

The CEO Forum

Special Edition on **Transformational CEOs**

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Former CEO
Sprint



Terry Jones
Founding CEO
Travelocity.com



Jim McCann
Founding CEO
1-800-Flowers

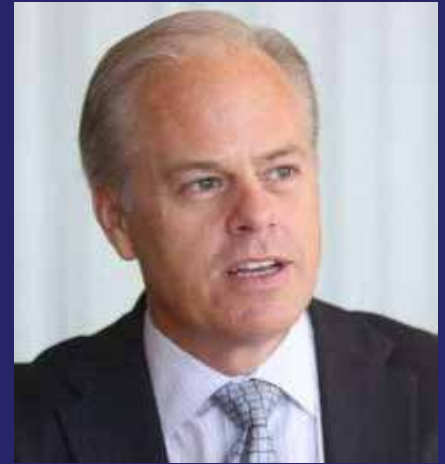
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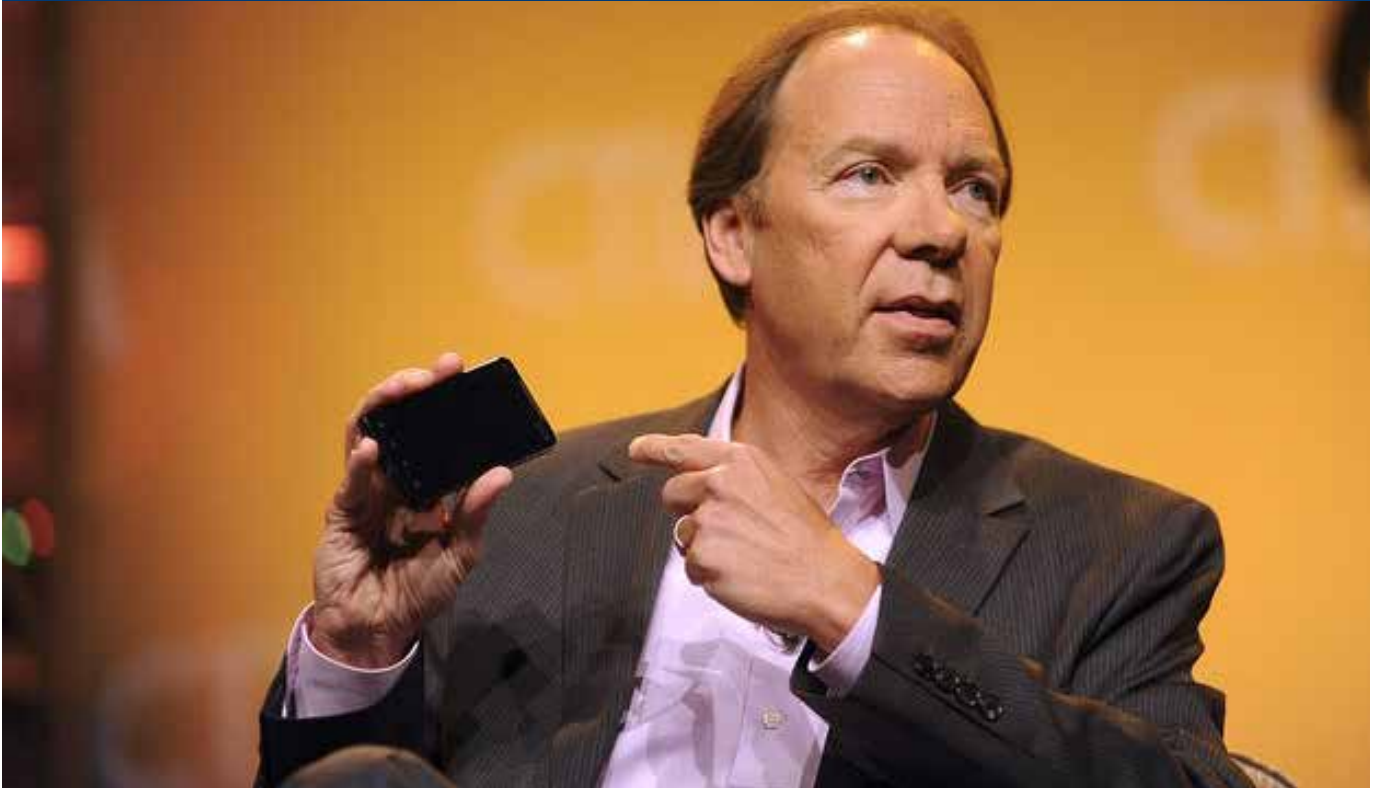
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President & CEO
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Jack Mitchell
Chairman
Mitchell Stores



Mike Gregoire
CEO
CA Technologies



“The real game-changers I learned about early on were time shifting, place shifting, and the power of creative destruction.”

Robert Reiss: Prior to becoming CEO of Sprint, you were CEO of AT&T Wireless and witnessed first-hand the formative years of digital. Can you share some inside-the-scenes historical perspective?

Dan Hesse: You mentioned AT&T. It was back in the early 80’s and our main business back then was voice telephony. That was the core business – remember “reach out and touch someone?” But during that period, we were given two new technologies to start using ourselves. One was email. This was long before the internet – an “intranet” called AT&T Mail. The second was voicemail, but not from the point of view of you call somebody, miss them, and get their answering machine. The primary new application of voicemail was allowing the user to record a message and send it through the network. These new applications were moving us away from analog, using digital bits, both email and voicemail, to disrupt the core business. The first big “aha moment” was the ability to shift time. If I wanted to send somebody a message at midnight or 1 o’clock in the morning, I didn’t have to worry about waking them up. I could send and receive messages whenever I wanted to.

Time shifting is now a big deal in all types of media. For example, it has changed cable television. If you have a

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DVR or you get your programs over the internet or over-the-top, you watch when you want to watch. You create your viewing schedule, not the schedule of the TV networks. But what was so instructive for me very early in my career was the notion of “creative destruction.” Our primary business was real-time voice telephone calls. We were coming up with new concepts that were going to compete directly with the core business.

What made these time shifting tools even more useful was mobility, where place, which had been so important in our landline world, lost relevancy. As soon as I got a car phone in the mid-80s, I learned how much more powerful voicemail could be because place was no longer important. I used voicemail to send and receive messages, while in my car (hands free, of course!). It used to be time and place were critically important. Now, time wasn’t important and with mobile phones, place wasn’t important either. The real game-changers I learned about early on were time shifting, place shifting, and the power of creative destruction.

Ganesh Ayyar: What was your personal experience going through this pioneer phase of transformation?

A lot of people forget just how innovative AT&T was as a company back then. These were the days when Bell Labs was the most preeminent research organization, public or private, in the world. I was a young product manager on a product called INWATS and I had a small team from Bell Labs assigned to me to work with me. Back then, there were payphones everywhere, at every gas station, at every intersection. INWATS was basically for truckers or for transportation companies where drivers go to a phone booth to call dispatch, but they would need exact change to make the call. INWATS was a toll-free number product for trucking companies, a small, niche business.

We decided to do market research to see if there might be new applications we should put into the next “generic” soft-

ware load into AT&T’s long distance switches, the 4ESS. The market research showed that if we created the capability to make customized numbers, like 800-FLOWERS or 800-CARRENT for example, or shift calls to different locations or call centers depending on the time of day, for instance in the morning, calls could go to the east coast, in the afternoon, to the west coast, we might create a brand new business. So we changed the name of INWATS and created something very different, “Enhanced 800 Service.” We developed many telemarketing programs around these new 4ESS features, sold the new “telemarketing” concepts to American businesses, and the old INWATS went from insignificant revenues for the giant AT&T to where the newly-created 800 Service represented almost half the long distance traffic on the network during the business day five years later. I had the opportunity to learn how to create, which was critical, because with a large market share, AT&T back then couldn’t grow by taking share from competitors.

Let’s fast forward a few years later. It’s the end of 1995. We’re getting ready at AT&T for something called Trivestiture. I remember getting a call, “Dan, we’d like you to launch this new business. It’s called the internet and there’s a lot of debate on whether it’s going to be a big thing or not.” A nickname I was given at headquarters once I started this new job was Rubber Ducky (a nickname in a hit song about the Citizen’s Band Radio) because the CB Radio was a well-known example of a “fad of the year” that had faded, and lots of people at AT&T thought the internet was going to fade. But when we were doing the business case for the internet, we realized that our objective on 800 Service was to have the 800 number at the bottom of every ad for every company, as the front door of that company, but that when we launched the internet business, the internet address or URL, www.hilton.com for example instead of 800-HILTONS, could take a huge chunk out of the 800 business and potentially destroy what had become a large and profitable business.

A few years earlier, at divestiture, I had been asked to

take a look at how we might change a business that we dominated, enterprise private line networks controlled by high-end AT&T PBX's. I was on the development team for the "Software Defined Network" with a lot of Bell Labs folks again, and I ended up selling the very first Software Defined Network, or SDN, I believe the world's first virtual private network, or VPN, to the Exxon Corporation. We put key capabilities of the PBX up in the "cloud." Virtual networks and cloud computing are taken for granted now, but in 1984, this was ground-breaking. The PBX became far less important, as did private lines. I learned that if you want to be at the leading edge, to be a true leader in a technology business, you had to be willing to destroy your existing business.

I was the guest speaker at a reunion of former AT&T executives, asked to talk about my career at AT&T, and one of the people in the group said, "I remember when you got up to give the pitch at the senior leadership group about Digital One Rate." At the time, I was CEO of AT&T Wireless, and wireless was also a new business for AT&T with the recent acquisition of McCaw Cellular. AT&T Wireless made its largest margins on two businesses: roaming and long distance.

Digital One Rate (DOR), which eliminated roaming and long distance fees, should not only put our profitability at risk, but as I was reminded at that recent meeting of

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former AT&T colleagues, AT&T was particularly concerned with what "DOR" would do to the calling card business. Back in 1998, if you went to any airport, there were lines of payphones as far as the eye could see and lines of people waiting to make calls on those payphones with their AT&T calling cards. Later, they would go to their hotel rooms and they would use their AT&T calling card as few took their mobile phone on the road because long distance charges and roaming charges were so complex and exorbitant. Digital One Rate transformed the way that business travellers communicated. When I talk

to people who were in the wireless industry in 1998, almost everybody remembers where they were when they heard about Digital One Rate. It was that radical.

I had the opportunity to learn about and apply creative destruction so many times at AT&T. Learning how to create a business is vital. At AT&T when I started, we had 80% or 90% market share. You couldn't grow by taking someone else's customers. We had them already. We had to create brand new businesses. I am so fortunate to have been given the opportunity and the support to do that.

Reiss: This creative destruction was really business cannibalization, which for a leader is most often a challenge. What companies have you seen succeed in business cannibalism?

Many ask why more innovation doesn't come from big companies with money and intellectual property. It's because they have so much to lose -- the hesitancy to destroy the cash cow. That's why new companies often come in and do it. A great example of business cannibalism is Netflix, who came in and destroyed Blockbuster's bricks and mortar with mail-in DVDs. When Netflix owned the DVD mail business, you'd think they'd be on top of the world, however it was just the opposite. They realized where the competition in the future would come from, so they destroyed their very successful mail business by converting to a streaming model. They did it themselves, and that kind of creative destruction is called the "J-curve." At Sprint, I had the opportunity to also apply it later on.

After about four years at Sprint we had become the fastest growing brand among the major US wireless carriers in terms of net subscriber growth rate. We were number one in customer satisfaction. We offered the first unlimited plan which was very successful. Things were going very well, but our weakness was our network. We had a kludgy network as the company had formed from three different companies coming together: Sprint, Nextel and Clearwater. We had three separate, incompatible networks. So we started thinking "How can we turn this weakness into a strength?" The best way was to destroy all three networks: pull the plug, replace every nut, bolt, screw, and wire. It would be a transformation like Netflix's when they moved from mail to streaming. One

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needs to be ready for the business to go down for a while before it comes up, a curve shaped like the letter ‘J.’”

We realized that if we ripped everything out of the network, it was going to disrupt customer service. It was going to disrupt the network customer experience because you can’t do it without any perceivable impact. There was no playbook. No one had done what we were attempting that we could learn from. We believed we could create something special if we got rid of three networks and built one network optimized to take advantage of the low-band spectrum from Nextel, the mid-band from Sprint, and the high-band spectrum from Clearwater, and add in emerging technologies like MIMO and carrier aggregation.

We endured two and a half years of network service disruptions, and resulting subscriber challenges, as we made these massive changes to the network, but once we were done, we had a fantastic network, crucial to growing in the future. The willingness to “destroy” a current way of doing things and create something entirely new might be required at times to grow in the future.

Reiss: The remarkable thing about the Sprint creative destructive turnaround was not only did you become number one in customer service ratings, but you were the S&P #1 performing stock for your last two calendar years as Sprint CEO ... right ahead of Netflix, coincidentally. When you look at the future of the digital revolution, what



did you see happening?

I think our current digital revolution is the most impactful change in the history of mankind. Wireless is the most rapidly adopted technology in history, and the digital transformation is driven by the mobile internet.

Historically, if you look at national economies, every ten points of mobile penetration – like going from 60% of the people having mobile phones to 70%, that ten points of penetration yields about a half a percentage point or more of GDP growth. In the U.S., a Recon Analytics study concluded that in the last ten years, \$1.5 trillion has been added to U.S. GDP from the productivity resulting from the mobile internet. A digital divide between nations still exists. North America has almost half of the 4G connections in the world and only about 10% of the wireless users, but that disparity should improve. From an environmental perspective, a lot of e-waste, electronic waste, has been created in the U.S. each year to fill up a line of dump trucks bumper to bumper from Washington D.C. to Orlando. But, on the other hand, mobile phones take many things out of landfills because one smartphone could replace your TV, your computer, your flashlight, your camera, your music player, your handheld GPS device and more.

In terms of education, it used to be if you wanted to take special classes like an advanced placement class, you had to go to a large high school or top-notch private high school. Now with online alternatives like Khan Acade-

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my, you can be anywhere in the country or the world and have access to the best educational resources.

Regarding safety, these devices contribute to distracted driving accidents, but on the other hand, smartphones increase safety too. You can dial 911 anywhere, smartphones can locate your children if they carry phones, they provide helpful warnings and instructions during natural disasters, and they’re very helpful to first responders.

The societal impact of the mobile internet has been massive. An Elon University study concluded that a young, digital generation is growing up with something they call “fast-twitch wiring.” On the positive side, they’re fast-acting multi-taskers. They find it hard to “relax” or do just one thing. If you watch young people watch television, they’re likely on their smartphone at the same time. They also can be decisive. That’s positive from a productivity point of view. On the other hand, Elon found less deep thought and reflection, plus a need for instant gratification. This generation can be almost addicted to their device. It’s been called FOMO, fear of missing out.

In my view, perhaps the greatest societal benefit from the mobile internet will come as we age. There’s speech to text for the hard of hearing, text to speech for those with trouble seeing, self-driving cars, personal assistants with artificial intelligence, robots, social networking which allows us to stay connected as we age, and some will use crowd-sourcing techniques to tap the vast reservoir of experience of our retired workforce, which might also give the aging a greater purpose in life. We’ll be able to live independently longer. There are some negatives from the societal changes coming as a result of the mobile internet, but more pluses than minuses.

Ayyar: What advice would you give to a CEO who has successfully run an analog business to be successful in the digital world?

Number one, and it’s hard to do with Wall Street the way it is today and the pressure on the short term, is to take the long term view and to look around the corner. If you’re just focused on the next quarter, your traditional competitors, or new competitors you’re not paying attention to, may change the playing field. Change could come from new technologies or applications not widely used now, like virtual reality. Look ahead, not down, and be willing to creatively destruct. As I was describing with respect to Sprint, the J-curve comes with short term pain before the long term gain.

Number two is delegate. To keep up with the information deluge and constant change, all your people have to be alert, involved and engaged. A company moves as fast as the number of decisions that are made everyday, which is directly related to the number of decision makers that you have, so you need to delegate.

Continuous learning is incredibly important and more important than ever. We would travel as a senior team at Sprint regularly to Silicon Valley to meet with angel investors, leading private equity funds and start-ups to keep our finger on the pulse of innovation. We would immerse ourselves in courses at Singularity University where we would learn about 3D printing, robotics, artificial intelligence, and machine learning, fields that may not be “core” to our business today but have the potential to transform or grow our business.

Finally, build a culture focused on innovation. We celebrated innovation, and had a language about new ideas.

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Dan Hesse currently serves as a member of the board of directors of PNC Financial Services Group, Inc. (NYSE: PNC) and Akamai Technologies (NASDAQ: AKAM). Dan served as President and CEO of Sprint Corporation from December 2007 to August 2014. Previously, Hesse was the Chairman and CEO of Embarq Corporation, a \$6 billion telecommunications services company. From 2000 - 2004, he served as Chairman, President and CEO of Terabeam Corporation, a wireless telecommunications technology company. Hesse spent 23 years at AT&T. From 1997 - 2000, he served as the President and CEO of AT&T Wireless Services, at the time the United States' largest wireless carrier. He served as a member of the board of directors of VF Corporation from 1999-2008 and of Nokia from 2005-2007. He received a BA from Notre Dame, an MBA from Cornell, and an MS from MIT where he was awarded the Brooks Thesis Prize.

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We called them “nukes.” We celebrated patents. In my last two years at Sprint, we were being granted on average of over two U.S. patents every business day. Ingrain innovation and creativity in your culture.

Reiss: Dan, we’re going to do our rapid fire segment. I’ll say a word and you give a one word answer.

Virtual reality. Immersive.

Digital revolution. Mobile enabled.

Digital 2050. What’s the difference between real and not real?

Culture. Eats strategy for breakfast.

Customer. Never forget your people are your internal customers.

Thank you for sharing this historic perspective with us.

In addition to receiving Corporate Responsibility magazine’s Lifetime Achievement Award, he has been named “Most Influential Person in Mobile Technology” by LAPTOP magazine (Steve Jobs was #2), Wireless Industry “Person of the Year” by RCR magazine, “Executive of the Year” by Wireless Business and Technology magazine, “CEO of the Year” by the National Eagle Leadership Institute, “Kansas City’s Best CEO” in a readership poll by Ingram’s Magazine, one of the five “Best Turnaround CEO’s of All Time” by Fierce Wireless, one of “10 Inspirational Leaders who Turned Around Their Companies” by Entrepreneur magazine, and he has twice received Wireless Week magazine’s Leadership Award. Glassdoor consistently named Hesse one of America’s highest rated CEO’s by employees. Hesse received the American India Foundation’s award for excellence in corporate leadership and philanthropy. He serves on the National Board of Governors of the Boys & Girls Clubs of America, the board of directors of the JUST Capital Foundation, and on the advisory boards of the New York Global Leaders Dialogue and of Rutberg and Company.

The 2014 American Customer Satisfaction Index recognized Sprint as the most improved U.S. company in overall customer satisfaction, across all 43 industries, over the previous six years. During Dan’s years at Sprint, the company was recognized 20 times by J.D. Power and Associates for excellence in customer service. For his last two full calendar years as CEO, Sprint’s Total Shareholder Return (assuming reinvested dividends) ranked #1 among all S&P 500 companies.