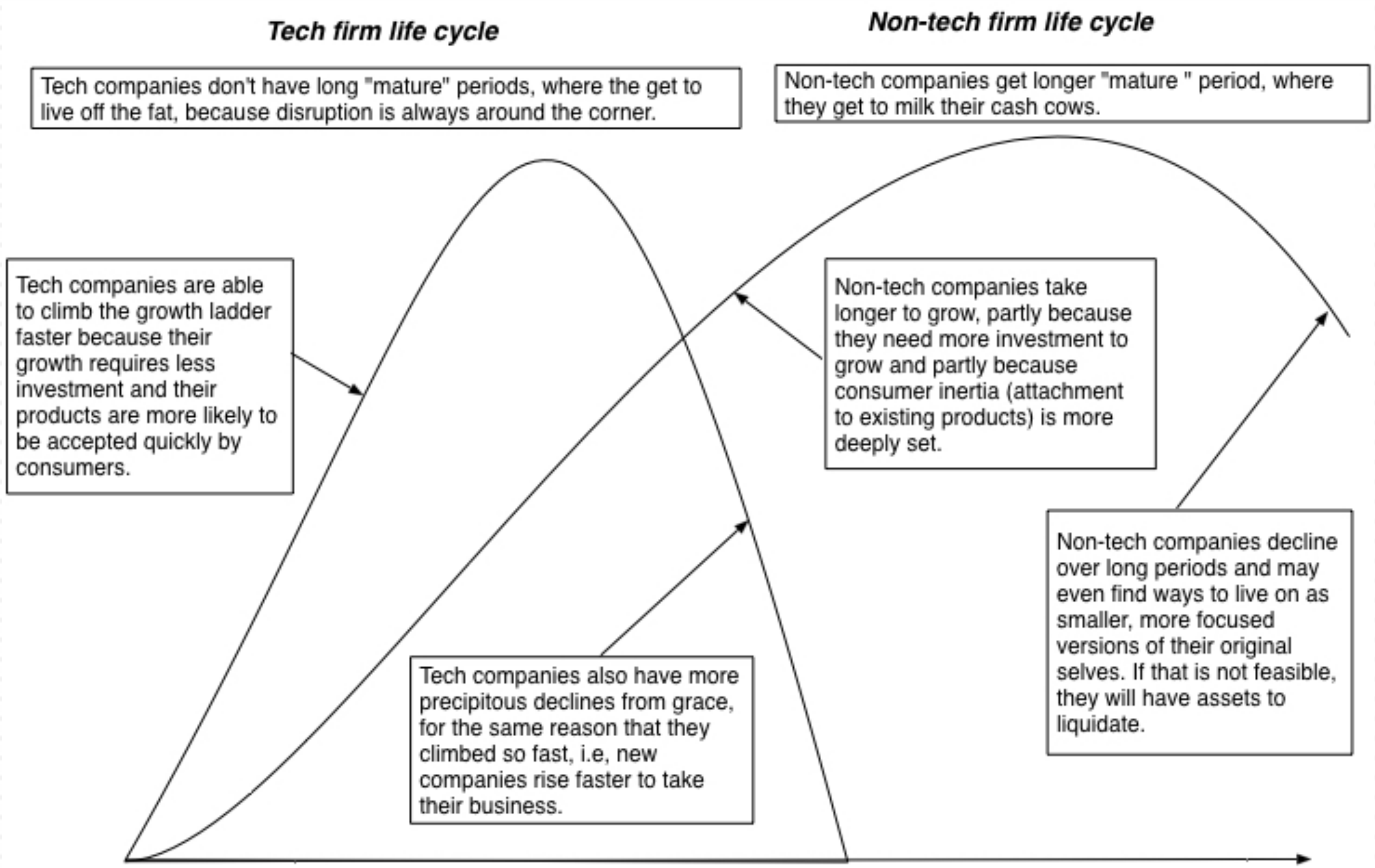
THE TECH COMPANY LIFE CYCLE: THE MANAGEMENT CHALLENGE

Of moats, drawbridges & barbarians

The tech life cycle



The Managerial Challenge: Plausible response

1. Accept a short life cycle and manage the business accordingly.
2. Work at creating a portfolio of tech products that reseeds itself and keeps life cycle going.
3. Change the business

1. Acceptance

- During your ascendance, its all about growth: Keep your focus on delivering that growth and don’t get distracted by control issues or debt.
- When mature, use debt with restraint and keep it short term: You are exposed to far more danger from debt, since your mature phases may last a few years rather than decades.
- In decline, return cash with a vengeance: Your cash returns, whether in the form of dividends or stock buybacks, should reflect the speed of your decline.

2. Reseed and Regrow

- On the presumption that it is tech products that have a short life cycle, not tech companies, you try to reseed the growth machine by coming up with new products, using your old product's payoffs.
- While alluring, there are two potential pitfalls:
  - Payoff from strategy will depend on whether what you pay to get new products (R&D, acquisition) exceeds what you get from extending life.
  - The more successful you become, the larger each new product has to be to contribute to growth.

3. Change the business

- Having used low cost entry, easy scaling up and customers switching to climb the growth ladder quickly, you have to work at removing those advantages for the firms that follow you.
  - Increase the cost of entry into the business, using either legal protection or new gate keepers.
  - Increase the cost of scaling up, by changing the way the product is designed, marketed and used.
  - Increase customer stickiness (with your product), by adding features that learn from your use or by creating work product that will not travel to a competitor's product.

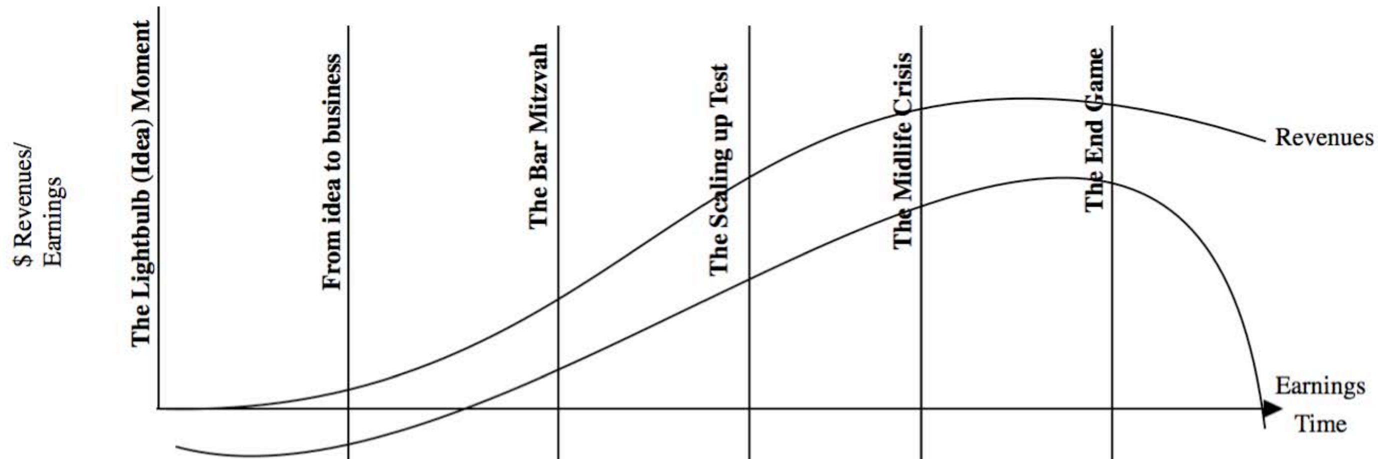
The Moat Analogy

- In value investing, investors use the notion of a moat to describe competitive advantages that a company may have in a business.
- Good value investing is based on investing in companies that have substantial moats.
- The moat analogy can be extended and enriched to bring in tech companies (and especially disruptive ones).

The Extended Moat – The Status Quo

The Extended Moat – The Disruption

The “Right” CEO



Growth Stage	Stage 1 Start-up	Stage 2 Young Growth	Stage 3: High Growth	Stage 4 Mature Growth	Stage 5 Mature Stable	Stage 6 Decline
All Narrative → ***All Numbers***						
The Top Management's Job	Tell a compelling and plausible story with potential for huge profits	Stay consistent in word & actions with your story	Start delivering numbers to back up the story	Keep your narrative in sync with your numbers	Adjust your narrative to reflect where you are in the life cycle.	Act your age (in terms of narrative & choices)
The Right CEO	**The Visionary**	**The Builder**	**The Opportunist**	**The Defender**	**The Realist**	**The Liquidator**

The tech company challenge..

- If you buy into the notion that tech companies don't get a chance to coast and can very quickly turn from high growth to speedy decline, here are the implications:
  - The visionary, risk taking managers are successful in the hyper growth phase. They bring charisma and story telling ability to the job. (Steve the visionary)
  - In the decline phase, you want managers with much less ambitious agendas, more focused on getting the best deal for their stockholders. (Larry the Liquidator)
- If you don't change management or management style and the company transitions to a new life cycle stage, all your value creation will come to naught.
- Since it is difficult for one person to have all the characteristics that you need to make it through the life cycle, you are likely to see more:
  - Value destruction at tech companies, as they move into the decline phase
  - More CEOs removed at tech companies, as investors push back
  - More activist investing at tech companies, as the first wave of aging hits the sector.
  - Regrets about giving up voting rights at tech companies in the last decade.