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Article

"Every company needs to have a strategy for the platform economy"

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Doing Business with Platforms





Sangeet Paul Choudary
Entrepreneur and expert in platform economy

“Every company needs to have a strategy for the platform economy”

Sangeet Paul Choudary is an Indian entrepreneur, advisor and business co-author of the best-selling book Platform Revolution. For his contribution to the field of platform economics Choudary was named Young Global Leader by the World Economic Forum and in 2016 nominated in the Thinkers50. At the INSEAD Business School he is an Entrepreneur in Residence.

**The interview is conducted by Martin Schumacher, M.Sc.,
Research Assistant at the Institute of Marketing, University of St. Gallen**

Everyone is talking about digital platforms and everyone seems to plan on building one. What is your definition of a digital platform?

A platform is an organising mechanism that organises a set or an ecosystem of participants to interact with each other. The participants of this ecosystem produce and consume value, exchange this value with each other, and the platform manages all of these activities. These interactions can be of a social or economic nature. You can think of Facebook as a platform organising social interactions and Amazon as a platform organising economic interactions. That’s primarily how I think of platforms.

And what are the key aspects of a digital platform?

The first key aspect of a digital platform is that it provides an open-end, connected infrastructure. By virtue of the fact that we are talking about digital platforms and not just platforms in general, this connected infrastructure is hosted on the Internet.

The second key aspect is that it provides the standard and the rules of governance that determine how the participants should perform their functions and how they should act on the platform. It is not restrictive, but it can provide standards by using a mechanism for curation or quality control – so that they are able to manage the activities on the platform. It is largely these two specific qualities.

The third quality that we often see in successful platforms is that they tend to be neutral players so that there is no conflict of interest with other parties in the ecosystem. But there are many exceptions to this rule. While the first two are necessary and sufficient conditions, the third is just something that we see in most platforms, because it makes sense to be neutral, rather than to compete with your own ecosystem.

Some people argue that a platform is nothing but a marketplace, just a digital one. When did this phenomenon of platforms first appear?

I think there are two things that are particularly unique about digital platforms that were not there in the traditional platforms or marketplaces in the traditional sense. One is that these platforms learn; they have learning effects. The more activities happen, the more they are able to learn. The traditional way of marketplaces is just a physical concentration of buyers and sellers. But players like UBER and Airbnb learn from the activities of the buyers and sellers. The learning effect is one thing that was not there before.

The second key aspect is that the digital platform has a persistent value. In a marketplace, you set up a stall and afterwards you remove your stock. But if you look at digital platforms, the Internet hosts content. Because of that, the more people come, the more content will stay on over time and offer more availability of transactions. Which means the value is not just the number of people on the platform, but the content that accumulates over time. Think of YouTube: it's not just about how many videos get posted, but the fact that they stay there is creating interactions in perpetuity.

The third important distinction between digital and traditional platforms is that the non-digital/traditional platforms had a barrier to scale because at a certain point they would become congested. If you think about the medieval market square in European cities – that market square is a platform that brought buyers and sellers together. But beyond a certain number of buyers and sellers it would get congested. As for digital platforms, because they are able to learn from the needs of users, they are able to filter and serve specific contents based on what the users need, hence the congestion never happens.

Talking about distinctions, how do digital ecosystems relate to platform business and which roles do platforms play here?

An ecosystem is a set of interacting parties that perform value-exchanging interactions with each other. Now, you



„This is the fundamental shift in management, which the people running these platforms have to think about: how they attract, leverage and utilise external resources rather than internal ones.“

may organise an ecosystem using a platform, or you may organise an ecosystem using other mechanisms like contracts or standards. For example, with the CD standard every player (e.g. CD manufacturer, CD player manufacturer or record company) was using the same standard to coordinate their activities.

Where the platform is different is that unlike contracts or standards which only provide the information that determines how each player should coordinate with each other, a platform provides not only just the information, but also the tools and has a feedback tool that communicates back to the ecosystem how they should change their behaviour based on the data it's capturing. Because of these aspects, the fact that it provides the tools for the ecosystem to come on board and the fact that it is intelligent enough to understand what they are doing, it is a much more compelling way to organise the ecosystem.

The test of a true platform is not to just match different parties together and help them discover each other, but it helps the parties scale their activities over time. If I have a business and I move it to a platform, I should be able to create more revenue for myself over time. That is a test of a true platform.

Thinking about management, you mentioned in your book Platform Revolution a shift from resource control to resource orchestration. Is there a paradigm shift taking place in management?

There is definitely a paradigm shift that's taking place right now. I think the fundamental shift that's taking place is the idea of resources and the source of resources. Traditional resources involved capturing resources internally. For instance, if you're an oil company, you'd capture the oil field and drill out the oil. But if you are a data company, if data is the resource in today's world, you need to get that data from the ecosystem. If you're Airbnb, and you're in the accommodation industry, you need to get that accommodation from the ecosystem.

There are two changes here that we are talking about. First, the definition of resource itself is no longer just physical resources and services, but also data. Secondly, the source of the resources is not what you control internally, but what you are able to attract externally. You are able to attract them because you are able to orchestrate interactions around that resource. As Airbnb, I can attract a room onto my platform because I can then match it to the right consumers and hence create value for the room owner. This is the fundamental shift in management, which the people running these platforms have to think about: how they attract, leverage and utilise external resources rather than internal ones.

Should every company become a platform?

That's a great question. Not every company should become a platform, but every company needs to have a strategy for the platform economy. Because what is emerging very rapidly and very clearly is that every industry ecosystem will end up moving in the direction of platform economy. It's a question of when rather than if.

But not every player will have to be a platform; some players will have to partner with platforms, some will have to work and create value on platforms; some will potentially find a niche specialisation because of which they will be able to succeed even if they're not a platform. Some players

will succeed by providing important back-end capabilities to platforms, which means the platform becomes somewhat dependent on players with these important capabilities.

So, basically it is important in the platform economy to pick your place. Be either an orchestrator or a service in this ecosystem?

That's right. The strongest position is obviously that of the platform itself, but it is also important to know that playing the role of a platform is a game. If you don't end up winning, you might end up losing everything.

Many of the successful platforms were not launched by incumbents but by new challengers. Will this stay the same or will this change? What is your prediction?

I think there are two ways of thinking about the ecosystem around platforms: complementary ecosystem and competing ecosystem. You need to build a complementary ecosystem, that's one of the key aspects. So even if you're an incumbent, you can build a platform for complementary partners who do not compete with you directly. So, incumbents can also build platforms. They might have a business in one area, but they can create a platform in another area. Think of Walgreens, the pharmacy; its platform is not bringing other pharmacies on board, but it's providing health services from different parties. That kind of platform strategy will work for incumbents.

„If you don't end up winning, you might end up losing everything.“

There are extremely few cases where a competing platform strategy actually works. One such example is Amazon. It works because the players which are on Amazon are much smaller than Amazon itself. Therefore, the platform's negotiating power is virtually insurmountable, giving Amazon a significant advantage. Otherwise, in general, a competing platform strategy doesn't work. A very good example is Symbian; Nokia had a majority share in Symbian, therefore none of the other device manufacturers wanted to participate in Symbian. On the other hand, if you look at Android: Google never created a phone, so the other manufacturers were comfortable working with Google.

Nike announced that they will collaborate with Amazon. Is it a deal with the devil or is it more of a win-win situation?

You have to evaluate relationships with platforms very closely. It is going to be a frenemy relationship; it is neither positive nor a deal with the devil per se. However, you have to be very careful about the exact terms and conditions. You have to ensure that the platform does not capture so much data about you that you become a commodity, making it able to compete with you. Therefore, I believe that brands, like Nike, will have to collaborate more frequently with Amazon in going forward, because of the access and the capability that

„Europe is now planning several measures to create a single digital market, which is a step in the right direction.“

Amazon offers. At the same time, Nike has to ensure that the data sharing agreement leaves them with as much power as possible over customer relationships, which will be exceedingly difficult.

One question regarding the management implications: Many B-to-B companies claim that it's all about personal relations and that they don't need platforms. They have their clients on their speed-dial list and the platform revolution started predominantly in the B-to-C sectors. Will the same happen to B-to-B companies as well?

It is already happening in the B-to-B space, but the way it happens in B-to-B is different, because what these B-to-B companies are saying is actually correct. In B-to-C, you value choice and variety over reliability. However, in B-to-B you value reliability and trust over choice and variety. Therefore, in B-to-B, platforms are not going to look like marketplaces or mass marketing engines. Platforms will first be used to digitise and manage the existing activities between the various parties. Once that is done, the data that comes out of these activities will help to inform which parties should interact with which party. That's where marketplace elements will come in.

B-to-B platforms are like the flip version of B-to-C platforms. I'll give you a few examples that illustrate this.

Think of Maersk, the shipping company from Denmark that has partnered with IBM to create a blockchain initiative, which is essentially a shipping platform. Instead of creating a marketplace for shipping companies, what they do is to digitise their shipping lifecycle. Specifically, they digitise various events in the shipping lifecycle and the various contracts that will get executed across that lifecycle. The entire shipping lifecycle is managed on a single platform. It's a place to manage the activities of multiple parties rather than help them find each other. As you manage those activities you gather data, which informs you about how good these parties are at what they do and what is their reputation. That data helps you create new recommendations for the using parties in the future, so that they can improve their relationships. That's the way B-to-B platforms will work compared to B-to-C models.

Coming to the final part – platforms from the macroeconomic and social perspectives. You recently took part in the platform summit in Berlin. Especially in Europe, the dominance of American and Chinese platforms measured by market capitalisation is critical. Why are the Americans and Chinese very good at creating digital platforms, while the Europeans are so slow?

I think if I had to choose just one reason for that, it is the size of the market. The size of the market is one big reason, and the fact that the market is homogeneous. Therefore, you are able to cater to a wider user base with only one solution. Europe, by being fragmented into many different countries, has for a long time struggled to do that. Even if you think beyond the American and Chinese platforms, some of the biggest platforms are coming out of India and Indonesia, because of their big markets. So, the size of the market becomes quite important. Europe is now planning several measures to create a single digital market, which is a step in the right direction. Unfortunately, right now it is still fragmented even with the single market. What we need is a greater regulatory agreement across different countries, so that there is a single market that can be created even for regulated industries.

Some people see platforms quite critically. On the one hand, research shows that platforms can empower individuals, for example to close the tax on poverty, but on the other hand, powerful monopolies can form. What is your opinion from the social perspective?

Are platforms good or should they be broken up at some point?

First, I don't think those are the only two choices. But to answer your question, from the social perspective it is important to realise the dynamics of where we are right now. Because if you look at the industrial economy, they had a very specific economic model that, as a company became large, benefited from economies of scale and economies of scope. Therefore, it was able to achieve an even stronger market leadership. That was the self-reinforcing cycle of industrial companies. But there was a balancing force, which was innovation. If you look at the whole theory of innovation, the smaller firms who started at the lower end of the market are able to innovate faster than larger firms with economies of scale and scope – that is why, eventually, the larger firms will be replaced.

However, that is no longer the case now. Because the larger firms do not only have economies of scale and scope, they also have the most data, which helps them to be even more innovative. Therefore, a company like Google is absolutely able to make AI-backed tools. The fact that innovation and scale now belong to the same company creates a kind of barrier to the balancing force that used to exist.

„Even if the platform company has the best intentions, because it has become the one social centre for all activities, it becomes a single point of failure.“

The reason I am saying this from a societal perspective is because this shows that there is no longer a balancing force. These companies are increasingly mediating more and more social interactions. Because they are mediating social interactions, there are two kinds of things that can happen, both of which are not very positive. First, as the company gains so much power, it starts manipulating the ecosystem and starts making decisions that are unfavourable for the ecosystem. Since it is mediating social interactions, it starts making decisions that disrupt good social behaviour. This is something that we've seen with Facebook and its impact on democracy, for example.

The other aspect is equally important. Even if the platform company has the best intentions, because it has become

the one social centre for all activities, it becomes a single point of failure. There is absolutely no resilience in that system. Any party can weaponize the platform and harm the ecosystem participants. An example would be the election meddling in the US by Russian hackers. My main concern is that it is bad for society, simply because a balancing force is lacking.

At the same time, I don't think breaking them up is a solution. Breaking up a monopoly in general is only a short-term solution. AT&T was broken up, but they are still one of the most powerful companies in that space. At the same time, breaking up a digital business is even more complex, because the boundaries of how you make up a digital business are much more complex. For example, if you are to break up Amazon by verticals, how would you break up the user data, how would you break up the deep-learning models that have been created based on the multiple verticals? Those are the challenges of breaking up a company today.

M: If you would like to take a deeper look at the different governance structures and platforms from the branding perspective – what are future developments?

One key aspect is to think about inter-operability vs. building a closed platform – in a lot of B-to-B industries right now there are efforts to create inter-operability, like the blockchain initiatives in container shipping or healthcare. But at the same time, after inter-operability, somebody will create a close cut. That's one big question of how you invest in inter-operability, while realising that your partner might end up creating a wall cut. How to protect your interests while co-investing in inter-operability is one question.

A second question is this whole idea of distributed trust. Everybody is claiming that with blockchains there will be distributed trust, therefore you won't be the central trust-making authority, but we haven't seen that work out yet. What are the conditions under which this distributed trust model would work and what are the conditions where it wouldn't work? I haven't seen any rigorous research laying out when a distributed trust model is better than a centralised trust model and hence whether or not platforms should be investing in blockchain technologies. 🚩