

Chapter 19

Business Model Innovation

Netflix changed the video industry and drove Blockbuster into bankruptcy. Zipcar is emerging as a credible substitute for owning a vehicle. Both of these companies started by offering a service that differed substantially from what was the norm, not only in terms of what service customers were offered, but also in how each company delivered its service. Both are innovators and, in particular, both are examples of *business model innovation*—a term that has become a recent buzzword, used to explain the success of a number of rapidly growing businesses.

To be complete, one should acknowledge that such radical innovations are by no means a recent phenomenon. Dell revolutionized the computer industry over the course of the 1990s, a time period in which Southwest Airlines redefined air travel. One might even argue that Gottlieb Daimler and Henry Ford redefined transportation and forced many producers of horse carts out of business. Nevertheless, modern technology has surely enabled a steady stream of business model innovations in recent times.

The purpose of this chapter is to understand the forces behind such new business models. Instead of compiling a set of buzzwords and anecdotes, we want to present a solid framework that helps you understand and create new business models. Not surprisingly, given the title of our book, our framework is based on the idea that a firm can increase its profitability by identifying new and better ways in which it can match supply with demand. More specifically, in this chapter, we aim to explain:

- The economic forces behind the new business models of Netflix and Zipcar.
- The different ways in which a firm can innovate and which of these innovations classify as business model innovations.
- How a new business model can increase customer utility and often draw a new set of customers into the market.
- The ways in which a firm can leverage its operations to deliver on this utility while maximizing its profitability.

19.1 Zipcar and Netflix

In case you are not familiar with Zipcar and Netflix, this section describes what they offer and how they offer it.

Zipcar is a car-sharing company that was founded in 2000. Within 10 years, the company grew to an 8,000-vehicle fleet that serves a customer base of some 560,000 members. Members