

Strategic Options to Respond to Disruptive Business Models - Role of Strategic Leaders

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Abstract

Business model innovation with creation of new business models, changing dimensions of business eco-system and changes in value proposition to gain a sustainable competitive advantage through automation-extension and transformation. This is leading to 'disruptive innovation'. Such disruptive innovation is bringing about substantial change in a market and industry eco-system and evolving the interactions among industry participants. The study aims to assess the impact of disruptive innovation on customer value curve and also assess the strategic options to respond to Disruptive business models based on organisational lifecycle analysis and value-effort assessment framework. The value-effort assessment framework has been restructured as the value-endeavour assessment framework to measure the feasibility of each strategic option across the two axis. Value of each strategic option is measured in terms of return, revenue, output or outcome and endeavour is measured in terms of input, time, labour, resources and opportunity cost of each strategic option. Two grids have been formed based on these two frameworks and a graphical representation of the impact of disruptive innovation on customer value curve has been undertaken in this study. Strategic leaders need to embrace unprecedented changes and the ongoing emergence of new business models and culminate a culture of collaboration, innovation and excellence. The study highlights the importance of change management and tactics to be embraced by strategic leaders to respond to disruptive innovations.

Keywords: Business Model Innovation, Disruptive Innovation, Life Cycle Analysis, Value-Effort Assessment Framework, Disruptive Business Model

Introduction

Business model innovation refers to changing one or more elements of the business model or creation of new business models with changes in the value proposition, product and service offerings to gain a sustainable competitive advantage over its competitors. Innovations that can be easily copied will not provide a sustainable advantage unless they combine with some other unique, difficult-to-imitate component of the business.

Business model innovation can be pursued by:

- Start-ups approaching a market with a new model – with new product development or new market development strategy.
- Existing businesses pursuing competitive advantage through greater market penetration by offering existing products to existing customer segments through increasing the frequency of product usage, attracting new customers within the existing segment, finding new applications for the existing products or through cross-selling of products such as free value-added services to existing clients/customers or through new product development, new market development strategy and lastly the highest risk option of diversification.
- Existing industry participants responding to competitive threats.

Innovation through transformation changes the established practices of conducting businesses, shifts the basis of competition in the industry causing 'disruptive innovation' resulting in changes in the industry value curve through changes in the factors of competition among the industry participants. This causes substantial and incessant changes in a market or industry (1, 2).

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This often results in two key types of disruption.

Two key types of disruption (1)

- *Low-End Disruption:* This describes disruption that is a low-performance based, low-price innovation serving in existing low-end markets. This kind of disruption targets the price sensitive segments of the market. This does not take away the market share of the existing participants drastically but gradually. This type of disruption is based on the performance attributes of the Kano Model (9). Netflix began with a low-end disruption with its initial video rental service that involved customers ordering online and then waiting some days to receive the video by mail but with advent of internet technology, adoption improved. Netflix moved to an online streaming

model offering low-price subscriptions and the convenience of on-demand consumption phasing out service offered by video rental stores.

- *New-Market Disruption:* This type of disruptive innovation is also often a low-performance and low-price innovation but serves new markets. New-market disruption occurs when characteristics of existing products limit the number of potential consumers. The advent of online stockbroking is an example of new-market disruption.

The study aims of develop a grid view of strategic options to respond to disruptive business models based on organisational lifecycle analysis and value – effort assessment framework. The study also aims to assess the impact of disruptive innovation on customer value curve.

Disruption Mechanism and New Value Curve Creation

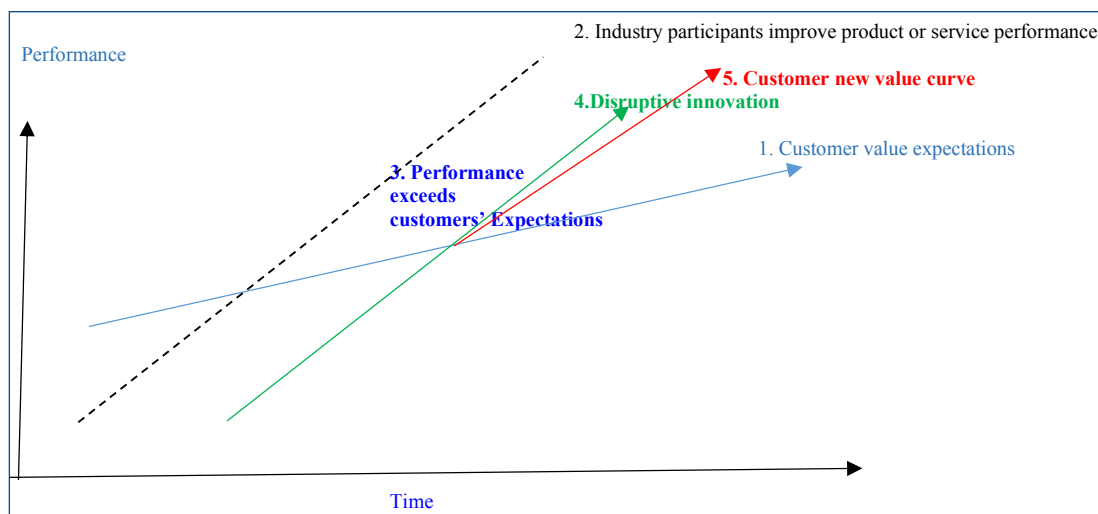


Fig. 1: Disruption Mechanism and New Value Curve Creation (3)

Based on theory of disruptive innovation the study tried to develop the disruption mechanism and its implication in new value curve creation thereby raising the level of customer expectations/needs as disruption often creates new needs for customers or often capitalises on untapped or unrealised customer needs. Thus disruptive innovation facilitates new need creation and forces the industry incumbents to pursue a wide array of strategies – sustained and improved performance, change management, adapt to new systems, raise the level of offerings, efficiency and effectiveness, reduce wastage of vital resources, lean and agile supply chain management, eliminate non-value added segments/services.

Disruptive Business Models (4,5)

The Subscription Model

The subscription model is a long-established business model in which the subscriber pays at regular intervals for ongoing access to a product or service. This is a hyper-disruptive business model where the disruption occurs via the lock-in period through the payment of subscription fees for continued access to the product or service. This is enhanced by the use of customer data to personalise or customisation of the product or service over time where switching might cost consumers a lot. Many of these

businesses leverage this technology. This model has been able to prevent piracy, imitation or espionage as online global launches are a barrier to copying.

The Free Model

The free model involves collecting and selling personal data harvested by offering consumers a ‘free’ product or service that captures their data and/or attention. This model disrupts industries where organisations have traditionally charged for purchase or access to the product or service. Examples include Google, social media platforms and free online news and entertainment sites. Different forms of free model include:

- The organisation seeks to attract users so that they may be presented with advertising messages. The advertiser pays the organisation for access to the audience. E.g. Youtube.
- Barter - A product or service is given to customers in exchange for something of value such as personal data. E.g. Social media platforms.
- Gift - A product or service is provided for free because the producer derives satisfaction or some other benefit from doing so. E.g. – Open source software.

The Freemium Model

The freemium model extends beyond the free model through payment of fees for some additional premium services apart from the basic services which can be availed for free. This model is applicable where marginal cost for extra units and distribution are lower than advertising revenue or the sale of personal data. This model disrupts businesses that could have formerly charged even for the basic services. E.g. Professional networking platform LinkedIn.

The Digital Platform Model

The digital platform model creates a digital marketplace bringing together buyers and sellers and facilitating direct exchange transactions based on need. This model disrupts the marketplace by directly connecting providers and enhancing the quantum of competition and enhancing the number of participants in the digital marketplace. E.g. Amazon.

The Access-Over-Ownership Model

The access-over-ownership model provides temporary access to goods and services traditionally only available through purchase. This includes ‘sharing-economy’ disruptors, which acts as a liaison between lenders of assets (home, car) and borrowers on behalf of commission.

The Hypermarket Model

The hypermarket model disrupts by using market power and economies of scale to crush competition, often by selling below cost price. Established organisations often resort to cash-burns to establish a position intended to provide long term profitability and prevent new entrants from gaining market share.

The Service Ecosystem Model

The service ecosystem model disrupts by selling an interlocking and interdependent suite of products and services. This creates consumer dependence. E.g. Apple’s interoperating system of computers, smartphones providing automated synchronisation across devices.

Cross-Subsidisation Model

An organisation gives a product or service to customers for free or at a cheaper rate to enhance the sales of a complementary product.

Crowdfunding

Crowdfunding is the use of online platforms to raise finance to fund a specific project, crowdfunding enables innovators to access funds for ideas that investors want to support for reasons not just for financial returns. This disrupts the existing business models of traditional lending services.

Social Enterprises and Benefit Corporations

Social enterprises and benefit corporations are organisations that operate for the purpose of creating shared value for all stakeholders rather than primarily serving shareholders. They focus on crowds, subjects, players and context setters – four diverse types of stakeholders based on power and their relative interest in the organisation. These organisations outway the performance of organisations focussing only on players (high power-high interest group) (6).

Strategic Options to Respond to Disruptive Business Models an Organisational Lifecycle Analysis – A Grid View (7)

Phase	Start-Up Phase	Growth Phase	Maturity Phase	Shake Out Phase	Decline/Renewal
	<p>If the disruption occurs when the business is at the Start-up Phase</p> <p>At this stage there will be many different visions as to how the industry will develop and many different approaches to the industry, in terms of product type, features, performance and target markets. Leaders are mostly innovators and huge amount is invested in R&D despite limited resources.</p>	<p>If the disruption occurs when the business is at the Growth Phase</p> <p>Once an industry becomes established and grows rapidly, it enters the growth stage. This phase sees a surge in new competitors. Growth rate is above the industry average. High-growth rates enable most organisations to survive. Although cash-flow improves but further investment is needed to cater to expansion plans. Competitive differentiation is less critical at this stage and leaders focus to support product expansion and improve distribution channel for sustainable competitive positioning.</p>	<p>If the disruption occurs when the business is at the Maturity Phase</p> <p>As growth rates reduce and moves towards industry average rate, the organisation enters the maturity stage. Rivalry is intensified, and some companies may consolidate through mergers and acquisitions. Power of buyers' increase with enhanced knowledge, not all of the original products, organisations or strategies survive hence improved and customised products and services are demanded. This is the longest stage in an organisation's life. At this stage, cash flow is positive. Leaders focus on efficiency, cost control, market segmentation, defend market position and maximise profits.</p>	<p>If the disruption occurs when the business is at the Shake out Phase</p> <p>This stage is characterised by a plateau and a possible decline of growth and profitability in the industry. Many organisations in this stage will leave the industry due to their low returns, thereby reducing rivalry and competitiveness. The remaining, small group of organisations then dominates the industry and often consolidates. It becomes imperative that organisations in this stage protect their positions and maintain profitable operations. The challenge for leaders is to choose between exit or combat and defend the position.</p>	<p>If the disruption occurs when the business is at the Decline Phase</p> <p>The industry enters the decline stage once growth, ROI and profitability decline consistently. The threat of Substitutes is very high. Domination of the industry by a few large competitors no longer yields sufficient returns. The industry's products or services may no longer be useful to consumers. Leaders may create niches or even decide to revolutionise the industry through redefining strategies and innovation.</p>
Combat Strategy	<p>Invest in Disruption Model - This response involves actively investing in a disruptive threat such as disruptive technologies, developing the organisation's intellectual and physical capabilities, creating new digitised processes</p>	<p>Block Strategy - This involves by using all legal and regulatory measures including use of intellectual property rights to inhibit the disruptor.</p>	<p>Redefine the Core Business Strategy - This strategy involves building an entirely new business model, often in an adjacent industry where it is possible to leverage existing knowledge and capabilities.</p>	<p>Milk Strategy - This strategy involves extracting the most value possible from vulnerable businesses while preparing for the inevitable disruption. It often ends in wind-up when the organisation is unable to create any value.</p>	<p>Redefine the Core Business Strategy</p>
	<p>Retreat into a Strategic Niche - This strategy involves focusing on a profitable niche segment of the core market where disruption is less likely to affect.</p>	<p>Invest In Disruption Model - As business in growth stage and aims for expansion and may raise funds to acquire companies that already possess these strategic resources and capabilities.</p>	<p>Invest in Disruption Model</p>		

Phase	Start-Up Phase	Growth Phase	Maturity Phase	Shake Out Phase	Decline/Renewal
		Disrupt the Current Business Strategy - This is an aggressively competitive strategy that involves new product or service development that competes directly with the disruptor, and leveraging inherent competencies such as scale, market knowledge, brand, access to capital, relationships to build the new business.	Disrupt the Current Business Strategy	Retreat into a Strategic Niche Strategy	Retreat into a Strategic Niche Strategy
			Block strategy	Diversification	Milk strategy
			Diversification – new product development and targeting new markets	Exit strategy - The exit strategy involves winding up the business entirely ideally through a sale of the business while value still exists.	Exit strategy
Role of Strategic Leaders	Risk-Takers	Risk-Takers	Caretakers – Nurture the organisation to move from growth to maturity phase	Surgeons — They have an ability to prune or sever parts of the organisation based on the case	Undertakers — Enable an organisation to salvage what is viable and shut down the rest to prevent incurring prolonged losses.
Disruptive Business Models that can be Adopted Based On Stages of OLC	Freemium Model, Digital Platform Model, Crowdfunding, Social Enterprises and Benefit Corporations, Access-Over-Ownership Model	Digital Platform Model, Subscription Model, Freemium Model, Service Ecosystem Model, Cross-subsidisation	Subscription Model, Free model, Hypermarket Model, Service Ecosystem Model	Free model, Hypermarket Model, Cross-subsidisation, Social Enterprises and Benefit Corporations	Access-Over-Ownership Model

Strategic Options to Respond to Disruptive Business Models Based on Value/Effort Assessment framework (8)

<p>High</p> <p>VALUE (Output measure)</p> <p>Value of each strategic option is measured in terms of return, revenue, output or outcome</p>	<p>Mini-Max Low-hanging fruit option – (Minimum endeavour-maximum return) high-value and low-endeavour options</p> <p>Low-hanging fruit Strategic options to Respond to Disruptive business models</p> <ul style="list-style-type: none"> • Block Strategy • Milk Strategy 	<p>Max-Max Blood, sweat and tears option – (Maximum endeavour-maximum return) high-value and high-endeavour options require time and resources but have great potential to create high value for the organisation.</p> <p>Blood, sweat and tears Strategic options to Respond to Disruptive business models</p> <ul style="list-style-type: none"> • Invest in disruption model • Disrupt the current business strategy • Redefine the core business strategy
<p>Low</p>	<p>Mini-Min Delegate or dump - (Minimum endeavour-minimum return) low-value and low-endeavour options can often be delegated or can be rejected altogether if they do not provide sufficient value</p> <p>Delegate or dump Strategic options to Respond to Disruptive business models</p> <ul style="list-style-type: none"> • Exit Strategy 	<p>Max-Min Dead ducks - (Maximum endeavour-minimum return) low-value and high-effort options</p> <p>Dead ducks Strategic options to Respond to Disruptive business models</p> <ul style="list-style-type: none"> • Retreat into a strategic niche
		<p>ENDEAVOUR (Input measure)- is measured in terms of input, time, labour, resources and opportunity cost of each strategic option</p> <p>Low High</p>

Conclusion

The fast-changing business environment and ongoing business model innovation elevate the importance of continuous change management through creation of agile organisations. Such change management to respond to disruptive innovations or create disruptive business models is linked to organisational life cycle, risk appetite of leaders, resources and capabilities, social dynamic at workplace and organisational culture. Strategic leaders need to embrace unprecedented changes and the ongoing emergence of new business models and culminate a culture of collaboration, innovation and excellence.

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