



**The Year Ahead 2016**

# Catching the Digital Wave

*Jan 15, 2016* | **DOMINIC BARTON**

NEW YORK – Technological change has always posed a challenge for companies. But, as we saw once again in 2015, it has never occurred as rapidly, or on as large a scale, as today. As innovation sweeps across virtually every sector, from heavy industry to services, it is transforming the competitive landscape, with the most advanced companies – rather than the largest or most established players – coming out on top.

For incumbents, the threat of displacement is very real. The average tenure of a company on the S&P 500 has fallen from 90 years in 1935 to less than 18 years today. Disruptive new players like Uber, which has upended the taxi industry, are tough competitors, often staking out market share by shifting more surplus to consumers. This is part of a broader trend of intensifying competition that, according to recent research from the McKinsey Global Institute, could reduce the global after-tax profit pool from almost 10% of global GDP today to its 1980 level of about 7.9% within a decade.

The effect of technology on competition arises largely from the power of digital platforms and network effects. New digital platforms reduce marginal costs (the cost of producing additional units of a good or service) to nearly zero. Adding, say, a Google Maps user carries negligible costs, because the service relies on GPS location data that is already stored on a user's phone. This allows Google to scale incredibly quickly, and then to leverage this scale (and the convenience of having a single platform) to move into adjacent sectors – such as music (Google Play), payment (Google Wallet), and word processing (Google Docs). In this manner, tech firms can quickly come to challenge incumbents in seemingly unrelated industries.

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