1 Beyond Digital Ubiquity: The Digital Business Model Iron Triangle

We live in a digital world: digital services surround us in every moment of our daily lives. These devices, such as smartphones, have revolutionised the way we communicate, entertain ourselves, connect and form political opinions, as well as the way we look for information regarding products and services and how we buy and access them. Mobile phones have become more than another digital device since they are now used as an extension of ourselves. Not surprisingly, some of the most successful companies of our times, including Facebook, Google, and Apple, have managed to capitalise on their intimate access to and knowledge of the hyperconnected consumer. They have positioned themselves at the heart of the digital ecosystem, which provides them with unlimited reach to all of us, along with an ability to collect and harvest behavioural data about any end-user. These companies are trading on ubiquity, an omnipresent awareness of the customer and their journey. In this book, we surpass digital ubiquity to analyse how internet companies foster a digital business ecosystem and establish a sustainable competitive advantage by developing new revenue and business models. In this chapter, we contextualise this new digital environment, followed by contrasting the dynamics behind the success of the two transformative digital players – Netflix and Spotify – to illustrate how digital businesses can create, propose, deliver, and capture value. This leads us to propose an Iron triangle of a business model that echoes three key questions: Who is creating value? Which configuration (shape) does this value take? And finally, how sustainable is the competitive advantage?

1.1 Be Kind, Rewind

Let’s stop the time, and rewind. Fifteen years ago, almost none of us had a smartphone – the iPhone was first released in the United States on June 29, 2007. Ten years ago, many of us owned a smartphone, and if we could do almost everything that we can do today via digital devices (the iPad was released in April 2010), most of us did not.

The digital devices were available; however, they were not as pervasive, and certainly not ubiquitous. Most of the companies – Google, Spotify, Netflix, Airbnb, Uber, Strava, Slack, Twitter, Facebook, LinkedIn and YouTube, to name a few – that were going to shape our everyday interactions with one another, with ourselves and with companies and services had already been founded. Certainly, entrepreneurs toyed with ideas and concepts, which are now well established; however, those concepts and ways of interaction had not yet found their spot in our everyday life. We were – at least sometimes – still buying (and using) CDs and renting DVDs. We may still have called hotels to book a room and walked (or phoned) the restaurant for a pizza. We were running without knowing exactly how many kilometres we were running and at which pace.

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We Were Going Fast. . .

Through our rapid adoption of digital devices and the lagging but corollary change of behaviour, we were expeditiously increasing the pace of the digital revolution. By 2016, 3,668 billion smartphones were already circulating around the globe, and according to Statista, that figure has now doubled to a whopping 6,259 billion;[1] implying that around 84% of the world population (7.9 billion) is now digitally connected.

Now, what about our behaviour? Well, it has also evolved, as we now spend much more time in front of our screens – between 1.5 and 7 hours per day on average for the western world!

This is a cause for concern, and screen addictions are now a well-identified pathology. Consumer buying behaviour has also advanced. The 24/7 communication characteristics of mobile technology have not added or withdrawn any steps in the consumer's purchase journey; consumers still undergo the need, research, purchase, experience, and sharing of experience stages. However, with a mobile phone, which acts now as a digital extension of us, all these moments have now been merged into what some authors have described as a digital ubiquitous moment of truth (Muzellec & O'Raghallaigh, 2018).[2]

In the office, the pace of change was somehow slower. Decades of teaching and research in business schools taught us about linear value chains, setting prices through the markup and estimating the value of a company through its potential market size. All of it is relevant and valuable in the real world; however, it is often not as useful in the digital world.

We Need New Ways of Reading the Reality Surrounding Us

We need new models, tools and eyes to read the reality around us and the models behind the services we continuously use.

We can read everywhere about the parallelism between Uber and Airbnb and the flagship cases of the platform economy. We read articles that continuously pit Amazon and Apple against each other. Twitter, Facebook, Instagram and TikTok are all different faces of the same business. i.e., social networks. Spotify is the Netflix of music, and Netflix is the Spotify for movies.

Using comparison or what we already know, we tend to simplify the reality. By finding patterns, we wish to express a novel concept through another concept that we may be more familiar with. This book aims to avoid this and rather provides the reader with the right tools to examine the differences amongst all the digital services;

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1 https://www.statista.com/statistics/330695/number-of-smartphone-users-worldwide/.
2 Muzellec, L. & O'Raghallaigh, E. (2018). Mobile Technology and Its Impact on the Consumer Decision-Making Journey. Journal of Advertising Research, 58, 12 LP–15. doi: 10.2501/JAR-2017-058.

and, more importantly, the complexity and sometimes the uniqueness of their business model, otherwise known as "the way they make money". Hence, let's have a look and spot the key differences between the business models of two companies that are often presented as very similar.

1.2 Spotify and Netflix: Spotting the Uniqueness of a Business Model

Spotify and Netflix are two of the greatest game-changers in the entertainment industry.

Spotify was founded by Daniel Ek and Martin Lorentzon in Stockholm, Sweden, in April 2006. It went live in 2009 in the UK, with the slogan and vision, "Music is for everyone". Nowadays, Spotify has more than 400 million users worldwide, garnering around 10 billion US dollars in revenues, while streaming most songs produced and delivered in the world.

Netflix has a longer history. Reed Hastings and Marc Randolph founded it in 1997 in California. In 1998, it went live with its first website, with 925 movie titles available, which were to be sent around the country in DVDs through the mail system. Nowadays, it has more than 220 million users spread across the globe, with almost 30 billion US dollars in revenues and a continuously evolving catalogue of movies, TV shows, and games.

These two companies are often told as similar stories in comparable industries. Spotify challenged and changed the music industry significantly by introducing a new revenue model along with several other changes. Netflix is considered the pioneer of the streaming platforms revolution that is changing various fields at once, from the television industry, which sees its affectionate viewers being less and less affectionate, as well as the cinema industry, which saw a new competitor/player entering in the game for theatres, producers, and the overall distribution chain.

They may look similar, but they have a few notable differences that can be illustrated through the value dimensions that underlie a business model and thus revisited in a digital business: value proposition, value architecture and value capture.

Value Proposition: What is the Clearest Benefit for Users?

Let's begin by assessing what these two companies propose to the market. Value proposition deals with the product or service offering and more broadly the definition of what the company proposes to its customers.

A very first exercise, useful to assess how a company portrays its offering to the market, is surfing the web – as not logged-in users – to assess the very first message it provides to a prospect. Spotify, following a promotion to acquire three months of premium for free, shows its mission: “Listening is everything: millions of songs and podcasts. No credit card needed”.

These few words, and the short ad, tell a great deal about the company. It constitutes the initial value proposition. Spotify offers a freemium service focused on listening, and it deals with songs and podcasts. It can also be completely free to use. In other words, Spotify offers a legal way to listen to music and podcasts for free from all over the world, with millions of songs available at your disposal anytime, anywhere, with a tap.

Netflix starts off differently: “Unlimited movies, TV shows, and more. Watch anywhere. Cancel anytime”. By scrolling down the page, we can find various call outs: the chance to watch it on your TV, download shows, multi-home on various devices, and a dedicated sections for kids.

Netflix is a streaming platform that aggregates various kinds of visual content and makes them available everywhere, paying a subscription fee that you can cancel anytime. We’ll return to this notion soon.

The value proposition of the two companies seems similar to us as end-users when they are compared. It changes the object – from audio to video – but it offers great points of commonalities: it is everywhere, on-demand and digital.

Those value propositions may evolve over time and may be communicated differently.

“Listening is everything” is not the first claim they used. Spotify started off with a slightly different claim: “Music is for everyone”. This shift in focus reveals the initial ambition of the company and its aspiration for the music industry.

In the early 2000s, the music industry was quite diverse. Those years are characterised by the legal battles of the music labels, trying to compete against the rising digital world. It began in the 90s when DVD/CD burners enabled people to duplicate CDs. This continued with digital services that enabled peers to share digital files, such as music. CDs sales dropped dramatically, and the more labels fought against these digital services by closing them down through legal actions for copyright violation, the more they popped up someplace else, always more successful. Among these services was uTorrent, one of the most famous peer-to-peer communities, which was headed for a short while in 2006 by Daniel Ek, just before he established Spotify.

Being aware of the piracy world, the founder of Spotify wished to create an environment where Music was for everyone – i.e., all types of listeners, but also all types of artists who needed to live off their art. The platform aimed to offer a model that was believed to be fairer than what it used to be.

Netflix also aimed to develop a better model for serving users and a better way of making money. Netflix challenged the model of big players, including Blockbuster. The Blockbuster model had a major flaw; essentially, it was making money in a manner that was distressing for the customers. Traditional rental companies let customers rent a DVD for 24 hours and then imposed late fees for anyone who failed to return the DVD in time. This was quite inconvenient for potential users who had to rush to watch the DVD in less than 24 hours or felt punished and stupid if they forgot to rush back to the store to return it.

Netflix erased those pains through a subscription-based service. Take the DVD, keep it as much as you wish, enjoy it, and when you are done, send it back. Customer value was at the epicentre of the business model.

In 2007, the company moved towards streaming services. Netflix proposed a prize of $1,000,000 to the first developer of a video-recommendation algorithm that could beat its own existing algorithm, Cinematch. The competitive set had evolved, and Netflix needed to beat a different set of companies, such as cable television in the US or pay-tv in Europe. Netflix's competitors included all companies that make, through various technologies, a premium selection of titles available for the customers.

The "Cancel anytime" slogan took on a completely different meaning. Have you ever tried to cancel a subscription on pay-tv? It is one of the most challenging adventures you may have in the entertainment world between letters, credit cards, and banks. Netflix doesn't want it. Cancel anytime. They subtly claim that the service is just so good that you will want to stay. You – the customer – are at the centre. The current slogan, "See what's next" is more subtle and does not refer to a specific attribute. As explained by Barry Enderwick, former Director of Marketing and Subscriber acquisition at Netflix (2001–2012):

> "See what is next" has at least three connotations: 1. Netflix is creating new content all the time (see the next big hit), 2. They're 'reinventing TV (see the next platform), 3. You can binge watch since episodic shows as they're available all at once (see the next show).

The implies the same focus on user value but different stories and communication tactics. . . yet it's probably dependent on what they do and how they do that wherein the two companies differ.

Value Architecture: How is the Value Created and Engineered Over Time?

How do those two digital players create value? What are their competences? What are their key assets? Who are their key partners? Overall, what are the mechanisms by which the products and services they offer acquire value that can be then brought to the market?

Both services are often referred to as "platforms", and as such, share some common characteristics.

Spotify changed the music industry, but it is not a music company. It is a tech company, which could possibly be a data company. It creates value by enabling parties to meet on its platforms through a match-making mechanism. In other words, Spotify matches customers' taste or listeners to specific artists who can deliver their music worldwide through the tech infrastructure built by Spotify.

Let's put it in a very straightforward way: artists cannot be suppliers. Suppliers are paid for what they supply, like vegetable producers who sell their vegetables to a restaurant, or movie producers who sell the rights to broadcast a movie for a certain amount of time to a television channel. There is no reason for the supplier to say no, if not for strategic reasons.

For Spotify, it was different. Spotify was required to convince copyright holders – primarily labels and publishers, but also distributors, performing rights organisations and artists to join the platform – they are providers who are not receiving money just for existing, but rather, they will make money if someone listens to them. In 2021, Spotify paid out $7 billion to the music industry. As for Airbnb or Uber, Spotify could be considered as a platform – a transactional one, as we will see later in the book.

Spotify creates value by setting up the architecture where listeners meet artists. This encounter is facilitated, thanks to a great ability to manage data. Spotify built a great recommendation algorithm through which it builds playlists, suggests songs and new artists, or simply lets you listen to something when an album is over. You usually like this feature so much that you hardly realise it.

And Netflix? Well, there is a huge point of contact: data. Still, it might probably be the only one. Netflix creates value exactly in the way we mentioned above while discussing a television channel. Netflix picks movies and tv shows, probably many more than a usual tv channel. This is probably the reason why it has several features that make it look like a platform. Netflix works as a curator of a great, large, wide and continuously changing schedule.

However, this is not what made it such a great company. Netflix, especially outside the States, achieved the greatest of its popularity starting from its original shows. House of Cards, their first great success, was followed by Stranger Things, La Casa de Papel, Squid Games, Bridgerton, The Witcher, Lupin, and several others.

Netflix is a tech company, but it is also a producer of movies, tv-series, and tv shows. Netflix heavily relies on data, which is used for individual recommendations. Better yet, it is used to decide which movies to produce, which series should be created and with what kind of casts, how to work on the plot to keep viewers engaged, and so on.

The two companies differ only slightly in their value delivery, which traditionally describes the choice made by the company for target market segments and distribution channels. Both have a general and wide target with an individual and family offering, which provides each member of the household the ability to achieve a personalised recommendation, thanks to data. Due to its value capture mechanism based on freemium, Spotify reaches a wider and younger base of individual users.

In terms of channels, they are both mobile apps, desktop apps, and third-party apps for almost any type of digital support, such as smart TVs and game consoles.

Value Capture: Where is the Money?

Value capture corresponds to the process through which the company capitalises on the value it has created to generate benefits for itself, generally in the form of revenue. Once again, the two cases seem very similar, since most of their revenues are derived from subscriptions, and yet, those revenues are managed very differently.

Spotify captures value from the listeners' side – who pay a subscription – or from advertisers – in case listeners enjoy the free service. At the end of 2021, Spotify had 406 million monthly active users, including 180 million premium subscribers who generated about 8.5 billion euros in premium revenue (i.e., subscription) and 226 million ad-supported (i.e., free) listeners who generated 1.2 billion in ad-supported revenue. Advertising serves as much of a value capture mechanism as a pain point that entices free users to convert to premium users.

However, that value is shared with the artists that contribute to creating the overall Spotify experience. After 30 seconds of playing a song, a new stream is counted. Each artist receives a pay-per-stream payment at a defined rate. Spotify reportedly pays out roughly 70% of what it gets to artists.

Netflix has a different value capture mechanism. It has a set of fixed and variable costs, related to the production of movies and series and the "rent" of external productions to be streamed on their service, but they do not share their revenues – originating from subscribers and licensing of certain original material – with external producers based on the views on the platform.

This quick comparison between the two cases shows how unique digital business models may be. They may indeed be very similar in terms of value proposition and delivery, as well as their user, technological and data focus. Yet all businesses are unique; in this instance, the two differ in how they create and communicate, as well as the manner in which they capture value.

This book aims to provide the readers with the right tools to analyse and spot the nuances of successful digital companies and properly assess the fundamentals of their business model. This analysis can be conducted using several tools and frameworks, which can be encapsulated within three dimensions that we labelled the Iron Triangle.

1.3 The Digital Business Model Iron Triangle

Three questions have obvious answers in a traditional business: **Who** creates value? What is the underpinning value architecture or the **shape** of the digital business? How is the **value sustained over time**? The answer to those questions is less clear for digital businesses, hence the imperative to ask them.

Who is Creating Value?

Spotify creates value-enabling transactions along with value analysis and processing a large amount of data, but listeners, artists and advertisers each play a key role in the business ecosystem. With even a single one of them absent, the others would not exist. Netflix creates value through its technology and the data originating from the end-users and the partners that create their valuable original products.

In both cases, the "network" plays a great role, but who is the network? And what are the contributions of participants (both sides) and the service provider in the creation of the value behind the digital business? Digital – as a technology – has enabled in an unprecedented way, the opportunities to engage participants – as value creators and/or recipients – in a network mode. Therefore, those who survive and grow master the power of network effects. This will be explored in the first part of the book.

How Do Digital Businesses Reshape Market Configurations?

Is it a platform? Is it a social network? Is it a marketplace? Is it a simple digital service? Digital services may look similar, but they often build on different value architectures that give birth to various outlooks of business models. Behind the similarities and the differences between Netflix and Spotify, we touch on the idea of market configurations. Digital reshapes industries, sometimes in quite disruptive ways. This will be the focus of the second part of the book, addressing different configurations of markets reshaped by digital players, namely e-commerce, social networks and sharing economy.

How is the Value Sustainably Captured over Time?

Finally, even if digital businesses are often perceived as free, or almost free, they can only survive if they have a good value capture mechanism. Hence, the sustainability of their revenue model over time must be carefully considered. Subscription can be a way, but it is not the only one. Platforms, for example, enable subsidisation, while data trading is another popular alternative. All ventures have a profit and loss statement (P&L) that seeks a good return on investments. Creating value is important; however, capturing part of this value and converting it into sustainable revenues is a necessity. This will be covered in the last part of the book, where we address different pricing models (brokerage model, subscription model, free-based business models) and their specificities in the digital arena.

These three perspectives, the who, the shapes and the sustainability, altogether represent a unicum for each digital business, a balanced equilibrium that's hard to achieve, but extremely consistent and eventually valuable once found.

This is the reason we called it the Digital Business Model "Iron Triangle" (Figure 1-A). The idea of the "iron triangle" emerges from Project Management, where the three main variables – time, cost, and quality – must be properly balanced in the planning phase and then managed throughout the project. During any project, something might happen that will try to unbalance the triangle, wherein the project manager's goal is to balance it back by working on the other variables.

We propose here the same for the digital leader: find your balance, manage the three variables to achieve the best trade-off between the who, the shape and the sustainability and work throughout your digital business growth to keep it balanced!

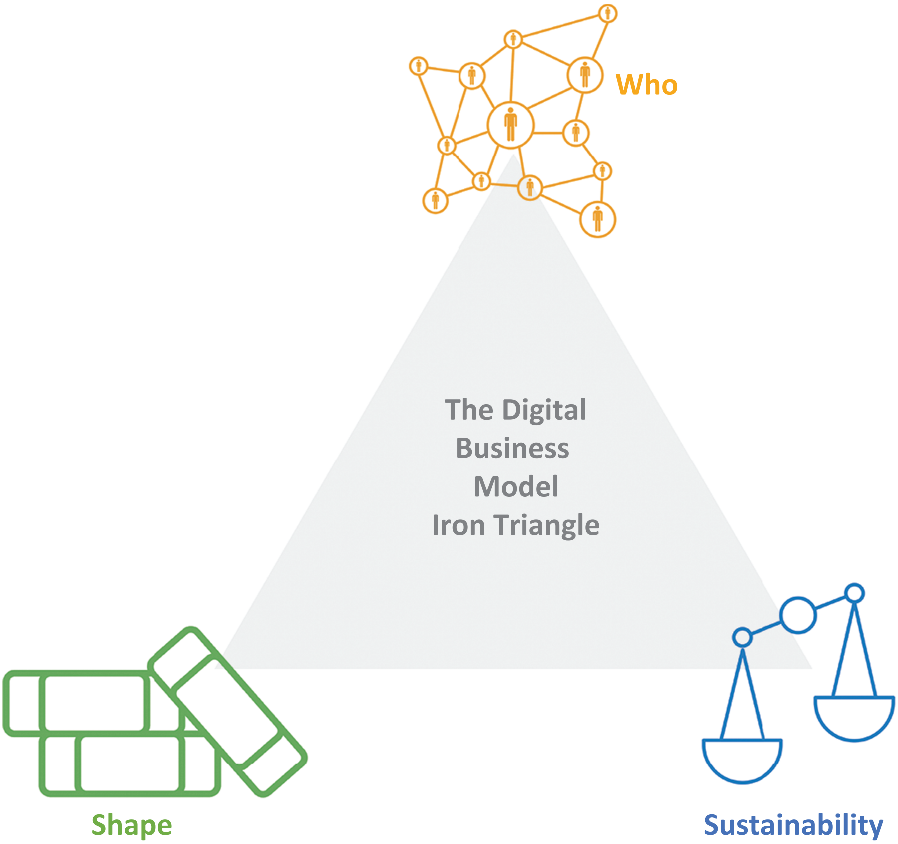

Figure 1-A: The Digital Business Model "Iron Triangle".