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Introduction [00:00:00] Welcome to Accenture is XaaS a service files the podcast for business leaders helping their companies transform using innovative digital business models. Here, you'll learn from some of the industry's leading movers and shakers, senior executives from companies around the globe who are changing the way the world works and plays by delivering all types of compelling subscription services. Join your host Kevin Dobbs Accenture as XaaS service managing director who brings 20 plus years of experience as an entrepreneur, CEO and senior executive to the table. Kevin has led dozens of as a service business transformation for some of the largest technology and industrial companies globally. Now let's get to today's episode.

Kevin [00:01:04] Thanks for tuning in today to our XaaS Service Files podcast. My name is Kevin Dobbs and I run our as a service practice here at Accenture. And today we're hoping to see if we can decode Wall Street's view of digital transformation. And I'm really excited to have Steve Strongin from Goldman Sachs join us. Steve is a senior adviser at Goldman Sachs. Previously, he was head of Global Investment Research for more than twelve years, where he was a member of the management committee. And before Goldman was the director of monetary policy research at the Federal Reserve Bank of Chicago. Steve, welcome.

Steve [00:01:41] Thank you, Kevin. Pleasure to be here.

Kevin [00:01:45] So the reason I thought it would be great to have you on the show is that you've written a lot about everything as a service and digital transformation and disruption and how they create value in the marketplace. I know today talk about disruption. You've got COVID 19 really wrecking havoc on the economy. And what's happening seems like Wall Street's continuing to do well. But, you know, a lot of businesses are now rethinking what they want to do around, you know, how they build their business going forward. I thought it would be great. I really like your recent piece called The Big Reset, and it'd be great if you could kind of talk about it. You talk about different phases companies are going through is reacting to the COVID 19 pandemic. Would be great to get your thoughts on that.

Steve [00:02:35] Sure, Kevin. You know, whenever you're faced with an emergency, the first phase is simple survival, which I call preservation. This is about marshaling the resources necessary to make it to tomorrow. The second phase, which is mostly where we are today, is consolidation. And that's where you have a chance to observe which strategies are working and which ones aren't, which suppliers were able to supply things which customers are still buying. And that tends to create a sort of self-reinforcing cycle where people tend to focus in on the winners, mostly because they were winners, not because of any particular technical advantage or brilliant insight or deep competitive advantage. But the simple demonstration that they could cope with the emergency.

Kevin [00:03:28] So it's interesting. So, you don't think we're in preservation? You think we're in your consolidation. Second phase, why? Why is that?

Steve [00:03:37] Because we've had enough time to observe companies like Amazon and Zoom and Microsoft, the sort of work from home, shop from home companies demonstrate really good results. We've had lots of time to observe which infrastructure, which transport companies have been able to continue to deliver. We've been able to reengineer parts of

things like the food chain. And so, once you're into the reengineering, the physical processes, you're deep into the consolidation phase.

Kevin [00:04:08] And then there's another phase. What's the other phase?

Steve [00:04:11] Innovation. One of the tricky aspects from a Wall Street standpoint is that consolidation doesn't really discriminate between lucky winners and smart wimps. Right. You could have had the right organizational design for accidental reasons. It may not, it may have been the best for the moment, but not the best going forward. And so that tends to create sort of false signals about competitive advantage. What happens in the innovation phase is that everyone in the system gets to observe the things that worked. But they also get to observe the sort of clunky aspects of the system. I suspect there's not a single person watching listening to this podcast who hasn't spent more time on Zoom and Microsoft Teams and various digital linkages than they ever have in their lives before. And I suspect they have a long list of things they hate about every one of applications.

Kevin [00:05:17] Yes.

Steve [00:05:18] Now, those companies may be the first to fix those problems or it may be a new entrant. But what happens is everyone has a much clearer notion of what works and what doesn't work. And that creates a situation where people get to copy what worked and focus on what didn't work. And it's the people who fix those remaining problems who end up winning in the innovation phase.

Kevin [00:05:44] So when they're retooling their businesses, are you saying companies may be moving from; if I'm manufacturing something, probably I'm not going to move my business and become Teams or Zoom. But is it the companies are building in some of those capabilities into their model? Is that, is when you talk about retooling, is that what you're referring to?

Steve [00:06:09] To a certain extent. My own belief is that, you know, more often than not, that's not about fixing the way you operate. It's about figuring out how to change the way you operate. So that's somebody who has fixed it, can do it for you. You know, you know, if you were running your own payroll system at the beginning of this, the odds are you figured out how to get someone else to run it internationally. You know, if you know Amazon as an example, was very successful in maintaining their cloud and I'm sure we'll talk about why they were able to do that. But a lot more companies and Amazon successfully dealt with the cloud simply by getting on top of Amazon's cloud. So, for most companies, it's not solving the engineering problem. It's about finding a vendor who has solved it.

Kevin [00:07:00] So is it almost, you're trying to figure out what you're really good at, what your core competency is and then maybe outsourcing everything else or finding somebody who can build in. And I know the next topic we'll talk about is this term resiliency into, you know, things like the supply chain.

Steve [00:07:19] Yes. You know, the major business reorganization that's been operating this century, this century and the last has been a greater or greater focus on the things you do well and exiting the things you don't. And a lot of the technical advances we've seen in the digital domain really have allowed companies to do less and yet scale more. You know, when you look at a company like, you know, Netflix is probably a great example in the COVID period, had a massive increase in demand. And really didn't have to do

anything to meet it. Because they were sitting on other people's applications that were already operating a scale well above the size of that Netflix. So, it is a great example of how you can inherit other companies' abilities if you are correctly designed. You know, one of the you know, one always has to be worried about false learning. There are there are a few of the giant tech companies that sometimes appear to have very diffused business models, like they seem to have a finger in everything. If you actually look at them more carefully, which you typically find is they have one or two things they are deeply focused on and a bunch of stuff they wander by when it's convenient. You know, it's like since we since we already brought up Amazon, I'll stay there. Right. Amazon is a completely dominant firm when it comes to things that ship in a cardboard box, that don't require refrigeration and can be carried by one person. If it doesn't fit that description, Amazon doesn't have a particularly large market share.

Kevin [00:09:11] That's interesting.

Steve [00:09:15] Right. And so, you know, we have a tendency to think they've done. You know, if you look at SKUs, they look like the largest retail in the history of mankind.

Kevin [00:09:24] Right. Right.

Steve [00:09:26] On the other hand. Right. If you want fresh produce, they don't deliver it very many places. If you want a piece of furniture, it's a pretty small, whiter. They're not going to deliver, and so forth, and so on, and the complimentary organization. Right. If you think about Wal-Mart, which, you know, 30 years ago we thought of this as a logistics company. Today, a large part of its evolution as a company has been to avoid selling the things that fit into a box that can be shipped overnight in some in some ways, Amazon and Wal-Mart became complements of each other, defined by the effective logistics region of UPS and FedEx. If you saw the same battle going on in China that line is about what you can carry in a bicycle with a cart behind it, as opposed to a truck, it gives you a very different definition of where the back the boundaries are between types of companies. Right. So, all of a sudden, fresh food and restaurant goes in the Ali Baba. But much, but they scale out a much sort of lighter goods that Amazon does. Amazon easily can handle 70, 80 pounds. Not so easy when you're on a bicycle.

Kevin [00:10:48] Yeah, yeah. So, at different supply chains, too. Right. If you're thinking about Wal-Mart, your supply chains delivering to physical stores, whereas Amazon is delivering to the end consumer. So, they design their supply chain to be probably much different than and does that make it more resilient than because they are the least to the people who have been experiencing Amazon during the pandemic, it feels like they haven't had any disruptions. Maybe things have slowed down a little bit, but it didn't seem like there are supply chain broke or had any serious problem.

Steve [00:11:28] Actually both companies were in a position to be pretty resilient for similar reasons, you know, and this goes back to that narrowness of business model that we talked about earlier. So, resiliency basically requires a nodal structure, because what resiliency is about is how you cope with failure. It's not about how efficient you are when everything's working. It's about how efficient you are when six things break.

Kevin [00:11:58] Right.

Steve [00:11:59] Ok. And when you want to design a system to work, when six things break, you have to have lots of sort of a nodal structure where you do the same thing in

multiple places. So, you know, the phrase I sometimes use is local, global company that's local everywhere, meaning that lots of nodes, lots of places, lots of paths, lots of ways of getting to the same result. So, when one breaks down, you can take a different one. You know, the companies that had major problems here were ones that had very long, very skinny supply chains that had been highly optimized for cost but had not been optimized to be able to deal with shocks.

Kevin [00:12:47] Right. And may have been very old, they had been established.

Steve [00:12:52] And some sometimes all, I think more. The problem was just narrow.

Kevin [00:12:57] Yeah.

Steve [00:12:58] You know, I you know, I have a tendency probably because of the things I've done for a living, to sort of do business with some companies just to watch how they work. And one of the things I observed during this period was a number of the sort of mid-sized companies that I use as a vendor. Right, but just because of size had fairly specific supply chains.

Kevin [00:13:24] Yeah.

Steve [00:13:25] And I've been getting very complex letters explaining how this factory in Shanghai, they needed to find a replacement over here in Taiwan and how the people at Taiwan had different bandwidths on their electronics and the people in Shanghai and now that required them to reengineer a process. That's the very definition.

Kevin [00:13:46] You've got some letters? Letters about your supply disruption?

Steve [00:13:50] Well, it shows it shows you the kind of companies I buy from, right?

Kevin [00:13:53] I haven't had that yet, but okay.

Steve [00:13:57] Right. And it's been fascinating to sort of to watch them evolve their notion of supply chain. But they were the very definition of fragility. Right. Where all they needed was one vendor in that chain to go out and the whole chain stopped. Right. And that's the kind of thing where even a very modern company can fall into the trap if they never thought about what happens.

Kevin [00:14:23] So in your other examples like Netflix and Zoom and others, that was a digital supply chain. So, they had a lot less kind of fragility. Much more kind of resiliency. But that's hard for a physical company who's made manufacturing goods and services, right?

Steve [00:14:42] It can be, but it doesn't have to be. If you look at the physical industries that over the years have been hit by supply shocks, the oil industry, petrochemicals being a great example of this in the 1970s. Right. They redesigned to that same global but local everywhere structure. Right. You know whether you're talking about Clorox bleach or you're talking about gasoline. Right. There are probably six, seven vendors within a relatively small radius who can deliver that product because they had supply shocks in the 70s. They redesigned their physical systems around those supply shocks. And so, they were actually pretty deep. And so, no one had any problem getting gasoline during this problem.

Kevin [00:15:29] Right.

Steve [00:15:31] That a lot of people had trouble getting certain types of fresh fruit. Right. Since that narrowness was supply chain really has a tendency to evolve out of over optimization. Then the particular nature of the supply chain itself. It's certainly easier to structure a sort of nodal network in telecommunications or the cloud that it is in manufacturing widgets. But if you look at the widget manufacturers over the years, like petrochemicals that have faced this, they figured out how to do it. You know, and, you know, practically every industry you can name has reorganized itself in ways in the last 30 years that make that easier. You know, outsourcing, which started out very much as a discussion around cost, also forced standardization. And standardization and inherently is about creating a multi-vendor network for competition.

Kevin [00:16:37] And it's funny, Steve, because kind of the way you're describing it in my world, what we call it is sort of like building a platform business. So, you create a platform and then you've got the partner to plug in who have different roles. And you may even have like an ecosystem that of partners who are kind of providing various goods, services, data, you name it. But it's you're providing like that all looks kind of plugged in to and I guess you could use that example for an oil and gas company. Right?

Steve [00:17:13] Right. You know, I use very much the same language in Survivors Guide to Disruption. The distinction, I think, is that a lot of people, when they talk about platforms, always want to be the platform.

Kevin [00:17:28] Right. That's where the control is, right?

Steve [00:17:32] Well, yes and no. Right it's certainly where you get to, like, hold on to the widgets. Right so, if you think of control as the ability to visit the floor. Right, then, being the platform is essential. Right. On the other hand, if you think of being able to choose the supplier is the essential element that actually using the platforms. Right so, there are great examples of both of this in lots of industries. You know, the tech foundries are a great example of a whole bunch of companies producing relatively similar goods. Right, as a group, they represent a highly diverse platform. Maybe you don't really want to be one of them. You'd much prefer to be one of the companies that assembles their own products.

Kevin [00:18:23] Right.

Steve [00:18:24] You know, Apple is a weird company that sort of rotated a few times through how they relate to other companies.

Steve [00:18:34] OK.

Steve [00:18:36] But historically, right, they've been more successful as they've done fewer things in their own manufacturing chain. They controlled more things but do less things, right. And so that notion of control is a slippery one right.

Kevin [00:18:52] Yeah

Steve [00:18:53] You know, you know, you know, and particularly, you know, if you mentioned the Wall Street perspective, the only things require a lot of capital. Buying things does require nearly the capital. So, if you're trying for a return on equity, return on

capital, you'd love for somebody else to own the stuff. You know, the great, the great innovator there, which you normally don't think of as a manufacturer, but very much is, is McDonald's. Right. So, McDonald's took this industry that historically it involved owning a lot of stuff and created the franchise, so it didn't have to own anything.

Kevin [00:19:32] So they are an assembled [unintelligible] to a manufacturer.

Steve [00:19:37] They even managed to get out of the assembly part of it, right. They sort of became a supplier of blueprints and ads, right. Control freaks don't want to suggest they ever gave up the control of anything. Right, and but, you know, they you know, they had regional vendors for the meat, which they specified the fat meat content. They had all this local, very complex real estate transactions moved into the franchisors. Right.

Steve [00:20:05] So they got out of the asset business very much into the intellectual product business, right. I know that Netflix is sort of the modern extreme example of this. Right. It's really hard to name something that Netflix actually does for themselves.

Kevin [00:20:24] Make content.

Steve [00:20:26] They don't make content. They hire people to make content.

Kevin [00:20:29] That's true.

Steve [00:20:30] Right. Right. You know, they don't supply content. They don't talk to their own customers. Right. It's actually a fascinating business model to compare to an online company. Right. You know, they don't really have to know who are their customers? What do they produce? Right. You know, they sit on top of Amazon because they're a competitor.

Kevin [00:20:54] The Wall Street loves them, though.

Steve [00:20:58] Because they don't use any capital. They're incredibly resilient. They were had very little trouble adjusting to the moment. They're very flexible.

Kevin [00:21:07] Yeah. One of the things that I was going to ask you is that you've used a number of examples. And our world is sort of the recurring revenue is also important. It's having kind of a model, because we find that kind of a recurring revenue model tends to be more resilient in that you start the beginning of your year and 80 percent of your revenue is booked already as long as you're taking care of your customers and they're not churning that, that seems to be a great model. And Wall Street seems to like that.

Steve [00:21:35] Oh, yeah. I mean, you know, I spent 25 years of my life in the trenches in Wall Street and you know, people have a tendency to think of Wall Street as this highly complex organization, right, that does many things. That's true, but the people who are trying to decide whether to buy a company typically is this poor individual sitting in a cubicle with a P.C. and a spreadsheet trying to guess what that company is going to do this quarter, next quarter or the quarter after that. Right, and the more confidence they have in those numbers, the more they want to buy the company relative to the product. Right.

Kevin [00:22:17] So recurring revenue would help.

Steve [00:22:19] Recurring revenue helps. Easy to explain. Easy to model. Right.

Steve [00:22:24] The easier it is to put in a spreadsheet, the easier it is to get paid for it. You know, there's a there's a major exception to that. That makes the debate very confusing. Which is right, companies get paid for two things. They can get paid for predictability or they can get paid for hope. OK, and there's a whole bunch of companies out there, where the market isn't paying for the recurring revenue. It's paying for the hope. The belief. Right, the entire biotech industry fits this mold. Right. Certain parts of software fit this mold. And then every once in a while, you have some really strange company, like a car company that somehow manages to sell hope to.

Kevin [00:23:17] And is really good at it.

Steve [00:23:19] That's right. Other companies want to know how do I get paid? You know, I've got hope too, I've got product designs. I want to get paid. But there's a real there's a deep paradox and getting paid for hope, which is the market wants high volatility. It's an option. They want low capitalization. And they and this is the part that's most paradoxical to a standard sort of business executive. They wanted to be flimsy.

Kevin [00:23:49] And what do you mean by that? What's flimsy mean?

Steve [00:23:52] Right. So, if you let let's take a simple call option. Right. Pure math of this. Right. The option value is maximized when the intrinsic value is minimized. Right. And the volatility is increased. And so, you have these tiny little biotech companies that have no product, no sales. Right. That are hoping to do a human test someday. Right. They're essentially the infinite multiple. Right. Right, we're a company with real assets and real skills. Right, and real customers. We'll never get near that multiple. Right, and very often. Right. They own a few of those options, too and they're trying to figure out why they don't get paid as much for those options as that little biotech does. And the answer, right, and this goes to the notion of flimsy is because their deep pockets allow them to keep throwing good money after bad at projects that don't work. Right, which you why an options portfolio is a lot of lottery tickets that go away when they don't work.

Kevin [00:25:01] Yeah.

Steve [00:25:02] Right. You know, when you have the CEO of a real company talking about how committed they are to, you know, a Mars landing or reinventing technology or pick the dream. Right, the investor thinks, my God, the amount of money they can waste. Right, and the more they sell the dream, the more money Wall Street sees being wasted. And so, again, you can either be predictable or you can be hope. You got to model yourself to what you are. And you can't be both at the same time.

Kevin [00:25:33] And this will be something in our next segment. We'll talk a little bit more about the hope. Hope projects. But then one last thing I wanted to kind of touch on, too, about kind of what's happening in the market and maybe opportunities for companies is what you kind of call sticky learning is where all of a sudden we're learning things that we didn't know we could do at mass scale. And, you know, I'd be interested do you think that that provides companies a lot of opportunity, too? Because one of the things we've seen at Accenture, you've got five hundred thousand employees. Everybody's at home, for the most part, working would have thought that that could have ever happened. But it's a lot of other examples of that. Well, I think you'd pocket.

Steve [00:26:19] Yes, I think sticky learning is going to be the most transformative of all aspects of COVID. I think, you know, a year from now we'll probably have, you know, three or four therapeutics, we'll have five or six vaccines and so, all of the risk discussions will have sort of receded and life will be sort of normal. On the other hand, we'll all of learn many things and changed many things we never would have dreamed of doing. You mentioned work from home. I can remember sitting through management meetings where we discussed, and we plan to do experiments where five percent or maybe we'd stretch to 10 percent of people would work from home. Right, would this help with diversity, would it help with gender, a whole variety of things. You know, I don't know what Accenture number is, but Goldman hit ninety eight percent.

Kevin [00:27:16] Yeah. We're close.

Steve [00:27:20] You never would have agreed to run that experiment, right? Now, it didn't all work. Right. You know, you discovered that senior people could do lots of things from home. Certain departments, legal as an example, right, really don't need to be there every day and maybe even can have higher productivity, not in the office. On the other hand, if you're trying to cultrate, a new analysts, new traders.

Steve [00:27:50] There's a lot of informal communication that goes into that process of culture, of method, of learning that you really can't do virtually. So, everyone's got a much clearer notion of what can and can't be done. You know, telemedicine, we've been talking about telemedicine for as long as we've had cell phones, right. We've now done a lot of it, and we've discovered that some stuff works, and some stuff doesn't. There's another aspect of this, though, that I think is going to be even more important. And that has to do with a word that used to go all through almost every tech and every digital strategy, which was early adopter.

Kevin [00:28:31] Oh, yeah.

Steve [00:28:32] Right. So, a lot of absurd amount of research and development was aimed at early adopters. Why? Because if they didn't use it, you were never going to have an audience.

Kevin [00:28:43] Right. Won't scale.

Steve [00:28:45] That's right. Right now, we've essentially trained an entire generation of much better customer, more money, more loyalty, more stability, right. To use digital platform. They're now going to be the natural target of that R&D dollars. You know, I was talking to a bank president and, you know, three weeks before COVID, he had a normal adoption curve. That his less important younger clients were 80 percent digital and his more important, much richer, older clients were 10, 20 percent digital.

Kevin [00:29:22] Right.

Steve [00:29:23] By the fourth week of COVID, it was 90 on both sides.

Kevin [00:29:28] Yeah. They had no choice.

Steve [00:29:31] That's right. Right. But on the other hand, having learned how to do it right, they don't really want to go back. Those older customers don't want to go back into those branches, because it turns out digital is actually easier for most things, right. And so

that that that client is a much better client, now is much more scalable source of potential revenue and so, the fight for the older digital customer is about to get really intense, where before COVID that probably was, you were probably going to wait a generation for that. Right. And so, a lot of businesses that generally were still bricks and mortar businesses because they were primarily aimed at older customers are now going have to completely reassess that. And there's also a chance, and I think a pretty big chance that skill with early adopters is going to turn into a disadvantage and a lot of digital businesses, cause they were never very good customers, they were always really strange. I happen to be one. Doesn't change the fact they're strange customers. Like I said, I get up. I use vendors that send me letters about their supply chains. I'm not the customer you want to have. Right. You know, you want a customer who's going to continue to work, you know, who's going to continue to buy, not think too much about the margin and not think too much about that process. And that's a different kind of development, right? It's about getting Zoom to have a better mute button. It's not about getting backgrounds that have fireworks, right. Think about what Instagram did to get share, right, versus what if you want a sixty-year-old to show up what you're going to have to do, right? Right. You know, there are I'm sixty-two. There is not a 60 to 62-year-old in the world whose primary desire is that higher resolution cameras under Zoom.

Steve [00:31:28] Right. It's a different development prospects here. That's right.

Kevin [00:31:33] Yeah, I know. I know. For my mother, who's 80. If I, if it was just a big button that she could just push to make it go on and off would be fantastic. So maybe that's where the R&D dollars will go.

Steve [00:31:46] I think it very much is. It's going to be ease of use for better customers who've now learned how to be digital in a way that we probably would about a wait 20 years for without COVID.

Kevin [00:31:57] This has been great. Obviously, a lot of insights there in a short amount of time. But really appreciate you talking to us today and look forward to continuing the dialog.

Steve [00:32:08] It's a pleasure.

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