Chapter 2

STRATEGY'S SEVEN FATAL FLAWS

Why Strategy Gets A Bad Name And What To Do About It

Let me come clean. In my experience, many successful CEOs and senior executives resent the time they have to spend on developing strategy. There are two reasons for this. First, strategy is seen as being difficult. Consultants and academics have somehow succeeded in creating a misguided mystique around strategy that only people with an IQ of 150 or more and who have attended the world's best universities can do it. Despite the overwhelming evidence to the contrary that demonstrates that the best business strategies are created and led by pragmatic leaders who are willing and able to consider alternative futures for their business, many executives feel intimidated about their ability to create a credible strategy for growth.

Second, and more importantly, strategy development is perceived to be irrelevant to managers' daily and most pressing issues. Attending strategy meetings and retreats feels like a world away from the real work that must be done, and as the meeting progresses the frustrated executives begin to take a peek at their smart phones so that they are able to keep up to date on what's really happening with their business.

To a large extent, the frustrations of these executives are not their fault, but result directly from the way strategy is developed and managed in many organizations. I have identified seven 'fatal flaws'. By addressing each of these flaws, you will start to hardwire your strategy work into the real issues and opportunities facing your business. It will no longer be seen as separate to your ongoing operations, but will help your managers make better decisions on a daily basis, as well as helping you to make the big calls and create an organization that is able to thrive and grow.

So, let's look at each of these fatal flaws in turn.

Fatal Flaw #1: Allowing Planning To Kill Strategy

What is your reaction when you hear the phrase "strategic planning"? Are you energized by the chance to create exciting new opportunities for future profit growth? Or are you depressed by the thought of endless form filling, requests for further information, and periodic fights to protect your budgets? If you chose the latter option, you are not alone. I once read a consulting firm's survey that suggested that less than a quarter of senior executives agreed that they made major strategic decisions during the process.

Less than a quarter!

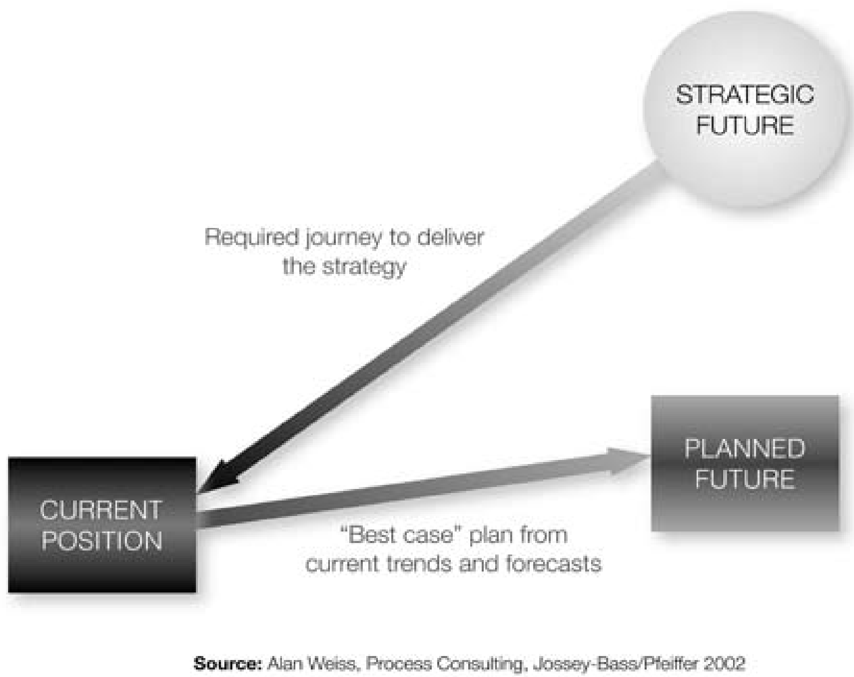

Figure 2.1: Strategy vs. Planning

In fact "strategic planning" is an oxymoron. It is virtually impossible to develop a winning strategy for growth during an annual planning process. Yet too many companies try, and fail, to combine the two tasks. The end result is typically a 1-3 year budget plan, not a coherent strategy for sustained and substantial growth.

Figure 2.1 compares a planning-led and strategy-led approach. Under a planning-led system, the senior management team tends to start the process with a level of growth that must be achieved in the next year or two to maintain momentum. Using a process that is generally led by the finance department it is, essentially, a budget exercise and the levels of growth pursued are commonly based on the company's current performance trends plus or minus a percent or two. Executives and managers may talk about the strategies required to deliver the results, but often they are simply dancing on the head of a pin. The big management discussions are not on major issues of strategy but on detailed budgetary issues, such as whether the gross margin target should be 32.4% or 32.5%.

In contrast, a strategy-led approach starts with a view of what kind of business you are trying to build. Your first tasks are to clarify how you can best win in the future, to agree your level of ambition for your company and to determine what size and shape of organization will enable you to make this happen. Once you have alignment on these issues, you can then determine some of the key steps you need to take to move you from your current position to your strategic future.

Using this approach you will end up taking actions you would never even consider under a planning-led approach. Paradoxically, it is often when companies are facing a real crisis that they find the resolve to use a strategy-led approach and break out of their planning-led incrementalism. At that point CEOs know that improving margins by a couple of percent will be insufficient to deliver sustainable success, and that bigger-thinking and more radical decisions are required. The problem is that by then it may be too late for the business to reverse its fortunes. Following the 2008 economic crash, for example, many of the US car makers that have been struggling to face up to international competition, finally made some of the major steps required to enable them to compete in the twenty-first century. However, having failed to arrest their decline over the past 20 years, there is no guarantee that these measures will be sufficient.

The time to drive strategy is when you're already succeeding and the best way to achieve that is to separate strategy development from annual resource planning, for four good reasons:

Planning vs. Strategy

1. **They answer different questions.** Strategy development is focused on how you wish to win in your chosen market, what distinctive advantages you need to make this happen and what capabilities and assets you require to underpin this approach. Although you will need a robust fact base to make progress, it is as much a creative process as it is analytical. Planning, on the other hand, seeks to identify the best way to achieve your objectives within the resource constraints you have. It is more about control than direction.

2. **They have different timelines.** Planning is required to ensure that managers across the organization know what resources they have, and what they are expected to deliver with them. A set timetable is required so that when the new financial year begins everyone understands what is expected of him or her. Strategy, however, responds to market issues and opportunities as they emerge. There is no annual timetable that can cater for these changes. It is not therefore surprising that few planning processes lead to major strategic decisions.

3. **They require different metrics.** The end result of planning typically comprises a profit and loss, capital expenditure and cash-flow budget, *possibly* supported by some market share projections. In short, the language of planning is financial. Metrics that help strategy development include, but are not limited by, financials. Innovation, speed, quality, customer satisfaction, loyalty, and brand strength can be equally valid measures. However, such metrics are often ignored during the annual planning process in favour of P&L projections.

4. **They involve different players.** Annual planning requires executive approval and sign-off, but can often be led by a central planning team working with line managers. Strategy development, however, requires the active involvement of the leaders of the business. Although support is required from other players, it is only when the leadership team has fully argued through the merits of different alternatives to future growth that clear strategic decisions can be taken. In short, strategy cannot be delegated.

Don't let planning kill strategy. By separating out strategy development from the annual planning process you will have radically increased your organization's chance of identifying new opportunities for substantial future growth.

Fatal Flaw #2: Incremental Thinking

Although a planning-led approach will almost inevitably deliver incremental gains, a shift to a strategy-led approach does not guarantee that major breakthroughs will follow. Incremental thinking is driven as much by your own mindset as it is by a particular process you follow. Taking a step back to look at your business is simply not enough; you must completely change your perspective and find ways to kick-start your brain into new ideas.

There are three key factors that drive incremental thinking.

1. An unwillingness to be wrong

An unwillingness to be wrong, or, more importantly, an unwillingness to be *seen* to be wrong, prevents many senior executives from proposing more radical alternatives to their existing strategy and business model. A *Business Week* survey once found that the most important factor driving the success of many of Silicon Valley's most successful entrepreneurs was an ability to 'experiment fearlessly'.

If you need to be right, and you aren't ready and willing to be wrong, you will only take incremental steps. You will never reach out far enough to take the actions that lead to step-change improvements. I'm not suggesting that you should take reckless actions, but without prudent risk there is unlikely to be material gain.

2. Unclear or limited goals.

Many of the organizations I visit either have no medium-term goals or have set a goal or vision that is so woolly that managers cannot possibly work out what needs to happen to achieve them. Instead, current year profit targets drive these corporations.

Now, I've nothing against profit targets. On the contrary, they help create focus and ensure accountability. However, if that's all there is managers will find ways to manage, and perhaps even manipulate, their activities to deliver the results required. A longer-term goal, and potentially one that is not purely focused on profits, can drive new thinking, different behaviors and greater commitment to the company's ongoing success.

The critical factor is that the goals you set are not driven by hubris or your ego, but by an understanding of what is possible for your business if you and your teams make the strategic and organizational changes necessary to deliver it. I once came across an organization that had set a goal of double-digit sales growth for each of the next five years. The only problem with the goal was that no one believed it, not even along the executive corridor. As a result, the final budgets that were agreed with the commercial teams were only half of the company's supposed ambition. Unsurprisingly, the rest of the business did not take the CEO and the top team seriously and within a matter of months several executives had left the organization.

In comparison, when Wal-Mart set a goal in the early 1990s of becoming a $125 billion business by the year 2000 (equivalent to three times their existing sales revenues) the executive team did so with a sincere belief that the goal could be achieved if they relentlessly and persistently improved and extended their existing business model. Success was far from certain, but it was at least possible, and the goal was rooted in a deep understanding of the company's capabilities and the potential prize that was available to the business.

3. Resistance to changing the rules of the game

In the 15 seasons between August 1994 and May 2009, Manchester United, the UK's leading football team, played 286 home games in the Premier League. Of those matches, United won 212 and lost only 23. Visiting sides had, on average, an 8% chance of coming away from Old Trafford with three points, and a 75% probability of leaving with nothing but a poorer goal difference. Not only did the visiting teams have United's great players to deal with, but also crowds of up to 70,000 people or more, and match officials who may (or may not) have been intimidated by those fans, let alone United's manager, Sir Alex Ferguson, and his infamous stopwatch!

Few managers, planning their seasonal campaigns, look forward to the visit to United with any kind of optimism. And yet, many businesses operate in markets that are the equivalent of playing away at Old Trafford every week. Trying to imitate the market leader, they effectively end up playing to another company's rules, on another company's pitch, with another company's ball. Unlike sport, you are not tied to a particular set of rules, only to those that you decide to follow. Yet, in my experience an executive team is ten times more likely to invest time and effort in benchmarking the performance and strategies of their company's competitors, than they are in developing and articulating radical changes to create an organization that is uniquely advantaged.

Fatal Flaw #3: Putting Financials Ahead Of Ideas

Developing a business strategy relies on creativity and idea generation far more than it is driven by analysis. The reality is that most successful businesses start with an idea. Some times the idea is created in a *eureka* moment. Paul Allen and Bill Gates, who had been – mostly unsuccessfully – developing software for minicomputers, saw the cover of the latest edition of an electronics periodical, which showed a new, smaller computer that could fit on a desktop. They immediately realized that the future of computing was the PC and that they should focus their software development on these smaller, desktop machines. They called the makers of the PC and, within a few weeks, had written software for the machine and started a new company, Microsoft.

Other times the idea emerges more gradually. Fred Smith, for example, combined his post-graduate business studies, his general observation that most activities were becoming more automated and his experience as a charter pilot to develop the idea of an overnight parcel delivery service using a hub and spoke distribution model. Smith then joined the marines and it was only after he left the armed services that he pursued his idea with earnest, and created FedEx.

In both these stories, as in most business development successes, the idea emerges from individuals or small groups who have a strong desire to change the world in some way, and who are able to combine their expertise and experience in a particular niche with an insightful understanding of the broader changes driving the markets in which they operate.

Unfortunately, most of the books on business strategy have focused on analytical methods and tools, rather than how to create new business ideas or how to recognize and exploit your organization's unique experience and expertise. Contemporary models of business strategy begin with economic analyses, and strategy's leading authority is Michael Porter who, in the 1980s, produced two highly influential books, *Competitive Strategy* and *Competitive Advantage*, both of which are focused on analytical rather than creative processes to drive strategy development.

A certain level of analysis is essential for business strategies to succeed. But without a greater focus on ideas, you will simply end up with a greater understanding of your current market position, rather than a compelling basis for driving new profitable growth for your business. Figure 2.2 compares analytical approaches with creative approaches to strategy. Which best describes your strategy development processes?

Analytical Approaches	Creative Approaches
Focus on analysis of markets and performance	Focus on new ideas
Desktop assessments	Real-life experience
Follower	Leader
Problem solving	Innovation
What's happening?	What if?
Dealing with the past	Focused on the future
Financial proof before action	Action before financial proof
Forecasts and long-term plans	Rapid learning action plans
Strategy teams staffed with analytical experts	Ad hoc strategy teams staffed with a mix of 'thinkers' and 'doers'

Figure 2.2: Analytical vs. Creative Approaches To Strategy

One of the critical differences between the two approaches is that an analytical approach drives a need to obtain financial 'proof' before taking action. In the past I have sat in endless meetings where a manager comes to an internal forum to ask for some initial funds for an idea, only to be faced by a group of people with no real understanding of the idea being discussed, who then attempt to dissect it, criticize it and find as many reasons as possible not to do it. One of the initial questions this group will ask is *"Can you show me your business plan and financial forecasts?"* The meeting will then quickly descend into a detailed examination of the financials, rather than the quality of the idea itself. And if the initial financials are not deemed strong enough, even if the idea has real merit and could, if properly pursued, create significant growth, it will be dropped, often forever.

A few years ago I was working with a retailer that was looking for new growth ideas. One of the ideas suggested was to target a new group of customers through a non-retail channel. The potential prize was huge – up to 50% top-line growth. There was one problem, however: the initial financial modeling suggested that the profit margins would be only half of the margins delivered by the existing retail business. For that reason – and that reason alone – the idea had been dropped. It took a proactive and persistent commercial manager nearly a full year of negotiation with the executive directors to show that, if certain changes to the new idea's business model were made, the profitability could increase.

Even so, the new idea is being pursued with a fraction of the resource that I believe it warrants. If managers had put as much effort into learning about the new opportunity through rapid trials and low-cost prototypes than it did into writing more financial spreadsheets, both the company, and its customers, would be a lot better off.

How would these internal forums have dealt with the initial ideas of Sergey Brin and Larry Page, the founders of Google? The answer, we can safely assume, is not very well. Brin and Page would have been given short shrift by these risk-averse groups as it took them a couple of years or so before they determined how they could turn their search engine technology into a money-making business. For Brin and Page, as for most innovators, the idea is developed first and the business model second.

Until your business escapes the trap of seeking financial proof before taking action, you will always face a dearth of radical growth options and compelling innovations to drive your strategy forward.

Fatal Flaw #4: All vision and no direction

A vision is not a strategy. Unfortunately, many executives believe that creating a vision can equate to setting out a growth strategy. It doesn't. Your people may be inspired by your vision, but it won't necessarily help them decide how they should focus their efforts. Only when you have sufficient clarity that helps determine your managers' daily actions can you be confident that you have a strategy that is capable of becoming embedded across your business.

I once worked with a retail service business that had spent a significant amount of time and effort to set out a clear vision for the company's future. This vision was deeply held by the executive team and they had communicated it across the business. The vision statement went something like this: *we will be the best at what we do in the world*. The trouble, however, with such statements – that the company will be the best, the most admired or the avatar in its industry – is that they provide no guidance as to what you really want to achieve. As a result, my client's retail teams were carrying on as they had always done, and even the executive had not particularly changed its strategic agenda. The CEO and his team had not taken the next critical step of defining *how* the company was to become the best in the world.

Term	Definition	Example
Values	What's important to you about how you operate	**IBM**: Dedication to every client's success; Innovation that matters, for our company and for the world; Trust and personal responsibility in all relationships
Mission	Why your organization exists, over and above making money (also called your core purpose)	**IKEA**: To create a better everyday life for the many people.
Vision	An inspirational, over-arching long-term future goal	**SAMSUNG**: Inspire the world, create the future.
Strategy	A framework for guiding decisions and actions across your organisation to deliver superior performance and your vision	**BMW**: The BMW Group is the leading provider of premium products and premium services for individual mobility.
Plan	The allocation of resources to implement an agreed set of actions	**FIFA**: Russia will host the 2018 World Cup and must deliver the plan set out in the bid document

Figure 2.3: Strategy-related definitions

Figure 2.3 sets out definitions for several strategy-related terms that are often confused. Samsung's vision, for example, which states that the company will *"inspire the world, create the future"*, can help its executives and teams to raise the bar on their current levels of performance but it doesn't articulate the markets in which the company will participate or which customers it is targeting.

BMW's simple strategy statement gives a clearer sense of where and how the company should be operating. It gives guidance about how managers should be operating, but is not completely restrictive. For example, its market or business domain is 'individual mobility'. This means the automobiles and motorcycles the company already produces, but could potentially include pedal-power bicycles or even personal jets in the future. The inclusion of 'services' as well as 'products' certainly means it will deliver its current range of financial services, but again does not preclude the offering of broader transportation services. In short, the strategy statement provides a framework for what the current business is, but also how it might evolve in the coming years.

Fatal Flaw #5: A Failure To Make Trade-Offs

The corollary of identifying the core of your strategy is deciding what you're not, and what's of less importance to your business. At this point we reach the dreaded word in strategy development – *trade-off*. If you are unwilling to make clear and proactive trade-offs, it is unlikely that you will have a leading position in your market or a winning strategy.

So why is this so hard? The answer is simple. Making trade-offs means that you're giving something up and, if you're not 100% confident in your stated strategy, it is more than tempting to hedge your bets, have a look at what the competition is doing and say to yourself "*Let's try a bit of what they're doing*." The result is that your own business spends all its time keeping up with the Joneses, rather than trying to create something that is distinctive and uniquely valuable.

When I was growing up my older brothers and I used to finish our meals as quickly as possible in the hope of getting some of the food from my younger brother's plate. Once we had eaten our dinner we would intently watch him eat every mouthful, silently willing him to put down his cutlery and finish his meal. Whenever he left some food we would collectively pounce on his plate and fight for the scraps that remained.

There is an old medieval word for our behavior of silently and longingly staring at someone else's food in the hope of being offered it: it's called *groaking*. And it's not only greedy, adolescent schoolboys who *groak*. Many business executives look longingly at their competitors, wanting what they have. In particular, they look to copy the market leader in a bid to enjoy a bit of their meal.

Corporate *groaking* (you might call it competitive benchmarking) results in competitors becoming pale imitations of the #1 player. In the UK coffee shop market, chains including Café Nero, Costa, Eat, Coffee Republic, Coffee Primo, Café Ritazza and other local cafes were established in the hope of enjoying some of Starbucks' success.

The problem for the challengers is that in most markets it is only the leading players that make meaningful returns. It is the leaders that occupy the biggest share of buyers' attention and spend. Unless something dramatically different comes along that is clearly better than their current provider potential customers will be unlikely to notice 'me-too' suppliers.

By seeking to copy the leaders, these challengers end up fighting over scraps in much the same way as I did with my brothers. It is unsurprising that many of the players in the coffee shop market have either performed poorly or even ceased trading. There are two tests of your customer proposition and business model you should apply to understand whether you are equipped to grow profitably:

1. *Are you distinctive?* Do you offer something that is dramatically different to other players in the market? Is there something unique and compelling about your proposition or business model that customers immediately notice? For example, Dell offers fairly standard PC's and laptops, but provides customers with low prices, customized specifications and delivery direct to their home or the office.

2. *Are you advantaged?* Are you able to turn this distinctiveness into superior performance? Can you create a system to deliver your proposition that others will find difficult to copy? Over time Dell has built and refined a business model that is completely aligned with its source of distinctiveness and which has created and sustained its advantage over its competitors. For example, building-to-order has allowed Dell to align its suppliers into a 'just-in-time' supply and manufacturing system, significantly reducing the company's working capital, improving its cash flow and increasing its return on investment.

Fatal Flaw #6: Insufficient focus on action

Few, if any strategies emerge from implementation unscathed. By pursuing your big objectives, implementing your initial plans and taking action you are likely to change, in some way, the direction you have set. It is only by learning from your actions that you can really clarify how you can best succeed in the future. The results of your actions will drive your strategy at least as much as your strategy drives your actions. The ideal cycle of idea generation – action, learning and refinement – is set out in Figure 2.4. The critical aspect of this cycle is to learn as quickly and as cheaply as you can. Your ability to create competitive advantage is, to a large extent, driven by your ability to operate this cycle faster, cheaper and more effectively than your rivals.

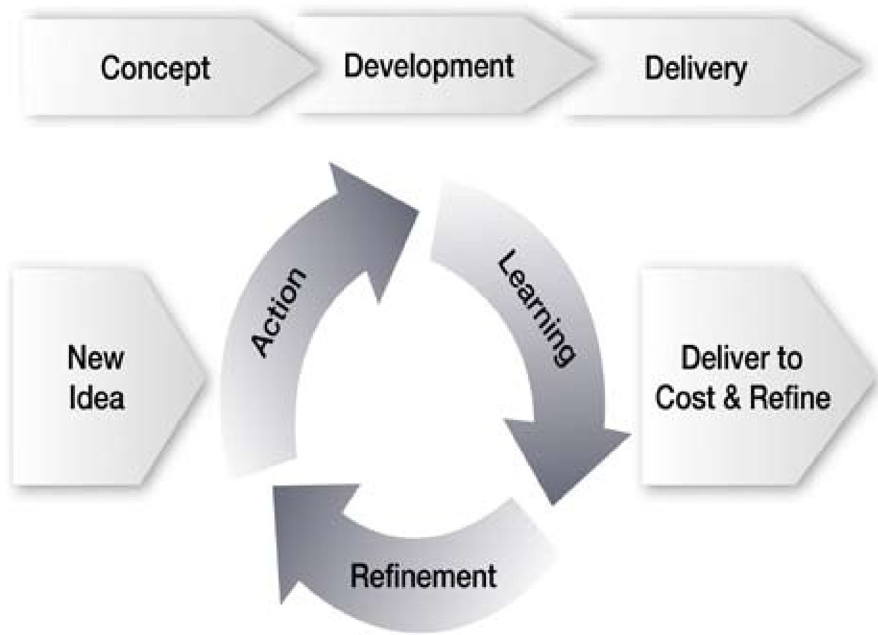

Figure 2.4: The Rapid Learning Cycle

However, the pursuit of planning ahead of strategy, a bias towards incremental thinking and the need for financial proof ahead of the desire to develop new ideas, all mitigate against taking action. Instead, managers spend their time perfecting their financial models and plans and only commence delivery once they are confident that success is virtually guaranteed. That usually means that, even in the initial trial phase, the focus of the project is on hitting a particular financial target rather than maximising learning. If there is any risk that the financial target won't be hit, then the trial will not be sanctioned and no action will take place.

The problem with this approach is that the managers are asking the wrong question. In the early stages of developing new business ideas you should not be asking, *"Can we make sufficient returns in this area?"* but should, instead, be asking these questions:

- *Is this idea likely to help us to become a market leader?* If the idea only helps you to play catch-up, and produces a me-too offer that imitates what's already out there, it may help you keep up with the pack but it's unlikely that it will transform your performance. If you have an idea, however, that could take your business to the forefront of your industry, you are likely to create the energy and focus for your organization that can't help but drive action.

- *Do sufficient numbers of customers like this idea?* If they don't, then by all means you should kill the idea (although you may find that by refining it you get a different customer reaction), but if your initial trials suggests that you have a potential winner on your hands, you can then begin to work out how to create an attractive business and financial model.

- *How do we make the idea technically feasible?* Prototyping your products, services and processes is a critical element of driving your strategy forward. Over a five-year period James Dyson made over 5,000 prototypes of his revolutionary bagless vacuum cleaner before creating a fully trademarked, production version.

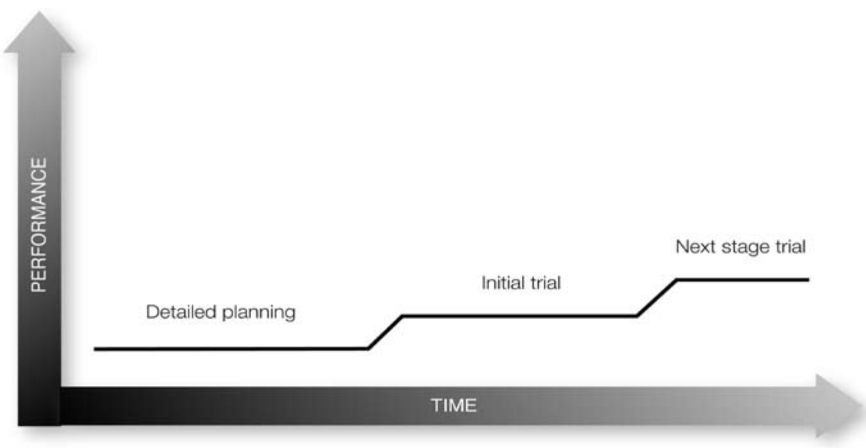

Figure 2.5a: How An Action-Based Approach To Strategy Succeeds – Traditional Approach

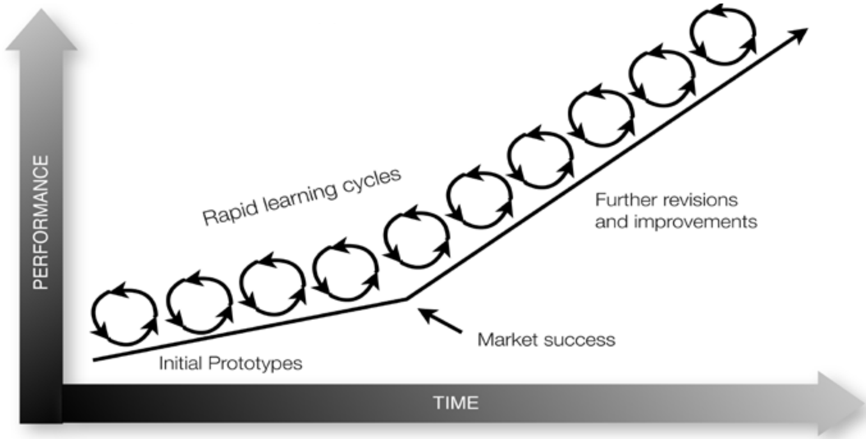

Figure 2.5b: How An Action-Based Approach To Strategy Succeeds – Action-based Approach

By changing the questions you ask you are more likely to drive action, learn how to succeed and actually achieve something. Figure 2.5 demonstrates the difference between the two approaches. At its heart is a shift in managerial mindset from one of risk aversion and a need to have as many questions answered before doing anything, to one where trial and error and learning through action drives a succession of prototypes and versions that drive your business forward. In his book, *Bloomberg By Bloomberg*, Michael Bloomberg, the founder of the eponymous financial information and media empire, put it like this, *"We made mistakes of course. Most of them were omissions we didn't think of when we initially wrote the software. We fixed them by doing it over and over, again and again. We do the same today. While our competitors are still sucking their thumbs trying to make the design perfect, we're already on prototype version No. 5. By the time our rivals are ready with wires and screws, we are on version No. 10. It gets back to planning versus acting. We act from day one; others plan how to plan – for months."*

Fatal Flaw #7: An overreliance on external consultants

The final fatal flaw that undermines business strategy is a reliance on external consultants. As a consultant myself I know that, done well, working with external consultants can add real value to the development and delivery of your business strategy. The problems arise, however, when CEOs and their executive teams start to rely on these consultants for strategy, rather than working with them as partners. This means that instead of asking the consultants for help with process and for input on ideas, managers end up delegating to the consultants the overall strategy itself.

Such reliance creates the following problems for executive teams:

- **Lower levels of management involvement and ownership.** Developing and executing a great business strategy can be time-consuming and hard work. But it is a key job of your managers, and, behind all the jargon, is less difficult to do than many managers believe. By all means get external support where this makes sense, but a commitment to action is driven by a sense of ownership of the strategy, and that sense of ownership is, in turn, driven by involvement. The most successful businesses I have worked with all have a huge sense of ownership of their strategy, and although their top team may work with external advisors, it is the leaders that take the lead in setting the direction, determining the big goals and taking accountability for their delivery.

- **A focus on analysis ahead of action.** Many consultants have followed a traditional business school education, which emphasises analytical tools and approaches. Unsurprisingly, these consultants tend to focus their efforts on analysing data and producing information packs, rather than helping the company's managers and teams to take action. I am sure that you have seen the data-rich 'decks' that consultants produce and which, more often than not, lie undisturbed in the CEO's filing system for years after the work is complete. It's not that the analysis is not accurate, but that it just doesn't help move the business forward.

- **A me-too strategy.** Consultants, under pressure to demonstrate their expertise, share their knowledge of their clients' key markets and identify what others have done to succeed as the basis of their recommendations for growth. Their insights and recommendations are fine as far as they go, but they will not create true distinctiveness. It is difficult to imagine an external consultant recommending breakthrough business ideas such as Apple's iTunes, Facebook or, in a previous decade, Renault's distinctive design of its family of automobiles. Each of these business decisions carried too much risk to be made by consultants, and relied on the trial-and-error, action-based approach that market leaders and innovators pursue, and that can only be driven by the company's executives and managers.

By all means work with trusted consultants to aid and accelerate your strategy process, and to offer ideas and challenges to your company's internal thinking and priorities. But do not let the consultants take over. If you ever believe that the consultant rather than your team has set the agenda for a strategy meeting, you should start to be concerned. Do not be afraid of strategy – the techniques and approaches in this book can help you take hold of the steering wheel and make sure that you are in the driving seat, not the back seat, when setting the future direction of your organization.

Key Points

There are seven fatal flaws that you must avoid if you are to create and deliver an effective, high-value strategy:

- Fatal Flaw #1: Allowing planning to kill strategy;
- Fatal Flaw #2: Incremental thinking;
- Fatal Flaw #3: Putting financials ahead of ideas;
- Fatal Flaw #4: All vision, no direction;
- Fatal Flaw #5: A failure to make trade-offs;
- Fatal Flaw #6: Insufficient focus on action; and
- Fatal Flaw #7: An overreliance on external consultants.