june 2015

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article

the great business model disruption

Today's business models won't stand up to the tsunami of technology and digital disruption coming their way

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Right thinking

1. First it was telephony, now it's financial services, next it's sustainability – sectors in which use of the environment is core business (electricity, gas, transportation, water and waste) – that will succumb to business model disruption
2. New technologies and digital platforms are enabling the great disruption of business models that don't deliver efficient outcomes for shareholders, customers and society
3. This five part framework is an enabler for businesses to change their business models to withstand the impending disruption

Disruption is coming. Better business models for operating key sectors of our society now exist.

The next wave of disruption will impact on sectors in which use of the natural environment is core business – electricity, gas, transportation, water and waste management – which have only incrementally changed over the past 100 years. Most of the existing infrastructure in these areas was developed to meet the needs of Australia at a very different stage of development – sparse population, abundance of land and little concern for limiting adverse environmental impact. In addition, older assets still used to operate our cities, like office buildings, which are on average 31 years old in Melbourne (Wilkinson 2009), were built for an era of low utility prices and where tenants yields were not tied to access to creative spaces, natural air flow and light.

The opportunity for sustainable disruption is significant due to the age of the business models, infrastructure and assets in these sectors. This opportunity can be exploited by creating new business models that utilise new technologies and digital platforms to deliver better outcomes for customers.

The five part framework set out in this article, leverages 20 years of research in the field of 'disruptive innovation', for companies to avoid the rapid obsolescence of their existing business models. Disruptive business models deliver new offerings that create new markets or invade established markets by better satisfying customers' needs (Economist 2015). They do this partly by harnessing new technologies, but also by developing new offerings that exploit old technologies in new ways.

For an example of the inevitability of sustainable disruption, let's do a quick dive into the electricity market. The 100 year old model of generating electricity in regional areas and transmitting it hundreds of kilometres to major population centres is currently being challenged. On the economic front, 'old model' electricity prices for households have risen 100% in the past six years (Chester 2015) and the economics of solar, now on over 26% of eligible Australian homes (Grattan Institute 2015) is already more favourable. On the social front, there is more community dissent to AGL's coal seam gas project in Gloucester, NSW (Hamman 2015) than solar panels or heat pumps installed by neighbours in your street. Furthermore, the environmental impact of energy consumption, currently a staggering 65% of Australia's emissions (Wood 2015), can be drastically improved by the adoption of proven new technologies in the areas of electrification (electric vehicles, induction cooktops), renewable energy (solar, energy storage) and energy efficiency (sustainable building technologies like LEDs and remote control and automated appliances).

The framework adapted primarily from Christensen (1995, 2000 and 2012) to develop and execute new offerings that drive sustainable disruption has five key elements. All of these elements need to be considered in parallel:

Framework for developing your disruptive offering

Element		Strategic question	Disruptive examples that demonstrate the importance of this element
1.	**Develop disruptive offerings**	Will it overtake the performance characteristics of existing offerings?	Uber for taxis; Skype / Viber for overseas calls; solar panels on the home; LED lights
2.	**Define the strategic significance**	Will the offering better satisfy our customers' future needs?	AGL Energy will offer battery storage to its customers by end of 2015
3.	**Locate the initial market**	Where can we get quick wins to prove the potential of the offering?	Uber started in one geography (Sydney); Amazon subsidised hardware (Kindle) to drive take-up; Ubank started at the lowest home loan price point
4.	**Determine how to bring the opportunity to market**	Do you have the right skills, culture and capacity to rapidly execute on the idea?	NAB entered online lending by establishing a separate business (Ubank); Google develops new offerings in a separate company (Google X); AGL has set up a new division (New Energy) for delivering 'behind the meter' energy solutions
5.	**Determine how to scale-up the offering**	Is the existing business or a new division the right place to scale-up the disruptive offering?	SunEdison scaled up its solar power purchase offerings by setting up a separate company (TerraForm) to hold its energy assets and then listed the new company to increase its access to capital (Clover 2014).

1. Developing disruptive offerings

This involves developing new ideas and assessing cutting edge offerings that will better satisfy your customers' future needs using proven clean technologies, digital or a combination of the two. The objective is to identify offerings that have the potential to soon create new markets or invade established markets.

There are many structured ways to assess and develop disruptive offerings. One approach currently popular in the tech world is getting staff together (in particular engineers and web developers) for an off-site 'hackathon'.

2. Define their strategic significance

This requires an assessment of whether the new offering might immediately or soon better meet the needs of future customers. If the new offering might better address the needs of the customer in the near future it is strategically significant.

For example, Tesla's Powerwall and Powerpack battery storage offerings are likely to be considered strategic by electricity retailers with a high proportion of customers with solar PV on their homes.

3. Locate the initial market

At this point, market research is seldom helpful. When a company needs to make a strategic commitment to a disruptive new offering, it may be that no concrete market exists.

With the likely emergence of new markets or market segments, managers will need to create information about such markets – for example, who is the target customer and what is the right price point?

Examples of approaches to selecting an initial market include: by geography (Uber), sales channel (Xiaomi started out as online only), price point (Ubank) and where the economics work best (Tesla has identified Germany and Australia for its Powerwall battery storage offering) (Parkinson 2015).

4. Determine how to bring the offering to market

To commercialise the new offering, companies must protect the commercialisation team from the processes and incentives that are geared to serving existing customers.

Where the new offering needs new processes and values, because the offering is not a direct fit with the existing organisation and needs new capabilities, companies should create a new space where the necessary capabilities and processes can be developed.

Options available for creating a new space for the commercialisation team include creating new organisational structures within the corporate boundaries; spinning the team out into an independent organisation; or acquiring a different organisation whose processes and values closely match the requirements of the new task.

5. Determine how to scale-up the offering

Similar to the decision on the structure for commercialising the new offering, a decision needs to be made on where to scale-up the offering, once it is proven.

Bringing the proven offering back into the existing business can limit its impact, because it may have a: different target market (be B2C not B2B), lower profit margin in the near term (which creates a tendency to allocate capital to existing offerings at budget time), or be held back so as not to disrupt existing offerings (management interference).

Up to now shareholders have had to pay a premium for participation in new opportunities arising from new technology and digital platforms as the new business models have been developed by start-ups and nimble mid-size companies before being bought by established industry participants. This will become an increasingly high risk strategy for established industry participants given the scale of the opportunity and the risk of rapid business model obsolescence. Entities of any size can participate in this opportunity by devising a clear strategy covering the elements in this framework and then committing the resources required to win.

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