Ashridge Strategic Management Centre

Strategy Journal Retrospective, September-October 2019

Pointing you to articles of interest to strategists in leading publications

In this edition: deciding which innovations to pursue, the simple "green box" approach to allocating innovation resources, the turnstile strategy behind ecosystem businesses, AI-enabled strategy, and vitality, a forward-looking strategy indicator

How to Know Which Ideas Your Company Should Pursue

Dirk Deichmann, Violetta Rodopoulou and Inga Hoever. HBR

Organisations are notoriously poor at choosing which ideas to pursue, and can get hung up on the relative merits of novelty, feasibility, and market potential. The solution, according to these authors? **Organisations should evaluate the benefits an idea promises relative to the cost of developing it.** The benefit in question can be profit, of course, but a company is free to define benefit to refer to customer satisfaction or loyalty. This approach will select for ideas that convert the resources they needs to realise different types of benefits as efficiently as possible – meaning, for example, that an idea that offers only incremental benefit but requires little investment might be more profitable than a fantastic idea that requires a lot of investment. More

The Innovation Commitment

Daniel Cohen, Brian Quinn, and Erik Roth. McKinsey Quarterly.

In the "green box" approach to innovation, a company's leaders quantify how much growth in revenue or earnings the firm's innovation needs to provide in a given timeframe. The green box is the value generated from all forms of innovation—breakthrough and incremental—over a set time frame, for example, five years. The value is quantified using metrics such as net new revenue, earnings growth, or both, and it represents growth that can only be traced back to innovation. All other possible sources of growth, including market momentum, pricing adjustments, distribution and marketing activities and M&A, are taken out. The green box is a simple framework that delivers significant insights. For example, reviewing a chemical company's innovation portfolio, the authors found that 65% of it was dedicated to small, product-related initiatives – safe bets, but not projects that were capable, over time, of meeting the company's rising growth expectations. Indeed, while few leaders are brave enough to say that innovation is not a priority, the green box can help a decide whether it should really be the highest area of focus, or whether the company can meet performance targets by running core operations effectively and relying on incremental initiatives. Of course, the green box doesn't exist in a strategic vacuum. It needs to be preceded by a "north star" vision that describes in detail what success will look like, translated into a strategy and key actions that include qualitative and quantitative metrics for measuring progress. (One of these is the size of the green box). And, as in any good strategy process, accountability for the delivery of innovation needs to be clear. More

Ecosystem Businesses Are Changing the Rules of Strategy

Julian Birkinshaw. HBR

Lloyd's of London, a classic ecosystem business, was founded in the 17th century. 254 years later, ecosystem businesses are a hot topic in the strategy literature. Will today's ecosystem giants – Amazon, Tencent, Uber, Google – have an enduring competitive advantage? Most of these ecosystem orchestrators are low on assets and don't manufacture what they sell, so the asset and positioning-based logic we're used to using to think about competitive advantage is less relevant. In fact, while business strategists look to protect existing assets and to keep competition at bay, the new ecosystem businesses are happy to open up to competition and to share intellectual property. They operate what the author calls a **turnstile model**, where the aim is to maximise the number of people coming through the turnstile, not to successfully defend on the basis of position or price. The author offers rules for successful turnstile models: **(1) focus on keeping customers coming in, (2) give people a reason to stick around, (3) don't steal your partners' business** (Amazon has to strike a delicate balance between pushing its own products and scaring away other vendors; its competitor AliBaba has chosen not to sell its own products at all, and has double Amazon's e-commerce business with an eighth of Amazon's staff), and **(4) keep evolving** (open up new services, as Google's analytics platform does). More

Strategy For and With AI

David Kiron and Michael Schrage. MIT Sloan Management Review

We hear a great deal about creating a strategy for AI, but not nearly enough has been said about creating strategy with AI, which the authors say matters quite as much. Ideally, both should be pursued together. In a machine learning era, the authors say, overall enterprise strategy is a function of the key performance indicators (KPIs) that a company's leaders choose to focus on and optimise for. For AI-enabled strategy to work well, selecting and ranking KPIs becomes core to a company's strategy work. For example, Uber has determined that estimated time to arrival (ETA) is one of its key success metrics. Uber's Map Services team, which uses a segment-by-segment routing system to estimate ETA, has used a machine learning model to predict ETA errors and incorporate corrections. It has now rolled that approach out globally, with a dramatic increase in ETA accuracy – and improved competitive advantage. But, to achieve AI-enabled strategic success in this way, Uber has had to downgrade the importance of KPIs that conflict with improving ETA. Another example: McDonalds, which acquired Israeli machine learning company Dynamic Yield for $300 m in March, has made regaining its status as a family destination that appeals to parents a core strategic goal. It can use machine learning to classify geotagged Twitter data and analyse comments about neighbourhood fast-food locations. At the same time, it can see whether advertising and menu options produce store conditions that annoy parents – and can learn to optimise for its core goal of becoming attractive to parents again. AI-enabled strategy can also help companies optimise between partially competing goals – for example, working out how to optimise revenue-enhancement KPIs in the context of customer satisfaction and net promoter score KPIs. More

Achieving Vitality in Turbulent Times

Martin Reeves, Gerry Hansell, Kevin Whitaker, Tom Deegan, and Hen Lotan. BCG Insights.

Most commonly used indicators in business – growth, market share, and profitability, for example – measure only what *has* happened. In turbulent times, these authors say, that's no longer a strong indicator of what *will* happen. They propose a new, forward-looking indicator: vitality, which is the capacity to reinvent the business and grow sustainably. Vitality is a challenge, especially for large, established companies, where complexity and inertia have increased as the firms have aged and grown, making change difficult. BCG research shows that revenue growth is the primary driver of superior financial performance, even during economic downturns (even in financial downturns, performance is driven by top-line growth rather than by cost-cutting). Moreover, companies that grow faster during downturns tend to continue growing faster once the economy improves. How does BCG define vitality? As the authors explain in detail, BCG has developed a vitality index that comprises several components: market potential (the expectation of future growth from financial markets, defined as the present value of growth options); strategy, technology, and investment; people; and structure. It incorporates non-financial data – ESG (environmental, social and governance) scores, for example, gender diversity, a point on which companies with high vitality tend to score high. Analysis using the vitality index clearly shows that the companies with the highest potential are not necessarily the ones with the highest performance today: exactly half are also above average in current performance (as measured by EBIT margin) and half are below. This means that companies will need leaders skilled in what the authors call ambidexterity, namely the ability to run their businesses while reinventing them at the same time. More