et al. Uber, on the other hand, checks off four of the six features (personalization, asset sharing, user-based pricing, and collaboration). Certainly, traditional taxi companies appear to be responding to Uber as a disruptive threat to their more conventional business models.

Using Business Models to Growth Innovation

Employees, customers, and competitors all look to a company's business model to understand how it competes in its chosen marketplace and how it plans to succeed. Business models articulate the firm's strategy into specific outcomes that describe the customer's perspective of value. Business models focus more narrowly than the mission and vision, and also include pricing, revenue, and growth models as well as cultural factors that influence a firm's success (e.g. processes and resources).

While examining a firm's current capabilities in the product and service mix, a business model also describes the essence of a company's decision-making processes. How and when are decisions made? Who makes decisions regarding innovation? A more customer-centric view can enable a firm to recognize emerging trends in the marketplace, and because business models are enacted through the near term, opportunities can be grabbed before competitors.

Business Model Basics

In particular, technology serves as an integrating factor for business models to deliver customer value in new ways. By itself, technology does not offer new or disruptive business models, but by recognizing the advantages of personalization, asset-sharing, and collaboration, for instance, a firm can find new and interesting ways to serve customers. It is through these unique applications of technology that disruptive business model innovations are implemented.

To learn more about disruptive innovation, check our in-depth course at [Simple-PDH.com](https://www.simple-pdh.com) or learn more about business models in New Product Development Professional (NPDP) [certification workshops](#). Contact us at info@globalnpsolutions.com or 281-280-8717 for more information.

About the Author



An outstanding **author**, Teresa is President of [Global NP Solutions, LLC](#), a **strategic innovation provider**. She is an *accomplished visionary* and *results-oriented professional* with extensive industry experience from creative research to effective portfolio management through stream-lined new product development processes.

As a **lifelong learner**, Teresa has shared a unique breadth of innovation knowledge with dozens of individuals preparing for the *New Product Development Professional* (NPDP) certification exam, yielding an *impressive 100% pass rate*.

Dr. Jurgens-Kowal earned a B.S. degree in Chemical Engineering from the **University of Idaho** in Moscow, Idaho, a Ph.D. in Chemical Engineering from the **University of Washington** in Seattle, Washington, and an MBA from **West Texas A&M University**. She is a licensed Professional Engineer in the State of Louisiana since 1998 and a **Project Management Professional** (PMP®). Teresa is a **certified New Product Development Professional** (NPDP) by the Product Development Management Association (PDMA) and [Global NP Solutions](#), is a **Registered Education Provider (REP)** with PDMA. Teresa is also a certified **Professional Engineering Manager (PEM)** through the American Society of Engineering Management (ASEM). She is also the **Book Review Editor** for the *PDMA*.

Teresa holds chemical process and catalyst patents, and is published in the Journal of the American Chemical Society, Journal of Physical Chemistry, and *authored a popular series of blog posts* at ChEnected.com called "**Talking to Your Bo\$\$**". She is also the author of the [#1 NPDP exam preparation study guide](#) available at Amazon.