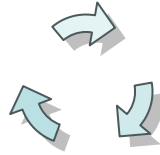


Does your Business Model Fit the New Normal?



Ask 7 out of 10 business owners to describe their business model and they will give you a half hearted 30 second commercial followed by a detailed discussion of how they provide a quality product or service at a fair price. Very few business owners invest the time necessary to fully engage themselves in understanding their true business model. Fewer yet take the time to research their options and validate their assumptions with data. Perhaps this explains why 95% of small businesses fail within the 1st 5 years. Certainly I don't want to sound pessimistic, but with statistics like this, it only makes sense to invest some time in figuring out how you are going to make money now and in the future. Ultimately that is what a good business strategy explains. From an investor's standpoint, do you have a viable product or service for which there is visible demand, and will the investor be able to recoup their investment and then some. From the entrepreneur's standpoint, how will I make money and continue to do so in changing technological and economic conditions? Buried within 10-50 page business plans, a story must unfold that clearly and concisely describes how the business will capitalize on a competitive advantage and ultimately make money. However, the business platform (competitive field) has changed significantly during the last decade, and more so during the last 3 years that a different approach is necessary to effectively compete. How can companies continue offering the same products and services to markets with collapsing demand using futile marketing efforts? At what point should a company pull the plug on what its doing and move in another direction? This article is intended to demonstrate not only the importance of a well defined business model, but the absolute necessity in understanding and being able to communicate it at a moment's notice.

Truth be told, a business model is simply a clear discussion of how a company makes money. Of course, if it were this simple more people would put the effort into thinking about it or discussing it in their organization. Discussing your business model is a clear step in the right direction of successful business navigation. Quite often business leaders are unclear where to begin. What are the key components that make up a solid business model? Harder yet, how should they approach communicating the model with their management team and staff. First, the discussion must address revenue streams. Revenue streams can be a touchy subject as many ***business experts*** will argue that a new business should only focus on 1 product or service during their infancy stages. The idea of specialization is intended to foster higher

productivity and better quality output. Furthermore, specialization allows a new and inexperienced company to better manage their resources. However, the other side of the coin says that businesses should put as many ores in the water as possible. As a matter of fact this discussion can often be the first high level disagreement among new business partners. This point of reference leads to the discussion of opportunity cost. Given that each and every day companies must choose where to spend their often very limited resources, the topic of opportunity cost has great merit when discussing business models. If we take what's behind door A we may be giving up what's behind B and C. In order to make an educated guess the business owner is left looking for proof. What proof can we generate to give us confidence that our business model has value? One word, demand. Where there is demand there is opportunity, plain and simple. The art and science of running a business requires developing profitable business models that are flexible and sustainable. So once we are able to identify a consistent string of demand for a particular segment, it is our job as business owners, managers, and leaders to seize the day. We have to create the "secret sauce" that clearly communicates our advantage to consumers. Of all of the people in the world that offer your type of product, service, close substitute, or even generic, why should they get it from you? Once your secret sauce is identified, the focus shifts to maintaining your competitive run for as long as consumer demand will allow. A well crafted business model addresses these areas and seeks to derive profit opportunities from an identified need.

There are old business models, new business models, and even newer models being created each day. Let's start by taking a look at the subscription based model. The subscription based model focuses on charging a fee for a service or access to some type of specific information. The user benefits in many ways including being able to cancel at any time and avoid large upfront costs. The business selling the service benefits from establishing a cost that decreases with an increase in users. (Also known as economies of scale) The company also benefits from having some predictability in their revenues for the future. Even smarter companies benefit from continued engagement on behalf of the user, lowering the selling costs of their related products and services.

Business models don't need to be incredibly innovative or even brilliant. Successful models are driven by connecting market demand to other internal and external characteristics of the business environment. The franchise model has been around for decades, and is very popular among people that have significant capital, but lack specific expertise or creativity. Franchisees benefit from not having to reinvent the wheel. New business owners are able to capitalize on someone else's tedious efforts of trial and error. In addition, new business owners are able to gain from the marketing brand power of the franchisor. The franchisor's benefits are just the opposite. The franchisor gets to take their knowledge and package it into a bundle of annuities with an upfront payout. Moreover, they are able to quickly grow their brand with lower capital risks. Lastly, let's peek into the distribution/channel model. In this model, the process drives the business more than the actual products. Big Box retailers are masters at this model. Using a distinct focus on building excellent systems that ultimately drive down costs, retailers are able to offer more products that people want and at lower costs. Although, most small businesses are not in position to exploit this model, it is extremely important to be aware of it as you may have to address it in your own back yard someday.

What if you are not in a position to affect the business model of your entire company? The same premise holds true for individuals as well. Remembering that your business model is the way in which you make money, how might this apply to an individual banker or a lawyer? Stepping back and observing your activities over a specific period of time is a powerful exercise. Not only does it lead to better decision making, it offers you the ability to evaluate the validity of your work in a more meaningful way. Take a banker working for a local bank specializing in small business clients. This individual has numerous avenues for gaining new business. However, how many bankers stay locked in the past of sending out unsolicited letters after a chamber of commerce meeting or sending brochures to new businesses in the area. I have never seen such an egregious misuse of paper. I have not cracked the numbers but I would be willing to bet on a .00001% conversion rate. This method simply does not work. I would also argue that most unsolicited efforts are useless today for a couple of reasons. First, we live in a connected world in which we have so much access to information that we not only seek but expect to receive prior information about our purchases. Second, there is concealed message that is sent out when we receive unsolicited junk mail for personal services. Junk mail essentially says that the sender was not able to creatively, authentically, or meaningfully obtain the recipients attention so here is my card. Individual target marketing is just as important for small businesses as it is for fortune 500 companies. Regardless of the selected business model, there are certain factors that drastically impact success.

The recent financial crisis is a perfect example of how just about all businesses are susceptible to an adverse economic climate. Many businesses reacted differently to the recession. Some businesses reduced their workforce quickly while others waited and faced tough consequences. I firmly believe that the days of evaluating your strategic plan every 3-5 years are over. The environment changes too fast. Technology makes markets obsolete over night and if companies expect to stay competitive, it is vitally important to measure the effectiveness of their strategy on a more continual basis. Social demographics will play an even greater role in the future of business. Companies are spending Billions of dollars upgrading systems, hiring the appropriate workforce, and expanding their capabilities to collect and analyze data. Data will continue to drive better decisions by managers. The smartest businesses will use data to better understand where demand will be in the future. American business has had a long history of building great inventories and waiting for demand to swoop in to save the day. That era is over. By better understanding demand, companies will build specifically what people want and deliver it to them in a more efficient manner.

I often look to the financial markets to better understand the environment for general business. It often appears that the financial services industry gets tomorrow's toys, communication devices, and analysis landscapes before the general business industry starts to use them. One overriding theme that has become extremely prevalent in the last 3-4 years in the financial markets is speed. Speed will continue to be a dominating performance driver in the next 5 years for all businesses. Business opportunities will appear and disappear before many even figure out that they were there. Speed will not only be important for evaluating opportunities but also for executing business tactics and strategies. Companies will need to be more agile in the way they implement their plans. Many specific areas such as

governance and decision making authority will have to be reevaluated to take advantage of intellectual capital within the organization.

This thought brings us to the last point. I strongly believe that yesterdays focus on growth in numbers, such as headcount and service offerings will give way to a focus on operational efficiency. At many points during the article I referred to the growing usage of analytics by companies. This data is being used to improve the decision making process and to avoid wasted resources. The best companies will engrain this process into their strategic plan as well as their culture. People will not be patted on the back for saving the company money, it will be expected.

Essentially the theme of this discussion has centered on a distinct shift in business models that have become more agile, data driven and efficient in the future. Less truly is more, and the sooner that companies as well as individuals come to grip with the concept, the better positioned they will be in the future. Clearly a hybrid approach offers the greatest opportunity for businesses going forward. Companies that can clearly and efficiently identify revenue streams with the greatest probability for success, while aggressively mitigating their risks will be in the best position for growth. One thing is certain, whatever most companies were doing in the past, will come under fire at the very least in the future. Speed and efficiency will win.

About the Author



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