E-commerce
business, technology, society.

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CHAPTER 2
E-Commerce Business Models
and Concepts

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Learning Objectives

- Identify the key components of e-commerce business models.
- Describe the major B2C business models.
- Describe the major B2B business models.
- Recognize business models in other emerging areas of e-commerce.
- Understand key business concepts and strategies applicable to e-commerce.

Kozmo Finally Crashes

- Use the Internet to combine the convenience of a catalog with the immediate gratification of in-store shopping by offering entertainment, food, and convenience products delivered within one hour, with no minimum order required and no delivery charges.

Kozmo Finally Crashes

- Created a Web site that featured localized offerings based on customer zip code.
- An order placed on the Web site would be transmitted directly to Kozmo’s distribution center, packed, and delivered.

Kozmo Finally Crashes

- $250 million in Venture capital
- Rapid expansion and intensive spending to gain market share and brand recognition
- No concern for short-term profitability
Kozmo Finally Crashes

- Painful lessons:
  - Hard to make money delivering low-priced convenience store items.
  - Business model didn’t work everywhere.
  - Company founders are not necessarily its best managers.
  - Difficult for a new firm to establish a profitable e-commerce business in an entirely new market niche.

E-Commerce Business Models

- Business model
  - a set of planned activities designed to result in a profit in a marketplace
- Business plan
  - a document that describes a firm’s business model
- E-commerce business model
  - a business model that aims to use and leverage the unique qualities of the Internet and the World Wide Web.

Eight Key Ingredients of a Business Model

<table>
<thead>
<tr>
<th>BUSINESS MODEL COMPONENTS</th>
<th>KEY QUESTIONS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Value proposition</td>
<td>Why should the customer buy from you?</td>
</tr>
<tr>
<td>Revenue model</td>
<td>How will you make money?</td>
</tr>
<tr>
<td>Market opportunity</td>
<td>What advantages do you intend to serve, and what is its size?</td>
</tr>
<tr>
<td>Competitive environment</td>
<td>Who else occupies your intended marketplace?</td>
</tr>
<tr>
<td>Competitive advantage</td>
<td>What special advantages does your firm bring to the marketplace?</td>
</tr>
<tr>
<td>Market strategy</td>
<td>How do you plan to promote your products or services to affect your target audience?</td>
</tr>
<tr>
<td>Organizational development</td>
<td>What types of organizational structures within the firm are necessary to carry on the business plan?</td>
</tr>
<tr>
<td>Management focus</td>
<td>What kinds of experiences and background are important for the company’s leaders to have?</td>
</tr>
</tbody>
</table>

Eight Key Ingredients of a Business Model: Value Proposition

- Defines how a company’s product or service fulfills the needs of customers.
- Questions
  - Why will customers choose to do business with your firm instead of another company?
  - What will your firm provide that other firms do not and cannot?

Eight Key Ingredients of a Business Model: Revenue Model

- Describes how the firm will earn revenue, produce profits, and produce a superior return on invested capital.
- E-commerce revenue models include:
  - advertising model
  - subscription model
  - transaction fee model
  - sales model
  - affiliate model

Eight Key Ingredients of a Business Model: Revenue Model

- Advertising revenue model
  - a company provides a forum for advertisements and receives fees from advertisers (Yahoo)
- Subscription revenue model
  - a company offers its users content or services and charges a subscription fee for access to some or all of its offerings (Consumer Reports, or Wall Street Journal)
Eight Key Ingredients of a Business Model: Revenue Model

- Transaction fee revenue model
  - a company receives a fee for enabling or executing a transaction (eBay or E-Trade)
- Sales revenue model
  - a company derives revenue by selling goods, information, or services (Amazon orDoubleClick)
- Affiliate revenue model
  - a company steers business to an affiliate and receives a referral fee or percentage of the revenue from any resulting sales (MyPoints)

Five Primary Revenue Models

<table>
<thead>
<tr>
<th>REVENUE MODEL</th>
<th>EXAMPLE</th>
<th>REVENUE SOURCE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Advertising</td>
<td>Yahoo.com</td>
<td>Key from advertisements or exchange for advertisements</td>
</tr>
<tr>
<td>Subscription</td>
<td>WSJ.com, Consumersreport.org, Spiegel.com</td>
<td>Fees from subscriptions in exchange for access to content or services</td>
</tr>
<tr>
<td>Transaction fee</td>
<td>eBay.com, E-Trade.com</td>
<td>Fees (commission) for enabling or executing a transaction</td>
</tr>
<tr>
<td>Sales</td>
<td>Amazon.com,DoubleClick.com</td>
<td>Sales of goods, information, or services</td>
</tr>
<tr>
<td>Affiliate</td>
<td>MyPoints.com</td>
<td>Fees for business referrals</td>
</tr>
</tbody>
</table>

Eight Key Ingredients of a Business Model: Market Opportunity

- Market opportunity
  - refers to the company’s intended marketspace and the overall potential financial opportunities available to the firm in that market space
  - defined by the revenue potential in each of the market niches where you hope to compete
- Marketspace
  - the area of actual or potential commercial value in which a company intends to operate

Marketspace and Market Opportunity is the Software Training Market

Eight Key Ingredients of a Business Model: Competitive Environment

- Refers to the other companies operating in the same marketplace selling similar products
- Influenced by:
  - how many competitors are active
  - how large are their operations
  - the market share of each competitor
  - how profitable these firms are
  - how they price their products

Eight Key Ingredients of a Business Model: Competitive Advantage

- Achieved by a firm when it can produce a superior product and/or bring the product to market at a lower price than most, or all, of its competitors
- Achieved because a firm has been able to obtain differential access to the factors of production that are denied their competitors -- at least in the short term
Eight Key Ingredients of a Business Model: Competitive Advantage

- **Asymmetry**
  - exists whenever one participant in a market has more resources than other participants

- **First mover advantage**
  - a competitive market advantage for a firm that results from being the first into a marketplace with a serviceable product or service

Eight Key Ingredients of a Business Model: Competitive Advantage

- **Unfair competitive advantage**
  - occurs when one firm develops an advantage based on a factor that other firms cannot purchase

- **Perfect Market**
  - a market in which there are no competitive advantages or asymmetries because all firms have equal access to all the factors of production

  - **Leverage**
    - when a company uses its competitive advantage to achieve more advantage in surrounding markets

Eight Key Ingredients of a Business Model: Market Strategy

- The plan you put together that details exactly how you intend to enter a new market and attract new customers

  - **Best business concepts will fail if not properly marketed to potential customers**

Eight Key Ingredients of a Business Model: Organizational Development

- Describes how the company will organize the work that needs to be accomplished

  - Work is typically divided into functional departments

  - **Move from generalists to specialists as the company grows**

Eight Key Ingredients of a Business Model: Management Team

- Employees of the company responsible for making the business model work

  - Strong management team gives instant credibility to outside investors

  - A strong management team may not be able to salvage a weak business model

  - Should be able to change the model and redefine the business as it becomes necessary

Major Business-to-Consumer (B2C) Business Models
Major Business-to-Consumer (B2C) Business Models

Page 68, Table 2.3 continued

<table>
<thead>
<tr>
<th>BUSINESS MODEL</th>
<th>VARIATIONS EXAMPLES</th>
<th>DESCRIPTION</th>
<th>REVENUE MODEL</th>
</tr>
</thead>
<tbody>
<tr>
<td>E-tailer</td>
<td>virtual merchants (online retail store only)</td>
<td>Includes news and entertainment companies that provide digital content over the Web</td>
<td>typically utilizes an advertising, subscription, or affiliate referral fee revenue model</td>
</tr>
<tr>
<td>Content Provider</td>
<td>processes online sales transactions</td>
<td>Typically utilizes a transaction fee revenue model</td>
<td></td>
</tr>
<tr>
<td>Market Creator</td>
<td>uses Internet technology to create markets that bring buyers and sellers together</td>
<td>typcially utilizes a transaction fee revenue model</td>
<td></td>
</tr>
<tr>
<td>Service Provider</td>
<td>offers services online</td>
<td>Community Provider</td>
<td>provides an online community of like-minded individuals for networking and information sharing</td>
</tr>
<tr>
<td>Transaction Broker</td>
<td>processes online sales transactions</td>
<td>typically utilizes a transactions fee revenue model</td>
<td></td>
</tr>
<tr>
<td>Service Provider</td>
<td>offers services online</td>
<td>Community Provider</td>
<td>provides an online community of like-minded individuals for networking and information sharing</td>
</tr>
</tbody>
</table>

Major Business-to-Consumer (B2C) Business Models

• Portal
  - offers powerful search tools plus an integrated package of content and services
  - typically utilizes a combines subscription/advertising revenues/transaction fee model
  - may be general or specialize (vortal)

Insight on Technology: Google.com -- Searching for Profits

• Web's hottest search engine
• Started in 1998 by two enterprising Stanford grad students
• Uses outside criteria to validate that a search result is likely to be relevant
  • the more outside links there are to a particular page, the higher it jumps in Google's ranking structure
Major Business-to-Business (B2B) Business Models

<table>
<thead>
<tr>
<th>BUSINESS MODELS</th>
<th>VARIATIONS</th>
<th>EXAMPLES</th>
<th>DESCRIPTION</th>
<th>REVENUE MODEL</th>
</tr>
</thead>
<tbody>
<tr>
<td>B2B Hub</td>
<td></td>
<td></td>
<td>also known as marketplace/exchange</td>
<td>Transaction fees</td>
</tr>
<tr>
<td>B2B Service Provider</td>
<td></td>
<td></td>
<td>sells business services to other firms</td>
<td>Transaction fees</td>
</tr>
<tr>
<td>Matchmaker</td>
<td></td>
<td></td>
<td>links businesses together</td>
<td>Transaction fees</td>
</tr>
<tr>
<td>Infomediary</td>
<td></td>
<td></td>
<td>gather information and sells it to businesses</td>
<td>Transaction fees</td>
</tr>
<tr>
<td>E-distributor</td>
<td></td>
<td></td>
<td>supplies products directly to individual businesses</td>
<td>Transaction fees</td>
</tr>
</tbody>
</table>

Insight on Business: E-Steel.com Breaks the Mold

- B2B marketplace
- 3,500 member companies trading globally
- Uses private negotiation model rather than auction model

Business Models in Other Emerging Areas of E-Commerce

<table>
<thead>
<tr>
<th>TYPE</th>
<th>MODEL</th>
<th>EXAMPLE</th>
<th>DESCRIPTION</th>
<th>REVENUE MODEL</th>
</tr>
</thead>
<tbody>
<tr>
<td>Consumer</td>
<td>Market Connecter</td>
<td>eBay.com</td>
<td>B2C consumers connect with each other; places bids</td>
<td>Transaction fees</td>
</tr>
<tr>
<td>Peer-to-peer</td>
<td>Content Provider</td>
<td>Napster.com, MySpace.com</td>
<td>Technology enabling consumers to share files and services via the Web</td>
<td>Subscription fees, advertising, transaction fees</td>
</tr>
<tr>
<td>M-commerce</td>
<td>Various</td>
<td>Amazon.com</td>
<td>Enabling business applications using wireless technology</td>
<td>Sales of goods</td>
</tr>
</tbody>
</table>
### M-commerce Business Models
- Traditional e-commerce business models leveraged for emerging wireless technologies to permit mobile access to the Web

### E-commerce Enablers’ Business Models
- Focus on providing infrastructure necessary for e-commerce companies to exist, grow, and prosper

### E-commerce Enablers

<table>
<thead>
<tr>
<th>Players</th>
<th>Infrastructure Players</th>
</tr>
</thead>
<tbody>
<tr>
<td>IBM, Sun, Company, Dell</td>
<td>Microsoft, Sun, Apache Foundation, Oracle, Ariba, eBay, Amazon, IBM</td>
</tr>
<tr>
<td>Cisco</td>
<td>Checkpoint, Javico</td>
</tr>
<tr>
<td>E-commerce Software Systems (B2B, B2C)</td>
<td>Real Networks, Microsoft</td>
</tr>
<tr>
<td>Payment Systems</td>
<td>PayPal, CyberCash</td>
</tr>
<tr>
<td>Performance Evaluation</td>
<td>Adobe, CacheFlux, Intercom, iCera, Digital Island</td>
</tr>
<tr>
<td>Databases</td>
<td>Oracle, Sybase</td>
</tr>
<tr>
<td>Hosting Services</td>
<td>E本事、Equinix, Global Crossing</td>
</tr>
</tbody>
</table>

### Seven Unique Features of E-Commerce Technology

- **Ubiquity**
  - Alters industry structure by creating new marketing channels and expanding size of overall market
  - Creates new efficiencies in industry operations and lowers cost of firms’ sales operations
  - Enables new differentiation strategies

- **Global Reach**
  - Changes industry structure by lowering barriers to entry, but greatly expands market at the same time
  - Lowers cost of industry and firm operations through production and sales efficiencies
  - Enables competition on global scale
Seven Unique Features of E-Commerce Technology

- **Universal Standards**
  - Changes industry structure by lowering barriers to entry and intensifying competition within an industry
  - Lowers costs of industry and firm operations by lowering computing and communications costs
  - Enables broad-scope strategies

- **Richness**
  - Alters industry structure by reducing strength of powerful distribution channels
  - Changes industry and firm operations costs by lessening reliance on sales force
  - Enhances post-sale support strategies

- **Interactivity**
  - Alters industry structure by reducing threat of substitutes through enhanced customization
  - Reduces industry and firm costs by lessening reliance on sales force
  - Enables differentiation strategies

- **Personalization/Customization**
  - Alters industry structure by reducing threats of substitutes, raising barriers to entry
  - Reduces value chain costs in industry and firm by lessening reliance on sales forces

- **Information Density**
  - Changes industry structure by weakening powerful sales channels, shifting bargaining power to consumer
  - Reduces industry and firm operations costs by lowering costs of obtaining, processing, and distributing information about suppliers and consumers

E-Commerce and Industry Structure

Page 88, Figure 2.3
How the Internet and the Web Change Business: Basic Business Concepts

- Industry Structure
  - the nature of players in an industry and their relative bargaining power
  - by changing
    - the basis of competition among rivals
    - the barriers to entry
    - the threat of new substitute products
    - the strength of suppliers
    - the bargaining power of buyers

- Industry Value Chains
  - set of activities performed in an industry by suppliers, manufacturers, transporters, distributors, and retailers that transform raw inputs into final products and services
  - reducing the cost of information and other transactional costs

- Firm Value Chains
  - set of activities performed within an individual firm to create final products from raw inputs
  - increasing operational efficiency

E-Commerce and Industry Value Chains

Page 90, Figure 2.4

E-Commerce and Firm Value Chains

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How the Internet and the Web Change Business: Basic Business Concepts

- Business Strategy
  - set of plans for achieving superior long-term returns on the capital invested in a firm
  - offers unique ways
    - differentiate products
    - obtain cost advantages
    - compete globally
    - compete in a narrow market or product segment