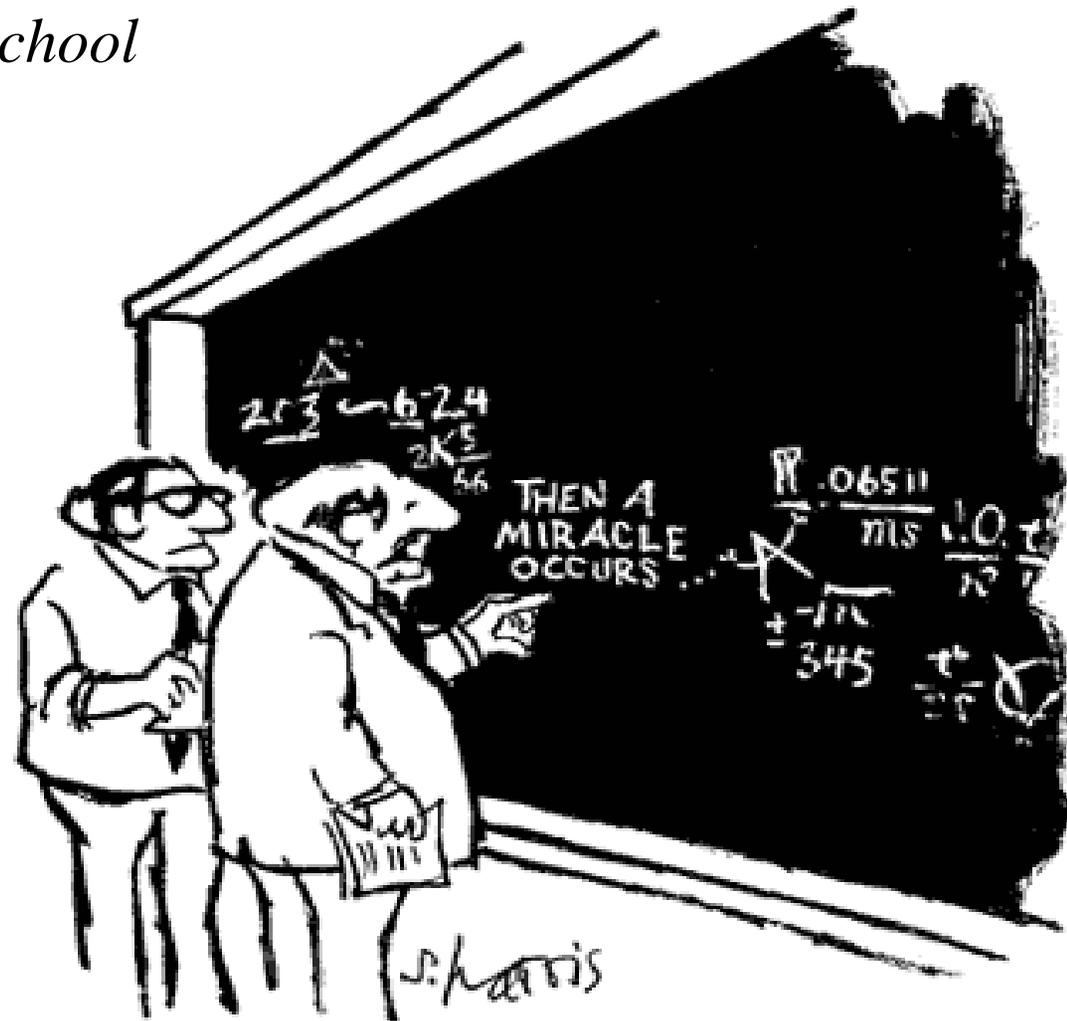


Investing in Growth

Clayton Christensen

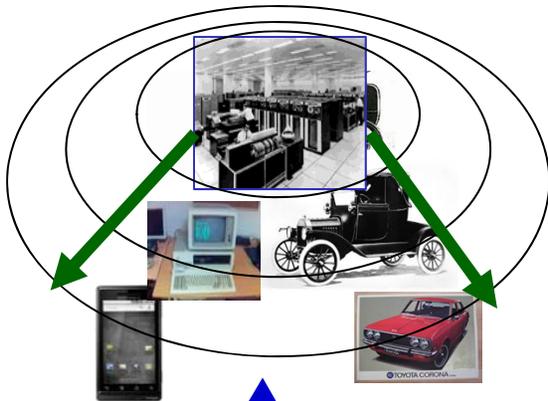
Harvard Business School



"I think you should be more explicit here in step two."

The economic engine

Market-creating innovations



Jobs
Capital

Market-creating

Creates
Uses

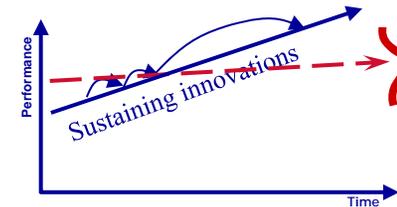
Sustaining

Few
Limited

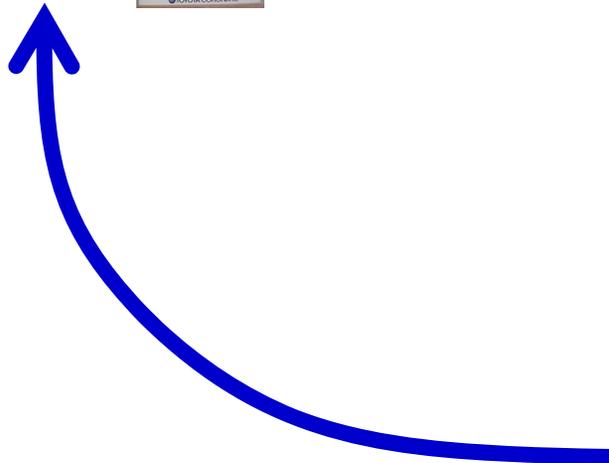
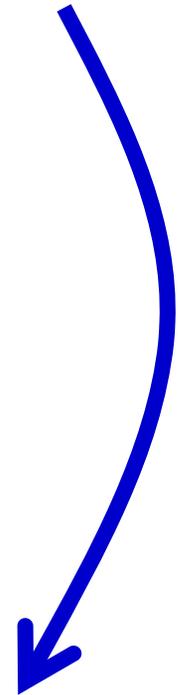
Efficiency

Eliminates
Frees

Sustaining innovations



Efficiency Innovations



The Church of New Finance



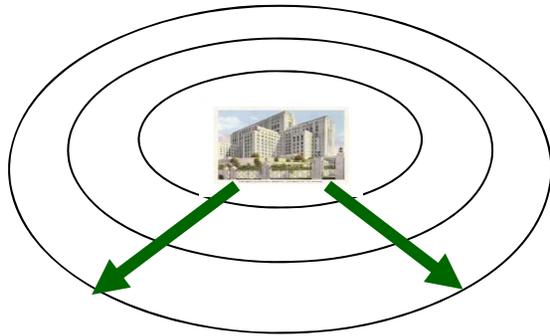
The high priests: business professors; partners in private equity, venture and hedge funds

Thou shalt measure success by:

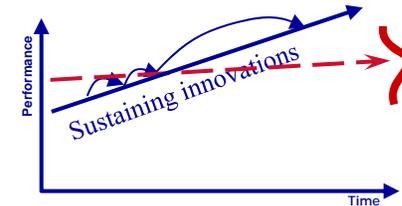
1. Return on net assets (RONA)
2. Return on capital employed (ROCE)
3. Internal rate of return (IRR)
4. Earnings per share
5. Gross margin percentage
6. Economic value-added (EVA)
7. Marginal cost / marginal revenue
8. Debt/Equity
9. Growth rate
10. Revenue per employee

The economic engine

Market-creating innovations



Sustaining innovations



Market-creating

Sustaining

Efficiency

Jobs

Creates

Limited

Eliminates

Capital

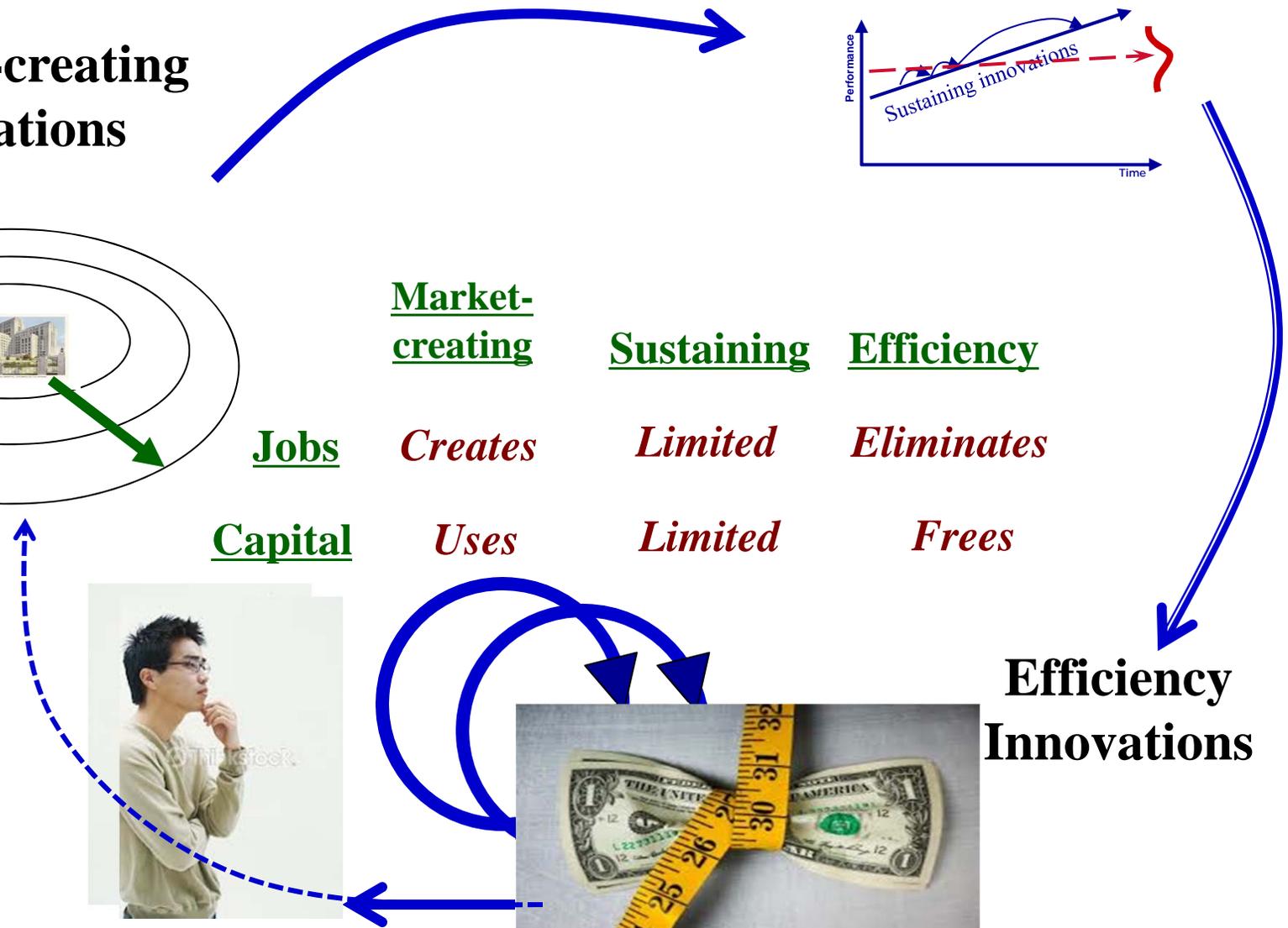
Uses

Limited

Frees



Efficiency Innovations



Capital superabundance

“The growth rate of the real economy of goods and services has been slowing in recent decades, while growth in the financial sector has been accelerating. Bain estimates that total financial assets are today almost 10 times the value of the global output of all goods and services, and that the development of financial sectors in emerging economies will cause global capital to expand by half again by 2020. We are awash in capital”

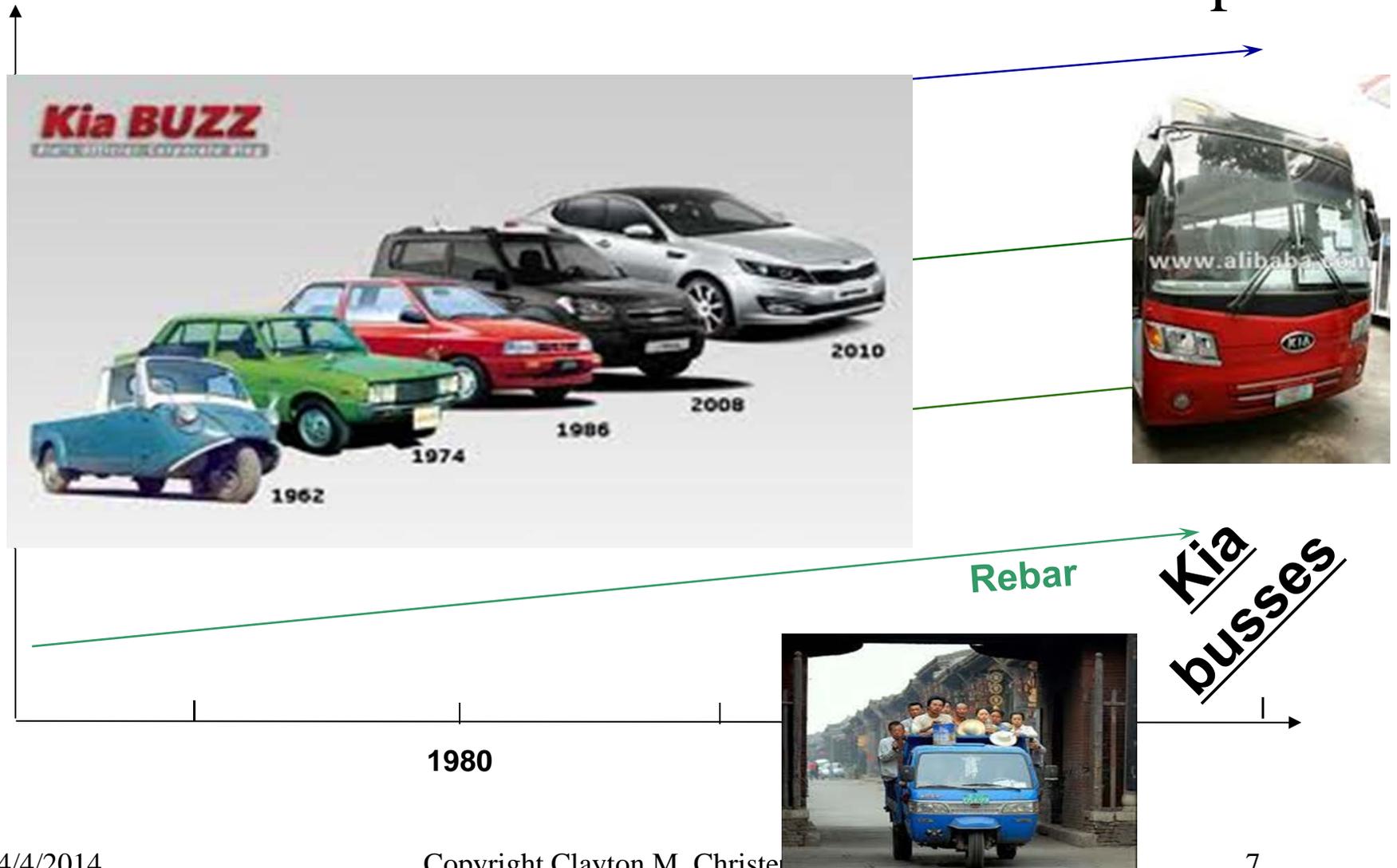
A World Awash in Money: Capital Trends through 2020,
Bain & Company.

What can be done?

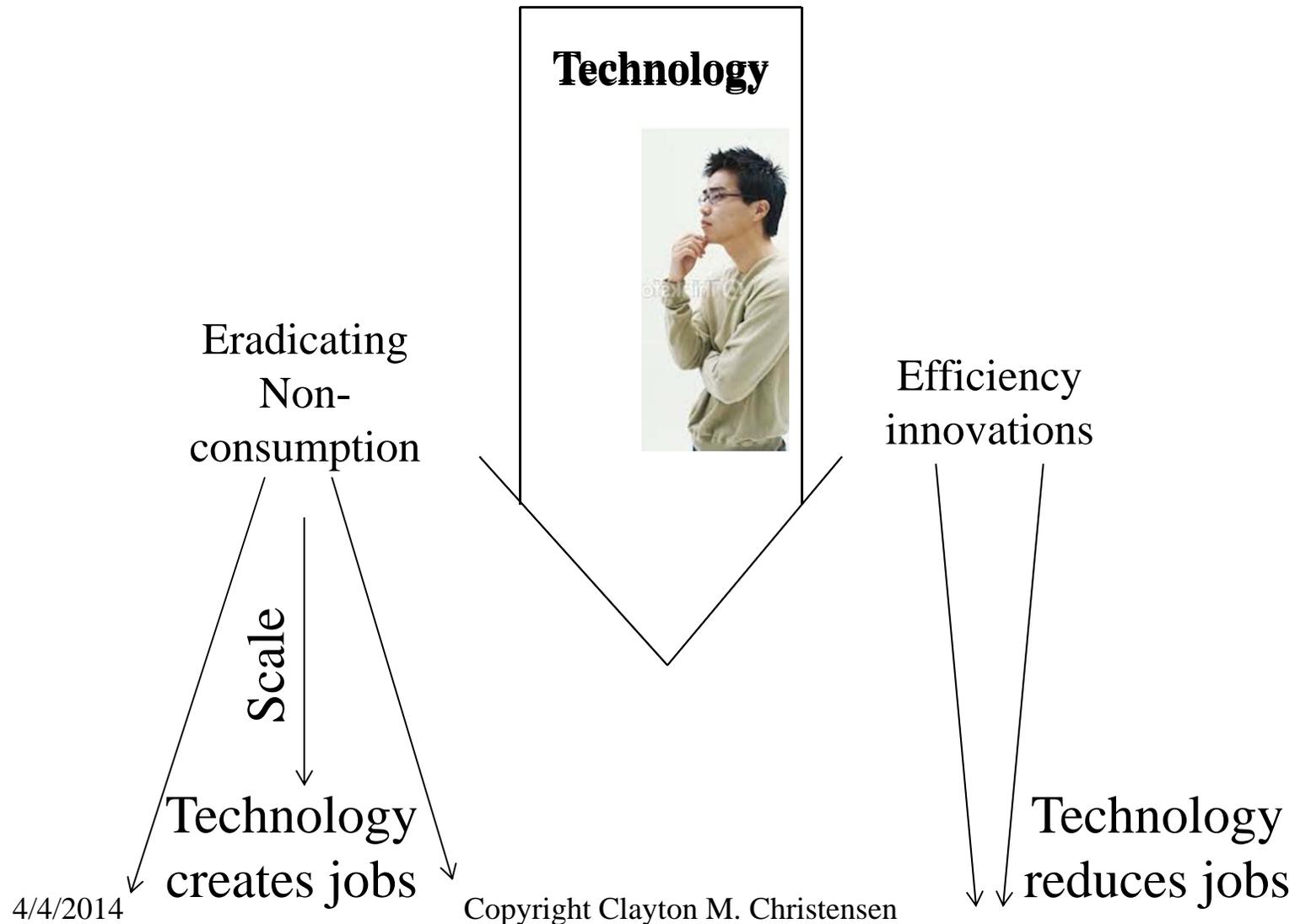
- Repurpose capital
 - Tax rates
 - L-Shares
- Reorient business schools
- Pensions
- Embolden executives
 - Homestead / disenfranchised votes
 - New measures of success

Disruption in automobiles

Each began in as a domestic disruption



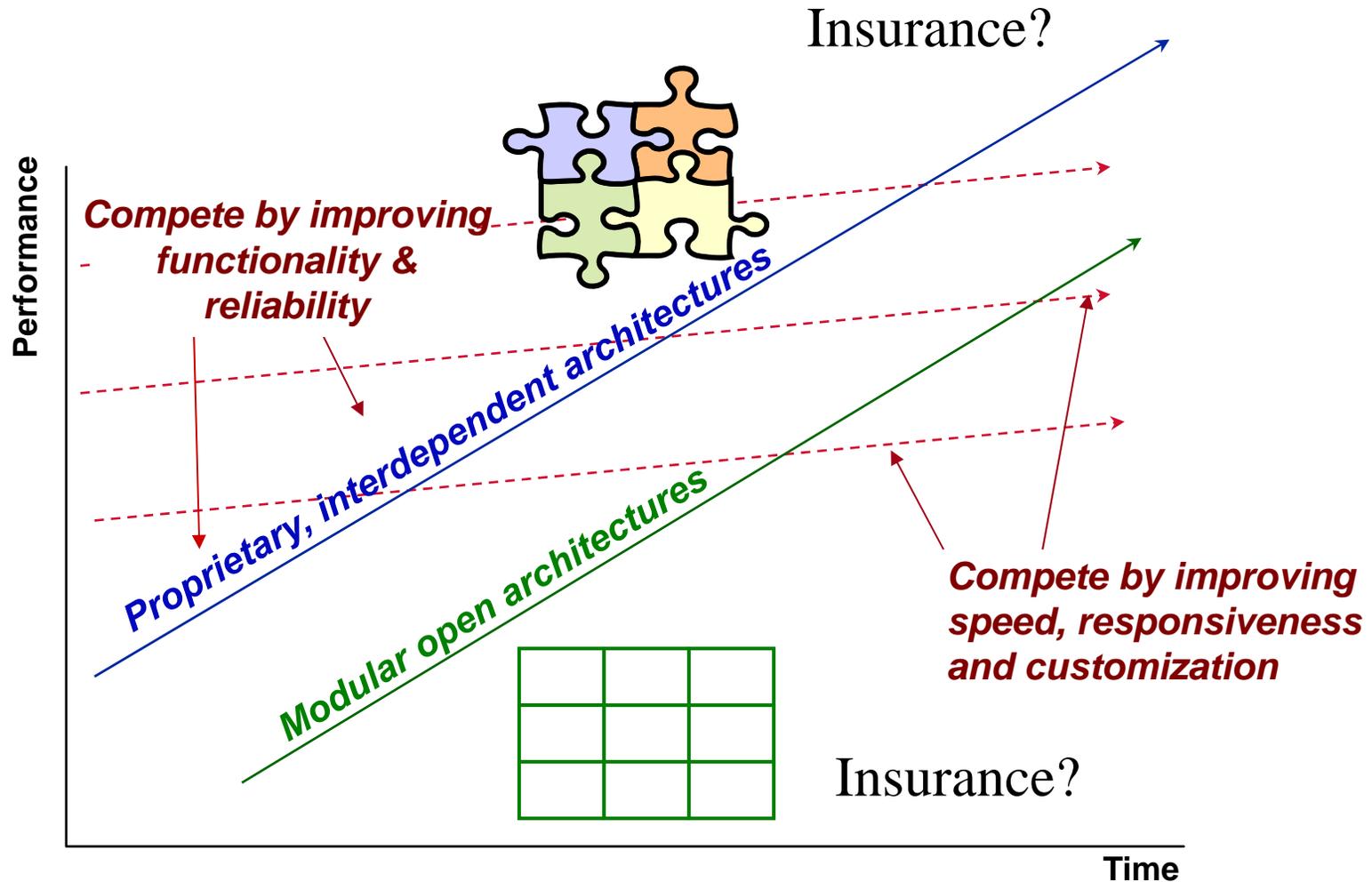
Managerial efficiency vs. entrepreneurial market-creation



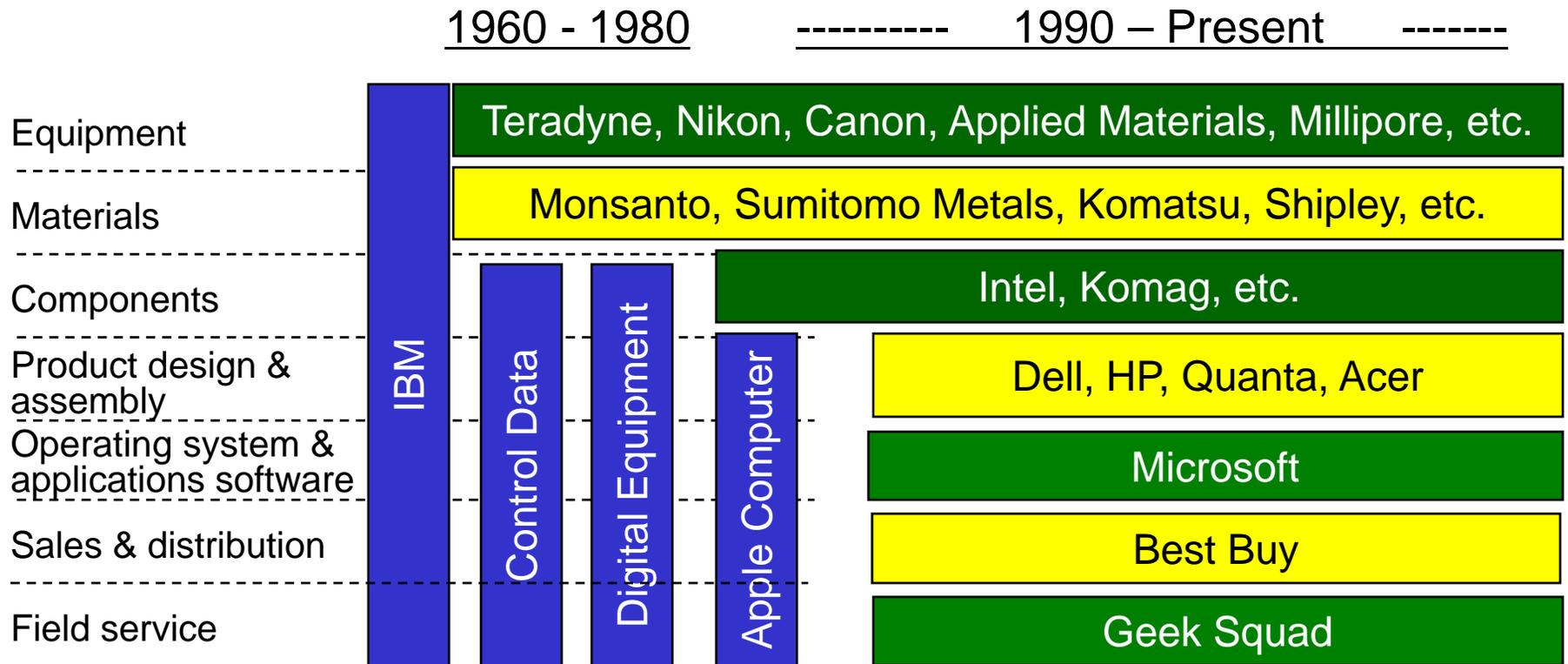
In the end, finance destroys finance

- Monetary policy is now the equivalent of pushing a string.
- Commercial and retail banking become obsolete
 - Deposits are a burden; middle-market lending has stopped.
 - Revenues and variable costs are evaporating; fixed costs are not.
- Because we are awash in cheap capital, we can use capital abundantly.
 - Discount NPV at 2%, not 20%
 - Measure success by different metrics. When the return is nearly zero, maximizing return on capital, and maximizing the accumulation of free cash flow, loses meaning.
- Measuring investments in people is a likely candidate

The right product architecture depends upon the basis of competition



Changes in product architecture have profoundly changed the architecture of the computer industry



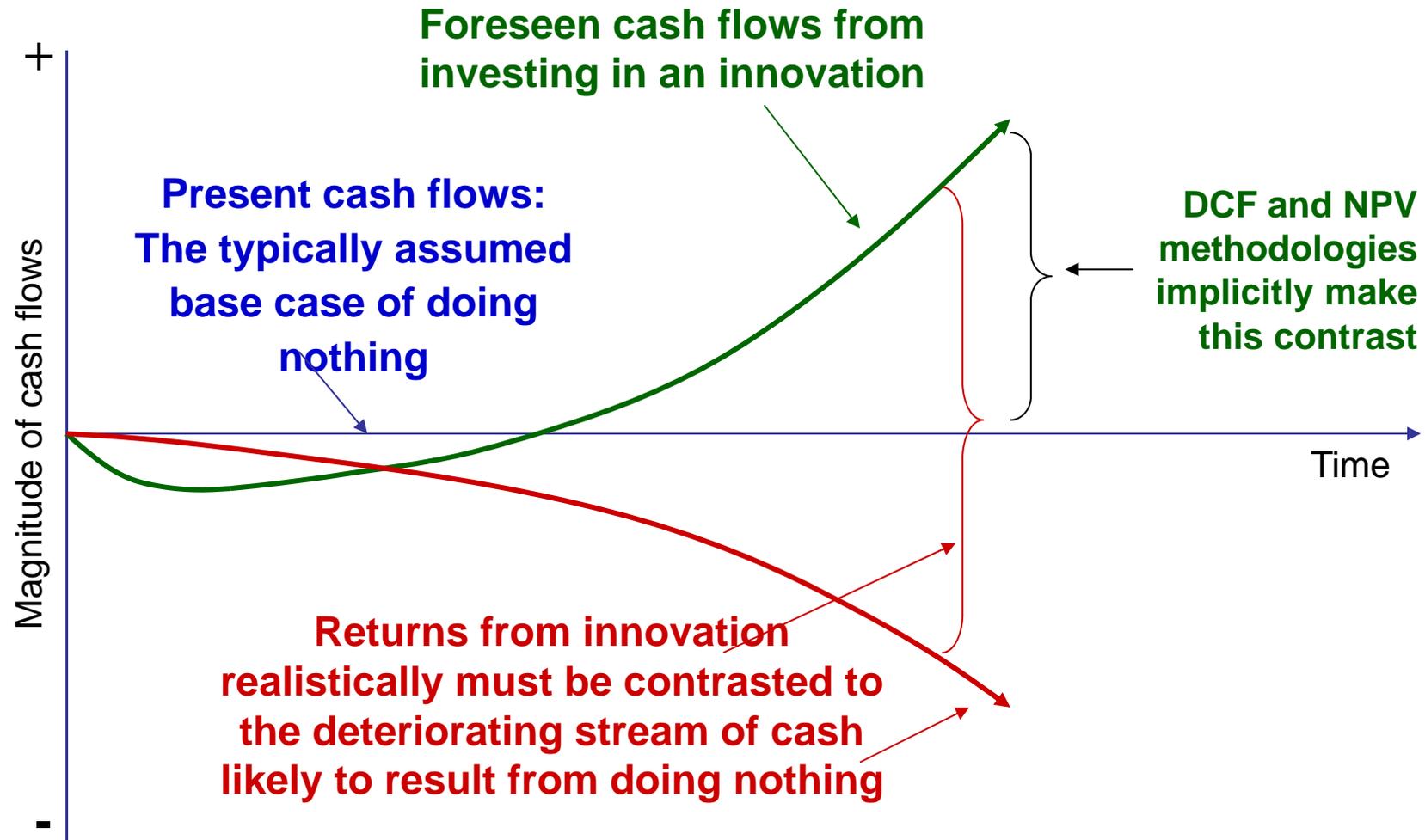
The law of conservation of attractive profits

De-Commoditization: services & products that make use of the product more effective

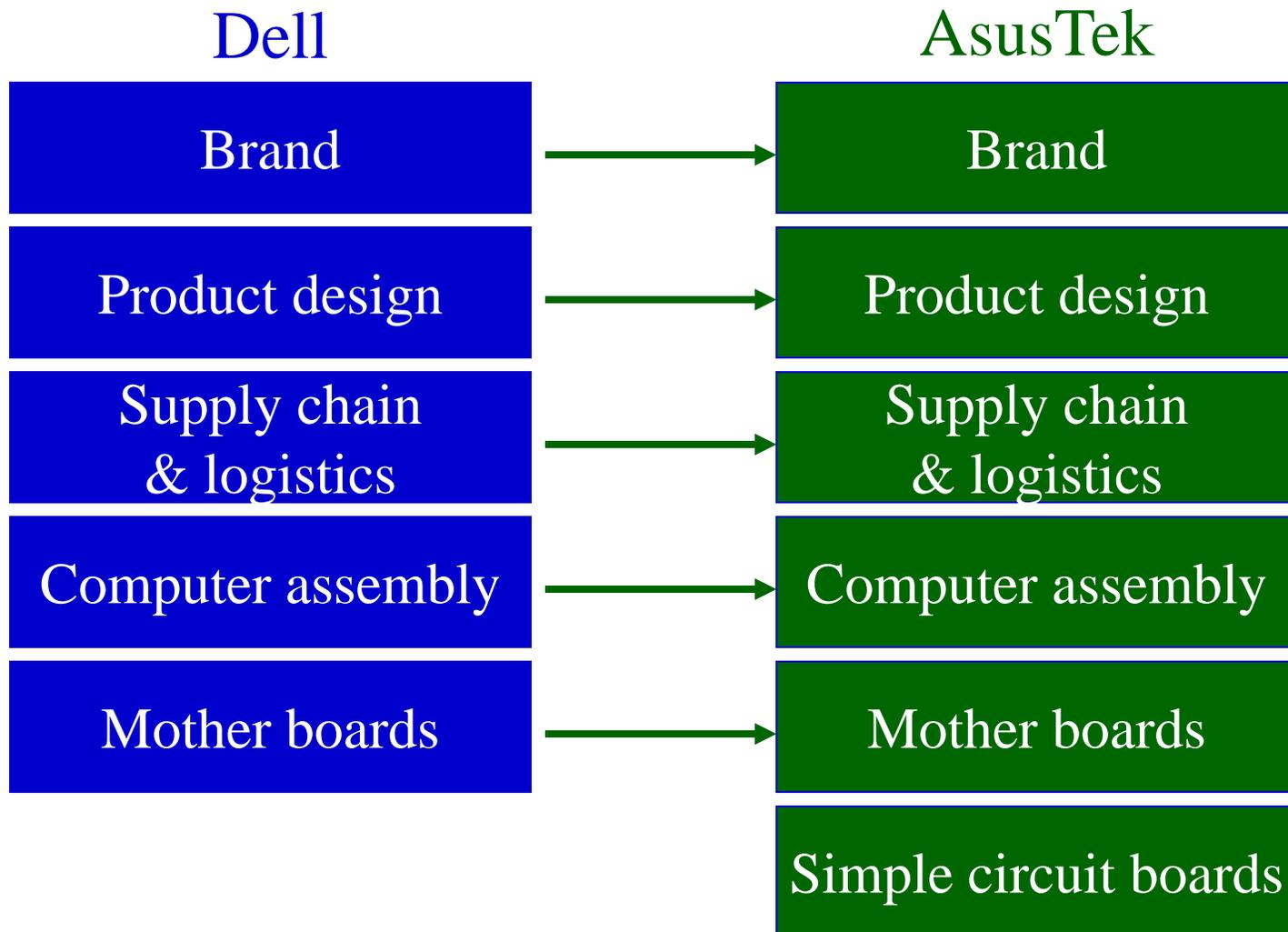
Commoditization thru modularity, over-shooting

De-Commoditization: sub-systems that drive the performance of the modular product

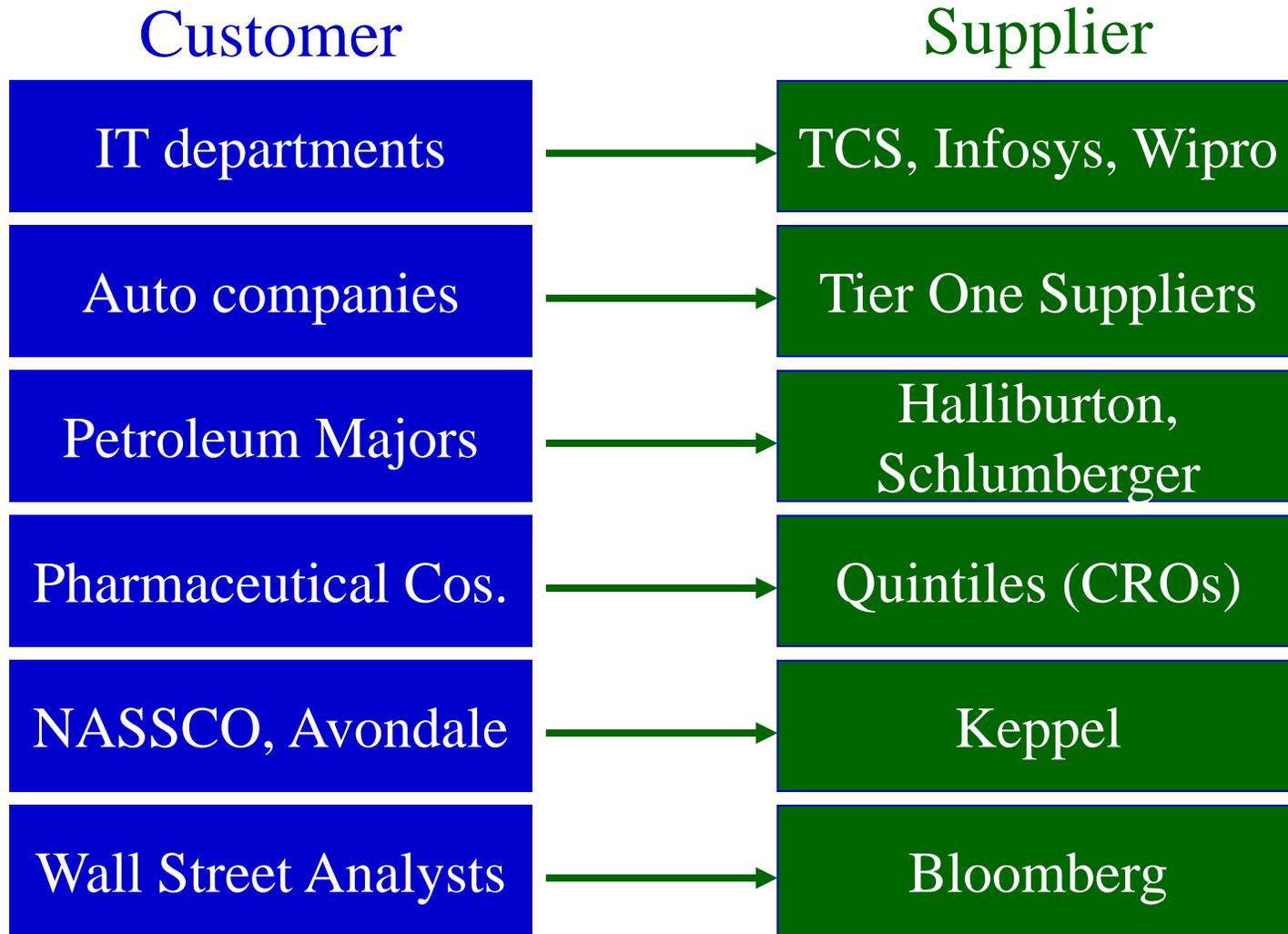
The common methods of financial analysis systematically bias managers against innovation



Outsourcing often sets in motion disruptive business model liquidation



Outsourcing often sets in motion disruptive business model liquidation

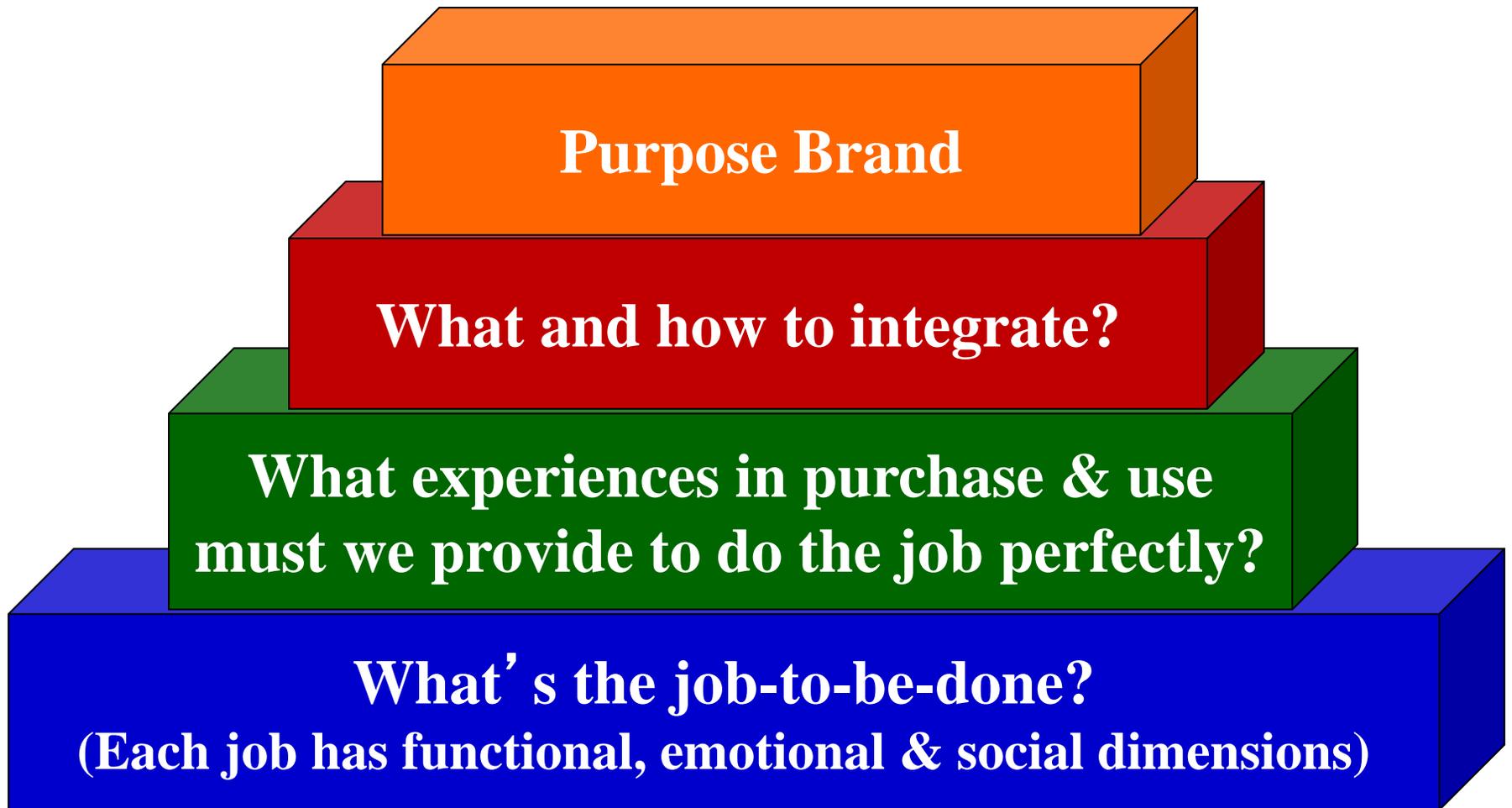


Market Understanding that Mirrors how Customers Experience Life



“The customer rarely buys what the company thinks it is selling him” - *Peter Drucker*

Four levels in the architecture of a job



Organizing by jobs to be done would change the processes of care.

It might also change the business of risk

I know what is wrong. I don't want to see a doctor. Just fix it.

Something is wrong and I need to know what it is.

Help me care for myself or my family member

Help me stay healthy.

Potentially jobs for cars..

**My car
is my office.**

**I need
a car that will
lubricate
my life.**

**Whatever
happens, I need to
be sure that my
family and I
are safe.**

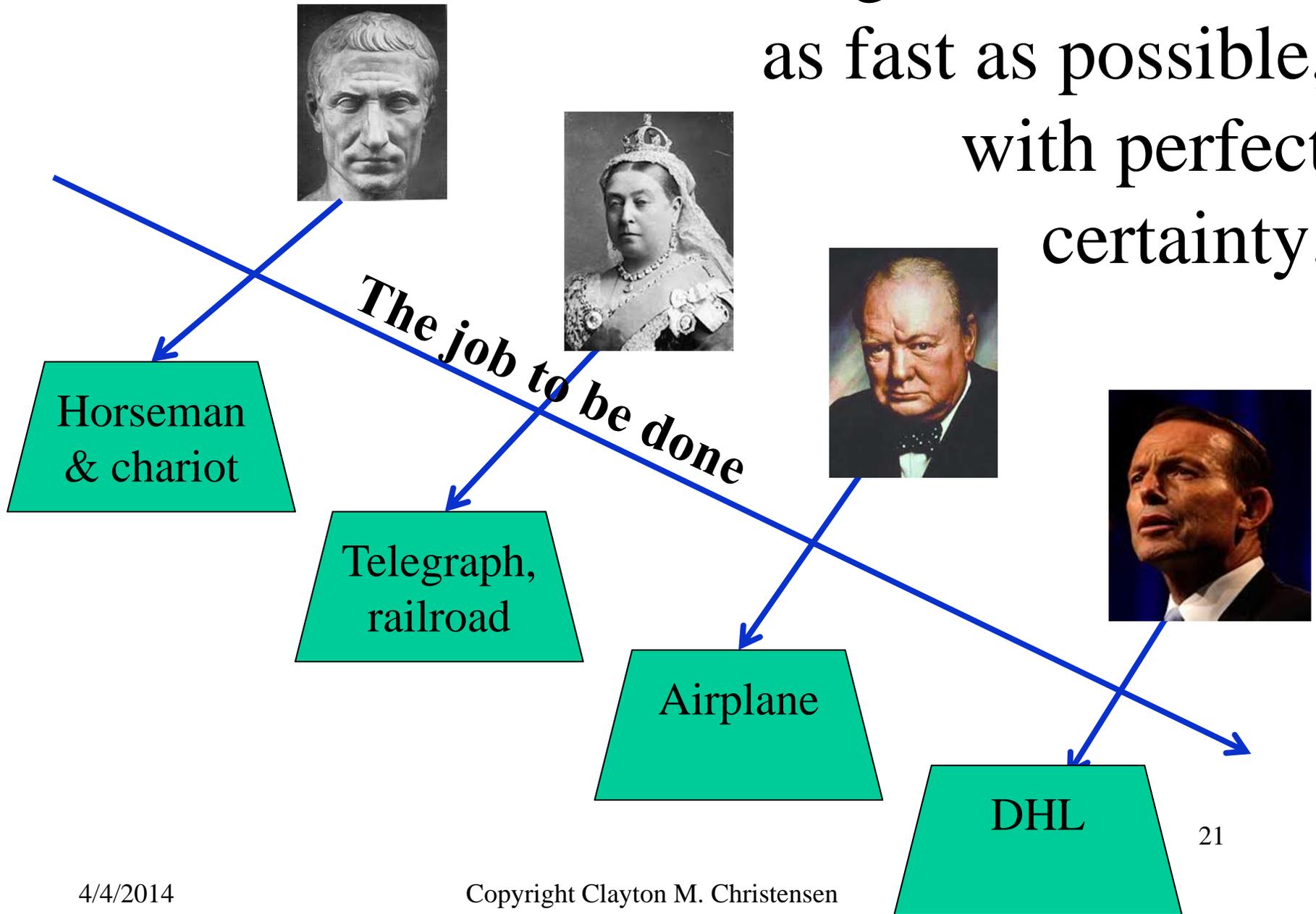
**Help me
feel like the person
that I want
to be**

Understanding a job is a “mining” process, not an event.



- More growth
- Potential for enduring differentiation
- More → few competitors from customers’ perspective
- Two-sided compass

I need to get this to there
as fast as possible,
with perfect
certainty.



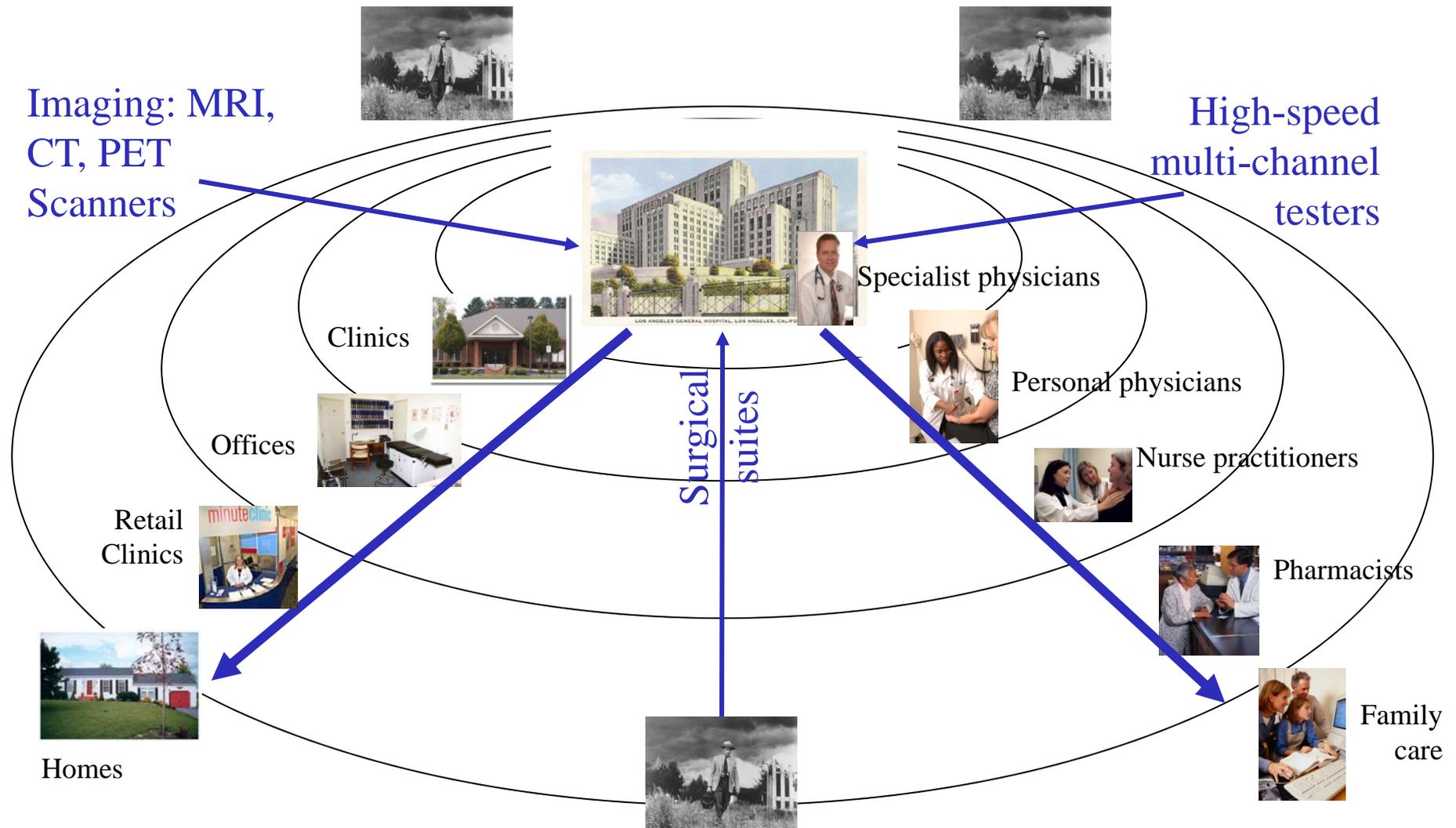
The advantage of focusing on a job-to-be-done.



The advantage of focusing on a job-to-be-done.



The decentralization that follows centralization is only beginning in healthcare



1. Bring the problem to the solution. 2. Then bring the solution to the problem.

SOLUTION SHOPS

- Consulting firms
- R&D organizations
- Diagnostic & intuitive activities of hospitals

FEE FOR SERVICE

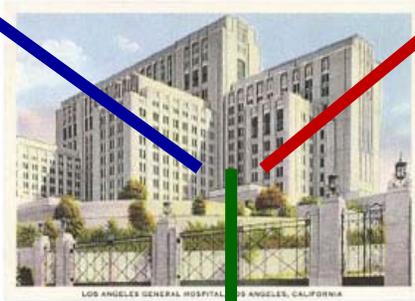


National Jewish Medical Center
Pulmonary & Respiratory Diseases



Dave Snow, asthma
CEO, Medco

**Typical hospitals
are not
complicated.
They are
impossible.**



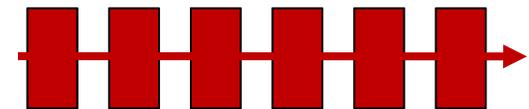
PROCESS BUSINESSES

- Manufacturing
- Education
- Construction
- Medical procedures

*FEE FOR
OUTCOME*



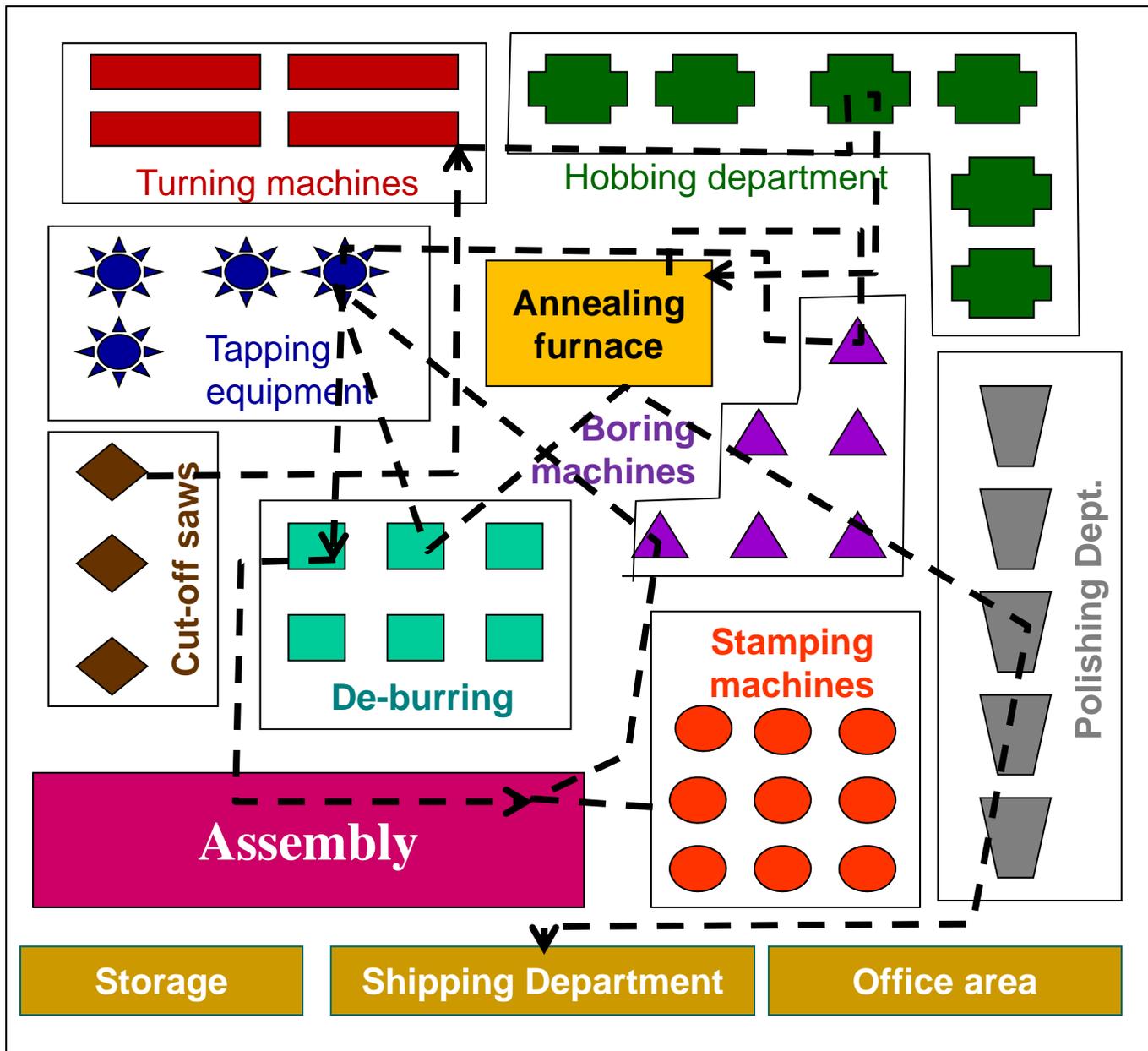
**Shouldice Hospital:
Hernia surgery**



FACILITATED NETWORKS

- Telecommunications
- Insurance
- EBay
- D-Life; Crohns.org

*FEE FOR
MEMBERSHIP*



We'll do anything for anybody.

- Overhead = 85% of total
- Overhead increases 30% for each doubling of complexity
- Variable quality

When one business model predictably will diverge into two



When two business models predictably converge into one



4/4/2014

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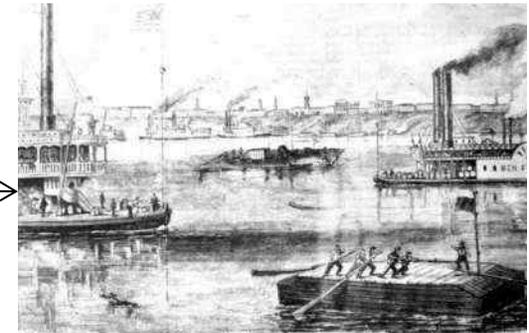
28

A Theory of Hybrids

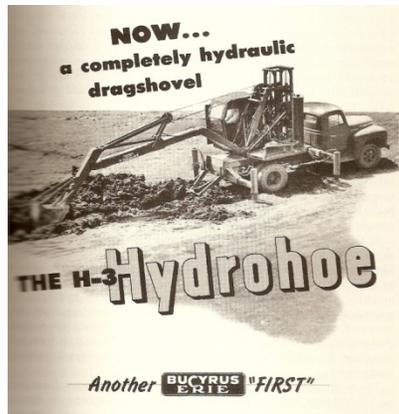
Hybrid when deployed
as a sustaining technology
against consumption

Original Technology

Pure-play deployed
against non-consumption



Memphis, Tennessee, circa 1850. The shallow draft keelboats and flatboats of the eighteenth century did not necessitate extensive river improvements, the steamboats of the nineteenth century did.

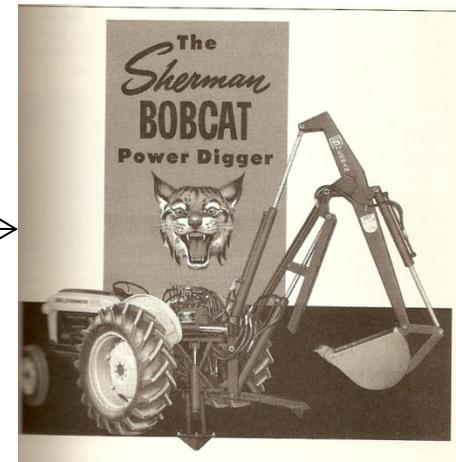


4/4/2014

Figure 3.1 Cable-Actuated Mechanical Shovel manufactured by Osgood General



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The spreadsheet (1978) changed management.

1. Analysts now build financial models of companies; and then effortlessly test the impact of different inputs onto the outcomes that matter: RONA, ROCE, & IRR.

2. This enables 26 year-old analysts to teach executives how to run their companies. With shorts, calls & puts, they can punish executives who don't meet or exceed the numbers.

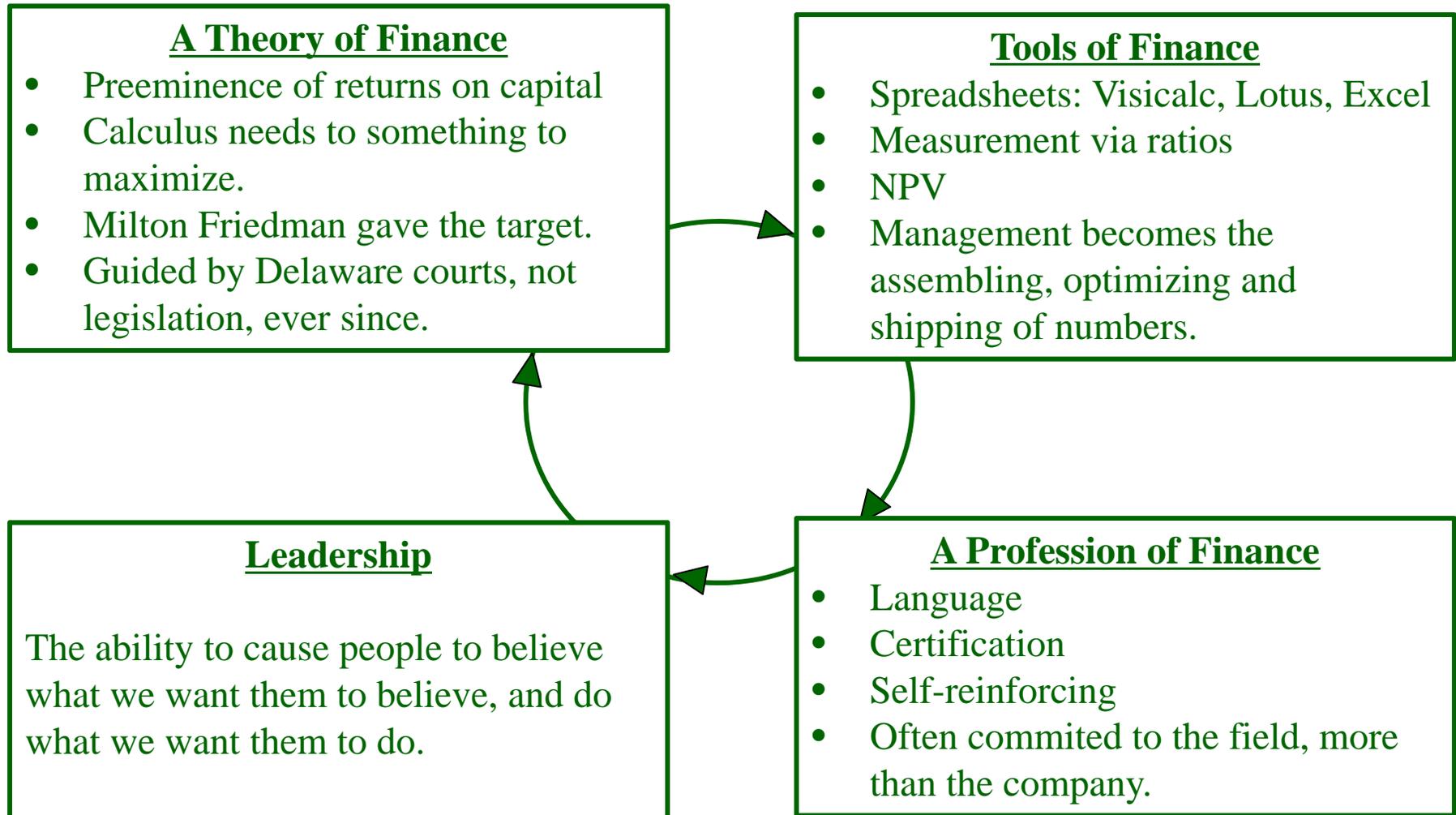


3. The manager has been commoditized. The job essentially has become the assembly and shipping of numbers. The agenda of meetings with direct reports begin and end with searching for numbers.

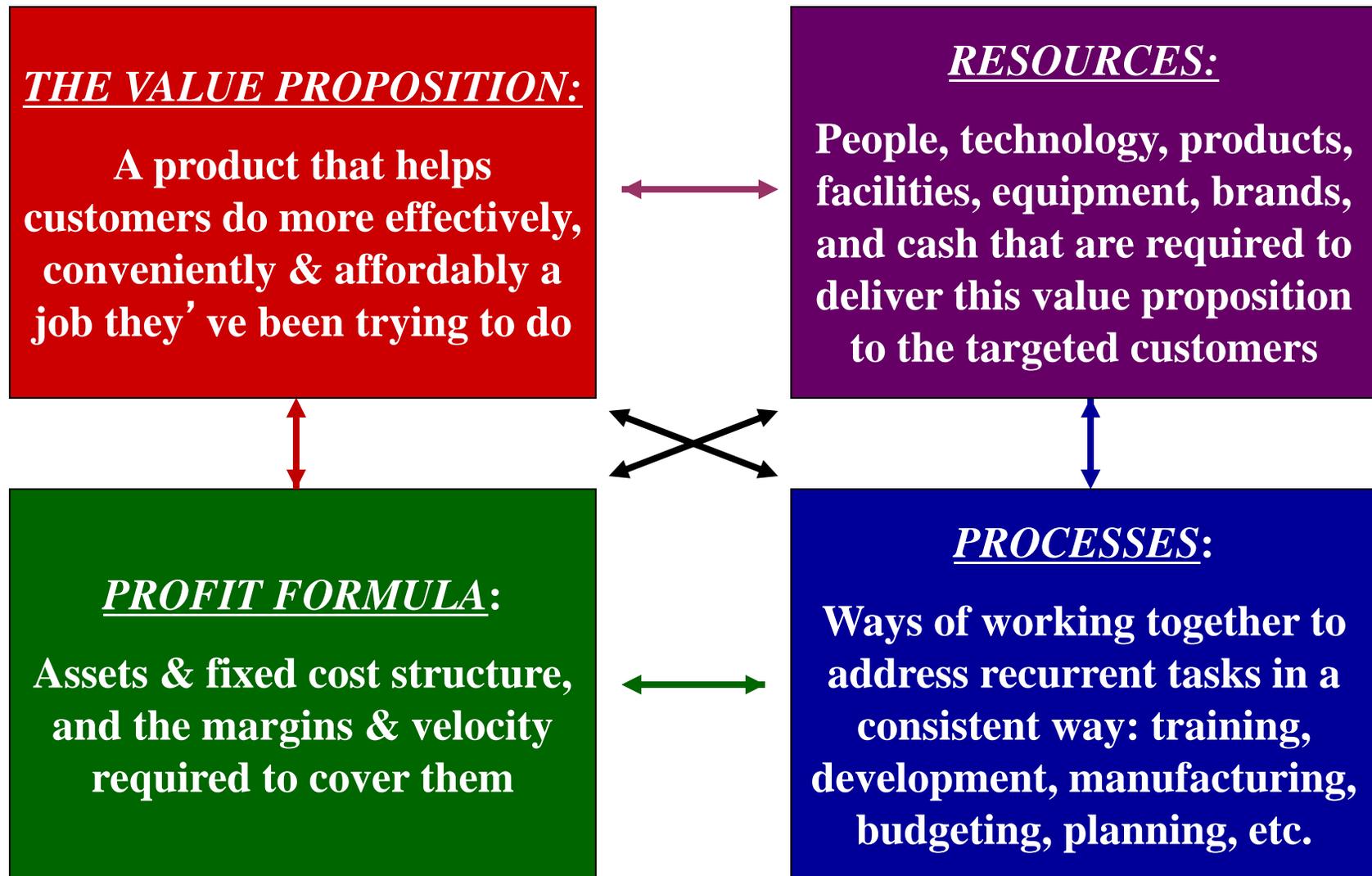


Finance:

Lubricates and fuels → Commands and captures



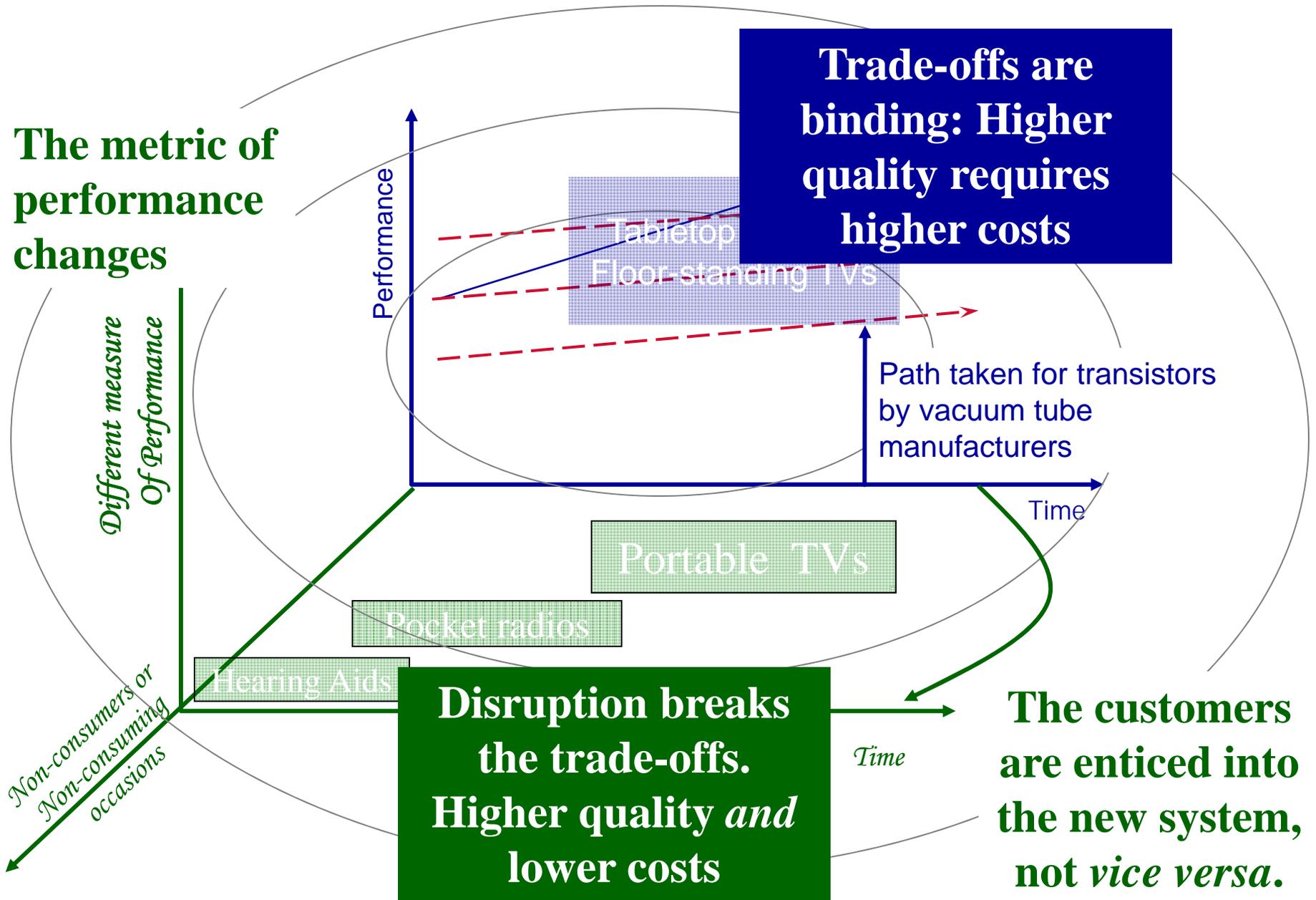
What is a business model, and how is it built?



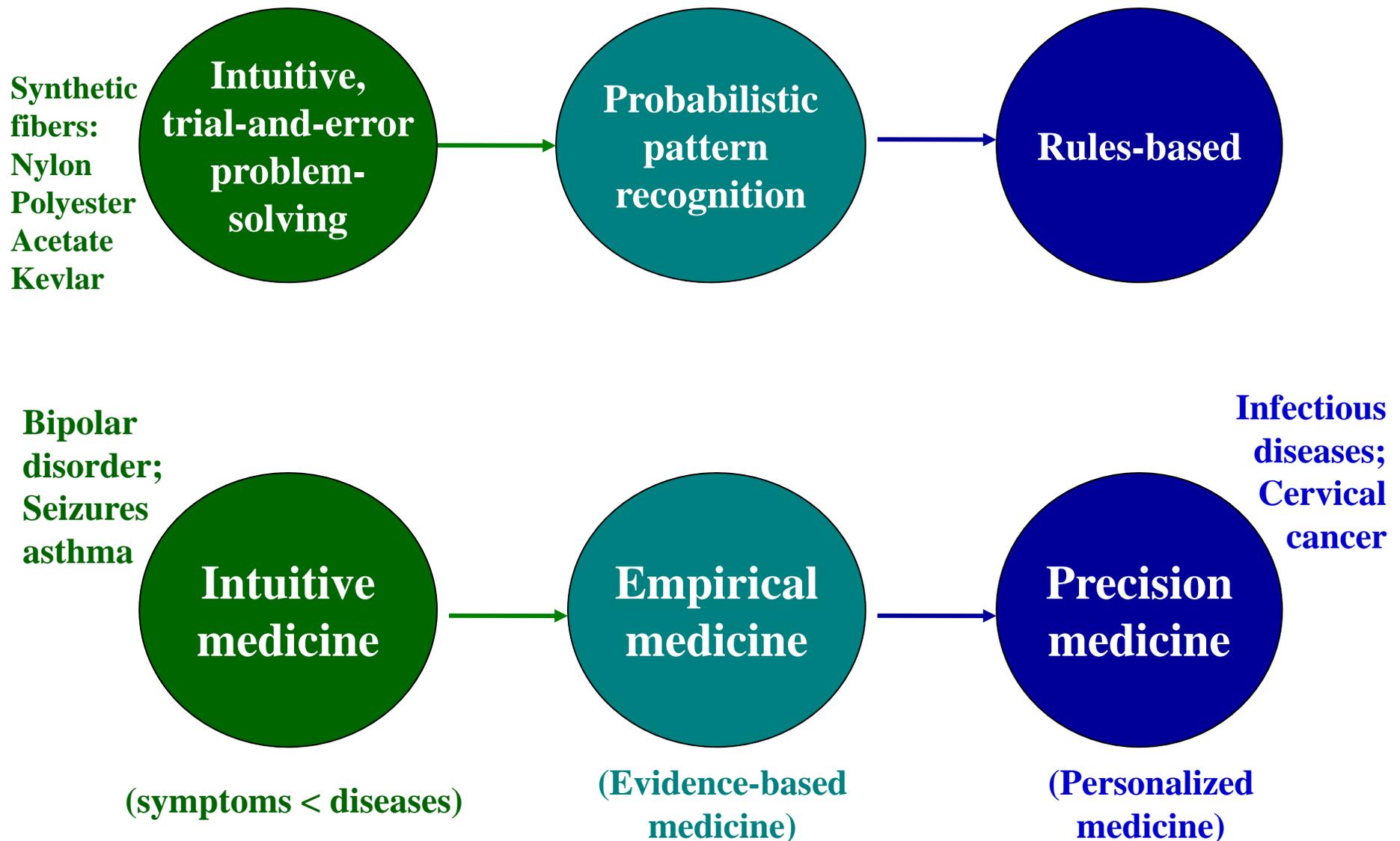
Are there two paths to growth?



The metric of performance changes



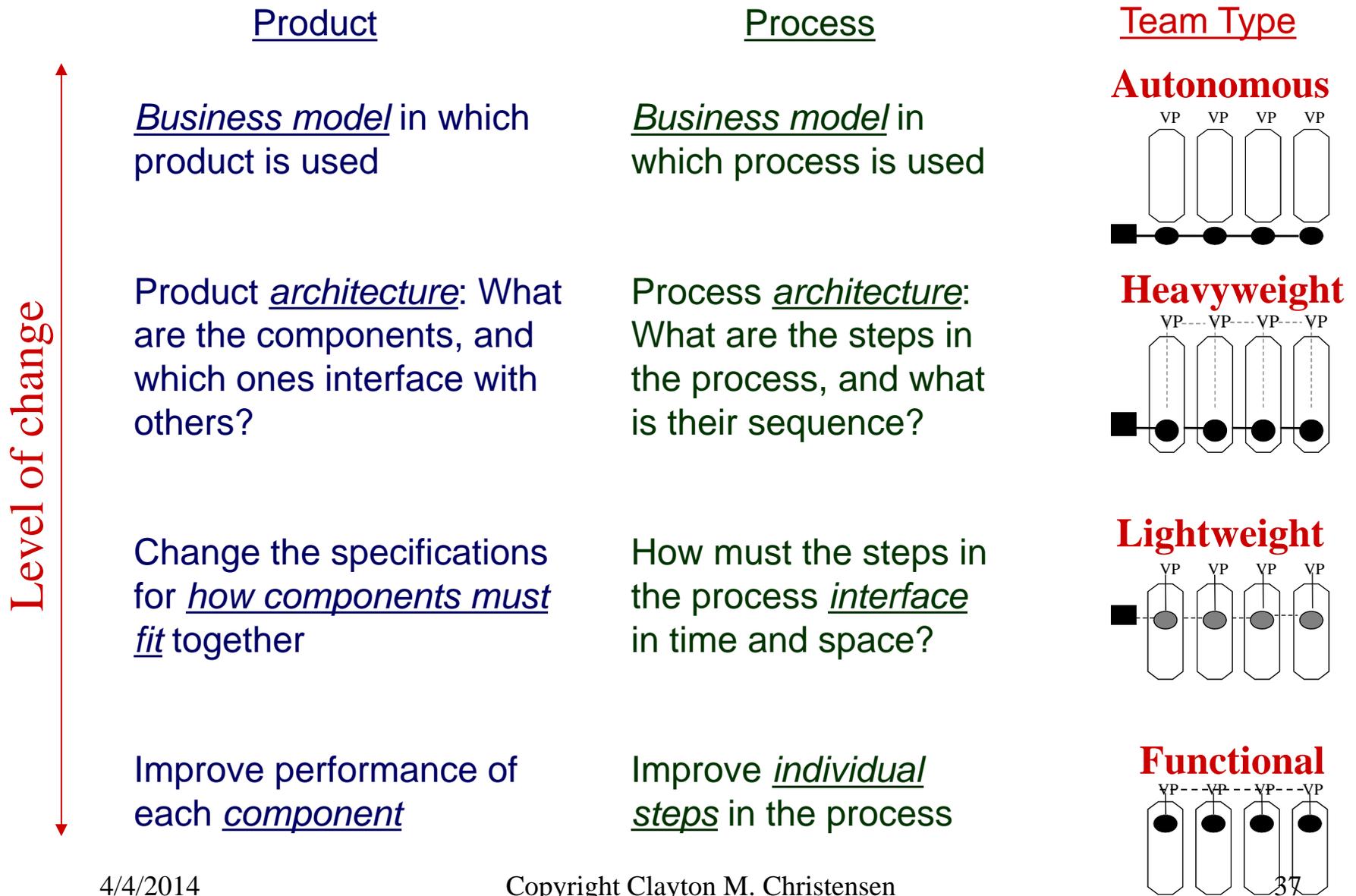
Scientific progress that commoditizes expertise plays a critical role in disruption



Stephen Gould: Panda's Thumb

- General, community hospitals
 - 1920s: doctors cheap, transportation expensive
 - Do everything for everybody
 - 2013: doctors expensive, transportation cheap
- Marginal cost is lower than whole cost
- Doctors choose this profession so that they can control their destiny and choose how they will work.
- Reducing cost inherently impairs quality of care

Proper team structure is crucial in every project



Discovery-Driven Planning is a better way to manage the flow of projects through the development funnel

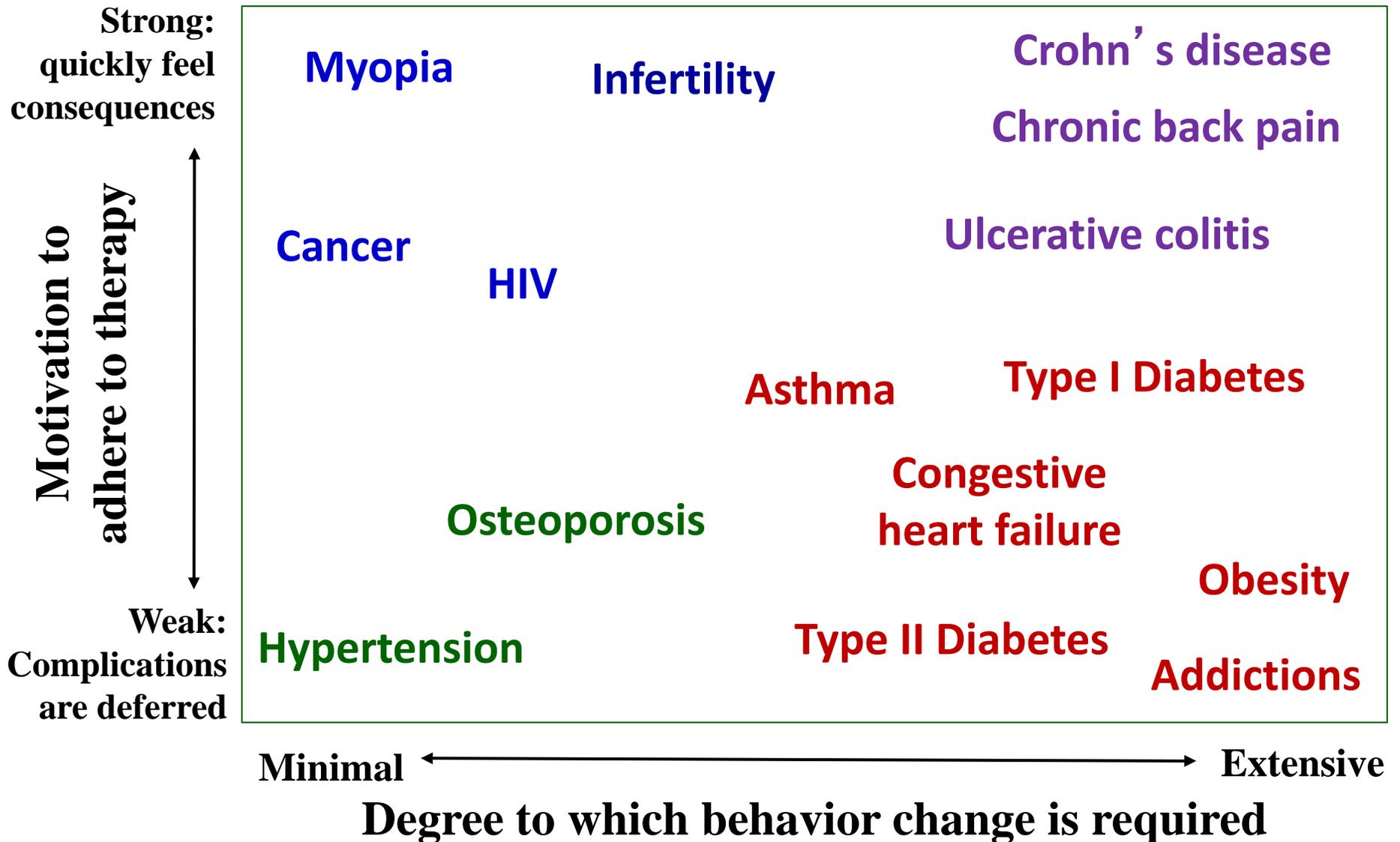
Platform-based planning

1. Make Assumptions
2. Build projections based upon assumptions
3. Make decisions to invest based upon projections
4. Implement the deliberate strategy

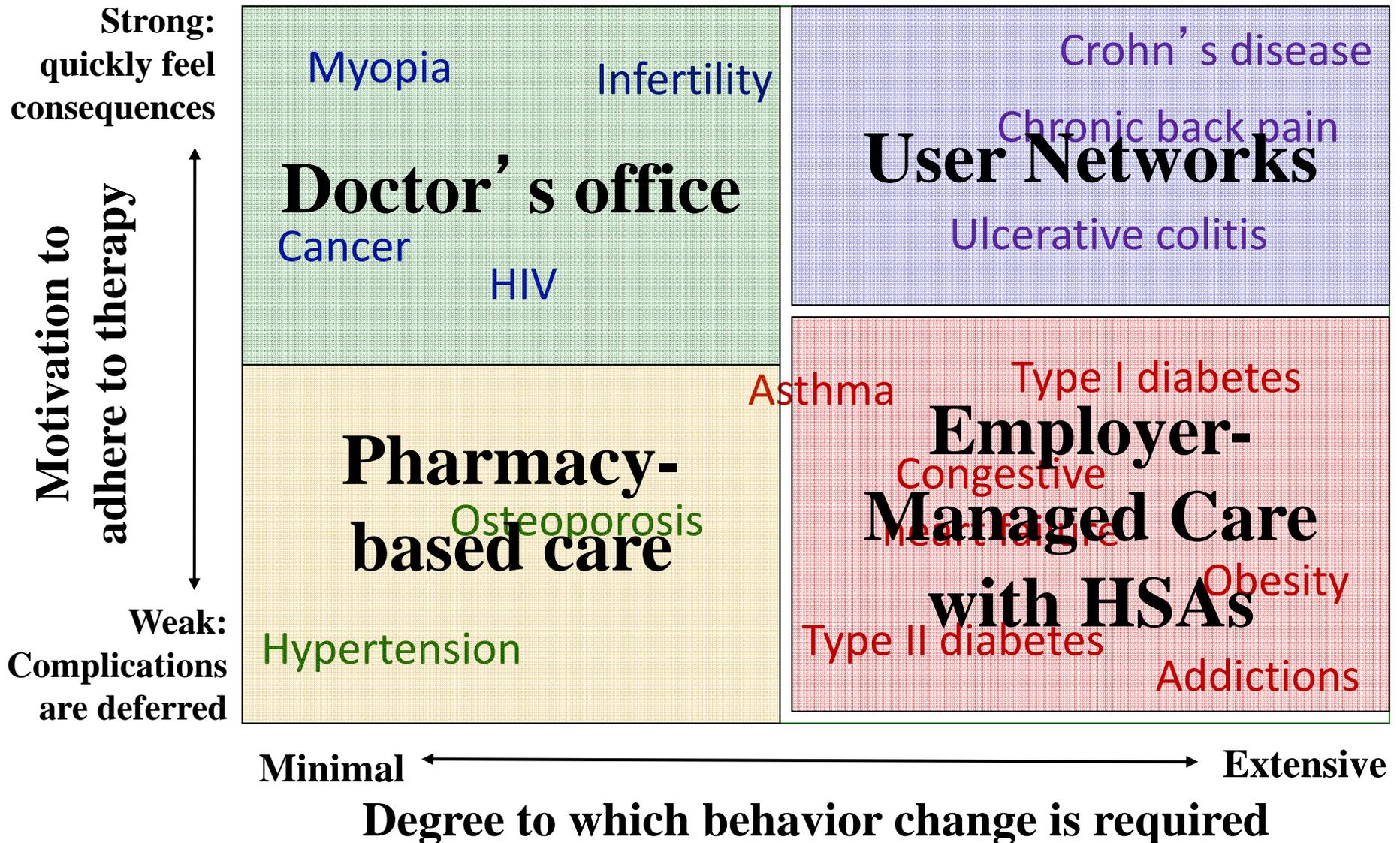
Discovery-driven planning

1. Make Projections
2. What assumptions must prove true for the projections to happen?
3. Implement a plan to learn -
- to test whether the critical assumptions are reasonable
4. Move to the next stage when key assumptions prove valid

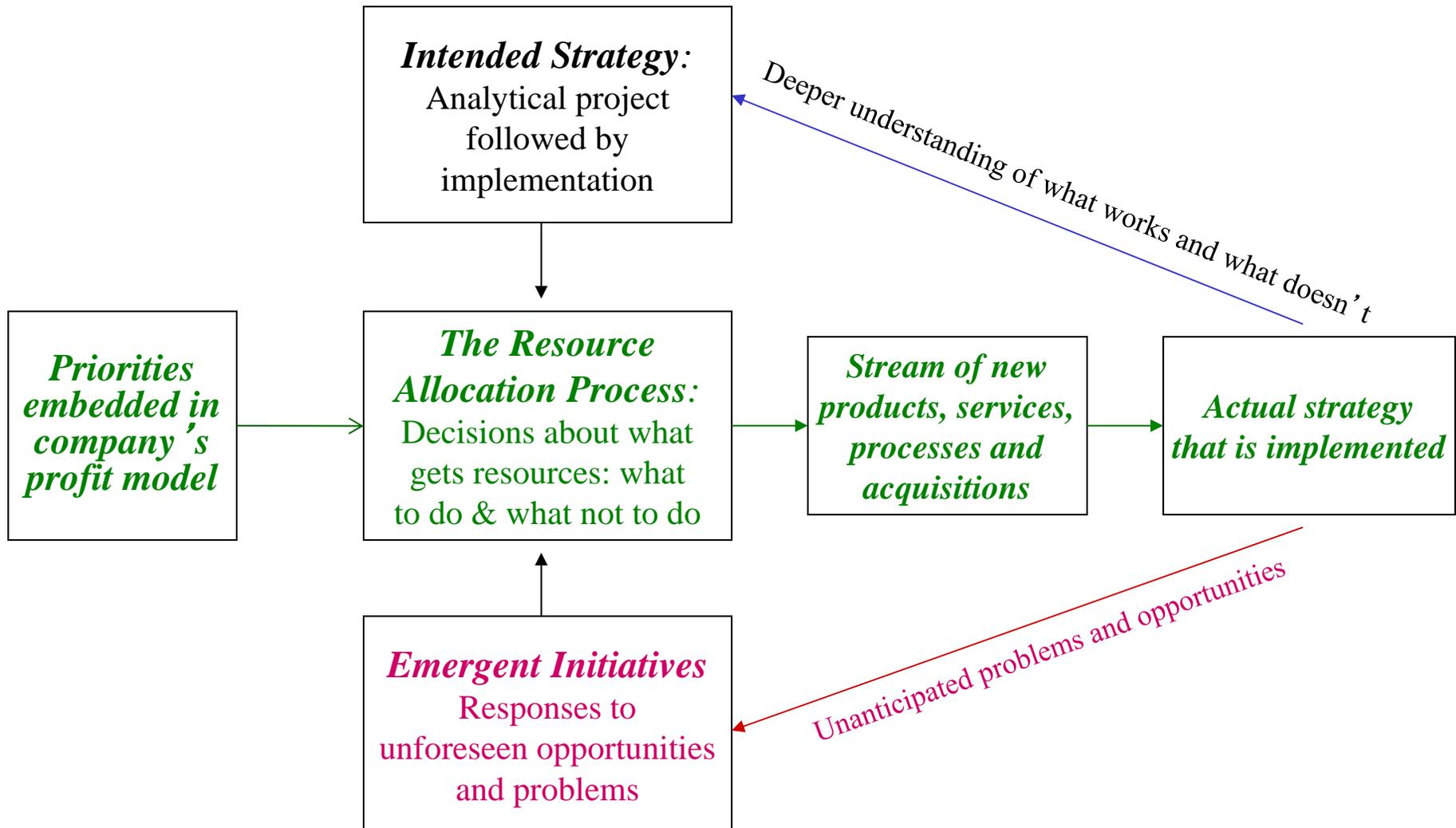
Business models for adherence in chronic care



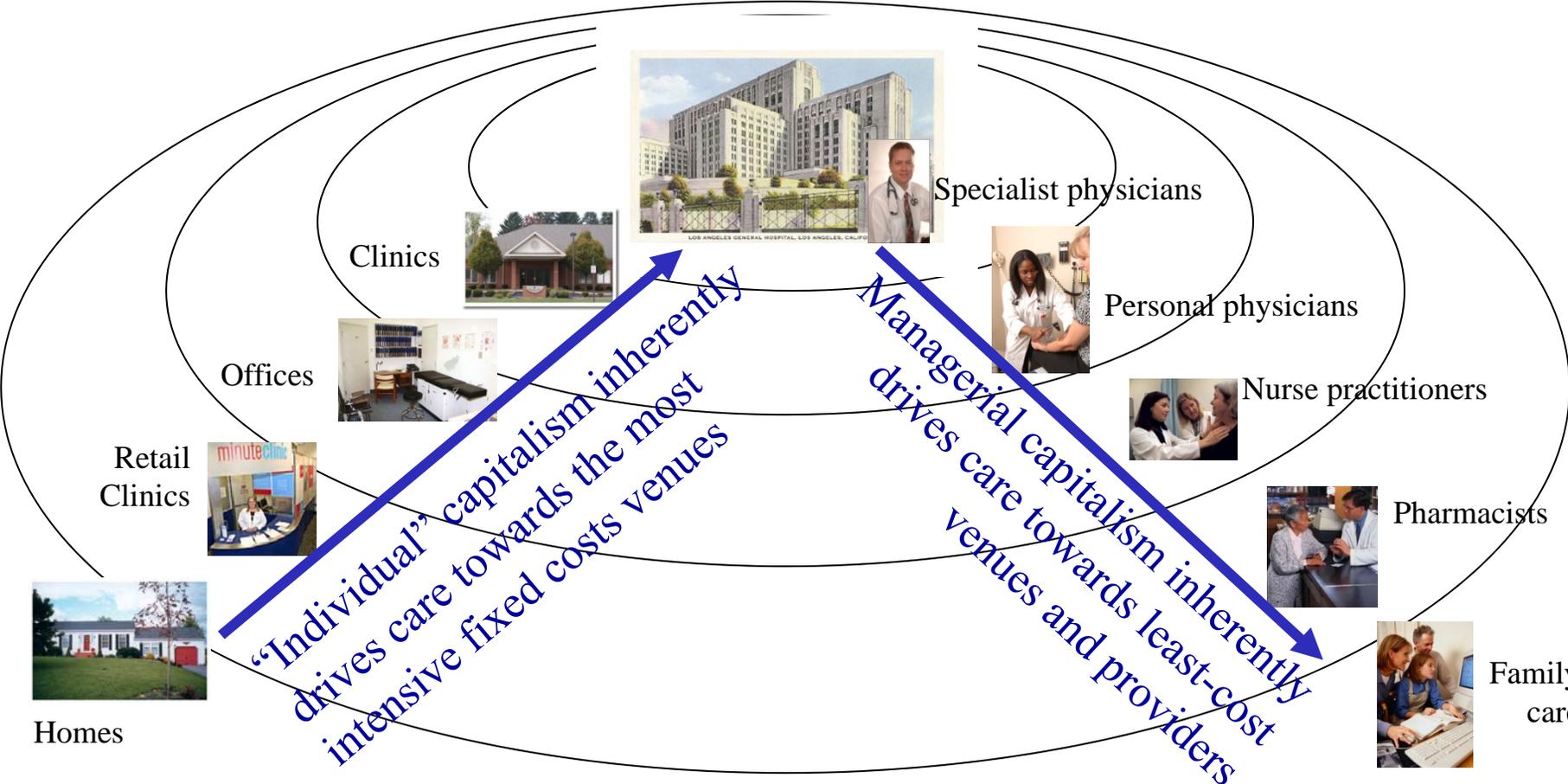
Business models for ongoing care



Processes of Strategy Formulation and Implementation



Most of America has the Titanic. Re-arranging the chairs on its decks will not solve its problems.



Migratory Capital

**Metric of profitability:
% (RONA, EVA)**

**Marginal cost thinking
(Ignore sunk and fixed
costs)**

**Base case of NPV:
continuation**

Useful life

Enterprise Capital

**Metric of profitability:
Money.**

**Henry Ford-thinking: You
pay the full cost anyway,
whether or not you get the
machine (or the business)**

Base case: Deterioration

Competitive life