Business Model Generation – The Emperor’s New Clothes?

A review of Osterwalder’s & Pigneur’s Business Model Generation approach and its potential for improving business development

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Table of contents:

Rapid Propagation .......................................................... 5
A well thought out business model for the Business Model ........................................... 5
  A picture tells more than a 1.000 words ......................................................... 5
  It is about you first and about the model second .............................................. 6
  Cartoon Format ................................................................................................. 7
  Graphic Facilitation ......................................................................................... 8
  An App for the iPad ........................................................................................ 8

The Business Model Front Office ................................................................. 8
  Market Segments and the Value Propositions .................................................... 8
  Channels ........................................................................................................ 9
  The software industry channel definition ....................................................... 9
  The value chain ............................................................................................... 9
  The Channels and the Business Model ........................................................... 10

The Business Model Back Office .................................................................. 10

The Business Model Environment ................................................................. 11
  Separating the controllable from the uncontrollable ......................................... 11
  The Business Model Environment in the future ............................................. 11
  Mitigate and exploit ....................................................................................... 12

The Four Business Model Environment “Forces” ........................................... 12
  Key Trends .................................................................................................... 13
  Market Forces ............................................................................................... 13
  Industry Forces ............................................................................................. 14
  Macro Economic Forces .............................................................................. 15

Managing the business model environment .................................................. 15

How do they make money? ............................................................................. 16

Is Business Model Generation the Emperor’s new clothes? ......................... 17
  Reality Distortion Field .................................................................................. 17
  The quick fix and the low hanging fruit .......................................................... 17
  Business Model Generation is not a shortcut ................................................. 18
  Prototyping ..................................................................................................... 18
  The water may look flat, but.... ....................................................................... 18
  Not a one night stand ...................................................................................... 19
  Management Consultants and Business Model Generation .......................... 20
  Involvement ..................................................................................................... 20

Our conclusion ............................................................................................... 21

About the Author ............................................................................................ 22
Targeted audience
The target audience for this whitepaper is the board of directors, the CEO and other executives of software driven companies with ambitions for achieving global market dominance.

The whitepaper is applicable for all types of value chains\(^1\).

Abstract
The whitepaper discusses the application of the Business Model Generation framework, the use of the 9 building blocks on the Business Model Canvas and the Business Model Environment analysis.

The whitepaper argues that the approach is not a quick path to success, it is not a way to achieve fast and monstrous results by doing very little and it is not an approach to harvest the so called “low hanging fruit.”

Contradictory to common perception, Business Model Generation facilitates a comprehensive, structured and on-going process of gradually improving the business setup, which delivers steadily increasing value to customers, attractive profit for the owners and remains tough to copy by competitors. Business Model Generation combines the narrative description of a business with the associated P&L\(^2\) simulation of the revenue and cost streams creating a blue print, which can be tested against reality and implemented when proven valid.

Business Model Generation is not a one-time effort. A start-up will return to the business model blue print weekly. The company in Go-Go\(^3\) will check monthly, the company in Adolescence will check quarterly and the enterprise in Prime will check twice a year.

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\(^1\) See [http://tbkconsultblog.com/2013/02/12/partner-pl-the-way-to-make-partners-in-the-software-industry-productive/](http://tbkconsultblog.com/2013/02/12/partner-pl-the-way-to-make-partners-in-the-software-industry-productive/)

\(^2\) P&L: Profit & Loss

\(^3\) See [http://www.adizes.com](http://www.adizes.com) for definitions of Go-Go, Adolescence and Prime

In the span of just a few years the Business Model Canvas and the formats used by Alexander Osterwalder and Yves Pigneur have spread like wildfire all over the world.

Alexander Osterwalder and Yves Pigneur didn’t invent the concept of “the business model.”

They provided a precise and consistent definition and made the concept comprehensible, operational and accepted.

The business model used to launch the book and its’ concepts were well thought out. Inspiration had been drawn from the open source communities and the promise of graphical facilitation\(^1\).

In June 2009 Osterwalder organized an event in Amsterdam (NL) to share knowledge and experience around the topic of business model innovation. The event accompanied the upcoming release of the Business Model Generation book.

Before writing a single sentence or drawing a single illustration Osterwalder and Pigneur invited people to co-create the book. Those who signed up had to pay between $24 (Early Birds) and $250 (Late Birds). The book was paid for before it was even written.

The book isn’t the traditional academic “volume” making things look sophisticated and comprehensive. It is more like a comic book or an illustrated step-by-step manual.

Compare Osterwalder’s & Pigneur’s Business Model Generation with books such as “Good to Great” by Jim Collins, “Innovation: The Five Disciplines for Creating What Customers Want” by Curtis R. Carlson & William W. Wilmot (SRI), “The

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\(^1\) See ”Visual Meetings” by David Sibbet.

All of the books mentioned are famous and promise that a new approach will provide improvement in corporate and/or personal performance.

What makes Business Model Generation so different?

The book makes a bold statement on the cover:

You’re holding a handbook for visionaries, game changers, and challengers striving to defy outmoded business models and design tomorrow’s enterprises. It’s a book for the Business Model Generation.

Who wouldn’t love to be a member of that group? Game changers? Yes, here we come.

However, not everyone belongs to this group. Not everyone is a visionary and/or a game changer. Not everyone is a challenger striving to defy outmoded business models and design tomorrow’s enterprises.

Osterwalder and Pigneur knew that bringing something new to the market would be met with resistance and ignorance from the established authorities and the mass market. The law of diffusion of innovation also applies to innovative business development concepts.

Osterwalder and Pigneur intelligently addressed their new approach to the early market. Targeting the Business Model Generation framework at technology enthusiast and visionaries they managed to stir the interest of the only group who would be receptive to new ideas.

However they also knew that jumping the chasm between the early market and the mainstream market requires momentum.
Thus, the first couple of pages are filled with names of people who have made contributions to the book\textsuperscript{2}. If you subscribe to Business Model Generation you will be joining an innovative community. No need to be sceptical, you are not the first. With Business Model Generation you will never have to eat alone.

Today Osterwalder and Pigneur's approach to Business Model Generation has been widely adopted and is used by people and companies in the mainstream market. It is by no means restricted to “the game changers and the challengers”. Even big corporations and governments now pay consultants to teach and tutor partners and startups on the Business Model Generation concepts.

On page 18-19 you get the full picture and you understand it immediately.

You get the big picture instantly. Yes, this is a 360-degree depiction of a business. The small graphical icons support your immediate understanding and your ability to memorize the picture.

It takes just 28 pages to describe the 9 building blocks making up the business model. Each of the pages is rich on graphics and is segmented into short paragraphs. Compared to the books listed above we are in a completely different universe.

\textsuperscript{2} And paid between $24 and $250 to have their name mentioned
Are any of the nine building blocks more important than the others?

The answer is very simple: No!

Neglecting any one of the nine building blocks may cause your business model (and thus your business) to suffer or fail.

However, experience shows that the some of the building blocks are more difficult to get right than others. The building blocks in the business models front office are the most challenging.

The combination of the Market Segments and the Value Propositions are the most difficult to get right. These two building blocks define which products/services are very attractive to which customers AND are better than the competitive alternatives available to these customers.

Supporting the process of defining and constantly improving The Market Segments and the Value Proposition relationship Alexander Osterwalder has developed the Value Proposition Canvas.

As a management consultant I can testify that this is the toughest part for all companies.

You can run a business with a mediocre value proposition and blurred market segmentation, but it is impossible to scale and the P/E relationship will remain lousy.

The Value Proposition Canvas is helpful, but I still find the NABC approach developed by SRI a more mature approach to the challenge of finding the right combination of product and customers.

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4 P/E: Price/Earning. A valuation ratio of a company’s current share price compared to its per-share earnings. The term is also used for non listed companies when making a investment/divestment transaction.

According to Osterwalder the main activities of the Channels are:

- Creating awareness
- Helping customers evaluate
- Helping customers purchase
- Deliver
- Providing after sales support

The channels in the B2B software industry can assume just a few or many more functions than those mentioned by Osterwalder.

The word “channel” is used in the software industry to describe independent companies that assume various roles and obligations in bringing a software product to the customers. The definition is rather broad, since the roles and obligations can vary substantially from “simple” reselling to system integration, solution development on top of the software, implementation in terms of consulting, project management, customization, training and support.

A value chain describes the steps and activities required to find, win and keep happy customers.

Figure 2: Sample Value Chain

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6 Alexander Osterwalder is addressing all types of business activities including government and non-profits. He therefore from time to time misses out on issues, which are specific to certain industries and types of businesses.
All B2B software products have a version of the value chain illustrated in fig. 2.

The choice of channels has a profound impact on all the other business model building blocks.

This tight relationship between the choice of channels and the business model causes most software companies major headaches.

The solution is to operate with two sets of value propositions:

1. The customer value proposition(s)
2. The channel partner value proposition(s)

These value propositions are fundamentally different and generate completely different demands for the business model back-office building blocks.

The roles of the business model back office building blocks are to support the execution in the front office.

The separation of the business model back office into Key Activities, Key Resources, Key Partnerships and Cost Structure is logical and works well.

A well functioning back office can compensate for a mediocre front office, but you must be a well-established brand to sustain this imbalance for long.

Keeping the back office in sync with the front office is a constant effort. While you can always work on refining the back office from within most of the changes to your front office are forced upon you from without.

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7 Forces outside your business model may have caused your front office to slide from excellent to mediocre
When we take a close look at the business model canvass we notice the absence of some significant areas impacting our business.

Where do we deal with the competition, the technology trends, the legal and environmental issues, the global economy, etc. etc.?

No business model lives in a vacuum and the toughest part in business is dealing with the issues that we cannot control.

We have to make it to page 200 in Osterwalder & Pigneur’s book before we are exposed to what they call the business model environment.

Reading most reviews of the book and listening to consultants and other supporters of the business model approach indicates that they apparently never made it to page 200. Most probably just read the 50 pages that you can download for free from Osterwalder’s web site.


*Doing the business model canvas part only is like planning to put a man on the moon, but ignoring the weather, the earth’s gravity, the moons’ gravity, cosmic radiation, the friction of the earth’s atmosphere and probably a lot of other external factors that I don’t even know about.* A business model exercise *that skips the analysis of the impact from the business model environment is at best a complete waste of time and resources, and at worst is downright hazardous and dangerous.*

To make things even more difficult we have to consider the business model environment of tomorrow rather than business model environment of today.

The business model environment changes continuously. The
success of our business model is a result of our ability to take advantage of the business model environment, especially the changes in the business model environment.

The business model environment is by definition the circumstances under which we have to operate. We basically have two options:

1. Mitigate the impact of the factors and changes in those factors that are working against us or are exerting risk upon us.

2. Exploit the factors and changes in those factors that could work to our advantage.

Can we change the business environment?

Yes - from time to time business models permanently tweak the business environment. Microsoft, Google, Apple and Facebook are examples of companies that have changed the business model environment for a lot of other companies.

However, just because Apple & Co. did it doesn’t mean that you can/will do it, too!

Most software companies will have to develop and manage their business model under a given set of business model environment characteristics. If your business model is so strong and successful that it changes the entire industry, then that is certainly an accomplishment that will benefit you tremendously, but don’t count on it at the outset.

The business model environment is divided into four major areas:

1. Key Trends
2. Market Forces
3. Industry Forces
4. Macro Economic Forces
Osterwalder actually names these areas “forces”, which in my opinion may confuse them with Porter’s “Five Forces” to which there is some overlap.

However, Osterwalder’s four business model environment areas are fairly comprehensive and complete and will work well for most software driven companies.

The key trends include:

1. Technology Trends
2. Regulatory Trends
3. Societal & Cultural Trends
4. Socioeconomic Trends

Most software-driven business models are receive substantial impact from the Key Trends force. The software driven industry is also the main technology driver in itself, and aggregated the industry has more impact on the business model environment forces than any other industry.

The rapid proliferation of the Internet, the standardization of digital media formats, the acceptance of smart personal mobile computers (smart phones and tablets), the “invention” of apps and apps ecosystems, the development of the “cloud”, the availability of in-memory analytical tools, etc., are technology drivers disrupting some companies’ business models while enabling other companies’ business models.

The market forces include:

- Market Issues
- Market Segments
- Needs & Demands
- Switching Cost
- Revenue Attractiveness

Although market forces also change over time, the main consideration here is the nature of your potential customers’
situation, needs and behaviour associated with their purchase process and decision for your type of product/service.

Key issues to consider are:

- Is there a market for your product/service?
- Is your market growing or shrinking?
- Can this market support your growth ambitions?
- Are some segments of the market more attractive than others?
- Do you (in the eyes of the market) offer “must have” or “nice to have” value?
- Is it easy to identify the key decision makers for your product/service?
- What prevents your potential customers from buying your product/service?
- What is the switching cost?

The software industry is probably the greatest innovation engine the world has ever seen. New solutions to existing problems and new opportunities for completely new markets pop up every day. Although the business model innovation approach helps us analyze and optimize our business model it hasn’t eliminated gravity.

We still have to face the law of diffusion of innovation.

We still have to cross the chasms.

The industry forces include:

- Competitors (incumbents)
- New Entrants (insurgents)
- Substitute Products & Services
- Stakeholders
- Suppliers & other value chain actors

Managing your business model without an eye on your customers’ alternatives seems hazardous. You should not ignore your competitors, but you can choose to ignore the moves of your competitors, if you see no threat to your business.

Very low barriers to entry characterize the software industry.
Starting a software business requires very little capital. Thus, the software industry is crowded with incumbents and insurgents in all segments. That’s not necessarily a negative thing. Having someone helping you make a market can lower your cost of sales considerably.

Stakeholders are people in organizations that have influence on your business model without being customers. Stakeholders are typically your staff, labour unions, shareholders, industry associations, the government, lobbyist, consultants, analysts and the press.

The macro economic forces include:
1. Global Market Conditions
2. Capital Markets
3. Commodities and Other Resources
4. Economic Infrastructure

The macro economic forces affect big companies, although smaller companies are less affected directly. As the software industry is made up of primarily small companies, and as software is mostly boosting productivity, the software industry is often unaffected by the macro economic forces.

Osterwalder and Pigneur make another important yet often ignored observation: No individual alone in your organization could paint a holistic picture of your business model’s environment and design space. Only by mapping out each specialist’s knowledge can you develop a shared understanding of your environment.

Although there is nothing in the business model and business model environment approach that prevents us from keeping the strategy considerations in the board room, Osterwalder and
Pigneur are passionate believers in “inclusion.” They recommend drawing on the insight already residing in the organization and bringing this knowledge into play as we review and refine our business models.

About the same time as the book hit the streets the people behind Business Model Generation launched a business model simulation tool for the iPad.

The App is a very nice graphical representation of the Business Model Canvas allowing you to add sticky notes and to perform P&L simulations. It is also a tutorial, as it will provide you with explanations and suggestions in each of the 9 building blocks.

Soon after the release of the App a web based Business Model simulation tool was also released. The web version supports collaborative sharing and working on business models.

The Business Model Generation concepts are “freeware.” Anybody can copy and use them. The Business Model Foundry (Osterwalder’s and Pigneur’s company) make money on selling Apps, subscriptions to the web version, training and consulting.

Osterwalder, especially, travels the world on invitations from enterprises and governments to introduce his Business Model Canvas and concepts and to help develop business models for individual clients.

An army of smaller consulting firms have adopted the approach (it is freeware!) and provide consulting in all forms and shapes around Business Model Generation.

Surprisingly for many, Osterwalder characterize his company as a software business. He does not want to build a consulting company, but rather a software company providing all the external and internal consultants with smart tools facilitating the modelling process.
No, we will not claim that Business Model Generation is an illusion.

Business Model Generation certainly is a genuine and solid approach to map, simulate and develop a business idea or an existing business.

However, we will claim that is not what most people expect or hope it is.

Just because it looks easy doesn’t mean it is easy.

We have assisted in several Business Model Generation projects and our clients have all been surprised (some even overwhelmed) by the number of iterations required to start and sustain a Business Model Generation process.

Most companies still subscribe to this approach:

“Let’s do something and see what happens”.

The implications of this approach are described in depth by Eric Reis in his book “The Lean Startup1.”

You will always see what happens. However, it may not be what you expected or hoped to see and you may not have learned anything from the experiment. You are most likely left in a situation where you don’t know what to fix to improve the outcome.

People still keep talking about “the low hanging fruit.” A metaphor, which has lost its’ relationship with reality ². Most people are looking for ways to achieve fast and monstrous results by doing very little. Conceptually a sensible and meaningful

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1 Eric Ries, The Lean Startup, September 2011

2 Today’s orchards have straight trees ensuring equal amounts of sunlight and making all the fruit easily accessible for picking.
approach, in reality completely useless, because there are no “low hanging fruit.” And if there were, someone else took them yesterday.

People looking for the low hanging fruit go to bed hungry. The competition for the low hanging fruit is gigantic.

Expecting that the Business Model Generation is a short cut to fixing problems fast and generating profit instantly is a common misconception. And this comes as a big surprise to many.

The book is (especially the first 50 pages) almost self-explanatory, which leads people to conclude that Business Model Generation is a walk in the park. A little introduction and couple of ½-day workshops and we are home free. You call in a management consultant to help you and within a week or two your business model is rock solid.

Business Model Generation is a tool for prototyping. It is a way to try out many different ideas before committing too many resources to a test that will fail. Failure is an integrated element of prototyping. Most early models will fail. That’s exactly why we prototype. Failing is learning. Our first business models are based on assumptions and guesses. As they fail, we will learn something that we incorporate in our next iteration.

The number of iterations and the time required to develop a business model that works is unpredictable. In this respect Business Model Generation is no different from other innovation approaches. The three biggest advantages of Business Model
Business Model Management

Generation are:

- It deals with the entire business model and not only the product/service
- It keeps down the cost of experimentation
- It organises the learning curve

A business model is a blueprint we use for testing against reality. The philosophy behind Business Model Generation says that there is no need to test a business model that doesn’t even work on paper. Let’s keep prototyping until it works on paper, then let’s go and test versus reality.

Not a one night stand

The best illustration of how to use Business Model Generation can be found in Steve Blank’s book “The Startup Owner’s Manual”.

Don’t think this book is not for you.

A startup company or startup is a company or temporary organization designed to search for a repeatable and scalable business model.

Many companies are dragging along for years with business models that they can neither repeat nor scale. Survival is a tough daily fight to make ends meet and the business cannot generate enough profit to invest in growth.

Steve Blank provides the prescription for getting out of this quagmire. Business Model Generation is an integrated tool in his approach together with his renowned Customer Development approach.

Steve Blank adopts the Business Model Canvas as the graphic representation and simulation model for your current state and your next “assumption”.

As you move forward and test new approaches you constantly update your business model.

Business Model Generation is not a one-time effort. It is an on-

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4 http://steveblank.com/2012/03/05/search-versus-execute/
going exercise and process. You are mapping the waters as you sail them. You keep testing and adjusting your business model until it works or until you abandon it, pivot and try a different route.

Steve Blank argues that you cannot delegate your Business Model Generation to a management consultant. You have to dig in yourself.

Although we are management consultants we agree with Steve Blank.

As management consultants we can help facilitate the process and we can play the devil’s advocate to your assumptions and interpretation of your experiments, but we cannot make the models for you.

Bringing all the people involved in a certain business problem/challenge together to review the issues and develop potential solutions is by no means a new concept.

Coming from Scandinavia with the shortest power distances in the world we have to involve people in the problem definition as well as in the solution identification. Otherwise nothing will be accomplished.

There are other cultures where a hierarchical top down approach still reign and where problem definition as well as the solution identification is undertaken at the executive level, then passed on to the operative level for execution.

If you want a recent update on the power of involvement you should read Karen Phelan’s new book: “I’m Sorry I Broke Your Company – When Management Consultants are the Problem, Not the Solution.”

“I’m Sorry” is also not the traditional academic thesis based on years of “research” which characterize most management literature. The book is based on Karen’s personal experience, her common sense and some secondary source research. The book
has several illustrative examples from Karen’s own praxis and also refers to other cases, which have reached the public domain.

It is a refreshing and convincing explanation of the power of involvement.

**Our conclusion**

We believe that the combination of the 9 building blocks of the Business Model Canvas from Osterwalder & Company, the application of visual facilitation as promoted by David Sibbet and the power of involvement as expressed by Karen Phelan hold tremendous potential for the development and execution of meaningful and profitable business models.

The combination of the three approaches (and executed the Steve Blank way) may be the best approach available to companies in today’s rapidly changing environment where technology offers so many opportunities for new value creation.

Combining the three approaches has no relationship with quick fixes and “low hanging fruit.” Rather it is a structured framework to maintain a persistent and steady course and gradually approach a business that is valuable for many customers and profitable for the owners.
Hans Peter Bech

Hans Peter Bech is a software industry “growth consultant”; he has more than 30 years of operational experience with global business development in the software industry.

His experience includes all types of software from high priced enterprise management solutions to low price/high volume software sold over the Internet and/or through telesales.

Hans Peter has been exercising all Go-to-Market variations such as direct enterprise sales into foreign markets, indirect through resellers and distributors, through own subsidiaries, through franchises and through acquisitions.

Hans Peter is the author of several whitepapers on software business development and Business Model Management in the software industry. He frequently writes articles on the subject.

He started his career as a management consultant in 2003 and founded TBK Consult in 2007. Since then he has built the company to its present position with 24 senior consultants in 16 countries.

Hans Peter oversees the development of TBK Consult as well as performing management consulting assignments for selected clients.

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More about Hans Peter Bech