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Accounting for the Apple Inc business model: Corporate value capture and dysfunctional economic and social consequences

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ABSTRACT

In this special issue the authors account for the Apple Inc innovative business model in terms of its capacity to create and capture value from its global supply chain. The authors argue that there are a number of reasons why the Apple business model may not be sustainable and more broadly explore the dysfunctional social and economic aspects of corporate behavior that seeks to fragment and elongate global value chains to capture value within the firms financial reporting boundary whilst displacing cost and risk.

Apple Inc is known for its CEO Steve Jobs, who achieved iconic status with the production and marketing of digital lifestyle products, especially the iPhone and the iPad, and preceding them the iPod that have put highly sophisticated technology in the hands of consumers. Innovative products coupled with adaptations to the Apple business model captured value and generated spectacular returns for investors. In terms of generating shareholder value this was a brilliant success. In this special issue the authors generate a variety of accounts about the nature and extent of transformation of the Apple business model. These accounts draw attention to a general paradox in terms of how the Apple business model contemporaneously captured value with the reporting entities financial boundary and displaced costs and risks. This process of economic and social displacement is dysfunctional because at the same time as it promotes value capture it also threatens to undermine Apple's ongoing sustainability. The second set of papers in this special issue extend this idea about the dysfunctional economic and social consequences of business models to inform policy making and generate relevant corporate social responsibility disclosures.

The first four papers in this special issue are specifically about the Apple business model: how it is constituted and to what extent it is sustainable. The authors of this group of papers share a common objective, which is to conceptualize the Apple business model and provide a series of accounts about its evolution, development and financial sustainability. The Apple business model has evolved over time where value creating activities arising from innovation are blended with value capture from the exercise of power over suppliers and customers. Where, both value creation and value capture helped to transform Apple's operating financials, share price and market value (MV) for shareholders. The Apple business model is about how and in what ways stakeholder relations can be manipulated to modify financial boundaries and transform internal financial operating ratios. Apple's financial transformation can be located within the prism of double entry book-keeping that ensures that one firm's financial transformation is mirrored by a displacement of cost and risks into a broader economic and social space. The final set of papers in this special issue focus on UK food retailers and the London Borough of Enfield where the authors explore how opportunist dealing and displacement of financial values and risk leads to dysfunctional economic and contradictory social outcomes.

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Lazonick, Mazzucato and Tulum (*Apple's changing business model: What should the world's richest company do with all those profits?*) consider the future of industrial R&D by reviewing the: 'evolution of strategic control, organizational integration, and financial commitment as conditions of innovative enterprise that ultimately determined Apple's success'. On the nature of strategic control the authors argue that: 'Steve Jobs led Apple as a professional manager, not an owner, who was driven by the desire to produce superior digital devices that would find demand, even at premium prices, in mass markets'. And that 'the development of Apple's epoch-making digital devices entailed a high degree of organizational integration of large numbers of people with a wide-range of functional specialties. This organizational integration was fundamental to the development of the technologies that underpinned Apple's growth'. This combination of elements helped to generate strong profits, which were re-invested into the innovation process.

Lazonick, Mazzucato and Tulum's argument is that the Apple business model can be critically understood in terms of a framework of analysis that conceptualizes the *innovative organization*. Where an innovative organization can be evaluated in terms of three constituent elements: the nature of strategic control, organizational integration and financial commitment to innovation. The authors reveal how the emphasis given to these elements changes over time and summarily reflected in, for example, Apples strategic commitment to R&D spend which falls from 10% to 2% of sales over the two decades 1992–2012, its fragmented organization structure from outsourcing and off-shoring, and adaptation to shareholder activism by distributing more of its cash as dividends and share buy-backs.

Haslam, Andersson, Tsitsianis and Yin's '*Apple's financial success: The precariousness of power exercised in global value chains*' observe that Apples success is represented in the form of financial 'point values' by financial analysts and these multiples are then employed to estimate a share price and market value. The authors argue that these aggregate financial ratios need to be deconstructed to reveal the evolution and adaptation of the Apple business model around the strategic objective of value capture. Using financial information from Apple's annual reports the authors reveal how the firm's financial boundary is modified as it out-sources manufacturing, reduces spend on R&D and captures margin from retail sales.

> Apple exercised power to externalize expenses such as product development and component manufacture whilst capturing value extracted within the boundary of its own financial accounts in the form of inflated cash margins and return on capital.

This process of contemporaneous value capture and financial displacement into the supply chain is located within a prism of variable power relations, and this frames their argument about the precarious nature of Apple's profit margins and returns on capital. Significantly, the authors reveal that Apples financial transformation only brings it back to levels comparable to its peers (Intel, Microsoft, IBM) and that this transformation depends upon the continued exercise of power over suppliers. These power relations are complex, variable and contingent and, as the authors argue, do not straightforwardly guarantee value capture going forward.

Bergvall-Kåreborn and Howcroft's paper (*The Apple Business Model: Crowdsourcing mobile applications*) considers Apple's rapid dominance of the mobile market. This they argue led to the emergence of a business model that weaves together internet-enabled mobile devices with digital content, brought together within a closed proprietary platform or ecosystem. The authors employ a global production network (GPN) analysis based on fieldwork among Apple mobile application developers in Sweden, the UK, and US. Crowd-sourcing, the authors argue: 'allows Apple to effectively source development to a global base of software developers, capitalizing on the mass production of digital products, while at the same time managing to sidestep the incurred costs and responsibilities associated with directly employing a high-tech workforce'.

The authors note that this modification to the business model is not without risk: 'The Company relies on third-party intellectual property and digital content, which may not be available to the Company on commercially reasonable terms at all'. The "apps" that are developed and then used on an Apple device that are downloaded from its ITunes store and Apple, in return, takes a 30% top slice of the total revenue received before paying apps developers.

> I find it very unfair that 30% of my application bill goes to a company that had nothing to do with it. Apple gets the money from the actual hardware [iPhone] and even the software [SDK] they created. When you develop apps this makes the phone better, so Apple shouldn't then be making money out of developers as well.

The Apps developer is also placed at some distance from the consumer in terms of capability to adjust quickly to feedback and also dependent upon the apps approval process and timescale set by Apple. According to the authors: developers shoulder the burden of costs while Apple circumvents the investment and resources required for in-house product development and marketing. This is the essence of crowd-sourcing: harnessing creative labor at little or no cost, while minimizing risk. Yet for the Apple business model there are risks associated with sustaining the relationship with apps developers who can easily move to another software operating platform such as html-5, which could disconnect apps developers from hardware manufacturers (see Haslam et al., 2013).

In the paper by Montgomerie (*Owning the Consumer – getting to the core of the Apple business model*) the authors draw on the existing business model literature to argue that a central element of the Apple business model is its ability to 'own the consumer'. In short, the Apple business model is designed to drive consumers into its ecosystem and then hold them there.

> Apple dominates the retail landscape by acting as both a primary supplier of hardware to retailers but also as a major competitor through its own retail stores. Apple then ensures consumers are "locked-in" to the multi-channel platform by imposing high switching costs as Apple content can only be played on Apple hardware.