

Migration Paths in Business Model Innovation of Small Enterprises Three Cases from Colombia

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Abstract

Business model innovation is still a subject of debate. Moreover referring to Small and Medium Enterprises (SMEs) from developing countries, where research is scarce despite the general acknowledgment of them as natural innovators. Current literature provides definitions and concepts, however time is briefly discussed and authors seldom build on each other. This study integrates previous developments into a single tool that helps three Colombian small enterprises to elaborate a blueprint of their business model, pointing out past, current and future innovative aspects. In turn, managers identify the innovation mode they have engaged in at various points in time. Consequently, results reveal a Business Model Migration Path (BMMP) along different components of the business model, and a Mode Migration Path (MdMP) pertaining resultant innovation modes, both with particular cyclic behaviors that open further research issues. In sum the study evidences the relation between a dynamic business model innovation and a small firm's sustained value appropriation and eventual success. Overall, it delivers an additional instrument to periodically review the company's business model, seeking for innovation opportunities, and anticipating possible consequences.

Introduction

In recent years studies have concluded that the success of a company not only resides on an efficient process or an attractive product design, but also on an effective business model that generates profitable returns. (Lin, Ke, and Whinston, 2008). Withal, there is no widely accepted definition of what “business model” really means (Casadesus-Massanell & Ricart, 2007); yet, companies can only survive by continuously reinventing it (De Reuver, 2008). Paradoxically, in many cases managers are not always capable of communicating their business model in a clear way (Linder & Cantrell, 2000). In addition, the relationship between business models and time is little discussed and authors rarely build on each other (Osterwalder, Pigneur, and Tucci, 2005).

Furthermore in many cases innovation has been analyzed mainly within the context of large, multinational, technology firms (Chesbrough, 2003); nevertheless, there is only little research made on business models of SMEs (Nissilä, Salmivalli, Suomi, and Puhakeinen, 2004), even though they are active and natural innovators (King & Ockels, 2009). In this sense, SMEs cannot be ignored as they play an important role by their contribution to both employment and economic growth (Nissilä et al., 2004), even in developing and emerging markets that can also

drive innovation (Kramer, Jenkins, and Kats, 2007). Accordingly, this study aimed to determine first, if a conceptual tool, which results in a blueprint of the company's business model, would allow managers to point out past and current business model innovations, and to foresee which aspects of the business model could be innovated in the future; and second, if those innovations were related to a specific innovation mode. Correspondingly, the present research focused on combining previous concepts and developments to analyze the business model innovation scenario of three small enterprises in Colombia over time.

Theoretical Background and Hypotheses

Business Model Innovation in SMEs

In their study, Osterwalder et al. (2005) define the business model as a conceptual tool with the objective to express the business logic of a specific firm. In this sense they propose four pillars comprising nine blocks to help managers and companies specify their conceptual business model: Product (Value Proposition), Customer Interface (Target Customer, Distribution Channel, and Relationship), Infrastructure Management (Value Configuration, Core Competencies, and Partner Network), and Financial Aspects (Cost Structure and Revenue Model). Furthermore, these pillars and blocks could be considered an expansion of the description found in Mahadevan (2004), of three dimensions: What (Value Proposition), Who (Target Customers) and How (Value Delivery System), being the core elements of a business model; in addition, he defines business model innovation as a strategic initiative to configure or reconfigure various elements pertaining to these three dimensions to enhance value creation potential of the firm and sustain it over a longer time. He portrays five main categories of innovating firms: Deterrence mode, War mode. Trend setters, Imitators, and Followers; and he argues that firms possibly migrate from one mode to another over time.

Commonly, SMEs started focused on creating an innovative product or service, once they have grown as far as they can without efficient business processes and practices, they need to analyze their business model to identify ways to innovate them into business strengths instead of business roadblocks (Lenz, 2003). In general, innovation is a process rather than a single event (Jenkins, 2009), and in the contemporary innovation landscape, smaller firms take a more prominent role but they are nevertheless left out of the research (Vrande, Jong, Vanhaverbeke, and Rochemont, 2008). Moreover, contemporary business model planning does not fully adjust into the needs of SMEs (Nissilä et al., 2004). Furthermore, research studies regarding Business Model Innovation in SMEs in Colombia are practically non-existent, and unfortunately, there is no up to date information, official data source, or a continual measuring process regarding behavior of industrial establishments; still, SMEs are and will be an important mainstay for Colombian economy as employment generators, as wealth re-distributors and as contributors to national gross product (Giraldo & Daza, 2009). In summary, the following hypotheses comprise the main focus of the present study:

H1: The use of a simple conceptual tool that enables Colombian SMEs' managers to depict a blueprint of their company's business model, allows them to identify previous and current innovations within the components of the business model, and to conceive which aspects of the business model could be innovated in the future.

H2: The business model blueprint permits managers to outline migration paths in terms of which components of the business model were, are, and will be innovated; and along business model innovation modes over time.

Procedure for Collecting Data

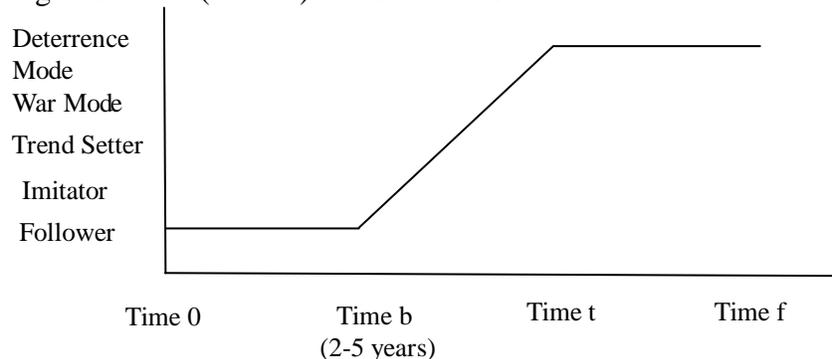
Three firms from different sectors were selected for the study: a young startup, a developed organization that is actively innovating its business model, and a mature company that has stopped modifying its business model. All three managers were asked to consider the following points in time: Time 0 (the time when the company entered the market), Time b (any point or points in time between Time 0 and today), Time t (today), and Time f (short term future: anytime within the next 5 years). The interview asked managers to first describe their company's business model at Time 0, in terms of what they did, how they did it and who their customers were. Subsequently they were asked to identify, if any, innovator elements, and to point out they resultant innovation mode. Afterward, managers were asked if they could identify one or more points in the past, where innovations had taken place; if positive they were asked about the time when that happened (2-5 years, 5-10 years, or 10-20 years after Time 0). A similar inquiry about innovations and their classification was done considering Time t. All the same, for Time f managers were prompted if they could identify possible ways to innovate in the future and to predict what could be the innovation mode then. Furthermore, managers completed a questionnaire and were interviewed in order to obtain in depth information. A survey research method was used; it combined open-ended questions when inquiring about what the company does, how it is done and who its customers are, and close-ended questions, when referring to the identification of innovation modes. This fact led to a qualitative research that may yield rich description and explanation of the processes (Mair & Marti, 2004). Participants were offered an article with the results and conclusions from the study.

Results

Case One – Fromcolombia Ltda

In 2003 Fromcolombia Ltda. entered the furniture export sector in Colombia, its initial business model depicts the dynamics of the business model innovation from the very early stages of a small enterprise, and it is summarized through Table 1.

Figure 1. Mode Migration Path (MdMP) – Fromcolombia Ltda.



Originally, its manager believed the company to be an imitator, but in fact, after creating the company's first business model blueprint, he situated the firm as a follower instead. He realized that it diverged from its competitors in terms of “Who” the company did business with,

more specifically in its Customer Interface and to be punctual in the Distribution Channel that was employed. In this sense, Table 2 depicts the firm's Business Model Migration Path (BMMP), this means how the firm has modified and plans to continue doing so, the components of its business model along time, looking forward to differentiate itself from other enterprises in the sector and to remain competitive.

Table 1. Business Model Building Blocks and Description of Initial Business Models

Business Model Building Block	Description Fromcolombia Ltda.	Description Universal de Carga S.A.	Description La Bonanza
Value Proposition	Furniture	Land transportation of liquids	Beef, pork, and entrails
Target Customer	Furniture retailers in Australia	Fuel and lubricants companies	Homes, restaurants and schools
Distribution Channel	Sales through commissioners	Personal visits to customers	Retail shop
Relationship	Commercial agreements with retailers	Commercial agreements with customers	Commercial relations based on good customer service
Value Configuration	Two persons in charge of finding appropriate providers	Compliance with legal regulations and availability of the vehicles	Location of the shop, cash availability, knowledge of the processes and necessary tools
Core Competencies	Knowledge of the sector, expertise in international trade, trustworthy contacts abroad	Availability, quantity and quality of the vehicles used for transportation	Ability to negotiate cattle, carcasses, and butchering services
Partner Network	Favorable payment terms agreed with providers	Agreements with customers, cargo in exchange for consumption of their products	Relations based on punctual payments
Cost Structure	Low administrative costs	Excellent cash-flow, obligations paid on time	Excellent cash-flow, products that compensated profit margins that others lacked
Revenue Model	Buying from good low priced providers and reselling abroad	As an intermediary for transportation services	Live cattle and carcasses bought, transformed and resold ready for consumption

This firm indeed, poses itself as an active innovator and in fact, each one of the decisions taken to innovate its business model, results in a corresponding innovation mode. Nonetheless, it can be noted that recurrent innovations within the same building block may relate to different innovation modes, and similarly, innovations in different building blocks may as well lead to the same innovation mode.

Table 2. Business Model Building Blocks and Innovations Over Time (Business Model Migration Path BMMP– Fromcolombia Ltda.)

Business Model Building Block	Innovation Time 0	Innovation Time b (0 – 2 years)	Innovation Time t	Innovation Time f
Value Proposition		Switch from exports to imports	Improve product design	

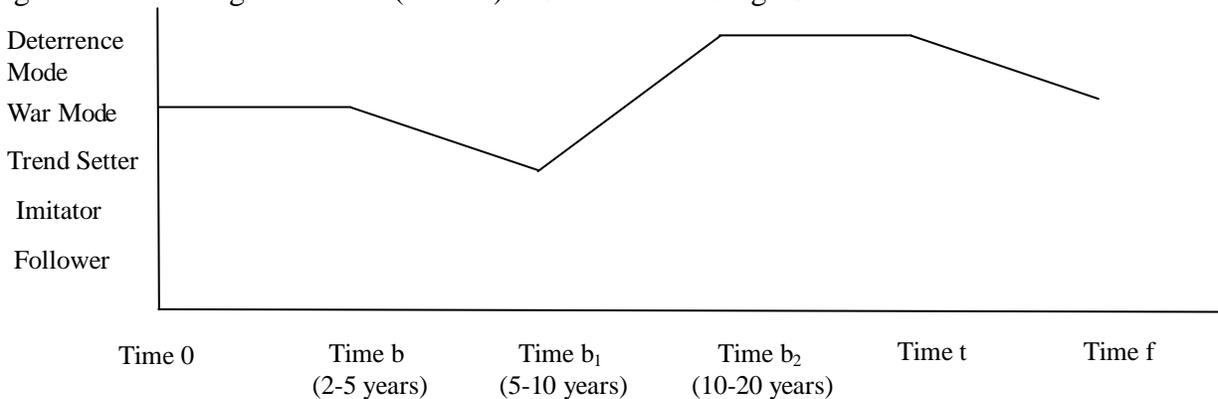
Figure 1 portrays the company's Mode Migration Path (MdMP), which is how the firm has migrated, and plans to continue doing so, along the five business model innovation modes.

Case Two – Universal de Carga S.A.

With the French oil company Elf Aquitaine as its only customer, Universal de Carga S.A. was founded in 1982. Table 1 outlines the original business model of this cargo transportation firm that was selected for this study because it depicts what could be considered a successful Business Model Migration Path. Even though research on what exactly is a “good” or “weak” business model is still in its infancy (Osterwalder et al., 2005). Universal de Carga S.A. began its BMMP in terms of “How” they did business, as it can be observed in Table 3. Moreover, in relation to the Value Configuration of the Infrastructure Management pillar. At the same time, this innovation links up with being a war mode innovator, suggesting though that the firm started its innovation process on the right foot, as this particular mode often employed by new enterprises, helps a firm not only appropriate value, but also prevent the competition from imitating for a period of time (Mahadevan, 2004). In a similar way, the second step of the BMMP involves an innovation regarding the “Who”, specifically the Target Customer building block of the Customer Interface pillar. Consequently, the firm's manager also associates this move with a war mode of innovation and it reinforces the argument presented in the previous case: innovation in different business model construction blocks may or may not lead to the same innovation mode.

All the same, the next decision to innovate an aspect of the business model takes place in reference to “What”, that is the Value Proposition or Product the company deals with, and it situates the firm as a trend setter. The company's following innovative decision however, allowed it to evolve from being a trend setter to a deterrence mode of innovation. Accordingly, this decision relates to a new innovation of the “How”, and specifically the Value Configuration of the Infrastructure Management, which by the way, was the starting point of the BMMP of this case.

Figure 2. Mode Migration Path (MdMP) – Universal de Carga S.A.



Presently, the firm is innovating regarding its “How”, but in reference to the Financial

Aspects and to be specific to the Revenue Model. This fact, which according to the manager still keeps the firm on a deterrence mode of innovation, suggests that small enterprises focus on innovating their Customer Interfaces and Products, and when they have been able to achieve a high degree of sustainability they look for other strategies, involving other aspects of their business model. Anyhow, a future innovation concerning the “How”, but in regards to the Partner Network closes a cycle that implies the return of the BMMP to the same pillar where it began. Furthermore, the company's manager states that this innovation would send the company back to a war mode, strengthening the idea of a cycle completion.

Table 3. Business Model Building Blocks and Innovations Over Time (Business Model Migration Path BMMP – Universal de Carga S.A.)

Business Model Building Block	Time 0	Time b (2–5 years)	Time b ₁ (5–10 years)	Time b ₂ (10 – 20 years)	Time t	Time f
Value Proposition			Additional modes of transportation			
Target Customer		Diversification of customers				
Distribution Channel						
Relationship						
Value Configuration	Quality and quantity of vehicles			ISO Certification		
Core Competencies						
Partner Network						Alliance with a customs broker
Cost Structure						
Revenue Model					Credits offered to customers	

In synthesis, the firm has innovated five of the nine business model building blocks; its BMMP has gone through all the business model dimensions and pillars. Undoubtedly, it constitutes a clear example of the flexibility and adaptability of small firms. Accordingly, its MdMP fluctuates mostly between war and deterrence mode, as it can be observed in Figure 2. In any case, this company has been able to appropriate value over a relatively long period of time, and it has achieved an important degree of sustainability. It has become a leader in its sector and its manager still has the vision to dynamically cope with the ever-changing business environment.

Case Three – La Bonanza

La Bonanza was founded 25 years ago as a small retailer of meat and meat products. Its founder envisioned several aspects that if modified, could differentiate him from his competitors, so he took the chance and the company started operating with only one employee and very scarce resources. Nevertheless, without the conceptual tools used in this research, the company's owner had difficulties trying to describe his initial business model, however after inquiring about each component of it throughout the interview, the whole picture came out, as shown in Table 1.

La Bonanza displays a peculiar BMMP that proved itself promising and successful during the company's first decade. Initially, the firm began innovating in regards to Relationship, which belongs to the Customer Interface pillar and to the “Who” of the business. In this sense, according to its manager the company was a trend setter, and coping with Mahadevan's description, it portrayed a high degree of differentiation evolving into a war mode afterward.

Table 4. Business Model Building Blocks and Innovations Over Time (Business Model Migration Path BMMP– La Bonanza)

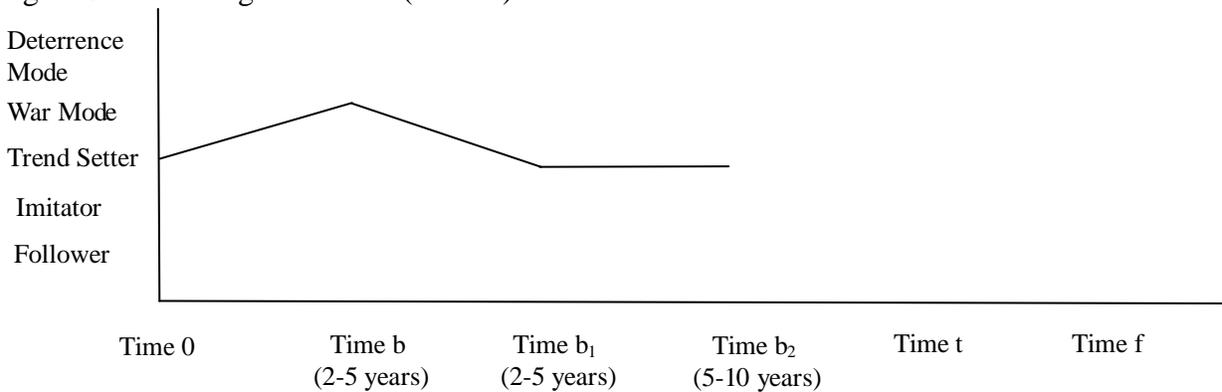
Business Model Building Block	Time 0	Time b (2–5 years)	Time b₁ (2–5 years)	Time b₂ (5 – 10 years)	Time t	Time f
Value Proposition		Inclusion of chicken and delicatessen				
Target Customer						
Distribution Channel				Publicity, visits to customers, and delivery		
Relationship	Outstanding customer service					
Value Configuration			Relocation, improved facilities, machinery and training			

Correspondingly, this firm also innovated its Product right after its Customer Interface; its Value Proposition was then the main differentiating factor. All the same, its subsequent innovation relates to “How” the company was operating, the Value Configuration of the Infrastructure Management pillar was substantially modified, placing the company on a trend setter mode one more time. Nonetheless, the next step of the BMMP displays an innovation in terms of, once again, “Who” the company regarded as customers, moreover this change of the

Customer Interface pillar has to do with the Distribution Channel. However, after the firm's first decade, the business model of La Bonanza has remained practically static, what seemed to be a prosperous and ongoing innovation process, has progressively decayed and is currently facing obstacles that appear to be impossible to overcome.

In summary, La Bonanza has innovated three of the four pillars of the business model, doing it as well in a cyclic manner. However, it did not innovate repeatedly any of the building blocks, as it is shown through Table 4. Withal, in this particular case an innovation in three different aspects has resulted in the same innovation mode, which unluckily for the firm implies a low degree of sustainability despite its high degree of differentiation. After several years without any substantial adjustments in its business model, La Bonanza has fallen behind its competitors, all the revolutionary elements that were once the company's battle horse are long gone, and at the moment daily activities are just enough to break even. The future, though, does not present a better landscape according to the company's manager, at this point, he assures, it could be more profitable to even shut the shop down and rent out the property. Consequently, the MdMP depicted in Figure 4, has been truncated after ten years of commercial activity due mainly to tortuous relations with business partners who are also family members.

Figure 3. Mode Migration Path (MdMP) – La Bonanza



Analysis of Results and Further Research

Cross – case analysis

The BMMP of each one of the cases begins by innovating a different aspect of their particular business model. Withal, at a certain point in time, all of them did it in regards to the Customer Interface pillar, and subsequently in relation to the Product pillar. Furthermore, this concurrency suggests, that in small enterprises an innovation of the Customer Interface tends to be followed by one of the Product, following the affirmation of Schlenker and Crocker (2003), that the vast majority of SMEs do not create their market, but rather just react to their clients' demands. Further research however, could confirm if an innovation of the Customer Interface, leads to clients' demands that can be interpreted as a requirement for a Product innovation, or if the choices to innovate from Customer Interface to Product, complement each other well and could be understood as a reinforcement (Casadesus-Masanell & Ricart, 2007), that small enterprises tend to pursue naturally. Moreover, it could shed some light on how other pillars and blocks are affected when a specific one is innovated.

Anyhow, all three BMMPs present a cyclic behavior; Fromcolombia Ltda. first innovated

its Customer Interface, followed by two Product innovations and plans to innovate, once again, the Customer Interface in the near future. In a similar way, Universal de Carga S.A., innovated in relation to the Infrastructure Management, subsequently in regards to the Customer Interface, then in terms of the Product, and it also returned to innovate the Infrastructure Management. All the same, the BMMP of La Bonanza went through Customer Interface, Product, Infrastructure Management and it ended up with another innovation pertaining the Customer Interface. In sum, Universal de Carga S.A. as well as La Bonanza, both show a BMMP along all of the business model pillars. Nonetheless, La Bonanza has ceased its business model innovation dynamic, and in this sense, additional studies may focus on the identification of factors that drive SMEs to stop innovating their business model over time, as a way to prevent managers to fall in those pits. Fromcolombia Ltda. in turn, is still a very young company; however, its early BMMP indicates a strong tendency to innovate in terms of Customer Interface and Product. This fact may suggest that Financial Aspects are less likely to be modified during the first years of operation, when a firm is still starting to go through a cycle of initial value creation, value shrinkage and value migration (Mahadevan, 2004). Nonetheless, additional research is required to validate this affirmation.

The MdMP of the three cases also shows some occurrences. In contrast to Fromcolombia Ltda. that began as a Follower, Universal de Carga S.A. began as a War Mode innovator, and La Bonanza as a Trend Setter, the latter two portray a cycle that after some time returns them to the initial business model innovation mode. An insight look to these cycles pertaining the MdMP and the BMMP, is still necessary in order to clarify issues like what factors drive them, when is the right time to migrate from one mode or pillar to another, and which, if any, are the most appropriate migration paths for small firms in a specific sector. Additionally, the continuing business model innovation process of the studied companies is carried on by first making decisions regarding particular aspects of the business model, and then recognizing a consequent innovation mode. However, additional studies may consider if it is viable to begin the other way round, which is, specifying the desired innovation mode first, and accordingly formulating an appropriate BMMP. Accordingly, ample research in specific sectors and countries is needed, in order to elucidate if it is feasible to establish common Business Model Migration Paths and Mode Migration Paths, that increase the possibilities to appropriate value over time and to achieve the sustainability that all managers should crave after.

Conclusions

Two migration paths were identified and correspondingly defined as Business Model Migration Path and Mode Migration Path. However, no elements additional to the nine blocks proposed by Osterwalder et al. (2005) were identified. Additionally, since the business model innovation of SMEs seems to depend on the specific situation and opportunities regarding a particular industry and the company itself, the Mode Migration Path and BMMP of the three cases differ from each other, however some coincidences were still found. Yet, more extensive sampling and in depth studies of SMEs from specific sectors are imperative. In synthesis, even though the conceptual tools used in this research help managers get an insight of their enterprise's historical development, in practical terms they are also tools for the present and the future. Furthermore, they may be used as instruments to periodically review the company's business model scanning for innovation opportunities and to predict what will be the consequences within the business model, and which innovation mode will the company engage

in, after the choices have been made. Furthermore, the present study illustrates how the BMMP and the MdMP can be traced from the early stages of a firm, proposing that business model innovation can be taken care of from the very beginning; it argues that recognizing aspects in which the company has innovated in the past, is currently innovating, and could innovate in the future, constitutes a powerful tool for managers to pursue sustainability and to appropriate value over time; and finally it exemplifies how a stoppage in the BMMP plays a determinant role in the sustainability of a company. Moreover, several directions in which further research may be of great use are pointed out, all of them converging in finding tools to maintain the kinetics of the business model innovation process, which clearly constitutes a decisive factor in the eventual success of a firm.

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