



Developing and Testing your Business Model

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Objectives

- At the end of class, you should be able to:
 - Define a business model and its purpose
 - Describe the segments of a Lean model canvas
 - Complete the LC based on case study information.
 - Complete the LC based on business idea

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Testing your Business Model

- Once you confirm that the idea is feasible, you can develop and test a business model.
- A business model is how your business plans to create and deliver value for the customer and then to capture value for the business.



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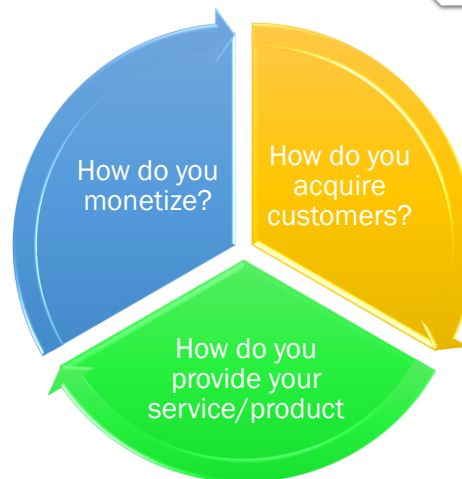
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Business Model

- A business model can be defined as the rationale of how an organization creates, delivers and captures value.
 - Business model = Create Value + Deliver Value + Capture Value*
- There is no one universally right business model, as it depends on your specific situation
- Your business model is how your business strategy plays out.



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Testing your Business Model



- Phase 1- **Outline your business model.**
- While there are several ways to outline your business model, the business model canvas/Lean Canvas allows the team members involved in the start-up to work from a common framework.
- A business model adds more detail to the evaluation of a new business begun during the feasibility analysis by graphically depicting the “moving parts” of the business and ensuring that they are all working together.
- The team documents all of the hypotheses about the business model that require further investigation and keeps track of changes in the model that result from testing the hypotheses.

Testing your Business Model



- Phase 2.
- The second phase in designing the business model is to test the problem that the team thinks the business solves through its core value proposition. This is best done with primary research data. That means the entrepreneurial team must “get out of the office” and test the model with real customers. By engaging potential customers early in the development of a new business and listening to what they have to say, the team has a much better chance of developing a business model that will attract customers. By engaging with real customers, the entrepreneurial team asks the following questions.
 - Do we really understand the customer problem the business model is trying to address?
 - Do these customers care enough about this problem to spend their hard-earned money on our product?
 - Do these customers care enough about our product to help us by telling others through word-of-mouth?
- *By answering these questions the entrepreneur assesses the actual need for the product and the intensity of that need.*

Testing your Business Model



- **The third phase** is to test the solution to the problem in the market. One technique to test the solution offered by the business model involves business prototyping, in which entrepreneurs test their business models on a small scale before committing significant resources to launch a business that might not work.
- Business prototyping recognizes that every business idea is a hypothesis that must be tested before an entrepreneur takes it to full scale. If the test supports the hypothesis and its accompanying assumptions, the entrepreneur takes the next step of building a business plan. If the prototype flops, the entrepreneur scraps the business idea with only minimal losses and turns to the next idea.
- *The Internet is a valuable business prototyping tool because it gives entrepreneurs easy and inexpensive access to real live potential customers.*

Testing your Business Model



- **The fourth phase** of designing a business model is to make changes and adjustments in the business, called pivots, based on what the entrepreneur learns from engaging the market about the problem and the solution that the new business intends to pursue. Some pivots may be subtle adjustments to the business model, while others may be fundamental changes to key parts of the model, including in the value proposition, markets served, or ideal revenue streams.
- There are three major types of pivots
- Product pivot. The features that make up a product may not match what the customer really wants or needs. Sometimes the entrepreneur adds features that are not really important to the customer. Although customers may be willing to accept these features as part of the product, they are not willing to pay extra for them. On the other hand, sometimes the entrepreneur does not offer enough features to fully address the customers' problem. In this situation, the entrepreneur must add the additional features the customer expects.

Testing your Business Model



Customer pivot. Although a product might solve a real market problem or need, sometimes the initial business model targets the wrong customer segment or even the wrong market. For example, PayPal targeted the handheld device market that included the Palm Pilot for its electronic payment system. However, the founders of PayPal soon realized by listening to customer feedback that there was a much larger market for its product. Businesses were beginning to engage in commerce on their Web sites. PayPal pivoted its business model and as a result rapidly grew to become a \$1.6 billion company facilitating Internet commerce

Revenue model pivot. There are many ways in which the revenue model may pivot. One of the most basic revenue decisions is whether to use a high margin/low volume model or low margin/high volume model. Other revenue model pivots change the type of payment received. The model may change from a single payment to recurring revenue, or it may shift from hourly billing to charging a fixed price per service. Social entrepreneurs can pivot from a revenue model based on a nonprofit that raises money through grants and donations to a social enterprise that generates revenues from a product or service

Testing your Business Model



- Several pivots may also be necessary for a business model around operational aspects of the business, including promotion, distribution, staffing, or outsourcing.

Lean Model Canvas



PROBLEM List your customers top 3 problems	SOLUTION Outline possible solution for each problem	UNIQUE VALUE PROPOSITION Single, clear, compelling that turns an unaware visitor into an interested prospect	UNFAIR ADVANTAGE Something that can't be easily copied or bought	CUSTOMER SEGMENTS List your target customers and users
EXISTING ALTERNATIVES List how these problems are solved today	KEY METRICS List key numbers telling how your business is doing today	HIGH LEVEL CONCEPT List your X for Y analogy (e.g. YouTube = Flickr for videos)	CHANNELS List your path to customers	EARLY ADOPTERS List characteristics of your ideal customer
COST STRUCTURE List your fixed and variable costs		REVENUE STREAMS List your sources of revenue		

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BM Building blocks Explained- Lean Canvas (LC)



1. Customer Segments
 - Early adopter
2. Problem (s)
 - Existing alternatives
3. Unique Value Propositions
 - High level concept
4. Solution
5. Channels
6. Unfair Advantage
7. Revenue Streams
8. Metrics
9. Cost structure

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BM Building blocks Explained- LC



1. The Customer Segments Building Block

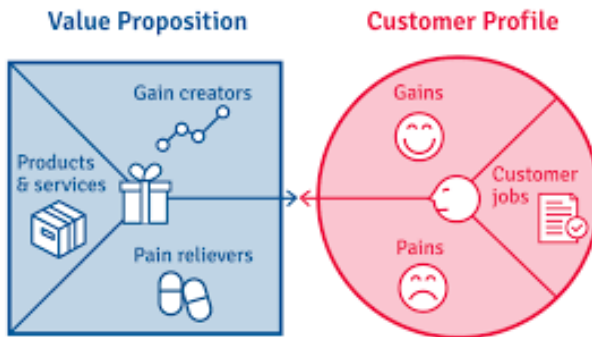
- The 'Customer Segments' section also contains a piece with the **Early Adopters**, or your most potential customers...These are the people you are going to approach first to validate your assumptions.
- 2. **Problem**-Without a problem worth solving, you have no product or service. For each key customer segment, come up with one to three high priority problems.
 - The 'Problem' section also contains a section with **existing alternatives**, this is meant to write down your competitors that solve the same problem.
 - Note, this does not necessarily mean your direct competitors, but really companies that focus on the same problem.
- 3. **Solution**
 - You will not find the solution to your problem in your first attempt. The solution is also not in your office, you will find it with the customer. Get Out Of The Building, or in other words, engage with the customer and validate different solutions.

BM Building blocks Explained- LC



- 4. **The Unique Value Proposition** is the reason why customers turn to one company over another. It solves a customer problem or satisfies a customer need. Each Value Proposition consists of a selected bundle of products and/or services that caters to the requirements of a specific Customer Segment.
 - The "what" that makes customers turn to you, over your competitors? Which of their problems are you best at solving?
 - Some popular questions to ask while determining your Unique Value Proposition are:
 - Which specific customer pain point are you trying to solve?
 - What job are you helping customers get done?
 - How does your UVP eliminate customer pain points?
 - What products or services do you provide that answer this specific pain point?
 - **High Level Concept** - write down briefly and clearly what your product or service represents. This is how your team or customers name your company to their friends, for example as "The Uber for boats"

BM Building blocks Explained- BMC



- Customer Jobs- What the customer wants to accomplish
- Customer pains- Challenges around accomplishing the job
- Customer gains- What your customer would have should the pain be taken away.
- Gain creators-What you customer gets from your product. (value)
- Pain Relievers- description of exactly how the product or service alleviates customer pains.
- Products and services – the products and services which create gain and relieve pain, and which underpin the creation of value for the customer.

BM Building blocks Explained- LC



5. **Channels.**-The Channels Building Block describes how a company communicates with and reaches its Customer Segments to deliver a Value Proposition.
 - Communication, distribution, and sales Channels comprise a company's interface with customers.
 - Channels serve several functions, including:
 - i. Raising awareness among customers about a company's products and services
 - ii. Helping customers evaluate a company's Value Proposition
 - iii. Allowing customers to purchase specific products and services
 - iv. Delivering a Value Proposition to customers
 - v. Providing post-purchase customer support
 - Finding the right mix of Channels to satisfy how customers want to be reached is crucial in bringing a Value Proposition to market
 - Chose between direct Channels and indirect ones
 - Chose between owned Channels and partner Channels.

BM Building blocks Explained- LC



5. Continue.....Channels.

- **Owned Channels** can be direct, such as an in-house sales force or a Web site, or they can be indirect, such as retail stores owned or operated by the organization.
 - Owned Channels and particularly direct ones have higher margins but can be costly to put in place and to operate.
- **Partner Channels** are indirect and span a whole range of options, such as wholesale distribution, retail, or partner-owned Web sites.
 - Partner Channels lead to lower margins, but they allow an organization to expand its reach and benefit from partner strengths

BM Building blocks Explained- BMC



6. Unfair Advantage

- The Unfair Advantage is about a specific part of your company, product or service that your competitors can't just get or copy.
 - This could be exclusive access to data, a community, authority, experience or perhaps a particular feature.

BM Building blocks Explained- LC



7. **Revenue stream building** block represents the cash a company generates from each Customer Segment (costs must be subtracted from revenues to create earnings)
 - If customers comprise the heart of a business model, Revenue Streams are its arteries.
 - A company must ask itself, For what value is each Customer Segment truly willing to pay?
 - A company should consider the best way to capture the value from the customer.
 - There are several revenue models, each with its own pros and cons.
 - It is possible for a business to use several revenue models and to even change its revenue model.
 - Examples of Revenue Models;
 - The Freemium Model
 - The Usage-Based Model (prepaid)
 - Subscription
 - Licensing
 - The Up-Front Charge Model

BM Building blocks Explained- Lean Canvas



8. **Key Metrics**-Every business has certain metrics that provide insight into how it is performing.
 - A Key Metric could be daily visitors to your site, the number of company emails opened by consumers per hour or the monthly sales of a specific feature

BM Building blocks Explained- LC



9. **The Cost Structure** describes all costs incurred to operate a business model.

- This building block describes the most important costs incurred while operating under a particular business model. Creating and delivering value, maintaining Customer Relationships, and generating revenue all incur costs. Such costs can be calculated relatively easily after defining Key Resources, Key Activities, and Key Partnerships.
- Two broad classes of business model cost structures
 - Cost-driven**
 - Cost-driven business models focus on minimizing costs wherever possible. This approach aims at creating and maintaining the leanest possible Cost Structure, using low price Value Propositions, maximum automation, and extensive outsourcing.
 - Value-driven**
 - Some companies are less concerned with the cost implications of a particular business model design, and instead focus on value creation. Premium Value Propositions and a high degree of personalized service usually characterize value-driven business models.

Lean Canvas Example

