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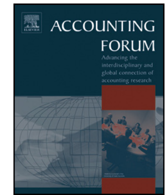

Owning the consumer—Getting to the core of the Apple business model

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ABSTRACT

This paper uses a business model framework to analyze the main limitations of Apple Inc. post-2003, a significant turning point in the company's history. As such, we move beyond an exclusive focus on what makes Apple unique or different by evaluating the mundane and out-dated elements of its business model. To do so, we examine the end-to-end supply chain, from source to store, to present a more holistic evaluation of the Apple business model. Drawing on the existing literature, we argue that the quintessential 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, which has been hugely successful to date and has allowed Apple to wield enormous power in the end-to-end supply chain. We demonstrate this through a detailed evaluation of Apple's physical and content supply chains and its retailing strategy. Moreover, we find that the very business processes that enable unparalleled corporate control bring with them new problems that Apple has thus far been unable, or unwilling, to adequately address.
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1. Introduction

The Apple business model affects not only its direct shareholders but also moves markets, which impacts overall macro-economic performance. In April 2012, Apple's shares reached a high of $636.00 and market capitalization surged to $570 billion, more than the value of Google, Microsoft, Hewlett-Packard, Dell and Yahoo combined (Russolillo, 2012). At the time, Apple Inc. comprised four percent of the Standard and Poor's 500 stock index and almost 18 percent of the Nasdaq 100 (Levisohn, 2012), making it able to singlehandedly sway market indices, affecting index-linked mutual or pension funds and all those people dependent on them. Current explanations of Apple's stunning performance and success tend to focus on innovation in product design or marketing strategy. An emphasis on innovation does not devote adequate attention to the tangible limits to growth of this particular business model. One example is the imperative to continually create new and revolutionary products to sustain its current profitability and expand at an above average market rate.

The objective of this paper is to analyze the post-2003 Apple business model to highlight the weaknesses created by its perceived strengths. This requires us to move beyond an exclusive focus on what makes Apple unique or different when evaluating their business model and include the mundane and out-dated elements of its processes that may be undermining its ability to compete and grow in a changing market. To do so, we examine the end-to-end supply chain, from source to store, to present a more holistic evaluation of the Apple business model. First, we begin by isolating the post-2003 business

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model from the many iterations of Apple Inc. since its creation in 1978, which links directly to key conceptualizations of Apple within the business model literature. From here, we explore the space created to more closely consider the limits to growth engendered by this particular business model.

Second, we argue that the quintessential 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, which has been hugely successful to date and allowed Apple to wield enormous power in the end-to-end supply chain. This business model gives Apple the unique ability to maintain a low cost sourcing strategy while maintaining high price points and subsequently locking the consumer in through high switching penalties. We argue that a key facet of the Apple business model is ensuring that Apple content can only be played on Apple devices, as this helps maintain digital download market share and in turn drives sales volume for profitable hardware devices. Apple maintains this multi-channel platform integration through legal and technological means and extends its mantra of control past the multi-platform to all partners in the supply chain, including suppliers and manufacturers.

Third, we show that the power Apple derives from owning the consumer is evident downstream in the supply chain, e.g., with retailers, as Apple designs its own in-store displays and places their own sales staff in big box retail stores to promote Apple products. Access to the lucrative Apple consumer is a prize big box retailers cannot resist, even though it places them at a disadvantage because of direct competition from Apple stores and a consistent loss of content to Apple's online store.

Finally, we consider how the very business processes that enable unparalleled corporate control over its end-to-end supply chain bring with them new problems that Apple has thus far been unable, or unwilling, to address. For instance, Apple clings to an outdated efficiency-based supply chain design, putting it in the firing line of human rights groups, which will only serve to undermine its brand image in the long term. Moreover, Apple has yet to adopt a sophisticated category management scheme that would allow for a more strategic use of the retail landscape. These limitations are made clear by Apple's on-going difficulties competing with emerging rival ecosystems (Android, Symbian) and devices (smartphones and tablets). We conclude by considering how the study of business models allows for a richer evaluation of the strengths and weaknesses of corporate strategic management practices. Moreover, we consider how more detailed research into Apple can help us understand how market leaders are created and, inevitably, decline.

2. When the 'novelty' wears off

There are many different explanations for Apple's recent success. Some regale the 'return' of Steve Jobs as the decisive factor leading Apple out of the technology wilderness (Harvey & Novicevic, 2006; Strategic Direction, 2008; Swallow, 2011). Others focus on innovation, be it marketing and product design, software and content delivery, or good timing and a hint of serendipity (Dedrick, Kraemer, & Linden, 2009; Reder, 2009; Zott & Amit, 2010). Finally, there are those that point to Apple's ability to extract extraordinary margins due to a low cost manufacturing strategy and an ability to maintain high price points by providing a 'unique' retail experience (Duhigg & Bradsher, 2012; Froud et al., 2012; Sorescu, Frambach, Singh, Rangaswamyd, & Bridges, 2011; Useem, 2012). While each observation has merit, they tend to highlight only one element of Apple's business to explain the entirety of its current success. Here, we use a business model framework to analyze how these different practices combine to create a recognizable Apple business model. The strength of the business model approach is that it frames a system of interdependent activities that transcends the focal firm and spans its boundaries, breaking down the 'inside-outside' distinction when evaluating what constitutes firm activities (Amit & Zott, 2001; Zott & Amit, 2010). The boundary-spanning nature of business models emphasizes activities performed for the focal firm but outside its boundaries by partners, suppliers or customers; for instance, even when key activities, such as product development or manufacturing, are shifted outside the firm, they remain a central part of the business model (Chesbrough, 2006).

Specifically, we analyze the post-2003 Apple business model. Apple has undergone several corporate iterations since its founding in 1978: at the outset, Apple's business model allowed outside companies, such as software and component providers, to use and enhance the base model. In 1978, the Apple II personal computer had an open architecture platform, allowing several new companies to produce specialized hardware and software components to rival the vertically integrated giants IBM, Burroughs and Digital Equipment (Hagel & Singer, 2000). In 1997, Apple devised a more collaborative approach to PC making by fitting Macs with Intel processors and allowing users to run both Mac and Windows operating systems (Strategic Direction, 2008). However, we argue that 2003 marks a decisive turning point in the business model through the integration of two new technological platforms, the iPod and the iTunes Music store (iTMS). By controlling the interface between its hardware and content, Apple was able to gain complete control of the multi-channel platform and realize the first opportunity to truly 'own the consumer'.

Fig. 1 illustrates the significance of 2003 as a turning point: by the end of 1997, Apple's stock price was $3.23. Apple's shares did make some significant gains over the next two years due to the dot-com boom and market excitement over Jobs' return, rising to $29.00 by the end of 1999. However, contrary to enthusiasts who herald the return of Steve Jobs as the firm's turning point, Fig. 1 shows how shares actually plummeted to $7.00 by the end of 2000 as the dot-com bubble burst, a full three years after Mr. Jobs' return. Others see the 2001 launch of the iPod music player as the catalyst for Apple's current success, but a year after its launch, just 125,000 devices had been sold and Apples share price stagnated between $7.00 and $11.00 until 2003 (Lloyd, 2012). It was not until 2003, when Apple launched its third-generation iPod in conjunction with the iTunes Music Store (iTMS), that Apple's share price began its dramatic ascent.

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