The amazing case of the shrinking corporate lifespan

One of the many consequences of the tech boom is a much briefer average tenure for companies on leading indices. How will this affect buy-and-hold investors?

Longevity isn’t what it used to be. As the pace of innovation in technology picks up, the average lifespan of companies on major equity indices is shrinking. Consider the following: in 1965 a typical S&P500 company could expect to spend 33 years on the index. By 1990 that average had fallen to 20 years – by 2026 that number is expected to have shrink again, to just 14 years.¹

The implied churn rate means that over the next 10 years about half of the constituent companies on the S&P 500, an index comprised of the 500 leading US companies, will be replaced (see Figure 1).

Figure 1: Average company lifespan on the S&P 500 index

For Amin Rajan, chief executive of CREATE Research² and author of a new BNY Mellon Investment Management-commissioned report³ on the impact of mega trends, declining corporate lifespans raise a key question. If the revolving doors of key index constituents turn faster and corporate lifecycles become shorter, do investors need to re-assess their own timescales for asset allocations?

² BNY Mellon and CREATE Research are unaffiliated entities.
³ Future2024: Future-proofing your asset allocation in the age of mega trends. September 2019
To illustrate how destructive the forces of technological change can be, Rajan highlights the case of the Eastman Kodak company. Founded in 1888, by the midpoint of the 20th century Kodak had become a blue chip fixture of the S&P 500 and had embedded itself as a cultural touchstone in the lives of millions of people. At its height, its share of the photographic film market was more than 80% in the US and 50% globally.\(^4\)

The advent of digital photography changed all that. Beset by declining demand for photographic film — which remained its core offering — the company exited the S&P 500 in December 2010.

Just two years later, the once-mighty global innovator filed for bankruptcy, selling its remaining patents to a group of companies including Apple, Amazon and Google — that is, the self-same companies that helped popularise the technology that unpicked its business model. Today, the Kodak brand lives on, emblazoned on everything from inkjet cartridges to a cryptocurrency offering, but the company is a shadow of its former self.

Observes Rajan: “It’s not just the Kodaks of this world, though. Think of Nokia handsets or Blockbuster video or Borders bookshops. In virtually every sector, the casualties of innovation are legion. You only need to look at the ubiquity of a company like Amazon — and the scale of its ambitions — to understand where we might be heading next.”

But perhaps complacency in the face of technological change is understandable?

Lale Akoner, market strategist, BNY Mellon Investment Management, describes how many businesses fail to react in the face of innovation until it is too late due to a lag in time from when the new technology is announced and when the impact of that technology is ultimately felt.

“Many companies fail to respond because of overpride in their original products and lack of willingness to change. They also seem to miscalculate the true potential and may be slow to invest in a new technology until they see tangible business results, hence missing the first mover’s advantage. For instance, 3D printing was announced years ago but it’s only now that we’re starting to see the way it’s changed the healthcare, construction and automotive sectors, and potentially many other sectors in the future” she explains.

So, how should investors respond? In creating the BNY Mellon Investment Management Future 2024 report, Rajan interviewed a global set of leading asset allocators probing their response to the challenge of technological change.

Observes Rajan: “A key finding was how interview participants are adopting a more pragmatic approach to the old adage — that ‘time in’ the market matters more than ‘timing’ the market. They are resorting to one or more of three options: greater reliance on passive investing that gives ready liquidity; a stronger focus on high-conviction investing centred on smaller positions backed by a strong stewardship role; and private equity investing that provides exposure to turnaround companies.”

Akoner takes a similar view: to take advantage of disruption brought about by new technology, she says, investors not only need to think about whether a certain technology has potential to disrupt the industry, but also they must be able judge the second-order long-term effects of a disruption.

The technology sector involves special risks, such as the faster rate of change and obsolescence of technological advances, and has been among the most volatile sectors of the stock market.

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