Quick takes

Larry Goodson

These brief summaries highlight the key points and action steps in the feature articles in this issue of Strategy & Leadership. Larry Goodson, an S & L contributing editor, is a veteran strategy consultant based in St. Louis, Missouri. He is a Partner at LDGA Consulting, which offers Lean operations and strategy development services (ldgoodson@msn.com)

Interview

Roger Martin: The problematic economic efficiency mindset that threatens corporations and democratic society

Brian Leavy

"On its current path, American democratic capitalism is, I believe, heading for an ugly fall."

So warns Roger L. Martin in his new book, *When More is Not Better: Overcoming America's Obsession with Economic Efficiency*.

Strategy & Leadership: What are the main indicators that America's economic system is now heading in the wrong direction, and how long has this been going on?

Roger Martin: Sadly, American democratic capitalism has been on the current path for over forty years. The annual increase in the median family income in America, from 1947, the year it started being tracked, to 1976, rose at a real compound annual rate of 2.4 percent which implies doubling in thirty years. Since then, it has grown at a meager 0.6 percent, which implies doubling in 116 years!

S&L: The "core design challenge" for the future of American democratic capitalism "is to achieve a much better balance between efficiency and resilience in the system." Why is this and what should our new complex adaptive system "design principles" be?

Martin: A natural system needs to have resilience in order to survive and prosper over time. Efficiency, especially narrowly-defined as is the current case, provides no guarantee of either survival or growth.

- First, in designing for complexity, we need to balance the "pressure" for more efficiency with the application of productive "friction" to limit its damaging extremes.
- Second, in designing for adaptability, we need to balance the desire for "perfection" and the drive for "improvement."
- Third, in designing for systemic structure, we need to balance the march toward "connectedness" and the enforcement of "separation" because, while a connected world is more efficient, a system which is too tightly coupled can be vulnerable to failing.

S&L: Among the recommendations that you make for political leaders are to "seek improvements rather than solutions," to "write revision into the laws you make," and to "seek mental proximity when designing policy." Why is this crucial?

Martin: You can't fix a complex adaptive system. All you can do is help it get better. So adopting a solutions mindset will just cause political leaders to set themselves up for failure by attempting too much and guaranteeing that they reap unintended consequences.

S&L: Finally, given that America's potential future still fills you with "a combination of concern and hope," what, in light of your work on this book, gives you the greatest grounds for optimism?

Martin: The grounds for optimism stem from knowing that all of my

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recommendations either are already being done successfully in America, were previously done successfully in America, or are being done successfully elsewhere. So they are all eminently doable.

The challenge: 20th Century vs. 21st Century management

Stephen Denning

There are currently two strikingly different ways of running a corporation in a coherent and consistent fashion. In one—the predominant mode of 20th Century management refined over the last 50 years—the goal of the firm is to maximize shareholder value.

In contrast, for 21st Century management – the pioneering mode of Agile enterprises and of leading Silicon Valley firms, as well as individual businesses in Europe and China—the goal of the firm is to create customers.

Understanding how 20th Century and 21st Century management differ offers an evidenced-based theory why today's leading firms are leading and why yesterday's giants are flailing.

The principles of 20th Century management

The characteristic structure of work in 20th Century management is that of bureaucracy: individuals fill specific roles and report to bosses. The dynamic is command-and-control.

The strengths of 20th Century management

20th Century management is a coherent and internally consistent way of running a corporation. It is resilient: it hangs together as an integrated system.

Then the world changed

As the century ended, 20th Century management was becoming steadily less effective. Four major causes stand out:

- The pace of change accelerated.
- Technology made radical leaps.
- Knowledge work predominated.
- Power in the marketplace shifted from the firm to the customer.

How 21st Century management emerged

Beginning initially in software development initiatives and small startups in and around Silicon Valley, as well as individual firms in Europe and China, these firms adopted a different goal: to create a continuous stream of value for customers and users. Making money was a result, not the goal.

The processes of 21st Century management

When firms first began to adopt these different principles, they often experienced difficulty integrating them with the processes they had inherited from 20th century management—leadership hierarchy, competitive strategy, line-extension innovation and so on. And so they also had to reinvent their processes. These firms grew rapidly because they found ways to transform the lives of customers and users with new ways of communicating, connecting, working, accessing knowledge, shopping, transportation and entertainment.

Two different modes of thinking

A significant hurdle in making the transition to 21st management is that it requires not only doing things differently but also thinking differently. The problematic principles and processes of 20th Century management reflect the idea of the firm as a machine. In contrast, 21st Century management views the firm, not as a machine, but rather as a complex adaptive system.

The future of management

Firms that successfully embrace 21st Century management can look forward to an exciting and sustainable future.

Designing employee experiences to create customer experience value
B. Joseph Pine II

Increasingly the Service Economy is transitioning to an Experience Economy, where legacy business models that merely provide satisfactory services or goods are no longer adequate. What customers increasingly want are experiences – memorable events that engage each individual in an inherently personal way. When companies accept the proposition that they are in the experience business, the factors that make up the profit chain change dramatically. Think of the customer/employee relationship as the experience profit chain, one that interacts in multiple and complex ways to yield a connected human experience.

It’s about time

The employee experience depends on how well companies design the time employees spend that creates value for customers. A fundamental design principle is: services provide time well saved while experiences offer time well spent.

Time well saved

Be sure to focus on saving employee time, not just saving company resources. It’s surprisingly easy to confuse the two. Managers need to fully take into account the burden of time that bureaucratic red tape adds to employees’ days, time that could be productively spent creating value for customers.

Time well spent defining the qualities of experience

There are five core types of truly significant customer experiences: robust experiences, cohesive experiences, personal experiences, dramatic experiences and sometimes transformative experiences. Each of these types, and the principles and frameworks designed to deliver them, are equally important to the creation of employee experiences.

Time well invested

Companies – whether in offerings to customers or engagement with employees – need to recognize that transformations yield time well invested.

Time to change

As Rightpoint CEO Ross Freedman writes in “The New Competitive Advantage Is Experiences for Customers and Employees Alike.”

> Experience companies shift from this inside-out thinking to an outside-in mindset, in which they consider customers’ needs first, then work backward. Additionally, consider what customers are really looking for from your brand, beyond what they are asking for.

Now is the time to change not only the way you think but how you operate, embracing experience design principles – in particular those that enable the business to stage engaging and memorable experiences that are robust, cohesive, personal, dramatic and even transformative – to create connected human experiences for customers, employees and all contributors.

Interview
Frances Frei and Anne Morriss: The dynamics of empowering leader/follower relationships
Brian Leavy

Much of the vast literature on leadership to date has tended to focus more on the characteristics and qualities of the individual leader and less on the nature, quality and dynamics of the relationship between the leader and the led. Few experts are as well versed on this relationship as Frances Frei and Anne Morriss, authors of *Unleashed: The Unapologetic Leader’s Guide to Empowering Everyone Around You.*

Frances Frei and Anne Morriss: Conventional leadership narratives assume that the vision-having, strategy-making, troops-rallying leader is the most important person in the room. The practical definition of leadership we use in our work is that leadership is about empowering other people as a result of your presence—and making sure that impact continues into your absence.

S&L: Why do you see trust as the foundation of empowerment, and can you explain the thinking behind your "trust triangle" framework for leaders?

Frei and Morriss: Leadership is a sacred exchange that's impossible without trust. People tend to trust you when they think they are interacting with the real you (authenticity), when they have faith in your judgment and competence (logic), and when they believe that you care about them (empathy). These are the three drivers of the "trust triangle."

Empowering your people through strategy and culture

S&L: Leading an organization or business unit of any size requires two additional tools, strategy and culture, How does the empowering relationship work with strategy?

Frei and Morriss: Your first job as a strategist is to be better than your competitors at the things that matter most to your customers. In most cases, this means you'll also have to be worse than your competitors at other things, ideally the less important ones. We believe that strategy is a primary way that leaders embed who they are, their core values and beliefs, into their organization's behavior. It carries who they are into corners of the company – and beyond – which they could never reach by their own presence.

S&L: How do you see strategy and culture working together?

Frei and Morriss: Whatever it is that strategy has not made clear to your extended team, culture will unapologetically fill the void. Culture establishes the rules of engagement after leadership leaves the room.

S&L: Finally, where do you see your work going from here? What are the next priorities on your empowerment leadership agenda?

Frei and Morriss: Our readers are really hungry for practical insight into creating inclusive cultures and building organizations where belonging is embedded deeply into both strategy and operations. Our next project will be to examine the extraordinary opportunities of inclusion and equity. As part of this exploration, we'll also explore the dynamic intersection of identity, experience and leadership.

Redirecting resources to promote post-pandemic growth

Christian Bieck and Anthony Marshall

With the extreme disruption caused by the COVID-19 pandemic, the systems of optimization in many industries profoundly failed. Before the epidemic, much of the global business community was focused on becoming lean by widely deploying production efficiency methods. Now the COVID-19 pandemic has revealed how precariously intertwined our economic systems and our lives really are. Supply chains across much of the global economy fractured.

Don't panic, prioritize

A recent IBM Institute of Business Value (IBV) global survey of 3,450 business leaders, conducted during the full force of the pandemic, explored which business capabilities executives are prioritizing.

Asked about the most pressing of those priorities, C-suite executives ranked "workforce safety and security" number one, closely followed by crisis management. But right after that they ranked familiar concerns: cost management and cash flow management

To lease or to buy?

A central theme in the search for cost efficiency is the question of investment and ownership, or capital expenditure (CapEx), versus operating expenditure (OpEx).

For example, shifting CapEx to OpEx might free up funds, but that is only useful if organizations pursue other strategies with these assets, such as digitizing operations and sales.

Invest the right way: CapEx with a technology twist

Cost management continues to receive high focus, 87 percent of respondents stated they planned to prioritize cost management to a significant or very great extent. But artificial intelligence (AI) could see the greatest leap in investments. Fourteen percent of respondents reported highly prioritizing AI in 2018, yet more than four times as many (57 percent) say that they plan to prioritize AI in 2022.

Recommendations for forward-looking executives planning to invest for recovery

Re-affirm digital transformation. Of the executives surveyed, as little as 20 percent of their overall workforce is currently enabled to work remotely. The root cause of such constraints is low digital maturity, inadequate digital integration and poor interoperability.

An ongoing transformation, evolution, or reinvention is crucial to enabling organizations to navigate the inevitable next discontinuity.

Re-think resource allocation. The current economic environment has shattered long-held, entrenched assumptions, helping the most successful companies identify and eradicate organizational weaknesses. Cost cutting should be viewed as a mechanism to redirect resources to enterprise transformation investments.

Mandate change as a fundamental cultural principle. All corporate functions should participate in some level of cost cutting to contribute to overall enterprise transformation goals. A “flexibility as necessity” vision needs top management commitment.

How to improve revenue forecasts from strategic investments

Daniel Deneffe and Herman Vantrappen

Many practitioners and scholars now question the point of devoting time and energy to systematic business strategy formulation. Given the rapid changes they must cope with, some executives turn to back-of-the-envelope calculations, gut estimates or unfounded optimism when making investments in potential new products or line extensions. In order to obtain vastly more reliable revenue estimates than those based solely on such guesstimates, business executives should recognize four principles for assessing market opportunities:

1. The company’s potential market is smaller than the total market

Before a company can even hope to successfully enter a new target market, it must surmount two hurdles. The first: it has to know the size of the potential market, which are those customers in the target market who would consider buying from a new supplier. Even when the company’s offering creates a new-to-the-world business and, hence, there are no “current suppliers,” there are usually alternatives which the target customers may prefer. This finding also means that business executives should devote energy to sizing the potential market rather than spending time and resources at getting the most accurate estimate of the total market.

2. The company's accessible market is smaller than its potential market

The second hurdle is identifying the "must-haves" of customers in the potential market. While a customer in the potential market will consider buying from a new supplier, that customer will not consider any suppliers that fail on any of his or her minimum requirements, even if those suppliers score well on all others.

3. What matters are the preferences of individual customers, not of some representative or average customer

Once a company has passed the first two hurdles, it can start thinking about how to position itself relative to its competitors. "Competitors" include those that may be unknown to the company and, in the case of a new-to-the-world offering, providers of substitute solutions. A customer will select the offering that gives him or her the best deal, that is, with the largest difference between the customer's willingness-to-pay and the offering's price, which we call the "deal value." However, what often leads to revenue estimates that are way off is to attempt to identify some average willingness-to-pay and to position and price an offering accordingly. Estimating the average willingness-to-pay is insufficient to make good pricing decisions or get reasonably reliable revenue estimates.

4. The design of the company's offerings should be driven by customers' points of indifference

Companies need a solid preference-elicitation method that helps customers discover their preferences in an unbiased manner. It should allow the company to find out which specific combination of benefits and features – out of many possible choices – and what price will maximize its revenues or margins. To determine that specific combination, executives can use so-called tradeoff methods to show customers different pair combinations, until a point is reached where the customer can make no discernable distinction between the combinations in the pair, the point of indifference.

Informed decisions: upfront analysis pays off

As well-informed customers today have more choices than ever, careful customer analysis is of paramount importance to minimize the risks that can be managed and, as a result, maximize the chances of making successful strategic choices.

Revisiting risk management in a time of crisis

Norman T. Sheehan

To say that the 2020 global pandemic has been a crisis event is an understatement. Given the resulting market turbulence, it is an opportune time for corporations to take stock of their risk management systems.

The answers to three leading questions can help organizations deal with this crisis and others that arise:

- Why did organizations fail to prepare for a global pandemic?
- What are effective risk responses for risks related to the global pandemic?
- How best to assess the optimal risk level for an organization?

A review of the major risk management action steps sets the context for answering the three key questions.

Action step 1: Identify risks and score them

Managers use a variety of techniques to identify risk events that may prevent their organizations from reaching its strategic objectives, including historical data, experts, simulations and brainstorming.

Action step 2: Propose and implement risk responses for each risk

After scoring each raw risk's probability and impact, the next step is to formulate risk responses and then implement these.

Action step 3: Review the organization's residual risk after implementing the risk responses and adjust as needed

After formulating cost effective risk responses there are two questions boards need to ask to determine if the organization's residual risk level satisfies its risk appetite. Has the organization taken on the right risks? And is the residual risk level appropriate for the organization?

How best to assess the optimal risk level for an organization?

Boards first need to assure themselves that the organization is taking the right risks in pursuit of value. Boards and executives can use CAM-I's Risk-Value Curve which reflects that organizations can take too little risk and thus create a sub-optimal amount of value, or they can take on too much risk and be on the precipice of a crisis. The take-away from the Risk-Value curve is that boards not only have to specify the maximum amount of risk they want their organizations to assume – the organization's risk appetite – they also need to specify the minimum level of risk to assume.

Time to review and prepare

An organization's long-term success ultimately depends on the ability of its board and executive team to navigate through crises and discontinuity. Due to changes in the world and improvements in risk management best practices now is an opportune time to review their risk management systems and make improvements.