Viewpoint: Paul Ormerod
Failure and Success

Failure is all around us. Failure is pervasive. Failure is everywhere, across time, across place, and across different aspects of life. 99.9 percent of all biological species which have ever existed are now extinct. Failure in this context is measured over hundreds of millions of years. On a dramatically shorter time scale, more than 10 percent of all the companies in the United States disappear each year. Large and small, from corporate giants to the tiniest one-person businesses, they fail.

Yet, paradoxically, failure at the individual level is the key to the success of the system as a whole. The market-oriented economies of the West are stupendously successful, far more so than any other form of social and economic organisation which has ever existed. In the old Soviet Union, everything was planned with great precision. No individual enterprise was allowed to fail. But, eventually, the whole system collapsed. In the West, individual firms fail all the time, but the system as a whole delivers the goods.

Despite this, the existence of failure is one of the great unmentionables. Business gurus eulogise contemporary success, conveniently ignoring the fact that many of these firms often fall on harder times soon after they receive their accolade. Enron, for example, was praised to the skies for its dynamism and innovative thinking right up to the point when it became the epitome of corporate greed and mal-administration.

Books proliferate, and occasionally sell in very large numbers, which claim to have found *the* rule, or small set of rules, which will guarantee business success. But business is far too complicated, far to difficult an activity to distil into a few simple commands, or even some of the more exotic exhortations of the business gurus. It is failure rather than success which is the distinguishing feature of corporate life.

But spectacular and unanticipated success can happen just as readily. Microsoft’s early strategy, announced very publicly, was to link closely with IBM and to develop OS/2 as the standard operating system for PCs. Early versions of Windows were not popular, and attracted bad reviews. Microsoft announced that it would cease development of Windows when version 3.0 was launched, and concentrate on OS/2. Windows 3.0 came out on 22 May 1990. It sold two million copies in the first six months. The rest is history. No-one under the age of 35 even remembers the failed OS/2. Everyone knows Windows.

It is this vision, this possibility of success on a stupendous scale, which motivates and drives many people who set up their own companies. Many fail, but some succeed. The person who will eventually destroy Microsoft might be working in her garage at this very moment on the concept.

Such people are the lifeblood of our economy. Small companies, especially new ones, are where all the best new ideas are conceived, the best new products developed. The risks of failure are high, but the rewards can be great.

America has always had a much more positive attitude towards failure. Try a concept and see if it works. If it doesn't, try another. It is this willingness to accept failure which, paradoxically, is the key reason why the United States is so successful.

Peter Mandelson, Britain's current European Commissioner, has called on Europe to be more like the United States in this respect. And he is absolutely right. Fortunately, British attitudes *are* already changing for the better. Bright and energetic young people are now much more open to the idea of starting their own company then they ever were.

A practical example is a bottled beer widely sold in Indian restaurants. Curry has virtually replaced roast beef as England's national dish. The beer many people prefer with their curry is Cobra. And on Cobra's website is the stark statement: 'The scales that weigh every brand were weighted against us'. The founder, Karan Bilimoria, still had student debts. Britain was in the grip of the massive economic recession of the early 1990s. The beer market seemed sewn up by the corporate giants. Any business school textbook would tell you the concept was bound to fail. But it worked. Success, like failure, comes in many unexpected ways. All that is needed is a vision of how your product can change the world, a lot of work, and a slice of luck.

It is in the very early years of a company's life when it is most at risk. Elementary mistakes lead to a high death rate amongst small new companies. The single most important cause of failure amongst small businesses is cash flow. You might have a great idea that will work eventually, but not before you have run out of money. Making sure there is adequate finance at the start is the best way of insuring against initial failure. The sums of money do not have to be large, just enough, in fact, to tide you over the first few fraught months. Another common problem is to ignore any particular quirk of your market. For example, you are reading a magazine at this very moment. You might have a fantastic concept for a new magazine. But unless you realise that as a matter of policy most advertisers will only place material in the second but not the first issue, you are likely to fail.

The upside of all this is that once the first couple of years are successfully negotiated, the chances of a small company going under in any particular year are not much higher than those of the very largest. Size alone offers no guarantee against failure. And neither does age. A company which has survived for, say, 50 years, is almost as likely to go out of business as one which has survived for only 5 years.

Some multi-national giants have escaped extinction by the skin of their teeth. Coca-Cola seems to have been with us for ever. But by the early 1980s, Coke's leading position in the soft drink market was gradually being undermined by Pepsi. After a massive market research effort, Coca-Cola responded by introducing New Coke in 1985. Sales collapsed catastrophically. The company was only saved by the board rapidly abandoning their investment and withdrawing New Coke completely.

It may seem simply bizarre even to consider the idea that British Petroleum, say, could be driven out of business. But such things can and do happen. Almost incredibly, General Motors, once the very symbol of the dynamism and success of the American economy, is in serious difficulties. Each of America's largest 100 companies is very large. Yet every decade, one in every four of these drops out of the top 100, and over the course of a human lifetime half of them disappear completely.

The fundamental problem facing firms is that the human world is so complex and difficult to understand, much more so in fact than the physical one. So many things can happen that even the most carefully prepared plans come unstuck, as Coca-Cola discovered. The popular image of big firms is of captains of industry steering their giant tankers carefully through the reefs. Reality is much more like white water rafting.

Charles Darwin's theory of evolution explains not why species fail, but why they succeed. In the Darwinian theory of the process of evolution, species gradually become better adapted to their immediate environment, become fitter for survival.

In spite of this, nemesis eventually claims them, and species become extinct. The survival of even the very fittest confronts the Iron Law of Failure. Darwin wrote almost 150 years ago, but it is only very recently that biological theorists have begun to analyse systematically the evidence of failure at the species level. New mathematical models have for the first time made major advances to the Darwinian theory of evolution, explaining subtle and complex features not of evolution but of extinction.

The Iron Law of Failure extends from the world of biology into social and economic organisations. The precise mathematical relationship between the size of companies and the frequency of their extinction, for example, is virtually identical to that which describes the extinction of biological species in the fossil record. Only the time-scales differ.

Successful systems need to encourage change, to promote innovation. Germany is a prime example of a system of social and economic organisation which has become ossified. For many years after the war, the German system, with its careful consensus building and reluctance to upset any major stake-holding group, was a great success. But the world in which it operated changed. Britain changed. America became even more dynamic. The Far East finally started on the evolutionary path to prosperity. Yet Germany itself has stood still. No wonder that its unemployment is now over 5 million, higher than at any time since Hitler came to power, and that its growth has stagnated for 15 years.

We need structures which encourage exploration and innovation. We need to accept that in the real world, full of complexity and uncertainty, we cannot plan the future precisely. We cannot know the optimal strategy. Instead, the process of selection and evolution enables us to discover strategies that work. And we need to accept the necessity for failure. It is failure that breeds success.

Karl Marx famously wrote that the motto of capitalists was 'Accumulate, accumulate, that is the law of Moses and the Prophets!' As in many other respects, Marx was completely wrong.

'Innovate, innovate!' is the guiding principle which companies have used to overcome the inherent uncertainty that surrounds all their decisions. It is the best strategy for successful systems, and it is a strategy from which we all, as consumers and citizens, have benefited immensely.

The Best Sources of Help

Book:

Ormerod, Paul. *Why Most Things Fail: Evolution, Extinction, and Economics.* London: Faber, 2005.

See also:

Turnaround Strategies