

# Taking Competitive Advantage By Business Model Innovation

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## **ABSTRACT**

*In the world and Turkey there are many companies that both survive and increase their market shares and profits by changing business models. Business model innovation is one of the best and prevailing methods to tackle with the difficulties emerged in crisis and recession periods and the other endangering factors that should be reacted at once as well as to increase market share and to make profit. In this study, some significant points that companies have to consider for taking competitive advantage by business model innovation are indicated. Taking these findings into consideration will help managers to cope with the crises caused by environmental and/or organizational factors.*

**Key Words:** Business Model, Business Model Innovation, Crisis.

**JEL Classification:** M19, L25.

## **İş Modeli İnovasyonu ile Rekabetçi Bir Avantaj Yakalamak**

## **ÖZET**

*Dünyada ve Türkiye’de iş modelini değiştirmek suretiyle hayatta kalan ve pazar payı ile karını artıran pek çok şirket mevcuttur. İş modeli inovasyonu, krizden ve resesyon dönemlerinden ve diğer acil tepki gösterilmesi gereken durumlardan kurtulmanın da, pazar payını artırmanın da kar elde etmenin de en iyi ve geçerli yoludur. Bu çalışmada işletmelerin iş modeli inovasyonu ile rekabetçi bir avantaj yakalamaları için dikkate alınması gereken hususlar tespit edilmiştir. Bu tespitlerin yöneticiler tarafından dikkate alınması, çevresel ve/veya örgütsel faktörlerden kaynaklanan krizlere karşı işletmelerin başarı ile çıkmasına yardımcı olacaktır.*

**Anahtar Kelimeler:** İş Modeli, İş Modeli İnovasyonu, Kriz.

**JEL Sınıflaması:** M19, L25.

## **I. INTRODUCTION**

The survival of the companies depends upon the level of adaptation to the environment and shaping the behaviors with respect to expectations of environment at the one hand, and the harmony of sub-systems at the other hand. The environment of the companies continuously changes due to many social, political, legal, economic and technological factors. Those changes introduce new opportunities and challenges. The success of the companies highly relies on their capability for noticing and evaluating these opportunities and challenges. Perceiving and assessing of changes happened in the environment as well as capacity for taking necessary measures are mostly pertinent to the structure of the company and the characteristics of the management (Genc, 2004:335). Frequently companies face with some serious crises since they cannot realize the challenges and opportunities caused by change, or take necessary steps even if they realize. If necessary measures are not taken, some factors, which are not arisen from the

causes such as new markets, a new technology or economic recession, but eventually bring about loss of prestige and credibility, can result in confronting crises. A crisis can simply be defined as the circumstances endangering the existence and life of the companies (Simsek, 2002:327). The crisis is generally caused by the free will decisions of the organizational management whereas various environmental factors out of management decisions may also induce crises.

The crisis process begins with the receptions of crisis signals caused by interior and/or exterior environmental factors. Whatever the root is every crisis appraises by some signals that it is about to come up. The organization should have an information system that allows the reception of these signals just in time and in a robust manner. In addition, the managers who are entitled to make decision should be sensitive towards these signals. As a matter of fact, the crises are stemmed from either the lack of capability for monitoring signals or the ignorance of signals itself. This attitude results in negative outcomes such as inappropriate investments, unexpected costs, reduced profit margins, late market penetration, loss of market share, etc. All of the negative outcomes mentioned above are the endangering factors that should be reacted at once.

Companies choose their actions in the context of specific strategies. Getting over a crisis basically depends upon the strategic decisions made by management. Crisis management determines this kind of decisions before a crisis happens. By this way, the emergence possibility of crisis lowers; in addition, panic is prevented even if the crisis happens (Ornek, 2008:38). Hence, companies should seek for making difference in the strategies they pursue. Likewise, managers should monitor the outcomes, and change strategies if needed. What differentiates the winners and losers is neither the newest technology nor the timing for market penetration. Companies can create values only if they compromise innovation and benefit as well as cost and price (Kim and Mauborgne, 2005:13), which eventually makes them in the winner's side. Innovation and selection of differentiated strategies indeed necessitate the reassessment of factors that an industry has been competing for a long time and the restructuring of market boundaries. In other words, instead of complying with the environmental changes managers can change business model so that they can manage the change and create innovation and make difference. As Ken Chenault, the CEO of American Express, points out that hard times entail to be more innovative for the companies (Ozgenç, 2008:34). Chakravorty (2010:103) also states that under tough circumstances the innovative new business models are of crucial importance. With no doubt, this requires abandoning the traditional methods and implementing various new approaches untested before.

In the world and Turkey there are scores of companies that perished, lost market share or made loss as a result of unchanging business models. In contrast to this, there are many companies that survived, increased market share and raised profits by changing business models. It is stated that serious problems and intimidating obstacles can be considered as a blessing opportunity for creativity

and innovation, and that these troubles can always be triggering particularly in crisis periods (Chakravorti, 2010:103). Jeffrey Fox, mentions that companies surpassing their rivals in innovation, during the Great Depression and 12-recession periods afterwards in the United States, possessed always much stronger market shares after these economic crisis and gained more profits (Fox, 2010:170).

The study performed by Gulati and others verifies how important Fox's remarks are. Gulati et al. (2010:64) decided to mount a yearlong project to analyze strategy selection and corporate performance during the past three global recessions: the 1980 crisis (which lasted from 1980 to 1982), the 1990 slowdown (1990 to 1991), and the 2000 bust (2000 to 2002). They studied 4.700 public companies, breaking down the data into three periods: The three years before a recession, the three years after, and the recession years themselves. Their findings are stark and startling. Seventeen percent of the companies in their study didn't survive a recession: They went bankrupt, were acquired, or became private. The survivors were painfully slow to recover from the battering. About %80 of them had not yet regained their prerecession growth rates for sales and profits three years after a recession; in fact, 40% of them hadn't even returned to their absolute prerecession sales and profits levels by the end of that time period. Only a small number of companies – approximately 9% of their sample – flourished after a slowdown, doing better on key financial parameters than they had before it and outperforming rivals in their industry by at least 10% in terms of sales and profits growth.

In the next section, after underlining the importance of business model and business model innovation, the necessary points that companies should take into consideration to take competitive advantage in the crises stemmed from environmental and organizational factors will be defined. Then, some companies, which increased market shares and profits by changing business models on time, will be illustrated and the reasons of competitive advantages of business model innovation will be discussed.

## **II. BUSINESS MODEL INNOVATION**

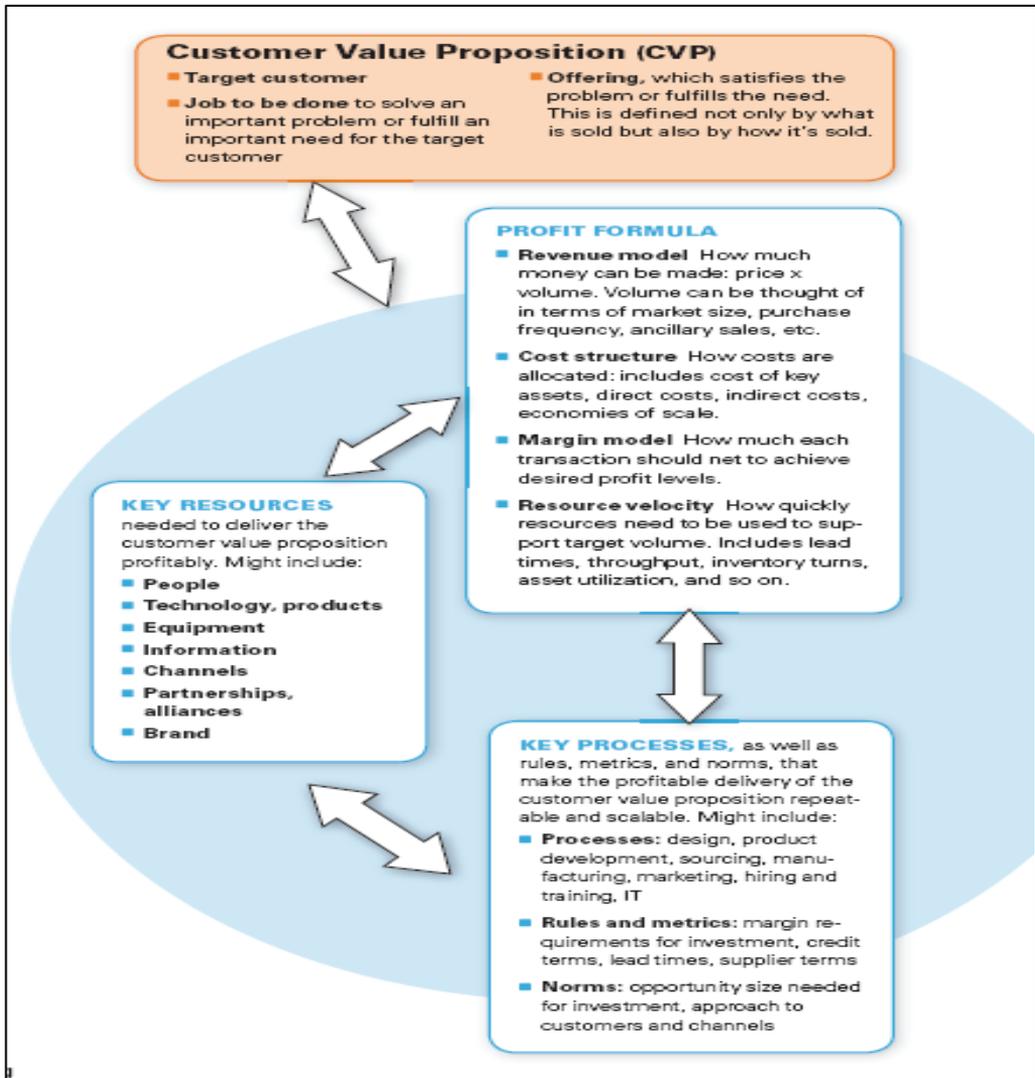
In the history of companies it is observed that success is cultivated either after a crisis or when a company manager who is not satisfied with the current status of the company decides to change company strategy or when market competition intensifies and technology changes or when a different business model comes out against the competitors, as a result of the company's success, business model is replicated by competitors. A good business model is imperative for all the institutions. Any prevailing enterprise, whether it is aware of, is built on a solid business model. A business model answers Peter Drucker's age-old questions: "Who is the customer? And what does the customer value? It also answers the fundamental questions every manager must ask: How do we make money in this business? What is the underlying economic logic that explains how we can deliver value to customers at an appropriate cost?" (Magretta, 2002:87).

The success of a business is determined by answering these questions correctly, which can be carried out through a business model.

A business model consists of i) a customer value proposition performing an important task for customer much better than competitors' presentations, ii) a profit formula demonstrating how the enterprise will make money while providing value for customers, iii) necessary key resources, such as human, technology, products, facilities, equipment, channels and brands, to deliver this proposition to the customer, and iv) key processes, such as training, development, production, budgeting, planning, sales and services, allowing the enterprise to create the value (Johnson et al., 2008:52-53). Customer value proposition, profit formula, the key resources and key processes constitute building blocks of a touchstone. While customer value proposition and profit formula define the value for the company, the key processes and key resources reveal on how to transfer that value to both the customer and the company (Johnson et al., 2008:53). In short, the business model convenes the parts of business in harmony in a way to convey value to the customer and the company. Figure 1 illustrates the elements of a successful business model.

Accordingly, it seems impossible to form a business model without determining a customer value proposition. One can claim that a successful company is one that has found a way to create value for customers. When a company comprehends all dimensions of a problem that needs to be resolved, it can contemplate the value to be proposed to customer. If alternative products and services cannot resolve the problem of customer, it means that the company has the best opportunities to form a customer value proposition. The profit formula is the blueprint that defines how the company creates value for itself while providing value to the customer.

It consists of the following: The revenue model demonstrating how much money can be made, the cost structure displaying how the cost of resources that business model require are allocated, the margin model denoting the expected contribution of each transaction to achieve desired profit levels under a certain volume and cost framework, the resource velocity depicting how successfully resources are used to reach the target volume and make envisaged profits.



**Figure1.** Elements of a Successful Business Model (Johnson *et al.*, 2008:54)

Having articulated the value proposition for both the customer and the business, companies must then consider the key resources and processes needed to deliver that value. Oftentimes, it's not the individual resources and processes that make the difference but their relationship to one another. Key resources can be defined as the resources needed to deliver the customer value proposition profitably. Key processes are the rules, metrics, and norms that make the profitable delivery of the customer value proposition repeatable and scalable.

Companies will almost always need to integrate their key resources and processes in a unique way to get a job done perfectly for a set of customers. When they do, they almost always create enduring competitive advantage. To make the

new business successful, the business model should be applied in a different way from the competitors. Boston Consulting research on this subject would be more descriptive (Ates, 2007:33): According to this research, product presentation of 86 of 100 companies is in the scope of “me too” (I exist, a copy of competitor) and product presentation and the business model of remaining 14 companies are on value innovation. In addition, while turnover of “me too” companies increased by 63% and profits increased only by 39%, it is observed that proportions of companies on value innovation occurred in the opposite direction, 38% turnover increase and 61% profit increase.

Indeed, descriptions and/or metaphors such as W. Chan Kim and Renée Mauborgne’s “Blue Ocean Strategy”, Robert I. Sutton’s “Weird ideas that work”, Richard Foster’s “Creative Destruction”, Clayton M. Christensen’s “Disruptive Technologies/Innovation”, Jim Collins’ “Power of Catalytic Mechanisms”, P&G’s “Disruptive Market Innovations” and many others are nothing but nomenclature of this issue, and the common point of definitions and descriptions mentioned above is business model innovation.

In a study conducted with 160 CEO participants on how CEOs affected by worldwide economic fluctuations with the economic credit ratings of the United States downgraded and the negative news on economies from the US and the European Union, 50,6% of CEOs stated that their businesses adversely affected by the global economic waves. The percentage of the CEOs revealing that they were not affected was identified as 27,7% (Buyuk, 2011:82).

However, by relying on business model innovation, crisis periods can also be transformed into a competitive advantage. Indeed, 18 of the 30 firms currently on the Dow Jones Industrial Index were founded during economic downturns. In addition, The Kauffman Index of Entrepreneurial Activity showed that the rate of new-business creation was higher during the deepest part of the 2009 recession than it had been in the 14 previous years including the 1999-2000 technology boom (Chakravorti, 2010:103-104).

In Thomas Meyer’s book “Innovate! How Great Companies Get Started in Terrible Times”, 21-recession periods in U.S. history were examined. It reveals that many major companies were established during these periods, as shown in Table 1 (Meyer, 2010:4-24).

**Table 1.** Most of the Major Companies were established during Recession Periods

Recession Dates	Founded Companies
1797-1800	American Bank, Chase Manhattan, Alex, Brown&Sons
1807-1814	John Wiley&Sons, The Hartford, Rogers Orchards
1819-1824	William Underwood Company, Consalidated Edison
1837-1843	Procter&Gamble, Tiffany&Co, Berkshire Hathaway
1857-1858	Macy's, Bernis Company, Fifth Third Bank
1873-1879	Bank of America, Chevron Co., General Electric
1893-1896	IBM, Maytag, Lincoln Electric, Macmillan Publishers
1907-1908	General Motors, The Hoover Company, UPS
1918-1922	Zenith Electronics, Great Western Bank, Universal Corp.
1926-1927	McKinsey&Company, 7-Eleven, CBS, Marriott International
1929-1939	Morgan Stanley, Leo Burnett, Ritz Carlton, HP, KFC
1945	Baskin-Robbins, Mattel, Fisher Electronics
1948-1949	Toys "R" Us, Manpower, 20th Century Fox TV
1953-1954	Colgate- Pamolive, Playboy Ent., Walt Disney
1957-1958	Enterprise Rent-a-Car, Hush Puppies, Valentino's
1960-1961	Domino's Pizza, Tyco International, Vitamin World
1969-1970	GAP, Korn Ferry, Wendy's, FedEx Office, Saatchi&Saatchi
1973-1975	Bain&Company, Turner Sports, Burke Corporation
1980-1982	Sun Microsystems, Symantec, BMC Software
1990	Warner Bros, Studio Store, United Electronic Industries
2001	Accelrys, BMI Garning, First Equity Card Corporation

### III. ORGANIZATIONS LOSING COMPETITION

Every steady organization is based on a sound business model. In other words, a good business model is needed for all organizations. A business model portrays how the company works and how the sub-parts of the business conform to each other. A successful business model may expire when technologies or markets change; in this case, the model has to be changed. Despite developments in technology and varying markets with the increasing customer expectations, it is observed that companies grasp business models as an irrevocable fact and that they conform to traditional processes unless conditions of competition are vigorous (Cirik, 2008:120). The literature research done in this regard reveals that even the international companies may enter into markets lately, lose market share and be unsuccessful against local enterprises. Furthermore, it has also been seen that big companies abstain from delivering products and services to the poor. However, according to Fisk, the volume of the poor market is approximately 5 trillion dollars (Fisk, 2010:19).

Richard Foster, as a result of his study covering 1.000 company from 15 different industries, indicates that even the world's most respected and well-known corporations sustain competitiveness for at most 15 years and that companies maintain their market domination through restructuring themselves and that the key to success is the constant change and creativity that can keep up with the change (Yavuz, 2009:96). Although it is specified that 70% of change initiatives resulted in the failure (Beer and Nohria, 2000:133) enterprises should re-evaluate their business models and re-configure themselves according to

market conditions. Enterprises that do not conduct such an assessment and change themselves accordingly have limited chance to persevere in the market. Once an enterprise starts operating, the underlying assumptions of its model – about both motivations and economics – are subjected to continuous testing in the marketplace (Magretta, 2002:89). In this context, business models should have flexible and variable features in the early years (Johnson et al., 2008:56). This is because the success is achieved by the business model revisions consistent with market conditions. For example, when Disney opened EuroDisney in 1992 in Paris it had been deemed that its successful business model in the United States would have been valid for Europe. But, Disney's all the assumptions had gone wrong. By 1994, Disney had lost over \$1 billion. The company made breakthrough after it had modified some business model factors in accordance with the Europeans (Magretta, 2002:89; Rothman, 2007:213).

Apart from environmental reasons, organizational factors and managerial qualifications may also play an important role in some cases in which prestige and reliability of the company are damaged. On such an occasion a company may have to deal with negative outcomes such as lagging behind competition, loss of market share, credibility erosion, etc. What companies can do in such cases is examined below.

#### **A. Companies Having Late Market Entry**

Even the companies well positioned in the market rarely change their business models. In this regard, author of the book "Game Changing Strategies", Costas Markides, reveals that 95% of different business models in the world have come up from the companies newly entered the market and, mature companies do not want to change the rule of the game, but have to take precautions against the successful business models in the market (Bayiksel, 2008:204). Indeed, a recent American Management Association study determined that no more than 10% of innovation investment at global companies is focused on developing new business models (Johnson et al., 2008:52). In this case, the result is to enter the emerging market late and, thus, lose its competitive advantage and watch the competitors snatching the market. Some of the examples on this subject in the literature are as follows (Bower and Christensen, 1995:43):

- Goodyear and Firestone entered radial tire market quite late.
- Xerox let Canon create the small-copier market.
- Bucyrus-Erie allowed Caterpillar and Deere to take over mechanical excavator market.
- Sears gave way to Wal-Mart.
- IBM dominated the mainframe market but missed by years the emergence of minicomputers, which were technologically much simpler than mainframes.
- Digital Equipment dominated the minicomputer market with innovations like its VAX architecture but missed the personal-computer market almost completely.

- Apple Computer led the world of personal computing and established the standard for user-friendly computing but lagged five years behind the leaders in bringing its portable computer to market.
- Even though Motorola introduced the world's first cellular phone, Nokia seized the leadership (Ries and Ries, 2010:68).
- Polaroid couldn't carry its brand beyond instant-photo and Kodak failed to display success in digital films despite its success in photograph films (Ries and Ries, 2010:127).

In Wall Street Journal, Don Listwin, CEO of Openwave Systems, stated that two-thirds of companies dominated in their sectors chose wrong companies as their rivals and lost their positions because they got into panic about them and were defeated (Ates, 2006:191). The fact that a business exists together with its competitors should always be remembered. In 2006, after the Daimler Company had handed over Chrysler since Chrysler's sales fell by 7%, the management of Toyota, which was the major rival of Chrysler that was in crisis and close to a collapse, remarked that the USA government had to rescue Chrysler otherwise the consequences could affect them (Izgoren, 2009:138). It can clearly be conceived from the examples given above that for the success of the companies it is as much important to determine competitors right as to determine right objectives for themselves. While wrong competitors lead to unforeseen targets it may also result in unmonitored opponent to move forward (Ates, 2006:191). In this context, it is of great importance for businesses to follow other sectors aside from their own sectors. What companies that entered the emerging market late and consequently lost competitive advantage have to do to respond the challenges of change is discussed below.

### **1. Rethinking the Focusing on New Technologies**

The most important reasons why companies cannot adapt themselves to the change are i) to invest too much to improve existing technologies, ii) focus on the development of existing technologies more than enough by gradually and deliberately meeting the needs of customers, and iii) not to seek markets to welcome for technologies developed in their laboratories (Anthony et al., 2006:106). For these reasons, these same companies are rarely in the forefront of commercializing new technologies that don't initially meet the needs of mainstream customers and appeal only to small or emerging markets (Bower and Christensen, 1995:44). For example, Polaroid assumed that a 3-minute tape with \$7 price could compete effectively with a half an hour videotape with \$20 price. After all, Polavision lost \$200 million for their films. Polaroid assumed that high cost of video recording and playback devices is prohibitive on most consumers. Meanwhile, companies following up these technologies continuously pulled-down costs (McGrath and Macmillan, 1995:44).

These kinds of companies developing technology in their sectors face with difficulties to be out of a certain thought patterns (Yilmaz, www.yenilesim.org). Thus, customers face a large number of convenient products and services turned into a commodity and the urge for innovation to meet

customers' tacit expectations and to find better ways to solve their problems is destroyed (Fisk, 2008:94). As a result, until market meets financial conditions desired by the company and until the existing customers demand the new technology, companies follow "wait and see" approach and when markets reshaped, it is too late for them. Indeed, each time a disruptive technology emerged, between one-half and two-thirds of the established manufacturers failed to introduce models employing the new architecture in stark contrast to their timely launches of critical sustaining technologies (Bower and Christensen, 1995:46). Executives can prevent this situation by being vigilant towards potential disruptive technologies that do not meet the needs of existing customers.

## **2. Changing Business Model on Time**

One of the reasons of losing competition is the becoming late in changing business model on time. In order to dominate the market, enterprises should make a timely transition to new business model and also create an infrastructure to support new business model. Apple's iPod/iTunes revolution is a good example in this regard (Johnson et al., 2008:51-52; Lindgardt et al., 2009). With an infrastructure supporting a new business model, in just three years, the iPod/iTunes combination became a nearly \$10 billion product, accounting for almost 50% of Apple's revenue. Apple has purchased a good technology and offered it by a business model that combines hardware, software and services. Apple's real innovation is to facilitate digital music downloads. Apple has signed an agreement to make music legally downloadable from internet with five largest music companies, namely Sony, Warner, Universal, EMI and BMG (Young and Simon, 2009: 324) and the iTunes Music Store launched a catalog for 200.000 songs with sale prices of 99 cents per song or \$10 per album for the iPod owners. After a while, the iTunes Music Store dominated the 70 percent of legal music download market from Internet. In a year, the online store sold 85 million songs. This model described the value in a new format and led consumers to do something easily in a new way from top to bottom. The lesson that can be drawn from this example is that managers can prevent becoming late by paying attention to potentially disruptive technologies that do not meet customers' expectations as well as by creating an innovative culture in their own companies.

### **B. Companies Losing Competition against Locals**

Despite the assumption that the probability of surviving against multinational enterprises of local enterprises in countries opening their economies to global competition, reducing tariffs and freeing foreign investments is near to zero, a 3-year study conducted in the fastest growing 10 countries (Bhattacharya and Michael, 2008:86) identifies that local enterprises not only survive against multinational enterprises, but also dominate the market with their successful strategies and practices. Indeed, Innovation and Entrepreneurship Group Chairman of Massachusetts Institute of Technology, Eric von Hippel, claims that small and local enterprises in the world are more innovative than global companies (Cirik, 2008:124). Consider a few local companies that have fended

off foreign competition during the past five years or more (Bhattacharya and Michael, 2008:86):

- In Brazil, Grupo Positivo has a larger share of the PC market than either Dell or Hewlett-Packard, and Totvs is the enterprise resource planning (ERP) software leader in the small-and midsize-company market, ahead of the world's largest business software provider, SAP.
- In China, daily use of the search engine Baidu exceeds that of Google China by fourfold; QQ, from instant-message leader Tencent, is ahead of MSN Messenger; and online travel service Ctrip has held off Travelsky, Expedia's eLong.com, and Travelocity's Zuji.com.
- In India, Bharti Airtel has taken on Hutchison Telecom, which sold its Indian operations to Vodafone in 2007, and emerged as the leader in the cellular telephone market.
- In Mexico, Grupo Elektra, which has created one of the country's biggest retail networks, has taken the battle to Wal-Mart.
- In Russia, Wimm-Bill-Dann Foods is the biggest producer of dairy products, ahead of Danone and Coca-Cola.
- Kentucky Fried Chicken had left the Guatemala market for sometime because of the success of Pollo Campero (Ates, 2008:60).

As all examples clearly show that strategies of multinational enterprises do not work much in developing countries. Of course, there are successful cases such as Pizza Hut and Taco Bell as well. However, what is making valuable to investigate local businesses in terms of business model is the cases of local enterprises against the giant enterprises, such as Dell, HP, Google, Vodafone, Wal-Mart, Danone and Coca-Cola, where the world follows their every movement and application. In this context, it is apparent that there are a number of issues to be learnt by global companies from local and small enterprises. What big companies have to do to be successful in the competition with local industries change is discussed below.

### **1. Questioning Traditional Patterns**

Even the best companies can run into serious trouble if they don't recognize the assumptions buried in their plans (McGrath and Macmillan, 1995:45). Adherence of companies to traditional patterns makes them think that a standard business model and strategy will be valid for every situation. A large number of companies just try to implement strategies succeeded in the past once again in a better way. However, enterprises with an in-depth understanding of customers and know-how of how people's preferences vary with respect to urban/rural areas, income level, age group and gender are able to provide customized, at a limited extent, and cheaper products and services to consumers. For example, Goodbaby, the leader in Chinese market for baby-related products such as strollers, sells as many as 1.600 items in 16 categories. Customization becomes the basis on which companies like Goodbaby differentiate themselves from and get a leg up on multinational rivals (Bhattacharya and Michael, 2008:87). One of the other outcomes of adherence to traditional patterns is that it

makes enterprises to recognize structural and infrastructure problems that would prevent them to conduct their business in accustomed way as an insurmountable barrier. Business model innovation seeks an answer for the question “How can we do?”; not for the question “Why can it not be done?”. Successful enterprises develop strategies to overcome these obstacles. For instance, the global leaders in video games, such as Microsoft, Nintendo and Sony, haven’t made much headway in China because of software piracy. Chinese companies such as Shanda, which entered the industry in 2001, have developed a thriving game business by developing massively multiplayer online role-playing games (MMORPGs) instead. These products are impossible to pirate since they are live experiences created by technologies that link many players over the Internet. China’s MMORPG industry, which generated revenues of about \$600 million in 2005, has been growing at 40% a year since 2003, according to iResearch (Bhattacharya and Michael, 2008:90).

## **2. Finding Innovative Solutions to Structural and Infrastructure Problems**

Adherence of companies to traditional patterns and their misbelief that a standard strategy is valid for all circumstances make them to be indifferent to structural and infrastructure problems of the sector at which they operate. They generally assume that they have a strategy that was tested before, implemented successfully, and proved its superiority against competitors. If companies will not be aware of hidden assumptions such as “previously what was successful will be successful again” in their planning they may encounter serious problems. If they had used the accurate control tools and the right planning, the initial failure of EuroDisney could have been prevented and the costs could have been under control. The intention for right planning and accurate control tools is “the right perspective”. It should be admitted that a new initiative includes inherent uncertainties – such as serving a customer segment that has not been addressed previously in the market, using the potential of technology to optimize the current work or to make better products/services cheaper or to optimize them –. In the past, there were too many assumptions in connection with an untested application (McGrath and Macmillan, 1995:44). Since many companies insisted on attempts to build on the platform-based implicit assumptions (use of common parts, methods, or technologies together for different products) they plunged into the situation of Disney (McGrath and Macmillan, 1995:46). Therefore, it is advised to be vigilant to implement platform-based methods on new initiatives.

While structural and infrastructure challenges are defeated with low-cost labor, innovative ways to overcome qualified staff shortages should be sought. For instance, Focus Media, which has become China’s largest outdoor advertising firm. It has placed LCD displays that it engineered in-house in more than 130.000 locations in 90 cities to create a national advertising platform. Focus Media uses a decidedly low-tech solution to refresh and service all those LCD screens: A veritable army of employees who move from building to building on bicycles and replace, when necessary, the DVDs and flashcards that play the advertisements.

Focus Media could link the LCD screens electronically – as any blue-blooded transnational company would – but it doesn't. Using people keeps the company's operating costs low while enabling it to offer clients a great deal of flexibility. Were Focus Media to use an automated system, the Chinese government could deem it a network-based broadcaster and regulate it as a media company, which might curtail its growth (Bhattacharya and Michael, 2008:92). Here, this identifies how important it is to know the rules and regulations of a country. As another example India's Apollo Hospitals, another case in point, has developed a good reputation by recruiting some of the best doctors and nurses. The quality of its services is a key differentiator, allowing the chain to charge patients 10 times what they would pay in a public hospital (Bhattacharya and Michael, 2008:92).

### **C. Companies Not Serving Bottom of the Pyramid**

C.K. Prahalad (2008) in his book "The Fortune at the Bottom of the Pyramid" states that companies can profit by providing products and services to poor people who are more than 4 billion in the world and making a living for less than \$2 per day. He identifies the poor as "a hidden market" and entitles poor segment as the "bottom of the pyramid". A traditional product, services and management style has not been able to create a value for this market and a new innovative approach for business model is necessary. Some of enterprises prevailing with a different business model for the bottom of the pyramid and challenging management style of developed markets are as follows:

- PRODEM FFP, a Bolivian financial services enterprise, introduced smart ATMs which are color-coded, touch screen and able to speak three local languages. ATMs recognizing fingerprints provide 24 hours high quality financial service even for illiterate consumers. This system has also been used in developed countries (Prahalad, 2008:21).
- ITC, an Indian holding, had decided to connect PCs of Indian farmers in their villages. ITC e-Choupal (village meeting place) offered farmers to monitor not only local sale prices, but also sales prices of soybean futures stock exchange in Chicago Mercantile. Thus, income of farmers who can reach prices of goods anywhere in the world increased by 5% to 10% (Prahalad, 2008:21).
- Considering that the poor people had brand consciousness like the rich people, P&G created consumption capacity by offering single-use packages of luxury shampoo of Pantene in India (Prahalad, 2008:18).
- HLL, subsidiary of Unilever, realized that traditional methods would not make them reach remote villages; it launched a new program letting village women distribute its products in villages where it can't provide full service using its existing dealer and supplier system. Similarly, Avon converted more than 800.000 Avon Women to distributors in order to reach to the remotest corner of Amazon and became one of the largest cosmetic enterprises in Brazil (Prahalad, 2008:14).
- Cemex, one of the world's largest cement factories in Mexico, help consumers for cash buildup savings and investment on a "do it yourself"

project focused on the market in the bottom of the pyramid and provided access to good quality homes. By instigating groups of 3 women pressuring each other for cash build-up and keeping project alive in a “group discipline”, Cemex alleviated build-up and access to credits for adding bathroom or kitchen to their homes (Prahalad, 2008:19).

- Aravind Eye Care System in India performs, in the same manner that is done in the United States, a cataract surgery between \$50 and \$300 that can cost \$2,500 to \$3,000 in the United States. Despite 60% of patients is not charged for the surgery and the fees for the surgery are that low, Aravind still makes profits. A few hospitals following Aravind are specializing in heart health more and more (Prahalad, 2008:41).

What companies have to be aware of the reasons of why they do not serve to the bottom of the pyramid and what they can do in this respect are discussed below.

### **1. Questioning Implicit Assumptions**

The companies not serving to the bottom of the pyramid first of all have to question their existing assumptions. Companies assume that people with such low incomes have little to spend on goods and services and that what they do spend goes to basic needs like food and shelter. They also assume that various barriers to commerce – corruption, illiteracy, inadequate infrastructure, currency fluctuations, bureaucratic red tape – make it possible to do business profitably in these regions (Prahalad and Hammond, 2002:5). In other words, large companies do not see the poor as the target consumer group. They tend to suppose that technology can only be used in developed countries whereas the poor cannot spend on technological innovations and, therefore, do not concern with the bottom of the pyramid. However, doing business based on customer requirements will increase both the purchasing power of customers and company revenues. Doing business based on customers requires a radical reversal in business method (Fisk, 2008:77). The competitive necessity of maintaining a low cost structure in these areas can push companies to discover creative ways to configure their products, finances, and supply chains to enhance productivity (Prahalad and Hammond, 2002:8). As a matter of fact, a new development happened in these companies can create great opportunities for innovation that could be used in developed countries as well.

In addition, it assists companies to develop internal management style and financial situations. New initiatives require the company, by its very nature, to imagine unknowns. It would be wise to give a new direction to new initiatives since assumptions about the unknown often come out wrong (McGrath and Macmillan, 1995:44). In this context, in order to turn assumptions into knowledge, significant resource commitments should be postponed until the proof of the previous stage presents signs for taking risk to step up for the next stage. This is the formula for “invest a little, learn a lot” (Anthony et al., 2006:111). This can be summarized as putting something on the market, monitoring the reactions

and making corrections. So, expecting assumptions to turn into knowledge encourages administrators to address the uncertainties at the lowest cost possible.

## **2. Running Business Based on Customer Requirements**

Living and working conditions of consumers require the rethinking of functionality. Washing out clothes under running water outside is different from washing with a washing machine that is automatically adjustable depending on the intensity of the dirt and colour of the country. For example, solutions developed for the poor are not valid for sources used in developed countries. The question to be asked in regions with water shortages: Can we catch the western world at living standards without water or with insufficient water? Can we wash clothes without water? Can we keep ourselves clean without taking shower? These all require new solutions and new perspectives. Doing business based on customer requirements is a radical reverse method in doing business method (Fisk, 2008:77). It means to learn how to create value for customers by means of centralizing them.

The success of Grameen Bank as a commercial operating on microfinance developing in Bangladesh is a good example attracting a global interest to process. Initially, the amount of average loan is less than \$20. Today, including the United States, there are 17.000 micro enterprises in the world as variations of Grameen Bank. A global conference on microfinance revolution topics is held each year now (Prahalad, 2008:59). As a result of process innovation, making products and services purchasable by the poor is an important step.

### **D. Situations Inducing the Loss of Prestige and Credibility**

Companies go through crises not only during economic recessions. A big crisis that yields loss of the company's reputation and credibility may emerge from a negativity that occurs on products or services, mistrust of employees on managing team of company or corporate managers who do not act within the scope of social responsibility in accordance with ethical values (corruption, insensitivity to the environment and so on) or others not directly related to a failure of management or economic reasons. Such crises are usually caused by bad decisions and wrong assessments on leadership and strategy selection, in other words, are emanated by not being prepared. Crises that are not well-managed and decisions that are not well evaluated can lead to shut down of a company (Tichy and Bennis, 2011:38). So, it is utmost important to make accurate decisions. Therefore, it is essential to reevaluate the proposed customer value, profit formula, key resources and processes; in other words, the business model must be questioned. As is clear from the following examples, at least one element of the business model is in violation in such cases.

- In 1989, a large oil tanker of Exxon sank in Alaska and that the oil spill would cause a long-term permanent damage to the environment grabbed the headlines of all newspapers. At that time, the CEO of Exxon never took responsibility of the problem and never appeared in public at all until two weeks after the accident. When showed up the CEO acted extremely

insensitive to the environmental damage and stated that Exxon was not responsible for the clean up of the crash site, never apologized and accused media to stretch the truth on a tiny accident in the eyes of the world. But the company lost public relations since it insensitively abused the environment and lost its dignity even in the eyes of its people. In 2006, it was sentenced to 2,5 billion dollars for the environmental damage. This figure increased to 4,5 billion dollars with interest rates (Tichy and Bennis, 2011:218-219).

- In 1992, the supermarket chain Food Lion suddenly found itself thrust into the public spotlight when it was accused of selling spoiled meat. The company's stock plummeted, bottoming out at slightly greater than half its precrisis value. But Food Lion acted quickly, offering public tours of stores, putting large windows in meat-preparation areas, improving lighting, putting workers in new uniforms, expanding employee training, and offering large discounts to draw customers back into stores. The company eventually earned an "excellent" rating from the Food and Drug Administration, and in locations where it had previously been well established, sales soon returned to normal (Augustine, 1995:156).
- Merck's CEO did not accept to face the problem and tended to delay the problem until the drug Vioxx pills were proved to increase the risk of heart attack in 1993 and multi-billion dollar law suits were filed against the company. Yet, 86 million people in 80 countries were using Vioxx tablets (Tichy and Bennis, 2011:33). Johnson&Johnson suffered a similar problem to that of Merck. When Tylenol capsules in Chicago caused a series of deaths due to mixing of cyanide into the capsules, its proactive actions to protect the health of users of Johnson&Johnson's product, such as showing that there was no danger all over the country before without waiting the emergence of a more comprehensive evidence to take action, stopping the production of Tylenol capsules and announcing refunds on drug returns to them, etc., made all employers and consumers confident that they promptly took necessary measures against the crisis (Tichy and Bennis, 2011:38; Ates, 2006:105; Augustine, 1995:154; Paine, 1994:109).
- When it was suggested that Intel Pentium micro-processors were problematic on complex mathematics calculations at the end of 1994, the company asked customers to prove that chips were faulty. Intel suggested that the error would probably not affect most users. However, customers' confidence was shaken on the product. Despite protests, the company did not change its position for a month. After a while, IBM which is one of the leading purchasers of the Pentium, micro-processor announced that it had stopped shipment of the computers with the chip. Intel had decided to a return policy on this without any question. Interestingly, the amount of the product returns was virtually in non-existent levels. This is because people want to know whether they could get a new chip, rather than insisting on a new chip. Shortly after, the company announced that it

suffered a loss of revenue of \$475 million (Augustine, 1995:152-153; Smith et al., 1996:102).

- In the late 1990s, Lockheed Martin Corp., a rival of Boeing, accused Boeing of obtaining its thousands of pages of company files using illegal methods and use some of the documents in favor of Boeing to win a state contract for a rocket design Project (Tichy and Bennis, 2011:57). Boeing's board of directors forced CEO Phil Condit to resign because he violated ethical standards in dealings with government condoning and damaging the company reputation. New CEO McNerney convert the company's internal culture and leadership movement by turning crisis into an opportunity, rather than fighting against the claims, making a song about or blaming former leader.
- When Beech-Nut Nutrition found out that its suppliers sold apple juice concentrate which includes sugary water and some chemicals to prepare "100% pure" apple juice, the company could have destroyed its products in stock and asked for a recall of the products from the supermarket shelves. However, a 25% price advantage offered by the supplier of fake juice concentrate yielded the cost control targets of the company. Therefore, counterfeit products were launched. However, in 1987, the Food and Drug Administration, as a result of an investigation, found the company guilty of selling misrepresented juice. This incident cost the company \$25 million, including fines, legal expenses and lost sales (Paine, 1994:108).

What companies have to be aware of the facts about losing prestige and credibility and what they can do in this respect are discussed below.

### **1. Making Clear the Guiding Values and Principles**

The examples above reveal that managers put not only their personal reliability, but also organizational reliability at risk. Johnson&Johnson's decision to recall its Tylenol capsules is the result of a decision taken by thousands of people working at all levels of the organization. If there had not been guiding principles and a set of shared values that permeates the whole organization in-depth, it would have been doubtful for Johnson&Johnson to show a robust response so fast, consistent, and morally right (Paine, 1994:109). For this reason, managers have to establish systems that facilitate ethical behavior for their companies. In this context, the guiding values and principles should be transferred to the employees clearly and administrators should also act in accordance with company values. One of the good examples of managers behaving in accordance with company values is Ford's CEO Jack Nasser. Upon the increase in Ford Explorer SUVs accidents in 2001, although it was uncertain whether the accidents are caused by faults of Ford, or by Firestone tires attached to these vehicles, Ford's CEO took over full responsibility for this event for the solution of the problem and demonstrated that they cared about their customers (Tichy and Bennis, 2011:220).

## **2. Being Ready for a Crisis before Exposed to the Crisis**

Businesses may encounter with very different crises even when there is no direct management error. Therefore, businesses must primarily be prepared for crises. Drucker indicates that the most important task of the leader of an organization is to predict a crisis (Maciariello, 2005:112). In a study conducted with general managers of Fortune 500 companies (Augustine, 1995:151), 98% of survey respondents stated that crises were inevitable in business, but it was observed that 50% of them didn't have any plan to deal with crises. Despite this, 97% of them stated that they had confidence in themselves for the best response if there is a crisis situation. Even though they made such statements, dealing with a crisis requires preparation for crisis. In this context, a list of anything that may cause a crisis should be prepared, a brainstorming study should be conducted on the possible consequences and responses and finally action plans should be prepared. A crisis team should be organized from appropriate people having the knowledge about how to deal with a crisis. By revealing a crisis, managers should acknowledge and confront it with the fact that they are concerned about it. Managers remaining silent in the time of a crisis, not taking any personal responsibility, and not making any apology would not provide a spontaneous solution to the problem. Such an approach will cause the company to lose billions of dollars of compensation pay, in addition to prestige losses.

## **IV. ORGANIZATIONS WINNING COMPETITION**

It is a fact that enterprises prolong their life by re-evaluating and changing their business models under certain circumstances such as a new market emergence, new technology diffusion, economic stagnation and crisis. Why the business model should be changed is revealed clearly by the study of a famous management expert, Arie De Gues: The average span of life of companies has decreased from 45 years to 18 years in Germany, 13 years to 9 years in France and 10 years to 4 years in the UK. According to World Bank data, 80% of the enterprises established in Turkey go under before their fifth anniversary and 96% before their tenth (Ates, 2007:26). Additionally, the average holding period for a share of common stock has declined from three years in 1980s to nine months today (Zook, 2007:75). This is because new technologies are decreasing the costs nowadays and capital, innovation and management capability are moving more freely and more quickly around the world. Technological and market basis of every business disappears over the time. As an example, Kodak is the best photographic film trademark. It was ranked 16th best trademark in the world in 1999 and 82th in 2007. This is because Kodak was unable to launch a second brand to the market while the world's photography was turning into digital (Ries and Ries, 2010:46). Therefore, when it is time the business model needs to be changed.

A 2005 survey by the Economist Intelligence Unit reported that over 50% of executives believe business model innovation will become even more important for success than product or service innovation. A 2008 IBM survey of corporate CEOs echoed these results. Nearly all of the CEOs polled reported the

need to adapt their business models; more than two-thirds said that extensive changes were required (Johnson et al., 2008:52). While the annual number of patents for “business model” is only 1.000 for 1997 this figure reaches 8.000 for 2000 and 11.800 for 2007 (Ates, 2008:61).

In a case study of the most innovative companies published yearly by the Boston Consulting Group and Business Week, companies are classified as companies engaged in business model innovation, companies engaged in product innovation and companies engaged in process innovation. It has been found that enterprises engaged in product innovation and process innovation provided to their shareholders premiums more than average of the same industry, and enterprises engaged in business model innovation provided to their shareholders 4-fold greater premium than former innovation types’. In addition, it has been observed that business model innovation is more permanent and, even after 10 years, enterprises with a business model innovation maintain better performance than their competitors and companies with product and process innovation (Lindgardt et al., 2009). Indeed, 11 of 27 companies, which were established in the last quarter and succeeded in entering into Fortune-500 in the last decade, has achieved their success by business model innovation (Johnson et al., 2008:52). A.Meyer, one of the leading names in innovation, states that difficult periods are unique opportunities for innovation (Meyer, 2010:3). In this context, some examples of enterprises prolonging their existence by changing their business models, providing a competitive advantage, increasing profits and market share are given below (Cirik, 2008:118):

- Lego was selling only small children legos through traditional retail channel, but has become electronic distributor and software programming publisher of Midstorms Robot as well.
- Starbucks was only a worldwide American chain selling coffee and coffee by-products and has become music CDs and movie distributor in its stores and web site as well.
- Stata Corp. was only a statistical software developer and maintaining direct sales to consumers, and today is distributing customized software for installation over the Internet as well.
- Boyner in Turkey, was mainly in textile business with its famous brands such as Mayer and Altinyildiz, and has developed Advantage credit card model and sold it to HSBC. It is also in the service sector with Back-Up.
- Pasabahce in Turkey was a company manufacturing and selling only glass and glass products and has opened concept stores. It has grown into a chain selling home decorating products as well.
- TAV in Turkey was established as a consortium for the construction and operation of Istanbul Ataturk Airport, gained experience and, it has created airport construction and operating model within its periphery.
- Altinkiliclar in Turkey was only in coffee production and mass sales of coffee. It now offers coffee chocolates directly to consumers through its cafe chains renown as “Coffee World” (Cirik, 2008:118).

- Pegasus in Turkey started scheduled flights by changing its business model in mid 1990s while it had flights only for tour operators before. In the last 10 years, it has grown 42% in the sector while other big actors in the sector declared deficits and more than 20 entered the market and relinquished (Demirel, 2011:76)

Companies mentioned above did not choose competition as criteria within the industry, instead they used the strategy of, so called, “value of renovation” described in W. Chan Kim and ReneéMauborgne’s (2005) book of “Blue Ocean Strategy”. Rather than focusing on defeating the rivals in competition these companies rendered competition meaningless by activities in other business areas to create value for the company and the customers.

It is obvious that companies winning competition do not the faults that companies losing the competition do. Why business model innovation provides competitive advantage is discussed below.

#### **A. A Business Model Forces Managers to Think Rigorously about their Businesses**

A business model actually forces managers to think rigorously about their businesses (Magretta, 2002:90). In fact, business models built on incorrect assumptions about customer behaviors are doomed to failure. Changes in the market and technology entails companies to divert from traditional processes and to make a difference by creating a new business model based on customer needs. Making a difference actually means catching the success. For example, Dell has become the world’s largest personal computer manufacturer not because of manufacturing better products than its competitors, but because of marketing its products with a different system. In the same manner, Red Bull has become a global brand not because of being a better drink than others (cola drinks, fruit juices, etc.), but because of being a distinctive one: Red Bull was the first energy drink. Amazon was grown to be a leading bookstore by selling books over the Internet instead of selling them through retail stores (Ries and Ries, 2010:51). In Turkey Mavi Jeans, due to its “perfect fit” approach, was chosen among the world’s top 16 brand jeans in 2006 by the Design&Style magazine. “Perfect Fit” jeans are emerged from ideas of creating jeans that would fully fit to the body as well as culture and budget. Mavi Jeans sustain distinguishing itself, with the collection sensitive to the environment and human health, by manufacturing blue jeans from 100% organic cotton produced in recent years (Altun, 2008:180).

#### **B. A Business Model Enables Doing Current Jobs Better**

A new business model, which is defined and implemented to retain market share from competitors, may turn on designing a new product for an unmet need or it may turn on a process innovation, a better way of making or selling or distributing an already proven product or service (Magretta, 2002:88). For example, when FedEx first started the parcel delivery it did not compete with lower prices or with better marketing activities. Instead, it focused on a faster and a more reliable long distance delivery, which could not be achieved by any cargo company before (Johnson et al., 2008:57). In Vodafone Group and in Turkey,

Vodafone Turkey launched a “voice signature” project, for the first time, where the call center recognizes a calling customer by analyzing customer’s biometric voice. Due to this, speech recognition provides much safer and faster processing by eliminating steps for customer’s identity validation process, such as, place of birth, date of birth, tariff information, etc. (Gozutok, 2009:266). While the success of Fedex is emanating from solving an unaddressed problem before, the reason for success of “Signature Voice” project is due to accomplishing the existing task in much better way. When an innovation enters the market, it upsets the player’s expectations, and choices and introduces uncertainty in decision making (Chakravorti, 2004:2).

### **C. A Business Model Presents a Better Solution than Current Alternatives**

A successful business model represents a better way than the existing, and creates a new and escalating expectation (Magretta, 2002:88) and, as a result of this, it sketches all the sectors from a scratch and distributes values in billions of dollars (Johnson et al., 2008:52). Nano brand cars produced by Tata Community Enterprises constitute a good example in this regard. Ratan Tata from Tata Community Enterprises observed a large number of families driving motorcycles in a dangerous path around cars in India and, because of this, deemed to propose a safer alternative for poor families with motorcycle: Offering a reliable and cheap car they could buy for \$2.500 (Johnson et al., 2008:55). Nano with this price as the world’s cheapest car is a novelty allowing hundreds of millions of people who are currently unable to buy cars in the developing countries to buy it (Fisk, 2008:162). In order to make the expected profit from a product sold in this range of price, production and distribution processes must be reestablished (Tan, 2008:61): Instead of manufacturing cars in a classical factory and distributing them to dealers, Tata developed a new model where the cars are manufactured in pieces in factories and where these pieces are shipped to dealers, and, based on the sales, installation and after sale services are performed.

## **V. CONCLUSION**

Business model is the combination of key resources and processes creating value for customers and enterprises in harmony. Every successful enterprise has a successful business model. However, there is not any everlasting business model. With developing technology to meet increasing customer demands, enterprises are urged to change their business models. Business model innovation is the combination of key resources and processes different than competitors’ to create value for the enterprise and its customers against the commodification of goods and services. It is apparent that enterprises engaged in business model innovation are more successful than enterprises engaged in product and process innovation.

Entering into a new market, emergence of a new disruptive technology, economic stagnation and crisis periods characterize hard conditions for enterprises to re-evaluate their business models. Studies show that innovative businesses are the ones that prosper in these difficult conditions. Therefore, crisis

periods can be transformed into a competitive advantage with the business model innovation. However, it is observed that the existing business models of enterprises are mostly unchangeable because unless intensified competition conditions do not compel, enterprises do not change the traditional processes. As a result of this, companies enter the market late and large enterprises are forced to quit against local businesses. They also miss great opportunities upon not considering poor as a target population or implementing well-known business strategies in poor markets. Since business model innovation ensures the current work to be done in a better way and resolves a problem that has never addressed before with a new product or process innovation, or addresses to a customer segment that has not previously addressed before, it is the best and valid way to profit, in addition to elude from the difficult economic conditions like crisis and recession periods and to grow the market share.

One of the important indicators to determine whether a business model is successful is the profit obtained. Profits are important not only for their own sake but also because they tell you whether your model is working (Magretta, 2002:90, Johnson et al., 2008:59). Profit is obtained as a result of producing value for the customer and getting a customer reward in return for this. Profit of enterprise from new business is a powerful symbol indicating the success of new business (Govindarajan and Trimble, 2005:65).

While new technologies keep low operating costs they provide the ability to offer quality products and services to enterprises and as a result of this, they allow enterprises to make profits. Therefore, use of new technology is extremely important for the success of this business. It is observed that use of technology in successful business models that are at the bottom of the pyramid as well is of utmost importance.

The CEOs personally should manage the crisis themselves and the decisions must be taken quickly right after determining the priorities. A chosen company spokesman should continuously inform the customers, owners, employees and social environment of the company. The subject matter is that how the public perceive the crisis should be taken into consideration. Evaluation of the crisis based on public's point of view will lead the company to move in line with public expectations. This is of great importance for the protection of the company's reputation and credibility in the long term.

It may not be necessary to create a new business model everytime for a new business. Moreover, enterprises should not thoughtlessly get engaged in business model innovation. Enterprises should maintain their existing business models if, by using most of the key resources and processes with profit formula, they may generate a new customer value suggestion by the same core criteria, rules and norms presently used. In this case, companies can defeat their competitors without making fundamental changes in their business models. It is a waste of money and time to create a new model that is new only to company and not focused on changing rules in the market or in the sector. What is important here is whether the yield of opportunities is worth to the effort or not. It is mostly

regarded that business model change can be seen as suitable when there is an opportunity to address through disruptive innovation (as in the case Tata's Nano car) to a customer segment previously not been addressed, when there is an opportunity to exploit a new technology with a new business model (Apple iPod/iTunes as in the case), when solution of a problem does not exist in the market, but it is essential to find out (as in the case of FedEx), when it is necessary to remove cheap and poor quality market disruptives (If Nano becomes successful, other car manufacturers will face a threat) and replace them (Johnson et al., 2008:57).

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