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What are Business Models? Developing a Theory of Performative Representations

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Abstract

Despite a rich extant literature, it is unclear what business models are. We argue that rather than an actual feature of firms, business models are performative representations. We begin by noting the importance of business models for the development of new technology. We then assess three dominant conceptions of business models in the academic literature: as transactional structures, value extracting devices and mechanisms for structuring the organization. To overcome the shortcomings of these approaches, we advance an alternative conception of business models as performative representations. We argue that they work as narratives that convince, typifications that legitimate, and recipes that guide social action.

Introduction

In her seminal work, Joan Woodward (1965) pointed out that technology shapes the organizational structures and dynamics of control in organization. While this insight has remained at the centre of organizational sociology for many years, it may be due for an overhaul. While some questions around contingency are more theoretical in nature (Orlikowski, this volume), others are more empirical. In particular, some have asked to what extent the results Woodward derived from a study of manufacturing organizations apply to organizations that are heavily reliant on post-industrial technologies like software, bio-medicine, and complex materials science (Lewin and Stephens, 1993; Zuboff, 1988). Commentators have argued that new technologies call for new organizational structures which are simply inconceivable using Woodward's framework (Zammuto et al., 2007).

One particular aspect that has intrigued researchers is whether contingencies go beyond the level of organizations and include the ecologies and networks in which firms operate. For instance, in emerging and fast-moving technology contexts, firms with more external ties and more central networks are more successful than their less connected peers (Powell et al., 1996). The characteristics of a firms' 'value network' have a decisive effect on the direction of its innovation activities which in turn determines long-term performance (Christensen and Rosenbloom, 1995).

A favorite concept to capture such contingencies is the notion of business models. In

their simplest form, business models are ‘stories that explain how enterprises work’ (Magretta, 2002: 4). A business model encapsulates the way in which a firm, endowed with a given technology, can successfully configure an organizational structure and its relationships with external stakeholders (Amit and Zott, 2001). For instance, the idea of the business model is used to describe how firms have linked the manufacture of electronic devices with digital distribution technologies (Osterwalder et al., 2005) or succeeded in invoicing third parties such as advertisers for services rendered to other customers for free within the context of multisided markets (Rochet and Tirole, 2006).

Despite widespread discussions about business models in the popular press, there is a remarkable degree of uncertainty about what the concept actually means, both within practitioner-oriented and academic audiences (George and Bock, forthcoming; Osterwalder et al., 2005). The gap between widespread use and conceptual ambiguity is puzzling. In this short paper, we argue that business models are not naturalistic entities but representations deployed by business managers as strategic resource (Hardy et al., 2000). This allows us to question the now familiar claim that radical new technologies require new business models. We maintain that a contingency approach is not particularly helpful in understanding the hype around business models. In fact, the concept of business models is both theoretically contested and empirically ambiguous, and its use tends to be normatively inflected. Rather, we conceive of a business model as a performative representation. It works by articulating narratives to entice potential constituents, typifying and thereby creating legitimacy for the venture, and providing recipes that instruct practical action.

We begin by reviewing the existing literature on business models. We claim these approaches assume business models describe some underlying reality while they ignore how they are used as performative representation of reality to construct and articulate a particular value around a technology. We conclude by illustrating how a representational approach helps us to move away from the crude contingency model which underpins most talk about business models, and develop a more complex idea of contingency of the kind espoused by Orlikowski (this volume).

Theorising Business Models

The notion of business models is widely used in business practice. A search of the *Financial Times* archive for the phrase ‘business model’ results in more than 6,000 hits for the five-year period 2004-2009. The concept gained enormous popularity during the Internet boom of the late 1990s and later spread across a wider community of management practitioners and business analysts (Ghaziani and Ventresca, 2005). However, it is only relatively recently that management researchers have turned their attention to this concept. While the academic literature on the topic remains sparse and diffuse, contributions can be grouped into three conceptions of business models: transactional structures, value extraction mechanisms, and organizational structuring devices. Below, we summarise each of these approaches.

A first approach conceptualises business models as transaction structures. In this view, business models describe the way firms configure their *transactions* with groups of stakeholders including customers, suppliers and vendors (Zott and Amit, 2008). In other words, a business models is ‘the content, structure, and governance of

transactions designed so as to create value through the exploitation of business opportunities' (Amit and Zott, 2001: 511). For instance, the business model of *Google* generates profit from providing Internet search by organizing transactions between users and advertisers (Rappa, 2004). Differences between transaction structures have led researchers to generate various business model taxonomies. Zott and Amit (2008) argue that there are two generic types of business models – efficiency centred models and novelty centred models. By contrast, Bienstock and colleagues (2002) argue that there are 40 different possible business models based on differences in the number of buyers, number of sellers, price mechanism, nature of product offering, and frequency of exchange. Common among these approaches is the assumption that business models, *qua* transaction structures, constitutes a variable that can be influenced by firms independently from other variables, such as strategies, product strategies or alliance models.

A second approach emphasizes business models as mechanisms for creating and capturing value (Shafer et al., 2005). At centre stage here are the processes and structures through which a firm creates and captures value from a given technology. The business model is a manipulable 'focusing device', mediating between technology and economic value creation (Chesbrough and Rosenbloom, 2002). Because technology development is capital-intensive, time-consuming and uncertain, it often results in outputs for which there are no obvious and immediate applications within a given business context. In this situation, certain business models may help to exploit the given technological affordance by deciding whether to exploit, acquire or sell certain technologies (Chesbrough and Rosenbloom, 2002). For instance, *IBM* has used 'open business models' to create value around particular technologies they owned by leveraging the inputs of a variety of external innovators' (Chesbrough, 2007: 22). Focusing on how value is created and exploited has led researchers to identify various ways of tapping into value streams. For instance, Mahadevan (2000) identified four possible 'value streams' in an Internet-based business: virtual communities, reduced transaction costs, exploitation of information asymmetry, and value-added market-making processes.

A third approach treats business models as devices for structuring and designing organizations. Business model are seen as templates for configuring various components within an organization (Winter and Szulanski, 2001). For instance, to implement its 'direct' model, Dell had to undertake a significant re-design of its internal processes and relationships with the distribution chain (Morris et al., 2005). This means the business model is the manifestation of how certain organizational variables are configured and the consequences of that configuration on business performance (Casadesus-Masanell and Ricart, 2008). For instance, (Yip, 2004) defines the business model as a certain configuration of the following organizational components: a value proposition; the nature of inputs; how inputs are transformed; the nature of outputs; vertical scope; horizontal scope; geographic scope; nature of customers; how to organize; etc. (Yip, 2004). Similarly Osterwalder et al. (2005) argues that business models include a value proposition, a customer interface, infrastructure management and financial aspects. Some working in this tradition argue that designing adequate business models is one of the main drivers of business performance (Slywotzky, 1999). The central insight in much of this work is that the business model is made up of a series of managerial choices of how to organize components of a firm around a particular technology even though some point out that

the design of business models can be emergent (Ghoshal and Bartlett, 1994) and not necessarily drawing on a-priori managerial fiat.

Criticisms of the Business Model Concept

While the three strands of work on business models offer us a beginning point, they also pose some significant problems. First, it is unclear how the concept *fits* with the existing literature on business strategy and organization. Some of the definitions of business models given in the practitioner-oriented literature are so broad they include nearly every aspect of the business, rendering them of limited use as abstract or even middle-range concepts. George and Bock (George and Bock, forthcoming) found that managers from different firms singled out different aspects of the business model concept as relevant. While some managers regarded the resource aspect of the business model as primary, others viewed transactive or value aspects as more salient (George and Bock, forthcoming). In the more academically oriented literature, is unclear whether the concept can be meaningfully distinguished from other, already established concepts. For instance, 'business model' is often used synonymously with 'business strategies' (Casper and Kettler, 2001) even though some authors have attempted to establish the concept as stand-alone theoretical construct (Zott and Amin, 2008). As a result the business model concept remains polysemic and ambiguous among practitioners and academic researchers.

The second problem with the existing literature on business models concerns *construct validity*. This means is it uncertain whether the concept refers to something that actually exists. This may be among the reasons why researchers looking for business models often encounter inconsistent empirical signals. Often they find themselves examining what entrepreneurs, investors or perhaps the press claim to be business models. On further investigation, these claims are often weakly linked to what is going on within an organization and play a rhetorical rather than representational role. It appears the concept has the most substantive meaning when it refers to a replicable template of how a business works (Winter and Szulanski, 2001). However, in many instances, the concept is generalized to capture an organization's 'essence', meaning that it becomes indistinguishable from the organization. For instance, when observers refer to IKEA's or Ryanair's business models (Casadesus-Masanell and Ricart, 2008; Normann and Ramirez, 1993), they include so many aspects of these organizations that it becomes questionable whether they are actually replicable or rather idiosyncratic features of these organizations. As a result, even airlines generally associated with 'budget airline' business models are still very different from each other. All the above make it difficult to think of business models as something that has a measurable essence. If business models are referred to in this way, they appear to express the ambition by firms and managers to be *like* others, and be considered successful businesses in their sector.

This leads us to a third related problem with existing approaches to business models – namely their *normative inflection*. Many proponents of the business model concept emphasize how thinking about business models can help firms achieve certain goals such as greater innovativeness, creating new revenue streams or organizational transformation. In the same way that practitioner knowledge is situated and concerned only with fulfilling particular purposes in particular circumstances (Schön, 1983), these contributions detail certain courses of action rather than establishing the general

validity of the concept. The 'interpretative flexibility' (Bijker et al., 1987) of the concept enables different authors to promote their own versions of the central underlying idea. In this respect, the representational quality of the notion becomes secondary to its potential to underpin idea entrepreneurship, which often relies on putting 'old wine into new bottles' (Abrahamson, 1996).

We have identified three issues arising from the existing literature: the relationship of the business model concept to existing strategy and organization literature, the lack of construct validity and normative inflection. Taken together, these issues raise questions about the epistemological status of the concept. Below we suggest that, rather than looking at business models as a naturalistic feature of organizations, they should be seen as a performative representation used in business life.

Towards Theory of Business Models as Performative Representations

To address the conceptual ambiguity, construct validity problems, and normative inflections that haunt most existing accounts of business models, we outline an alternative approach. We suggest that business models can be thought of as a performative representation. A business model is a representation in that it is a text that re-describes and re-constructs reality – whether actual or imagined - in a way that is always partial, interested and intent on persuading (De Cock, 2000; Jeffcutt, 1994). Texts are more durable and intransitive than mere actions and therefore play an important role in infusing change (Phillips et al., 2004). A business model is performative in the sense that it is a text that does things through reconstructing the social world in their own image (Austin, 1962; Callon, 2007; MacKenzie and Millo, 2003). Business models are representations that create material effects such as enrolling buyers and suppliers, persuading investors, and directing employees. Below we suggest that business models are performative in three ways: as narratives that persuade, as typifications that legitimate, and as recipes that instruct.

First, business models are narratives used by promoters of a new venture or technology to entice key constituents (George and Bock, forthcoming; Magretta, 2002). Narratives, or stories, are a genre of text that describes a sequence of events (Bruner, 1991; Lounsbury and Glynn, 2001; Polkinghorne, 1988). A story's components usually comprise a subject searching for an object, a 'destinator' (a force determining the subject's destination), and a set of forces furthering or hindering the subject's quest for a desired object (Fiol, 1989; Lounsbury and Glynn, 2001). For a firm to embrace a business model as a narrative then means to construct a representation of how a business might succeed or thrive in a particular environment. The subject of the story is the firm, in search of prized objects, most obviously represented by profitability or victory over rivals. The destinator is represented by the market's merciless fight for survival, and the set of forces facing the subject are the tactics and strategies deployed by the business and its rivals. Because of their temporal, projective aspect, business model stories may be instrumental in inducing expectations among interested constituents about how the businesses' future might play out (Downing, 2005).

Existing research in other contexts such as corporate failures suggest that narratives are important ways which people seek to infuse uncertain and ambiguous situations with meaning and persuade sceptical audiences that their account of reality is believable (Brown, 2000). Hence narratives may be used to convey how a new

technology (or business idea more broadly) might perform commercially (Lounsbury and Glynn, 2001). Business model narratives may draw on whole range of linguistic techniques that have been identified in existing research on narratives in organizations more broadly (Czarniawska-Joerges and Czarniawska, 1997; Gabriel, 2000; Rhodes et al., 2005). These include the mobilization of fantasy scenarios, using widely known cultural myths, appealing to archetypical figures, constructing a series of episodes, and mobilizing well-known literary tropes such as metaphors. By bringing these components of a story together in a skilful and appealing way, a promoter can craft a new technology as being plausible and appealing to potential constituents such as investors, suppliers and potential clients.

Second, a business model is also a way in which a venture can associate itself with a particular type or identity, thereby creating a sense of legitimacy. For a firm, adopting a certain business model means identifying itself with a group of other, similar firms. Equally, it distinguishes a firm from other firms that are not part of such a group. In this sense, a business model is an external identity that a firm can assume (Pólos et al., 2002). External identities are directed at audiences that judge whether an organization qualifies as a member of one group or another. These audiences can penalize them for deviating from what they do not consider a valid manifestation of a certain type or in turn reward them for conforming to a certain type (McKendrick and Carroll, 2001). For instance, Zuckerman (1999) showed that firms that failed to attract coverage from the financial analysts who specialized in a firm's industry had their equities to trade at a discount.

This kind of consideration is particularly relevant for firms in new technology contexts characterized by high uncertainty over future performance. Particularly early stage organizations suffer from legitimacy deficits that they often address by adopting impression management and other symbolic management techniques (Zott and Huy, 2007). This is because they are often highly resource-dependent on financial investors such as venture capitalists. Similarly, they may try to woo certain audiences as customers, for instance by styling themselves as craft beer producers and hence signaling that they are relevant to certain group of beer consumers (Carroll and Swaminathan, 2000).

In this situation, firms may attempt to make themselves identifiable by associating with certain business models that form known categories. For instance, an Internet firm might choose to adopt an advertising-centred business model, allowing it to take advantage of the existing legitimacy of that model on the basis of success stories such as *Google*. Because investors and other stakeholders recognize this as a legitimate category of organizations, even novel entrants will be granted a legitimacy bonus compared to others sporting an illegitimate business model. As a result, the more legitimate a business model is, the more likely it is to be adopted (Kostova et al., 2008). This is particularly true if the market is emerging and there is little certainty about the value associated with a business idea (Sanders and Boivie, 2004; Zimmerman and Zeitz, 2002). To summarize, business models serve as representations that build into identification processes performed by audiences relevant to firms' resource mobilization strategies. By deploying business models as known categories, they can help firms to obtain a legitimacy bonus that in turns may result in real resource flows.

The final way in which business models work is through providing a recipe that instructs actors involved with the business what they should do. Managers are often guided in their decision by cognitive frameworks that privilege certain courses of action to the exclusion of others (Tripsas and Gavetti, 2000; Walsh, 1995). Firms tend to adopt 'industry recipes' (Spender, 1989) as simplified way of conducting business and understanding the environment. These recipes are typically adopted by many firms in an industry and provide practical guides to what a firm in a particular industry does. They constitute mental models that codify some key causal relationships assumed to underpin 'the business' a firm believes to be in (Porac et al., 1989). Over time, mental models and strategic choices intertwine to create a stable set of expectations among industry participants (Porac et al., 1989).

But business models are more than just simplified cognitive maps. They often take the form of carefully constructed models, which like a scientific or architectural model, do not just represent reality but also guide the practice of remaking that reality. An instance of models directing the construction of social reality can be found in economics (Callon, 2007; Ferraro et al., 2005; MacKenzie, 2006). A now classic case of this is how the Black-Scholes model for pricing financial assets eventually came to shape the markets that they claimed to describe (MacKenzie and Millo, 2003). The model was created as a guide to direct traders' buying and selling securities. Over time, with more and more traders following the instructions given by the model, the market actually shifted to fit the model.

Business models play a similar role within firms, and the wider ecosystems in which firms operate. A business model provides a standardized normative recipe and directs the activities of those working with the business model. Business models tend to be ideal types that may never be instantiated in reality but provide ongoing inspiration for improvement and change. For instance, the ongoing and never-ending efforts to reduce cost at Ryanair, the European budget carrier, are legendary. When Ryanair was at the brink of bankruptcy in the early 1990s, the adoption of the 'budget airline' business model provided ongoing guidance for business transformation and eventually became reality (Casadesus-Masanell and Ricart, 2008). The result is that what was once a fanciful representation can actually begin to generate its own reality.

Business models can become locked in and reinforced when they are become entrenched within managers' cognition or even across organizational fields. Studies of managerial cognition suggest that managers deeply immersed into existing industry or firm specific thought templates are reluctant to engage in de-framing and reframing. For instance, Polaroid Corporation failed to successfully enter the market for digital cameras even though it had developed leading edge technology in the digital imaging field (Tripsas and Gavetti, 2000). Senior management was able to develop new beliefs only to the extent that they were consistent with the 'razor and blade' business model underlying instant photography. This meant they were unwilling to shed features that it saw as salient.

Conclusion

We have argued that the concept of business models constitutes an important addition to the long debate about technology and contingency that Joan Woodward (1965) opened up. The debate about business models suggests that structural contingency considerations need to go beyond organizational features. This involves examining

how choices are made about how a firm relates to is ecosystem of customers, suppliers and partners. In this way, technology is not just bound up with organizational structures, but also with how an organization chooses to position itself within its broader environment. Our contribution is to suggest that business models are performative representations that business agents deploy for this purpose. We believe our approach delivers a more useful and appropriate conceptualization of business models. It avoids the problems of naturalistic approaches that focus on how match specific technologies to business models, and how in turn the technology-business model configuration impacts on performance.

We have argued that business models should be approached as performative representations. As a discursive construct deployed by managers, journalists and investors, such representations have three main qualities: they constitute narratives designed to convince constituents of the quality of a firm's business, they are typifications that create a sense of legitimacy around the venture, and they are a recipe that instructs constituents about what exactly they should do. Following our approach, the study of business models should seek to examine more deeply the narrative work which is used to convince particular constituents, the processes that underlie the emergence of certain well-recognised and legitimate types, and the conditions under which business models as recipes might or might not direct the activities of constituents.

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