

Module 1. Introduction to business modelling

Unit 1.1 Concepts and elements

Start-up creation is a global movement that has emerged and it continues developing everyday without intentions to stop. The development of technologies that are getting cheaper, the access to information and the connectivity degree among people have made it possible for start-ups creation to be more accessible, with low resources required and easily achievable.

Business modelling is a tool that (without necessarily replacing the business plan, as we will see later on) has different versions that adapt to each entrepreneur's needs. The lean work philosophy, the agile methodologies and the design thinking evolve constantly and entrepreneurs multiply, with global and local failures and successes.

This simplification allows us to put ideas in our mind into practice and express them in a model, to facilitate our model explanation to a partner, a customer, an investor, a friend or a relative. The business model tool includes the critical parts in a start-up and it allows us to understand the logic in the area in which it is immersed, the involved participants and the requirements to develop it. Besides, it is a tool that helps entrepreneurs to generate new ideas and opportunities for their business, so they discover possible connections with other market participants and they help them to innovate following a logical order.

1.1.1 Business model versus business plan

Many times the business plan and the business model concepts are mixed up, but their scope, as well as their goals, are completely different to innovate following a logical order.

- The business plan consists of a written report, which is more formal, with technical details about the project, implementation ways and processes. It also includes a

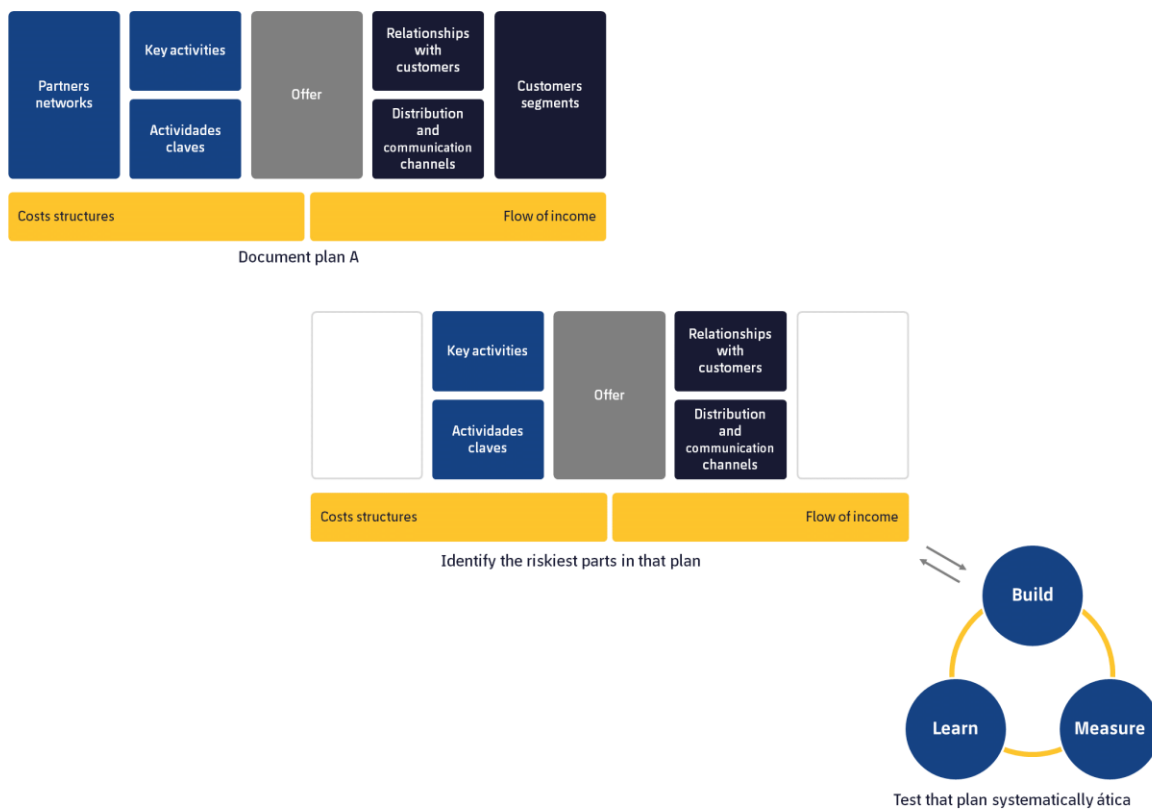


business feasibility analysis at the economic-financial level. It has a linear approach where one step follows another.

- The business model allows for expressing an idea or a concept in a simpler way. It facilitates the analysis of how feasible a concrete opportunity is and to explore its options and variations. It allows for certain creativity in business. It has a holistic approach that allows for assimilating all variables and their impact at the same time. It is a less linear and more flexible model.

At the beginning of start-ups, entrepreneurs only have a series of hypotheses to prove. That is why they resort to a business model, which precisely consists in building hypotheses to validate. It is known from the first moment that work will not be to execute a plan perfectly but to learn it and build it, taking the plan as a base.

Figure 1: Business modelling process



Source: Adapted from Osterwalder and Pigneur, 2011.

Just as the figure shows, the idea is to work firstly on an initial business model draft, where the initial idea proposition with all its hypotheses is expressed. Then, we should identify the riskiest parts in the mentioned model, the ones we believe are less certain

and if we are not aware of them they will become highly risky for the project success. Finally, from there, we will start validation through the build-measure-learn loop.

In general, the riskiest parts are the value proposition, the customers' segment and the problem-solution fit, because they are the base for the whole model.

Something very important to highlight is that this work's focus is on the systematic test of the plan, through hypotheses, tests and measures, learning and repeated iterations (small changes) or pivots (big changes) and not on plan execution. When the company starts to be set up, the project is still on the discovery and research stage. And it will be like that until finding a repeatable and scalable business model.

1.1.2 Business modelling Canvas

What is a business model? How is it useful? How is it used?

“A business model describes the bases on which a company creates, delivers and captures value” (Osterwalder and Pigneur, 2011, p. 14).

Besides, we could define it as a simplification of the idea we have in our minds which will enable us to express it and to define the following:

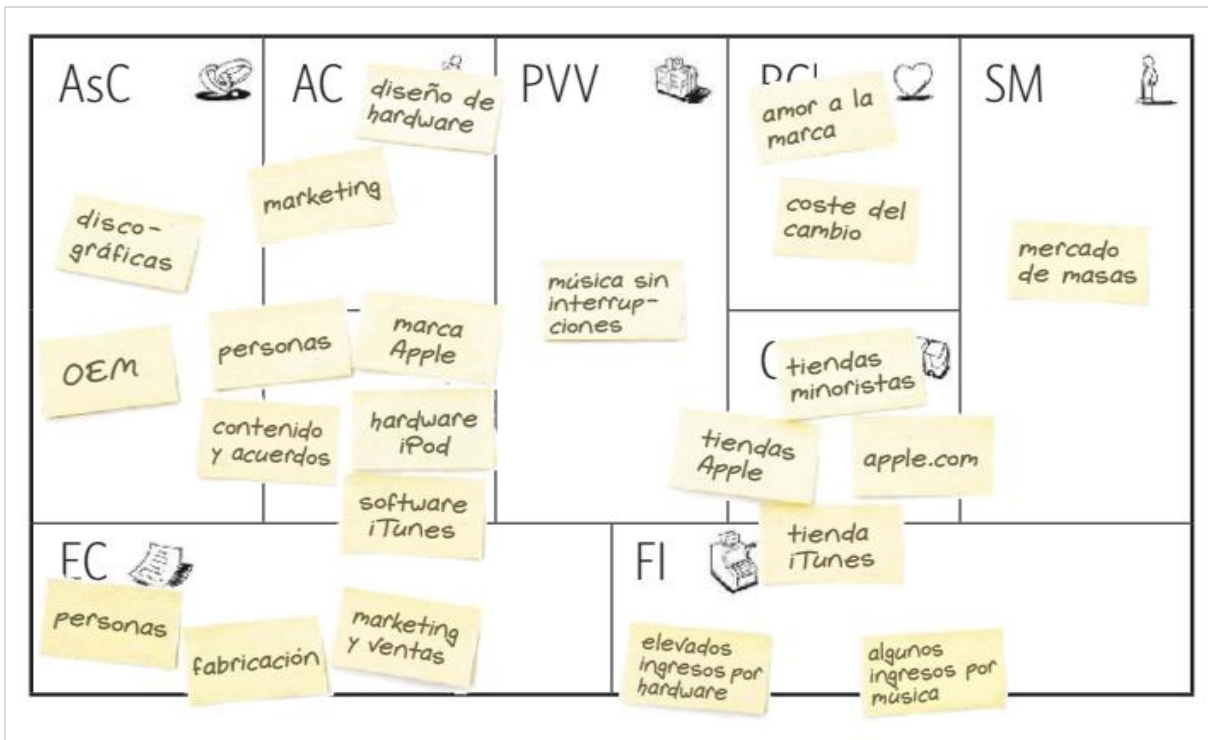
- 1)** How the business will create value for somebody.
- 2)** How that value will be delivered.
- 3)** How that value is captured and transformed in profitability, in capital or some other benefit for having provided that value.

The model is focused on these three points.

It is also a visual and a teamwork tool that is used a lot nowadays in companies to work on open innovation.



Figure 2: Canvas example



AsC Discográficas OEM	KEY PARTNERSHIPS Record companies OEM
AC Diseño de hardware Marketing	KEY ACTIVITIES Hardware design Marketing
RC Personas Marca Apple Contenidos y acuerdos Hardware iPod Software iTunes	KEY RESOURCES People Apple Brand Content and agreements iPod hardware iTunes software
PVV Música sin interrupciones	VALUE PROPOSITION Music without interruptions
RCL Amor a la marca Coste del cambio	RELATIONSHIP WITH CUSTOMERS Love for the brand Change cost
CD Tiendas minoristas Tiendas Apple Apple.com Tienda iTunes	DISTRIBUTION CHANNELS Retail stores Apple stores Apple.com iTunes store



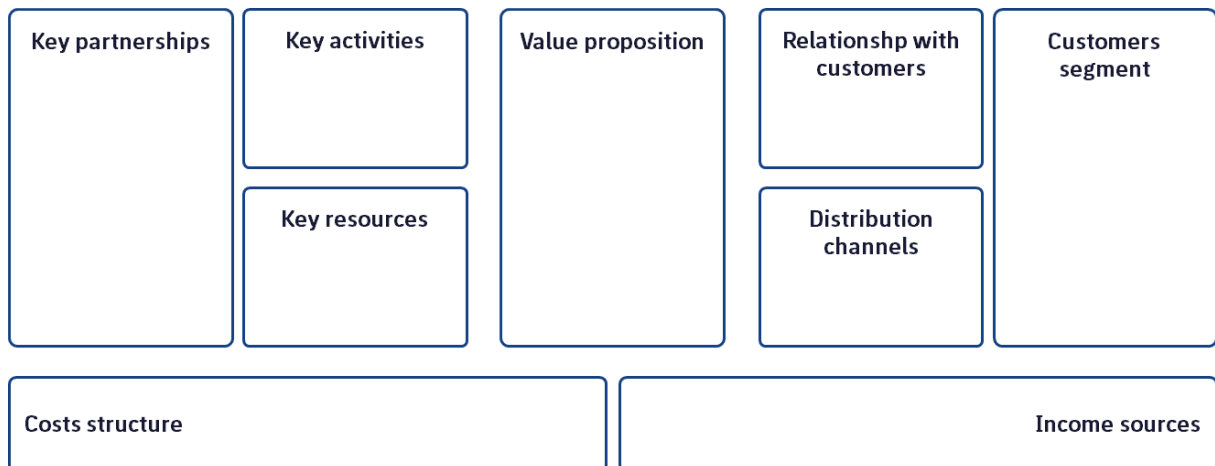
SM Mercado de masas	MARKET SEGMENT Mass market
EC Personas Fabricación Marketing y ventas	COSTS STRUCTURE People Manufacturing Marketing and sales
FI Elevados ingresos por hardware Algunos ingresos por música	INCOME SOURCES High income by hardware Some income by music

Source: Osterwalder and Pigneur, 2011, p. 46.

This tool states—mainly when working with new ideas—that issues added are hypotheses, since you can believe that the value proposition or the customers' segment is clear, but that can change once validations or observations are made. It is then when you start having different versions about the different tests you perform and to how the model evolves.

Business modelling is dynamic and flexible. Its focus is on customers and people and it integrates the creative to the logics, different from a business plan, which is a written document that includes the characteristics of a project at a specific moment.

Figure 3: Canvas



Source: Adapted from Osterwalder and Pigneur, 2011.

As a conclusion, the business model canvas allows us to do the following:

- To create an initial business model and to iterate until one that works.



- To have everyone speaking the same language. It is a communication and a teamwork tool.
- It helps not to leave variables outside and to take into account all key aspects for a business.
- To build practical solutions for clients and to build customer loyalty in the process.

The Nespresso case is one that can be used to illustrate and understand what is a business model canvas. Nespresso added one more variable to drinking coffee: the capsule, with a fully-designed machine, coffee from anywhere in the world, in a few minutes. That model revolutionized the coffee machines industry.

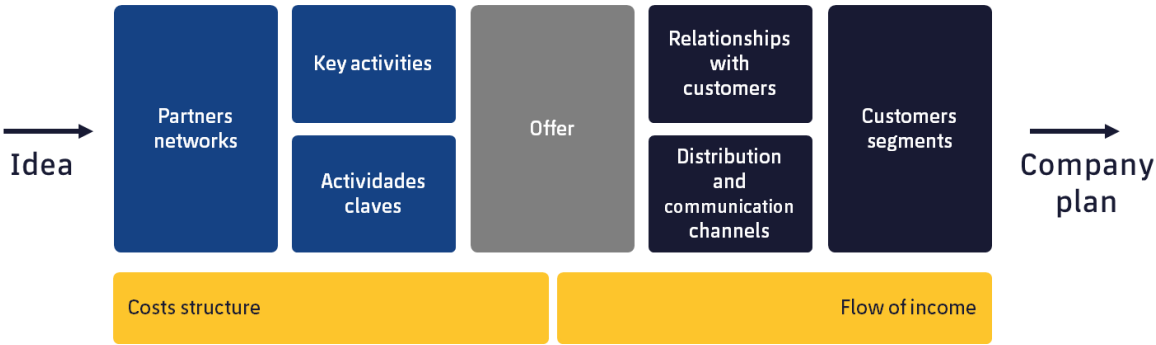
Another case is the one of Apple, which not only transformed the computers and software industry, but also the music, the mobile phones and connectivity businesses. All this was achieved by the offering of unique and irreplaceable products with end-to-end closed systems and with integrated hardware and software; they have changed the consumption model for music available to everyone through the Internet and they have democratized access to information and connectivity through their revolutionary iPhone and the products that have followed it.

If we use the canvas to put these examples' business model in order, we can clearly see how the tool allows us to organize and find the distinguishing and disruptive variables in these businesses.

The business modelling canvas tool is useful not only for commercial start-ups but it is also used nowadays in many places, by entrepreneurs, governments, different size companies and consulting firms that work in modelling existing businesses, to capture all variables in a certain business.



Figure 4: From the idea to the plan process



Source: Own creation, 2020.

Once the product-market fit on the company escalating plans was achieved, we can start using tools that are more related to the business plan rather than with the business model, since a market need was identified, the best communication and distribution channels, the product price and others could be validated. So, it is time to make the company grow with investment and with clear growth plans. That is why Canvas is used for expressing and moulding an idea until finding the best version of the product or service for the market. There are companies that, although having thousands of employees and customers, they keep using the business model to think about new ideas or projects, to explore opportunities and think about their business in the future, so they are not out of the market and, that way, they are still innovative.

Below, we will briefly develop the nine elements that are part of the model:

Table 1: Model elements of each block

ELEMENTS	BLOCK
1. Value proposition	1 VALUE OFFER
2. Customers' segment	2 CONSUMER
3. Distribution and communication channels	

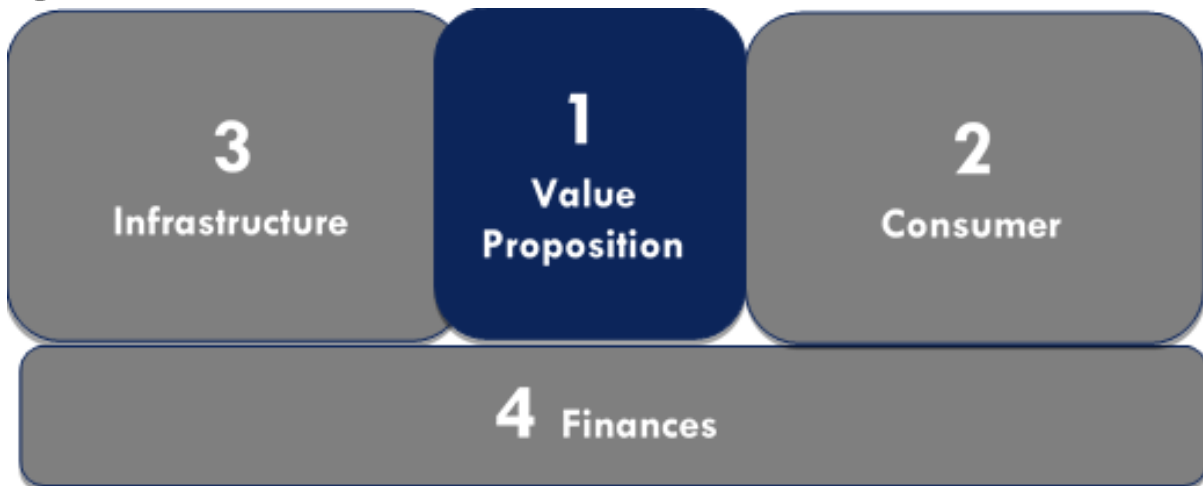


4. Relationship with customers	
5. Key resources:	3 INFRASTRUCTURE
6. Key activities	
7. Key partnerships	
8. Costs structure	4 FINANCES
9. Income sources	

Source: Own creation, 2020.

A simple way of reading the model is by the following figure.

Figure 5: Section 1



Source: Own creation, 2020.

In the first place, we can find the value proposition, then we analyze everything related to the consumer (both aspects, the value proposition [VP] and the customers segment [CS] are the model base). Then, we go to infrastructure and the finances block at the end.

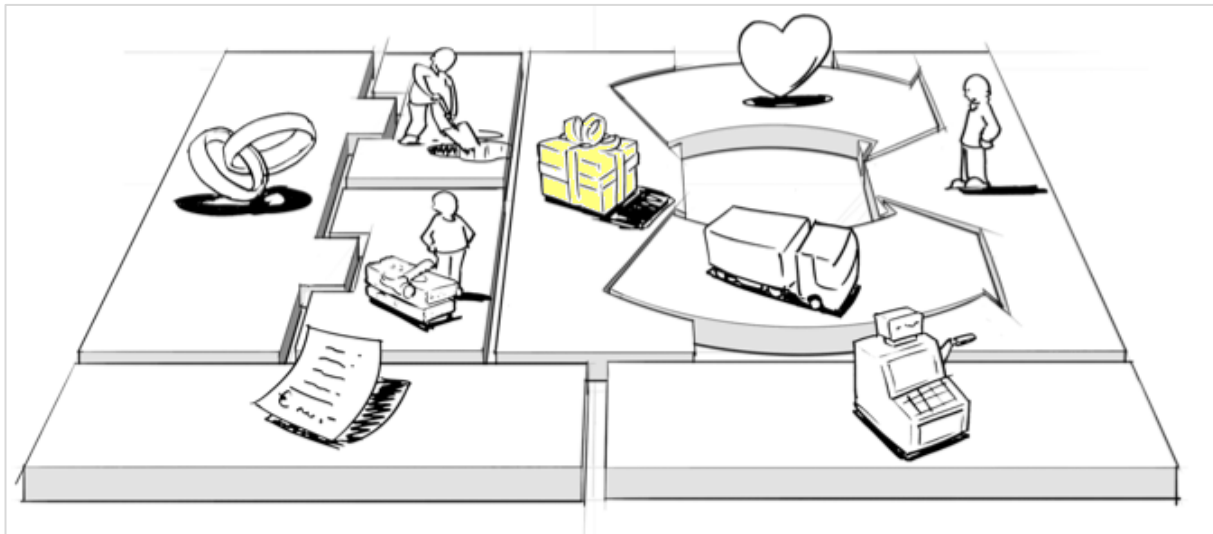
1. Value proposition

The model is located at the centre in the value proposition since it is the most important and it is the base for developing the rest of the elements.

The value proposition is a group of products or services that meet the conditions of a certain market segment. In this sense, the value proposition constitutes a series of advantages that a company offers to customers. (Osterwalder and Pigneur, 2011, p. 22).



Figure 6: Value proposition



Source: Adapted from Osterwalder and Pigneur, 2011.

In order to develop the value proposition, we should ask ourselves the following:

What value are we offering to customers?

Which problem are we helping to solve?

Which customer's need are we satisfying?

What type of product and service's package are we offering to each customers segment?

Remember that, when having different segments, you will have to work on different value propositions and, therefore, with other price strategies. That is, each value proposition is directed to a customers segment.

Let's see an example.

Appetize is a technological company with an application in different areas, one of them, the sports area. It is an online delivery platform that enables people to order from anywhere in the stadium; it accelerates transactions and it compensates fans' participation. It is a way to boost yields and to improve customers' experience.

Appetize characteristics:

- Technological renewal.
- Solutions developed following each area's needs.
- Improvement in management tools.
- Reduction in maintenance and support costs.

Following Osterwalder and Pigneur (2011) and, as it was dealt with in reading 1 in the Value Proposition course, a value proposition should create value for a certain market segment with a specific mixture of elements that are adapted to this segment's needs.

These characteristics could be quantitative—like price, service speed, among others—or qualitative—like design or customer experience, for example (Mejía Trejo, 2017).

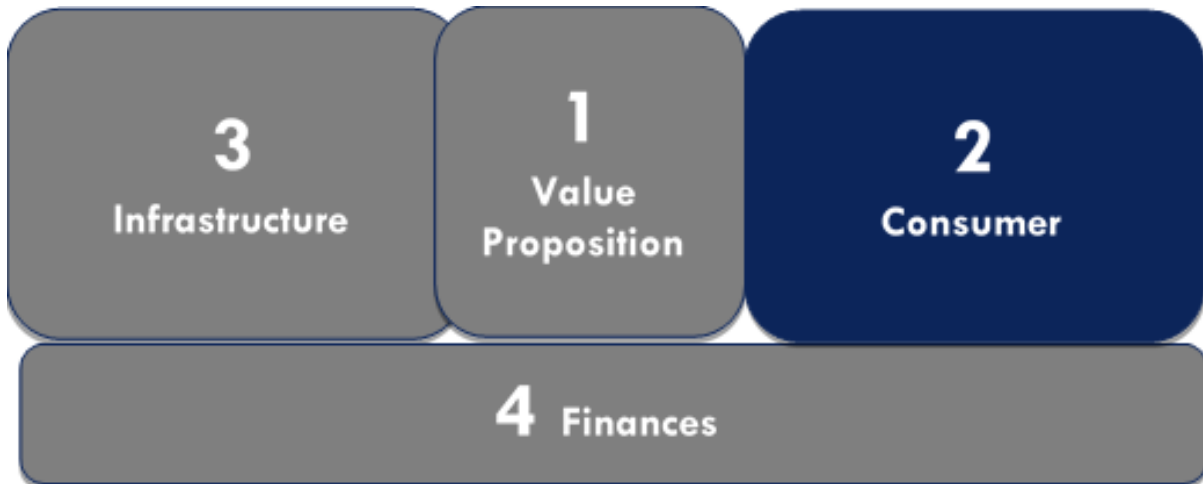
According to Mejía Trejo (2017), some examples you can work with when generating value for customers are the following:

- **Novelty:** in general, this type of value is related to technology.
- **Performance improvement:** a quicker product, a product that is more powerful, more precise.
- **Personalization:** products and services' adaptation to customers or the market segment's specific needs creates value.
- **Design:** This is an important factor, although it is difficult to measure. In the fashion industry and consumer electronics, this could be more evident, but the design can constitute an essential part of the value proposition.
- **Brand or status:** some customers can find value on the simple fact of using or displaying a specific brand that might be associated with social status or to a certain position.
- **Price:** to offer a similar value at a lower price to satisfy the needs of market segments that are governed by it.
- **Costs reduction:** another way of creating value is by helping customers to reduce costs, as in the case of Salesforce.com, that sells an application for managing relationships with customers called CRM (Customer Relationship Management), stored on the cloud. This way, customers do not have to invest the money and time involved in buying, installing and managing the CRM software by themselves.
- **Risks reduction:** customers need to reduce the risk that products or services' acquisition means.



- **Accessibility:** investment funds are an example of value creation thanks to greater accessibility since it is a financial product that allows investors with modest capital to create diversified portfolio investments.
- **Comfort or utility:** iPod and iTunes from Apple offered customers the comfort of searching for, buying, downloading and listening to digital music. Now then, Apple dominates this market area (Mejía Trejo, 2017).

Figure 7: Section 2



Source: Own creation, 2020.

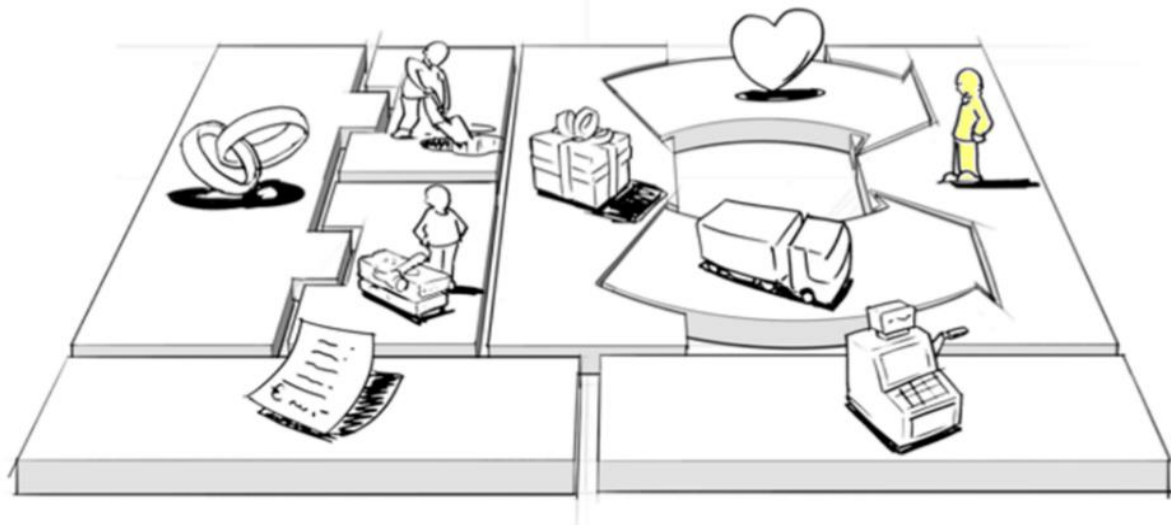
Once the value proposition has been defined, you should move to the second block related to the consumer. In this block we will find three elements:

- 1) Customers' segment
- 2) Communication and distribution channels
- 3) Relationship with customers

2. Customers' segment

It refers to groups of people or entities to whom you pretend to serve or assist with the value proposition. Your selection must be reflected on a solid understanding of their needs.

Figure 8: Customers' segment



Source: Adapted from Osterwalder and Pigneur, 2011.

In order to know which is our customers segment, we should ask ourselves the following questions:

*To whom are we creating value?
Who are our most important customers?
Which are their most distinctive characteristics?*

Let's see some examples for market segments that Osterwalder and Pigneur (2011) present which are exposed to the following chart.



Table 2: Market segments typology

<p>Mass market</p>	<p>Business models that are focused on the general public do not distinguish market segments. Value propositions, distribution channels and relationships with customers are directed toward a group of customers who have similar needs and problems. It is a habitual business model in the great consumer electronics area (Cervato, 2015).</p>
<p>Market niche</p>	<p>These business models are directed toward specific and specialized segments. Value propositions, distribution channels and relationships with customers are adapted to market division-specific requirements. It is the case of many car accessories manufacturers that depend, to a great extent, on main car manufacturers (Cervato, 2015).</p>
<p>Segmented market</p>	<p>These models distinguish and assist various market segments with slightly different needs, but with the same product or service, or with small variants (Cervato, 2015).</p>
<p>Diversified market</p>	<p>They are models that assist two or more market segments that are not related and present very different needs and problems (Cervato, 2015). It is the case for Amazon, which in 2006 decided to diversify business with retail sales by offering computing services on the cloud (cloud computing). Product or service characteristics vary according to the market.</p>
<p>Multilateral platforms (or multilateral markets)</p>	<p>It refers to models that are directed to two or more market segments that depend on each other. A credit card company, for example, needs a great customer base and a great shops base that would accept their cards (Cervato, 2015). It is also the case of e-commerce, where you need sellers and buyers and the former would not exist if there is not enough amount of the latter.</p>

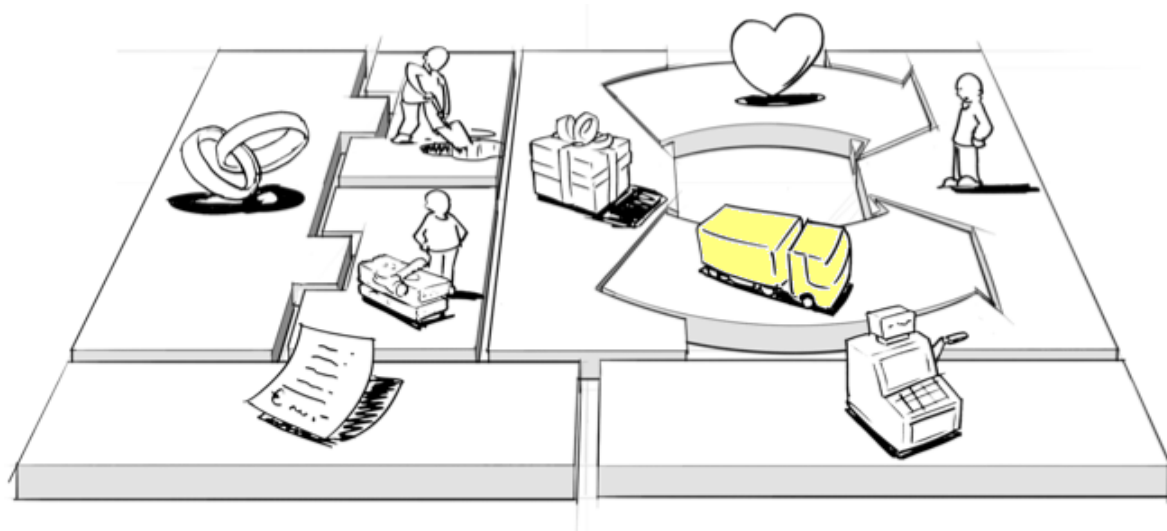
Source: Own creation, 2020.



3. Distribution and communication channels

It is the most intelligent, effective and recurrent way you have to reach your customers or customers segments.

Figure 9: Communication and distribution channels



Source: Adapted from Osterwalder and Pigneur, 2011.

Some questions to work on this element:

*How do I distribute my value proposition?
How do I reach the segment now?
Which are the functions that work best?*

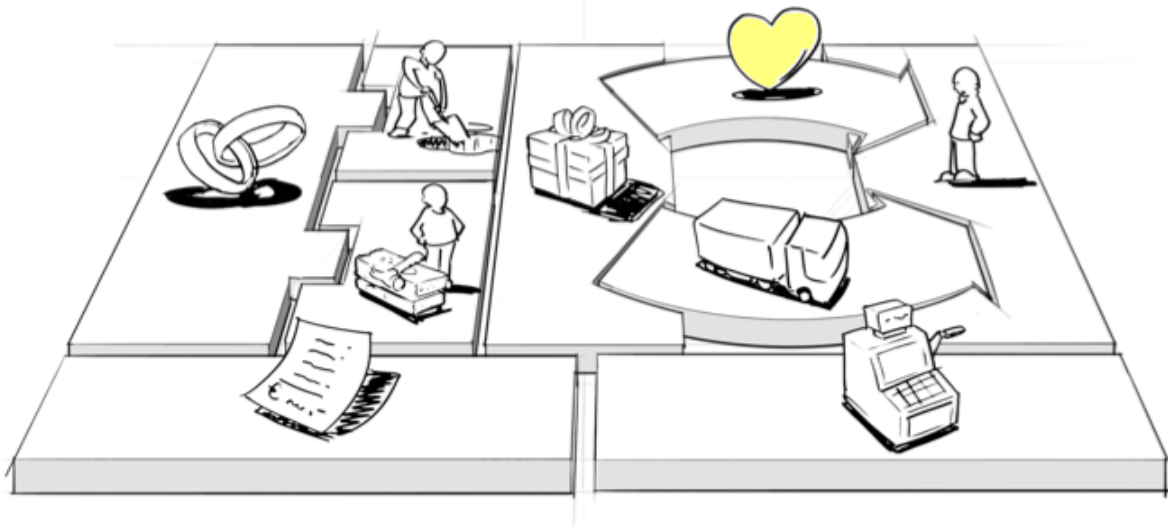
Channels could be different if you target different segments.

Later, we will develop this element in more detail.

4. Relationship with customers

It has to do with the connection modality and intensity between your start-up and customers.

Figure 10: Relationship with customers



Source: Adapted from Osterwalder and Pigneur, 2011.

Some questions you should ask yourself:

- What kind of relationship are our customers expecting?*
- What kind of relationship have we established?*
- How do they relate with the rest of the elements in the business model (resources, activities, partnerships)?*
- How do customers expect we relate with them?*

The type of relationship the business model demands from your start-up has a great effect on the global experience your customer will have.

According to Osterwalder and Pigneur (2011), there are various connection categories with consumers that can co-exist with relationships a company has with a certain market segment. These can be observed in the following chart:



Table 3: Types of relationships with customers

<p>Personal assistance</p>	<p>This relationship is based on human interaction. Customers can communicate with a real customer service representative so that he/she can help them in the sales process or later. This type of relationship is established, for example, on points of sale, on-call centres, by e-mail, etc. (Cervato, 2015). It can be virtual or in-person, but there should be humans on the other side.</p>
<p>Exclusive personal assistance</p>	<p>In this type of relationship, a customer service representative is specifically devoted to a particular customer. It happens in the banking sector, for example, where executives have their customer portfolios for giving attention or account managers who are in contact with important clients (Cervato, 2015).</p>
<p>Self-service</p>	<p>Here, the company has no direct relationship with customers, but it only provides them with all the necessary means so they can serve themselves (Cervato, 2015).</p>
<p>Automatic services</p>	<p>This type of relationship combines a more sophisticated self-service way with automatic processes. Automatic services recognize different customers and their characteristics, to provide them with information that is related to their orders or transactions. Best automatic services can simulate a personal relationship (Cervato, 2015).</p>
<p>Communities</p>	<p>It is more frequent that companies use the users' communities to go deeply in the relationships with their customers, or potential customers, and, consequently, to facilitate contact among community members. Many companies have online communities, which allow users to exchange knowledge and to solve other members' problems. Besides, communities help companies to better get to know their customers (Cervato, 2015).</p>
<p>Collective creation</p>	<p>Many companies go beyond traditional relationships and resort to customers' collaboration to create value. Some companies foster customers to collaborate on the design of new and innovative products (Cervato, 2015).</p>

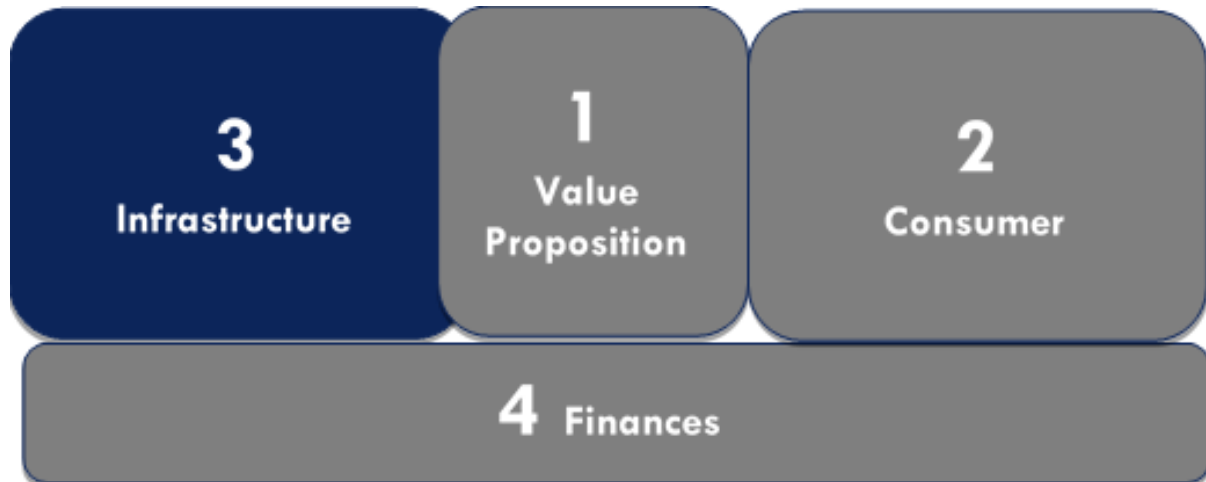
Source: Own creation, 2020.

This block in particular could be a key differentiator in the business model. Some brands choose to be excellent in their customer service and relationship no matter the cost since they get benefits by building customer loyalty. On the other hand, some



companies are not too concerned about their relationship with customers. However, the current tendency is to have excellent customer service and adapt to the type of relationship the customer expects, which is going to vary depending on the segment.

Figure 11: Section 3



Source: Own creation, 2020.

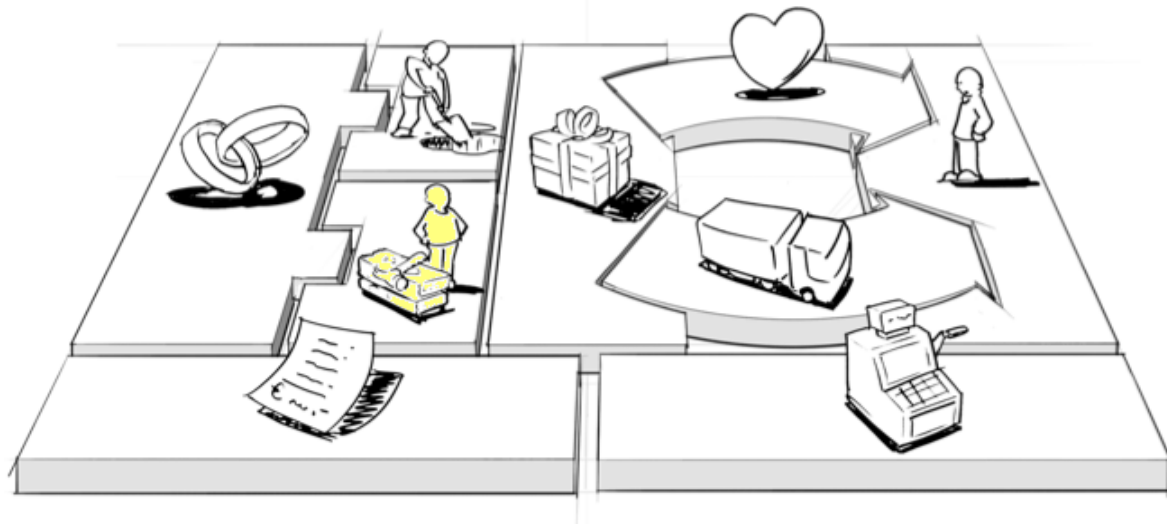
After working on these two blocks, we should go to the third one, which is the one related to infrastructure. In this block, we find three elements:

- 1) Key resources
- 2) Key activities
- 3) Key partnerships

5. Key resources

They are the most important assets you need to make your business model work, for example, facilities, people, licenses, utilities, machinery.

Figure 12: Key resources



Source: Adapted from Osterwalder and Pigneur, 2011.

Here, it is important to ask ourselves:

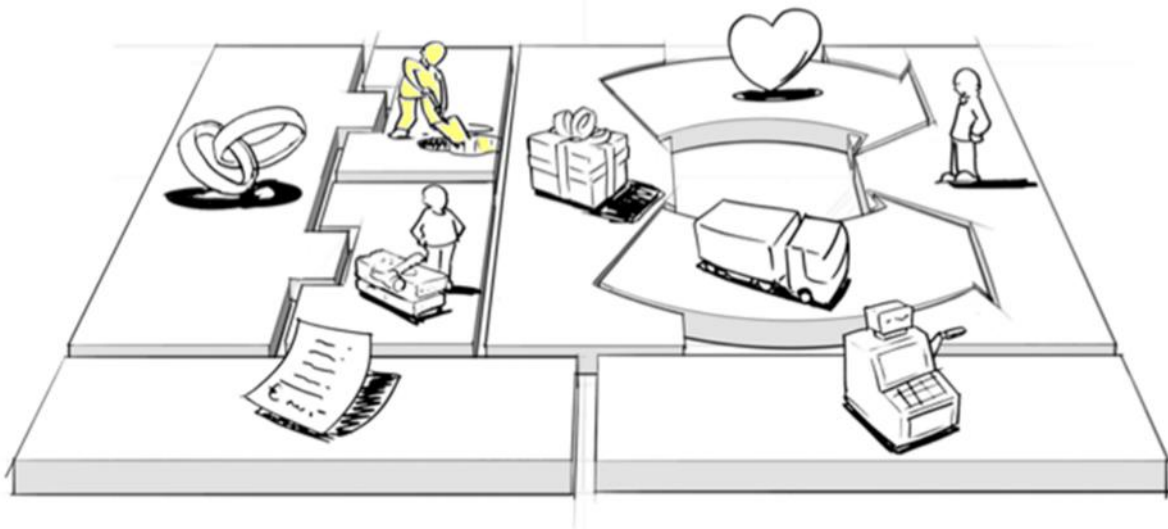
*Which key resources are key for our value proposition?
Which require communication and distribution channels?
Which is the relationship with customers?*

6. Key activities

They are the things that you have to do for your value proposition to exist; you should think about which are the most important activities in which you should focus, like production, sales, logistics, among others.

They can also be defined as the critical actions to follow for success and, as key resources, they are necessary for creating and offering your value proposition, for reaching markets, for establishing relations with your customers and generating income.

Figure 13: Key activities



Source: Adapted from Osterwalder and Pigneur, 2011.

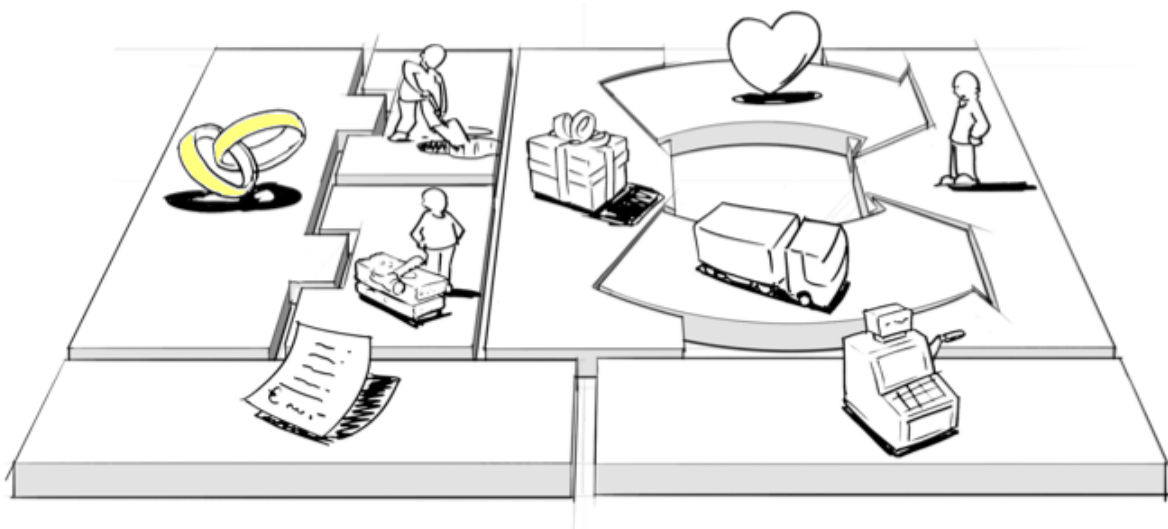
These are the questions that need to be asked:

Which key activities are required by our value proposition, communication and distribution channels and our relationship with customers?

7. Key partnerships

They refer to potential impact partnerships that you can create in the way to improve your value proposition, for example, with suppliers.

Figure 14: Key partnerships

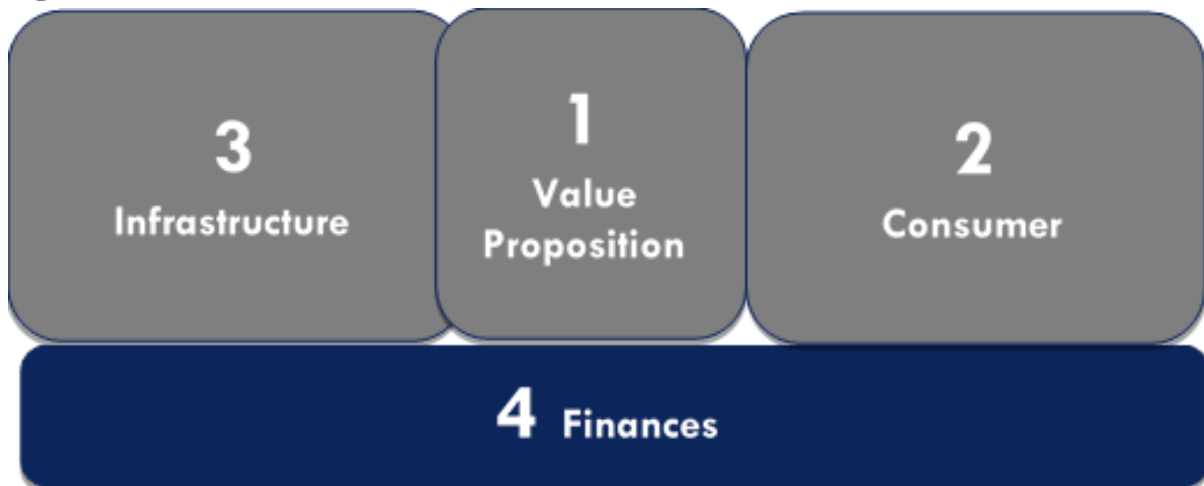


Source: Adapted from Osterwalder and Pigneur, 2011.

As in previous cases, there are questions to ask:

*Who are our key allies or suppliers?
Which strategic resources are we acquiring?
Which key activities do our allies develop?*

Figure 15: Section 4



Source: Own creation, 2020.

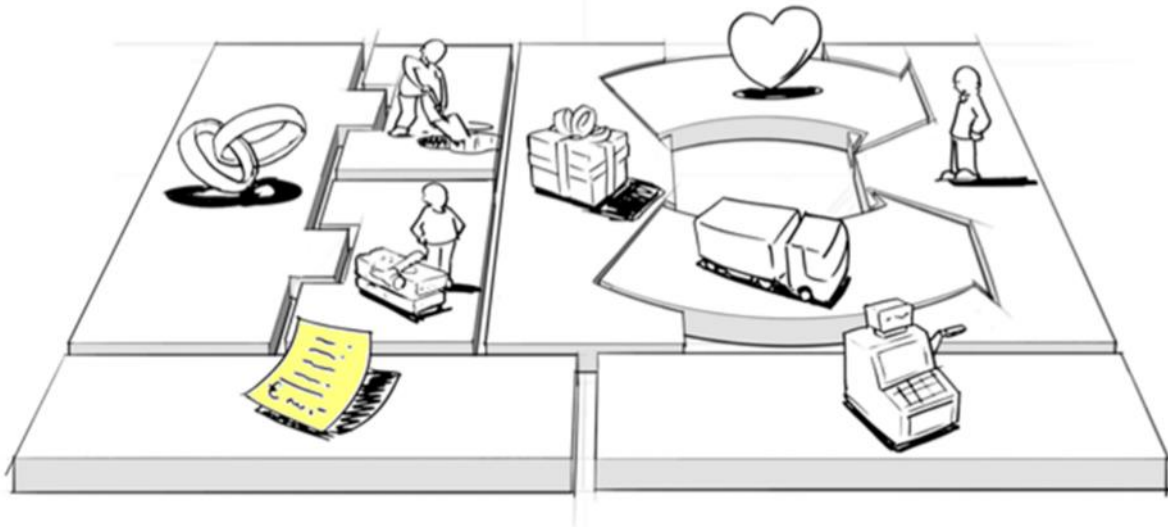
Finally, you should work on finances block. In this block, you will find two elements:

- 1) Costs structure
- 2) Sources of income or benefits

1. Costs structure

In this element, you should identify the most important costs. It is about expenses that must be paid to make all the elements in your model a reality.

Figure 16: Costs structure



Source: Adapted from Osterwalder and Pigneur, 2011.

*Which are the most important costs?
Which are the most expensive key resources?
Which are the most expensive key activities?*

Costs should be minimized in all business models. Nevertheless, it can be useful to distinguish between two types of costs structure that start-ups can present: the cost model and value business model (many business models are between these two extremes).

- Cost model: its goal is to cut expenses wherever it is possible; therefore, the idea is to create and keep a costs structure which is as reduced as possible, with a low price proposition value by using automatic systems as much as possible and with a high degree of externalization.
- Value business model: some companies prefer to focus on value creation. Premium value propositions and personalized services are distinctive features in these models. (Cervato, 2015).

To complete this element, we will briefly define fixed and variable costs, since they are dealt with in detail on Module 3 reading on this course.

Table 4: Fixed and variable costs

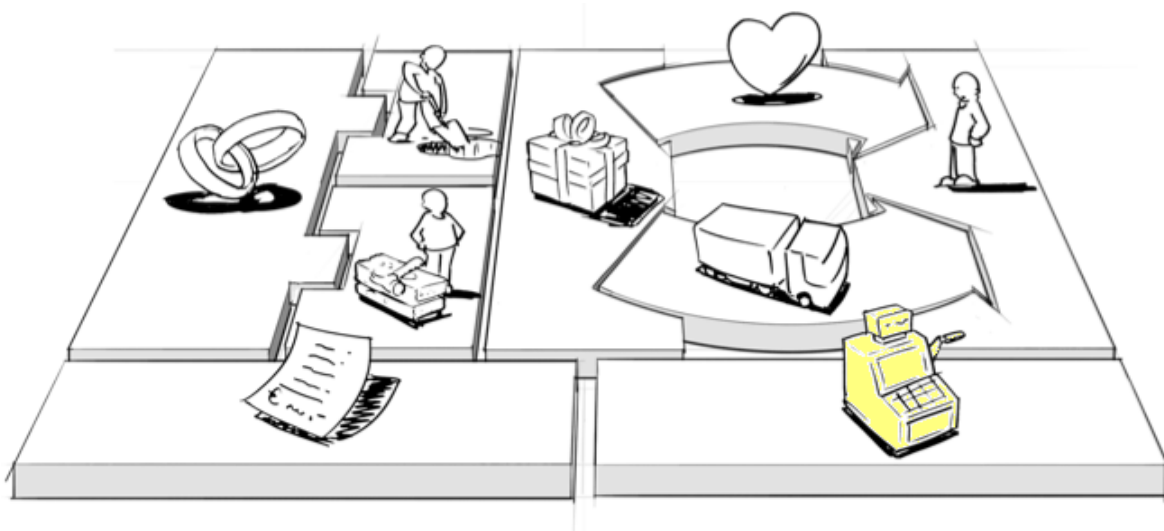
Fixed costs	They do not vary about the volume of produced goods or services. For example salaries, rents and manufacturing facilities (Cervato, 2015).
Variable costs	They vary in direct proportion with the volume of produced goods or services. For example the raw material or production or production inputs (Cervato, 2015).

Source: Own creation, 2020.

2. Sources of income or benefits

It is the group of ways of generating benefits or cash flow in your startup, from the prices that you have for each of the value delivery instances.

Figure 17: Income sources:



Source: Adapted from Osterwalder and Pigneur, 2011.

*Where are income and benefits generated?
 How much are our customers willing to pay?
 What do they pay for currently?
 How are they paying nowadays?
 How would they like to pay?*

Income sources are generated when your customers acquire your value proposition.

According to Osterwalder and Pigneur (2011), if customers are at the heart of your business model, income sources are your arteries. That is why a central question must be asked:

How much is our market segment willing to pay?

If you answer this question correctly, you will be able to create one or several income sources in each one of your market segments (Cervato, 2015).

Following Osterwalder and Pigneur's proposal (2011), a business model can constitute two different types of income sources.

- 1)** An income by transactions derived from particular customer payments.
- 2)** A recurring income derived from regular payments done in exchange for providing customers with a value proposition or an after-sales customer service.



Table 5: Ways of generating income sources

Sale of assets	It is the sales of property rights on a physical product. Amazon.com, for example, sells books, music, consumer electronic products and others on the Internet (Cervato, 2015).
Pay per use	This income source is based on the usage of certain service. The more a service is used, the more the customer pays. In hotels, for example, customers pay the number of nights they spend in their facilities (Cervato, 2015).
Subscription payment	It implies access to a particular service. For example, fitness centres that sell their customers monthly or annual subscriptions in exchange for access to their sports facilities (Cervato, 2015).
Loan, rent or leasing	This income source is constituted by the concession of an exclusive right in return for a fee to use a certain asset for an established period of time (Cervato, 2015).
License concession	It corresponds to the concession of permission to use intellectual property in return for a license payment. The property generates income for property rights holders who do not have to manufacture products or commercialize services. It is habitual on the technological industry, where patent owners give other companies the right to use patented technology in exchange for a license payment (Cervato, 2015).

Source: Own creation, 2020.

Later, we will see business models patterns that will allow us to discover more different ways of generating income.



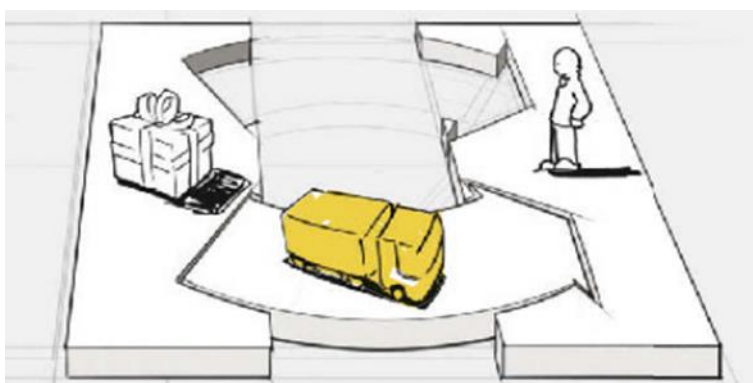
Unit 1.2 Distribution and communication channels

As we saw in the previous unit, when we talk about distribution and communication channels, we refer to the intelligent, effective and recurring way you have to reach your customers or customers segments.

Communication, distribution and sales channels establish contact between the company and its customers. They are contact points with the customer that play an essential role in their experience. Channels have, among others, the following functions:

- Information: To make the company's products and services are known to customers.
- Assessment: To help customers to assess a company's value proposition.
- Purchase: To allow customers to buy specific products and services.
- Delivery: To provide customers with a value proposition.
- After-sales: To offer customers an after-sales service. (Osterwalder and Pigneur, 2011, p. 26).

Figure 18: Distribution and communication channels



Source: Osterwalder and Pigneur, 2011, p. 26.

You should think intelligently and effectively to be permanently communicating and capturing more customers that are distributing your product. You should analyze and define which is the most efficient channel for each public.

Some channels examples are the following:

- Account executive
- Banner on the web page
- Events
- Training
- Word of mouth
- Social networks

Something key at the moment of commercializing your value proposition is to choose the best channels combination to reach your customers properly.

According to Osterwalder and Pigneur (2011), the following are the types of channels:

1) Own channels

They could be direct (internal commercial team or a web site) or indirect (own store or store managed by the company).

“On own channels, especially in direct ones, benefits margins are bigger, but the costs of starting it up and managing it could be high” (Ostewalder and Pigneur, 2017, p. 27).

2) Commercial partners channels

They are indirect and they include options like wholesale distribution, retail sales or partners’ web sites. These channels report smaller benefits margins, but they allow for increasing the scope of activity and taking advantage of strong points in each of them.

3) Both

It is important you take into account that the key is in finding a fair balance among the various types of channels to integrate them in a way that you could offer the best experience to your customers, obtaining the highest possible income (Osterwalder and Pigneur, 2011)

Some points to consider on the analysis and definition of distribution and communication channels :



- How is the contact with customers established nowadays?
- Which are the channels preferred by different customers segments?
- How do the different channels relate to each other? Which of them get better results? Which are more profitable?



References

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