

Corporate Survival Tip: Ask Your Team This Question Once Every Year.

Thomas M. Siebel was the founder of Siebel Systems, a pioneer in the Customer Relationship Management (CRM) and is CEO of C3.ai, a provider of enterprise artificial intelligence software. He was named by BUSINESSWEEK as one of the top 25 managers in global business and is a three-time recipient of EY Entrepreneur of the Year.

Let's assume this person knows what he is talking about!

Here is our takeaway from Mr. Siebel's new book, *DIGITAL TRANSFORMATION: SURVIVE AND THRIVE IN AN ERA OF MASS EXTINCTION*. (2019):

Here is the one question to ask your team each year:

“Is our industry facing evolutionary change or are we going through a period of “punctuated equilibrium?”

This question sounds like something a philosophy professor might ask in an undergraduate seminar. The question is anything but academic.

How the Board responds to this question can then be a North Star for creating corporate strategy, corporate culture, hiring, and compensation.

Evolutionary Change vs. Punctuated Equilibrium:

When Charles Darwin wrote *ON THE ORIGIN OF SPECIES* (1859), he proposed evolution as a process of continuous change—a slow and unceasing survival of the fittest over vast periods of time.

In business we constantly see evolution. Each year new and improved car models appear. Each year our computer operating systems are upgraded. Apple comes out with a new and better mobile device every two years, etc. The laptop you are using may be

“modern” but its evolution can easily be traced to the Xerox’ Alto Personal Computer of 1973.

Evolutionary change implies that there is time to spot industry trends and slowly adapt at your own pace.

Thomas Siebel issues business leaders this warning: evolutionary change is the exception and not the rule.

Fossil records show discontinuity as the rule.

As opposed to Darwin’s evolution concept, Punctuated Equilibrium suggests long periods of slow evolution punctuated by dramatic transformation.

Species may stay in equilibrium for thousands of generations. And then there is a rapid explosion of new species. This period of disequilibrium is followed by a long period of relative stability.

Punctuated Equilibrium in Business:

Siebel’s thesis is that we are amid an evolutionary punctuation.

Since 2000, 52% of the Fortune 500 companies have either been acquired, merged, or have declared bankruptcy. It is estimated that 40% of the companies in existence today will shutter their operations in the next ten years.

Mass corporate extinction doesn’t happen without a reason.

The author states the reason is the confluence of four technologies: cloud computing, big data, the internet of things, and artificial intelligence.

Each technology is important. The interaction of these four technologies, however, means massive industry disruption.

Metcalfé’s Law:

In the 1970’s, Bob Metcalfe invented Ethernet. This was a technological breakthrough that allowed previously discrete computers to move into interactive networks. Metcalfe understood that the power of the network itself would be greater than the sum of all its components. To dramatize this idea, he formulated Metcalfe’s Law: the power of the network is a function of the square of the number of devices connected to that network.

When one person was on Facebook, the service at little value. As the network of Facebook users expanded to 2.38 billion in July 2019 the commercial importance of the total Facebook user network has become greater than any one Facebook user or even the totality of Facebook users at the individual level.

Imagine Metcalfe's Law as it applies to the Internet of Things.

According to Siebel, do not think of a sensor as only a sensor. It is a small computer or will soon become a small computer.

We will have 50 billion small computers connected to a network. Fifty billion squared is equivalent to the number of stars in our universe. Siebel states:

The Internet of things may be the single most important defining feature of the 21st century economy.

A powerful global network becomes a new computing platform. And much of the computing will take place within the sensors at the periphery of the network rather than at the core of the network. For example:

A sensor will alert a grocery store employee that a particular lettuce has a shelf life of four days.

Metcalfe's Law Meets Moore's Law:

In 1965, Gordon E. Moore—the co-founder of Intel (NASDAQ: INTC)—postulated in a magazine article that the number of transistors that can be packed into a given unit of space will double about every two years.

Gordon Moore did not call his observation "Moore's Law," nor did he set out to create a "law." Moore made that statement based on noticing emerging trends in chip manufacturing at Intel. Moore's insight became a prediction, which in turn became the golden rule known as Moore's Law.

Moore's Law proved to be generally true.

For decades following Gordon Moore's original observation, Moore's Law has guided the semiconductor industry in long-term planning and setting targets for research and development (R&D). Moore's Law has been a driving force of technological and social change, productivity, and economic growth that are hallmarks of the late-twentieth and early twenty-first centuries.

Moore's Law implies that computers, machines that run on computers, and computing power all become smaller and faster with time, as transistors on integrated circuits become more efficient. Chips and transistors are microscopic structures that contain carbon and silicon molecules, which are aligned perfectly to move electricity along the circuit faster.

The faster a microchip processes electrical signals, the more efficient a computer becomes. Costs of these higher-powered computers eventually decrease by about 30% per year because of lower labor costs.

In other words, technology will get faster, smaller, and cheaper every two years.

How Big Is Your Data Moat?

According to Siebel, the combination is going to promote a flurry of industry consolidation.

“The future has never looked brighter for large companies embracing digital transformation.”

The reason is Metcalfe’s Law: large companies tend to have dramatically more data than smaller companies. Metcalfe’s Law predicts access to a vast amount of proprietary data becomes a “data moat” to discourage competitors.

Think of the data moats around Amazon, Facebook, and Google

Companies with large data moats have an easier time attracting capital and attracting the best technological talent.

The Board’s Role in Creating a Corporate Culture to Survive in Times of Punctuated Equilibrium.

If the Board concludes that the company remains in a period of evolutionary change, then there is no need to make dramatic change to culture. Keep things customer-centric, reliable, and predictable. Follow “Best Practices” of others rather than take a leadership role.

If the Board, however, concludes that we are in a period of Punctuated Equilibrium, then the Board needs to examine if it has a corporate culture that can rapidly deal with disruption.

The silo mentality needs to be quickly destroyed. Companies must be highly sensitive about attracting and retaining people who are open to change/new ideas. Those employees who view change as a threat may be a threat to the survival of the company.

Consider Blockbuster and Netflix:

At its peak, Blockbuster employed 60,000 people and earned \$5.9 billion in revenue. Netflix CEO Reed Hastings proposed a merger with Blockbuster whereby Netflix would run Blockbuster’s online presence.

Blockbuster declined as it did not see any value in the combination.

In 2019 Netflix has a market capitalization of \$160 billion and Blockbuster filed for bankruptcy.

Netflix had been wedded to video by mail order but saw the technological shift to streaming video. It dropped its mail order business and quickly transformed. Blockbuster remained committed to its franchise retail store model.

Questions to Consider Each Year at the Board Meeting:

Is our industry in a period of evolutionary change or are we in a period of punctuated equilibrium?

Depending on the Board's answer to this question, the following are follow-up questions to consider:

Is digital and cultural transformation being driven by the CEO across functional boundaries or is it driven by key C-Suite function leaders meeting resistance from other functions?

How does the company attract talent open to change/new ideas?

How does our answer influence the corporate strategy?

How does our answer influence the type of people we need to serve with us on this Board of Directors?

How does our answer influence how we pay our CEO?

Summary and Conclusion:

Kevin Coffee of Bajan Waters cautions boards about the importance of making public underlining assumptions. And one underlying assumption is the nature of change.

The assumption that the change will take place gradually means that the Board may lack appreciation for critical discontinuities that competitors grasp earlier. (2019).

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