A.T. KEARNEY

The A.T. Kearney Strategy Chessboard

A broader perspective on strategy development and formulation



For the past four decades, we have seen a staggering number of strategic schools of thought and frameworks. The 1980s were dominated by Michael Porter's thinking, the 1990s had multiple contributors (Prahalad and Hamel stand out in *Competing for the Future*), and the early 2000s saw noteworthy contributions from Kim and Mauborgne in *Blue Ocean Strategy* and Deans, Kröger and Zeisel in *Winning the Merger Endgame*. At the same time, the Santa Fe Institute has contributed valuable insights on the economy as a "complex adaptive system" and its associated strategy implications.

Dozens of schools and frameworks claim to be the most widely applicable and useful for strategy development. The question is, are these strategy schools universally applicable or can they complement one another?

Based on our extensive work in strategy development we have concluded the latter. With this in mind, the A.T. Kearney Strategy Chessboard was designed to help corporate leaders select the right starting point for strategy development and formulation.

This paper does the following:

- Challenges two common but often flawed assumptions: that industries are predictable and that a company's primary focus is adapting its positioning
- Lays out the Strategy Chessboard and its use of industry predictability, while discussing companies' willingness to adapt to or shape an industry
- Outlines how to use the Strategy Chessboard in strategy development

Predictability Versus Adapting and Shaping

Early schools of thought were commonly based on two assumptions about strategy development: first, that an industry is predictable, and second, that a company's primary strategic challenge is to adapt successfully to that industry for maximum competitive advantage. Many companies and managers today root their strategies in these two assumptions.

These assumptions are being challenged, however. The Santa Fe Institute's recent work with complexity theory argues that industry predictability, meaning the ability to forecast an industry over the medium and long term, is not guaranteed. Forecast confidence can rise and fall—whether in terms of market size, regulation, technology development, business models, competitors' moves or macroeconomics—and can have a major impact on strategy development.

The Santa Fe Institute argues that economists in the early twentieth century who emphasized

deterministic and equilibrium-based systems were using the wrong science analogies. Rather, the economy is more like a complex adaptive system—dynamic, non-linear, rarely at equilibrium, and populated by agents that use inductive reasoning to draw generalized conclusions and that learn and adapt over time in a co-evolutionary manner. These complex adaptive systems are, by definition, unpredictable at the local, granular level. However, global patterns may be predictable, and certain periods of time may prove more stable.

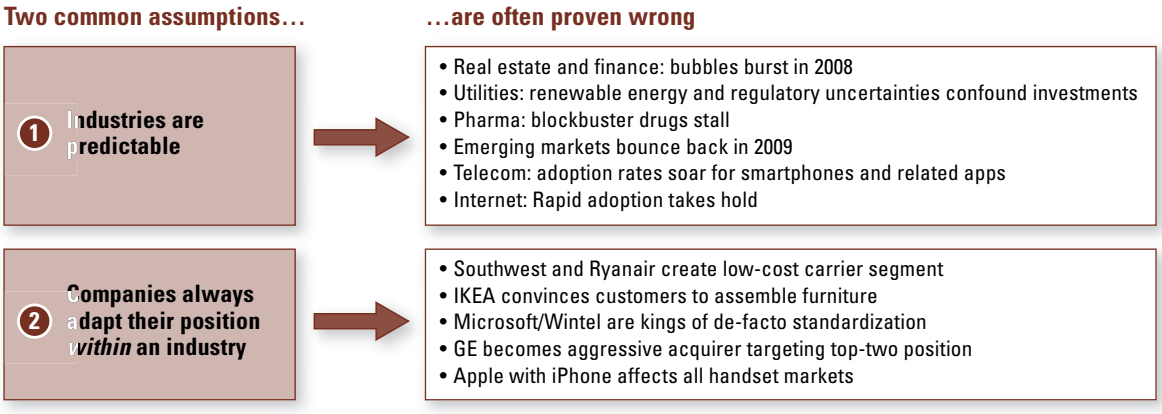
Considering the sheer size and vast complexity of the modern economy, an economic model (even focused on one industry) will never fully explain all of the characteristics and dynamics of the "real world" at any given time, as the model inherently will be a simplification. Specifically, the above model paradigms have different views about predictability. Based on real-life experience, our conclusion is that some industries at some time intervals are reasonably predictable, in line with the spirit of the 20th century science-based models, while other industries at certain time intervals are extremely hard to predict at the granular level as described in models based on complex adaptive systems. With this in mind, an effective strategy framework must include the level of industry predictability as a main dimension.

The top half of figure 1 highlights some major events that were arguably difficult or even impossible to predict: the growth rate of smartphone technologies; the impact of "green" technologies on the utilities industry; the dramatic impact of collateralized debt obligations (CDOs) and other new financial instruments on the banking industry. These events underscore the challenge of predicting an industry's future development, particularly as globalization, increasingly rapid technology cycles and consumer fads only increase volatility.

This does not mean that all industries are always highly uncertain—many can be analyzed to generate predictions accurate and granular enough for classic strategic decision making. Examining projects A.T. Kearney has participated in during the past decade, strategic predictability was achievable in a majority of the cases. The trick

Figure 1

Two common "mis-assumptions" impede strategists



Source: A.T. Kearney analysis

is to determine early during the strategy development processes whether your industry will undergo *evolutionary* or *revolutionary* change in the coming years. A revolutionary, or unpredictable, environment clearly requires a different strategic approach than an evolutionary one. In revolutionary environments, some leading companies challenge the assumptions and shape their industry to their advantage, rather than adapt to the current competitive environment. One company's actions in shaping the competitive environment may have an impact on all other players.

Rarely do the biggest corporate growth success stories rely on reactive acceptance of (and adaptation to) current industry developments—especially in more revolutionary environments. Instead, leading firms challenge industry assumptions and shape them to their own advantage—and perhaps to the overall industry's advantage. For example, Netflix usurped Blockbuster's dominance in the movie-rental industry nearly overnight, while Apple was the first to put all the pieces together in the twenty-first century digital music business and took a commanding lead in a new market structure. Amazon's revolutionary Kindle created a new e-reader market andleft many rivals in a wide range of industries—from book sellers to consumer electronics makers—scrambling to catch up.

Consolidation, enforcing better conduct by customers and competitors, deconstructing value chains, and redesigning business models are all ways to shape an industry to one's long-term advantage, and can be done with some precision in a predictable industry. Being an industry "shaper" is particularly important in highly dynamic and uncertain environments. By building acceptance among critical customers and stakeholders and developing the necessary technology base, infrastructure and key competencies, many companies have more shaping power than they realize—something that could create a huge competitive advantage. An attractive aspect of complex adaptive systems and their sensitivity to the "initial condition" is that small changes upfront can have a large impact at the end. This underscores the possibilities that shaping strategies have for future development. However, correctly estimating the consequences of actions is a true challenge. Shaping strategies are often perceived as somewhat riskier, meaning that new entrants with little to lose are usually more willing to execute them than incumbents.

As strategy development begins, the two main tasks are conducting an honest, critical assessment of the industry's predictability, and articulating whether the company intends to adapt its position within the industry or to shape the industry.

Two Dimensions, Four Approaches

Devising adaptation strategies for predictable industries is a traditional comfort zone in strategy development. But as noted earlier, predictability differs significantly over time and among industries. At the same time, not every company has the right DNA—desire, need and ability—to shape its industry's overall development.

Combining predictability and a company's DNA to adapt or shape results in mapping four distinct "umbrella strategies" and strategic approaches *(see figure 2 on page 4)*.

Position and conquer.

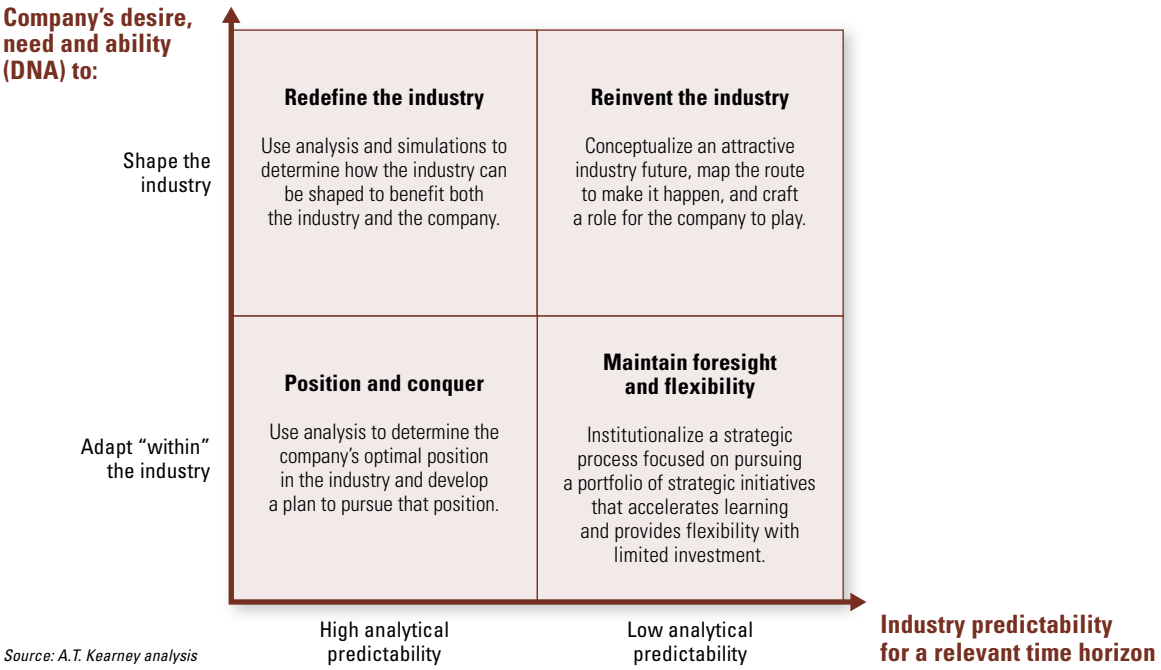
Strategic analysis helps determine what industry position a company should pursue and how to outmaneuver competition to grow at a faster-than-market rate. This is a classic approach to strategy development.

Within this quadrant, companies typically have the following strategic options as they adapt in a predictable industry:

Position to build competitive advantage. Identify and capture a leadership position in the

Figure 2

Two dimensions, four "umbrella strategies" and strategic approaches



Source: A.T. Kearney analysis

industry, or an attractive niche. The most influential contributor in the position and conquer area has been Michael Porter, whose book *Competitive Strategy* focuses on positioning for competitive advantage.

Deploy battle strategies. Increase market share through tactics inspired by battle strategies. Military strategy is often used to meet the competitive challenge; Sun Tzu, for example, has inspired many corporate strategists.

Grow in core, adjacent businesses and step out. Move into businesses adjacent to the core, or pursue step-out strategies (often leading back to the first two options). Growing the core business is a natural move for any company, as is seeking expansion in adjacent areas with excellent chance for success.

Identify and adapt to profit patterns. Adapt to capture emerging profit opportunities in new areas. Anticipating shifts in industry profit patterns will also guide a company in effectively adapting to new opportunities. Adrian Slywotzky has authored several books on profit opportunities and outlined how to identify and capture "pockets of profitability" in a competitive environment.

Why are these four options used the most? Because they help companies decide the best strategic moves to use to adapt to a predictable industry without bringing major industry change. Companies in this quadrant seek attractive, easily defensible strategic positions along with well-designed battle strategies that best grow relative market share.

Redefine the industry. Through analyses and simulations, companies in predictable environments can shape their industries to their own benefit and possibly that of the entire industry. In this approach, the company becomes an indus-

try architect that redraws the structure, boundaries, conduct and performance of the industry in a favorable direction and captures a leading role in its future.

The four main dimensions of redefining the industry are:

Pursue global industry endgame consolidation. Seek to consolidate the industry through mergers and acquisitions (M&A)—first regionally, then globally. Actions taken by one company will typically spur its main competitors to follow suit, further accelerating the pace of consolidation.

Through extensive research, Deans, Kröger and Zeisel have shown natural consolidation patterns in industries and how an ambitious M&A agenda can reshape the industry structure to a company's advantage. For example, ArcelorMittal's pattern of acquisitions demonstrates how one company can act as a powerful industry architect.

Converge or slice the industry. Pursue attractive industry convergence opportunities. Again, one company's actions will likely trigger other players to act—within the industry and also in neighboring industries. Alternatively, effective "slicing" strategies can improve competitive positioning—for example, splitting up the information technology (IT) industry into hardware, software and services sub-industries, or Bloomberg's use of convergence and deconstruction to change the business news industry.

Change industry conduct. Alter the way the industry conducts business in a direction favorable to one company. Well-conceived game theory strategies will broadly impact all PARTS—short for players, added value, rules, tactics and scope—and mold their conduct into something more beneficial for all members.

Reconfigure industry value chains. Redefine what is core and non-core in an industry. As suggested by Aurik and Willen in their book, *Rebuilding the Corporate Genome*, reconfiguring value chains also affects how an industry works. This will allow new third parties to enter the market, new ways to collaborate with competitors and customers, and new moves by competitors.

Why these options not others? If you seek to challenge and shape an industry, these four avenues are the most common. Aggressive industry M&A creates a consolidated playing field with typically higher return levels while also spurring globalization of the industry. Industries can converge both in terms of supply and demand, and from a product and technology perspective. Shaping convergence trends to your advantage is a critical task, often pursued using alliances and joint ventures for risk-mitigating shaping. Changing industry conduct—introducing more win-win situations—will significantly impact industry profitability. Reconfiguring industry value chains in an innovative manner can create a distinctively different industry landscape with new opportunities.

Reinvent the industry. If predictability is low, a useful goal for many companies is to reinvent the industry to gain advantage, reduce or off-load risk, or create new capabilities and resources. Uncertainty makes prediction difficult, but it also opens up significant opportunities for visionary leaders to guide others in a favorable direction. Companies in this quadrant often have powerful imaginations; they're able to develop both an attractive future vision and a shaping agenda to increase the likelihood the industry moves toward this vision.

The four strategies in this quadrant include:

Create and pursue a preferred future. Launch big initiatives complemented with smartly focused initiatives to shape an unpredictable industry. Scenarios are often used as a basis for crafting an attractive preferred industry future. Execution then focuses on ways to increase the likelihood the industry will develop in that direction.

In their book *Competing for the Future*, Prahalad and Hamel envision and argue for new value propositions, new technologies and new capabilities; we believe their thinking is in line with how we have worked with clients to find a preferred future, mobilize, and get there first.

Create Blue Ocean opportunities. Develop innovative, attractive customer value propositions that open up new market spaces. *Blue Ocean Strategy*, written by Kim and Mauborgne, outlines approaches for developing new and more innovative value propositions.

Think big and lateral. Use creativity and big thinking to develop out-of-the-box strategies to transform an industry. In his book *Big Think Strategy,* Bernd Schmitt introduces new ways to create such transformational strategies.

Cross the chasm with innovative products. Apply smart ecosystem building and vertical market segmentation, and initiate return dynamics to capture new market opportunities. In his books *Crossing the Chasm*, *Inside the Tornado* and *Dealing with Darwin*, Geoffrey Moore outlines strategies to get the mass market to embrace innovative products used by leading-edge adopters.

Why these strategies and not others? If you choose to shape your industry amid a high degree of uncertainty, then various adaptation strategies are no longer applicable while you are hesitant about the more aggressive strategies of the "redefine the industry" section. Here, visionary and imaginative leaders will seize the advantage.

Maintain foresight and flexibility. For companies unwilling or unable to reshape an industry, the key is to institutionalize a strategic process that accelerates learning across the company, while pursuing a portfolio of strategic initiatives that offer flexibility with limited investment. The company may encourage strategic experimentations in order to prepare for different futures.

The four main strategies within this area are:

Prepare for multiple scenarios. Develop alternative scenarios about the future to gain a better understanding of potential development needs, and to prepare a broad set of strategy options. Our clients frequently request scenario development—well-known because of the pioneering work of Royal Dutch Shell—as an effective means of preparing for uncertain or risky industry futures.

Deploy real options-based strategies. Evaluate strategies as real options for business models, capacity and markets to add a financial perspective on dealing with uncertainty. Such methods are frequently used for long-term, big-investment situations (for example, for utilities or large-capacity manufacturing plants).

Pursue dynamic strategies. Revisit the assumptions and premises of your current strategy. Several schools of thought about "dynamic strategy" stress the importance of frequent and flexible strategic planning, such as in *Fast Strategy* by Doz and Kosonen.

Implement an evolutionary strategic process. Use an evolutionary approach that emphasizes fast learning and adaptation, based on a broad base of experiments. Several important strategy contributions have been made to the evolutionary field, such as Eric Beinhocker's book *The Origin of Wealth*.

Why these strategies and not others? These strategies are best for dealing with unpredictable situations—when position-and-conquer moves prove too risky. When major growth investments in core and adjacent businesses cannot hold up to the uncertainty, companies may instead benefit from flexible and risk-mitigating strategic approaches. It is often wise to focus on learning and preparing for different possibilities while ensuring that the company can adapt quickly—and cost-effectively—once the future becomes clearer. The ability to conduct the right ventures and quickly realize what works and what doesn't is crucial to success.

The Strategy Chessboard

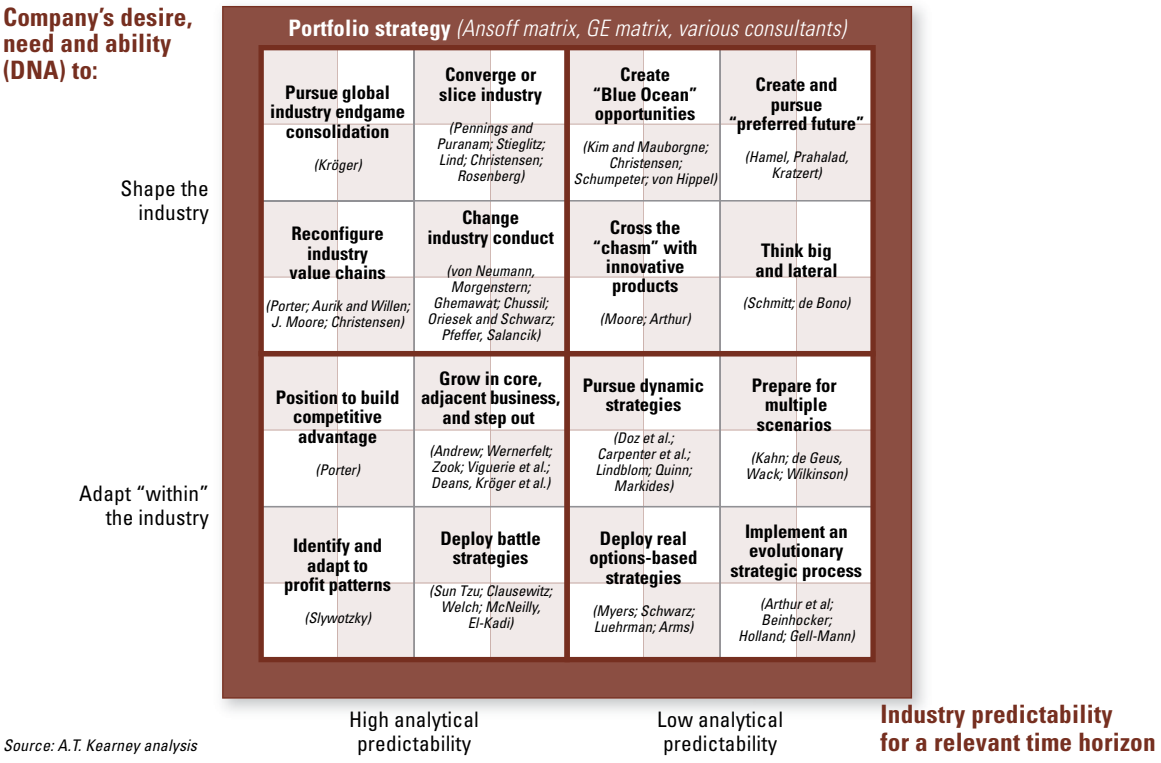
The strategic options listed in this paper—along with the portfolio strategy that is applicable in most situations—combine to make the A.T. Kearney Strategy Chessboard *(see figure 3).*

In creating the Strategy Chessboard we selected what we consider the most useful and complementary strategy schools of thought, based on our work with clients. We excluded more general leadership schools of thought, including In Search of Excellence, Built to Last, From Good to Great, and the Learning Organization, as these are more about identifying leading management practices. When deciding during a strategy-development exercise which strategy schools to apply, nothing is black-and-white. A clear choice tends to emerge, however, based on a company's DNA and the predictability of its industry. Remember that schools of thought are not completely mutually exclusive; those selected should provide a complementary and valuable strategic perspective.

The maturity and scientific depth differs substantially across the schools, with Michael Porter's *Competitive Strategy* likely being the most comprehensive and best-known school. Again, schools were selected based on how well a company could create a complementary portfolio of schools for its strategic development and formulation. We believe that most of the strategy schools are familiar to our readers, but the appendix on page 14 includes a short summary of the 17 discussed in this paper.

Figure 3

The A.T. Kearney Strategy Chessboard



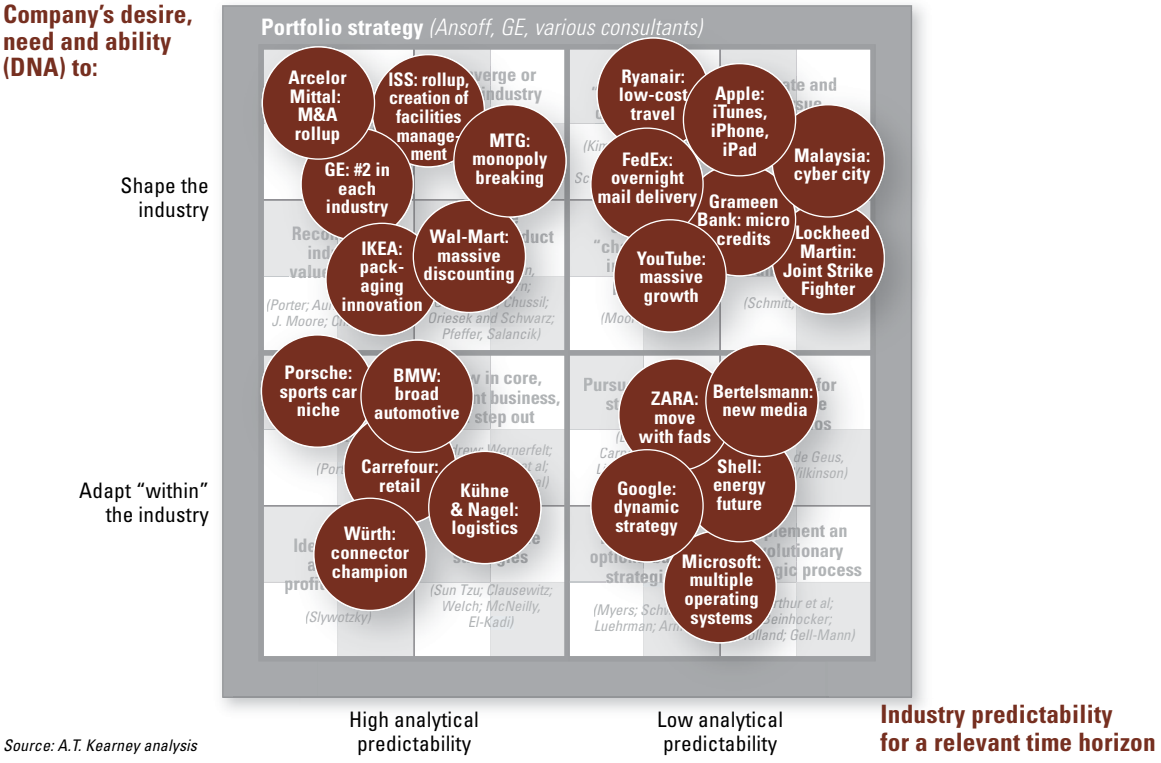
Source: A.T. Kearney analysis

The creators of individual schools of thought and strategic theories may argue that their ideas are more broadly applicable and should not appear as a mere square on the Strategy Chessboard. While such claims have merit, the chessboard summarizes how these different schools of thought have proven useful in a wide sample of strategic projects, how they complement each other, and when they may prove most useful for a company based on its individual situation. The chessboard provides a multi-dimensional perspective on strategy development and addresses an important but rarely discussed element: the selection of strategic frameworks to be used for a particular effort.

Strategy development begins with identifying where on the two axes of the chessboard a company is located. Industry predictability is determined by a high-level first assessment of industry drivers, such as potential demand changes, new technologies and offerings, strategies for established and potential new competitors, supplier behavior, future environmental and regulatory impact, and a company's own actions. The company's DNA is determined by assessing a company's desires, needs (both positive and negative), and ability to shape its industry. This high-level analysis enables you to select the most appropriate quadrant. Selecting a specific strategy within a quadrant comes down to understanding a company's unique strategic situation. In this case, picking a strategy school is akin to selecting the right tools for a job.

Figure 4

Different strategic situations land in different quadrants on the chessboard



Source: A.T. Kearney analysis

Figure 4 illustrates several examples of different companies' strategies and how they might appear on the Strategy Chessboard *(see sidebar: Quadrant Examples)*.

It's worthwhile to keep in mind some typical industry evolution patterns to help determine in which quadrant you want to play. For example, in stable industries with low consolidation—those in which the concentration ratio for the top three companies (CR3) might be less than 20 percent—companies often launch aggressive M&A strategies to consolidate the industry and strengthen their own roles. If you suspect this, you would be wise to investigate your industry-shaping options. In industries with lackluster performance, competitors are surely conjuring ways to reinvent the industry, and rather than be left behind, you'll want to lead from the front. If you've survived one consolidation push, it's a good bet that your competitors are thinking up new ways to reinvent the industry. In this case, you can hedge your bets by identifying opportunities to reinvent your industry and shaping these to your advantage. If your industry's future is uncertain, then it is likely that a few major players will lead the industry in a new—and for them, preferred—direction. The question for you: Are you content with following and adapting to

Quadrant Examples

Each quadrant is different, yet the success stories show how each can deliver outstanding growth in the right situations.

Position and conquer. Perhaps half of all companies pursue strategies in this quadrant, which focuses on finding an attractive industry position and building a competitive advantage. Porsche is an excellent example—it has built global dominance in its customer and product segment, honing its competitive advantage to a level few competitors can reach. Its revenue grew at a compound annual growth rate (CAGR) of 13 percent from 1993 to 2010.

Redefine the industry. This quadrant offers plays to change the industry, either by altering the existing business model or pursuing M&A within and outside the industry. ISS reshaped the facility management by incorporating "integrated facility management" and pursuing M&A—its revenues grew at a16 percent CAGR from 1997 to 2009. ArcelorMittal used M&A to reshape the steel industry and securing it a lead position. IKEA's flat packaging innovation and its control from furniture production to retail significantly shaped the furniture industry landscape.

Reinvent the industry. The common theme here is imagination and courage—creating something novel and making it happen. In the 1960s, Kennedy's "man on the moon" vision overhauled the American space industry; 20 years later, Bill Gates vowed to put a "computer on every desk." Apple stands out today—its iPods, iTunes, iPhones and iPads reinvented many industries, from music distribution and mobile phones to PCs and books. Its net income has more than tripled from 2007 to 2010. Bangladesh's Grameen Bank (founded in 1976) reinvented the emerging market banking market with its focus on microcredit, women, no collateral requirement and other innovations that have now been exported to more than 60 emerging markets.

Maintain strategic flexibility. Leaders in this quadrant are ready to benefit from multiple potential outcomes. A prime example is Microsoft in the late 1980s, when it engaged in at least a half-dozen operating system initiatives to maintain strategic flexibility. Shell is well known for using scenario- and real-option-based approaches in the uncertain and costly area of exploration. It has seen its revenues grow 10 percent annually over the past 15 years. Google has deployed an effective dynamic exploration approach, using multiple, sometimes-competing business development initiatives to identify promising business opportunities and quickly increase the scale of the most promising.

their direction, or would you rather be among those leading your industry forward?

Once a starting point and umbrella strategy are determined, it doesn't mean all other schools of thought are ignored. Applying several different schools can often help generate additional strategic insights and options. A case in point is the approach by which companies develop alternative scenarios. Most shape-the-industry strategies can be used to create scenarios.

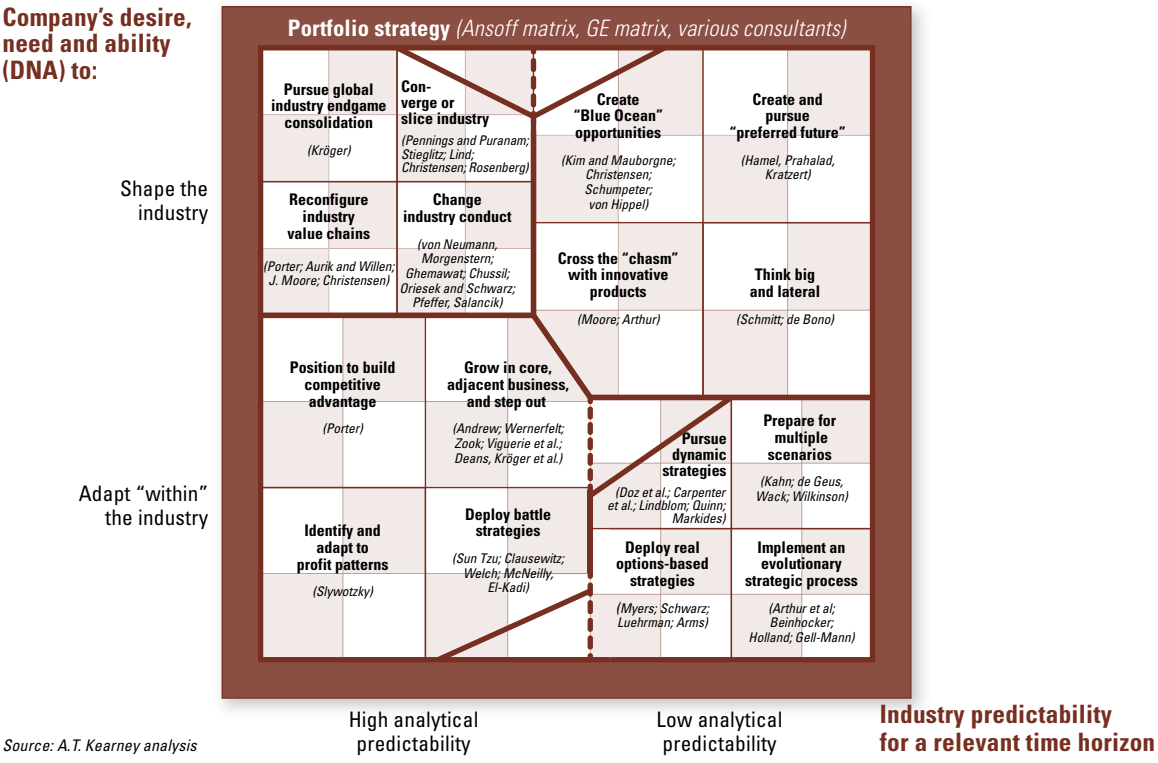
Redrawing the Chessboard

Observant readers will note a weak link between the two axes of the chessboard. To account for this relationship, we revised the Strategy Chessboard to become the playing field as outlined in figure 5.

For example, massive shaping strategies by one company could affect the predictability of an industry, if the company is influential enough. To capture this link, we can redraw the chessboard in such a way that the vertical midpoint between high and low predictability when selecting quadrants moves left when there is desire to shape an industry. Furthermore, to illustrate the typical distribution of industries with high versus low predictability, we can move the bottom half of the vertical line somewhat right. Additionally, we have found that in highly uncertain situations, the opportunity to shape an industry is usually too good to pass up, and companies should do whatever is necessary to influence industry development in the direction most beneficial to them.

Figure 5

A redrawn "strategic playing field" for hypothetical top-five players *Illustrative*



Source: A.T. Kearney analysis

Hence, the horizontal line between adapting and shaping should move to encourage shaping.

If your company is low on the vertical axis, then there will be a preference for being extremely adaptive, and schools related to maintaining foresight and flexibility will be more applicable. Also, at the end point of the adapt area, the need to stake out a clear direction and target position becomes stronger—meaning that even in uncertain industry environments, there is a preference to position and conquer. Lastly, at the top section of shaping, the willingness to shape could be so high that a company is prepared to reinvent the industry even when the industry is relatively stable. Alternatively, a company may seek to launch investment-heavy redefine-the-industry options, such as M&A, despite a high degree of industry uncertainty.

Still, while this new playing field may provide a better-calibrated perspective on which strategy to apply when, we suggest the standard Strategy Chessboard as a good starting point for strategic discussions.

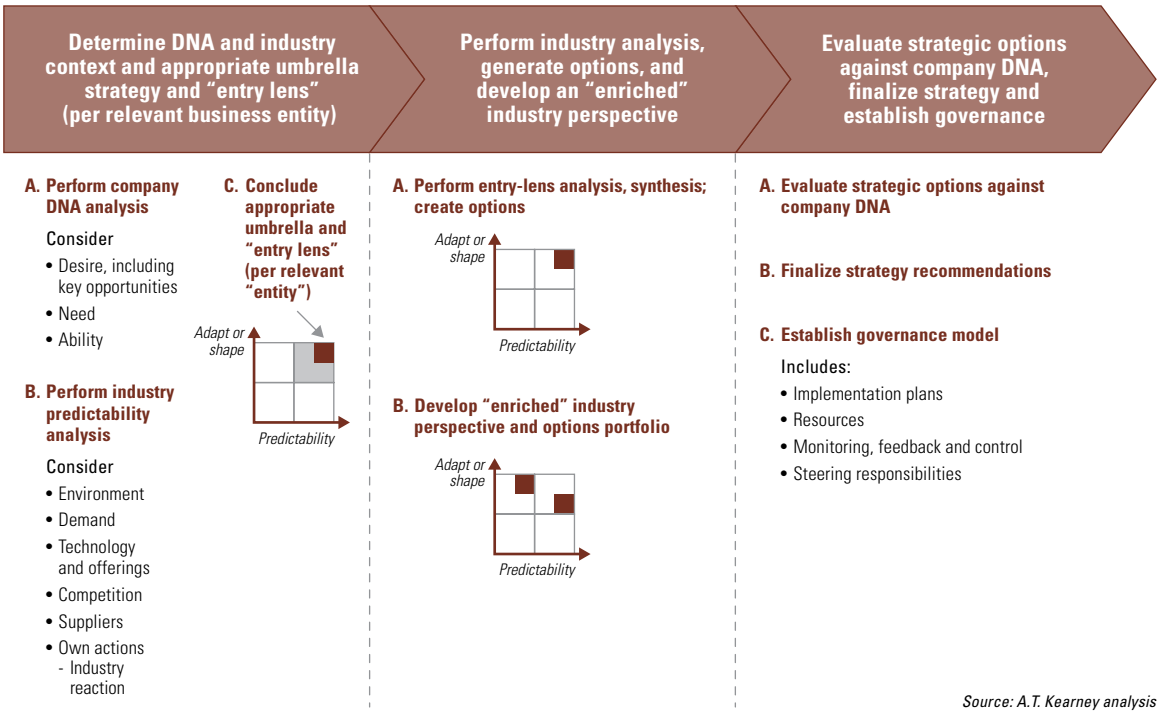
Avoiding Strategic Flaws

The Strategy Chessboard helps tackle three common flaws:

Strategic lens problem. Strategy development efforts can unintentionally be influenced by which "lens" companies use to analyze a strategy problem. A particular strategic framework will often predispose teams toward certain solutions. If a Porterian model suggests you can be a low-cost producer or a premium brand, you may find it difficult to consider more visionary strategies

Figure 6

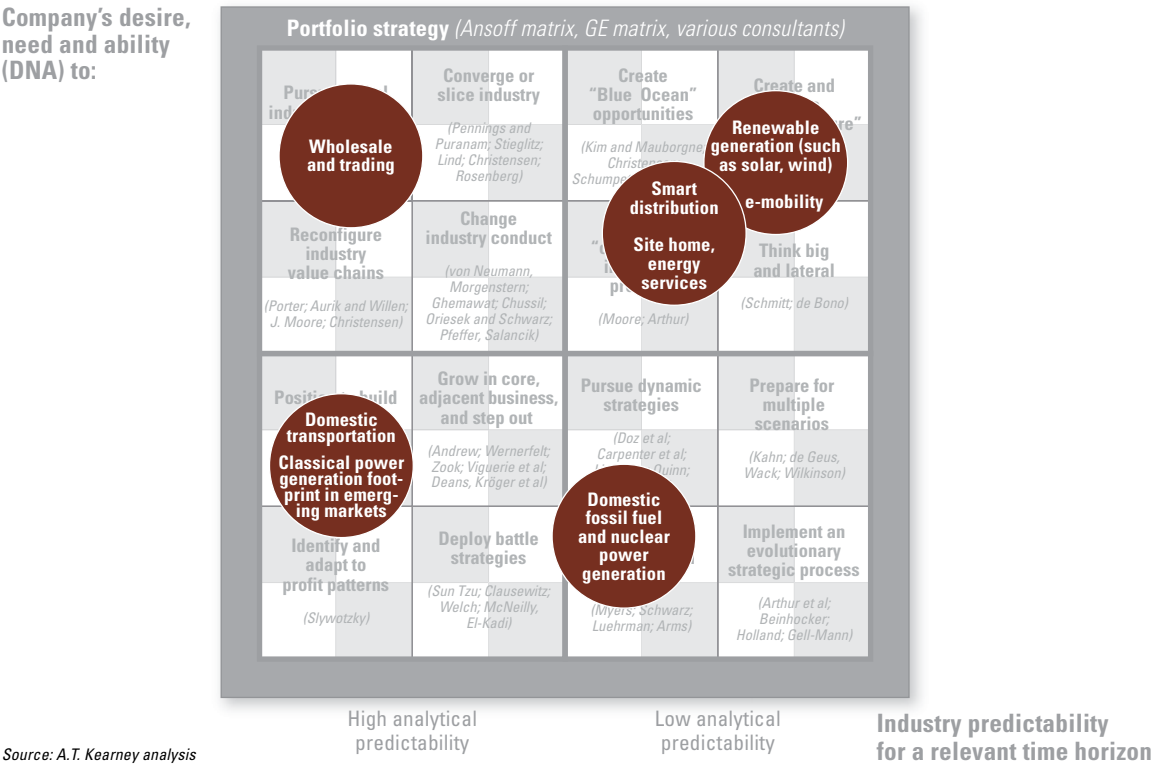
Chessboard-based strategy development



Source: A.T. Kearney analysis

Figure 7

Different entities within a company can require different strategies *Client example from 2010*



Source: A.T. Kearney analysis

that would allow you to deliver a superior product and lower cost. Generally, many of the adaptation-biased strategy schools close the door to industry-shaping options that may be more attractive.

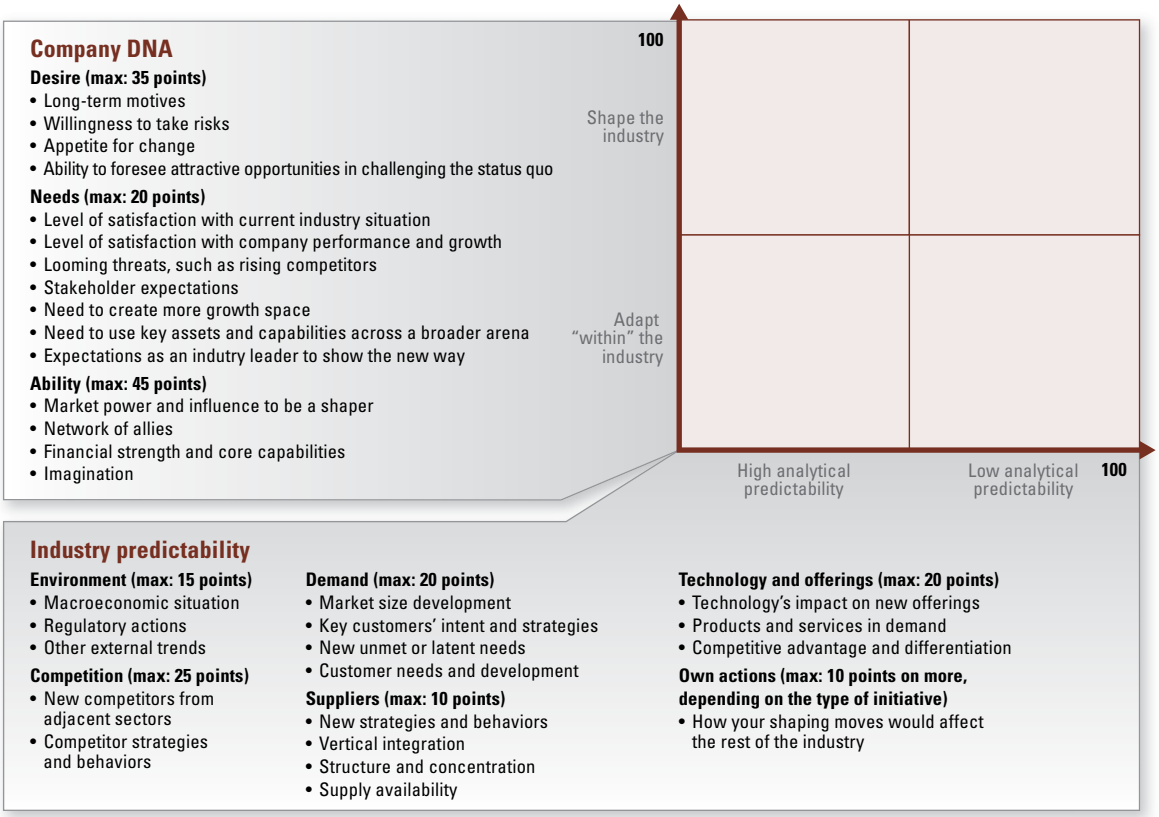
Selecting an umbrella strategy and an entry lens (or strategy school and framework) is a critical first step in the strategy-development process. Applying additional and complementary lenses enriches industry understanding and increases options by helping to compare and validate the analysis.

Sequencing bias problem. Conducting a comprehensive industry analysis before generating potential strategic options downplays a company's integral role in the industry. Considering industry analysis while you devise strategic options, however, has many advantages, as a company's strategic initiatives can often have a material impact on the development of the future industry—generating reactions from major competitors and stakeholders. It also ensures that the analysis utilizes appropriate frameworks, has the right focus, and that enough time is spent on the most important aspects of the industry.

Different approaches problem. It makes little sense to have different approaches to developing corporate, business unit and even product strategies. The issues and concepts needed are very similar but act on different levels of granularity: corporate strategy deals with a collection of business units; business-unit strategy deals with

Figure 8

Using a point scale to understand a company's DNA and its industry predictability



Source: A.T. Kearney analysis

a collection of product areas; and product-area strategy deals with a collection of products.

Winning on the Strategy Chessboard

An effective strategic process is explicit and easily understood, and our Chessboard-based approach is helpful in avoiding common strategic flaws. The approach uses the following three steps to develop the right strategy *(see figure 6 on page 11):*

1. Determine DNA and industry context and appropriate umbrella strategy and "entry lens" (per relevant business entity). This first step helps select the appropriate entry lens for the more detailed industry and company analysis that is used later to determine strategic options. The approach starts by identifying your company's DNA and likely industry predictability. To understand your DNA and industry conditions properly, you may need to break down your business into units, which may require different lenses. Figure 7 demonstrates a utility company whose different business entities fit into different parts of the chessboard.

Well-known techniques are used for this analysis, but the preliminary DNA analysis and structured determination of industry predictability are vital for its success, so we typically use our own frameworks *(see figure 8)*. In addition, understanding your key competitors' strategic approaches helps determine which umbrella strategies and entry lens to use for a more detailed analysis.

2. Develop enriched industry perspective and potential strategic options in parallel. The results of the high-level analysis in step one will help determine which umbrella strategy and strategy school to examine more deeply in step two. The strategy school is identified this way for prime "inspiration," but is then customized according to the company's unique challenges and objectives. This phase provides a rich foundation for analyzing the company, the industry and the strategic options.

It makes little sense to perform a detailed industry analysis without considering what strategies are available. Therefore, we typically use a more parallel process to ensure sufficient focus and granularity where it really matters. Devising an ambitious M&A strategy without considering other players' likely responses is not very useful, so an alternative approach helps. In most cases, applying additional lenses to the analysis will help you better understand your industry and potential strategic options.

3. Evaluate strategic options against company DNA, finalize strategy and establish governance. The final step is always validation, where strategic options are matched against company DNA. No company should implement a strategy that the leadership team and primary owners do not desire, need or have the ability to pursue. Hence, we make significant efforts to ensure DNA compatibility with the strategic recommendations, in addition to the standard financial and risk-based evaluations. Even in predictable industries, a comprehensive governance plan will help steer, monitor and adjust the implementation as necessary.

Honing the Craft

Just as skilled craftsmen control which tools to use at the right time, the Strategy Chessboard gives a structure to the toolbox of available strategic schools of thought. Using the chessboard, companies can design and implement strategies that align with their desires, needs and abilities—and help them succeed into the future.

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APPENDIX

Portfolio strategy

At the border of the chessboard is portfolio strategy, based on the view that managing a portfolio of businesses or products is a fundamental strategic task, regardless of which approach is used to develop strategy. On a regular basis, all companies must decide which products to keep, which to develop and which to eliminate. Igor Ansoff's product-market growth matrix is one of the first frameworks in strategic management. The GE multi-factorial model evaluates industry attractiveness (based on multiple factors, including market size, growth, price, competitive dynamics and segmentation) and business strength (market share, brand strength, margins, quality and talent). In addition, significant and mathematically driven contributions have been borrowed from finance theory. Harry Markowitz's modern portfolio theory analyzes risk and return for various types and combinations of assets.

Position and Conquer

Position to build competitive advantage

A pioneer of strategic thinking and a comprehensive thinker, Michael Porter has been enormously influential. His original framework centers on conceiving and building sustainable competitive advantage. Through an analysis of five industry forces—suppliers, customers, substitutes, new entrants and industry competitive intensity—companies can identify their strategic positions and the strategic moves that will strengthen these positions. This thinking is in the position-and-conquer quadrant of the chessboard because one of its preliminary assumptions is that a company should define its position within its industry. This approach has proven to be an excellent complement to other approaches.

Numerous authors followed Porter by publishing refined models, including the niche-based competition work of A.T. Kearney's Fritz Kröger and Michael Moriarty. In an industry environment driven by scale-based competition, identifying and conquering niches is its own strategic task. Niche types include regional, target group, product, brand, speed, innovation, cooperation, market splits, and counterniches. The appropriate niches to pursue depends on the industry's level of consolidation.

Grow in core, adjacent business and step out

Growth for a company can come from many sources, particularly new markets, new products and increasing market share. Identifying these sources is an important task of business strategy and has drawn the attention of many theorists. The main strategic thrusts have varied over time, from a diversification trend in the 1970s and 1980s to a move toward focus and globalization in the 1990s. The current prevailing wisdom favors making sure a company's core is in order before attempting to enter new businesses. The core capabilities and competencies can then be used to generate and capture new business opportunities.

Chris Zook models close, midrange and distant adjacencies before pursuing diversification. Kröger and Deans emphasize getting operations and the organization in good shape by exploiting various strategic levers and then stretching to achieve extraordinary growth. Patrick Viguerie defines three horizons of growth: extend and defend the core business, build the emerging business and create viable options. For each horizon three approaches can be used: portfolio momentum, M&A or share gains.

Identify and adapt to profit patterns

In a changing world, a company's ability to be successful and generate profits may depend on its ability to predict the future and act on it. Major trends create similar effects across industries, which means it's possible to develop skills and techniques to recognize them. Adrian Slywotsky, et al., in *The Profit Zone* and *Profit Patterns*, outlines 30 strategic prediction models divided into seven families of patterns: mega, channel, knowledge, value chain, customer, product and organization. By correctly understanding and applying these patterns, a company can become a more forceful competitor with additional profit generating capability. In addition, Slywotsky outlines 22 models that, depending on industry and situation, are likely to generate profits. Similar "islands of profitability" can be identified through microeconomic theory, for example, by understanding supply and demand, capturing monopoly and oligopoly rent, using information advantages and capitalizing on market failures.

Deploy battle strategies

Business competition is often analogous to warfare, and numerous attempts have been made to transfer military insights into competitive action. Sun Tzu's *Art of War* has served many as management literature. Strategies for attack, defense, flanking and guerilla competition can be applicable in marketing and general business strategy. Tzu's work leads to some basic business principles, such as capturing a market without destroying it, avoiding competitors' strengths and attacking their weaknesses, using knowledge and deception to maximize the power of business intelligence, using speed and preparation to overcome competition, using alliances and strategic control points to shape opponents and make them conform, and developing leadership character to maximize employees' potential.

Carl von Clausewitz, a Napoleon contemporary, sought to replace the established view of military strategy with a set of flexible principles to govern thinking about war. Such ideas had an impact on many CEOs, including Jack Welch in his approach to building General Electric.

Redefine

Pursue global industry endgame consolidation

Even though some business theorists argue that any industry that generates above-average returns should see a steady flow of new entrants and hence maintain an even rate of consolidation over time, this is generally not the case in practice. Long-time industry analysis by Kröger points to clear consolidation patterns across all industries, driven by globalization and the opening of financial markets. This pattern arises as an S-curve—an industry's concentration ratio plotted against time—that demonstrates how all industries move from a fragmented opening phase, to a scale phase where consolidation begins, to a focus phase of rapid industry concentration (ratios of 70 percent), and finally a balance phase in which the industry is fully consolidated, with three main players owning about 80 percent of the market. Because of this, M&As are imperative for any company with a strong shaping agenda.

Over their life cycles, industries can return to earlier phases in the consolidation pattern—perhaps because of a new innovation or government regulation. Some strategies allow attacking companies to benefit from breaking up monopolies and oligopolies, either through aggressive niche strategies or full-scale industry fragmentation.

Converge or slice an industry

An industry is defined by the types of products and services it delivers, the companies that operate within it and their resource base. Industry definitions change over time as technology changes and businesses develop. Typically, industries converge and form new industries, but there are also cases in which they are sliced—for example, the split of ground services from airline companies. Slicing can occur in several dimensions, for example through separating products that create new industries, changing the business logic, breaking up the value chain or breaking down entry barriers. A company with a shaping agenda can take active part in transforming definitions, creating a new and hopefully stronger position.

As Nils Stieglitz showed, industry convergence can be driven by technology or products, and driven by substitutes or complements. As convergence occurs, companies need to reconfigure their capabilities. Success in the marketplace will go to those with the best capabilities for the new environment.

Reconfigure industry value chains

In addition to his five forces, Michael Porter also developed the concept of the value chain, where the activities of an organization are placed and analyzed in logical order. Value chain analysis has since become an important part of both operational and strategic thinking. Over time, information technology (IT), globalization and deregulation have made it easier for companies to interact. This has led to more "horizontalization," by which companies focus on core parts of their value chains and hand off noncore parts to suppliers. The outsourcing trend within IT is typical of this type of disintegration.

Some strategy frameworks put additional emphasis on more radical and creative value chain reconfiguration, and not just forward or backward integration, disintegration or outsourcing. For example, partnerships between competitors can capture economies of scale in non-differentiating parts of the value chain. Or a company can decide to create a new supplier for downstream activities if the number of suppliers is too low.

A related concept to the value chain is the value network, where interrelationships among activities are mapped out, but not with the same sequential layout as the value chain. A biological analogy is an ecosystem—different players take different roles in sustaining the ecosystem and it thrives in competition with other ecosystems.

Change industry conduct

Game theory is a well-known tool for analyzing the dynamic interaction between competitors. In strategy development, game theory can identify the best actions to take in specific competitive situations. For repeated games, there are strategies with different benefits, namely: always defect, always cooperate, simpleton, vengeful, fair and tit-for-tat. Game theory is also a powerful tool for questioning the rules of the game—developing strategies to gain advantage by affecting different PARTS (an acronym for players, added value, rules, tactics and scope).

Related to this is business wargaming, which can analyze a broader set of situations than standard game theory. Simulation games in which groups of people act out different business situations can help identify which strategies work and which do not. A similar mathematical concept is the Monte Carlo simulation, in which simulation tools are used when the analytics become overwhelmingly difficult.

Cross the chasm with innovative products

More products today—often those with high technological content—are experiencing life cycles different from traditional products. The "inside tornado" product life cycle outlined by Geoffrey Moore attempts to describe this dynamic. It starts at product or technology inception, then gets to the crossing of a chasm in which it is very difficult to increase usage. In the next step, called the bowling alley phase, vertical segments help increasing usage. In the chasm and bowling alley phases, positive feedback loops—which amplify a system's changes—are typically at work beyond the simple cost of manufacture. Lastly, in the tornado phase, the product's increasing returns skyrocket. In the end, a single company (the gorilla) often comes out dominant. Apple's iPod is a classic example.

Related to increasing return economics is the concept of path dependence, which means that once a new state is established, it is difficult to move away from it. In other words, small events at the start of a product life cycle can leave a major impact many years down the line. For companies operating in this environment, being at the forefront of these events and determining the best way to take advantage of them is vital for success.

Creating and managing ecosystems is important over the life cycle, as different phases require different actions. In the beginning stage and at the crossing of the chasm, the ecosystem needs to make the product whole. In the bowling alley, the ecosystem must allow a company to address many different niche markets efficiently, while in the tornado it needs to enable rapid volume growth. Finally, in the last stages, the ecosystem can be a caretaker until the end of life.

Reinvent

Create "Blue Ocean" opportunities

W. Chan Kim and Renee Mauborgne focus on identifying new business opportunities in *Blue Ocean Strategy*. Instead of competing directly with competitors and identifying the correct position (as in Porter's strategies), companies can make competition irrelevant by conceiving new market space, or so-called value innovation. The strategy stresses significant step-outs from current offerings, so strategies developed in this fashion are clearly shaping in nature. There are six avenues to explore for such step-outs: industry (look across alternative industries), strategic group (look across strategic groups within the industry), buyers (redefine the pool of buyers), scope (focus on complementary offerings), functional-emotional orientation (rethink the orientation of the industry) and time (participate in shaping external trends over time).

Four actions can offer a new type of customer value: eliminating factors below the industry standards, eliminating those that the industry takes for granted, creating factors the industry has never offered, and raising factors above industry standards.

Innovation schools also emphasize new opportunities. Joseph Schumpeter outlines five main economic innovations: introducing a new good, introducing a new production method, opening a new market, conquering a new supply source, and creating a new industry organization.

Create and pursue a preferred future

Generating and capturing new business opportunities is essential in industries under constant development. Gary Hamel and C.K. Prahalad say that competing for the future means fighting to create and dominate emerging opportunities. This

can be done through intellectual leadership: gaining industry foresight by probing deeply into industry drivers, developing a creative point of view about the evolution, and then arriving at a strategic architecture. Next, migration paths must be managed to build core competencies, assemble and manage the necessary coalition of industry participants, and force competitors to take longer migration paths. Lastly, competition for market share begins by building supplier networks, crafting positioning, preempting competitors, maximizing efficiency and managing competitive interaction.

Hamel and Prahalad also argue that strategy and new business development should not solely emanate from the CEO's office; rather it should be engrained throughout the whole organization. To make this possible, the organization should know what its core competencies are, which of these competencies give it a unique competitive advantage, and what it should then do to strengthen these competencies.

To support this thinking is Thomas Kratzert's "Preferred Futures." In this vision, a company with ambition to shape an uncertain industry should attempt to steer development toward the preferred future and then take the necessary actions to reach that future. A preferred future is reached through a thorough, scenario-based understanding of how it might evolve and what impact it would leave on the industry.

Think big and lateral

Traditional business strategy is incremental in nature: improve products, capture markets, develop channels. Bernd Schmitt calls this "small think" and says the strategies that truly make a difference are the result of bold, "big think" ideas from completely different angles.

Big think strategies can originate from several sources—combinations of seemingly incompatible areas, benchmarks outside the industry, the elimination of sacred cows, restructured time frames and bearish strip strategies—that serve as tools for big thinkers who evaluate the ideas and turn them into strategies. In addition to this strategy development is a leadership flow that executes the strategies across the organization.

To think big, a good deal of creativity is needed. For such purposes, the tools and techniques by Edward de Bono, creator of the term "lateral thinking," are useful.

Maintain Foresight and Flexibility

Pursue dynamic strategies

One way to address an increasingly uncertain environment is to shorten the time horizon by conducting more frequent strategic planning. Truly dynamic strategies are under constant review, open and sensitive to signals from the surrounding environment, and ready and responsive to quick action when redefined. Mason Carpenter and William Sanders outlined a number of questions that a company constantly needs to ask itself in order to keep its strategy in order, such as arenas (where will we be active and with what emphasis?), vehicles (how will we get there?), differentiators (how will we win?), staging (what will be our speed and sequence of moves?) and economic logic (how will returns be obtained?).

Yves Doz and Mikko Kosonen outline the mindsets that separate strategy from fast strategy—from foresight-driven strategic planning to insight-based strategic sensitivity; from corporate-sub-unit planning processes and one-to-one CEO decisions to collective commitments by the top management team; from resource allocation, del-

egated subunit execution and staff control to resource fluidity in redeployment and sharing.

Constantinos Markides points out that a company that is flexible and sensitive to its surroundings can run a deliberate strategy of being a fast second. In this scenario, it doesn't face the penalties of innovating and opening up new markets, but benefits from being a very good follower.

Prepare for multiple scenarios

Royal Dutch Shell is frequently credited as a pioneer in scenario analysis. Even though the future may be difficult to predict for a certain industry, it is often analytically possible to understand industry drivers and put boundaries on the level of uncertainty. This way, scenarios can outline the solution space for what the future could look like. With the adapt mindset, the company would then develop a business portfolio that would work in all scenarios and a set of options to execute if a given scenario proves true. Once the portfolio has been developed it becomes important to track its development and enable timely adaptation. Scenarios used like this can broaden the perspective, increase the level of foresight, reduce the risk of unpleasant surprises, create a flexible strategy, and help understand industry development.

Deploy real options-based strategies

In some business situations, the success of an investment is highly dependent on a number of uncertain events. In these cases, real-options theory is a powerful tool for viewing investments, and call-option calculation theory can help with capital budgeting. In net present value (NPV) analysis, the most likely outcome is usually modeled. By contrast, real options valuation also values the flexibility of having the option. Typical options are abandonment, contracts, expansion, process flexibility, stop or shutdown, operating scale, deferment, sequencing and project scope. An example is a capital investment decision by an energy company about whether or not to mothball a plant. A fringe benefit of real options analysis is it forces users to examine their assumptions about risk. The rigor applied in the process could also uncover new possibilities.

Implement an evolutionary strategic process

If the economy is a highly unpredictable complex adaptive system—in which it is nearly impossible to predict networks and interrelationships—the best approach is to adopt an evolutionary process that develops a portfolio of experiments aligned with a general management ambition. The art of strategy development here would come down to executing the portfolio, identifying which initiatives gain market traction, amplifying those that work and killing off those that don't, and regularly filling the portfolio of experiments that fit with the lessons of past trials. Learning and feedback loops are particularly vital for reevaluating positions and adjusting to new market conditions.

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