Business Model Innovation for Cultural Organizations

(Beta version)

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"In order to change an existing paradigm you do not struggle to try and change the problematic model. You create a new model and make the old one obsolete". Richard Buckminster Fuller (1895-1983), architect and designer.

1. The knowledge-based economy

We live in a dynamic and increasingly complex world in which globalization and the rapid development of information technologies during the last decades have meant a shift in Western economical structure from a traditional product-based manufacturing towards a knowledge-based economy in which services and innovation are occupying a more decisive role for social and economical development than ever before.

A possible definition of knowledge-based economy says that it is a system of production and consumption in which intellectual capital is the main resource and the value of both organizations and individuals is based on intangible assets (as opposed to physical capital, natural resources, low skill labour, etc.). This type of economy is therefore based on the role of knowledge and information technology –as an enabler of knowledge distribution– in driving productivity and economic growth.

Some of the features contained in a knowledge-based economy are:

a) An economic and institutional model providing incentives for the efficient creation, dissemination, and use of knowledge, in order to promote growth and increase social welfare;

b) Highly educated and skilled workers able to create and use knowledge;

c) An innovation system composed of companies, universities (and other research centers) and other organizations that are capable to transform knowledge into valuable products and services;

d) A dynamic information-infrastructure capable of facilitating the effective communication, dissemination and processing of information.

Redefining the parameters of a traditional economic system, a knowledge-based economy emphasizes the relevance of innovation as a key feature to respond to future challenges. And, as other sectors, the cultural and creative sectors are also highly influenced by macroeconomic forces. Borders don't exist anymore for the global economy and the world is an open space where companies are free to operate in increasingly interdependent contexts.

Within the context of a knowledge-based economy, the development of new technologies of reproduction and communication, together with important sociocultural changes, has accelerated the production of cultural products in the last hundred years. And an increased demand for cultural products and services as well as new forms of entertainment has helped develop the creative and cultural industries in the last decades. As the importance of culture increased, so it started to be seen as a potential economic resource and the sector began to develop arguments about managerial efficiency and economic benefits in terms of employment, tourism, image enhancement and positive externalities.

2. Major challenges for cultural organizations

One of the driving forces of the globalization processes is technology, and internet has its major product and catalyst in the last decades. Nobody can deny nowadays that Internet has had a huge impact on cultural and creative industries, causing critical disruptions that have completely shifted the environment in which creative professionals and organizations operate leading to both fear and excitement in the sector.

If digital technologies have democratized the content production by allowing more amateurs to produce creative contents at very low cost and obtaining almost professional results, Internet has succeeded in increasing connectivity and simplifying content distribution processes thanks to the Web 2.0 tools. The direct impact of these two facts is a more participatory culture in which the line between producers and consumers of cultural digital contents has blurred, and the same thing has happened with the amateur/professional dichotomy. The immaterial nature of a great part of creative contents and its easy digitalization has favored its globalization and reduced restrictions to its access. Digital technologies have brought into being new types of content creators, new distribution channels and new audiences without the geographical constraints of the past.

The recent global economic turndown has also had an impact on the European cultural sector. Many assumptions and beliefs about the relationship between the arts and the government, as well as the funding models of cultural organizations have been challenged.

In this challenging context, in which changes happen faster and faster and no one can predict them, there is a vital need for an attitudinal shift in leaders of cultural organizations. They have to accept that they don't work anymore in a more or less predictable context and that if they want their organizations to survive they will have to avoid inertia. They will have to develop organizations with very clear and strong missions, goals, values and attitudes that will allow them to navigate in a constant-change sea. Resilience and innovation are key factors to exploit emerging opportunities, and strategies will have to adapt constantly in order to keep the organizational boat afloat.

However, even if considerably affected by the economic situation, the relevance and potential of the European cultural and creative industries should not be underestimated. As it proves the study presented by the Forum d'Avignon and TERA Consultants in 2014 regarding the economic contribution of these sectors to the economy, in 2011 the core creative industries in the 27 countries of the European Union generated approximately 4.4% of total European GDP and they represent approximately 8.3 million full time equivalent jobs, or 3.8% of total European workforce.

Technology and globalized markets provide opportunities for the cultural and creatives industries at national and international levels, but these also can find immense opportunities at local and regional levels, as they can contribute to sustain urban development, boosting local economies, creating jobs and supporting other industries development through cross-sectorial cooperations.

The main challenges for cultural organizations result from the fact that they are –generally speaking– under-managed and under-capitalized. Apart from external factors as intellectual property issues that are of capital importance but not the topic of this publication, cultural organization face an urgent need to:

1. Build new skills and capacities.
2. Identify new funding and financing streams.
3. Develop new cross-sectorial relations.

These three challenges bring the focus of cultural organizations to develop new sustainable business models and, in order to do so, they must become more innovative. If innovation is not an easy task, not even for organizations in other industries, shifting business models is even tougher, since managing this transition requires a high level of leadership and management skills to keep the organization going under the traditional business model while adapting to a new business mode that is still under development.

Culture and economy collide

Since first austerity measures that followed the recent economic crisis, governments have urged cultural organizations to focus part of their creative and innovative capabilities towards business innovation in order to adapt to new circumstances. The "creative" sector *par excellence*, the cultural sector, is asked to be creative and entrepreneurial if it wants to live under the rules of the new economic paradigm.

However, the relation between culture and economics as disciplines is not new. These approached for the first time in the 1960's when the government of the United States started analyzing the efficient utilization of public funds by beneficiary organizations and the legitimacy of state intervention in the cultural sector. In Europe, the relationship between culture and economy was developed in the late 1970's and early 1980's when governments examined the role of public expenditure in the cultural sector within the context of the early 1980's recession.

In the same decade, the business sector started to draw great attention to the importance of culture in organizational change. In this context, the term *culture* is understood as the sense of identity and the way that things are done (values, stories, beliefs, norms, etc.) inside an organization. Culture –as it is understood in this context– impacts on every aspect of business behavior and it is a key factor determining business success. An organization without a culture engaging employees at work cannot compete and respond to economic changes. Some authors called this process "culturalisation of the economy".

3. What's innovation?

Nowadays everybody talks about innovation as it was the newest thing, but innovation is as old as humankind. Humans are naturally driven by curiosity and an unlimited desire to explore and improve the world. And basically, innovation is a process of practical problem-solving that results in some kind of impact at society or market levels. To exist, innovation requires creativity, which is seen by most expert in the field as the process of developing ideas that are novel or original.

One of the most influential economist of the twentieth century, Joseph Schumpeter is the precursor of the concepts of innovation and entrepreneurship as we understand them today. In 1942 Schumpeter developed a theory explaining why innovation is the most critical dimension in economic development and change in capitalist economies. The seek for profits and the threat of the competitors forces entrepreneurs and companies to continually innovate without cease in a process called "creative destruction" –inherited from the marxist theory– that Schumpeter popularized as the essence of capitalism and described as "a process of industrial mutation that incessantly revolutionizes the economic structure from within, incessantly destroying the old one, incessantly creating a new one". For him "carrying out innovations is the only function which is fundamental in history" and the entrepreneurs –Schumpeter was probably also the first economist to theorize about entrepreneurship– are the agents that drive innovation and economical development by "doing things that are already being done in a new way".

In order to better explain the innovation concept, Schumpeter divided the innovation process into four dimensions: invention, innovation, diffusion and imitation. The invention process encompasses the generation of new ideas. The innovation process is about the development of new ideas into marketable products and processes. The diffusion process is when new products and processes spread across the potential market and start to be imitated by competitors.

Schumpeter's theories are still relevant and they have great resonance with students and businesspeople today. Several economists have stated that the 21st century is going to be "the century of Schumpeter" and they don't seem to lack reason when we see everywhere that innovation and entrepreneurship are seen by governments and companies all around the world as the most effective treatment leading to economic recovery after the financial disaster.

Since the term "innovation" started to get massive attention in the 1950's, companies explicitly embraced it due to the key role that it could play in their businesses as a way to crush competitors and grant them a leading position in their industry. However, now we know that for any type of organization –not just companies– innovation represents a great opportunity not only to survive and develop but also influence the direction of its sector and to have a positive impact in society. Innovation has proven to have major impact in social issues in the form of social innovation, which has been defined as "the process of inventing, securing support for, and implementing novel solutions to social needs and problems".

4. Types of innovations

Inspired on the idea of "creative destruction", other authors articulated innovation theories such as the s-curve discontinuity, radical innovation, etc. to explain how innovation affected existing markets or created new ones. Basically, an innovation can fall into one of the next three categories: It can improve, it can renew or it can disrupt. Let's see them on more detail.

In the late 1990's and early 2000's, Clayton Christensen, professor at Harvard Business School, classified innovations into three different types:

1. Efficiency innovations: Those that produce the same product but more cheaply, such as automating credit checks. This type of innovation doesn't involve much risk, usually fits the current business model of the organization and doesn't affect existing markets.

2. Sustaining innovations: Those that turn products or services into better ones. These enhancements help keeping a business competitive, such as new product features and service improvements.

3. Disruptive innovations: Those that bring to a market a very different value proposition than the ones that had been available previously. This type of innovations develop new value propositions and help to create new markets.

These three types of innovations can be applied to a number of areas in any organization, that at their most basic are:

Products or Services: The introduction of an improved version of a preexistent product or service, or totally new goods or service.

Processes: Innovation in this area involves changing internal processes in order to make them more efficient.

Organization and governance: This area of innovation focuses on decision-making processes as well as on organizational dynamics and structure.

Business model: To innovate in the way an organization creates, delivers and captures values is a very challenging and risky endeavor because it requires to change the main principles upon which an organization operates. Business model innovation also entails changes in the organizational processes.

In 2011 the innovation consulting firm Doblin made public the method it had been using to help its clients innovate for the last fifteen years. It offers a quite comprehensive framework for systematically tackle innovation inside any organization and is a key tool for innovators all around the world. The method takes into account ten areas of innovation and what follow is a summary of of them as Doblin defines them:

Configuration:

1. Business Model: *How the organization makes money.* It is about finding a fresh way to convert an organization's offerings and other sources of value into cash. Great ones reflect a deep understanding of what customers and users actually cherish and where new revenue or pricing opportunities might lie.

2. Network: *How the organization connects with others to create value.* In today's hyper-connected world, no organization can or should do everything alone. Network innovations provide a way for firms to take advantage of other companies' processes, technologies, offerings, channels, and brands —pretty much any and every component of a business.

3. Structure: *How the organization distributes and aligns talent and assets*. Structure innovations are focused on organizing company assets — hard, human, or intangible — in unique ways that create value. They can include everything from superior talent management systems to ingenious configurations of heavy capital equipment.

4. Process: *How the organization uses signature or superior methods to do its work*. Process innovations involve the activities and operations that produce an organization's primary offerings. Innovating here requires a dramatic change from "business as usual" that enables the organization to use unique capabilities, function efficiently, adapt quickly, and build market–leading margins.

Offering:

5. Product Performance: *How the organization develops distinguishing features and functionality.* This type of innovation addresses the value, features, and quality of an organization's offering. It involves both entirely new products as well as updates and line extensions that add substantial value.

6. Product System: *How the organization creates complementary products and services.* This type of innovation is rooted in how individual products and services connect or bundle together to create a robust and scalable system.

Experience:

7. Service: *How the organization supports and amplify the value of its offerings.* Service innovations ensure and enhance the utility, performance and apparent value of an offering.

8. Channel: *How the organization delivers its offerings to customers and users*. encompass all the ways that connect the organization's offerings with its customers and users.

9. Brand: *How the organization represents its offerings and activity*. Brand innovations help to ensure that customers and users recognize, remember, and prefer your offerings to those of other organizations operating in the same field.

10. Customer Engagement: *How the organization fosters compelling interactions.* These innovations are all about understanding the deep-seated aspirations of customers and users, and using those insights to develop meaningful connections between them and the organization.

5. Innovation drivers

Knowing that innovation is essential for organizations to adapt to new circumstances and to improve the value they deliver to their customers and users, why only few organizations actually innovate and even less succeed on doing so? The answer to this question is that there are some factors that prevent innovation from occurring: The fear of risk and its consequences, the lack of a culture of innovation, a limiting focus on short-term results, the lack of time, the lack of resources or staff, the lack of knowledge and a systematic approach to innovation, etc. In addition, many organizations don't really know or understand the actual needs of the people or organizations they are serving.

In opposition, if an organization is really committed to innovate, there are four key areas they might focus in order to drive innovation:

Leadership: The leaders and the organization itself have to be aligned around the importance of innovation. Leaders and managers need to be open to new ideas and their implementation not only in their words but also by allocating time for them to reflect and work on innovation and by providing their team with the time and resources to do the same. If leadership lacks the right spirit an motivation, any innovation effort will surely be doomed to fail.

Culture and values: An organizational culture that prioritizes openness and collaboration and is not afraid of risk and failure will have more chances to succeed on innovation. Consider failure as an approach to exploring new opportunities for the organization and try to avoid stigmatizing unsuccessful risk takers.

People and skills: Innovation goes beyond individuals, it is a social process, and it should not be restricted to a selected group of people within the organization. The more employees are involved in the innovation efforts of the organization, the better the results will be. All people contributing to the mission of the organization can be creative and you never know where a good idea will spark. The talent within the organization has to be nurtured without exception. In addition to the commitment of the staff, innovation also requires the right competences to succeed and the organization have to invest in the innovation skills of employees (creativity being one of them).

Processes and tools: Innovation doesn't happen spontaneously but it requires a systematic approach and supporting tools to enable idea generation, management and elaboration. Within the innovation and creative processes, exploration, divergence and rectification are common paths and all critical assumptions should be tested before further development. Without the right processes and structures in place, the wrong ideas might be prioritized, conducing to waste time and resources.

6. Overcoming prejudices related to business models

In the last years we have witnessed a major shift in the world economy and consequently in the public funding of cultural organizations in Europe. In spite of this fact, many social and cultural organizations still resist to adopt some concepts and practices that would help them improve their management and impact with reduced dependency of public grants. This is the case of the business model concept, which brings the taboo word "business" into the cultural sector. Many cultural organizations proudly proclaim that they are not businesses and therefore business rules don't apply to their sector.

The truth is that behind the "business model" term lays a very useful tool for any kind of organization, no matter whether it is a business enterprise, a social company or a non-profit organization. If an organization has a way to create, deliver and capture value, it has a business model. And the most important characteristic of a business model is that it is viable and sustainable. Non-profit organizations, like for-profit organizations, need to provide with valuable products and services to their end users at the same time that they also have to provide some kind of value to their funders: governments, foundations or private donors. And they have to do it in a financially sustainable way, which requires to have a business model.

All organizations have a business model but it might happen that it hasn't been explicitly designed but rather adopted by unconsciously copying the model from other organizations in the same sector. This practice was quite common during the industrial era, in which business models were perpetuated long time until a major change –in most of the cases technology-driven– materialized and changed the playing rules of the sector. In the past business models were taken for granted and most of the organizations in the same sector used the same models. For them it was not so important to explicitly design business models, even if implicit business models innovation brought major advantages to some companies.

All this dramatically changed with the emergence of the internet and the eruption of online businesses, which were using a completely and revolutionary technology. At their first stages these internet start-ups needed to figure out how to make money out of it and that is the moment when business models were placed at the core of business innovation. Nowadays, social, economical and technological hyper-quick changes create a very unstable and unpredictable environment for any kind of organization and business models don't last as long as they used to in the past. New affordable technologies are letting new players emerge all around, and in many cases they radically refuse to play by the same rules of the industrial era. That's why business model innovation is a new strategic imperative for all organizations, including the ones operating in the social and cultural sectors.

In addition to this, it is worth saying that even the notion of hermetic sectors without interactions among them has become totally obsolete and the new contemporary paradigm requires all type of organizations –public, non-profit and for-profit– to cooperate and work across sectors and working fields in order to have a more holistic approach to reality and more efficiently tackle the pressing problems that our societies are currently facing at all levels: social, cultural, environmental and economic. This is not science fiction, but reality and it shows that the borders between sectors are fading and old-fashioned prejudices are quickly shifting into more tolerant patterns. In today's eclectic organizational environment we can find for-profit social enterprises pursuing the common good, non-profit organizations with for-profit legal structures and for-profit companies with very compelling social-responsibility policies.

7. Business model innovation

Business model innovation is a system-level or holistic activity when compared to other areas of innovation such as product or processes innovation. This means that it focuses on the organization as a whole. Essentially, business models innovation is about rethinking the way that an organization operates around a value proposition and how it consequently aligns its resources and processes in order to capture enough value so it can sustain its activity. Therefore designing or re-designing a business model requires creativity, dedication, a good understanding of the organization, the organization's (potential) customers or users, external opportunities, the strategy of other agents operating in the same sector, recently available technologic innovations, suppliers, etc.

Although risky in terms of results, business innovation is usually not a highly intensive capital activity and it represents a good opportunity for organizations to innovate, specially in times of economic or technologic change. It might sound counter-intuitive, but periods of economic turmoil and transition create significant opportunities. Organizations might take advantage of these circumstances to reduce their costs, revisit their portfolio of partners and collaborators, increase their focus on their essential activities, introduce new organizational practices and, obviously, rethink their value propositions and business model. In fact, if business models innovation doesn't occur it is more likely due to other factors such as organizational inertia, unaware leadership, lack of knowledge and skills among the staff, lack of incentives, high dependency on external resources, etc. rather than to its cost.

The business model innovation process is not only analytical or theoretical, but it should also involve challenging existing and new assumption in a practical way, through structured experimenting and testing. Finding the right new business model requires analyzing not only one but as many alternatives as possible. A trial-and-error methodology will prove whether assumptions will lead to a successful improved or new business model or not before the new model is implemented. Moreover, since what is sustainable today might not be tomorrow –funding streams dry up or shift focus, users habits change, etc.–, every business model should be considered provisional and organizations' leadership should keep a continuos proactive attitude towards business model innovation.

When redesigning their business model, many organizations will mainly focus their efforts on improving or changing their revenue model, but they should not forget that business model innovation is also about rethinking the value proposition that they are offering to their (potential) customers and users. In this sense it is fundamental to revisit the needs of consumers/users and the way that other organizations and organization itself are satisfying or not those needs, as well as the technological and organizational possibilities that might exist.

8. Business Models and non-profit organizations

For decades, the relation between non-profit organizations and governments has been considered complementary as both were seen as partners in carrying out the delivery of public goods. This is particularly true in the case of cultural non-profits working with certain artistic and cultural manifestations that would have never found the desired financial sustainability without sufficient funding from the public administration.

In fact, non-profit organizations are traditionally defined as bodies of individuals who associate for any of three purposes:

a) To perform public tasks that have been delegated to them by the state.

b) To perform public tasks for which there is a demand that neither the state nor commercial organizations are willing to fulfill.

c) To influence the direction of policy in the state, the for-profit sector, or other non-profit organizations.

However, as it has already been mentioned before, the lines separating for-profit and not-for-profit organizations are becoming increasingly blurred and probably their relationship with governments should be revisited.

In the case of non-profit organizations operating in the cultural sector, they have traditionally had some traits that even today could be considered as characteristic:

a) Their are driven by a mission and not by profits making.
b) They are quite dependent on public funding.

b) They have difficulties to generate surplus from their core activities.

c) They are undercapitalized and, if they have any reserves, they are usually very small.

Of all the above mentioned characteristics of the non-profit cultural sector, the most peculiar one is its high dependency on public funding and on governmental institutions to provide them with sufficient resources to implement their activities. This critical resources dependency has enormously influenced the sector's business models and has been proved to be high-risk option.

When governments at any level –local, regional, national or international– decide to change their funding priorities and, as we have recently seen in many European countries, reduce their financial support to the cultural sector, organizations have to find ways to adapt to the new situation. The financial cuts in culture have driven many cultural organizations into situations of a broken business model that will need to be redesigned in order to avoid dependency on a very limited number of income streams.

The first step when an organization finds itself in a completely new situation such as the current one –let's call it a new paradigm– is to analyze it and start by changing mindsets. This is probably the main challenge that many cultural organizations are currently facing and it is surely not easy for them.

The second step is to rethink the organization's business model in order to understand and clarify the processes underlying it. In the case of Europe, the enormous structural deficits that state and local governments are currently facing has already had their first direct consequences but the effects of the recession will also put in risk the public funding for the cultural sector in the years to come. Therefore, revisiting this traditional generated-income sources of cultural organizations becomes crucial. If income diversification was not a priority for them until now it will have to be the top one priority from now on. They will have to revisit their funding portfolio, diversify it and look at more innovative ways to generate income.

9. Beyond non-profits: Mission-driven organizations

The non-profit status of an organization is a choice of its founders and it is a voluntary one. The biggest difference between a non-profit and a for-profit organization is that the former has prioritized a mission –which is assumed to be of general public interest– over profit maximization. For them money is not a priority, but one of the available means to deliver their mission.

As it happens also in the for-profit sector, having a clear mission brings obvious advantages for the organization in terms of strategic definition and planning. In addition, in the case of non-profits, a strong mission can also help to attract employees, volunteers, partners, funders and clients. It can motivate, align and strongly engage employees to the extent that they accept lower salaries than the industry average. It also brings some financial advantages such as tax exemptions in mission-related activities, but at the same time it adds some extra complexity to the business model of these organizations, such as multisided business models in which the primary beneficiaries of the services are not the ones paying for them.

In spite of the added complexity of non-profit models, clear and motivating missions in this sector can also be strong innovation boosters since they push organizations to focus their attention on improving those activities that most support the accomplishment of their mission. As many examples demonstrate, innovative organizations have clear advantages when compared with their competitors. For the non-profit sector, an increasingly competitive environment is nowadays a reality, when public funding is cut and a growing number of organizations compete for limited funding resources. This is one of the reasons why non-profit cultural organizations are experiencing increasing pressures to become more business-like and to focus on financial outcomes as the most logical way to achieve financial sustainability. At the same time, many professionals in the sector put in question whether this increased attention on performance would affect the organization's mission and the way their activities are implemented.

Historically, the idea of the “mission-driven organization” has been associated with the non-profit sector, but this idea has been changing throughout the last decades, in which many for-profit organizations self-proclaim mission-driven or start non-profit ventures. In fact, mission-driven businesses are a subset of social enterprises, an idea that is neither a new one but has increasingly captured the attention of a more mainstream audience attracted by social-aware businesses.

Western customers are nowadays more aware than ever of the social and environmental impact of the products and services they buy and consume. They have become more sophisticated and they don’t accept as easily as in the past the conditions under which companies produce and deliver their goods, which are usually the direct result of profit maximization and cost-cutting strategies.

Entrepreneurs and business owners are also more conscious about the social and environmental consequences of their organizational practices and many of them pay closer attention to ethical issues related to their businesses. Instead of focusing only on their finances, certain companies have started giving more consideration to the social, economic and environmental impacts. This three elements are what the social responsibility and sustainable development authority John Elkington used to base his influential framework called the Triple Bottom Line (TBL). The TBL intends to advance the goal of sustainability by combining three interrelated dimensions of business performance, the so-called 3 P’s:

a) Profit: the economic value created or the positive externalities.

b) People: good practices regarding labour and the community.

c) Planet: sustainable environmental practices.

While still driven by profits, mission-driven businesses like social enterprises attempt to sustain themselves by delivering products and services that aim to achieve social, community, environmental or cultural positive outcomes and, at the same time, allow the organization to support itself with the revenue. In contrast to traditional non-profit organization that are dependent on contributed income (public and private grants, donations, etc.), social enterprises base their activity on earned income.

On the surface, many of these social enterprises look like traditional businesses, but looking more deeply, one discovers that their mission is at the centre of their business. By providing products and services that produce social value, social enterprises invalidate the customer-beneficiary dichotomy that differentiates for-profit from non-profit organizations and proof that generating social value and commercial revenue are not incompatible. Many examples demonstrate that pursuing a mission, meeting the needs of a community and building a sustainable business, in some cases, can go hand in hand. This doesn’t mean that public grants and subsidies have to be eliminated, but they have to be efficiently distributed to support those areas in which public good products and services cannot achieve commercial viability.

The previous paragraphs show how the type of legal structure of an organization –for-profit or non-profit– can hugely influence its business model. In order to avoid the limitations imposed by a sole legal structure, many organizations establish subsidiary organizations that help them better develop their hybrid business models. Even if it seems paradoxical, combining non-profit and for-profit structures is a plausible option for many organizations in the cultural sector, for instance cultural centres.

In this type of business models a non-profit structure –an association or a foundation– develops the organizational mission while a revenue generation structure –a company– guides its commercial activities. This business model uses product or service sales to fund the social mission of the main organization, reducing dependence on donations, grants and subsidies. This solution helps exploit the benefits of both legal structures.

10. Business models and strategy

Leadership and management in all type of organizations have to continuously assess the present environment and circumstances to be able to think strategically about future possibilities for their organizations. While a business model and a strategy are not the same, both are closely related and should be articulated through a strong vision and mission.

The simplest definition of a vision is how the future will look like. A vision is not about the present or where your organization is now, a vision is where you will be in the future. Therefore vision must inspire and motivate those who are to implement it and has to be relevant to the organization itself in order to be credible. Having an inspiring, realistic and achievable vision is the first step in designing a business model and formulating a strategy. It sets a direction for the organization and provides a good reason for future plans. However, the best of the visions won't be very useful if the values of the organization don't match it. Indeed the beliefs, values, principles and practices of the organization – including those of the employees, leaders, clients and other stakeholders– are critical to guiding the vision and create the culture of the organization.

Together with the vision and mission, the business model is also at the core of any organization. It describes the system that allows an organization to create and deliver value to its clients/ community/end users while obtaining value in exchange in order to continue working in a sustainable way. Thus, every organization has a business model, whether it is explicit or not, and what a business model essentially does is to turn ideas into money or other types of value for the organization.

Complementing the business model, the strategy sets the plan or path to follow in order to position an organization in a unique and valuable way and to achieve its goals. The strategy defines direction, objectives, steps, processes, changes and performance targets for implementing a chosen strategic goal. Strategy is about efficiently allocating the resources of the organization so it can go there where it wants to position. Under the organizational strategy there are different strategic levels based on the structure or departments of the organization, such as financial strategy, marketing strategy, operations strategy, etc. Successful strategies at any of the mentioned levels require that the organization understands the needs of its clients so it can create and deliver value accordingly.

Since strategy and business model are two different concepts, two organizations may employ the same business model but obtain very different results based on their different organizational strategies.

11. Business models and business plans

Business models and business plans are not the same thing. As it has already been mentioned before, a business model describes how an organization is positioned within a sector and how it manages to provide value for its clients in a sustainable way, including its relations with stakeholders (suppliers, partners, etc.), the channels that will be used to deliver the services or products, the revenue model, etc.

The business plan details the opportunities that the organization is seeking to take advantage and translates the business model into a series of strategic actions and forecasts their financial impact. This implies that the business model is at the center of the business plan. In fact, the business plan is completely dependent upon the business model and it will have to change if the business model of the organization changes.

In essence, a business model is more of a conceptual tool rather than financial, while a business plan will pay great attention to the financial issues concerning the strategy of the organization.

More than ever, change is a common force in our world and cultural organizations must be able to adapt to the changes of the sector and the demands of its more and more sophisticated audiences. Those cultural organizations failing to adapt to the current and upcoming new circumstances will have to face the consequences. This is the reason why both business models and business plans have to be dynamic management tools that need to be revised periodically so they can allow organizations to rapidly change when required.

12. Definitions of business model

Since the beginning of 2000's the phrase Business Model has been one of the most used buzz phrases in the business sector and it has also become increasingly popular in the non-for-profit sector. However, the first time that people hear the expression "business model" they tend to imagine very complex financial formulas and overwhelming strategic theories but, believe or not, the five straightforward questions listed below are the core of any business model design.

The business model is a vital concept determining the success of any organization but despite its importance, there is no consensus regarding its definition and for many people in the arts and culture sector the concept still being vague and unclear.

The term business model was informally coined by those working in the technology sector, especially among the emerging internet businesses, in the late 1990's and it was quickly adopted by practitioners and scholars all around the world. The first academic definitions of the term are also dated by the end of the nineties. However this does not mean that business model didn't exist before the internet revolution.

Obviously, business models existed before but they were not designed in the same systematic way and using the well-defined repeatable processes that they are today. For organizations the approach to business models was then more intuitive and the business model was not explicit but it became clear only after the economic result. The same thing still happens today in certain sectors, especially in the non-for-profit, in which many organizations operate not being aware of having a business model and a series of underlying assumptions that are continually tested against reality. The fact that an organization continues operating and delivering value to its clients is the best proof that the business model is working.

But when did business models became explicit artefacts? It is well known that the American management guru Peter Drucker was the precursor of many concepts that were further developed by other authors after him. And this seems to be the case with the "business model" concept. In 1993 Drucker published a little book titled *The Five Most Important Questions You Will Ever Ask About Your Organization.* In five chapters of the book –written in collaboration with other management gurus such as Jim Collins, Philip Kotler, Jim Kouces, etc.– he proposes a strategic framework for non-profit organizations in the form of five questions grounded in his management theories that should help improve the performance of any organization (non-profit, government or business). These five simple –yet not always easy to answer– questions were:

1. What is our mission?
2. Who is our customer?
3. What does the customer/user value?
4. What are our results?
5. What is our plan?

The answers to these five questions should be enough for any organization to know where to focus and start acting on it.

In 2002, writing about the importance of business models and commenting on Peter Drucker's five questions, the Harvard Business School senior associate Joan Magretta stated that business models are, "at heart, stories that explain how enterprises work". For her a business model tells a logical story explaining who your customers are, what they value, and how you will make money in providing them that value.

If creating a business model is quite like telling a story, we all know that stories don't come out of the blue but they are, to some extent, variations and remixes of pre-existing stories. A bit like stories, successful business models are, in most of the cases, nothing but variations of other successful business models and they represent a better way of doing things than the existing alternatives. Indeed, successful business models "may completely replace the old way of doing things and become the standard for the next generation".

As Magretta believes, business models can be divided in two parts: the first part includes all activities related to making something (design, purchase, manufacturing, etc.) and the second part include all activities associated with selling something (finding customers, distribution, service delivery, etc.). Very simply said, a new business model may end by designing a new product or service based on our target customers' or users' needs; or it may turn on better ways (processes) of making a product: building, storing, distributing, selling, etc.

Some of the most successful and popular definitions of business model are the ones proposed by Alexander Osterwalder and Yves Pigneur: "A business model describes the value an organization offers to its customers and illustrates the capabilities and resources required to create, market and deliver this value and to generate profitable, sustainable revenue streams". Believing that a business model definition should be simple, relevant and easy to understand yet not oversimplifying–, some years later, these authors offered a more concise definition: "A business model describes the rationale of how an organization creates, delivers and captures value". For Osterwalder and Pigner, a business model can best be described through nine basic building blocks that show the logic of how a company intends to make money: customer segments, value proposition, channels, customer relationships, revenue streams, key resources, key activities, key partnerships and cost structure.

More definitions of business model

An architecture for products, services and information flows, including a description of various business actors and their roles; A description of the potential benefits for the various business actors; and a description of sources of revenues. Timmers (1998).

A BM is the method of doing business by which a company can sustain itself, that is, generate

13. Basic components of a business model

Scholars and authors researching and working on the field of business models have suggested different components for a business model based on their own understanding and definition of what a business model is. There is no consensus regarding how many and which elements should be included in a comprehensive analyze of a business model. We have seen how Osterwalder and Pigneur suggest a model with nine components. For Amit and Zott, a business model should focus on three areas: The content, the structure and the governance. Casadesus-Masanell and Ricart distinguish two sets of elements: a) the concrete *choices* made by management on how the organization must operate –including compensation practices, procurement contracts, location of facilities, assets employed, extent of vertical integration, or sales and marketing initiatives, etc.–, and b) the *consequences* of the choices –including policies, assets, and governance structures. Other authors think that a business model should basically reply to the following seven questions: who, what, when, why, where, how and how much. For Mark Johnson business models consist of four interlocking elements, that, taken together, create and deliver value: customer value proposition, profit formula, key resources and key processes.

Bearing in mind all these different perspectives we could we could point out four essential components within any business model: value proposition, customer/user segments, infrastructure (resources and processes) and a viable revenue model.

As we have seen previously, there are many different definitions of business model, but what almost all of them have in common is the central role of the **value proposition** within the system. The reason for this is that a well-crafted value proposition is essential to any business model, and it doesn't matter whether we talk about individual entrepreneurs, startup organizations or already established organizations, for-profit or non-for-profit organizations. For all of them a clear and focused value proposition determines their business model and the rest of components of the business model will only work for it to be delivered successfully and be financially viable.
It is important to keep in mind that crafting a value proposition is not to try to convince customers of the value of your products or services but, the other way around, to identify the needs of your (potential) customers or users.

The **infrastructure** would include: a) the *resources* the organization has or can access to, such as the people, the knowledge and information, the technology, products, equipment, partners, funding, the brand, etc. required to deliver the value proposition to the customer or user. b) The processes such as design, development, sourcing, manufacturing, marketing, hiring and training by which a company creates and delivers on the value proposition.

The **customer/user segments** are groups of people that a given organization aims to reach and serve. These groups can be based on needs, interests, behaviors, lifestyle or other factors. Without customers, no organization will survive for long.

Simply put, a **revenue model** is nothing more and nothing less than the way that an organization makes money. Business models and revenue models are often confused, but they are two different things. We will tackle this issue more in depth on chapter 16.

14. Multi-sided business models

In the most common business models used in the commercial sector, the end users of a product or service are often also the ones paying for them. This is not always like that and exemptions can be easily found, for instance, in products and services targeting kids, which usually don't have the buying capacity and instead their parents pay for them. Any company targeting kids will have to analyze the relationship between the two components of the customer unit (buyers and end users) in order to efficiently market their products or services.

A similar situation is the one that can be found in the non-profit sector, where most of the revenue don't come from the direct beneficiaries of the services but from third-party sources like governments, foundations, etc. Business models addressing this peculiarity are called multi-sided –or third-party funded– and they add complexity to the model by dividing the traditional customer unit into two different segments:

Beneficiaries, end users or recipients: These are the target group(s) that the organization is providing services or goods to.

Donors: These are third-party agents like governments, foundations, individual donors, etc. that fund an organization so it can fulfill its mission by providing services or products to the end users or beneficiaries.

Because of these two completely different "customer" segments, when designing or analyzing the business model for a non-profit organization, both have to be tackled separately. End users and donors have different needs and the value propositions they are offered will have to be also different. Same thing will happen with the channels the organization uses to communicate and deliver the services to them.

Since donors usually have their own agendas and funding priorities, those organizations' missions that don't fit their criteria won't be eligible for funding and, consequently, the above-mentioned non-profit multisided business model won't work.

15. Income streams: Contributed and earned incomes

One of the keys to organizational survival is the ability to acquire and maintain resources. Resources are not exclusively financial, but financial resources are usually one the major concerns of cultural organizations because un imbalance between revenue and expenses might seriously affect their programmes and activities, and ultimately threaten their survival.

The revenue volatility and high dependence on public funding of cultural organizations might be reduced thru a well-planned diversification of income streams. Moreover, multiple sources of income might lead to a more innovative culture within organizations and better respond to changes in the environment.

nonprofits can indeed reduce their through diversification, particularly by equalizing their reliance on earned income, investments, and contributions.

he need for a balance of profitable and loss-making activities in order to maximize mission impact

the need for a mix of contributed and earned income

Some of the sources are fairly unique to the nonprofit sector, such as volunteering and donations.

Nonprofit arts and cultural organizations might obtain revenues from both contributed and earned income streams:

Contributed income: Contributed income is cash or in-kind resources that are given to the organization in the form of a gift or grant. The most common contributed income streams for non-profit organizations are:

1. Government funds. These can be fundraised at local, regional, national and international levels.

2. Private funds. Contributions from foundations and other private grant givers.

3. Corporate contributions. In these cases, companies contribute cash to non-profit organizations so they can achieve their goals. In these kind of exchanges, there might exist a marketing-related interest of the donor.

4. Private donations. It is a gift made by an individual to an organization. These are commonly in the form of cash but they can take other forms, such as real state, goods, etc. A donation-based variant is crowdfunding, in which a large number of people contribute cash to a project or venture. There are a number of types of crowdfunding, rewards-based, equity crowdfunding, etc.

5. Volunteering. Driven by a personal motivation and/or the organization's mission, a person performs a service willingly and without pay. Both donations and volunteering are quite unique to the non-profit sector.

6. In-kind. In-kind exchanges refer to goods and services that an organization obtains form another organization at very low or no cost.

Earned income: The term earned income refers to direct exchanges of products or services for monetary value within market conditions. Non-profit organizations increasingly engage themselves in commercial activities for revenue generation. For some non-profit researchers this practice initials a potential loss of values distinctive to the nonprofit sector, but at the same time it can bring some advantages as an increased diversification of income streams. Basically, earned income for non-profit organizations is two-fold:

1. Mission related services and products: any profitable products or services that directly relate to the organization's mission and contributes to its achievement: government contracts, sales, fees, memberships, sponsorship, consulting, education, etc.

2. Mission unrelated services and products: these commercial activities refer to the provision of services or goods sales that are not directly related to the organization's mission or are offered to customers that are not the usual beneficiaries of the mission, but can generate revenue to internally subsidize mission-related activities. Some of the most common are: catering services, facilities renting, merchandising sales, consulting, etc.

Does your organization have a good business model?

I once heard somebody say that the sole valid business model is that one that is able to generate more income than expenses. Even if this sentence might sound obvious and arrogant, it doesn't lack reason and many managers in the cultural sector should think twice about it before continuing with their activity. Just remember that the financial situation of an organization is the result of its business model. Other than this, a good business model should:

1. Be aligned with the vision and mission of the organization.

2. Be packed with self-reinforcing elements that make it internally consistent.

3. Be robust enough to sustain over time but flexible enough to adapt to new situations.

16. Business Models and Revenue Models

The terms business model and revenue model are often equated and confused but they are not exactly the same thing. In fact, the revenue model is one of the several components of the business model and it could be defined as the structure through which an organization monetizes the value proposition that it offers to its customers and/or end users. Explained in a simpler way, it answers one of the most vital questions about the business model: How will the organization make money or capture value so it can continue delivering its mission?

However important, other elements of the business model are not less crucial, such as the need to build a customer value proposition based on actual needs of the people the organization intends to serve. Therefore, a well structured business model will include –among the rest of components– a clear and tailored revenue model which will ensure the organization's financial health.

There are lots of different revenue models but there are some of them that are quite recurrent in different sectors. What follows is a glimpse of some of the most common revenue models in both online and brick and mortar businesses:

1. Traditional Retailer: The traditional retailer profits by selling products and services directly to buyers at a mark-up from the actual cost.

2. Low Cost Retailer: This is a variations to the traditional retail model. The retailer operates on very low margins and relies on very high volumes of sales.

3. Premium Retailer: In this model, the retailer operates with very high margins by providing the added value of a prestigious brand.

4. Renting or Leasing: The customer pays for a service or to use a product for a fixed period of time. This service is often offered as an alternative to purchase. Both renting and leasing have been widely used by the vehicle industry.

5. Penalty charges: Used independently or as complement to the previous one, this model allows to use a service or product under certain conditions that can easily be failed to carry out. When the customer defaults, the service provider charges high margin penalties. Parking meters, video game and home video rental services profit of this model.

6. Subscription Model: This model has a number of variations but in essence it can be described as a recurrent payment once in a predetermined time period (days, weeks, months, years) for a service or the usage of a product. Its aim is to secure the customer on a long-term contract.

7. Licensing: This model is most commonly applied to innovations that involve sophisticated technology protected by intellectual property agreements. Licensing intellectual property can result in very high gross margins for the owner.

8. Cost-Plus: In this model, the selling price is determined by adding a percentage mark-up to the cost of producing the product or service. This is common in outsourcing or business to business transactions in which both parties want to share the risk of producing the product.

9. Advertising: Both newspapers and magazines have used this model for ages and websites use it nowadays because of their capacity to attract potential clients with certain demographic characteristics that meet the characteristics of the target groups of the advertising organization.

10. Razor and razor-blade: This model involves initially selling a product for a low price in order to generate revenues from complementary products that the primary product requires to be useful. The classic example is: sell cheap razors in order to sell blades at a high margin.

11. One-time Up-Front Payment plus Maintenance: This model adds a little variation to the previous: complementary products are replaced with maintenance services that keep the product running properly.

12. All You Can Eat: This model offers unlimited use of a product or service over a fixed period of time for a flat fee.

13. Freemium: This is a revenue model in which a product or service is provided free of charge, but money is charged for premium features or functionalities of the same product or service.

14. Reselling data: This model requires first attracting end users with a free product or service so users information can be then sold to third parties.

15. Intermediation Fee: This model is based on a commission that is paid by the seller to an intermediary every time that a referral leads to sale.

16. Pay As You Go: This is usage-based model in which the usage of the product or service is monitored and the client pays on the basis of what s/he consumes.

17. Mobile Phone Plan: This is a predictable, recurring base fee charged in exchange for a certain amount of committed usage, with additional charges, often at much higher marginal rates, if the customer uses more than their allotted amount.

18. Auction: It can be presented under different forms, but its main characteristics are that the price of the product or service is not fixed in advance and the final price is determined via competitive bids.

19. Micro-transactions: This successful model came into vogue with online computer games. The customer is asked to create an account and link a credit card to it so small transactions – sometimes less than 1€– can be made to buy digital goods in a very easy way.

20. Franchise. An organization pays royalties for the privilege to deliver the products or services of a well-established brand in a particular sector.

17. Business models and their visualization

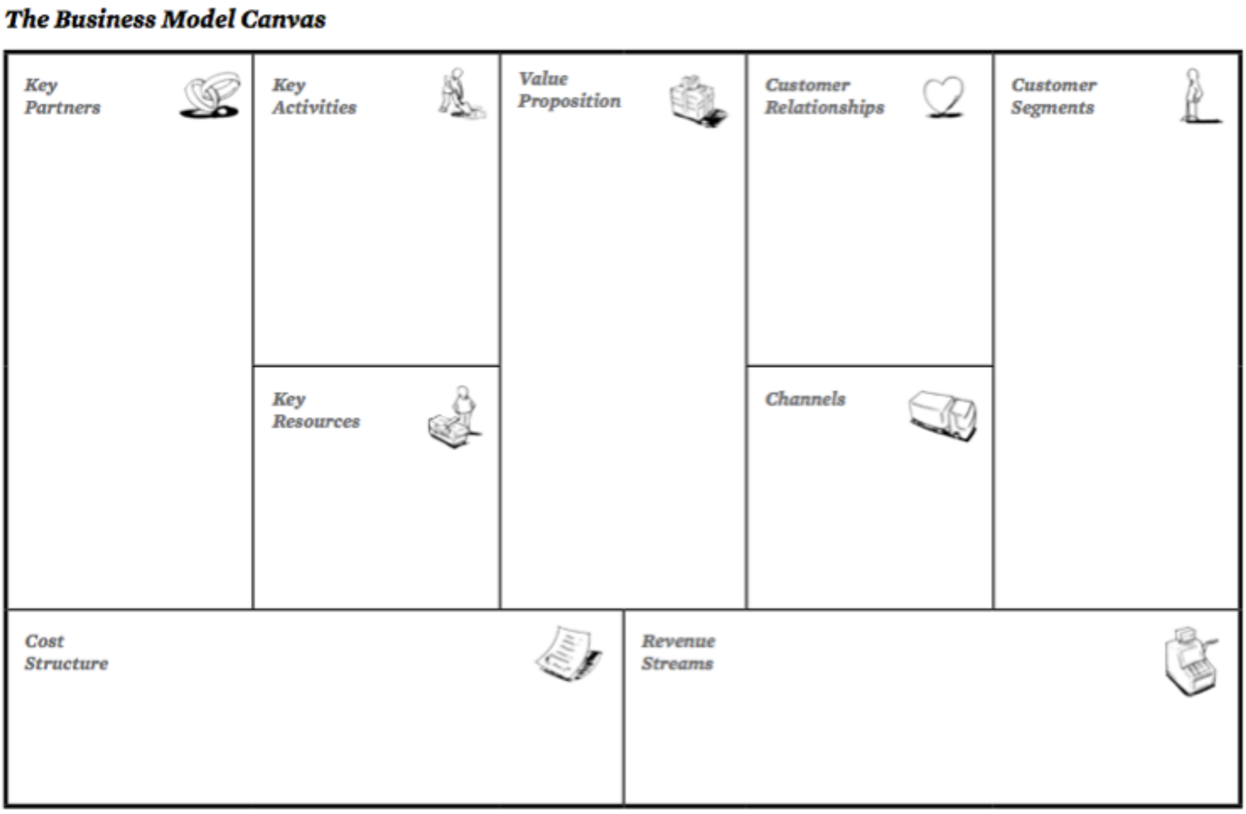
A business model has to be easily understood, communicated and remembered.

It is important to understand that a business model is a system. It can be a more or less complex system but in any case it remains a system made up of several components that are tightly interconnected and reciprocally influence each other. This system dynamics are not always easy to represent using the linear text, which is the most traditional and familiar form to represent ideas for most of the people. Instead the cognitive benefits of visual representation are well known and scientifically proven. In the case of business model design, visualization can help to make ideas much more clearly and to understand the interconnections and relationships of the elements within the system.

In addition, designing and developing a business model is not an individual task. In fact, business models innovation triggers individual and organizational challenges and should be considered as a team sport. And to get the best results out of it, idea generation processes should be developed in both formal and informal group collaboration. Therefore the first step to start working with business models is gathering a team to explicitly describe the organization's model. In this process, sharing ideas, communicating and manipulating knowledge is vital and visualization can help to elicit managers' implicit mental models and align the whole team. Moreover visualization usually provides a flexible, provisional and playful framework to boost innovation.

One of the most popular tools for designing and developing business models using visualization is the Business Model Canvas. In 2009 Osterwalder and Pigneur developed the canvas to help entrepreneurs, start-ups and organizations to innovate in their business models. It rapidly gained attention and recognition among practitioners because it is a very visual, collaborative and easy to use tool.

Briefly explained, the Business Model Canvas consists of nine blocks that represent the underlying logic of the business basic processes and allows to visualize them in only one page. It starts with a value proposition that meets the needs of one or more customer segments. The value proposition is delivered to customers through communization channels, distributors and sales channels. The value successfully offered to the customers is returned to the organization in revenue streams. Key resources are the assets required to offer and deliver the previously described elements by performing a number of key activities. Some activities are outsourced and some resources are acquired outside the enterprise by turning to key partners. All these business model elements result in the cost structure.



After Osterwalder and Pigneur other authors have simplified the canvas or developed it further by eliminating, adding or changing elements as well as by using different forms of matrix, tables or mind maps. If you search on the Internet you will find many different versions of the business model canvas. What they all have in common is the use of a one-page diagram that focuses attention on how all the elements of the system fit into a working whole, which brings some advantages: It is very easy to work with in groups; It is very concise and it forces to prioritize your ideas and carefully select the words you use to describe them; Compared to a business plan it is easier and faster to write and update; It allows you to design as many variations and alternatives as you want in order to compare and combine them; It is easy to share with others in order to facilitate conversations, etc.