



DISCONTINUITIES WHERE DID THE BUSINESS MODEL GO?

In 1942 Joseph Schumpeter in his work entitled “Capitalism, Socialism and Democracy” coined the phrase “Creative Destruction” defined as a “process of industrial mutation that incessantly revolutionizes the economic structure from within, incessantly destroying the old one, incessantly creating a new one.” Once again this concept is gaining popularity and being quoted by economist as they try to explain economic volatility. This resurrection is not due to a belief that innovation or creativity has increased but rather that the rate of destruction has accelerated. Historically, creative destruction involved marginal improvements occurring over many decades. Armed with a time advantage, businesses could adapt to the new methodologies. More importantly, the elapsed time frame allowed generational adaptation, whereas the originators of the obsolete technology were surpassed by the next generation of new inventors. It is a known fact that change occurs more freely when the innovator was not the originator of the first idea.

Human nature has always had difficulty accepting obsolescence of what they personally crafted with mind and hands. Contrarily, a family business heir can accept the need to change grandfather’s business, as they view the "old practices" as being outdated.

However, today changes are occurring rapidly; sand castles built in the morning are being washed away by the afternoons’ tide. Such expediency requires the originator to recognize and respond to creative destruction prior to a comfortable mental release of the old methodologies. Especially hard hit are the small to medium businesses (SME’s) with the founders nearing retirement. At an awkward point in their business life they are learning that their company asset (and once perceived safe nest egg) is yesterday’s business model and losing value daily. Unfortunately many business owners do not recognize or more accurately refuse to accept this inherent threat until it is too late.

False Beliefs and Perceptions

David Neeleman, the CEO and founder of JetBlue recognized the advantage of change. “There are two axioms in business. One says that when you figure out what makes you successful, take the cookie cutter approach; don’t change a thing and be the best at that. The other says that you have to continue evolving in order to take advantage of new opportunities. I choose the latter. I don’t want to be a prisoner of our business model.”

Even with today’s accelerated pace, creative destruction still provides advanced warning signs, albeit more subtle in time and tone. However, often these early signs are not heeded and the time advantage is lost without implementation of adaptation and change. The company owners refuse to recognize that the world around them has changed and this business model may no longer apply to the given environment. This is especially true in traditional business models that have stood the test of time through generations of family ownership.

If earlier attempts at new technology produce false starts, the business owner can become desensitized to the threat and gain a sense of false security. In this delusional state he discredits all future possibilities of imminent change.

Personally I witnessed such behaviors many times over the years, with my first memory occurring two decades ago while employed at a traditional typesetting company. Ken Hansen, the owner of Hilton Typographers Inc. was repeatedly being forewarned about the Macintosh's ability to replace traditional typesetting. After once such discussion he stated that he had heard this same story many times before and it simply was not going to happen. With hindsight it became evident that this last warning was the tsunami and within 6 months the company was closed. I have witnessed similar mental avoidance built on the false pretense of time; this business has survived through two generations and it will continue to do so.

According to Don Matso of The Valere Group., who works with companies to formulate transition strategies and what he calls strategic value creation, "Identifying these elements of value is key to an affirmative strategy to protect and enhance the value of the business in preparation for any type of transition, whether it be for succession or retirement and ultimately, to create liquidity. Buyers will never pay a premium for a business whose metrics are spiraling downward; however, the buyer community reacts favorably to the business whose market dynamics have negatively changed and have exhibited an ability to transform itself quickly."

Conclusion

It could be argued that each and every company will someday reach a point where the significant market shifts will no longer support the business model. If adjustments had been made throughout the years, these changes can be seen as new opportunities rather than threats. This dilemma is not limited to SME's as many of our American foundational companies are struggling hard to stay alive in the new economy. Who would have ever predicted that in 2006, analysts at Bank of America would downgrade GM saying the company has a 40 percent chance of facing bankruptcy within the next few years. In this the SME's have the advantage of agility through size and are not burdened with legacy cost. If myopic vision was removed, in a generation from now they could be the next American idol.

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