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## What are Business Models? Developing a Theory of Performative Representations

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### Abstract

Despite a rich extant literature, it is unclear what business models are. We assess three dominant conceptions of business models in the academic literature: as transactional structures, value extracting devices and mechanisms for structuring the organization. To overcome the shortcomings of these approaches, we draw on theories of performativity, social typecasting and managerial cognition. We propose an alternative conception of business models as performative representations that work in three ways: as narratives that convince, typifications that legitimate, and recipes that guide social action. Rather than actual features of firms, business models are representations that allow managers to articulate and instantiate the value of new technologies.

### Introduction

In her seminal work, Joan Woodward (1965) pointed out that technology shapes the organizational structures and dynamics of control in organizations. While this insight has remained at the centre of organizational sociology for many years, it may be due for an overhaul. In particular, one might ask to what extent the results Woodward derived from a study of manufacturing organizations apply to organizations that are heavily reliant on post-industrial technologies like software, bio-medicine, and complex materials science (Zuboff, 1988). New technologies may call for new

organizational structures which are inconceivable using Woodward's framework.

One way commentators have sought to capture the link between technology and organization is through the concept of business models. Put simply, business models are 'stories that explain how enterprises work' (Magretta, 2002: 4). A business model encapsulates the way in which a firm, endowed with a given technology, can successfully configure an organizational structure and its relationships with external stakeholders (Amit and Zott, 2001). For instance, the idea of the business model describes how firms have linked the manufacture of electronic devices with digital distribution technologies as in the case of the Apple iPod (Osterwalder et al., 2005). In this way, the business model concept appears to offer an attractive tool for determining correspondence between technology and intra- and extraorganizational structures.

Despite widespread discussions about business models, there is uncertainty about what the concept actually means (George and Bock, forthcoming). Many accounts of business models are both theoretically imprecise and empirically ambiguous, and they are often normatively inflected. In this short paper, we argue that business models are not naturalistic entities but representations deployed by business managers as strategic resource (Phillips et al., 2004). Drawing on previous work on performativity, social typecasting and managerial cognition, we conceive of business models as performative representations that articulate and help instantiate the value of a technology. They work by articulating narratives to entice potential constituents, typifying and thereby creating legitimacy for the venture, and providing recipes that instruct practical action.

We aim to contribute to debates on the relationship between technology and organizational structure by suggesting that new technologies have no intrinsic value that can be realized by deploying the 'correct' organizational structures. Rather, the value of technologies stems from the ability of entrepreneurs and firms to construct, often ex novo, organizational structures and networks of stakeholders and audiences in ways that allow for value realization. Specifically the high-technology industries have developed an enormous supply of technologies that are in constant search of value realization opportunities. Here the notion of business models provides a tool for

understanding the dynamic process through which actors seek to articulate how value might be extracted from highly uncertain and often ambiguous technologies. Rather than contingency, therefore, we emphasize a constructionist account of the relationship between technology and organization (Orlikowski, this volume).

We begin by reviewing the literature on business models. We claim these approaches assume business models describe some underlying reality while they ignore how they are used as performative representation of reality to construct and articulate a particular value around a technology. We conclude by detailing three elements of a preliminary theory of performative representations and their role for structuring the relationship between technology and organization.

### **Theorizing Business Models**

The concept of business models is widely used. A search of the *Financial Times* archive for the phrase ‘business model’ results in more than 6,000 hits for the period 2004-2009. The concept gained enormous popularity during the Internet boom of the late 1990s and later spread across a wider community of management practitioners and business analysts (Ghaziani and Ventresca, 2005). However, only relatively recently have management researchers turned their attention to this concept (Baden-Fuller and Morgan, 2010). Contributions can be grouped into three conceptions of business models: as transactional structures, value extraction mechanisms, and organizational structuring devices. Below, we summarize each of these approaches.

A first approach conceptualizes business models as *transaction structures*. In this view, business models describe the way firms configure their transactions with groups of stakeholders including customers, suppliers and vendors (Zott and Amit, 2008). A business model is ‘the content, structure, and governance of transactions designed so as to create value through the exploitation of business opportunities’ (Amit and Zott, 2001: 511). For instance, Google’s business model generates profit from providing Internet search by organizing transactions between users and advertisers. Differences between transaction structures have led researchers to generate various business model taxonomies. Zott and Amit (2008) argue that there are two generic types of business models – efficiency centred and novelty centred. Bienstock and colleagues

(2002) identify 40 different possible business models based on differences in the number of buyers, number of sellers, price mechanism, nature of product offering, and frequency of exchange. Common among these approaches is the assumption that business models, as transaction structures, can be influenced by firms independently from other variables, such as strategies, product strategies or alliance models.

A second approach emphasizes business models as mechanisms for creating and capturing value (Shafer et al., 2005). At centre stage here are the processes and structures through which a firm creates and captures value from a given technology. The business model is a manipulable 'focusing device', mediating between technology and economic value creation (Chesbrough and Rosenbloom, 2002). Because technology development is capital-intensive and uncertain, it often results in outputs for which there are no obvious and immediate applications within a given business context. In this situation, business models may help managers decide how to exploit given technological affordances. For instance, IBM has used 'open' business models to create value from its technologies by soliciting inputs from external innovators (Chesbrough and Rosenbloom, 2002). Focusing on how value is created and exploited has led researchers to identify various ways of tapping into value streams. For instance, Mahadevan (2000) identified four possible 'value streams' in an Internet-based business: virtual communities, reduced transaction costs, exploitation of information asymmetry, and value-added market-making processes.

A third approach treats business models as devices for structuring and designing organizations. Business models are seen as templates for configuring various components within an organization (Winter and Szulanski, 2001). For instance, to implement its 'direct' model, Dell had to undertake a significant re-design of its internal processes and relationships with the distribution chain. The business model is the manifestation of how certain organizational variables are configured and the consequences of that configuration on business performance (Casadesus-Masanell and Ricart, 2008). Yip (2004) defines business models as configurations of the following organizational components: a value proposition; the nature of inputs; how inputs are transformed; the nature of outputs; vertical scope; horizontal scope; geographic scope; nature of customers; how to organize; etc. The central insight from this work is that business models are made up of a series of managerial choices of

how to organize components of a firm around a particular technology.

### **Criticisms of the Business Model Concept**

Existing work on business models is exciting, but it poses some significant problems. First, it is unclear how the concept *fits* with the existing literature on business strategy and organization. Some of the definitions of business models given in the practitioner-oriented literature are so broad that they include nearly every aspect of the business. It is unclear whether the concept can be meaningfully distinguished from other, already established concepts. For instance, 'business model' is often used synonymously with 'business strategy' even though some authors have attempted to establish the concept as stand-alone theoretical construct (Zott and Amit, 2008). As a result, the business model concept remains polysemic and ambiguous.

A second problem with the existing literature on business models concerns *construct validity*. It is unclear whether the concept refers to something that actually exists. This may be among the reasons why researchers looking for business models often encounter inconsistent empirical signals. Often they find themselves examining what entrepreneurs, investors or the press claim to be business models. On further investigation, these claims are often weakly linked to what is going on within an organization and play a rhetorical rather than representational role.

A third problem with existing approaches to business models is that they tend to be *normatively* inflected. Many proponents emphasize how thinking about business models can help firms achieve certain goals such as greater innovativeness, creating new revenue streams or organizational transformation. In the same way that practitioner knowledge is situated and concerned only with fulfilling particular purposes in particular circumstances (Schön, 1983), these contributions detail certain courses of action rather than establishing the general validity of the concept.

Furthermore, the 'interpretative flexibility' (Bijker et al., 1987) of the concept enables different authors to promote their own versions of the central underlying idea. Hence the representational quality of the concept becomes secondary to its potential to underpin idea entrepreneurship which often relies on putting old wine into new bottles.

## **Towards a Theory of Business Models as Performative Representations**

To address the conceptual ambiguity, construct validity problems, and normative inflection that haunt most existing accounts of business models, we outline an alternative approach. We suggest that business models can be thought of as performative representations. A business model is a representation in that it is a text that re-describes and re-constructs reality – whether actual or imagined - in a way that is always partial, interested and intent on persuading (De Cock, 2000). Texts are more durable and intransitive than mere actions and therefore play an important role in infusing change (Phillips et al., 2004). A business model is performative in the sense that it engenders effects through reconstructing the social world in its own image (Callon, 2007). Business models are representations that create material effects such as enrolling buyers and suppliers, persuading investors, and directing employees. We suggest that business models are performative in three ways: as narratives that persuade, as typifications that legitimate, and as recipes that instruct.

First, business models are *narratives* used by promoters of new technology ventures to entice key constituents (Magretta, 2002). Narratives are a genre of text that describes a sequence of events (Bruner, 1991). Narratives comprise a subject searching for an object, a ‘destinator’ (a force determining the subject’s destination), and a set of forces furthering or hindering the subject’s quest for a desired object (Lounsbury and Glynn, 2001). For a firm to embrace a business model as a narrative then means to construct a representation of how it might succeed in a particular environment.

Existing research in contexts such as corporate failures suggests that narratives are important ways which people seek to infuse ambiguous situations with meaning and persuade sceptical audiences that their account of reality is believable (Brown, 2000). Because of their forward-looking character, business model narratives may be instrumental in inducing expectations among interested constituents about how a business’ future might play out (Downing, 2005). Business model narratives may draw on a whole range of linguistic techniques that have been identified in research on narratives in organizations more broadly (Gabriel, 2000). These include the mobilization of fantasy scenarios, using widely known cultural myths, appealing to archetypal figures, constructing a series of episodes, and mobilizing well-known

literary tropes such as metaphors. By bringing these components of a story together in a skilful and appealing way, a promoter can craft a new technology as being plausible and appealing to potential constituents such as investors, suppliers and potential clients.

Second, a business model allows a venture to associate itself with a particular *type* or identity, thereby creating a sense of legitimacy. For a firm, adopting a certain business model means identifying itself with similar firms whilst dissociating itself from others. In this sense, a business model is an external identity that a firm can assume (Pólos et al., 2002). External identities are directed at audiences that judge whether an organization qualifies as a member of one group or another. These audiences can penalize organizations for deviating from what they do not consider a valid manifestation of a certain type or in turn reward them for conforming to a certain type (Zuckerman, 1999).

Such considerations are particularly relevant for firms in new technology contexts characterized by high uncertainty over future performance. Early stage organizations often have legitimacy issues with financial investors that they address via impression management and other symbolic management techniques (Zott and Huy, 2007). Similarly, they may try to woo customers using similar techniques, for instance by styling themselves as craft beer producers and hence signaling that they are relevant to certain group of beer consumers (Carroll and Swaminathan, 2000). In this situation, firms may attempt to render themselves identifiable and legitimate by associating themselves with certain business models that form known categories. For instance, an Internet firm might adopt an advertising-centred business model, taking advantage of the existing legitimacy of that model on the basis of success stories such as Google. Because stakeholders recognize this as a legitimate category of organizations, even novel entrants will be granted a legitimacy bonus compared to others sporting an illegitimate business model. This is particularly true for nascent markets where there is little certainty about the value associated with a technology (Sanders and Boivie, 2004). By deploying business models as known categories, they can help firms to obtain legitimacy that in turn may result in real resource flows.

Third, business models provide *recipes* that instruct actors involved with the business what they should do. Managers are often guided in their decision by cognitive

frameworks that privilege certain courses of action to the exclusion of others (Tripsas and Gavetti, 2000). Firms tend to adopt ‘industry recipes’ (Spender, 1989) as simplified ways of conducting business and understanding the environment. These recipes are typically adopted by many firms in an industry and provide practical guides to what a firm in a particular industry does. They constitute mental models that codify some key causal relationships assumed to underpin ‘the business’ a firm believes to be in (Porac et al., 1989). Over time, mental models and strategic choices intertwine to create a stable set of expectations among industry participants (Porac et al., 1989).

But business models are more than just simplified cognitive maps. They often take the form of carefully constructed models, which like an architect’s model, do not just represent reality but also guide the practice of remaking that reality (Baden-Fuller and Morgan, 2010). An instance of models directing the construction of social reality can be found in economics (Ferraro et al., 2005). The Black-Scholes model for pricing financial assets eventually came to shape the markets that they claimed to describe (MacKenzie and Millo, 2003). Business models play a similar role within firms and their ecosystems. Business models tend to be ideal types that may never be instantiated in reality but provide ongoing inspiration for improvement and change. For instance, the ongoing and never-ending efforts to reduce cost at Ryanair, the European budget carrier, are legendary. When Ryanair was at the brink of bankruptcy in the early 1990s, the adoption of the ‘budget airline’ business model provided ongoing guidance for business transformation and eventually became reality (Casadesus-Masanell and Ricart, 2008). However, business models can become locked in when they become entrenched within managers’ cognition or even across organizational fields. For instance, Polaroid Corporation failed to successfully enter the market for digital cameras even though it had developed leading edge technology in the digital imaging field (Tripsas and Gavetti, 2000). Senior management was able to develop new beliefs only to the extent that they were consistent with the ‘razor and blade’ business model underlying instant photography. This example illustrates the power of business models in continuously shaping and reinforcing specific ways of doing business.

## **Conclusion**

The concept of business models constitutes an important addition to the long debate about technology and organization that Joan Woodward (1965) opened up. Reflections on business models have stimulated debates about the implications of new technologies for organizations, and have drawn attention to how firms relate to their ecosystems, in addition to how they are organized. However, many extant accounts of business models view them as naturalist features of firms. In this short paper, we argue that business models are better understood as tools that allow entrepreneurs and managers to imagine and craft organizations adept at drawing value from new technologies. One implication of our analysis is that value is not intrinsic in technologies but has to be realised via suitable and viable configurations of organizational structures and relationships with external actors. The very proliferation of business models in managers' discourse reminds us of the fact that there is no single 'best' business model for exploiting any given technology. Choices have to be made as to how technological affordances can be turned into viable organizations. In this process, business models – as texts – assist entrepreneurs and managers by providing narratives designed to convince constituents of the quality of a firm's business, typifications that create a sense of legitimacy around the venture, and recipes that instruct constituents about what exactly they should do.

We believe this approach to business models offers a way of thinking about how new technologies are configured through constructing a warp and weave of narratives, identities and recipes. Via such performative representations, promoters of new technologies attempt to articulate, instantiate and eventually extract the potential value of technologies. Following our approach, the study of business models should seek to examine more deeply the narrative work used to convince particular constituents, the processes that underlie the emergence of certain well-recognised and legitimate types, and the conditions under which business models as recipes might or might not direct the activities of constituents.

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