



Fixing the disconnect

The link from strategy to the performance it produces is a mystery to many. Some simple reasoning makes the connection clear

THE QUESTIONS YOUR STRATEGY EFFORTS MUST ANSWER



INDUSTRY VIEW

Given a promising strategy, management simply wants to know what to do to make it happen, what profit and cash flow to expect, and how to adapt to changing circumstances.

Unfortunately, strategy reference books, courses and articles have little or nothing to say on the topic.

Former strategy director and now a teacher and writer, Kim Warren says: "It is no wonder that executives are frustrated with 'strategy' and see little value in the business planning process. And it's no wonder, either, that we see so many big failures of strategy.

"But no-one ever talks about the majority of companies who continually under-perform because of poorly executed strategy. Missed opportunities for successful growth should be the real concern of managers and investors, not occasional disasters, however spectacular."

Some have tried to fix the links from strategy to action plans to cash flow. Balanced scorecards and strategy maps aim to lay out how a strategy should work, and deliver financial success. Others advise on how to define a business model – which customers to serve, with what products and services, and how to make it happen in a way that creates value. But with little rigorous science behind them, and important issues left out of the picture altogether (such as competitors!), the value of these methods is limited.

"Neither these nor any other strategy methods explain the time path of past profits, where those profits might go in future, or how a better future might be built."

Warren recommends starting with the simple logic that profit and cash flow come from customers (who drive sales), and staff and operating capacity (which drive costs).

"But clearly there's more. Customers are won and retained, staff hired and promoted, products developed, and capacity expanded – all of which are the actions-over-time that execute strategy and turn it into performance.

"Complications are, first, that lead times from actions to impact can be long – many years in the case of hiring or capacity changes – and second, that these resources depend on each other to develop and to be sustained," he says.

"This is the system at the heart of every organisation which drives its performance from period to period. A healthy system grows and sustains those resources, strongly and in balance, and is resilient to competition and other external forces.

"To this core, you can add any complexity you need; competition of course, the exploitation of new markets, intangible factors such as skills or brand reputation, learning

and scale effects, and so on."

This process delivers a rigorous, dynamic business model that actually plays out strategy and performance over time. "The method is not complicated or technical," says Warren. "But when necessary, we can easily simulate these models. We use simulation in other important fields, and we can do so in strategy. Shockingly, the professional tool to do this, system dynamics, has been known for over 50 years, so it is high time we used it!"

Business dynamics models bring to life, with numbers, the links between all parts of the organisation at all times. They automatically connect with past financial results and generate estimates for the future. They surface time-phased action plans for every part of the business, can test for risks and alternative scenarios, and they can – and must – be continually updated and adapted.

Kim Warren was formerly a strategy director with Whitbread and designed its transformation from a threatened beer company to restaurant and hotel powerhouse. He taught strategy at London Business School for 15 years, and now writes, consults and advises on strategy and business dynamics.

07802 485869

www.kimwarren.com

