LUMOS BUSINESS

BMi RevLine

Lumos Business Solutions Inc.

The #NewEraBiz

Let's jump into BMi RevLine by starting with what this document is all about:

(BMi) *Business Model Innovation*

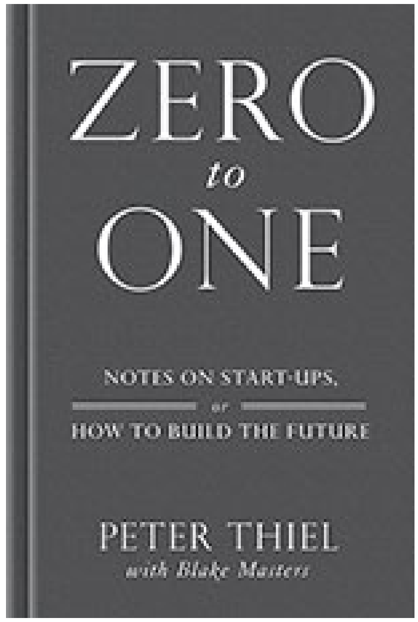
Business Model Innovation is not a science, it's a strategy. It's also not optional, it's necessary; the majority of companies in today's '*market economy*' will fail in the next decade if they don't innovate their business model.

> *Business model innovation* is the creation of a new or novel form of exchange at some point along a company's value chain.

It's about repurposing and repackaging the business model for today's increasingly connected world of conscious consumers. It's about shifting along the value curve in order to ensure that you can thrive in decades ahead and continue to create, capture and deliver value.

Within *BMi RevLine* we want to outline objectives, strategies and frameworks to begin achieving this and ultimately achieve new *SiteLines* to future *Revenue Streams*.

Using the sports car - the ultimate metaphor for agile performance in business - as a reference, we want to start the engines and begin shifting gears towards BMi.



The man of the moment when it comes to looking at BMi from a holistic perspective is Peter Thiel. The PayPal Founder, Facebook Investor and Rocketman backer (SpaceX) knows a thing or two about breaking open new industries via BMi and shared it in his recently published book Zero to One.

In his book, he states why we need to go from Zero to One to build *companies for the future*:

> *"What happens when we've gained everything to be had from fine-tuning old lines of business that we've inherited? ... the answer threatens to be far worse than 2008. Today's 'best practices' are dead ends; the best paths are new and untried."*

> *"Progress can take two forms. Horizontal or extensive progress means copying things that work - going fro 1 to n. Vertical or intensive progress means doing new things - going from 0 to 1."*

> *"From the Founding Father in politics to the Royal Society in Science to Fairchild's Semiconductor's 'traitorous eight' in business, small groups of people bound together by a sense of mission have changed the world for the better."*

According to Thiel, the most important question a business should ask is '*will this company be around a decade from now?*'

Concretely speaking, we need to be able to identify companies that have large *future cash flows*.

> *"Simply stated, the value of a business today is the sum of all the money it will make in the future."*

Low-growth businesses (ie. a local restaurant) typically have healthy cashflows today but will likely see those dwindle in the future. While most *high-growth businesses* (ie. new technology) are the opposite; they have negative cashflows for their first few years, but exponential upside in the future.

Assuming a company can execute on their strategy and achieve a '*monopoly*' in a huge untapped market, the bet is that those *future cashflows* will make investors a windfall and be worth the *up-front risk* that the venture entails.

> *"Creative monopoly means new products that benefit everybody and sustainable profits for the creator."*

Contrary to competition, which is an 'ideology' that according to Thiel:

> *"pervades our society and distorts our thinking. Competition means no profits for anybody, no meaningful differentiation, and a struggle for survival."*

We don't want to *compete* and build another razor or toothbrush, **we want to invent** and create a new technology or global energy solution:

> *"Rivalry causes us to overemphasize new opportunities and slavishly copy what has worked in the past"*

If we take a big problem, a long-term approach and bring together the right elements (people, capital, etc), then we invent *towards* a creative monopoly.

> *"Long-term planning is often undervalued by our infinite short-term world. A business with a good plan will always be underrated in a world where people see the future as random"*

According to Thiel, there are four general characteristics that define a monopoly in some combination:

Characteristic 1: Proprietary [Technology]

> *"Proprietary … is the most substantive advantage a company can have because it makes your product impossible or difficult to replicate."*

> *"As a rule of thumb, proprietary … must be at least 10X better than its closest substitute in some important dimension."*

Characteristic 2: Network Effects

> *"Network Effects make a product more useful as more people use it."*

> *"Paradoxically network effects businesses must start with especially small markets."*

Characteristic 3: Economies of Scale

> *"A monopoly business gets stronger as it gets bigger; the fixed costs of creating a product can be spread out over greater quantities of scale."*

> *"A good company should have the potential for scale built into its first design."*

Characteristic 4: Branding

> *"Creating a strong brand is a powerful way to claim a monopoly."*

> *"Beginning with brand rather than substance is dangerous."*

From there, you need to choose your market carefully and:

- start **small and monopolize** - focus on a very small market initially
- scale **up** - once you create and dominate a niche market, gradually expand
- don't **disrupt** - as you craft a plan to expand, don't disrupt - avoid competition.

Thiel's book, Zero to One, is chalk full of insights and definitely recommended reading for anyone interested in BMi; although there is a clear bias towards *Startup America*, as all the examples cited are related to his experience investing in US startups like *Facebook* and observing American tech giants like *Apple*.

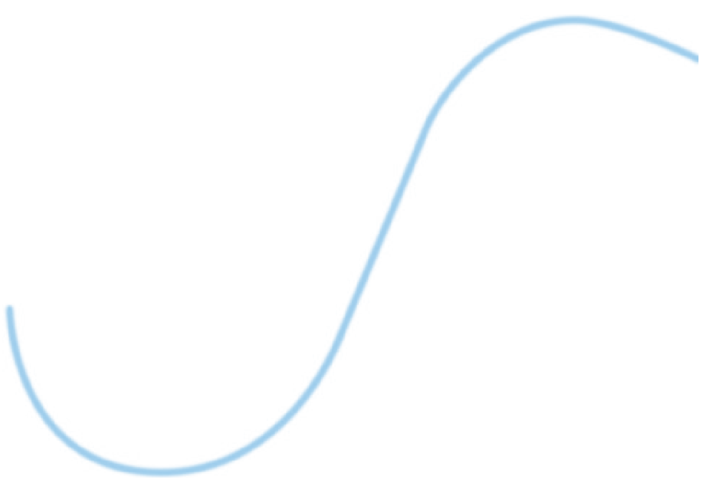
Consequently, he leans heavily towards technology as the great solution and doesn't add in any cultural context to explain big ideas that take root outside of the USA; however, he hits on several key points:

1. SHIFT your BUSINESS MODEL:

2. SOLVE a BIG PROBLEM:

3. SURROUND yourself with DEEP TALENT:

Before diving deeper into the *tactics* and the how of BMi, we need to shape our understanding around the J-Curve.

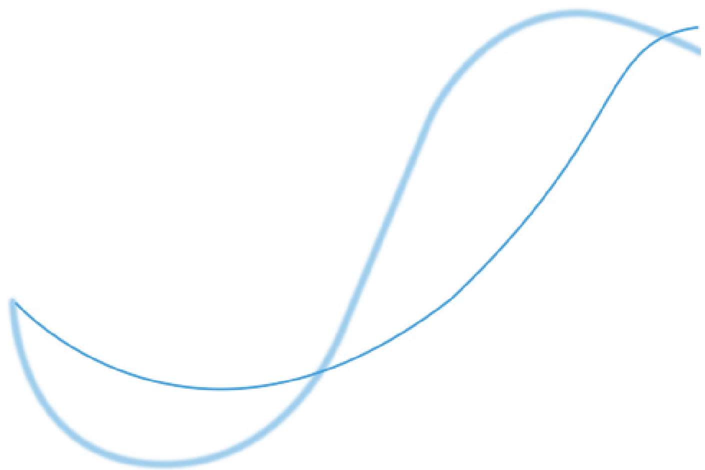


The J-Curve, in the field of Finance, illustrates a company's growth over time. Initially, we can expect to see negative returns followed by increasingly positive, and hopefully exponential, returns over time.

Traditionally, the *longest J-Curve* in any industry would be Pharmaceuticals. Heavy upfront investment in R&D is required with the idea that a drug that makes it to market will produce tremendous positive returns over the long-term.

The *shortest J-Curve* would be representative of any business that requires very little upfront investment, yet has very low potential for high positive returns.

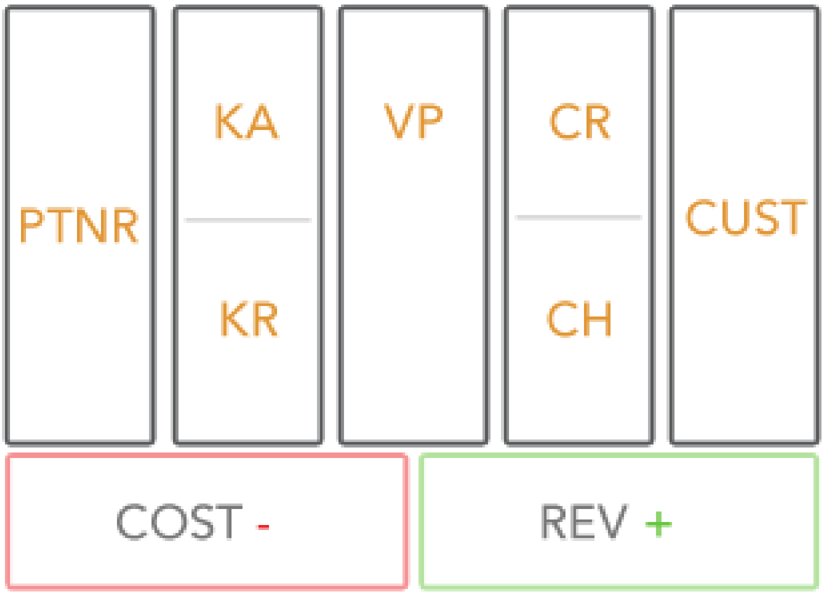
Therefore, the most innovative ideas tend to have long J-Curves, as they require significant upfront investment and take a long time to payoff for investors.



However, it does not mean that for a company to be innovative that they need to have a long J Curve. For the majority of people, access to the deep-pocketed investors with long-term outlooks is limited.

That's why we need to be creative and use the business model canvas, developed by Alex Osterwalder, to map out our proposed business model and identify opportunities available to shorten that J Curve.

Ideas include, partnering with firms who already hold expertise, finding new distribution channels to increase scale-up speed, or at a more basic level, using tools like crowdfunding to 'pre-sell' products and use that money to finance product Dev.



The business model canvas (BM Canvas) allows you to map out your business model on one page. There are 9 segments to the BM Canvas:

(VP) Value Proposition: What unique value does the company offer the market?
(CH) Channels: What channels do they use to acquire customers?
(CR) Customer Relationships: How do they build relationships with customers?
(CUST) Customer Segments: What group(s) of customers is a company targeting?

(REV+) **Revenue Streams:** How does a company pulling all of the above elements together to create multiple revenue streams and generate continuous cashflow?

(KA) Key Activities: What activities does a company engage in to execute strategies?
(KR) Key Resources: What proprietary assets and knowledge do they possess?
(PTNR) Partnerships: What strategic and cooperative partnerships do they form?

(COST-) **Cost Structure:** What are the costs associated with each of the above elements and which components can be leveraged to reduce costs?

[Download the BM Canvas (PDF)]

With a little Thiel to grease the gears and a BM Canvas in our hands to template the SHIFT, we can start working our way towards a concrete set of actions that can be carried out in order to *kickstart* the BMi process.

> "Your one big advantage is that your business model is not locked in."
>
> *Tim Kastelle writes on his blog about the Attacker's Advantage*

Two very prominent industries referenced by Mr Kastelle are:

- Newspapers

> *"When digital-only competitors like Huffington Post, Politico, and the myriad blogs and news sites that have arisen over the past few years started out, they didn't try to compete with the Times head-to-head. That is a losing proposition. Instead, they innovated the business model. "*

- Books

> *"In the 80s and 90s, B&N and Borders became enormously successful because they became enormous ... they created a competitive advantage by carrying 120,000 titles. When Amazon started to carry all the books, then 120K wasn't much of an advantage"*

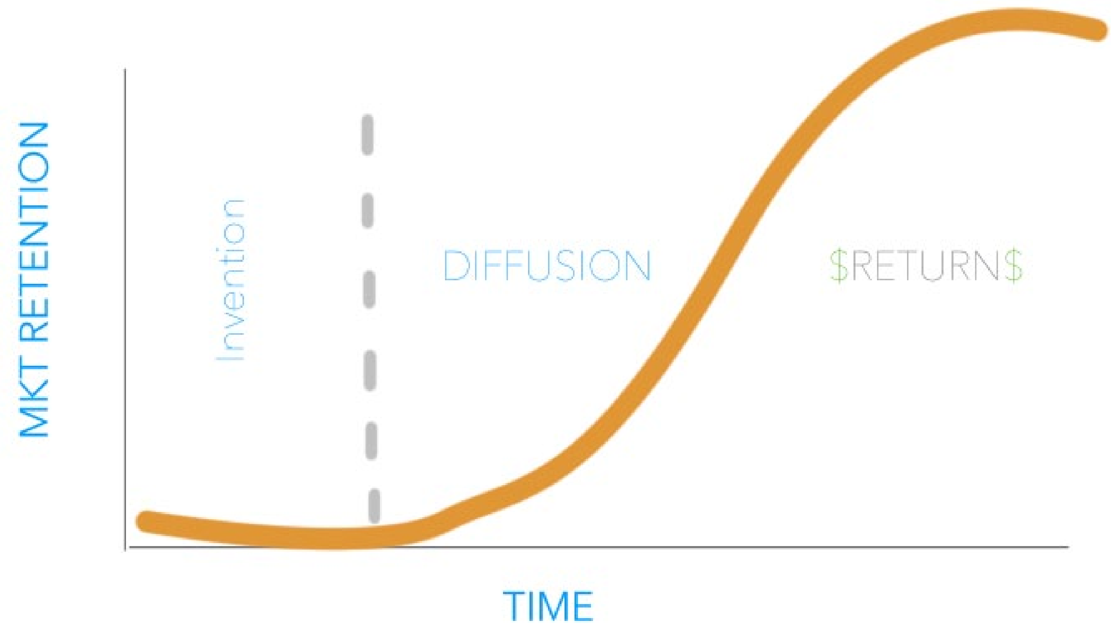
These are two industries whose downfall *everyone* can see around them in their everyday lives, and underscores Thiel's point about *the need* for BMi:

> *"What happens when we've gained everything to be had from fine-tuning old lines of business that we've inherited? ... the answer threatens to be far worse than 2008. Today's 'best practices' are dead ends; the best paths are new and untried."*

Ultimately, when we think about the concept of breaking open new markets, developing a new model and creating blockbuster returns for stakeholders and shareholders alike, we need a top-notch strategy.

> "All the innovation initiatives in the world won't matter if your strategy isn't right"

Timing the Market



In his blog post, On the '[Importance of Time in Innovation]' Mr Kastelle emphasizes the need to ensure that innovation - *defined as executing new ideas to create value* - is a fluid process of experimentation. We need to *contextualize failure* against the typical industry S-Curve that measures *time vs. performance*.

> *"30 years is a typical period of time between the first experiments with a new technology and mainstream commercial success"*

It is very common for experiments to fail in the flat part of the S-Curve, and yet we often expect our own '*innovative ideas*' to be adopted instantly. Especially engineers and computer scientists, who as Thiel describes:

> *"Engineers frequently … do not understand distribution. Since they don't know what works, and haven't thought about it, they try some sales, BD, advertising, and viral marketing—everything but the kitchen sink…"*

Therefore, we can use the S-Curve to manage our adoption expectations, the J-Curve to structure our *ROI timeline* and BMi to streamline the *innovation process*:

> *"This means that business model innovation needs to be part of our innovation management process. The right idea at the wrong time is still wrong. Business model innovation is one of the tools that can address this problem."*

BMi RevLine — From 1st to 2nd

Now that we have some backdrop for BMi, let's look at kickstarting the process. To SHIFT from 1st to 2nd gear requires a set of steps and a few sparks of inspiration.

Ultimately what we want is to explore the *new and untried paths* and identify a SiteLine to new Revenue Streams. We have three key elements to setting BMi RevLine into motion:

Bold Vision - what's about to happen in the next 5 - 10 years

Blue-Ocean Markets - what vast markets will this take place in

Big Bets - what major moves need to be made to make it stick

And to inspire us to go down this path with the right energy and attitude to see it through, we look at three examples, globally, who have achieved this in recent years.

M-Pesa • Pebble • Seedrs

BMi RevLine   Bold Vision

To reach the RevLine have a Bold Vision.

This has nothing to do with *market research* reports, *focus groups* or *big data*; this is about a core understanding of human behavior and an intuitive concept of what the future should and would look like at the exact point where your firms enters:

- On a scale of 5 - 10 years, where will the SHIFT occur?
- What are the mechanics of the market and the requisite behavioral changes needed to make this SHIFT a reality?
- Is the SHIFT dependent or independent of your company's entry?

You need to have a vision that is *big* enough for many people to participate in and *audacious* enough that those people will wake up everyday over that time period and be *inspired* and *fired up* to make it a reality.

If people are going to align themselves to the cause - *employees, first customers, investors* - then the vision has to be both conceivable and impossible at the same time; that way there is enough practicality to make it believable and enough fantasy to make it seem as though succeeding would be utopically optimistic.

#Imaginative + Intuition

"You must study the endgame before everything else"
Chessmaster José Raúl Capablance

To reach the RevLine find Blue Oceans.

The Blue Ocean market strategy was developed by two professors at INSEAD in 2005. The duo studied more than 150 strategic moves spanning more than 30 industries over 100 years and found that companies succeed more if they look for uncontested 'blue oceans' rather than highly competitive 'red oceans.' The strategy- '*Create Uncontested Market Space*' - is based on the premise that the best companies chart their own course and don't spend time 'worrying' about the competition:

- What are the dynamics of the market where the SHIFT will take place in?
- Are these markets where a SHIFT will require new channels, structures or distribution in order to capture the value?
- Is the market sufficiently big enough (*long-term*) to build strong cashflows and make the SHIFT strategy worthwhile if it pays off?

The markets need to be not only big enough, but have the right characteristics to make entry into them feasible and long-term profitable. The SiteLines towards Revenue Streams needs to happen in markets that are ripe, receptive and reachable.

#Strategic + Foresight

"Still round the corner there may wait, a new road or secret gate"
Author JRR Tolkien

To reach the RevLine make Big Bets.

Smart small, dominate a niche, scale up. This was the strategy that Thiel outlined for getting a startup from *Zero to One*.

First a company has to be in a space where nobody else is in order to plant the seeds for *long-term competitive advantage* and *big profits*. But there does reach a point where the niche has been developed and the Blue Oceans sit within view. At this point, where you have the market right in your wheelhouse, is where you need to make the Big Bets and invest maximum resources to make it happen.

- What SHIFT is happening in your niche that can be applied to bigger markets?
- What new infrastructure/resources do you need to put in place in order to SHIFT this innovation into Blue Oceans?
- What is the risk of not making the Big Bets now and losing the SHIFT momo?

Many companies nowadays are thinking about these decisions from a *Lean* perspective, with a *Minimum Viable Product* and continuous iteration based on *Customer Feedback*. This is all great up to a certain stage; but there does come a point, where if your vision is on track, and the Blue Oceans are staring at you in the face, that you need to go for it 100% and **build out your company as you envisioned**.

#Accurate + Timing

"There's no chance the iPhone is going to get any significant market share "
Former Microsoft CEO Steve Ballmer

Who: Launched by Vodafone UK in collaboration with Safaricom, Kenya's leading mobile service provider, Faulu, a local microfinance institution, and the Commercial Bank of Africa.

Where: M-Pesa was prototyped and launched in Kenya in 2007. The *mobile money transfer and payment platform* is now available across Africa, and in Afghanistan, India, and most recently Eastern Europe.

Investment: Vodafone secured £1Million in investment from the UK's Department for International Devlopment (DFID) Fund and matched the investment.

The story: In Swahili, the word *Pesa* stands for money. In 2003, a Vodafone executive identified a challenge Kenyans faced; *money was not mobile, it couldn't be transferred efficiently from one person to another*. Vodafone secured funding and launched a 6 month trial project in 2005 with its partners in Kenya. The pilot project on 450 customers was very successful, so they decided to launch at scale in 2007. Via a network of *M-Pesa agents,* the project was scaled out and enabled Kenyans to send money to one another via SMS. The company is profitable and growth is high.

The model: They charge commission on transaction - with fees ranging from 66% to 0.16% depending on whether users are registered or not.

The strategy: Start small, scale big; that was M-Pesa's strategy. Vodafone saw a big opportunity and put in the required resources to give it a shot, knowing that it was a long J-Curve. Then once it was tested, they moved to dominate the Kenyan market and scale into surrounding markets.

The Big Moves: Local Partners • Agent Network • Simple Technology

Who: Founded in 2012 by then 25 year-old Canadian entrepreneur Eric Migicovsky.

Where: Mr. Migicovsky began sketching designs for his '*connected watch*' concept in 2008 at the University of Waterloo. After designing a prototype, he went to Y Combinator (Y Com) in Silicon Valley in 2010. Although he failed to raise the required capital at Y Com, he ultimately founded the company in Mountain View.

Investment: The company raised more than $3 Million on the first day of its Kickstarter campaign; the campaign finished with more than $10 Million in crowdfunded capital by the time it was finished, a record at the time.

pebble

The story: Mr Migicovsky, a Vancouver native, began thinking while on exchange in the Netherlands "*Why can't you see who's calling on your wrist?*" He built his first prototype - InPulse - in the dorms at the University of Waterloo, and sold the 1,500 units of the beta version. Using Y Com funds, he did a production run but was only able to sell half the units. Back against a wall, he went on Kickstarter and raised the $10 Million and renamed the company Pebble. He has sold about 400,000 units to date and is the market leader in this rapidly-expanding market.

The model: The top Model - Steel - sells for **$199**, while the base model sells for **$99**. The company opened up it's Appstore earlier this year, billed as the '*first open platform for sharing apps optimized for wearables*.'

The strategy: '*I want an open platform that people can hack on top of - that's the future of computing.*' Pebble's advantage lies not only in the fact that it was first to market, but that is has an open ecosystem that will allow Developers to make apps for not just Pebble, but the whole Wearables category.

The Big Moves: Kickstarter crowdfunding • PR Push • Wearables App Ecosystem

Who: Co Founded by Jeff Lynn, a former American Securities lawyer, and Carlos Silva, a former IT Executive from Portugal

Where: Started in London, now legalized across Europe

Investment: Seedrs initially raised £1.3 Million in 2012, mainly from angel investors. The company raised an additional £2.58 Million through their own platform in 2013, setting a record for most money raised through equity crowdfunding.

The story: Seedrs started to jump on the equity crowdfunding bandwagon soon after Crowdcube launch in 2012. Seedrs was not the first equity crowdfunding platform on the market - Crowdcube was - but they were *the first regulator-approved* (FCA) platform, and have pioneered the '*nominee model*' whereby they represent 'crowds' of investors as the legal nominee, streamlining the whole model for companies to raise growth capital down the road. Initially, companies could raise up to £150,000 on the platform, and everyday UK investors could invest as little as £10. Now there are no maximums that startups can raise and investors across Europe can invest £10.

The model: Seedrs takes **7.5%** of capital raised and **7.5%** of the crowdinvestor's equity on all successfully funded campaigns. The company became profitable in July 2014 two years after launch.

The strategy: By creating a new nominee structure, and being approved by the FCA, Seedrs wanted to ensure that any company who raised money through their platform could smoothly transition into future financing rounds. This move opened the door to partnerships with funds, angels accelerators and a host of other capital sources.

The Big Moves: Nominee Model • Self-Funded Crowdraise • Euro Expansion