CRITICAL SURVIVAL SKILLS for the Great Disruption Ahead
Goals For Today

• Better understand the forces of disruptive change
• Understand how this applies to you
• Group discussion
Hey, Tom, I just realized that I don't need to outrun the bear; I only need to outrun you.
Dennis Stearns, CFP®

• Dennis Stearns is a financial planning practitioner and President of Stearns Financial Group, a fee-only financial planning, investment management and business consulting firm with offices in Chapel Hill and Greensboro and clients around the U.S. and overseas.

• The Financial Planning Association has called Dennis “one of the leading scenario experts and futurists in the financial planning industry.”

• Dennis is a TEDx speaker on The Changing Future of Jobs.

• Dennis has many business awards including Most Admired CEO (Triad), Most Influential People (Triad), Triad Entrepreneur of the Year and Chamber Small Business Advocate.

Jed Dunn

• Jed Dunn is a successful entrepreneur and business advisor and partner of Newport Board Group.

• Jed currently serves on the board of Triad Growth Partners, Guerrilla-RF, and is a trustee at Washington & Lee University.

• Jed works with CEO’s and Boards of Directors to accelerate value and create capital readiness.
Are You the Disruptor (Builder) or the Disrupted (Mason)?
Disruptive Threats Are Often Not So Obvious

“This invention called “writing” is dangerous: it removes our mind’s ability to stay well exercised.”

– Socrates

ON THE INVENTION OF THE TELEGRAPH:

“Maine and Texas, it may be, have nothing important to communicate.”

– Henry David Thoreau

ON THE INVENTION OF THE TELEPHONE:

“Would any sensible man transact his affairs by means of such communication?”

– Western Union

“It (the telephone) provides no permanent record of a conversation.”

– Samuel Morse, inventor of the telegraph

Both Western Union and Mr. Morse declined to buy the patent rights for the telephone.

ON THE INVENTION OF THE TYPEWRITER:

“This machine usurps the art of writing with one’s own hand.”

– NY Times
Critical Survival Skills for the Great Disruption Ahead

Four Powerful Converging Super Trends

Globalization

Technology Accelerators

Global Age Wave

Urbanization
The pace of change is increasing at 10 times the speed of the First Industrial Revolution and the power is 300 times, which equals 3000 times the impact of this Techno-Industrial Revolution versus the last one.

– McKinsey and Co. 2015 Report
“They offer compelling thoughts on how we succeed in a world that’s moving faster and faster every day. The massive changes they describe can be overwhelming, but they do a remarkable job of inspiring us to confront them with intellect, humanity, and a profound optimism about our future.”

Eric Schmidt – Google Executive Chairman
How Converging Super Trends Affected 2015-16

1. **Struggling top line company revenue growth** (demographic shifts, technology accelerators, globalization).

2. **Crashing energy prices** (technology accelerators, globalization).

3. **Deflation wrestles Inflation to a draw** (demographic shifts, technology accelerators, globalization).

4. **Unsettling job market shifts** (demographic shifts, technology accelerators, globalization).

5. **China’s sputtering growth** (globalization, urbanization, technology accelerators, demographic shifts).

Critical Survival Skills for the Great Disruption Ahead
• To begin with an obvious threat, BNSF, along with other railroads, is certain to lose significant coal volume over the next decade.

• At some point in the future – though not, in my view, for a long time – GEICO’s premium volume may shrink because of driverless cars. This development could hurt our auto dealerships as well.

• Circulation of our print newspapers will continue to fall, a certainty we allowed for when purchasing them.

• To date, renewables have helped our utility operation but that could change, particularly if storage capabilities for electricity materially improve.

• Online retailing threatens the business model of our retailers and certain of our consumer brands.
Buffett on Super Trend Effects
(from 2015 Berkshire letter to shareholders)

None of these problems, however, is crucial to Berkshire's long-term well-being.

When we took over the company in 1965, its risks could have been encapsulated in a single sentence: “The northern textile business in which all of our capital resides is destined for recurring losses and will eventually disappear.”

That development, however, was no death knell.

We simply adapted.

And we will continue to do so.
Most Businesses Settle into Familiar Trade Routes
Then You Find Yourself in Uncharted Waters...
If an enterprise does not have within itself an ability to adapt to change, it is obvious in a capitalist society that enterprise will fail.

— Chung Ju Yung, Founder, Hyundai
Traditional Defense to Disruption: The “Moat” Around the Castle

1. Deep management strength
2. Barriers to competitors
3. Strong network effect
4. Sustainable cost advantages
5. Intangible assets like patents, licenses or a strong brand
6. High customer switching costs
7. Limited market niche that disincentivizes competitors
## Examples of Economic Moats

<table>
<thead>
<tr>
<th>Width of Moat</th>
<th>Intangible Assets</th>
<th>Cost Advantage</th>
<th>Switching Costs</th>
<th>Network Effect</th>
<th>Efficient Scale</th>
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<tbody>
<tr>
<td>Wide</td>
<td>Pepsi</td>
<td>Walmart</td>
<td>Apple</td>
<td>Visa</td>
<td>Kinder Morgan</td>
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<td></td>
<td>Global brand name that commands a premium for beverages and snacks.</td>
<td>Possesses significant leverage over its suppliers/vendors when it comes to pricing because of its volume of global sales.</td>
<td>Apple &quot;eco-system&quot; comprised of its iOS operating system, iTunes, and iCloud create a captive consumer.</td>
<td>Payment method is accepted by merchants worldwide, which is convenient for cardholders, leading to more transactions.</td>
<td>Building pipelines is capital intensive and involves clearing many regulatory/environmental hurdles.</td>
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<td>Narrow</td>
<td>AbbVie</td>
<td>FedEx</td>
<td>Wells Fargo</td>
<td>United Health</td>
<td>Duke Energy</td>
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<td>Leading drug company. Majority of sales come from one drug, Humira, that will face generic competition later this decade.</td>
<td>One of the leaders in the global parcel shipping industry. Air freight segment is less efficient as a result of lower margins.</td>
<td>Strong financial firm with large, low-cost deposit base. Cross-selling to customers creates multiple product ties to the company.</td>
<td>Large membership base allows for flexibility in plan offerings as well as opportunities to create new products.</td>
<td>Regulated utility with high barriers to entry as a result of infrastructure costs.</td>
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<td>None</td>
<td>Delta</td>
<td>Alcoa</td>
<td>JCPenney</td>
<td>Sprint</td>
<td>Petrobras</td>
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<td>Well-known brand but consumers typically make airline decisions based on cost.</td>
<td>Leading producer of aluminum but lacks pricing power sufficient to produce consistently strong economic profits.</td>
<td>Large retailer competing in highly competitive market with peers including Macy’s and Belk.</td>
<td>Limited pricing power relative to Verizon and AT&amp;T and customer retention has struggled in recent years.</td>
<td>Brazilian government has limited foreign competition in the local oil industry but also placed price controls on Petrobras, limiting profits.</td>
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Source: Morningstar, Stearns Financial Group
BUSINESS OWNER SURVIVAL TACTICS
Right Focus, Right People, Right Execution

RIGHT FOCUS

1. Be clear about where you are headed.

2. Understand the true threats to your business from competitors, the four super trends and multiple sub-trends.
   - Where are you a threat to your competitors?

3. Create “early warning” indicators (M&Ms).

4. Have an action-oriented mindset.

5. Have a bias for innovation.
Right Focus, Right People, Right Execution

RIGHT PEOPLE

1. **Top Grading:** How many of your crew are “A” players and how many are “C” players? **Right seat on the bus?**

2. How would you assess your “idea diversity” inside and outside your company?

3. **Attitude and Training:** An agile crew may be critical to your ship’s ability to reach the New World.
   - Are all the members of your crew **enthusiastic and committed** to your ship’s goals? Do they **know what is expected** of them?

4. **Coming labor shortages:** Be prepared for other ships to poach your crew. [Surveyed your crew recently?]

5. Have you **sharpened your captain skills** lately?
Right Execution

1. How you and your crew manage the many daily challenges of sailing in a competitive world is still important.
   - Do you get real-time feedback from your crew?

2. In an increasingly consumer-driven economy, are you delighting your customers? How do you know?
   - Paradox: Companies that are more customer focused are more susceptible to demand side disruption.

3. What does your ship’s dashboard look like? Does it contain good information and a format to understand how you’re advancing towards your destination?

4. Are you regularly re-balancing resources and competing priorities in your ship?
The Four Villains of Decision Making

- Narrow Framing
- Confirmation Bias
- Short-Term Emotion
- Overconfidence
Two important ingredients:

1. The disruption doesn’t satisfy the needs of the core customer and is embraced by the underserved or unserved, and,

2. The technology then improves and truly disrupts existing products or services.

The uncertainty of whether a product or service will go from Stage 1 to Stage 2 is what makes identifying demand side disruption so difficult.
BUSINESS OWNER SURVIVAL TACTICS

Possible Solutions to Demand Side Disruption

1. **Double down** on existing business.

2. **Acquire possible disruptors.**

3. **Create a separate unit (or consultant)** that can function as a “red team” competitor to the mother ship.
   - Make sure the separate unit is well stocked with good human and capital resources and isn’t prematurely shut down, including when they become too much of a threat to the mother ship.

All of these options are expensive in multiple ways.

Most closely-held businesses don’t have the resources or the interest in creating a demand side “red team.”
Two important ingredients:

1. Continuous ("sustaining") improvement is keeping customers happy, and,
2. At some point, a disrupter leapfrogs and creates a whole new advance that the continuous improvement company hasn’t anticipated.

The solution to supply side disruption is to have a more integrated, agile company that can improve both incrementally AND, occasionally, in leaps and bounds.
Disrupt or be Disrupted
Draconian – outsized consequences for...
Failure to plan/failure to innovate

• EXHIBIT A:
Envelope Crowd Did NOT invent e-mail
Some Evidence and Experience

Didn’t think ahead – no long game – not quad 2
FD and H (nothing fails like success)
Complacent (on to other pursuits)
Innovators dilemma (careful study, TIO)
Think ahead
Bonuses tied to status quo
Yuge forces of change

BOTH change AND pace of change
Context/Domain $F'' = (F')' = F''(x) > 0$
• What this could feel like to the CEO.....
“But we are innovative....”

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<th>Sustaining Innovation</th>
<th>Disruptive Innovation</th>
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<td></td>
<td>Incremental improvement</td>
<td>Very Different</td>
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<td></td>
<td>May be commoditized</td>
<td>Capture emerging market</td>
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<td></td>
<td>Hierarchy and rewards support this</td>
<td>“Management” and existing metrics hinder</td>
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<td></td>
<td>Institutional memory is aligned</td>
<td>Threat to existing value network</td>
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Some Clues

Value Networks

Largest customers

Execution of sustaining innovation vs.

Trial and error of iterative disruptive innovation
BUSINESS OWNER SURVIVAL TACTICS
The Bottom-Line Solutions

1. Table stakes: make sure you have a good ship and crew, well-trained including “A” level proficiency digital sailors.

2. Have some of the crew (or outside consultants) keeping lookout for sea monsters, the disruptive forces that may sink your ship.

3. React slowly – disruption survivors are frequently not market leaders, they are market and trend followers.

4. Try to understand the nature of disruption you’re seeing and then decide how to respond.

5. Avoid the Four Villains of Decision Making while you’re taking measured, but decisive, action.
BUSINESS OWNER SURVIVAL TACTICS

The Bottom-Line Solutions

Appear that the barbarians will be coming over the castle walls in the future?

In this “3000 times the impact” environment, selling the ship and living on dry land free of business disruption is the right solution for 50% or more of closely held businesses.

Old school planning – figure out timing and market your business when you’re a winner and competitors are seeking answers to stagnant revenue growth.
Disruption Pop Quiz #1

Your customers alert you to a new product and service offering from your biggest competitor. They say they find some components innovative and interesting, but it doesn’t really work as well as your product and service package. Do you:
1. Make a mental note and ignore the new offering?
2. Call on all of your top customers and make sure they are still loyal to your offering?
3. Ask one of your senior management team to check it out with customers and suppliers?
4. Immediately begin looking at features to add to your current offering?
5. Form an internal team to evaluate the new offering?
6. Put together an external team to evaluate the new offering?
Equipping for the Change

The Stearns Advantage:

A way of thinking/believing/doing that says a CEO can align forces of change to benefit the company
Disruption Readiness for the CEO

- Right Aim
- Right People
- Right Execution
- 4 M’s at the ready

- Readiness in itself are THE steps for the CEO
QUESTIONS?

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