Surviving in an Increasingly Digital Ecosystem

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In summer 2015, *MIT Sloan Management Review* published our article “Thriving in an Increasingly Digital Ecosystem,” which introduced four business models for the digital era. We argued that given the amount of turmoil digital disruption is causing, it’s time for companies to evaluate these threats and opportunities and start creating new business options.

We identified four ways that companies can operate:

1. *Suppliers*, such as insurance agents, which are typically in the value chain of another powerful company;

2. *Omnichannel businesses*, such as large retailers and banks, which provide customers access to products across multiple channels, combining physical and digital;

3. *Ecosystem drivers*, such as Amazon.com Inc. and Tencent Holdings Ltd.’s WeChat, which become destinations for more and more of their customers’ needs by offering complementary or sometimes competing services; and

4. *Modular producers*, such as PayPal Holdings Inc., which provide plug-and-play products or services that can adapt to a variety of ecosystems.

Much has happened between since we began our research in 2012, and it’s time to update.

We have collected new data and completed new case studies that help us understand that it’s no longer about how companies can thrive, but rather how they must *reinvent to survive* — because that’s the key issue today.
How the Competitive Landscape Has Evolved

Three findings dominate our new research:

In the past five years, we have seen a consolidation — a Darwinian shaking out — of ecosystem drivers and modular producers. Back in 2013, over half of the ecosystem drivers we identified in our survey were small enterprises, often startups, trying to create a blockbuster business. The successful ones — which rely on having great platforms — have grown rapidly, while the others failed and often disappeared (or were acquired). As a result, the number of companies embracing these two business models has decreased markedly. From 2013 to 2017, companies that were predominantly ecosystem drivers fell from 20% to 9%, and modular producers fell from 18% to 8% (from 998 companies across two surveys).

More companies have embraced an omnichannel business strategy. Omnichannel businesses are more focused on meeting customers’ life event needs, but statistically we saw relatively few omnichannel businesses that were really great at customer engagement. It’s a big challenge to take a business designed for the physical world, add a digital channel, and make the new customer experience seamless. Most banks, energy companies, and formerly physical-only retailers are working hard on making the transition to an omnichannel model. The percentage of companies identifying as omnichannel businesses in our study rose from 21% to 37%. The fourth model, suppliers, was also up, slightly, from 42% to 46%.

Consumers are voting with their mobile devices and choosing from a handful of dominant ecosystem drivers for each domain in their lives. The consolidation of ecosystem drivers has limited the number of companies that customers think of first when they need to solve a problem and increased each of those dominant companies’ power in the marketplace. Think WeChat for daily life in China or Amazon for shopping in the United States.

For instance, Amazon accounted for 43% of all U.S. online retail revenue in 2016, and 20% of all U.S. consumers are Amazon Prime members. As significant, 55% of U.S. consumers begin their product searches at Amazon, dominating the search engines. Amazon has quickly become ubiquitous: The company supplies Dash Buttons for consumers to place anywhere in their homes to make one-click purchases of products they need without going online; Alexa, the Amazon voice-activated assistant, can take orders for products and is learning to do more every week; and Amazon is incorporating some physical stores, identifying what makes for a good physical store customer experience and perfecting the technology to support that experience. In its first major foray into the physical channel, Amazon acquired Whole Foods Market Inc., with lots of resulting speculation as to how Whole Foods Market stores will be incorporated into the Amazon experience.

How Will Your Business Compete?

We expect the consolidation trend to continue and affect every domain in both B2B and B2C businesses. We will see B2C customers identifying their go-to provider in each of their life domains (including health care, education, entertainment, financial services, travel, and social). We foresee a big battle for each domain, with
successful companies striving for broader domains than their initial target. For example, much like Amazon is doing in the United States, WeChat in China is combining many of its early domains (communication, purchasing, and banking) into meeting the needs of “everyday life.” B2B customers will also pick go-to destinations for their domains of need such as supply chain, consulting, business information, logistics, recruiting, industrial internet, and energy management.

How will you compete in this environment? How do you start building capabilities to add to your current business model or move to another one?

There is an emerging consensus among economists that competition has weakened significantly in two-thirds of industries, with two causes: mergers and technology. Enterprises that want to reinvent themselves in the digital era, perhaps pursuing different business models, need to make investments that quickly generate revenues — because it seems there’s a significant first mover advantage, often resulting in consolidation.

Given the consolidation trend, we believe that every large and ambitious company needs to buy options — that is, significant investments that create new business model prospects — for an ecosystem driver model. There are still markets open, and there’s still time to act. For example, there are opportunities to become ecosystem drivers in health care, energy management, B2B and B2C, continuing education, home ownership, transportation, small business management, consulting, legal services, and recruiting. What is the domain or market your company can define where you can be the go-to destination for your best customers?

Many companies will be able to thrive by operating several business models at the same time. If your operation decides to invest in options and to build ecosystem capabilities, you still have to optimize revenues and profits from your current omnichannel and supplier models. If you are only a modular producer, then you need to be the best — best products, best price, and best service. Only the top few modular producer companies are profitable in each market. Otherwise it’s a race to the bottom, and more and more modular producers will be chosen by a bot (for example, the choice of a mutual fund, spare parts, car insurance, or shipping container and business services).

One helpful tool for moving forward is to calculate the percentage of your revenues in each of the four models and their respective margins today. Then create a target for those numbers in five years. How will you get there? We see a combination of models and buying options for ecosystem driver business models (the most successful model in our research, with higher profit margins and growth rates) as the most promising strategy for larger companies surviving — and then thriving — in the era of digital ecosystems.
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