

# Business Models

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**COSS B04**

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# Summary

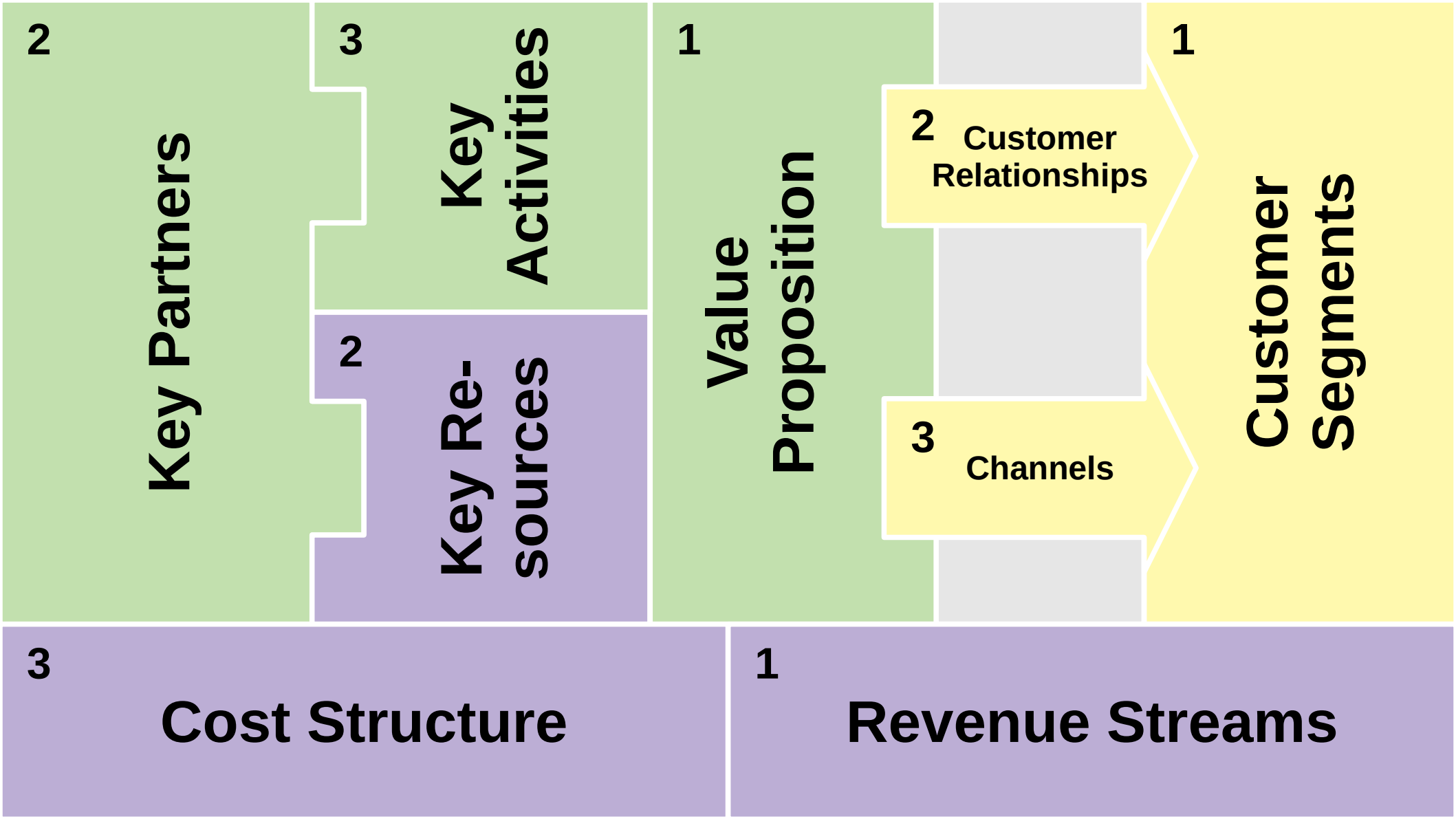
1. Business model (definition)
2. Business model canvas
3. Revenue generation
4. Production

# **1. What is a Business Model?**

# Business Model (Definition)

- A business model
  - Is a model of how a business (company) operates
- A model
  - Is a description of components and how they interact for a purpose
- A model gets instantiated a.k.a. execution

## 2. The Business Model Canvas



# Components (of a Business Model)

- Revenue generation
  - Value proposition
  - Customer segments
  - Customer relationships
  - Channels
  - Revenue streams
- Production
  - Value proposition
  - Key partners
  - Key activities
  - Key resources
  - Cost structure

## 3. Revenue Generation



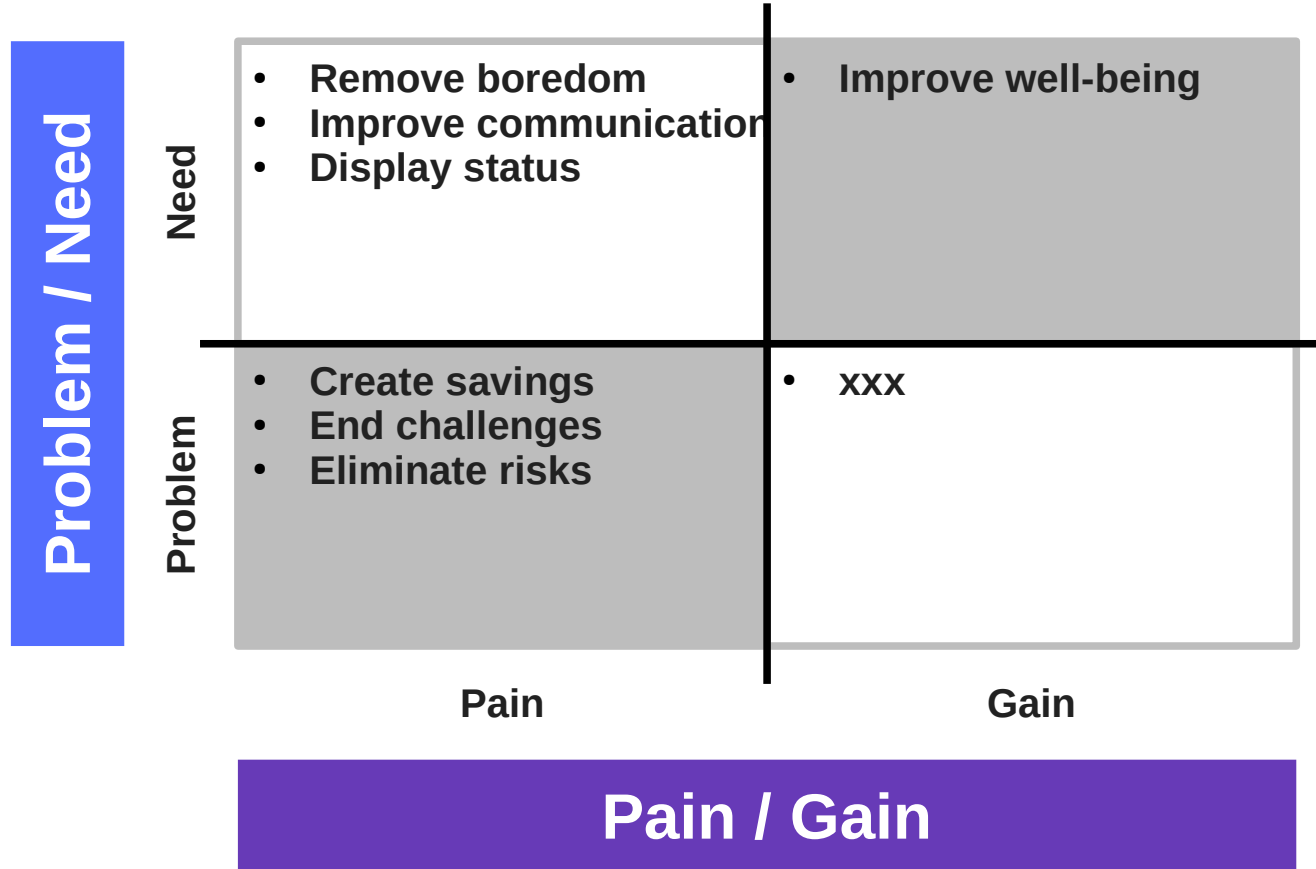
# Revenue Generation

- Revenue generation
  - Is the comprehensive process of
    - Deriving a **revenue stream**
    - By selling to a **customer segment**
    - A product or service built on a **value proposition**
    - Through a **channel** that reaches the segment
    - Base on **customer relationships**
  - Can vary by customer segment
    - Creates a unique combination then

# 1. Value Proposition

- The value to customers (so they buy)
  - Creating a gain or relieving a pain
  - Solving a problem or fulfilling a need
- Turned into a product or service
  - Cast as a minimum viable product
  - Consisting of distinct features

# Examples of Creating a Gain or Relieving a Pain



# Quantifying the Customer Gain or Pain

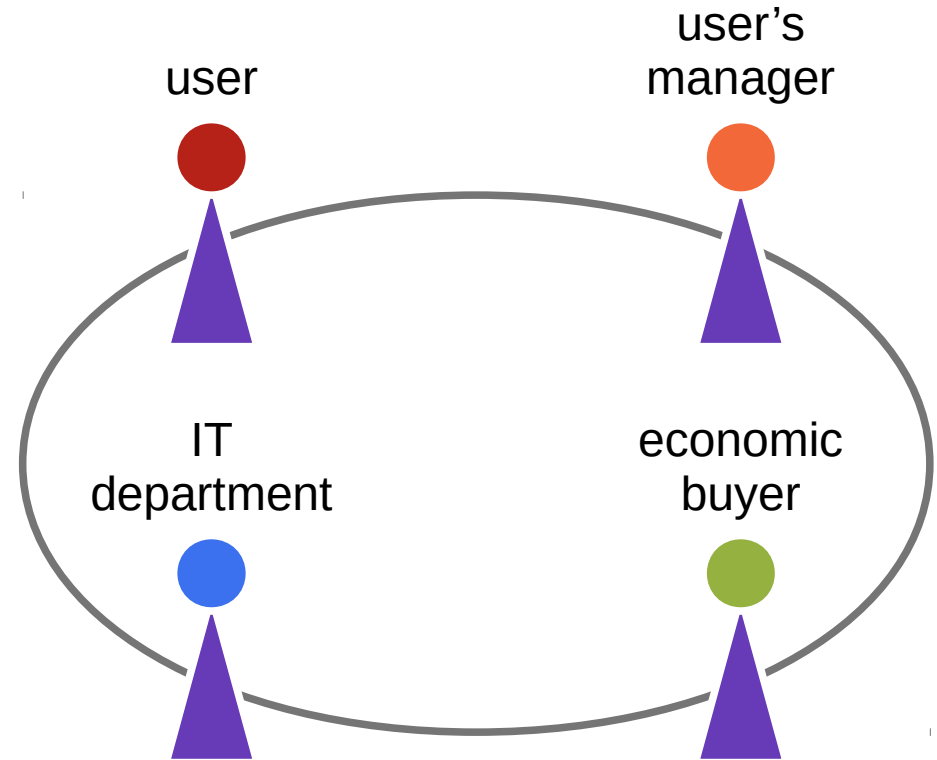
- By intensity or relevance of incidents
- By frequency of incidence

# (Markets and) 2. Customer Segments

- A customer segment
  - Is a cluster of similar customers
- Similar means
  - Defined by a set of shared characteristics; also: matching a profile
- In multi-sided markets
  - You have multiple types of customers, split further into segments
- All customer segments together constitute the total market

# Personas

- A persona
  - Is an archetypal [1] person
  - Within an archetypal customer
  - Within a customer segment
- At any customer
  - There are likely to be several personas
  - All with different powers re: purchase
  - And different profiles



[1] Archetypal = representing a cluster of similar people

# Example Market Structure Breakdown

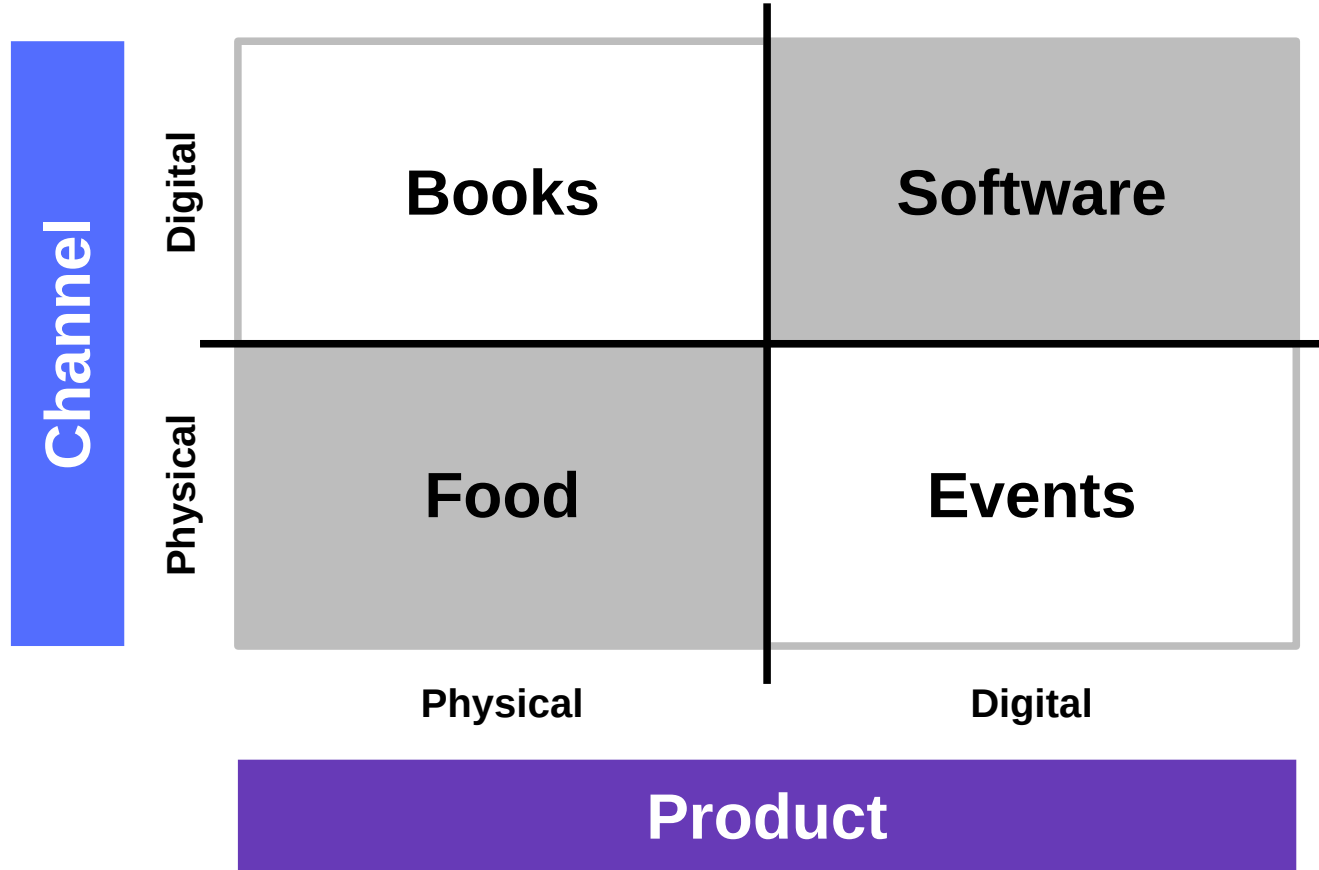
| Dimension         | Example  |
|-------------------|--|
| Markets           | Cars; beanie babies; ...   |
| Customer types    | Car buyers, car sellers; beanie baby collectors; ...                         |
| Customer segments | Truck buyers/sellers; minivan buyers/sellers; sports car buyers/sellers; ... |
| Personas          | Truck-buyer-user, truck-buyer-economic-buyer, truck-buyer-maintainer, ...    |

## 3. Channels

- 
- 
- Digital or physical channels
- Direct or indirect sales



# Physical vs. Digital



# Examples of Software Distribution Channels

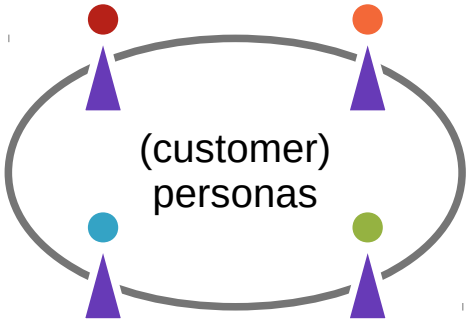
- Digital
  - Own web store
  - Platform app store
  - Digital retailers
- Physical
  - Book stores
  - Electronic stores
  - System integrators

# Direct vs. Indirect Channel Sales

- In a direct channel sale
  - Your company sells directly to the customer
  - You make maximum profit
- In an indirect channel sale
  - Your company sells through a reseller
  - Your profit drops by the cut intermediaries are taking
  - Some of your SG&A costs drop because selling got simpler

## 4. Customer Relationships

- As a business, you need to understand how to
  - **Get**
  - **Keep**, and
  - **Grow** your customer base
- For this, you use personas (see customer segment discussion)



# Customer Acquisition (Getting Customers)

- Marketing primes the sales funnel
  - Tries to create demand
    - Advertising
    - Trade shows
    - Trade magazines
    - Email, webinars
  - Output: Qualified leads
- Sales takes over qualified leads
  - Consumer
    - Low-touch sales
    - Web store
  - Enterprise
    - High-touch sales
    - Evaluation
    - Sale
  - Output: Sale + customer



# Customer Acquisition Cost (CAC)

- Each step in the sales funnel
  - Has a cost associated with every potential customer entering it
  - Reduces the number of potential customers moving forward
- Customer acquisition cost
  - Is the accumulated cost normalized for one realized customer
  - Is a key metric (cost) to be matched against revenue

# Example CAC for Enterprise Software Product

|                             | Cost per lead | Survival rate | No customers | Total stage cost |
|-----------------------------|---------------|---------------|--------------|------------------|
| Trade show lead             | 100 €         | 100 %         | 10           | 1.000 €          |
| Evaluation                  | 5.000 €       | 20 %          | 2            | 10.000 €         |
| Sale                        | 2.000 €       | 50 %          | 1            | 2.000 €          |
| Customer acquisition cost = |               |               |              | 13.000 €         |

# Customer Retention (Keeping Customers)

- Retaining existing customers is cheaper than getting new ones
- Techniques for keeping customers
  - Foremost, keep delivering a great product
  - Then create loyalty program, added benefits
  - Increase switching costs to lock-in customers



# Customer Attrition (Churn)

- Customer churn
  - Is the percentage of customers you loose in a given time period

| Churn | Period |         |         |        |         |         |
|-------|--------|---------|---------|--------|---------|---------|
|       | Start  | 1 month | 6 month | 1 year | 2 years | 5 years |
| 20 %  | 100    | 80      | 26      | 7      | 0       | 0       |
| 10 %  | 100    | 90      | 53      | 28     | 8       | 0       |
| 5 %   | 100    | 95      | 74      | 54     | 29      | 5       |
| 1 %   | 100    | 99      | 94      | 89     | 79      | 55      |

- Customer lifetime =  $1 / \text{churn}$ 
  - For example, a 1% churn rate = 100 months of customer lifetime

# Customer Growth

- Growing your customer base is cheaper than acquiring new customers
- Techniques for growing your customer base
  - Up-sell your customers
  - Cross-sell them
  - Ask for referrals

# Customer Lifetime Value (CLV)

- The lifetime value of a customer is
  - The total revenue from the customer over time in today's currency
- Steps to calculate (the average) CLV
  - Determine customer lifetime (from customer churn)
  - By period, determine revenues and costs for that period
  - Discount period profits by how far out the revenues are
- Customer costs include
  - Initial customer acquisition costs
  - Subsequent retention costs
  - Possible growth costs

# Heuristics for the Customer Lifetime Value

- CLV should be  $\gg$  than CAC
  - CAC dominates most costs
- Rules of thumb vary by domain

## 5. Revenue Streams

- Revenue (income)
  - A payment received from a customer
- A revenue source
  - Is a synonym for customer
- A revenue stream
  - Is the stream of revenues received from a source over time
- An aggregate revenue stream
  - Is the aggregation of several revenue streams from different sources
- The total revenue stream
  - Is the aggregation of all revenue streams
- Business intelligence lets you analyze your revenue streams

# Pricing

- The price of a unit of product or service
  - Is the money charged to the customer for that unit of product or service
  - Is best set equal to the value the potential customer sees in it
  - The value of a unit of product or service varies by time
  - This maximizes revenues by customer
- Price discrimination
  - Is the process of setting the price dynamically
  - For a given individual customer
- If you can't price discriminate, you price
  - By segment
  - By channel
- Always price based on value, never on costs

# How Revenue Streams are Structured

- Individual sale (revenue)
  - Is **price** x **no units** of product or service sold
- Revenues can be aggregated resp. broken down in many ways
  - By market structure: Markets → customer segments → customers
  - By classic (physical) break-down: location, demographics
  - By channel: Web store, retailer, etc.
- Prices (incl. volume discounts) may vary by breakdown

## 4. Production



# Production

- Production
  - Is the comprehensive process of
    - Creating, delivering, and maintaining the product or service

# 6. Partnerships

# Thank you! Questions?

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