



Two-sided Internet platforms: A business model lifecycle perspective



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ABSTRACT

Multi-sided platforms bring together two or more distinct but interdependent groups of customers, normally described as B2B and B2C. Two-sided platforms have proliferated rapidly with the Internet and this has led to the development of new business models to monetize innovative value propositions in online markets. This paper puts forward a model of the evolution of the marketing strategies and business models of two-sided Internet businesses. In this model, Internet intermediaries are visualized as resource integrators, involving consumers and business partners in a process of co-creation of value—an integrated, two-sided business model. An analysis of five early stage Internet ventures reveals that the business models of these Internet ventures show a clear pattern of evolution from inception to maturity, from B2C towards B2B, and ultimately to an integrated combination (B2B&C and B2C&B). This is primarily due to a shift in the relative influence of different business stakeholders, identified as change agents in the context of the business modeling of two-sided Internet platforms.

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1. Introduction

Multi-sided platforms, known also as multi-sided markets, are an important business phenomenon that has proliferated with the rise of information technology and the Internet. Two-sided platforms are specific multi-sided platforms that bring together two distinct but interdependent groups of customers. They create value as intermediaries by connecting these groups (Eisenmann, Parker, & Van Alstyne, 2006; Osterwalder, Pigneur, & Smith, 2010). Despite a better understanding of two-sided Internet markets, where a single online platform enables interactions between consumers (the primary audience of the site), and business customers (e.g. the advertisers) (Rochet & Tirole, 2003), the respective importance given to the business audience (B2B) and the consumer audience (B2C) in the business model of Internet ventures has not been clearly identified. Furthermore, the notion that the marketing strategy orientation towards the B2B and/or the B2C side may change over time as a business develops has not been considered. This is a gap in the literature, which this article attempts to address through a study of the interaction between the B2B and B2C sides of online business ventures and their relative influence over time on the business models.

Accordingly, the purpose of this paper is to better understand the evolution of the marketing strategies of Internet startup companies towards businesses and/or end-consumers, as well as the nature and

relative contributions of the two sides of the market (B2B and B2C) in the creation of value.

The article proceeds as follows. Section 2 provides a review of relevant literature on the dynamics of two-sided networks, focusing particularly on value propositions of the firm, as well as business ecosystems. This conceptual review yields several research propositions that we will investigate through an exploratory analysis of five case studies of newly established Internet business ventures. In Section 3, we describe our research design which relies on an extended case methodology. Sections 4 and 5 describe the case studies and present detailed analyses of the pattern of evolution, with particular emphasis on the relative influence of different stakeholders over time. Finally, in Section 6 our conclusions are discussed, along with the limitations of the study, and implications for future research.

2. Conceptual background

Before presenting the conceptual framework, it may be useful to define the key terms specific to this study and the Internet domain.

2.1. Definitional issues

This study focuses on Internet businesses and, more specifically, pure-players. A pure player is an organization that does business purely through the Internet; it has no physical store (bricks and mortar). The Internet is a ubiquitous information platform (Sharma & Sheth, 2004). Firms use the Internet to provide information, to provide connectivity and community, to allow transactions, and to share cost reductions (Sharma & Sheth, 2004).

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This definition of the Internet is important because it implies that most Internet businesses are in fact intermediary platforms,¹ in other words, two-sided or multi-sided platforms. This includes social networking platforms such as Facebook which link networks of users with the providers of various services and applications, e-commerce websites such as Amazon or eBay, which bring together buyers and sellers; and search engine platforms such as Google, which connect advertisers and Web users (Bakos & Katsamakas, 2008).

These Internet platforms typically have two types of participants (“sides”): a business side (B2B), which very often is the business customer (they pay for a service) and an end-user side (B2C) who is the consumer of the service, and who may or may not pay for the service. In any case, each side generally derives positive externalities from the participation of members on the other side.

The term business model came to prominence in the 1990s, largely as a result of the emergence of the Internet economy. As J. Magretta (2002) explained it: the “Business Model was one of the greatest buzzwords of the Internet boom, routinely invoked, as the writer Michael Lewis put it, ‘to glorify all manner of half-baked plans’”.

The bursting of the dotcom bubble in 2001 showed the limitations of many of these business models. It is believed that the majority of Internet ventures failed in the first three years of their existence (Feinleib, 2012). These failures may have occurred for many reasons but one of the most commonly cited is the fact that many startups relied on a flawed revenue model (such as advertising) and a poor definition of the value proposition (Clemons, 2009). In such instances, the failure of a company could be attributed to an inability to generate sufficient revenue from third parties through sponsorship, advertising or affiliation (Chen, 2003).

Today, a systematic approach to business models is more widespread and the survival rate of new online businesses is correspondingly better. Well-constructed business models identify a target consumer audience and a clear value proposition, they also specify the structure of the value network, a revenue generating mechanism, and they estimate the cost structure and profit potential of their business (Chesbrough, 2010). The business model is therefore a structural template that describes the organization of a firm’s transactions with its external business partners in factor markets as well as with its consumer audience or product market (Zott & Amit, 2008). In other words, the business model is “the rationale of how an organization creates, delivers and captures value” (Osterwalder et al., 2010).

The value proposition is at the heart of business models (Lindgreen, Hingley, Grant, & Morgan, 2012; Osterwalder et al., 2010), as it is also at the heart of marketing strategies (Slater & Olson, 2001). Hence it is de facto the bridge between strategic management and marketing literatures. A value proposition can be defined as a set of commercialization practices employed to make suggestions about how the provider’s capabilities, expressed as solutions, enable customers to create value (Storbacka, 2011).

The fundamental basis of all Internet businesses is the value proposition offered to consumers, on the one hand, and to business buyers, on the other hand, and so our starting point must be with the literature concerning the management of value propositions.

2.2. Value propositions and two-sided market theory

The concept of two-sided markets, originally conceived in economics, was gradually adopted in management and marketing. Rooted in the network externalities literature (Katz & Shapiro, 1985), the theory of two-sided markets states that Internet platforms must “get both sides of the market on board” in order to be viable (Rochet & Tirole, 2003). Two-sided markets refer therefore to two distinct user groups that

provide each other with network benefits. For example, Internet portals and online newspapers are platforms that compete for advertisers as well as for consumer users.

In economics, the theory is used to consider the optimum level of price discrimination among the participants in the network (Rochet & Tirole, 2003). In management and marketing, the model helps to identify markets for content providers and end consumers, and to determine the optimum size of the two user networks (Le Nagard-Assayag & Manceau, 2001; Nair, Chintagunta, & Dubé, 2004). It also attempts to determine which markets to subsidize in order to avoid a “chicken and egg” situation (Parker & Van Alstyne, 2005). For example, Parker and Van Alstyne (2005) find that the decision as to which market to subsidize depends on the relative network externality benefits: At a high level of externality benefit (the advantage gained when the other side participates in the market), the market that contributes more to demand for its complement is the market to provide with a free good.

The problem on the Internet is the same, and therefore one needs to determine which side contributes most to the demand of its complement (on the other side). The key question is to determine why any party might join the Internet platform. On the consumer side, the motives can be as varied as the benefits offered by the Internet platform; on the business side, the motives are linked to the size of the audience, its particular characteristics and/or the usefulness of the data collected from this audience. For example, Fish (2009) states that B2B companies involved in two-sided markets will benefit from consumers’ private data (the “privacy capital”), i.e. businesses advertising on Facebook do so because they can micro-target their audience based on the personal information (age, gender, interest etc.) provided through this audience. In any case, it seems that the typical two-sided digital business model sees end-consumers as loss leaders (they get the service for free) and business participants as subsidizers (they pay to reach the audience of end-users).

Free value strategy is based on offering value to customers, for which they are not charged. Andersen proposes that “free” can be a viable Internet business model (Andersen, 2009) but it does mean that somebody else has to pay (e.g. the business side). This means that web entrepreneurs have to find a compelling reason for business partners to join their business network in order to be able to deliver their value proposition to a B2C side. To do so, entrepreneurs need to formulate a promised benefit for business customers. This implies that Internet business models have to consider the value proposition for business partners just as much as for the consumer audience (Mahadevan, 2000; Osterwalder et al., 2010). It thus follows that:

Proposition P1. *Two-sided Internet platforms need to formulate two different value propositions—one for the end-user side and one for the business side.*

The literature on two-sided markets provides little information about the role of each of those sides. The concept of reciprocal value propositions offers some further insights on this issue.

According to service-dominant logic, firms cannot deliver value; they can only offer value propositions, i.e. a potential value that is only realized through customer usage (Vargo & Lusch, 2004). S-D logic states that customers participate in the co-creation of value, which they access through the sharing and integrating of resources with suppliers, especially their skills and knowledge. Rather than firms marketing to customers (i.e. producers taking products to market), emphasis is placed on suppliers and other parties marketing with customers as part of an interactive, relational process (Vargo & Lusch, 2004, 2008a,b, 2011). In this paradigm, goods are essentially part of the distribution mechanism for service provision rather than being produced in the supplier’s value chain. Value is therefore co-created by both the supplier and customer.

The concept of reciprocal value propositions represents a more recent development. Glaser (2006, p. 446) claims that if participants

¹ These websites are sometimes referred to as infomediary platforms. They gather and organize large amounts of information and act as an intermediary between those who want the information and those who supply the information.

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