Chapter 2 -- Collaborative Commerce

by Robert Porter Lynch & Todd Welch

The road took a sharp turn on our journey to the future, and many of us didn't recognize it when it was happening, we were so dizzied by the speed and complexity of the change. In surveys done in the last five years,[i] senior executives (45-65 years of age from every size and type of business) were asked to plot a curve given a simple set of instructions – on the graph, using 1970 as a baseline, as time has progressed to the present "what does the rate of change, complexity, and speed (illustrated on the vertical access) *feel like?* The participants were instructed to chart their own personal point of view, not what they had read or been told by someone else.

The "Shift"

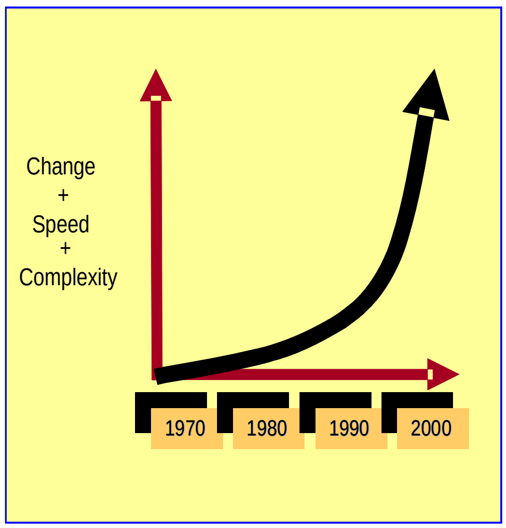


Figure 1: Rate of Change, Complexity, & Speed

Astoundingly, 80-90% responded with a curve that looked like Figure 1. [ii]

In the first half of this era (1970-1990), the business world was slower moving, a period of relative predictable change, characterized by five and ten year strategic plans and three year sales forecasts. Organizations were stand-alone and predominantly hierarchical. The rules of management in this era had been developed from years of experience, handed down through generations of tradition and the esteemed learning from our business schools.

Then hell broke loose. Fired by massive forces of change -- the compounded impact of the internet, computers, software, globalization of business, cell phones, and information technologies, what was once a somewhat predictable world almost instantaneously suffered a tectonic shift, becoming fast, discontinuous, and unpredictable. Long-term strategic plans were suspended, sales forecasts scaled into shorter horizons, and alliances burgeoned to enable adaptation to the shift.

There is no time in the history of the world when this type and magnitude of sustained change has occurred in such a short period of time.[iii]

In the face of this massive shift in speed, complexity, and change, everyone in business needs to ask the question: "So what? What's different today that wasn't true or important ten or twenty years ago?" If you haven't asked this question, we strongly urge you and your team to do so, because the answers may astound you.

> It is not the strongest of the species that survives, nor the most intelligent, but the one most responsive to change.
> -- Charles Darwin, English naturalist

At Charter Partners, when we saw the "shift" occurring, at first we didn't know or understand the implications. Now, we think we have a better grasp on what it means, and should cause us all to reconsider how we think about and operate our businesses.

Simply put:

The future isn't what it used to be!

We're in a period of business evolution that requires massive readjustment and reassessment of our priorities, styles of leadership, assumptions about people, and methods of interacting. Every entrepreneur must now consider how these issues impact his or her business.

Revolution in Innovation

Rapid change is the compelling reason to focus on innovation. Without innovation, any business is faced with becoming extinct, and faster than ever before. Thus innovation becomes essential for business survivability. We believe there is new fundamental rule for businesses today – both large and small:

In a fast moving, rapidly changing world,
the most sustainable source competitive advantage is
collaborative innovation.

Massive advances in computer and telecommunications technology have driven powerful shifts in business and economics. We are still trying to absorb the meaning of these changes. But, to the chagrin of many who seek a stable world, the old rules are being rewritten daily. Some of the new rules will astound the older generations, but, ironically, two things that were treasured in the past -- trust and relationships, will be more important in business now and in the future.

Ideas are the fuel of innovation engines.
Best of all: the fuel is free.

Hierarchies are dinosaurs

The hierarchical organization as we've known it is a hand-me-down from the Roman legions. It worked well in slow moving environments. However, in a fast moving world, connected networks that function more like the neural networks of the brain are more efficient. Yet our organizations are not changing at the rate of speed of the environment around them. Adapting to fast-changing conditions involves working closely and cooperatively. Even the U.S. military now understands this – the role of a private in a combat-centered battlefield network is far different today than in the Vietnam era; he's no longer a "grunt;" he's an integral part of the battle system: thinking, sensing, innovating, and acting. So too, in your entrepreneurial organization, should your employees be part of the "network."

Need for Collaboration

With the advent of the internet, powerful communications, and a major shift to greater connectivity between customers and suppliers, our new world of global enterprise is now far more integrated, accelerated, and connected. This calls for a new type of business –

one that is highly cooperative. For the older generation, cooperation may come as a shock. The premise of the past was that the "John Wayne style" hero was the epitome of the heroic entrepreneur. Independence is no longer a sustainable strategy for success. This doesn't mean we think the individual is obsolete or that individual initiative is a relic of the past – quite the contrary! But it does require the individual entrepreneur to think in new, connected and strategic ways.

Entrepreneurship is more Important than ever

Rapid action, less bureaucracy, and working on intuition is more prized now than in the days of slower bureaucratic corporations. Quick decision-making, agility in organization, creative solutions, flexible roles, fast alliances, and willingness to take calculated risks are the hallmark of the successful future business.

Information is a Commodity

In the past, access to deep knowledge was the privilege of the college educated. Today the internet has changed all that. Any young child with a computer and access to the world-wide web can have just about as much information as the Harvard MBA. So it's not about the information; today it's about ambition, creativity, organizational ability, and willingness to take risks.

Strategic Alliances & Networks

Unlike the prior age, where stand-alone companies produced nearly everything they needed to sell, this new era demands that we focus on what we do well. Successful companies are now learning the importance of being integrated, connected, networked, and allianced with their customers, their delivery systems, and their suppliers. Even giants like P&G, IBM, and Cisco Systems now pride themselves in the innovation flows that come from their alliance partners.

Power of Intellectual Capital

Information is now a commodity – available, cheap, and accessible by anyone. Money is accessible to those who have initiative and a truly good idea more prevalent than ever (even though we never seem to have enough of it). What becomes most *valuable* in the new era of *innovation* is the single thing which creates the most *competitive advantage* – and that's *intellectual capital.* The game every entrepreneur must play is establishing a sustainable competitive advantage to keep his or her business alive. The way this is done is different today than it was a generation ago: it's unleashing the collective creativity of your entire organization – internally and externally with your suppliers and customers.

Collaborative Innovation

If innovation is the most important means of creating sustainable competitive advantage in a fast moving, rapidly changing world, then how do we maximize our competitive advantage? By out-innovating the competition. But any entrepreneur, if operating solo, is destined eventually to run out of ideas. All the brain-power of Edison and Einstein combined would not be enough to produce the quantity of innovation required, given the rate of change around us. This should lead anyone to the inevitable conclusion: we must *collaboratively* innovate to win in the game.

The best way to have a good idea is to have lots of ideas
-- Linus Pauling, Nobel Prize-winning scientist

Leveraging Resources

Just ask any business, from the largest multi-billion dollar global giant to the smallest local sole proprietorship about resources: they will all say they don't have enough resources – money, people, time, or information. Studies have shown that companies with too many resources usually squander them – it's the resource constrained companies that tend to be most successful. Just look at how the lack of resources forced Apple Computer or Toyota to be resourceful, gaining enormous competitive advantages using ideas against brawn. Companies, from large to small are now learning to cooperate to compete, thus leveraging their resources enormously.

At Charter Partners, we pool our resources together between honorable competitors to gain major advantages in the marketplace. The key to collaborative competition is honorable interaction, and carving

Teamwork Inside and Outside

Leveraging resources and generating intellectual capital requires a little rethinking of what we do and how we do it. Teamwork used to mean getting people to work together *within* our organization, usually within a small part of our business. While this is still true, a larger truth prevails today: we must make teamwork fulfill the goal of making our organizations more efficient and effective; more innovative and agile; more connected and faster. But we can't limit the idea of teamwork to something within our companies – teamwork has to happen across boundaries: with our suppliers and our customers. Without seeing our company as part of an alliance network of suppliers and customers, we run the risk of thinking too tactically when competitors are jointly playing a strategic game.

Teamwork & Trust Create Competitive Advantage

In the game of business, where resources are limited, risks are many, and the competition is fierce, teamwork and trust are a powerful hidden competitive advantage because they are difficult for the competitors to see, never mind duplicate. Teamwork means people are energized and synchronized; they can trust each other to perform and they help each other out; they build on each other's ideas; they sense what's happening around them and call each other into action quickly. By building a group of highly energized, coordinated people synergize together, co-create, and coordinate with utmost precision (what's called *synchronicity*). Without trusting, the thinking and teaming parts of the equation won't compute. What's interesting about trust is that it was much more a part of capitalism during the pre-industrial (agrarian/ merchant) era, and it will be an even greater asset to a business in the future, because it enables high levels of speed, innovation, and integration – all major assets in our new, fast moving world.

New Economics

While digital technologies not only have impacted every aspect of business, they have highlighted a dimension of economics that had hitherto never been explored.

To understand the new economics, you must first think outside the box. Everything you learned about traditional economics works only part of the time. (If you took a course in economics in college, please put it aside for a few moments until we explain) First, there are actually two different types of economic systems running simultaneously at all times – one is quite evident called the economics of exp*e*ndables. The other less tangible, called the economics of exp*a*ndables. We'll show you the difference and how they impact on your business, your thinking, and your bottom line.

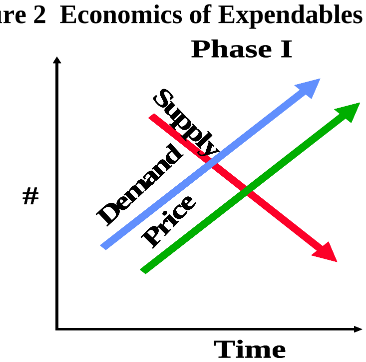
Economics of Expendables

This is really easy to understand, and the basis of all traditional economics.

Exp*e*ndable resources are *depleted* and *decrease* upon usage.

Let's use gasoline as an example of an exp*e*ndable. In this case, all the normal laws of supply and demand prevail. When you use a gallon of gasoline, the gasoline is gone forever – kaput. Each gallon of gas you use diminishes the supply of gas. As demand goes up, supply goes down, driving the price up (Phase I Figure 2 below).

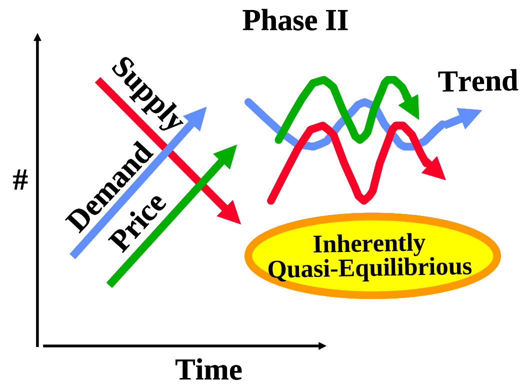
Figure 2 Economics of Expendables Phase I



If demand reverses course downward, supply increases, and price goes down. During the time the gasoline sits in your car, the utility (or value) of the gasoline remains stable.

As price is driven up, suppliers are encouraged to produce more, which increases supply, which in turn drives down prices. Eventually some zone of equilibrium is achieved in which prices and supply and

Figure 3 Economics of Expendables Phase II



demand tend to stay within a range. (Phase II Figure 3 demonstrates this graphically.)

That's pretty obvious and pretty simple. Here's where things start to get really interesting:

Economics of Exp<u>a</u>ndables:

This is what you weren't taught in school, and can't see as easily, but you know it from experience. Economists were puzzled by it when they saw productivity increase dramatically in the 1990's, but couldn't explain it with traditional thinking. Here's why: Unlike exp*e*ndables (which adhere to the universal price laws of supply and demand)

Exp*a*ndables are not limited by supply, and demand (usage) does not increase their price, but it *does increase their value.* Exp*a*ndable resources regenerate, or multiply the more they are used.

This is why 1+1=3. Let's look at an example of the economics of exp*a*ndables in practice. Take Edison's invention of the phonograph a hundred years ago as an early technological example in the "analog age." Once Edison created phonograph technology, the production of a single record could be reproduced at an extremely low incremental cost of production, though selling for a premium. Unlike consumables, playing the record did not "use it up;" the more it was used, the more utility was derived.[1] Phonographs were then superseded by radios, which extended the range and utility of phonograph records even further.

Software is a modern and extreme version of this phenomenon in the digital age. Software is inherently an exp***a***ndable resource. Using it daily does not diminish its size or impact. To the contrary, using software creates more value every time it is used -- therefore it expands. It's best used when shared, transferred and transmitted; hording it diminishes its value; using this resource brings it to life. Capturing the learning and sharing the knowledge generated by software only makes it more valuable, reaching more people, and generating more future possibilities. Software is inherently invisible, being only a series of magnetic imprints on a media. A disk or CD costs virtually nothing to produce (the CD or Disk's value is less than $1, and an Internet download is almost free), but the software may be valued at

Some examples of Exp***a***ndables
» Software
» Digital Technologies
» Networks & Information
» Innovation and Breakthroughs
» Teamwork & Cooperation
» Communications
» Caring, Happiness, Compassion
» Co-Creative Innovation

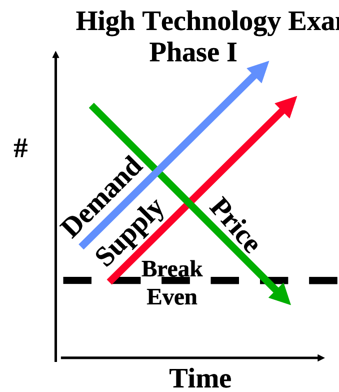
[1] Note: There is an in-between zone which includes ex***te***ndables (or durables) such as telephones, radios, houses, washing machines, cars, antiques, fine art, tools, and so forth, that have very long life spans, not being "used up" for a long number of years, and having very low cost per usage. *Replenishables* also fall into this zone because nature puts them back as we use them. For both extendables and replenishables, their incremental cost of production does not exhibit the same dramatic cost advantages of one of our latest digital technologies such as software or the internet, but yet provide massive economic advantages over exp***e***nables.

tens or hundreds of dollars, or more. In this software example, the incremental cost of production of the next package of software is so low, that the cost is next to negligible.

Therefore, a unique dynamic occurs: In the first phase of evolution, as demand for software increases, the supply of software (being easily expanded) can increase along with demand while cost drops dramatically for the software developer (because the incremental costs of production are virtually nothing compared to the sales price). If there is competition present the retail price to the customer may also drop. As the first phase of evolution progresses, still more competitors may enter the market, further depressing price and driving profits below break even.

This same phenomenon has brought the music industry to its knees as songs are exchanged over the Internet or on flash drives for free, making their price infinitesimally low. Figure 4 demonstrates what happens on the supply, demand, and price curves.

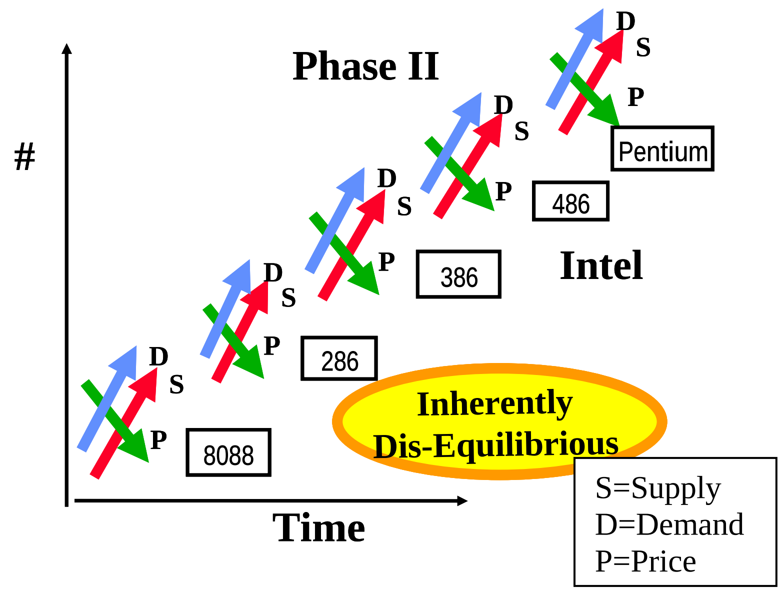
Figure 4 Economics of Expandables Phase I -- Software



This situation creates a vexing dilemma for many businesses in the digital arena. In order to keep prices from being driven lower and lower, two options exist: either attempt to control the market through a monopoly (as Microsoft has done) or innovate faster and faster (as Intel has done in computer chips or Apple has done with the iPod and iPhone).

The monopoly option, calls for buying competitors or driving competitors out of the market, thus creating an artificial price level substantially above the breakeven point. Microsoft has chosen this route successfully, forcing Netscape into oblivion and has made Bill Gates one of the world's richest men. But seldom can this strategy

Figure 5 Economics of Expandables -- Intel Example



last forever. Microsoft's Office Suite, which retails for $400 is now forced to compete with Sun's Open Office, which downloads for free; and because Firefox's Internet browser is free, Microsoft's Internet Explorer is also free. The other option calls for a regenerative strategy by which a new and better version of the technology is created rapidly to obsolete the earlier version, thus creating the second phase (or generation) of the evolution. Figure 5 illustrates the strategy of Intel from the perspective of the economics of exp*a*ndables (note: silicon, the major component of a computer chip, is one of the most abundant minerals on the earth.) Moore's Law (proposed by Intel's CEO Gordon Moore in the 1970s), the demands the capacity of a computer chip double every eighteen months, and the price per byte will drop by one half. Intel created this "law" to drive regeneration.

Other computer chip manufacturers are forced to adhere or to beat Moore's law, thus they track along this second regenerative phase, which is inherently dis-equilibrious (unstable, erratic, unpredictable) because the more demand, the lower the incremental cost of production for the next chip, hence the lower the actual cost of the next chip. The regenerative economic strategy enables competitors to survive only if they innovate quickly. Those who fail to innovate will be caught in a price war that strips them of the financial resources necessary to invest in the next round of innovation.

For Intel, this price/demand/supply relationship will burn itself out every 18 months (Moore's Law), unless Intel creates a totally new level of chips. The 8086 chip of the early 1980s had had to be supplanted by the 8088, then 286, then the 386, then the 486, then the Pentium I, II, III, IV, V, and onward. While Microsoft has employed a mixed monopoly-regenerative strategy, Intel has chosen a largely regenerative strategy.

The Internet is another example: The more demand for the internet, the more supply, and the lower the incremental cost of providing the service. Cable companies, having a monopoly on connections to a home or office can artificially keep the price of internet connectivity high. On the other hand, Cisco Systems, which provides the hardware that underpins the Internet, must keep innovating with a regenerative strategy lest its competitors carve out market share in a price war.

Now, for the leap: What other phenomenon demonstrate virtually unlimited supply, while its frequent use does not "use it up?" How about *creativity*, or *trust*, or *teamwork*, or *communication*? Creating demand for cooperation, and developing skills in cooperation does not "use it up;" but instead, the more it is

If you have an apple and I have an apple and we exchange these apples, then you and I will still each have one apple. But if you have an idea and I have an idea and we exchange these ideas, then each of us will have two ideas.
-- George Bernard Shaw

used, the more utility it generates – thus becoming a "regenerative system."

What we must know is when the system of economic scarcity is in play, and when we are engaged in the system of economic regenerativity. In the long run, an investment in a regenerative system plays much better dividends for the larger community that in a scarcity system (although scarcity systems can create short term aberrations in which large amounts of money can be made or lost for those trying to maximize their self interest, as Wall Street has done for years).

We must be able to distinguish between exp***e***ndables and exp***a***ndables when engaging in any collaborative relationship because the laws that govern one run counter the laws that govern the other, but *both are true and both mutually exist in our world*, and each has its applicability to totally different circumstances. To treat each with the same principles and rules of usage confuses and limits possibilities for collaboration to utilize the unique power of exp***a***ndables.

This problem manifests quickly when miserly minds can't acknowledge the laws of exp***a***ndables. Their limited understanding is often reflected in contracts for intellectual property, where negotiators can tussle for months and even years over ownership rights, or in chasing the lowest cost for a component, overlooking the potential of a supplier to provide innovation or other value-based services. Their hording and protectionist mentality blocks them from realizing that, if sharing of intellectual property rights occurred, or if they worked for mutual advantage, both sides would create more new ideas and command a more sustainable joint competitive advantage.

Unfortunately, the Economics of Exp***a***ndables are not well quantified, analyzed, or studied, and therefore does not form the foundation of traditional economic thinking. What also sets the Economics of Exp***a***ndables apart is that it is highly dependent upon the establishment of a regenerative system to support it.

Accessing the expansive possibility of sharing begins with the mutual belief that "the more you give, the more you're going to get."

When both partners hold this belief, it manifests. The general rule for the Law of Exp***a***ndables is:

Sharing Expands, Hording Contracts

Collaborative mind-power thus creates its own "regenerative energy," or a form of "synergy."

Is Capitalism Dead?

No, quite the contrary. Capitalism is very much alive. What's happening is that, just like capitalism in the previous eras, it is transforming to fit the new Era of Innovation. This is why we use the term Collaborative Commerce, to distinguish the new Capitalism from the old forms. (Some people call this capitalism with values, or with a heart.) There are a number of things that will be significantly different, and many people will be quite confused, because during any time *between* eras, the rules of a fading era will conflict with the rules of an emerging era, creating a duality that looks like a set of contradictions.

To help understand this shift in capitalism, a very short (and thus generalized) historic background is helpful. Let's take a quick look at where our commercial models came from and how they've shifted:

The History of Business (in a few pages)

Capitalism

The basis of modern economics is rooted in Adam Smith's classic book, *Wealth of Nations*, which advocates that money and self interest was the basis of economic power. He wrote his treatise in 1776, during a pre-industrial era where commerce was highly localized. Most business was done on the basis of trust with people who knew each other, lived in the same community, and whose reputation was vital to their ability to transact future business.

Soon thereafter, the early 1800s brought the Industrial Era. Wealthy business constructed vast empires in textiles, steel, chemicals, and railroads. Labor, then seen as a commodity, could be used to run machines. Sweat shops emerged, business exploited labor, especially children, and the environment became polluted.

Robber-baron capitalism concentrated enormous wealth in the hands of a few, making the rich richer and the poor poorer.

An uncontrolled rollercoaster of prosperity and depression ruled the economies of Europe and North America for over a century. Boom times were followed by depressions as the banking system cycled from greed-driven profit-making then recoiled as the bubbles burst (the Great Depression of the 1930s is a good example, as well as recent housing market crises).

Imperialistic nations spread capitalism across the globe in search of undeveloped nations whose natural resources could be exploited. During the Industrial Era, the major issues of the time were very much guided by how the political systems responded to economic forces.

Capitalism, which in the preceding Agricultural/Merchant Era had been localized and composed of small and medium sized businesses, changed dramatically. Business became more remote, distant, and transactional. Contracts and legal protections were required as the business community became more far-flung.

Communism

Exploitive capitalism triggered numerous reactions. Karl Marx wrote the Communist Manifesto in 1848 to counteract robber-baron capitalism. Marx proposed a communistic system that returned all the wealth and control to the working class, framing this as the struggle between labour and capital. Marx's proposed that labour, not capital, was the rightful foundation of economic wealth and that, to protect people from the robber-barons, a new social and economic order was necessary.

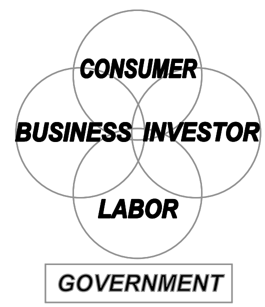
By 1848, Europe was awash in riots and revolutions as the workers revolted against capitalists, giving birth to the labour union movement. Russia, in 1918, and later China, adopted Marx's system.

Socialism

Less extreme responses to exploitive capitalism focused on enabling government to control the economic system, and balance the interests of labor and capital, under the name of socialism. Not willing to give up their power and privileges, the capitalists in control were forced by to make economic concessions and reforms as labour unions pushed for child protection laws, anti-trust laws, and safety regulations. Many countries in Europe followed this route.

Government-Disciplined Capitalism

It's important to understand that capitalism is essentially an alliance of four powerful interests: business (providing goods and services), labor (producing goods and services), investors (providing capital to grow businesses), and consumers (to buy goods and services). When this alliance works efficiently, in alignment and balance, capitalism is a highly productive system.



Unfortunately, this alliance has a strong tendency to get out of balance and alignment. Historically there have always been some businesses that have tried to sell consumers defective products, polluted the environment, and abused its labor force. Similarly, the investment community, made up of banks and Wall Street investment houses, has often let greed (and its flip side: fear) reign, pushing businesses to incessant profits at the risk of its own health. Some labor unions have been led by those who let power go to their heads, thus destroying the delicate balance calling strikes that drove their businesses into oblivion.

Government is the only force that represents the silent voice of consumers and the greater good of the whole. Thus it is the only entity that has the power to balance and align the system ensuring the four interests are working together effectively. In this way government acts like a system integrator and creates a "level playing field.

In North America, during the 20th century, government corralled exploitive capitalism with laws governing child labor, anti-trust, tax, pure food, and the environment. Labor unions counter-balanced abusive businesses, and political parties emerged to represent the interests of labor and capital. When labor abused its power, government stepped in, sometimes with the National Guard, to force labor to end strikes on the railroads or air traffic controllers. After the

Great Depression of the 1930s, new laws were put in place to prevent the excesses of the financial investment sector of the economy.

Left and Right Wing

In the United States, politicians built power-bases around either labor (left wing) or capital (right wing). Today's Republicans and Democrats trace their philosophical roots to either the capital or labor sides of this historic battle. Today Republicans tend to adhere to conservative values, while Democrats are now more associated with social consciousness. However, in any political campaign, business and investors will typically place more contributions in the hands Republicans, and labor unions will typically finance Democrats.

Understanding the Global Meltdown of 2008

Capitalism is a *system*. To understand why the system collapsed in the fall of 2008, one must understand a few basic things:

> *First*, all systems must have balance and alignment. For example, your own human body is a system. If the digestive system stops functioning, you starve and die.
>
> *Second*, the interests of those that comprise the system are not the same: Consumers want the best value for the purchases; businesses want to sell products and services competitively at a profit; investors want to make money, and labor wants to earn a living and have job security. (This is admittedly a bit oversimplified for sake of brevity)
>
> *Third*, the system is has some unholy elements in it. A small minority of those in the system (driven by greed, fear, or power), are prone to abuses. When they are not disciplined, the abuses can throw the entire system into disarray.
>
> *Fourth*, the system is analyzed predominantly by economists, who hold the false belief that people make rational decisions. But worse, a segment of these experts believe in *free markets* which they erroneously predict will automatically self-correct[iv]. The free market economists advocate governments play a minimalist role in balancing the system. Free market economists fail to understand that markets cannot act rationally because they can

be abused and be unduly influenced by the emotions of greed and fear (opposite sides of the same coin), and that there are members of markets who will unscrupulously attempt to manipulate the market forces for their own self interest.

To understand the current economic meltdown, it's also valuable to get a historic perspective on the factors that have caused debacles like this in the past. This type of economic crash has occurred every 20-30 years (or more) sometimes with catastrophic effects. There have been crashes like this in Europe and the United States in 1636, 1694, 1721, 1792, 1797, 1819, 1825, 1847, 1847, 1857, 1873, 1890, 1893, 1907, 1929, and now. In the last several decades Japan had a total meltdown of its financial system in the 1990s, and we experienced smaller regional or industry specific crashes in the U.S. the 1980s in real estate, silver, and internet stocks.

To create the "Perfect Storm" Financial Panic, there are common elements in each and every one of these historic economic disasters:

1. <u>Easy Credit</u> which artificially increases the supply of money in the economy
2. <u>Speculative Greed</u> of Investors which is fueled by easy credit by Banks
3. <u>Dalliance</u> between Investors and a Target Business Sector, which becomes the "Darling of Wall Street Analysts" who hype stock in that sector
4. <u>Frenzy to Over-Build/Buy</u> as the bubble increases due to Crowd Contagion
5. <u>False Sense of Security</u> that the underlying value of the speculative target/asset is stable and sound
6. <u>Delusion</u> that the Financial & Investment community can regulate itself (or that competition will cause it to self regulate)
7. <u>Lack of Transparency</u> into what is really happening and who's really driving the market, thus the collapse comes as a surprise
8. <u>Failure of Government</u> to see reality and protect the interests of the common person by regulating the system to ensure fairness, stability, and security

The Free Market Delusion

It's in the nature of speculators and the finance community to "make money" (a euphemism for "greed"). Beginning in the 1970s, free market economists began advocating the diminishment of government's role in the economy, except by regulating the monetary supply through the Federal Reserve. Government took its eye off the ball, and the economy went on a speculative spree, this time focusing on real estate. The forces to create "perfect storm" financial panic were quickly coming into being, much like a hurricane forms in the ocean.

Wall Street had a love affair with the free market economists, promoting their philosophies, their books, and their strategies. All over the globe, the delusionists began to drink their own bathwater. They loaned more, then used the over-inflated real estate as false security. It had happened many times before, and not very long ago in Japan and Norway, and in Texas and New England. But greed overpowered rational thinking as the frenzy continued[v].

We then let Wall Street control our thinking about economics and capitalism, control the measures of success (companies must make growing profits every quarter) and control the rewards and punishments (if you don't meet Wall Street's "expectations" we'll kill your stock value and arrange for you to be bought by a hostile entity).

Return of Robber Baron Capitalism

There are many (but certainly not all) in both the financial/investment and business sectors whose primary objective goes beyond the running profitable ventures. For this small minority, their purpose is to make money at all costs, including pillaging customers, consumers, employees, suppliers, pensioners, and small investors. These few consider that the purpose of business is to maximize the making of money – this is the gentleman's term for *greed*.

The problem with greed is that its underlying cause is *fear* of not having enough. Thus greed is insatiable as long as the fear exists. This greed drives massive desire for immense material accumulation, far beyond anything a human being needs to live happily. While greed (inherent in a few who operate within any capitalistic system) cannot be cured, it can curbed by sensible policies and legislation.

The term "free market" is a misnomer. When free markets become a "free-for-all" melee that gives unhealthy advantage to the big and the unethical, the system is out of balance. The self interest of the greedy can destroy the greater good of all, including the self-centered.

During the period leading up to the 2008 Meltdown, banks , driven by the drum-beat from their Wall Street brethren for ever-increasing profits, learned a cruel way of making money. First, they took a legal, but unethical avenue, issuing a mountain of credit cards to those lower income people who couldn't afford them, and charged exorbitant rates the moment the holder got behind in their payments. They enticed people with low initial fees, then hit them hard with interests rates and penalties beyond usury. It was certainly unethical, but legal. If some people defaulted, it was offset by the money they made on those who struggled successfully to keep up with their payments.

What the banks learned from their credit card experience was how to entice people into a bigger game – buy a house on credit through sub-prime lending. Then hit the low-income sub-prime homeowners with an Adjustable Rate Mortgage that would produce higher returns several years later. This was a hurricane ready to to make landfall with explosive force.

Role of Government

Because government's view of their role was jaded by the eloquence of the free market economists, Washington looked the other way and provided vehicles for buying the subprime mortgages, the house of cards continued on, until as one bank then another failed, the whole system came crashing down, taking with it nearly every legitimate business and worker, and pension-holder as innocent victims.

Free markets must mean freedom for the most creative to innovate freely, not be gobbled up by the dinosaurs of a by-gone age. The intrinsic value of something (like a home) must not be driven to speculative exorbitances to salt the meat of those hungry to make just another buck.

Imagine a competitive contest like a football game without rules and a referee. In short order chaos and calamity would prevail. There would be carnage as the playing field became a gladiatorial slaughterhouse.

The proper role of government in establishing "fair markets" is to act like a referee in a sports contest – interpreting the rules of fair play, enabling competitive performance to be rewarded, and impose stiff penalties for those that play below the belt, thus preventing the manipulation of markets by the powerful and the greedy, and protecting the investments of society: the small businesses, the workers, and the home owners from manipulation, speculation, and deflation.

Keeping the balance between self interest and the greater good of the whole is the worthy and rightful role of a government committed to honorable purpose.

Capitalism is not an "evil" system – in fact it has stimulated tremendous competition to create wealth that has grown a prosperous middle class that is the core of civilization.

Cooperative Commerce

Industrial Era in the U.S. lasted from the early 1800's through the 1970's[2]. (see Figure 6)

During the Industrial Era, it became clear that the two extremes: Dictatorial Communism and Exploitive Capitalism were becoming extinct because they did not work. The systems in the middle: Government-Guided Socialism and Government-Disciplined Capitalism were producing far better results for all people.

Labor strife diminished, people became conscious that the environment needed to be protected. Tax structures were reformed as the disparity of thinking between the "haves" and the "have-nots" diminished. Distinctions blurred between right and left wing ideals.

[2] Note: different countries enter and exit eras at differing times and rates, and residue from one era often continues into the next

The Russian communism collapsed, Chinese communism transformed, and European socialism became more symbiotic with capitalism.

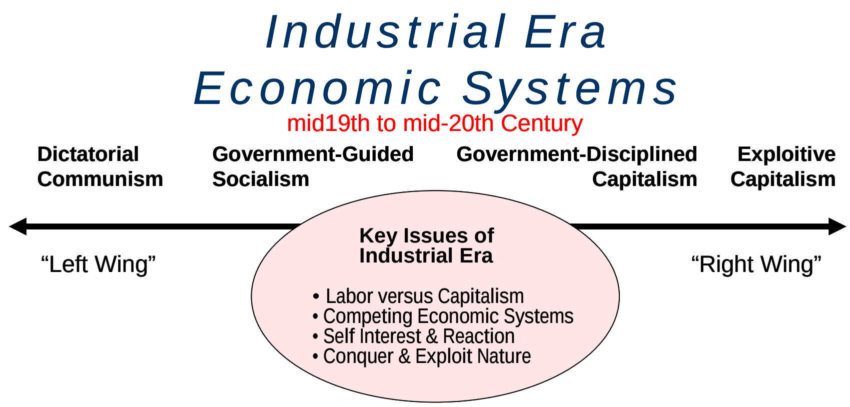


Figure 6 Industrial Era Economic Systems Rivalry

Information Era of Capitalism

Many changes occurred as we shifted eras from the Industrial Era to the Information Era, which began to emerge in the 1980s. (see Figure 7) Technological innovations of the late twentieth century connected the world, enabling a globalization of economies. Developments in the central banking system made great strides in smoothing out the boom and bust cycles, but (as described above) greed still disrupted the financial system; the philosophy of deregulation, which worked for many industries, didn't work for finance, because it attracted those whose need for gaining wealth at the detriment of others was insatiable. The level trust needed to run a fast moving system was still lacking. The computer revolution made data was available to everyone, accentuated dramatically by the internet. Digital technologies made the replication of software, data, and communications far less expensive per unit than ever before.

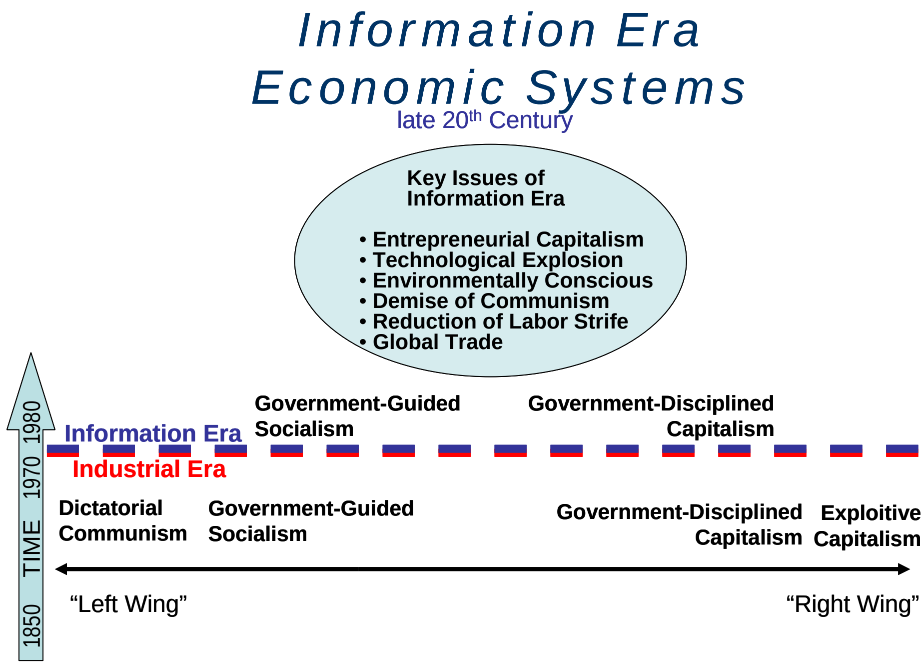


Figure 7 Shift from Industrial to Information Era

With this shift came a globalization of economies, and also a reframing of the rules of business. Money was less a precious resource, information became a commodity, and educated people became more valuable as we shifted to an economy based more on services and less on manufacturing.

A new entrepreneurial capitalism emerged that enabled small companies to grow rapidly (for example: Microsoft, Apple, Google, etc.) and the owners accumulate great wealth because the foundation of competitive advantage shifted from large behemoths to agile, fast, and innovative entrepreneurs.

With this shift, many industries of the earlier Industrial Era were diminished significantly, such as steel, railroads, machinery, and textiles.

Innovation Era of Capitalism

Unlike past eras that enjoyed long lives, the Information Era proved to be short-lived, just a twenty year transitionary step-stone setting the stage for the Era of Innovation.

This newest era is something uniquely different, but still remaining grounded on the capitalistic side of the fence. (see Figure 8 below). New capacities and integrations between computers and tele-communications have enabled networking of companies in ways never imagined just a few years ago. Competitors that used to be arch-rivals are now collaborating.

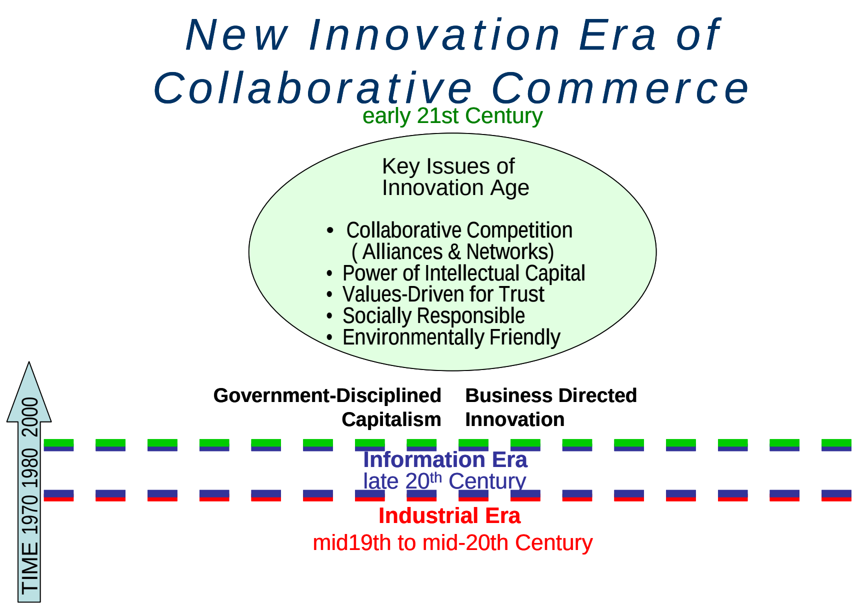


Figure 8 -- Emerging Themes of the Innovation Era

Financial capital, once the source of power in business, is being replaced by intellectual power. Workers, who once were treated like replaceable parts, are now being seen as a competitive advantage, being encouraged to work smarter not harder, using their ideas more than their brawn. The emergence of the service economy now balances the manufacturing economy, thus encouraging more thought-generated ideas from the workforce. Social responsibility is considered to be an integral part of a business' mandate. Environmental consciousness has evolved into environmental responsibility as the threat of global warming looms large.

During this new era, government's role is emerging both as a disciplinarian to prevent abuses, and as a facilitator to create economic and competitive advantages for its constituencies. To deal with the need for speed, integration, and innovation, many businesses are aligning their strategic direction using alliance-based business networks (eco-systems). The power of the eco-system will be dependent on their focus of alignment, global reach, their agility, and their ability to innovate rapidly.

It is this new Innovation Era of capitalism we refer to as "Collaborative Commerce" to distinguish it from earlier forms of capitalism. It's new, it's unique, it's guided by somewhat different rules and principles, and it's actually very energizing.

Caught in the Gap Between the Shifts

The rapidity of the shifts between the Industrial, Information, and Innovation Eras over the last thirty years has caught many by surprise and has confused many because what was considered truth in one era becomes a myth in the next.

Many academicians are still teaching old management principles that were very true just a few years ago. For example, one esteemed professor of business confidently stated recently (referring to supply chains):

– *Power is the primary basis for relative strength of the buyer-supplier relationship….*
– *In a world of scarcity, win-lose negotiations is the best approach because win-win is a fuzzy fallacy ….*
– *It's not in the interests of buyer & seller to maximize their mutual benefit ….*
– *Exchange is at the heart of all human existence ….*

He is clearly grounded in the thinking of the Industrial Era advocating strategies and practices that would fail dismally in the Innovation Era.

Business leaders are often baffled by the seemingly contradictory philosophies as advice is coming at them from perspectives grounded in each of the three different eras.

Old Truths – New Myths

Being caught in the gap between the eras has also created some anomalies in thinking. Here are just a few examples of "truths" of the old era that are becoming "myths" in the new era:

Old "Truth," New Myth: If It Ain't Broke, Don't Fix it

This made a lot of sense in a stable, slow-moving world where innovation was negligible. Big manufacturing plants ran on vast systems that were designed for efficiency, thus any change would cause major ineffiencies. In today's world of rapid innovation, if it's not broken, someone in the world is going to reinvent it and put you in a tough spot.

Old "Truth," New Myth: It's always a battle between Labour versus Capital/Management

This was always a half-truth, half lie, and is so outmoded, that it's not worth discussing the problems Communism had making the numbers work. The Russians and Chinese abandoned it, and only a few hold-outs like Cuba think it has any value. Sadly, the battles over this type of thinking lasted over a century, started wars, killed millions of people, and overturned governments. It became the realm of zealots and fanatics, just like a religious war. Some labour unions in a few isolated countries still hold this as a truth.

Old "Truth," New Myth: The Purpose of Business is to Create Shareholder Value

Another half truth, this one from Wall Street, which makes a lot of money from this mythology essentially because it enabled financiers to pad their own

The purpose of business is to provide goods and services to customers competitively at a profit.

pockets wheeling and dealing with other people's money. But small and medium-sized businesses are usually guided by more purposeful people who find the reason for their business is to provide a product or service they believe in at a profit. Their businesses run not on shareholder value, but on cash-flow (just ask anyone who's had to make a payroll). What's more, try motivating an employee on Monday morning with a rousing speech about how he or she is going to work all week just to serve some unseen and unknown shareholder. Reality: Making money for shareholders is just one measure of our success. – its not the purpose of the business, nor is it the motivation of most entrepreneurs or employees.

The Future of Business

In this new Era of Innovation, cooperative entrepreneurship will flourish based not on massive size or money, but how well you can collaborate, innovate, integrate and accelerate.

However, the changes required in thinking about collaborative commerce will require new approaches to the ideas of deregulation and government discipline.

Deregulation is a wonderful philosophy in a perfect world where all the players are honest, fair, and ethical. Unfortunately we don't live in that world. Government discipline is required to ensure the alignment between entrepreneurial self interest and the greater good of the society in which businesses exist. Recent debacles such as Enron and WorldCom, or the Wall Street meltdown[vi] illustrate how those with insatiable greed can take advantage of other peoples' money and trust in the most ignominious ways. The role of government in the emerging Era of Innovation must be two-fold:

1. to provide (with the input of ethical businesses and community stakeholders) coordination, guidance, and propulsion for sound business initiatives
2. to act as disciplinarian to ensure standards, ethics, fairness, and safety – that of "guardian" to ensure high levels of trust.

We encourage you to read Chapter 6 on Trust to see our system of how to rebuild trust in our business world.

Moving Forward

In the following chapter, we will show you how we have actually created real competitive advantage using the principles of collaboration. You will see it has been an exciting and rewarding journey.

---

[i] During the last 5 years, RPL, in speeches, seminars, and workshops, asked over 10,000 executives across the US and Canada about how change, speed, and complexity has changed. Between 80-90% of all audiences responded with the curve noted.

[ii] The only difference among these 90% was the point of inflection where the curve changes direction radically. For those in very rapid change industries, such as high tech, the point was generally between 1986 and 1990. For those in slower changing businesses, such as petro-chemicals the point tended toward 1995-7. The primary reasons for the shift cited by executives were: computers, faxes, globalization, cell phones, then the internet, each compounding upon the other.

[iii] The only possible exception to this type and magnitude of change might be the Second World War. However, the difference is that after the war, the world basically resumed its prior ways, whereas in this current change, the entire world is shifting its perspective, behaviors, priorities, and rules of engagement. George Santayana's admonishment that "Those who do not learn from history are doomed to repeat it," may not prevail in this environment where there is no precedent for the change.

[iv] (On October 24th, 2008 in Congressional testimony, former Federal Reserve chairman Alan Greenspan expressed astonished dismay that bankers could not self-regulate their propensity to be extremely greedy.)

[v] Charles McKay wrote in 1841 about the *Madness of Crowds*, that peer pressure can influence people to make ridiculous decisions, stirring up a feeding frenzy that warps even sane minds and lures intelligent, well-meaning people into foolish judgment. This can be kept alive by ideologues, like free market economists, who believe that the market is an accurate judge of real value. While the market *can* be a judge of value, it is often skewed by greed, corruption, and manipulation that highly distorts *intrinsic* value.

[vi] The Wall Street Meltdown of 2008 is a perfect example of *Greed Gone Bad*. We let the fox get into the henhouse during the mortgage boom when money managers sold mortgages to people at adjustable rates they knew people couldn't afford and financed homes to speculators when there was no rental market to lease the properties. This was simply bad business, and the place

where government's role should have been to replace greed with sanity. Government failed, pure and simple. In the new, emerging era, government's role will become clearer, as it learns it must replace systems based on trickery with honesty, complexity with simplicity, obscurity with transparency, and deception with trust. The games of shorting, derivatives, hedges, and unbridled speculation that artificially drove up the oil markets in the summer of 2008 must be curtailed as part of the reforms. The financial industry has lost sight of its fiduciary responsibility to protect the capital of people's 401K and pension funds to prevent further abuse. Self interest is the reason why capitalism has beaten communism as an economic system. But it was no robber-baron capitalism that prevailed, it was government-disciplined capitalism where unrestrained self-interest was bridled by the higher principles of the greater good, much like a spirited stallion is turned into a thoroughbred racehorse.