HOW DO EXTERNAL ENVIRONMENT INFLUENCE CHOICE OF BUSINESS MODEL

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ABSTRACT

The advent of Internet redefined the way business models were perceived. Internet, the WWW revolution, e-commerce and e-business phenomenon have had enormous impact on businesses. Today, it is very clear that technology and internet have changed business landscapes. Researchers like Merrifield (2000) have suggested that the impact of this technology hype would have been huge, even if traditional businesses were not abrogated. Technology has become an external environmental influence that is helping organizations work in partnership, offer joint value proposition, build up channels and distribution network and generate profit from diversified and shared revenue streams. Rentmeister and Klein (2003) call for new modeling methods in the domain of business models. Effectively, a whole range of authors propose using the relatively new concept of business models for managing companies in the Internet era (Chesbrough and Rosenbloom 2000; Afuah and Tucci 2001; Applegate 2001; Pateli and Giaglis 2003).

It is necessary to create a business model in response to environmental needs for the following reasons :

1) *Present business environment is characterized by complexity and uncertainty. This has given rise to a possibility of large number of business models. The concepts and tools to cope up with emergency environmental needs are still missing.*
2) *Successful business models are those which are based on coordination of large number of stakeholders, business partners, process designers and information management staff. But there are very few tools that shape business logic of today's firms.*
3) *Business models should be capable of generating revenue and steady financial streams. This means all aspects of business models should be optimized and reinforced to meet fierce global competition.*

Keywords : Business Environment , External Environment, Business Models

I. LITERATURE REVIEW

Due to technological change and globalization (Archibugi and Iammarino 2002), choosing business partners, reaching your customers and defining value proposition have become a complex task. However, new technologies, globalization and the abundant reservoir of choices to configure a business, make managing, a difficult task (Zahra and O'Neill 1998). Hodgson (2003) compares this phenomenon to capitalism. Competition pressure is forcing firms to pursue profit motives in two main means. Firstly, it is expanding businesses to new markets through geographical expansion or introduction of new products and services. Hogdson further

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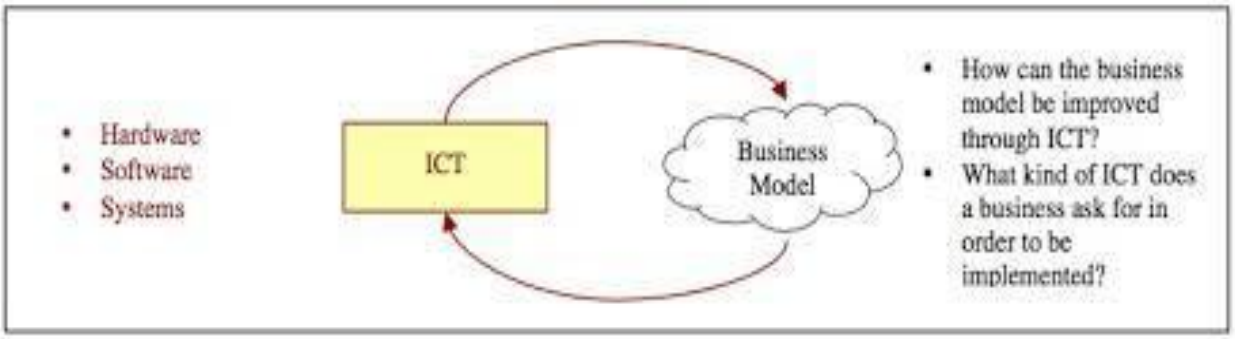
elaborates to state that innovation would be fuelled by expanding frontiers of science and technology, leading to new field of knowledge and enquiry. Second is cutting cost through smart use of technology. This will eventually help in balancing out resources.



Strategic Adaptation to Recession - A Recent example of Recession That Highlights Adaption of Business model to External Pressures

Recession and environmental shocks are likely to make business policies and strategies ineffective (Meyer et al. 1990). Adapting to business changes and environmental shocks are necessary capabilities in todays times. Strategic flexibility that refers to businesses ability to respond to changing competitive environment(Hitt, et al., 1998) influences any firms ability to perform in crisis. Others researchers suggest that discontinuous change within an industry stimulates the formation of inter- organisational relationships, promotes experimentation with new organisational forms and precipitates affiliations spanning industry boundaries (Meyer, 1982).

Recessions present businesses with a dilemma (Chastain 1982; Deans et al. 2009). Recession asks for cutting costs and reducing production, which in turn stops firm from recovering properly.

Designing a strategic response to recession is a complex processes and involves participation from various business stakeholders such as business owners and senior managers. Restructuring of business models and processes, replacement of managerial practices and functional reorganization are examples of strategic adaptation to recession(Whittington 1991; Geroski and Gregg 1994)

In simplest terms business adopts 3 kinds of response to recession : retrenchment, investment, and 'ambidextrous' strategies.

Business choose to retrench when they find it to be easier to reduce costs that generate additional revenue. Disinvestment in business, closure of establishment, reduction in labour hours, expenditure cuts and reduction in activities like R&D, marketing etc are signs of retrenchment (Rones 1981; Shama 1993; Geroski and Gregg 1997; Michael and Robbins 1998; DeDee and Vorhies 1998).

Firms may perceive recession as an opportunity and hence they are likely to go with the Investment strategy where they would like to invest, innovate and expand into new markets in order to achieve or extend a competitive advantage. Carnegie established dominant positions in the emerging oil and steel industries during the 1870s recession by taking advantage of new refining and steel production technologies and of the weakness of competitors (Bryan and Farrell 2008), and Edison established General Electric (Lynn 2009).

'Ambidextrous' combine retrenchment and investment strategies(Tushman and O'Reilly, 1996; He and Wong, 2004; Raisch and Birkinshaw 2008).

Information from academic studies of firms adapting to environmental constraints or jolts might also offer pointers to how firms adjust to recession.

II. DEVELOPING A BUSINESS MODEL - STEPS

2.1 Designing a Business Model

Under this step, management defines and designs the correct business logic that responds to market circumstances

2.2 Finance a Business Model

Management works out a financial structure for the business model (e.g. internal funding, venture capital, stock market funding)

2.3 Implement a Business Model

The business model is implemented into business structure, business processes and infrastructure

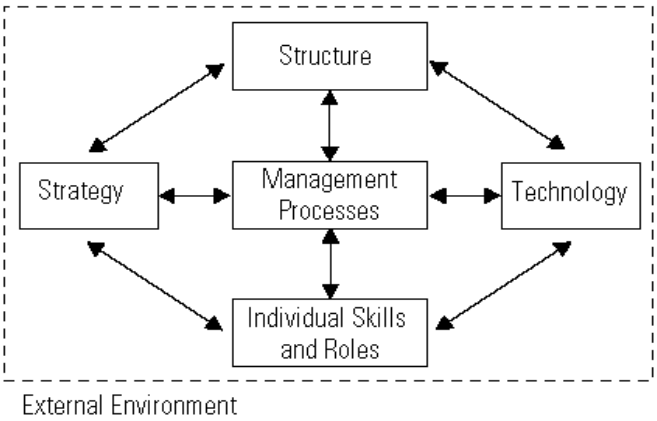
III. EXTERNAL ENVIRONMENTS INFLUENCE ON BUSINESS MODEL

External environment looks at business organizations and firms from a different angle and different business layers. Business founders position the company in the market to define the direction and formulate objectives and goals, whereas business managers have to understand and implement these visions into concrete objectives. This is where the role of environment in influencing the business model type is seen, and conceptually defined business models come into picture.

Firms earn revenue only when creating a common and shared understanding of money and communication, and by facilitating communication between people and heterogeneous elements (Fensel 2001).

The organizational business models are subjected to continuous monitoring by external forces. As Porter defines the forces, they can be classified as competition, legal, social or technological change and changes in customer demand. It is the manager's role to design or adapt a company's business model by responding to these external forces.

Figure 1 A Model of Strategic Change and Fit



Source: Adapted from M.S.Scott Morton, ed., *The Corporation of the 1990s: Information Technology and Organizational Transformation* (New York: Oxford University Press, 1991), p. 20.

Technology Evolution

The growth of technology and its impact on business application is changing rapidly. As technology is influencing every aspect of business, it becomes a manager's responsibility to oversee how technological pressures are being used by managers to improve the business logic of the firm. It will be an understatement to say that technological change is a major business influencer. In some cases, technological changes may even challenge the mere existence of the particular business model.

IV. COMPETITIVE FORCES

A second-major influencer, on a firm's business model comes from its competitors. For traditional industry players, adapting to changes in the competitive environment is especially crucial when new dynamic competitors rapidly dispute their market position as an incumbent (cf. Christensen 1997; Christensen 2003).

V. CUSTOMER DEMAND

Customer demand also exerts pressure on company's business model. Changes in consumer patterns, revenue streams and fashion are few of the examples of change in customer demand.

VI. SOCIAL ENVIRONMENT

Stakeholder theory (Friedman and Miles 2002) highlights how social mood can influence the business model of a firm. A firm has to be very careful to analyze how mobilizing of public opinion can work for or against the firm. Besides social pressures, changes in social environment, ethics and technology adoption approach is crucial to interpret.

VII. LEGAL ENVIRONMENT

Studying the legal environment and changes in regulatory regime are necessary to adapt business models. There have been examples in the past which show things as basic as anti-spamming laws may (hopefully) wipe-out business models because of sending out large trunks of unsolicited mails. It is necessary to have a good grasp over tax regime of a particular society as new taxes may make a company's value proposition too costly.

VIII. MAKING THE BUSINESS MODEL CHOICE

Linder and Cantrell (2000) propose categorizing business models focusing on two main dimensions, which are a model's core revenue generating activity and the activity's relative position on the value continuum. Various business model categories under this are:

1) Price Models
2) Convenience models
3) Commodity Plus Models
4) Experience Models
5) Channel Models
6) Intermediary Models

7) Trust Model

8) Innovation Model

Another well-known study for classification of business models is that conducted by Rappa (2001). According to him, a business model spells-out how a company makes money by specifying where it is positioned in the value chain. His classification scheme consists of nine generic forms of e-business models, which are

1. Brokerage
2. Advertising
3. Infomediary
4. Merchant
5. Manufacturer
6. Affiliate
7. Community
8. Subscription and Utility

Afuah and Tucci (2003), in contrast, explain that a business model should include answers to a number of environmental concerns:

1. What value you offer to your customers?
2. Which category of customers to provide the value to?
3. How to monetize and charge for the value?
4. What strategies to be undertaken?
5. How do you plan to provide the value?
6. How can the competitive advantage from providing the value be sustained?

IX.CONCLUSION

The analysis of academic research has shown that the business model concept and related influence of environment on the business models have a potential to be explored further. The ability to establish a transparent relationship between business and external environment, and relationship between various business elements seems to interest executives and consultants alike. Business models are necessary tools to understand fundamental questions of business. Choosing an effective business model is necessary to seize the business possibilities available for business practitioners. When defining business model generates a certain degree of confusion, many academic authors go deeper into defining specific environmental factors that govern what business models are composed of. It is very important to choose a business model in tandem with the environmental needs. The first step in selecting an effective business model is, viewing the business model as a tool understanding and defining the business logic of a firm.

The attempt to define business models should consist of business elements such as functions and attributes of a business model. Hence, our analysis concludes that the environment specific issues in business model frameworks are necessary for success.

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