

Advisory Outlook



Four Business Models for the Digital Age

As digitisation continues, end customers will increasingly expect you to cater to their likes and needs.

Digitisation, which is of course happening all around us, is opening up a whole new spectrum of opportunities to create value. But how do you navigate this new horizontal world?

Peter Weill and Stephanie Woerner offer some useful insights on these challenges in their 2015 Sloan Management Review article, "Thriving in an Increasingly Digital Ecosystem." In exploring these insights, and some of their implications, leaders can gain a fuller understanding of the landscape they face.

Opportunities for companies in every industry are occurring on two critical dimensions: knowledge of the end customer and business design, i.e., breadth of product and service offerings. These dimensions combine to form four business models for creating value (see figure): Suppliers, Multichannel Businesses, Modular Producers, and Ecosystem Drivers.

Suppliers, in the lower left quadrant, have little direct knowledge of the preferences of their end customers, and may or may not have a direct relationship with them. These companies sell their products and services to distributors in the value chain. Due to the ease of digital search, they are vulnerable to pricing pressures and commoditization as customers look for less expensive alternatives. Washing-machine manufacturers are a good example of Suppliers, as are companies that create mutual funds sold by someone else.

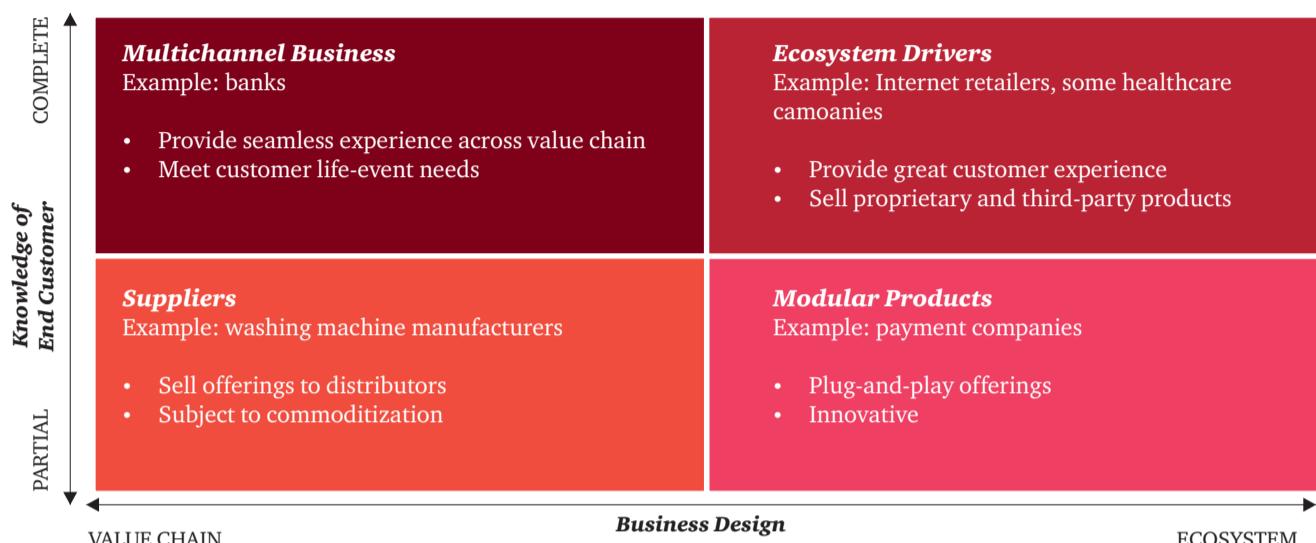
If you are a Supplier, you need to make sure your operations are as efficient as possible, but that's only the first step. As digitisation continues, end customers will increasingly expect you to cater to their likes and needs. So if you don't know much about your end customers and aren't intent on solving their problems, you'll need to find other ways to ward off commoditisation. That means making sure that your product is highly differentiated or that it goes through a distribution channel other than one controlled by an Ecosystem Driver, another of the business models, which has a broad supply base. Otherwise, you risk losing all the value your enterprise has created.

Haier, the world's largest manufacturer of white goods, has deployed various strategies to differentiate itself from competitors. It has developed a variety of niche products, including washing machines that accommodate the long gowns worn by women in Pakistan, and freezers that can keep food frozen for 30 hours in the event of a power outage in Nigeria. More recently, Haier used the Internet to open up its innovation process to people outside the company, enabling an unprecedented level of customisation.

Multichannel Businesses, in the upper left quadrant, have deep knowledge of their consumers because they enjoy a direct relationship with them. Companies in this category provide access to their products in various digital and physical channels to ensure the seamless experience their end customers have come to expect. Many banks and brokerage houses are Multichannel Businesses, as are some retailers and insurance companies.

If you are a Multichannel Business, there's no such thing as too much customer knowledge. Broadening

Exhibit: Strategies for Value Creation



Source: Adapted from Peter Weill and Stephaine L. Woerner. "Thriving in an Increasingly Digital Ecosystem," *Sloan Management Review*, June 16, 2015

your understanding your customers' life-event needs is essential for building out the integrated experience that will retain existing consumers and attract new ones.

IKEA, the world's largest furniture company, is an example of an Multichannel Business that continues to find ways to enhance the range of offerings within its value chain. Building upon its global presence — currently more than 300 stores in 41 countries — IKEA used its extensive knowledge of its customers (gleaned through visits to homes, for example) to develop "products for an everyday life" — from bedroom furniture to prepared food, all under IKEA's iconic brand. After decades of focus on the customer experience in its stores, IKEA recently launched online shopping, making the purchasing experience truly seamless and gaining a way to learn even more about its customers.

Modular Producers, in the lower right quadrant, offer a distinct capability that spans the ecosystem, but they have little direct knowledge of the end customer. Their plug-and-play offerings can work with any number of channels or partners, but they rely on others for distribution as well as for guidance on what the customer needs. A good example is payment companies that enable the consumer to pay for a wide range of goods and services, such as groceries and college tuition.

If you are a Modular Producer, you need to be the best at everything. As is the case with Suppliers, competition is fierce, so your offerings need to be innovative and well priced.

Square Inc. fits the profile of a Modular Producer. Founded in 2009, the B2B payments company has continuously launched innovative software and hardware products that are ecosystem-agnostic. Square's point-of-sale, payroll, employee management, and appointment apps can be used on Apple and Android devices alike, as can its chip and magstrip readers.

Ecosystem Drivers, in the upper right quadrant, have the best of both worlds: deep end-customer knowledge and a broad supply base. They leverage these dimensions to provide consumers with a seamless experience, selling not only their own proprietary products and services but also those from providers across the entire ecosystem. Thus, they create value for

themselves while extracting rent from others. Large internet retailers in the U.S. and China are good examples of Ecosystem Drivers, as are some healthcare providers.

If you are an Ecosystem Driver, you'll want to keep pushing the boundaries in both dimensions, increasing your knowledge of end customers and the breadth of offerings available to them.

As Weill and Woerner's research demonstrates, the prospects for creating value are greatest for companies that participate in ecosystems rather than in value chains, so Ecosystem Drivers have the greatest potential for value creation and Suppliers the smallest. All four paths are viable routes to enduring success, provided you are clear on what your generic strategy is and what that strategy requires. If, however, you are losing customers or growing more slowly than your market, you should consider moving to a different quadrant, either by expanding your knowledge of your end customers or by becoming more of an ecosystem.

Or even by doing both: GE is moving from being a Supplier of industrial products to an Ecosystem Driver in the Industrial Internet of Things, with the help of Predix, the cloud-based operating system it launched last year. Serving as a platform for services provided by third-party vendors as well as GE business units, Predix helps companies collect, analyze, and leverage operational data so they can optimize the performance of their entire system. As Predix's customer base grows, so will GE's status as an Ecosystem Driver.

As digital becomes the new normal, the paths to success are there for the taking. But be sure you know your destination before setting out.

This article by **John Sviokla** PwC's head of Global Thought Leadership was first published in *Strategy+Business*. For more visit <https://www.strategy-business.com>

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