

## What managers should know about value creation – and appropriation

**To grow, does your firm innovate, replicate or both? And how are economic gains distributed to stakeholders? IESE's Roberto Garcia-Castro and co-authors discuss their dynamic way to measure value creation over time and its implications for firm strategy.**



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Everybody loves a circus. The big-top tent, the agile acrobats, the juggling clowns... Even when it's a bit formulaic, new potential audience members are born each year and the show goes on.

But think about what happened once Cirque du Soleil appeared on the scene. With its culture of innovation, sky-high production values and higher ticket prices, Cirque du Soleil transformed the traditional circus model. Also, doing away with individual stars and with performing animals, it was able to create a new kind of show and capture greater value. A novel business model was born.

So, what kind of circus are you running? Or, put another way: How does your business model create value? Is it via innovation à la Cirque du Soleil? Or is it via replication, moving to new markets or over time like the more traditional circuses? Or is it somewhere in between — i.e., when your innovative company gains ground by taking business away from less productive competitors?

The answer to the above questions is key because it conditions the types of strategies pursued — as well as the type of managerial talent needed to implement those strategies. Clarifying the link between business strategy and a firm's productivity, co-authors Marvin B. Lieberman, Natarajan Balasubramanian and IESE's [Roberto Garcia-Castro](#) put forth a dynamic way to measure economic gain over set periods of time.

This work is based on their dynamic VCA model — which stands for Value Creation and Appropriation (as previously explained in "[A New, Dynamic Way to Measure Value](#)"). In academia, their relatively new VCA model is being rapidly diffused, entering tomorrow's textbooks on strategy and productivity. What is most novel here is the broader conception of value creation as it applies not only to shareholders, but also to other stakeholders — namely, suppliers, employees and customers.

In sum, the co-authors have created a new tool to better understand where value is going. It helps answer the question: To what degree is productivity benefitting shareholders, suppliers, employees and customers? The answer can help managers understand how much these stakeholders are then committed to the business going forward. Note that another defining feature of the VCA model is its dynamism, with value creation and appropriation intertwined.

## **The Low Cost Airlines Over Time**

The co-authors demonstrate their dynamic formula for measuring stakeholders' economic gain using public data from Southwest Airlines and competitor American Airlines over three decades.

Like Cirque du Soleil in its industry, Southwest is particularly notable for an innovative

business model that brought down costs, benefitting cost-sensitive customers and, notably, employees, too. Working for Southwest during its innovative period, employees were particularly committed and productive. The formula for economic gain helps show how these stakeholders' benefits shifted as Southwest's business model shifted, moving into replication mode as the low-cost model matured.

Knowing how value is distributed over time is very relevant to firms and managers, Garcia-Castro explains. It can help signal when strategies need to shift. "For example, employees may rapidly lose their motivation to work in the firm if they know their efforts today will not be rewarded," he notes.

At its core, value distribution is about fairness, about efforts being rewarded "fairly." From innovative to replicative business models, understanding who benefits when can lead to better management decisions.

See also, "[Where Is Your Firm's Value Going?](#)" for a look at the concept of VCA elasticity.

## **Methodology, Very Briefly**

The co-authors provide a firm-level measurement framework to quantify economic gain and its distribution among stakeholders. As an empirical illustration, they compare the creation and distribution of economic gain by Southwest Airlines and American Airlines between 1980 and 2010 using company data.

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