Internet revenue models & e-pricing
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WHAT IS AN INTERNET REVENUE MODEL?

- How does a company sustain itself in the long term? That is, generate revenue and profit.
- An Internet business model is the method by which a company plans to make money long term by taking advantage of the unique properties of the Internet.
- Can be either B2B or B2C (or a combination).
- Can be entirely online (what used to be called “PurePlay”), or a mix of bricks and mortar and online activities.
- Ask yourself “where is the money coming from?”
- Businesses that don’t generate direct revenue from online activities need to justify their e-business investment in terms of cost savings / efficiency.
E-BUSINESS MODELS

Business-to-Business (B2B)

Business-to-Consumer (B2C)

Consumer-To-Business (C2B)

Consumer-To-Consumer (C2C)
MAJOR CATEGORIES OF INTERNET BUSINESS MODELS

- Many businesses use a combination of revenue models
- Some common methods of creating a revenue stream due to taking advantage of the internet:
  - Brokerage
  - Advertising / Community
  - Data Broker / Infomediary
  - Merchant
  - Manufacturer / Direct-to-consumer
  - Affiliate
  - Subscription
  - Utility
  - “Sharing” economy / collaborative consumption
Brokers bring buyers and sellers together by creating markets and facilitating transactions. (B2B, B2C, C2C)

Revenue usually comes from fees or commissions charged to either buyers or sellers (or both) for each transaction.

Examples:
- auction sites such as eBay (relies on the "network effect")
- transaction broker – PayPal
- Uber also uses a commission method – they act as the broker between driver and passenger.

11 trips where you kept 70% of total fares

It's a new week and your trips are reset. See if you can top last week's record and keep even more of what you make.
How eBay Makes Money (from marketplaces)?

- Transaction fees on the products sold
- eBay seller services
- Access to eBay marketplace via website and mobile app
- Products for purchase on eBay online marketplace
- Product payments
Let’s see how Uber works
airbnb business model
### The Business Model Canvas

<table>
<thead>
<tr>
<th>Key Partners</th>
<th>Key Activities</th>
<th>Value Propositions</th>
<th>Customer Relationships</th>
<th>Customer Segments</th>
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<tbody>
<tr>
<td><strong>Who are our Key Partners?</strong>&lt;br&gt;Who are our key suppliers?&lt;br&gt;Who are the companies we are acquiring from?&lt;br&gt;Which key Activities do partners perform?&lt;br&gt;Which Key Activities are required to create value for partners?&lt;br&gt;What incentives do partners receive from us?</td>
<td><strong>What Activities do we perform?</strong>&lt;br&gt;What Value Strings do we generate?&lt;br&gt;How do we create value for customers?</td>
<td><strong>What value do we deliver to the customer?</strong>&lt;br&gt;Which of our customers are problematic?&lt;br&gt;Which of our customers are profitable?&lt;br&gt;Which bundles of products and services are we offering to each customer segment?</td>
<td><strong>What type of relationship does each of our customer segments expect us to establish?</strong>&lt;br&gt;What do customers expect us to provide?</td>
<td><strong>For whom are we creating value?</strong>&lt;br&gt;Who are our most important customer?</td>
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<tr>
<td><strong>What Key Resources do our Value Propositions require?</strong>&lt;br&gt;Our Distribution Channels?</td>
<td><strong>What type of resources do we need to generate?</strong>&lt;br&gt;What do we need to change or create?</td>
<td><strong>How do we generate value for customers?</strong>&lt;br&gt;Which activities do we need to perform?</td>
<td><strong>How are we managing our customer relationships?</strong>&lt;br&gt;What are our customer touchpoints?</td>
<td><strong>How do we define our customer segments?</strong>&lt;br&gt;Who are our most important customer segment?</td>
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<th>Cost Structure</th>
<th>Revenue Streams</th>
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<td><strong>What are the most important costs inherent in our business model?</strong>&lt;br&gt;Which Resources are most expensive? Which Key Activities are most expensive?</td>
<td><strong>For what value are our customers really willing to pay?</strong>&lt;br&gt;What do they currently pay? How are they currently paying? How would they prefer to pay? How much does each Revenue Stream contribute to overall revenue?</td>
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ADVERTISING: DISPLAY AND SEARCH ADVERTISING

- Company provides web site content/services to users at no (or lower) direct cost in exchange for the viewing of, or interacting with, advertising messages of various types. For example:
  - Facebook’s revenue for the full year 2016 was $27,638 billion
  - Google’s revenue for 2015 was $74.5 billion

- Advertising is often used in combination with other methods of creating revenue

- What are the biggest challenges for advertisers at the moment?
  - Rapid growth in Ad-blocking
  - Programmatic advertising and ad-fraud / bots
“When something online is free, you’re not the customer, you’re the product.”

Variously attributed to Bruce Schneier (October 2010) and Douglas Rushkoff (September 2011)
Classifieds – a subset of the advertising model, where typically a listing fee is charged

Examples: Monster.com, Craigslist.com

This shift of classifieds to the web has threatened which traditional industry?
LET'S SEE CRAIGSLIST
All craigslist postings are free, except for:

- Job postings in selected areas—$7-75 (fee varies by area)
- Brokered apartment rentals in NYC area—$10
- Various by-dealer categories in the US—$3-5
- Cars/trucks by-dealer in the US, Vancouver BC—$5
- Furniture by-dealer in the US, Vancouver BC—$3
- Therapeutic services in the US—$10 (reposts of live ads $5)

Visa, MasterCard, and American Express are accepted.

Paid posting accounts provide additional payment options in many cases.
MONETIZING COMMUNITY

• Relies on user loyalty, social networking, and user-generated content (UGC)
• Relies heavily on the “network effect” to attract and keep visitors
• Users are often also contributors of content and knowledge eg. Video (YouTube, Vimeo), book reviews (amazon.com), Gear Swap (mec.ca), forums (steam.com), personal information (Facebook etc)
• Free content for the web site owner / publisher. Free information about users (market intelligence)
• Attractive to advertisers – many community sites rely on advertising for revenue
DATA BROKER (INFORMEDIARY) MODEL

- Businesses that collect and provide information - typically data about user behaviour and preferences that is sold to interested parties
- Revenues come from sales of data about consumers that they collect by various means
- Examples: audience measurement and market research agencies such as Nielsen, and data mining firms like Acxiom
Nielsen Business Model

We provide...
- Retail sale measurement of consumer goods in stores
- Measurement of TV viewing, online surfing, and mobile phone activity

This helps...
- Consumer packaged goods clients
  - Enhance sales and marketing
  - Optimize pricing and promotion
  - Monitor distribution and inventory
- Media clients
  - Price advertising inventory
  - Maximize value of content
  - Plan, optimize, and measure ad spending

An example...
- P&G
  - Multi-year contract
  - 70+ year relationship
- NBC Universal
  - Multi-year contract
  - 50+ year relationship

*From Nielsen’s Investors Presentation*
Retailers and wholesalers of goods and/or services.

Make money from the profit margin on sale of goods (purchased from suppliers and held in inventory)

Very commonly used business method on the internet

May be:

- Online only eg. Amazon.com (except for their physical bookstores, Amazon Fresh pick-up spots, and Amazon Go)
- Bricks and mortar / online hybrid eg. Best Buy
- Online vendors - deal in purely digital products (software, music, images, video) eg Steam, iTunes
- Catalog merchant – eg. Lands’ End, MEC
• Commodity item – product that is hard to distinguish from the same products provided by other sellers. Very well suited to eCommerce.

• What is the Shipping profile? – collection of attributes that affect how easily a product can be packaged and delivered.

• Is it a high-touch item?
  – But shoes and clothing are successfully sold online – the key is in the return policy (eg. Kit and Ace: “shipping and returns are always on the house”)

• Is it an impulse / must have it right now?

• Note that pretty much everything is now bought and sold online (with just a few exceptions)
POSSIBLE PROBLEMS OF MERCHANTS OPERATING ONLINE & IN-STORE

Problem:
Cannibalization of one sales channel by another

Solution:
Web sites provide product information only – no ecommerce capability - directs customers to physical stores eg. Canadian Tire has a select online / pick up in-store model

• What is the problem with this strategy?
WHAT ABOUT THE WAREHOUSE MANAGEMENT?
POSSIBLE SOLUTIONS

- **Real-time synchronization** (higher infrastructure and management costs)
- **Scheduled synchronization** (periodic updating of the site with warehouse data; saves infrastructure costs)
- Simulation of the **double warehouse** (preventive allocation of the number of pieces to be sold online)
- **Synchronization on demand** (stocks are checked only after the product has been placed in the virtual shopping cart)
- **No management**
• The manufacturer or "direct model" is based on the power of the web to allow a manufacturer or producer (i.e., a company that creates a product or service) to reach buyers directly without any retail intermediary.

• This compresses (shortens) the distribution channel.

• Advantages: efficiency, improved customer service, and a better understanding of customer preferences. eg. Amazon Kindle, Dell, authors, indie musicians and artists etc.

• So why don’t all manufacturers sell direct?
How NIKE Makes Money?

- Contract Manufacturers:
  - Finished goods ready for retail and/or public consumption
  - Finished goods payments
  - Technology transfer
  - Investments in building sustainable & profitable business model
  - Brand premium
  - Goodwill

- NIKE:
  - Logistics costs including, shipping and handling costs
  - Revenues for buying the products and keeping inventories
  - Direct selling through a) NIKE brand and category experience stores b) online sales through www.nike.com and c) NIKE factory stores

- Influencers

- Dealers

- Customer Segments:
  - Footwear
  - Apparel
  - Equipment

- Cost Elements
- Revenue Elements
Affiliate Model

- An affiliate gets paid for sending customers to other sites by providing purchase opportunities wherever people may be.
- The affiliated sites provide a click-through link to the merchant site in exchange for a percentage of revenue if the visitor makes a purchase of the item clicked on. The link contains tracking code/cookies.
• Goods or services available by subscription (all you can eat model) Eg. Netflix, Globe and Mail, Spotify
• Users are charged a periodic -- daily, monthly or annual -- fee to subscribe to a service.
• Subscription fees are incurred irrespective of actual usage rates.
• Subscription and advertising models are frequently combined.
FREEMIUM

- It is quite common for sites to combine free content with "premium" (i.e., subscriber- or member-only) content – also called “freemium”
- Users of the web site or internet service are charged for “premium” content or service
- Newspapers, magazines, music, video, games etc, eg Slack (business messaging app)
- Networking / job searching on LinkedIn Pro
- The challenge for the company is to get the right balance of free / paid service
Business Model 101: Multi-Sided Customer Segments

HR Managers

A Multi-Sided Platform serves different target customers. Yet they are highly dependent on each other.

Therefore, it makes sense to serve both sides. In fact, that is how the overall platform gains value.

Thus, LinkedIn offers Hiring services to HR managers. Professionals, instead, can join the learning and development platform.

That is how hiring services become more valuable for HR managers because they can find more qualified candidates.

Also, professionals will find more value with subscription plans, since they will find a job more easily.

LinkedIn Hiring

Learning & Development

by FourWeekMBA.com
• The utility or "on-demand" model is based on metering usage, or a "pay as you go" approach.

• Unlike subscriber services, metered services are based on actual usage rates.

• Amazon Web Services (AWS) – "cloud computing" services (short video)
• Refers to internet-enabled software platforms that allow individuals (or firms) to “rent” assets (human and physical) owned by other individuals or firms.

• The software enables the market by connecting the person with the asset with the person who needs it. For example:
  – Cars eg. Uber and Lyft
  – Rooms – eg. Airbnb
Figure 1: The Sharing Economy business model; Source: Business Model Toolbox
E-pricing strategies
Buyers and sellers views of pricing

- The meaning of price depends on the viewpoint of the buyer and seller.

- Each party to the exchange brings different needs and objectives that help describe a fair price.

- If buyer and seller can’t agree on a fair price, then there is no sale.
Buyer perspective on price

- Buyers define value as **benefits minus cost**

- **Costs to the buyer**
  - **Money** – what is the real cost? How is it calculated; what does it include (shipping, taxes, duties, gift wrap)
  - **Time** – finding what you want, waiting for it to arrive, slow web sites
  - **Energy** – Web = self service, so no-one to help in research and locating an item
  - **Psychic costs** – frustration, lack of trust of web commerce, lack of confidence in on-line service delivery etc.
Seller perspective on price

- Sellers concerned with **profitability** — but there is some freedom to set price at a level that will draw buyers away from competing offers

- Profit lies between cost and price
- Affected by both internal and external factors

- External factors:
  - *Market structure and type of competition*
Internal factors affecting price for sellers

- Depends on pricing objectives (e.g., volume; building market share; high profits; matching competition)

- **Factors that push prices upwards** –
  - cost of distribution
  - commissions to affiliates
  - site development
  - customer acquisition costs

- **Factors that depress prices** –
  - Order processing – self service
  - Just-in-time inventory
  - Overhead (physical vs. online store)
  - Customer service costs lower
  - Printing and mailing costs
  - Digital product distribution costs
Pricing strategies

- **Fixed pricing** (similar to offline pricing strategy)
  - Price leadership
  - Promotional pricing

- **Dynamic pricing** (Internet-enabled pricing)
  - Auctions
  - Segmented pricing (geographic or based on customer profile)
Pricing Strategies: FIXED PRICING

- Occurs when sellers set the price, and buyers must **take it or leave it**
- Everyone **pays the same**
- This strategy is very **common in retailing**

- 2 types of fixed price strategy are
  - Price leadership
  - Promotional pricing
Fixed pricing: Price leadership

- A price leader is most often, but not always, the lowest-priced product entry in a particular category. The price leader is the one that sets the price levels for the market. Others follow the leader with comparative pricing (usually higher).

- Walmart is an example of a “low price” price leader that uses technology to leverage its costs and maintain profitability.

- An online company such as www.Buy.com consistently offers lower prices. It sells below market value and subsidizes price cutting with advertising on its web site.

- Very hard to maintain price leadership and remain profitable as the lowest price.

  - Can you think of industry examples where the price leaders have higher prices?
  - How do they succeed?
  - What does this mean for the internet market? How could you be a higher-priced price leader?
Fixed pricing: Promotional pricing

- This strategy used to encourage a first purchase, encourage repeat business, and close a sale.

- Promotions tend to carry an expiry date – creates a sense of urgency.

- Price promotions can be highly targeted using email and on web sites that use clickstream analysis (then it becomes dynamic).
Pricing strategies: DYNAMIC PRICING

- Dynamic pricing is fluid pricing
- Dynamic pricing is one of the most significant contributions the Internet has made to pricing strategy.

- Decreased “menu” costs on the web - **changing prices is easy** (no costs of changing price tags, catalogs etc)

- **Interactivity** - buyers and sellers from all around the world can interact and negotiate prices
Dynamic pricing: Auctions

- Variety of auction types
  - "English" auction - such as e-Bay where the price starts low and is then driven up
  - "Dutch" auction - the auctioneer announces a high price for the product, then gradually reduces it until a buyer will accept it
Dynamic pricing is also the strategy of offering different prices to different customers. It optimizes inventory management, segments customers by product use or other variables (e.g., frequent or infrequent purchasers), and web-based technology and database marketing have made this strategy much easier to implement.
Dynamic pricing: Segmented pricing

- Where the company sells goods or services at two or more prices, based on **segment differentiation**
- automatically generates a different price depending on a number of **pre-set variables or decision rules**

- The Internet gives the ability to recognize a consumer, then customize prices, segmenting sometimes to a segment of one
  - eg. anyone who has previously purchased 10 items gets a discount
  - May use your IP address to offer a product at an introductory price
  - May use behavioural cue: eg. if you abandon your shopping cart
Segmented pricing: geographic segments

- A company sets different prices when selling a product in different geographic areas.
- Uses IP address of user to guess at their location.
- Prices can then be related to circumstances in different countries – local competition, economic conditions etc.