



## Note on Debate over Relationship Between Business Model and Strategy\*

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### Abstract

**Purpose** – This short paper reviews the debate dealing with the relationship between strategy and traditional strategy approach on the one hand, and business models and new business model approach on the other hand and tries to offer useful direction to be more helpful to theoretical discussions.

**Research design, data, and methodology** – This paper makes a theoretical analysis to explain the confusion surrounding the debate, reviewing mainly literature survey papers and finds theoretical conjecture and its limitations in order to present useful direction to the future theoretical work.

**Result** – In order to comprise its diversity, business model studies should consider the characteristics of each firm, sector, and market. Adding further elements which are related to each sector or market, theoretical studies can capture the diverse phenomena related to business model and business model innovation.

**Conclusion** – The traditional strategy perspective can be utilized to the Business model phenomenon in the case of incumbent firms and non-digital sector and existing markets. Meanwhile the new business model perspective can be utilized to business model phenomena in case of start-ups and digital sector and emerging markets. Reconciling two perspectives, the studies dealing with the business model should focus on the characteristics of firms, markets, and knowledge from the perspective of business model innovation.

**Keywords:** Business Model Approach, Strategy Approach, Business Model Innovation, Existing Market, Emerging Market

**JEL Classification Code:** O3, M1.

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## **1. Introduction**

These days the focus of competition centers on the novel business model based on changing business landscapes (Teece, 2010). Even though there have been enormous business' endeavors to make an effective and sustainable business model, academic community has a long way to go to build a consensus on the definition of business model (Wirtz et al, 2016; Zott et al, 2011; Klang et al, 2014; Goyal et al, 2017; Bigelow & Barney, 2021). This discord may hinder enhancing understanding on the new way of competition based on business models and make a confusion on the proper addressing of business issues faced by incumbent or start-up firms. What is the business model, that is, which elements compose a business model, which function it performs? Such questions do not find a consensus.

One of the reasons is that the new business model and the decay or failure of old business model provoke an immediate trial from diverse disciplines (Wirtz et al, 2016; Foss & Saebi, 2017) and each work is based on the different status of firms and industries. These diverse concepts of business model led to the diversity of the interpretation on the relationship between business model and strategy (Zott et al, 2011, Wirtz et al 2016, Massa et al, 2017). These two points consist of the main debate surrounding the business model, in specific, what is the business model and what is the relationship between business model and strategy. The massive popularity of the business model concept and at the same time the confusion in academic work is what happened around the business model.

Previous literature tried to compromise this situation by summarizing and analyzing literatures dealing with the business model concept itself and the relationship with the business model and strategy. This literature helps to clarify the difference between business model approach and traditional strategy approach, making progress on the understanding of the concept of business model. But they also have some shortcomings.

Our position is that the latter debate is important for finding the avenue for the first debate. It is because the characteristics of business model concepts can be elaborated through the relationship between business model and strategy. The relationship can be utilized as a shared platform for advancing further theoretical discussions because the strategy has some solid theoretical background. The debate over the business model concept itself without any shared platform may not be converged if they deeply depend on each perspective and each different reality. Meanwhile, the debate over the relationship may be influenced by the existing coherent discourse of strategy, so that can be a shared platform for upgrading the discussions.

However, they have some limitations in that focusing on the difference forces them to narrow their attention, the concept of business model becomes a strict one to be applied. Even though it can be a logical one, it may not be helpful to capture the diverse business model-related business phenomena and to do an essential task with the business model. This short paper tries to explain the confusion surrounding the debate, reviewing mainly literature survey papers and offer useful future direction to be more helpful to theoretical discussions from the perspective of business model innovation.

For this aim, the next section tries to summarize the debate. Based on this summary the following section gives a critical review of it and its limitations and suggests extra considerations to be needed. Lastly this short paper makes a close by presenting a way of reconciling theoretical discord and future directions.

## **2. Theoretical Debate**

The debates over business models are mainly focusing on two aspects, that is, the business model concept itself and the relationship between business model and strategy. Firstly, we review the first debate and later the second debate.

Zott et al (2011) find out the common theme which business model literature has shared. First, the business model is a new unit of analysis that is distinct from the product, firm, industry, or even network and its boundaries can be wider than those of the firm. Second, business models emphasize a system-level, holistic approach to explaining how firms do business. Third, the activities of a focal firm and its partners play an important role in the various conceptualizations of business models. Last, business models seek to explain both value creation and value capture. It is also shown that the centrality of the notion of value is dominant in the business model literature. However, irrespective of these common themes, the concept of business model does not converge.

The business model at a general level has been defined or referred to with diversity as follows. It can be a statement, a description, a representation, an architecture, a conceptual tool or model, a structural template, a method, a framework, a pattern, and a set (Zott et al, 2011). Similarly, the business model is commonly described and reflects on (1) organizational design, (2) the resource-based view of the firm, (3) narrative and sense-making, (4) the nature of innovation, (5) the nature of opportunity, and (6) transactive structures (George & Block, 2010). According to Massa et al (2017), regarding the meaning and function of business models, three interpretations have been submitted.

Firstly, business models as attributes of real firms, secondly, business models as cognitive/linguistic schemas as observable manifestations, and lastly business models as formal conceptual representations of how a business functions (Massa et al, 2017; Cosenz & Noto, 2018). Each of the elements of a business model is affected by a firm's value configuration depending on whether the firm is a value chain, value shop, or value network (Fjeldstad & Snow, 2018).

The reasons for this divergence can be attributed to two factors. First, each scholarly work has a different academic background such as organizational studies, strategy studies, innovation studies, entrepreneurship studies etc. Second, it has kept a different situation in mind, such as different industries, different firms with different conditions. At the same time, it is necessary to remark that research related to business models in general has been provoked by the unusual phenomenon such as tremendous change of business model, rather than the theoretical work aiming to improve the understanding with challenging existing theoretical works. Considering these factors, the divergence seems to be even natural based on the existing theoretical landscapes.

Since the fascinating growth of literature focusing on BM, one of ensuing natural interest is the relationship between business models and strategy. It is because both terms address the overall direction of business. However, there is still no coherent understanding about cause-effect relationships and mutual dependencies in the linkage between the firm strategy and the business model (Spieth et al, 2016)

Conceptually there may be four cases. We can refer to Gorynia et al (2019) and Seddon et al (2014). Firstly, firm strategy and business model cover other areas of activity. Second, the subordination of firm strategy to the business model. Third, the company's strategy is superior to the business model. Lastly, the concepts of the company's strategy and business model are interchangeable.

George and Bock (2010) compare business model with strategy as follows. Strategy is a dynamic set of initiatives, activities, and processes; the business model is a static configuration of organizational elements and activity characteristics. A strategy may be reflexive, initiating change within the organization that impacts the emergent strategy; a business model is inherently non-reflexive. Business models are opportunity-centric, while strategy is competitor or environment centric. A business model is the organization's configurational enactment of a specific opportunity; strategy is the process of optimizing the effectiveness of that configuration against the external environment, including the potential to change the configuration, alter the underlying opportunity, or seek out new opportunities.

The cognitive processes associated with opportunity identification and enactment focus may or may not incorporate firm level strategic thinking, but the firm formation decision is based on the enactment of an opportunity through an explicit or implicit business model. The business model is therefore a core building block of the entrepreneurial enactment process of any opportunity (George & Block, 2010)

As such there are two main differentiating factors (Zott et al, 2011). The first is the traditional emphasis of strategy on competition, value capture, and competitive advantage, whereas the business model concept seems to focus more on cooperation, partnership, and joint value creation. The second factor is the focus of the business model concept on the value proposition and a generalized emphasis on the role of the customer, less pronounced elsewhere in the strategy literature. In this vein, their relationship is argued to be complements rather than substitutes (Zott & Amit, 2008) Seddon et al (2004) argues that a business model is viewed as an abstraction of a firm's strategy, and it outlines the essential details of a firm's value proposition for its various stakeholders and the activity system the firm uses to create and deliver value to its customers. However, unlike strategy, business models do not consider a firm's competitive positioning (Seddon et al, 2014).

How the concepts of strategy and business models relate to each other can be related to the question, whether business models determine strategies, or whether strategies precede business models (Seddon et al., 2004, Friis et al 2015). Some work tried to solve this puzzle by empirical investigation of real firms (Friss et al 2015, Cortimiglia et al, 2016). Whether the strategy is a reflection of the business model or vice versa depends on the phase in the business lifecycle of the company. (Friss et al 2015). Cortimiglia et al (2016) argues that business models are related to strategy execution during strategy making process, using quantitative surveys on 138 companies and case study.

Shortly reviewing, we come to find that it is inevitable to differentiate the theoretical construct from theoretical approaches which have nothing but their own specific set of logic. While strategy can be defined as a unifying theme that gives coherence and direction to the actions and decisions of an individual or an organization (Grant, 2010), strategy approach may be attributed to a traditional strategy school such as positioning school and capability school. Existing works, particularly works dealing with literatures do not explicitly distinguish these two things, and therefore naturally mixed up two things and fell into a confusion. For instance, while strategy and business model can complement each other, the theoretical approaches, focusing exclusively on the former or the latter can exclude each other. Bigelow and Barney (2021) exactly distinguish two things from the perspective of a strategy scholar and try to point out the theoretical contribution of business model perspective, compared with the received strategy literature.

Among the numerous literatures dealing with Business models, one of the outstanding works is Massa et al (2017), which gives an elaborate organization of the relationship between business model approach and strategy approach. Massa et al (2017) summarize the debate by dichotomizing two perspectives. The first is more traditional, which argues the business model is just one domain composed by strategy studies. The second focuses on the newness of the business model, arguing that separate studies are necessary, independently from the traditional strategy discourse. In other words, the typical position is related to the question, which is whether the business model is a separate field or not, therefore whether independent research on the business model is necessary or not. The latter position argues that the traditional strategy approach can be extended to exploring business model questions. It focuses on the means to compete as a function of business model.

Traditional perspective starts from the argument by M. Porter. Porter (2001) underestimating the influence of internet technology, argues that the business model, simply a loose concept of how to do business and generate revenue, could not be defined clearly and therefore would make a delusion and shift from the truly important elements of strategy such as creating economic value and industry structure. This argument is based on the early stage of internet technology and so-called dot-com bubble and following the dot-com crash. This perspective stemming from the positioning school and capability school views business models as a means to compete and does not consider the mechanism through which value is created (Massa et al, 2017).

As a typical study, Casadesus-Masanell and Ricart (2010) argues that business model refers to the logic of the firm, the way it operates and how it creates value for its stakeholders, and strategy refers to the choice of business model through which the firm will compete in the marketplace. For them, the object of strategy is the choice of business model through which firms intend to compete. They analyzed Ryanair, their argument is as follows.

“The high-level election to ‘become the Southwest of Europe’ was the company’s strategy - its plan of action to create a unique and valuable position by engaging in a new set of activities. The particular way in which Ryanair executed such plans was its realized strategy. The resulting business model - with its new logic, new way to operate, and new way to create value for its stakeholders - was the new Ryanair. (p. 204)”

Thus, strategy refers to a firm’s contingent plan as to which business model it will use. It is important to note the word ‘contingent’ - strategies should contain provisions against a range of environmental contingencies, whether they take place or not. An outside observer will only be able to observe the realized strategy, rather than the entire contingent plan. To them a business model is a tool to execute a strategy, whereas a strategy is a kind of vision to access to the goal.

Second approach is argued to be related to two considerations (Massa et al, 2017). First consideration has something to do with the decoupling of value creation and revenue creation. Second consideration is related to the creation of value itself made by a new business model. Therefore, unlike the traditional strategy approach, the business model approach places a highest emphasis on value creation for target customers and for the shareholders surrounding the focal firm. In addition, suitable for its attention to practical use, it lays stress on the discovery and experimentation rather than careful calculation and precise analysis. This approach has something with recent discussion on the business ecosystem (Adner & Kapoor, 2010) and demand-side perspective on strategy (Priem, 2007)

As a typical study, McGrath (2010) argues that unlike conventional strategies that emphasize analysis, strategies that aim to discover and exploit new models must engage in significant experimentation and learning, rather than analytical approach. In the same vein, Chesbrough (2007) makes a request for incumbent firms to conduct some experiments, gather the evidence, identify the most promising direction, and then run some further experiments, for a promising business model to be scaled up. Priem et al (2018) suggests that while mainstream strategy research centers on value capture for the firm, both the demand-side and business model streams highlight the strategic relevance of consumers and the importance of creating value for them

This work such as Massa et al (2017) can be interpreted as a typical work focusing on the debate among theoretical approaches rather than theoretical construct itself. Therefore, their organization of prior arts relating to business model discourses can be clarified, compared to other literature survey papers. Furthermore, it can advance the reasons for disagreement.

### **3. Review from the viewpoint of business model innovation – Area matters**

The debate should be viewed from the fundamental questions related to business model or essential tasks with the business model. The fundamental question is how to adapt and change the existing business model according to the changing business landscapes. For incumbent firms the starting point is their old business model which was built long ago. For start-ups the starting point is the other existing firms’ business model, and their effort is toward the departure

from it. Based on this rationale, the debate has to be viewed, assessed, and complemented from the perspective of business model innovation, which contains and is aware of the essential task with the business model.

Since the dot-com bubble, the business model has been regarded as a unit of innovation, in addition to traditional product innovation and process innovation. Since then firms can innovate their business model and feel obliged to renew or newly create their proper business model in order to survive in a turbulent environment.

Foss and Saebi (2017) distinguish four streams of business model innovation research, even though they do not lead to a cumulative research stream. The first one is conceptualizing business model innovation. Second one studies the organizational change processes that are needed to implement successful business model innovation. Third one deals with the outcome of the new and innovative business models. Last one is focusing on the organizational performance implications of business model innovations. According to these works it has come to be apparent that firms can introduce change into the design and architecture of their business models that are novel to a context and potentially build the basis of substantial appropriable value creation and competitive advantages (Foss & Saebi, 2017)

Practically, business model innovation through developing alternative business models can be explored through modifying a single business model element, altering multiple elements simultaneously and/or changing the interactions between elements of a business model (Ramdani et al, 2019). When trying to change business model, business model innovators usually face four strategic trade-offs and accompanying tensions during the implementation of their business model innovation process: (1) the level of independence granted to the developer (independence vs. dependence), (2) the degree to which the roadmap is planned in advance (discovery vs. planned execution), (3) the degree to which the value proposition challenges the status quo (challenging vs. maintaining status quo), and (4) the rigor to which business model innovators preserve the logic of the initial value proposition (solid vs. fluid logic) (Broekhuizen et al, 2018). These logics of business model innovation can be utilized for assessing the debate.

Massa et al (2017) try to explain the difference between two perspectives focusing on the relaxation of strict assumptions as academic studies have evolved. They argue that business models may be challenging the assumptions of traditional theories of value creation and value capture. The assumptions being challenged by the business model approach are 1) perfect information of firms and customers, 2) unlimited cognitive abilities and independent act of firms and customers, 3) no externalities and 4) single-sourced and only supply-side competitive advantage. This challenge looks like the one of positioning view toward main economic theory such as theory of perfect competition and the one of resource-based view toward positioning school. Their attempt gives a useful theoretical insight into the diversification and background to enhance the non-converging trend among perspectives.

However, it also has adverse effects. Even though it is more realistic to relax the strict assumptions, the new perspective focusing on business models departed from the traditional strategy perspective is engendering too strict focusing on specific business models. From the viewpoint of business model innovation, business model-related phenomena can be diverse from simply changing some minor elements to creating completely new elements and its architecture. The business model perspective departing from the traditional one can make study objects too narrow, therefore it can be a barrier to capture diverse business model-related phenomena and simple innovation of business model. Rigorous logic can be obtained with the sacrifice of overlooking the fundamental question, which engendered the business model innovation perspective. Broekhuizen et al (2018) even argues that business model innovators make pragmatic decisions that may deviate from the guidelines offered by existing literature.

Because business model innovation can either be evolutionary or revolutionary, approach toward it should comprise both things. In order to comprise its diversity and properly address the fundamental questions, business model studies should consider the major characteristics of each firm, sector, and market. Adding further elements which are related to each sector or market, theoretical studies can capture the diverse phenomena related to business models, and contribute to the innovation of business models. Further elements can be considered as follows.

Firstly, the difference between incumbent and start-up firms can be considered. In case of incumbents, existing resources can be constraint factors or asset factors, therefore, any discussion related to the business model may comprise these factors. However, in case of start-ups the focus should be factors related to new market opportunities and their attempt to address the opportunities can be limitless without constraint theoretically. Strict Business model perspective can be hindering the attempt and constraint of the first type of firms.

Secondly, the difference between digital sector and non-digital sector can be considered. Even though the development of digital technology causes the enormous expansion of the digital sector, a considerable share of industry stays in the non-digital sector and is not easily transformed into digital one because of its technical characteristics. There are considerable differences between the digital products and services, and non-digital products and services. Therefore, its difference should be considered in order to elucidate the whole picture related business model phenomenon. The difference between software and hardware, typically the difference between the service of Google and firms producing energy can be a good example.

Thirdly, the difference between existing markets and newly emerging markets. This difference can be overlapped with the second difference but is conceptually separate consideration. The difference can be shown typically in the customer-firm relationship. The relationship in existing markets cannot be the same with one in emerging markets. The difference of value setting and price system is apparent. In the case of existing markets, the level of value of a specific product or service is normally already shared by customers and firms, even roughly. This can function as a kind of benchmark. However, in emerging markets it is not certain what is valuable, which measures the proper level of value considered by customers, and what is the reasonable price system. Being based on these different market contexts, the attempt to relate to the business model and its outcome cannot be the same.

As such, the major characteristics of each firm, sector, and market such as 1) incumbent firm vs start-up, 2) digital sector vs. non-digital sector, 3) existing markets vs. new markets have to be considered for effectively understanding the business model innovation. These points are the factors previous work does not pay enough attention to.

#### 4. Concluding remarks and future directions

This paper tries to explain the confusion surrounding the debate, in particular the relationship between strategy and business model, reviewing mainly literature survey papers and offering useful future direction from the perspective of business model innovation. Even though some work shows improvement and reasonable explanation on the divergence of each view, the theoretical rigor can be obtained at the sacrifice of embracing diversity, which is central to changing business models.

After all, it is necessary to accept that 'one size fits all' does not hold. From our point of view, the traditional strategy perspective can be utilized to the business model phenomenon in the case of incumbent firms and non-digital sectors and existing markets. Even though their perspective should embrace new elements such as the effect of heightened customer and digital technology, their perspective can be extended to business model phenomena in this type of cases.

Meanwhile the new BM perspective can be utilized to business model phenomena in case of start-ups and digital sector and emerging markets. The new business model perspectives comprise all elements of the business model phenomenon, their focusing may be narrowed like the traditional perspective when the emerging market enters the maturity stage.

Reconciling two perspectives, the studies dealing with the BM should focus on the specific characteristics of firms, markets, and knowledge. At this point, it can be useful to refer to discussion on the sectoral innovation system (Malerba, 2005) which gives an importance to sectoral difference based on the difference of knowledge.

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