

Change It Up

By Bill Koehler, CFA

On October 1, General Electric (GE), an original member of the Dow Jones Industrial Average, announced they were “changing it up” in their executive suite. Out was CEO John Flannery. After a rocky 14-month tenure marked by a loss of nearly \$100 billion in company market value, Flannery lost the confidence of the GE board. In was 55-year old Larry Culp, the former CEO of Danaher Corporation which he successfully led from 2000 to 2014. It is Culp and his team who are now charged with resurrecting the formerly iconic company from a nearly 20-year malaise.

Kaizen – Good Change

In a Wall Street Journal profile of Culp’s management philosophy, the word “kaizen” is described as central to his thinking.

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The Journal goes on to say that kaizen is derived from the Japanese words kai, meaning change and

zen, meaning good. Essentially, a kaizen philosophy refers to positive change in the spirit of continuous improvement.

GE’s decision to change out the top spot is simply another example of the rapidity with which companies are willing to “change it up” in today’s business environment. That can mean changing executive leadership, corporate strategy or even branding. Whether this decreased aversion to change is being driven by short-termism, rapid technological change or Schumpeter’s creative destruction theory occurring at an accelerating rate is up for debate.

However, there is no doubt it is occurring. There appears to be less reluctance today to undertake significant changes more quickly, particularly if a business is struggling. As evidence, Equilar Research calculated the median tenure of CEOs at American large-capitalization companies was six years in 2013 compared to 4.8 years today.

In some cases companies are likely making mistakes and, in hindsight, will be deemed as showing a lack of patience. Perhaps the firing of former Ford CEO Mark Fields in 2017, after less than three years, will prove to be one of these cases. In others, the changes will pay off positively in ways that may surpass anyone’s expectations. Microsoft’s Satya Nadella refocusing the company’s business model on the cloud computing market is a successful case in point. His decision to refocus resources on a market that was underexploited has driven the company to record profitability and a tripling of the stock price over the last five years.

Sears: Yesteryear’s Amazon

Beyond a story like GE, any business leader today with a historical perspective cannot escape the reality that a generation ago Sears was the Amazon of its day. In our view, witnessing tremendous disruption such as that and others like it (i.e. Blockbuster and Netflix) injects a greater sense of urgency in managements’ attitudes toward change. We see more companies acting with the same mindset Google’s founders espouse of “not wanting to miss the future.” Certainly, public companies are under a larger microscope and must respond to the drumbeat of quarterly-earnings reporting four times per year. However, private companies must also be willing and able to meet the needs for “changing it up” when necessary to maintain a competitive edge and client



relevance. Is it any wonder that the global business environment has never been more competitive?

Beyond Donuts

Dunkin' Donuts is no more. While they are not taking the donuts out of their stores, they are taking them out of the new corporate name, Dunkin' Brands. Management recently decided new market realities around sugar and diet in an increasingly competitive and health conscious marketplace necessitated a change. While the Donuts moniker has served them well, they want to be recognized as a destination where it is possible to get healthier fare. Additionally, their own data told them more customers simply refer to them as Dunkin' and that coffee was an increasingly profitable product for the company. They decided connecting with their customers only as Dunkin' would also help them better compete in the coffee arena against Starbucks. With added investments in technology, I suspect their willingness to adapt to changing customer tastes and industry trends will be rewarded.

Other Examples

Dunkin' and GE aren't alone. Other examples of adapting abound, not just in the business world. At churches around the country, the time-honored ritual of passing the collection plate is becoming an anachronism. Plate passing is being replaced by apps on smartphones. At the University of Florida, administrators wondered why student attendance at football games has been shrinking in recent years despite having winning teams. They finally asked the students and learned the school was not adapting to a new reality. College students like to use their smartphones at games. They like to share their game experiences digitally through their mobile devices. However, the stadium, the "Swamp" as it is called, did not have sufficient Wi-Fi so they stayed away. They found out the students would rather skip the game than continually lose a Wi-Fi connection for four hours. The school is now working with Verizon and Extreme Networks to invest \$6.3 million in a Wi-Fi upgrade effort for the 2019 season.

Change and Investors

What does this new environment of change mean for investors? In evaluating companies for potential investment, the keys may well require an increased emphasis on companies that are maniacally focused on marketing and

innovation. Management guru Peter Drucker long identified any business enterprise as having two, and only two, basic functions, marketing and innovation. He defined marketing as knowing what the consumer needs and values so deeply that "selling" becomes superfluous. He described innovation as the creation of better and more economical goods and services, as well as processes and procedures. No better Drucker example would seem to exist today than the world's first trillion dollar market-capitalization company, Apple.

The company is increasingly setting its sights on a consumer base needing and valuing

better access to relevant data, particularly in the health care realm. In an evolutionary change, selected Apple watches will now offer the capability to perform FDA approved EKG tests for watch owners.

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As long as American business and other organizations keep striving to "change it up" for the better, our global economy, and particularly the American economy, will likely be a driving force for a long time to come. Profitable investment opportunities should remain plentiful for those willing and able to be skeptical, curious and alert to them.

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