The Firm of the Future

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The three great challenges facing business today are to create a commercial culture in which capital is more patient, work is more variegated and entrepreneurship is more mainstream

Anyone listening in on the conversations of executives over the last 10 to 20 years cannot help but have noticed that managerialism – the art of getting things done by and through other people – is the main source of frustration, disengagement and underperformance within most organisations. As a 19th century social technology for controlling and coordinating large numbers of relatively unskilled people, managerialism is delivering ever-declining value. We are trying to create wealth in a knowledge economy by relying upon structures and processes designed for the industrial age.

The language of planning and control, of targets and KPIs, of metrics and benchmarks, of efficiency and excellence, of specialisation and standardisation, of jobs and careers betrays a way of thinking that is wholly unsuited to the challenges confronting firms today.

The agenda has moved on. More management is not the answer. Tweaking the managerial model by opting for out-sourcing, de-leveraging, re-engineering, dis-intermediating, off-shoring, and other such administrative processes beloved of consultants, is a classic case of "doorknob polishing" when the stately home has long since fallen into disrepair.

The problems facing business have much less to do with <u>internal</u> systems and processes and much more to do with <u>external</u> or <u>contextual</u> variables, such as the institutions and structures within which companies are expected to perform. The five-day work week, the employment contract, the job description, the office hours mentality, the working time directive, the lifetime career, the long hours culture, the limited liability company, the quarterly reporting cycle, the acquis communitaire, and the regulatory mindset are just a few of the situational factors that contribute to a culture of indecisive management, compliant employees and passive shareholders.

For some time we have been witnessing diminishing returns to management. We need to pioneer alternative organisational models that have the potential to motivate and inspire those coming into the workforce, as well as re-energising those already within it. To borrow a telling phrase from Charles Handy's most recent book, we need to invent a "second curve" – a new way of working – if we are to attract millennial talent into the world of business and put it to work on behalf of a better world

Three deep-seated structures – or pathologies – are particularly responsible for holding back economic growth in today's world:

1. **The 5-Day Workweek**: we spend too many hours in the constrictive environment of the office and too little "out and about". Our working week is typically too monotonous, too uniform and too "full-on" to lend itself to creativity. What has been called "hurry sickness" is crowding out time better spent on inquiry, reflection, natural conversation and "downtime" generally.

2. **The 5-Week Shareholding**: perhaps this should read the "5-Second Shareholding". It has become a cliché – but none the less true for that – that capital markets are insufficiently patient to serve one of their main purposes, which is to match lenders with borrowers and, in doing so, help direct savings into their most productive uses (even though, shockingly, only about 3% of the assets of British banks are today devoted to this purpose). Short-termism is a rational response to the irrational state of affairs in which the business model that drives the decisions of asset managers conflicts with the interests of the investees, namely, companies and those whose money is invested in them.

3. **The 5-Decade Career**: the problem, as Charles Handy said many years ago, is not just unemployment, but also employment. As a legal structure and behavioural context in which individuals may be planning to build their working life in the 21st century, it is too closed, too restrictive and insufficiently developmental to meet their variegated needs.

Increasingly the role of senior management will be to redesign the organizational context in which work is done, rather than to supervise the content of the work itself. Ideally, there will develop a competitive market in employment practices and ownership rights – where, for example, different firms will experiment differently with the length and composition of the workweek, the incentives attaching to different classes of shares, and the opportunities for employees to become entrepreneurs in mid-career.

The 4-Day Workweek

"Remember, you only have 2,000 weekends, and then you die"
Ryan Carson, CEO of Treehouse, a company that treats Fridays as part of the weekend

John Maynard Keynes predicted that, by 2030, there would be a 15-hour workweek. Yet the statistics suggest that, if anything, people are working longer hours now than they did in the 1930s. This is a paradox. Presumably, Keynes' logic was that, as the wealth of the world increased, so the marginal utility of income would fall relative to the marginal utility of leisure, placing pressure on governments to encourage more flexible employment contracts and offering opportunities for firms to compete on the basis of hours worked. Yet the reverse would seem to have occurred. The wealthier we get, the harder we work, the longer we stay in the office, and the later we retire, if ever.

The working week needs a radical re-think. Just as the notion of a career – that is, working (often for the same employer) for 45 hours a week for 45 weeks a year for 45 years – was radically challenged by Charles Handy in the 1980s when he wrote about "portfolio working", so it is time to re-appraise and overhaul the unduly rigid notion of the 5-Day workweek.

The gig economy, the pop-up shop, the farmer's market, the boot sale, the innovation hub, the zero-hours contract and so on are all symptoms of the fact that work needs to break out of its straitjacket and try on different apparel. Ironically, zero-hours contracts have come in for a terrible pasting by the media and yet 80% of those on such contracts are delighted with them, such is the freedom and flexibility that they afford. Instead, the real problem is the formulaic nature of the everyday employment contract. We talk a lot about corporate agility and the merits of anti-fragility, yet we persevere with one of the most embedded and inflexible institutions in modern society.

In their genealogical explanation of civilization, Acemoglu and Robinson draw a distinction between <u>inclusive</u> institutions, such as those that "enforce property rights, create a level playing field, and encourage investments in new technologies and skills" and which "distribute political power widely in a pluralistic manner" with <u>extractive</u> institutions, such as those that "concentrate power in the hands of the few" or "are structured to extract resources from the many by the few". Today's workplace, with its rigid structures, burdensome rules, and mood of distrust is in danger of becoming the 21st century equivalent of the kind of extractive institutions that Acemoglu and Robinson believe to have been antithetical to human progress.

So why not move to a 4-day workweek? Why not "Thank God it's Thursday"?

Dan Hamermesh, an economist at the University of Texas at Austin, makes a fair point when he says that, "It's very easy for folks sitting back in their chairs to say, 'Yes, you need to be on a part-time schedule, or a four-day, 32-hour schedule', without thinking about the extent to which such folks want the income and are willing to put up with the hard hours". In other words, there's always going to be a tradeoff between hours worked and income earned. If everyone worked fewer hours, then surely the economy would shrink, and salaries and wages would suffer.

Yet this same argument must have been used 100 years ago when a New England mill, to the delight of the labour movement but perhaps to the consternation of the entrepreneurial class, became the first American factory to treat <u>Saturdays</u> as off-limits to employers.

There are two linked assumptions made by those defending the "long-hours culture": first, that there is a positive correlation between the length of the workweek and the productivity of the workforce; and second, that, given this fact, very few people would prefer to take a pay cut in exchange for a longer weekend.

However, there is some evidence that this may not be the case, for four principal reasons:

First, fewer hours to perform a task means less time to waste:
As Ryan Carson, Founder of Treehouse, an online education company, observes, "You get all Friday off, instead of pretending like you're working when you're not". The more hours that are made available for a job to be done, the more the job-holder will find ways to distract himself if only to break the monotony. This is an echo of Parkinson's Law: *work expands to fill the time available*. Twice the hours doesn't mean twice the effort or twice the output. Particularly in the case of knowledge workers or creative tasks, forcing longer hours is invariably counter-productive. To invert Parkinson's Law, perhaps work <u>contracts</u> to fit the time allotted, or, put another way, time <u>quickens</u> to achieve the task to be done.

The workaholic is a menace in the office. It is said that Field Marshall von Moltke sought out <u>intelligent and lazy</u> officers to be his Commanders because they placed particular emphasis on finding the easiest way of achieving a task; whereas he was notoriously averse to <u>stupid and energetic</u> officers because they made so many things happen but almost all of them wrong-headed. Many of us will immediately recognize this type of manager: he is the one who is endlessly setting targets, measuring effort, cutting costs, re-engineering processes, judging others – and working long hours.

Second, longer weekends refresh and stimulate the creative mind:
Creative problem-solving, innovation and critical thinking are more likely to thrive under conditions of trust and patience than supervision and urgency. Quality work happens best when uninterrupted. Guy Claxton has demonstrated that the creative mind works at a slower pace than the mind engaged on routine tasks. Jason Fried, the founder of Basecamp, a software company whose employees take Fridays off in the summer, discovered that "Better work gets done in four days than in five".

Third, more free time makes for a happier work environment:
Those countries that work shorter hours tend to be happier and more convivial than others, with no apparent loss of prosperity. An OECD report in 2013 found that, amongst full-time salaried workers, the Netherlands enjoys the shortest workweek in the developed world, at an average of 29 hours per week, followed by Denmark (33), Norway (33), Switzerland (35) and Sweden (36). Is it any coincidence that these same 5 countries, according to the World Happiness Report of 2013, were also the 5 happiest? The same report provided evidence that happiness is positively correlated with productivity, health and longevity.

When Kelly Holmes was rounding the final bend in the Athens Olympics' 800m final, for which she won the gold medal, Michael Johnson, the American sprinter who was commentating on the race for the BBC, remarked that, whereas every other athlete was <u>racing</u>, Kelly was <u>running</u>. What a wonderful insight. And what light it throws on today's workplace, which incentivizes racing rather than running. Julie Burchill, the writer and journalist, recently remarked that, "Most of us would do our jobs better if we did them less".

Fourth, a four-day workweek has formidable power to attract and retain talent:
Adding an extra day of freedom to each week is a magnet for talent. Any mention of a shorter workweek, even when this entails a cut in take-home pay, usually excites even the most industrious and sober of managers, professionals and working people. The millennial generation, in particular, is likely to price its freedom at a higher rate than earlier generations.

Patient Capital

"There is something unreal about the way in which finance has evolved, dematerialized and detached itself from ordinary business and everyday life"
John Kay

The extraordinary growth of the finance sector since deregulation – what John Kay has called the "financialisation" of the modern economy – has contributed remarkably little to the creation of new wealth; rather, it has discovered ingenious ways of expropriating the wealth created elsewhere in the economy and rewarded itself handsomely for doing so.

Once upon a time, or so our memory tells us, the investment landscape was peopled by a rather small number of prominent fund managers looking after a rather selective share portfolio on behalf of a rather larger number of influential private investors. The investment chain was much shorter. The fetish for index-tracking or index-hugging had not yet been adopted and the fashion for hedge funds making ultra high-frequency trades had not yet been invented.

Most observers of the world of business and finance – and indeed many who earn their living in this world – have long had concerns about short-term decision-making – and the perverse incentives that seem to reward this behaviour. Particularly since the crash of 2008, there have been innumerable recommendations for how to reverse the seemingly remorseless move away from long-term considerations in equity markets.

The response by US authorities to the 2008 crash was to invent ever more voluminous and intricate regulations, such as Dodd-Frank. John Kay believes that this is precisely the wrong response. "There has not been too little regulation, but far too much … we should put an end to the seemingly endless proliferation of complex rule books."

Nor can we count on virtue. In the last few years, we have learned that any change in behaviour that relies upon good faith, noble declarations, "social responsibility", value statements, well-meaning compacts and commitments, what Private Eye used to call "Solomon Binding", is likely to fall foul of the epithet that "the road to hell is paved with good intentions." Something much tougher is needed.

In Britain, the emphasis has been squarely on the reversal of financialisation. The Kay Report made four significant recommendations: release companies from the obligation to report their quarterly financial performance; replace this custom with a "stewardship code" and make asset managers who are responsible for other people's money personally (not corporately) subject to civil and criminal penalties; ban all short-term cash bonuses to executives; and encourage greater communication between shareholders and companies. On all these fronts, progress is being made.

However, there is one area where the pace of change needs to quicken.

It starts with the distinction between "investors" and "traders" – between those who buy shares on the basis of their understanding of the fundamental value of the company and those who buy on the basis of their expectations of short-term fluctuations in the share price. This distinction is not always clean-cut if only because some trading is necessary if liquidity is to be made available to investors. But the argument remains: the sheer volume of trading that we witness in today's capital markets is far in excess of this requirement.

A dramatic change in the incentive environment is needed if short-termism is to be reversed. How about firms offering different classes of shares with different degrees of power, such that voting rights are related not to <u>how many</u> shares you own but to <u>how long</u> you have held them? When buying the "more powerful" class of shares, for example, shareholders would register the length of the time they intend to hold them: the longer the time, the greater the number of votes. If the shares were later sold "prematurely", then there would be a financial penalty. One of the beneficial outcomes of such an arrangement would be that decisions about acquisitions and mergers – which are currently a major source of short-term bias – would be mainly in the hands of the more committed shareholders.

The limited liability company was originally a noble idea designed to give protection to shareholders who, as residual claimants, were more vulnerable to the failure of the firm than other stakeholders, such as creditors, employees and customers, whose claims were contractually prioritized. The balance has now swung decisively the other way. Such is the pressure on Boards of Directors to maximise shareholder value that other stakeholders, particularly future shareholders, are losing out. Colin Mayer has argued convincingly that, as a result, companies are seriously failing society by engaging in unjust forms of inter-generational wealth transfer.

The Post-Employment Enterprise

"Smart young things joining the workforce soon discover that, although they have been selected for their intelligence, they are not expected to use it"
André Spicer

In 30 years time, we will look back on employment habits and customs as the last vestige of a kind of feudalism in the workplace. This is not to suggest that today's employees can be compared to serfs but simply to bemoan the cynical and dispiriting assumptions about human nature that underpin so many workplace practices.

No one who expects to live to 100 – as do most of those coming into the workforce – is going to put their faith in a 70-year career, let alone a single employer. Those who are imaginative, energetic, optimistic, or adventurous will want to create for themselves some form of independence and self-responsibility by the age of 45. (Indeed, firms such as Uber and Airbnb, are capitalizing on this very trend.) But understandably most young recruits into business will still expect – *and need* – an "apprenticeship" in business acumen before they go it alone and found their own start-up. The firm's role will be to act as a kind of incubator in which employees in their 20s and 30s acquire the skills and confidence to design successful new ventures

It will be a rare employee who wishes to remain within the firm after, say, the age of 50. A society of free citizens will gradually come to be interpreted as a network of entrepreneurs, co-owning with friends and colleagues their own businesses and taking responsibility for <u>creating</u> jobs for those younger than themselves rather than occupying them. Firms will increasingly treat their employees less as loyal citizens over the course of their career and more as potential entrepreneurs whose businesses they help nurture and in which they invest capital.

All employees will, effectively, have two jobs: the "day job" delivering value to the core business and the "development job" preparing to launch their own new venture. These activities will be intimately linked. The day job will offer the experience from which the employee learns about business: how customers are won, how leadership works, how humans are motivated, and how wealth is created. The development job will translate these emerging skills into nascent businesses.

Let us illustrate the argument with some numbers. A firm of 10,000 employees will typically contain 2,000 in their 40s, an age that is ripe for the adventure of entrepreneurial innovation. Let's say that half of them – or 1,000 – are up for this. And let's also assume they have come together in teams averaging 5 members around a strong idea for a start-up. So the firm has the opportunity to invest in 200 new businesses every decade. Let's say half of them survive and grow. In other words, every year the firm is investing in 10 spun-off organisations, each led by 5 of its former employees.

My prediction would be that within 10 years the aggregate market value of these new ventures would be greater than that of the parent company that spun them off. This is the reward for moving the company from being a place to build a career to becoming a place to invent a business. We could name this new form of company "a venturesome enterprise".

The evidence for the viability of this model is growing all the time. It is well documented, for example, that the new ventures founded by Hewlett-Packard "alumni" since 1990 are now more valuable than Hewlett-Packard itself. The tragedy for HP, of course, is that it didn't foresee this turn of events and therefore didn't invest in these businesses.

Why do so many people need to be employed? Why do so few want to do the employing? We educate the young principally to find employment. Very few schools and very few teachers see the purpose of education as <u>creating</u> jobs rather than simply filling them. We look to others to provide work for us. We should not be surprised if there are people eager to fulfill this role, but we should be wary of becoming the followers of those who aspire to lead.

This is the real inequality in society: the disparity between those exercising power and those submitting to it. Disparities of wealth are innocuous by comparison with disparities of power and influence. Yet most of us aid and abet these disparities by choosing employment over self-employment. The economic health and vitality of a society can be measured by the proportion of people who resist the lure of employment and choose instead to manage their own working lives. To be employed at a young age is fine so long as its purpose is to grow out of the need for it. Rather in the way that parents bring up their children to grow out of childhood and to become adults, so employment should develop young adults to move beyond dependency into self-reliance.

Concluding Remarks

"Stop the world, I want to get off"

The conditions that Daniel Berlyne, the cognitive psychologist, discovered to be the ones most conductive to creativity are what called the "collative variables", such as uncertainty, novelty, surprise, complexity, incongruity and absurdity. The oft-repeated platitude that "business hates uncertainty" is not only a serious misconception of the role of business but also a slur on business and on the creativity of business people. Good businesses thrive on unpredictability. Indeed, markets reward those firms that detect opportunities in ambiguity and complexity that other, less creative firms don't. If the future were predictable, entrepreneurs would not exist.

Consider the following analogy: just as it makes no sense to say that you are "in heavy traffic" when the reality is that you are yourself the traffic about which you are complaining, so it is equally nonsensical to describe business as having to accommodate – or respond to – "a VUCA world", as though volatility, uncertainty, complexity and ambiguity were an unwelcome visitation rather than the natural and perennial ambience of business activity itself.

Volatility is what business is about. Indeed, most of the VUCA we experience in the world is the direct and intended <u>product</u> of business, particularly the globalization of the world for which business bears the primary responsibility. Trade has always had the effect of unsettling societies and disturbing the habits to which they have become accustomed. Business is intrinsically restless. Arguably, it has been the greatest disturbance factor in history. Hayek believed that the first moneylender was unknowingly the inventor of the modern world.

Gifted businessmen like nothing more than the uncertainty out of which innovative strategies are crafted. Most competitive advantages, most entrepreneurial breakthroughs and most sources of wealth creation arise from different interpretations by different people of the same data. The market itself is a filtering device for removing businesses that are fearful of the VUCA world or do not have the wit and energy to discover in the chaos the opportunities for disruptive innovation.

In this paper, I have put forward the argument that, with three relatively small contextual changes, businesses themselves could amplify and exploit the VUCA world in which they compete and thereby disproportionately enhance their opportunities for wealth creation. The firm of the future will be the one with the courage to do so.

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