CEO advisory

Leadership and strategy in the news

Craig Henry

Of strategies and strategists

Strategy in an era of ecosystems

A cherished idea in traditional strategy is that a company that has found a repeatable, reliable business model then needs to erect barriers to entry – some kind of obstacle that prevents others from simply copying or matching their offerings . . . . What we are witnessing today is a weakening of many traditional barriers and simultaneously the emergence of very powerful new barriers that institutions are struggling to figure out.

Consider the barrier represented by high costs of entry . . . . Today, in the access-to-assets rather than ownership-of-assets that is part of the transient advantage economy, none of that is necessary . . . .

A second twist on the conventional wisdom is that today, strategic advantage is often determined by complementary relationships rather than by product or service benefits . . . . Moreover, establishing an ecosystem of complementary relationships means that today, ecosystems compete with ecosystems rather than firms competing with one another independently.

Relatedly, today's most effective competitors are leveraging network effects to their advantage. Network effects refer to the increased value a firm captures when it has more users or customers than other firms. This is typically the strategy pursued by platform companies, which make their profits by combining different sides of a two-sided market . . .

All of this leads to an urgent need to rethink what "monopoly" really means. Traditionally, the presence of entry barriers would raise regulatory eyebrows as firms able to prevent competitive entry could raise prices since other competitors couldn't enter the market and challenge them. Today, market domination is gained by firms such as Facebook, Alibaba, Google and Amazon because of their extensive networks, desirable platforms and ability to deliver enormous value to customers without traditional barriers to entry. Rather than monopoly, we have monopsony conditions, in which firms do not so much raise prices for consumers as use low prices as a barrier to entry . . . .

Rita Gunther McGrath, "The New Barriers to Entry: Why Strategy Assumptions Need to Change in an Era of Ecosystems," *Global Peter Drucker Forum*, 23 October 2019 www.druckerforum.org/blog/?p=2307

What makes Amazon different?

Silicon Valley is filled with product companies. Google invented two products – a spectacular search engine and a set of algorithms for matching people's online behavior to ads – that today deliver eighty-five percent of its revenue. Facebook invented (and acquired) addictive social-media products and then basically imitated Google's ad-matching algorithms, and gets

Craig Henry, *Strategy & Leadership's* intrepid media explorer, collected these examples of novel strategic management concepts and practices and impending environmental discontinuity from various news media. A marketing and strategy consultant based in Carlisle, Pennsylvania, he welcomes your contributions and suggestions (craig_henry@centurylink.net).

ninety-eight percent of its revenue from those products.

Amazon is a process company . . . . No other tech company does as many unrelated things, on such a scale, as Amazon.

Amazon is special not because of any asset or technology but because of its culture – its Leadership Principles and internal habits. Bezos refers to the company's management style as Day One Thinking: a willingness to treat every morning as if it were the first day of business, to constantly re-examine even the most closely held beliefs. "Day Two is stasis," Bezos wrote, in a 2017 letter to shareholders. "Followed by irrelevance. Followed by excruciating, painful decline. Followed by death. And that is why it is always Day One."

Charles Duhigg, "Is Amazon Unstoppable?" *New Yorker* 10 October 2019

When strategies fail: The rise and fall of Forever 21

From its reign as king of the mall just a few years ago to its tumble into bankruptcy court last month, Forever 21 is a spectacular success story that seems destined for an unhappy ending.

South Korean immigrants Jin Sook and Do Wan Chang started the chain in 1984 with $11,000 that they saved from working in low-paying service jobs. Their first store was a 900-square-foot space in Northeast Los Angeles that offered cheap and trendy clothing to a young, mostly Korean-American clientele.

But the couple had a plan. Their fast-fashion business model, which was based on quick-turnaround designs that could be inexpensively mass produced, proved wildly popular with young customers who didn't have much money to spend but wanted the latest looks. By 2015, global sales peaked at $4.4 billion, with 480 stores occupying enormous spaces in malls across America, according to Business Insider . . . .

However, the couple didn't anticipate the so-called retail apocalypse, which began in 2017 and continues to threaten virtually every retail chain . . . . The rapidly changing retail sector put too much pressure on Forever 21, and the privately held company filed for Chapter 11 bankruptcy in late September. It announced that it will cease operations in 40 countries, including Canada and Japan, and close 350 of its 800 stores, including 178 in the US . . . .

Forever 21 expanded rapidly in a short period of time, going from outlets in seven countries to 47 in just six years. Even as other chains were downsizing amid the retail apocalypse, Forever 21 was opening new stores as late as 2016 . . . . "They weren't seeing the trends, and instead of slowing down on physical space, they were building up physical space. That was a tactical mistake."

Another big failure for Forever 21 is particularly baffling to Cesareo. She said the company didn't bolster its e-commerce platform, even though its core customers are young people who prefer to shop online.

"Fashion Fail: Where Did Forever 21 Go Wrong?" *Knowledge@Wharton*, 10 October 2019 https://knowledge.wharton.upenn.edu/article/where-did-forever-21-go-wrong/

Finding strategic advantage in digital disruption

Brian Kenny: According to Edison Research, as of April 2019, there are over 700,000 podcasts and the number rises by about 2,000 every week. It's an ocean of content in a rising sea, leading some to wonder if we've reached a tipping point. Today we'll hear from Professors John Deighton and Jeffrey Rayport about the case entitled, Gimlet Media: A Podcasting Startup.

Jeffrey Rayport: It's clear that what burgeoning media companies like Gimlet, aiming to become major media companies as podcasters, are thinking that what Netflix has done to movies, what the web to did to print, what YouTube's done to video, what Spotify has done to music, surely somebody in the podcast world could have the same extraordinary effect. [But] audio is more complicated, and it starts with this idea that we all understand what appointment television is, but has anyone ever talked about appointment radio? This question of how you actually get people to focus on this particular stream has in some sense been a long standing challenge . . . .

Brian Kenny: I would love to know more about podcasts listeners . . . . Jeffrey, who is listening to podcasts, and what makes them an attractive audience for an advertiser?

Jeffrey Rayport: One thing that makes them very attractive is they are about 25 years 30 years younger than your median age of a television viewer for say ABC in primetime. So they tend to be affluent, well educated. They tend to be male. They tend to be in their 20's and 30's . . . . So these are very desirable consumers who are very hard for advertisers to reach, and the argument around podcasting is wow, if this is a medium that uniquely appeals to what Gimlet calls, "The Unreachables", then maybe there's a commercial opportunity to be built there.

"Can Gimlet Turn a Podcast Network into a Disruptive Platform?" *Cold Call* Podcast, 2 October 2019 https://hbswk.hbs.edu/item/can-gimlet-turn-a-podcast-network-into-a-disruptive-platform?

Technology and disruption

When disruption turns strength into weakness

The type of disruption most companies and government agencies are facing right now is a once-in-every-few-centuries event. Disruption today is more than just changes in technology, or channel, or competitors – it's all of them, all at once. And these forces are completely reshaping both commerce and defense.

Today, as large organizations are facing continuous disruption, they've recognized that their existing strategy and organizational structures aren't nimble enough to access and mobilize the innovative talent and technology they need to meet these challenges. These organizations know they need to change, but often the result has been a form of organizational whack-a-mole – a futile attempt at trying to swat at problems as they pop-up without understanding their root cause . . . . A competitive environment should drive a company/ government agency into new forms of organization that can rapidly respond to these new threats. Instead, most organizations look to create even more process. This typically plays out in three ways:

Often the first plan from leadership for innovation is hiring management consultants who bring out their twentieth-century playbook. The consultants reorganize the company (surprise!), often from a functional organization into a matrixed organization. The result is organizational theater. The reorg keeps everyone busy for a year, perhaps provides new focus on new regions or targets, but in the end is an inadequate response to the need for rapid innovation for product.

At the same time, companies and government agencies typically adopt innovation activities (hackathons, design thinking classes, innovation workshops) that result in innovation theater. These activities shape and build culture, but they don't win wars, and they rarely deliver shippable/ deployable product.

Finally, companies and government agencies have realized that the processes and metrics they put in place to optimize execution (Procurement, Personnel, Security, Legal, etc.) are obstacles for innovation. Efforts to reform and recast these are well meaning, but without an overall innovation strategy it's like building sandcastles on the beach. The result is process theater.

For most large organizations these reorgs, activities, and reforms don't increase revenue, profit or market share for companies, nor do they keep our government agencies ahead of our adversaries . . . . The very processes that made them successful impede them.

Steve Blank, "Why Companies Do 'Innovation Theater' Instead of Actual Innovation," *Harvard Business Review,* October 2019.

Silicon Valley's enduring advantage

According to assistant professor Jorge Guzman, "When it comes to startups, location matters." "It helps you connect with the ideas around you, find capital, hire employees and even impacts whether you become an acquisition target or not."

For many entrepreneurs and startups, that place is the United States, but more specifically Silicon Valley, which continues to be the hub for financing, patents and the promise of profit in the tech world. "The key question is what creates a good entrepreneurial ecosystem, and how should entrepreneurs take advantage of the ecosystem given their own personal situation and unique abilities and background," Guzman says.

Guzman begins to understand the US ecosystem in a recent working paper, "What is the US Comparative Advantage in Entrepreneurship? Evidence from Israeli Migration to the United States," co-authored with Annamaria Conti of the University of Lausanne. Guzman and Conti demonstrates that firms that move to the United States tend to fare better in fundraising, are more likely to be acquired, are worth more than companies that stay in Israel, and introduce more products.

Guzman says the internet-driven tech economy, instead of allowing ideas and innovation to flourish anywhere, has forced people to be in the same location. "It's paradoxical, but it turns out that goods travel more easily than ideas," Guzman says. "Big ideas travel only a 15-minute drive in Silicon Valley, so it requires almost a face-to-face level interaction for ideas to happen in the fastest way."

Stephen Chupaska "Location Matters for Entrepreneurship," *Ideas at Work*, 29 October 2019 www8.gsb.columbia.edu/articles/ideas-work/location-matters-entrepreneurship

Facebook brings cryptocurriencies out of the shadows

Lawmakers and Federal Reserve officials are so concerned about Facebook's plans to launch a new digital currency that they're contemplating a novel response – having the central bank create a competitor – a US government-run virtual currency that would replace physical cash, a dramatic move that could discourage major companies like Facebook from creating their own digital coins.

Facebook's proposed currency, Libra, has forced the Fed to consider the issue because of a fear that private companies could establish their own currencies and take control over the global payments system . . . .

The growing pressure on the Fed is evidence of how rapid developments in technology are beginning to shake the foundations of the financial system, raising questions about whether policymakers are prepared. Some lawmakers want the Fed to take a more active role in fintech developments.

"A consumer payments system is a natural monopoly, the same way Microsoft Word is a natural monopoly," said Rep. Bill Foster (D-Ill.), who joined with Hill to ask the Fed to outline its options for creating a digital currency. "No one wants to use some incompatible word processor. . . . The question arises – shouldn't it be the US taxpayer and the US government that does it rather than any private firm?". . .

Sheila Bair, who led the FDIC during the 2008 financial crisis, is among those urging the Fed to act. She argued that a new Fed-developed digital currency could be used by the public to transfer money without the need for banks and fees. If based on distributed technology – allowing for a decentralized database of transactions across a network – Bair said it could be more secure, efficient and less costly . . . .

Zachary Warmboot, "Fear of Facebook spurs momentum for Fed to build its own digital currency," *Politico* 15 October 2019 www.politico.com/news/2019/10/15/facebook-federal-reserve-digital-currency-047477

Culture and innovation

Transforming government services

Singapore's economic transformation from third world to first world since gaining its independence in 1965 is a well-known story of how stable governance and entrepreneurial thinking has fueled economic prosperity for this small nation. What is lesser-known is the extent to which the Singapore government has embraced design in its strategies to improve citizens' lives.

As Singapore's Prime Minister, Lee Hsien Loong, said in 2018: "At the national level, design is . . . a core element of our nation-building. Singapore is a nation by design. Nothing we have today is natural, or happened by itself. Somebody thought about it, made it happen. Not our economic growth, not our international standing, not our multiracial harmony, not even our nationhood. Nothing was by chance."

Singapore has historically designed policies and services around citizen behaviors to affect long-term desired outcomes, from pension fund contributions to racial integration in public housing to road pricing. . . .

In 2017, the product development team at Singapore's Government Technology Agency (GovTech) was tasked to develop a tool to consolidate citizen-facing services previously delivered by different government agencies onto a single platform . . . . Its first effort focused on the very beginning of a citizen's journey, taking the form of a smartphone app focused on making life easier for new parents. The app enabled users to register the births of their children, access their immunization records, navigate healthcare and childcare options eligible for benefits, and apply for the Baby Bonus Scheme (a government program aimed at alleviating the financial costs of parenthood).

Organizing the delivery of services around a citizen's journey, rather than fitting their delivery to existing processes, requires extensive interagency collaboration beyond functional silos. Singapore calls this a "whole of government" approach – one in which agencies collaborate on the basis of shared outcomes for cross-cutting problems.

Vidhya Ganesan, Yishan Lam, and Diaan-Yi Lin, "How Singapore is harnessing design to transform government services," *McKinsey Quarterly* October 2019.

A wider view

Separating winners and losers in the next recession

Southeast Asia will feel the effects of the next global downturn, albeit to a varying extent in each country . . . . Preparing now enables companies in the region to gain market share and accelerate: Winners pulled away from losers during the last downturn and widened the profit gap during the subsequent expansion.

The winners excelled in four areas: a focus on cost productivity, tight balance sheet management, selective reinvestment for commercial growth and proactive M&A. . . .

Taking advantage of a downturn starts with a realistic assessment of a company's strategic and financial starting positions. To raise the odds of success, management teams can map out a series of offensive moves that aim to create a stronger business throughout the downturn and beyond.

Start with the end in mind. What do you want the company to look like at the end of the downturn and three years after? A "future back" approach that defines the desired future state helps you know exactly where to invest – that is, the customer segments to target, the value proposition, and the technologies and assets supporting the business. A clear plan lays out specifically how the business will outperform competitors throughout and beyond the downturn.

Thomas Olsen, Sharad Apte, Nader Elkhweet and Francesco Cigala, "A Downturn Favors the Prepared, Even for Southeast Asian Companies", *Bain Insights* 20 September 2019 www.bain.com/insights/a-downturn-favors-the-prepared-even-for-southeast-asian-companies/

Politics, principles, and the future of the cloud

In 2013 AWS [Amazon Web Services] scored a surprise victory to become the CIA's cloud computing supplier.

The deal, worth $600 million, made Amazon a major national security contractor overnight.

Since then, things have accelerated. Amazon has been investing heavily in new data centers in Northern Virginia, and in February 2019, after a heavily publicized contest, the company announced it had selected Crystal City, Virginia – a suburb of Washington, DC, less than a mile from the Pentagon – as the site for its second headquarters. . . .

So why has Amazon moved into national security? Many think it comes down to cold hard cash. Stephen E. Arnold, a specialist in intelligence and law enforcement software, has used a series of online videos to trace the evolution of Amazon from 2007, when it had "effectively zero" presence in government IT, to today, when it appears set to dominate. "Amazon wants to neutralize and then displace the traditional Department of Defense vendors and become the 21st-century IBM for the U.S. government," he says.

Trey Hodgkins agrees. "The winner of [the JEDI] contract is going to control a substantial portion of the clouds across the federal government," says Hodgkins, until recently a senior vice president at the Information Technology Alliance for Public Sector, an association of IT contractors. The alliance disbanded in 2018 after it raised concerns about JEDI, after which Amazon, one of its members, left and formed its own association. Civilian agencies, he says, look to the Pentagon and say, "You know what? If it's good enough and substantial enough for them – scalable – then it's probably going to be okay for us."

Sharon Weinberger, "Meet America's newest military giant: Amazon," *MIT Technology Review* 8 October 2019 www.technologyreview.com/s/614487/meet-americas-newest-military-giant-amazon/

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