Outthink the Competition®

A Manual for Applying the Rapid-Cycle Strategy Process

Rapid-cycle Strategy Innovation

"In battle, this ability to rapidly pass through the observation-orientation-decision-action loop (the Boyd cycle) gave American pilots a slight time advantage. If one views a dogfight as a series of Boyd cycles, one sees that the Americans would repeatedly gain a time advantage each cycle, until the enemy's actions became totally inappropriate for the changing situations."

- Robert Leonhard, *The Art of Maneuver*[i]

The OODA loop

John Boyd was one of the U.S. military's most brilliant strategists. Today he is known only by a small community of military tacticians and students of military methods. But his insights have come to define the basis of modern warfare.

During the Korean War, Boyd served as his squadron's commander and tactics instructor. Their F-86s yielded less firepower or thrust than their opponents' MIGs, yet Boyd's pilots averaged a 10:1 kill ratio against their enemies. Throughout much of Boyd's career as instructor, advisor, military theorist, and fighter pilot designer, he maintained a running bet that with forty seconds in the air he could beat any pilot in aerial combat. "Forty-second Boyd," as he came to be known, never lost this bet.

Asked to explain his methods, Boyd developed a theory of conflict that is now shaping militaries all over the globe. Central to his theory is that the entity—the squadron, army, company, government—that adapts fastest to changing events wins. He specifically identified four interdependent phases an organization or organism must pass through to adapt to changing reality: observation, orientation, decision, and action (the OODA loop, or the Boyd cycle). To beat your competition, then, you must cycle faster than them and/or hinder their ability to cycle through their OODA loop. Many of the 36 Stratagems achieve this dual objective by providing you with a creative response while obfuscating reality from your opponent.

Business cycles

Boyd's principle has been at work for millennia, determining winners and losers on battlefields and in corporate conflicts. We find evidence of cycle time being a determinant of competitiveness in business as early as the turn of the nineteenth century. In the early 1800s, Hudson's Bay, a trading company, was facing collapse because a competing trading company, the North West Company, had adopted a new distribution strategy—with trading posts located more closely to customers—a more flexible, decentralized management structure. Hudson's Bay's centralized bureaucracy hindered the company's reaction time, and by 1809 the company seemed destined to close. In that year, however, Hudson Bay's ownership changed hands. The new leadership quickly copied its rival's approach, moving trading posts closer to customers and decentralizing operations.

By breaking through rigidity to react to a changing environment, the new owners saved their company.[ii] Hudson's Bay beat its rival, merging with it ten years later, and survived as the Hudson's Bay Company, considered today to be the oldest surviving commercial enterprise in Canada.

The ability to cycle quickly proved defining in the battle of Intel versus its early Asian competitors or Frontline versus rival oil tanker operators. The ability to react quickly and creatively to a changing environment is fundamental to competitive advantage.

Rapid, creative response

Few companies have proven able to consistently respond creatively and quickly to environment changes. Companies stifle creativity, we have found, by relying too heavily on logical methods. When companies face a strategic challenge, they inevitably turn to one of two approaches for solving it: option narrowing or rules. Option narrowing involves laying out a seemingly complete set of choices, then ruling them out to arrive at the best one. The other is to study successful cases—companies, leaders, battles—and distill from these a set of commonalities that, we believe, if we follow we will be similarly successful. Although both approaches are critical to successful problem solving, they rarely lead to exciting, innovative solutions.

The 36 Stratagems offer an effective complement to these logical methods. My colleagues have found the stratagems to be surprisingly effective tools for helping modern-day strategists see beyond the obvious, to conceive out-of-the-box strategic options that come naturally to history's most creative strategists.

To ensure that creative options, once conceived, transform rapidly into action, my colleagues and I have found you must unblock one or more of seven key barriers to strategic innovation. The vast majority of the most competitive companies of the decade beginning in 1995 achieved their strengths by seeing and choosing a strategic option their competitors would not. The most competitive were able to surmount hurdles that their competitors tripped over. These seven hurdles are as follows:

1. Failing to <u>observe</u> that our environment has changed and that new opportunities or risks have emerged.
2. Having observed that the environment has changed, failing to <u>orient</u> ourselves to the implication of this change. We may observe clouds are forming, for example, but fail to understand that this means rain may soon fall.
3. Having oriented ourselves, we lack a clear <u>aspiration</u> and so are not compelled to take action, which might alter our current course.
4. Though we have a clear aspiration, we fail to <u>conceive</u> of a good solution. We are stuck with a few uninspiring options or, yet worse, fall entranced with a good-enough option. So we adopt an uninspired, copy-cat strategy.
5. We have conceived of an exciting, out-of-the-box solution but will not <u>consider</u> it either because we ourselves find it unreasonable or because our teammates and our organization view the idea as "crazy."
6. We are willing consider the solution but, after analysis, <u>choose</u> not to adopt it. Our decision is usually based on sound logic that we can prove is flawed only

after someone else—a successful competitor—proves that our original idea actually was a good one.

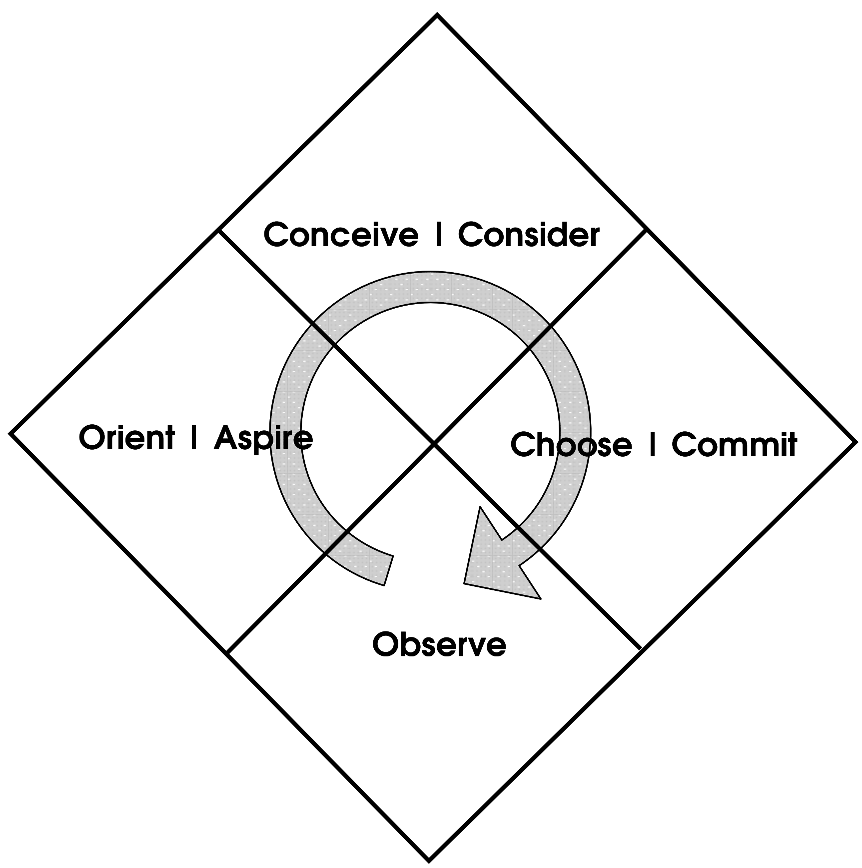
7. Though we choose a strategy, we fail to commit to it. Because we are unable to convince others to support our strategy, we never align our real strategy (what we do) with our intended strategy (what we plan to do).

You will notice that framework is an expansion of John Boyd's OODA loop. My colleagues and I have used this framework to help companies across several sectors spur strategic creativity. It is a simple model for incorporating the 36 Stratagems into a comprehensive strategy design process that increases the creativity and speed of an organization's strategic response.

Strategic transformation

This section will walk you through the process of applying the 36 Stratagems as part of a strategic planning process or strategy off-site. The aim is to help your organization rapidly devise and executive an innovative strategy that will take your competition by surprise.

The Strategy Cycle



Step 1: Observe

"Thus, what enables the wise sovereign and the good general to strike and conquer, and achieve things beyond the reach of ordinary men, is foreknowledge. Now this foreknowledge cannot be elicited from spirits; it cannot be obtained inductively from experience, nor by any deductive calculation. 6. Knowledge of the enemy's dispositions can only be obtained from other men."
- Sun Tzu

At least five of the most competitive companies of the decade beginning 1995 analyzed for this book assign their success in part to having observed something that the competition had not. Hon Hai Precision Industries, for example, has become one of the world's largest electronics manufacturers, serving clients such as Dell, Apple, Cisco, Nokia, and Sony, averaging 50% annual revenue growth over the decade, by observing an industry dynamic emerge before others. In 1974, at a time when most electronics manufacturers were busy producing consumer electronics, Hon Hai was founded as a plastics manufacturer. Toward the end of the 1970s, however, Hon Hai noticed an emerging trend. Because the company was located in Taiwan, the outskirts of this emerging trend, Hon Hai was one of the first to observe computer firms increasingly seeking to outsource production in Asia. In 1981, Hon Hai began producing computer connectors for a relatively unknown, six-year-old company called Microsoft. As Microsoft grew into one of the largest corporations in the world, Hon Hai enjoyed the pull of Microsoft's wake. By observing what few others were close enough to observe, Hon Hai took an early role in the emerging computer revolution. Today, Hon Hai produces $16 billion per year in revenue.[iii]

Your chances of outthinking your competition greatly improve if you can observe emerging trends before your competition. Sun Tzu advises using spies to tap such early information. Today, corporations use competitive intelligence. To outthink your competition and market, it helps to put in place an information network that can feed you early warning signs of critical changes. Ask yourself the following:

- What competitive or market developments should I look for?
- What are the "leading indicators" I would expect to see change before these developments appear?
- Am I currently able to observe these "leading indicators"?
- If not, where does this information reside and how can I monitor it?

To prepare for a strategy brainstorming session, gather as much trend data on these "leading indicators" as would be useful. Much of this information may already reside inside your company. Indeed, we have found that corporations often gather more information than they can process and so are surprised to find that many of the "leading indicator" data they need they are already collecting. By triangulating data organized from seemingly unrelated areas of your operation, you may pinpoint what you need.

Step 2: Orient

"Discontent is the first step in the progress of a man or a nation."

- Oscar Wilde

With "leading indicator" data in hand, you can assess your future with some degree of accuracy. This is critical because if you are content with your current future, your change efforts will lack momentum. Over the past ten years, for example, Puma has grown nearly twice as fast and has been nearly twice as profitable as its peers.[iv] Its rise from a troubled company in the early 1990s can be traced directly to the fact that Puma's leadership had grown so discontented with the company's performance that the leaders were prepared to make a radical strategic shift. The leaders replaced top management and embarked on a bold new strategy—one centered on fashion rather than athletic performance. Reebok faced similar financial troubles around the same time that Puma transformed its strategy. But because Reebok's performance was good enough to offer the company's leadership hope, the company never swallowed what was required to transform. In 1994, Puma's revenues were but 8% of Reebok's. Today, Puma has significantly closed this gap, reaching about 50% of Reebok's revenues.

Just as an addict will not seek rehabilitation until he reaches "rock bottom," you and your team's creativity will remain bottled unless you reach discontent.

The easiest way to achieve the requisite discontent is to assess your future from an unattached outside perspective. Ask yourself, what would an outsider say our future looks like? Project your company's future revenues and profits as an outside analyst would (we have even hired outside analysts to do just this). Sit back and assess whether the future to which you are headed inspires you. If you find it uninspiring or, better yet, scary, rejoice, because you now have the chance design a new one.

Step 3: Aspire

To understand a strategist's mind, study chess players. Scientists have been doing so for decades because, unlike strategists from the domains of war or business, strategic skill in chess is measurable. International rankings enable us to distinguish between good chess players (e.g., expert players) and truly outstanding ones (e.g., grandmasters), which in turn allows us to compare in detail their differences.

Such research has shown that good chess players approach their game backward. Novices stare at their pieces and think forward about their moves, their opponents' countermoves, and their possible responses. Novices try to move their pieces toward their opponent's king with the hope this will position them for a checkmate. But the grandmaster does precisely the opposite. She envisions checkmate and steps backward to consider the paths available for achieving it. The grandmaster, thinking backward, nearly always wins.

Master strategists in other context—business, politics, war, etc.—adopt a similar practice. By envisioning the desired outcome (i.e., "checkmate") and thinking backward about possible strategies for its realization, the master strategist can see possibilities others miss. In other words, great military and business strategists seem to envision before they strategize.

Countless good methods are available for creating visions. They all achieve the same thing: a simple, compelling, and measurable picture of your desired outcome. Your football team has a clear vision of its desired outcome (more points than the opponent, a trophy in their hands). Strategizing without a vision is like playing football without keeping score. Agreeing with your team what victory or what "checkmate" looks like will begin unlocking creativity.

Defining such an aspiration has a second salutary effect. It serves as a comparison to the future you defined in the "orient" phase, which exposes the gap between where you are headed and where you want to be. This gap further draws out your team's creativity.

To define your aspiration, answer the following questions:

1. Disregarding my past performance and where my "orientation" exercise suggests I am heading, where do I want my organization to be in the long term? What do I want my company to look like? What do I want to be true? How you define long term will vary according your company's industry and culture. We have found, however, five years to be appropriate in most situations. In answering these questions, stick to what you can see or imagine; avoid numbers or intangibles.
2. If my company is playing a game, how do we want to keep score? Here you decide with what measure you will define winning or losing. Athletic games may use points, while business games use revenue, profit, or shareholder value, but the role of score is the same. It tells you whether you won or lost.
3. Having decided how you will keep score (e.g., profit margin), you must now decide what score you are playing for (e.g., 30%). Ask, what score is consistent with my realizing my long-term vision?
4. Now begin working backward from the long term to the medium term (e.g., from five years in the future to three years from now). Ask yourself, what will have to be true in the near term for me to be confident we are going to achieve our long-term vision? Imagine it is three years from now: you have completed your fiscal year, and you thinking about the year you had. You suddenly realize that your long-term vision is within reach. Indeed, it seems so feasible that you are considering creating a bigger vision. What is true now about your company (again stick to what you can see, avoiding metrics or intangibles)? This is your near-term future.
5. Reviewing again the measure you decided on in question three, what near-term score is consistent with the near-term future defined above?
6. Finally, given your "orientation" exercise, what score is likely to have in the near-term with your current strategy? How does it compare with the aspiration score defined in question five above?

This simple exercise takes you through the thought process of a master strategist. You jump from the present to the far future to envision "checkmate." You work backward to the near future to define your middle game. Then you see where you are currently headed, based on your current situation and predictable trajectory. It should leave you and your team with a clear understanding of the "gap" between where you are headed and where you want to be.

Step 4: Conceive

"When you ask creative people how they did something, they feel a little guilty because they didn't really do it, they just saw something. It seemed obvious to them after a while. That's because they were able to connect experiences they've had and synthesize new things. And the reason they were able to do that was they they've had more experiences or they have thought more about their experiences than other people."

- Steve Jobs[v]

History's most successful military strategists—Sun Tzu, Alexander the Great, Genghis Khan, Napoleon Bonaparte, John Boyd, etc.—share one thing in common: an ability to see strategic options their opponents ignore. This ability is a distinguishing characteristic of strategists from other domains as well. Steve Jobs regularly surprises the market with new designs (e.g., the iPhone) and new business models (e.g., iTunes). Michael Jordan's conception of previously unknown basketball moves (e.g., the "fade away") helped him become one of the greatest basketball players of all time.

Innovative companies are filled with similarly creative strategists. They have more options than their competition because they conceive of more. And since, as Leland Stanford Sr., the founder of Stanford University, noted, "a man will never construct anything he cannot conceive," they can choose strategic possibilities to which their competitors have no access.

How can you conceive of more options? The key, as this book shows, is to use patterns (e.g., the 36 Stratagems) rather than logic at this phase in the strategy development process. By following the steps outlined in Appendix A, you can identify a set of stratagems and use them to brainstorm strategic options.

Though conceiving of options demands little effort or time, we have companies rarely even try. Few corporate strategy development processes incorporate a creative phase. Spending thirty minutes to an hour brainstorming with the 36 Stratagems should generate between fifty and 200 options. In that stack of options may lie the "silver bullet" that will take your competition and industry by surprise.

Step 5: Consider

"Here the success of everything depends on . . . seeing things in a way which afterwards proves to be true, even though it cannot be established at the moment . . ."

- Joseph A. Schumpeter[vi]

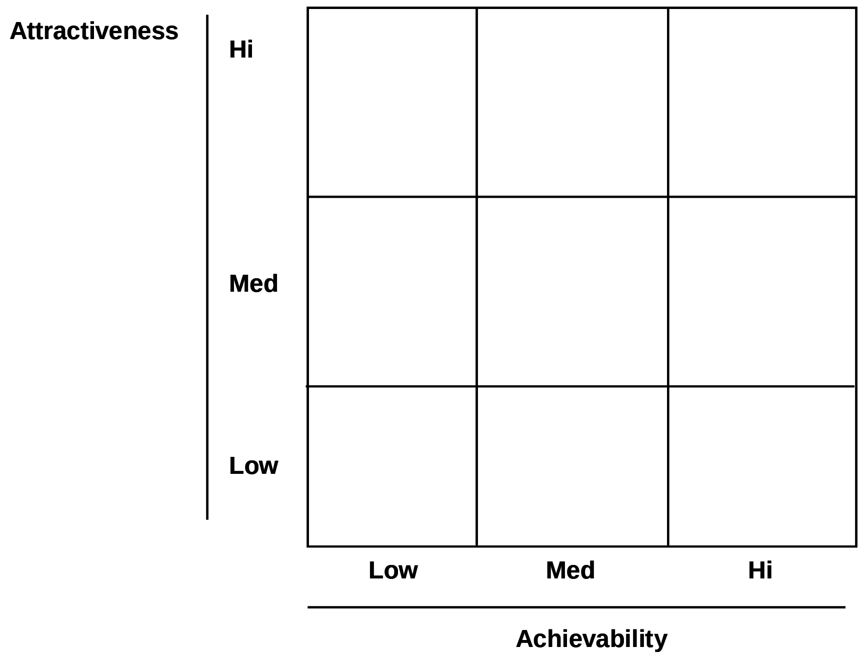
If you have conceived of enough options, you now face two dilemmas. First, you have too little time to think through all 200 options. Second, the most innovative options will necessarily seem illogical. If they truly are innovative, these ideas will be inconsistent with prevailing common logic. The result is that most companies, due to lack of time or appetite, kill off radical ideas before even considering them.

This killing off of ideas is subtle. It takes but a smirk shared by the group or a silent pause in conversation to set the idea aside from consideration.

Image if Michael Dell had conceived of his innovation to sell computers directly to consumers after he graduated from college instead of before. His interest in computers might have led him to a job at Hewlett-Packard. Had his innovation then occurred to him, had he mentioned it in a team brainstorming session, he would almost certainly have been dismissed. His employer, which depended on retailers and could generate significant profits through more mundane improvements (e.g., lowering costs of goods sold or improving its marketing spend effectiveness) would not have even considered Dell's idea.

To avoid your company's tendency to discard ideas they feel are too "new," we have found it helps to assess your ideas across two unrelated dimensions: attractiveness and achievability. Attractiveness is defined by the impact the idea would have on your business if your ability to achieve the idea were of no consequence. If you had a magic wand with which you could achieve every idea you conceived, how significant would the impact of this idea be on your business? Judge each idea's attractiveness using a scale of, say, high, medium, and low.

Then assess the achievability of each idea. Consider how little it will cost, how quickly it can be implemented, and to what extent you have the capabilities or knowledge to do so. Again judge the achievability of each idea as high (low cost, quickly implemented, and leverages our capabilities), medium, or low.



This exercise will result in four types of ideas:

1. "No brainers" – highly attractive and achievable ideas that you should probably begin acting on immediately.
2. "Tactics" – unattractive but achievable ideas that are easy to execute but that will not significantly improve your situation. You may want to execute these but do not prioritize them as strategic.
3. "Wastes of time" – unattractive and difficult-to-achieve ideas that are probably wasting resources. We often find that through this exercise companies identify many initiatives that are time-wasters. Remove these from your agenda to focus on higher-return efforts.
4. "Crazy ideas" – these are highly attractive but low achievable ideas. Innovative companies tend to keep these ideas alive. They continue to discuss such ideas, looking for ways to improve their achievability. Most companies, however, have no room for such ideas and risk being surprised later, but the creative competitor finds a way to make the idea work.

By jointly classifying each idea into these four quadrants, you and your team have to consider every idea. You remove completely your company's tendency to kill off ideas by refusing to consider them.

To complete the process, remove "wastes of time" and "tactics" from discussion and focus your time discussing how you can turn "crazy ideas" into "no brainers." The magic is in the "crazy ideas." These are ideas with true innovative potential.

Step 6: Choose

"If we want to understand creativity, we need to understand the process of choice . . . How can we enhance creativity by improving the way we select and implement new ideas?"

- Mihaly Csikszentmihalyi[vii]

Having generated a large number of options, considered them all, and identified a subset worthy of more complete analysis, you must now choose those you will execute. This requires transitioning from the creative right brain to the logical right brain.

Transitioning between the right and left brains can feel uncomfortable because your everyday business activities probably demand just one mode of thought. Your job demands you either usie logic all day or asks you act creatively all day. Switching seems unnatural.

Highly analytical companies (e.g., asset managers, engineering firms) tend to resist adopting a creative mode and so fail to produce sufficient strategic options. Highly creative ones (e.g., advertising agencies, design firms) tend to similarly resist putting their ideas to the test of data.

Choosing good ideas, however, requires that you do both. You have been creative. If you can now be analytical, you will be battling with two fists while your competition comes at you with one.

With the proper analytical approach, you can significantly reduce the risk of choosing the wrong idea as well as the time that analysis requires. Five steps will help you rapidly analyze your ideas:

1. Ask yourself, what would I have to believe to believe this were true? Write down three to seven things that would have to be true.
2. For each "belief" identified, ask again, what would I have to believe to believe <u>this</u> were true? Write down another two to three things for each belief.
3. Identify what data would support each of the requirements identified above. If you would have to believe, for example, that your product's lifespan will be at least fifteen years you might decide you need data showing that the lifespans of similar products in the past were at least this long.
4. Identify from what sources you can gather the required data.
5. As quickly as possible, gather the data and calculate your results.
6. Review your analysis and choose between three options: (a) execute the strategy, (b) abandon the strategy, or (c) determine what specifically you need to know before you are willing to do either.

This process should produce a set of strategic priorities (ideally between three and seven) that form a holistic advance.

Step 7: Commit

"Gongs and drums, banners and flags, are means whereby the ears and eyes of the host may be focused on one particular point."

- Sun Tzu

Your strategy is not what you say you will do, it is what you actually do. You have not yet created a strategy unless your action on the front line—how you treat your customers, from where you source your product, what you sell, through which channels you distribute, etc.—matches what you intended.

This final step involves aligning roles, measures, incentives, and communication. You must redefine roles to ensure people are taking the actions on the front line that are consistent with your new strategy. You then establish a set of measures to judge where and how well you are succeeding or failing. Then align incentives to these roles and measures. Finally, develop a compelling message and communication plan to ensure that everyone who needs to know is familiar with and is regularly reminded about your new strategy.

You have now transformed your strategy. But you are not yet done because the cycle never ends. You observe your progress, orient yourself to whether you are winning, aspire, conceive, consider, choose, and commit again. Companies that cycle through this process creatively and quickly are able to consistently outthink and outmaneuver their competition.

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[i] Quoted in Hammond, Grant T., *The Mind of War: John Boyd and American Security* (Smithsonian Institution, 2001), p. 35
[ii] Company web site (www.hbc.com)
[iii] Company Financials for 2005
[iv] Measured in cumulative average revenue growth and average EBITDA margins over ten years ending 2005
[v] Warren Bennis and Patricia Ward Biederman, *Organizing Genius* (New York, Basic Books, 1997) p. 66
[vi] Schumpeter, Joseph A., *The Theory of Economic Development* (New York: Oxford University Press, 1961), p. 85
[vii] Psychology Today staff, "A Creative Dialog," *Psychology Today*, Jul/Aug 1999