Ten Tests of Strategy

Idea In Short

Stop chasing the latest strategy fad. Take your existing strategy and stress-test it against ten rigorous tests covering market advantage, granular segmentation, privileged insights, uncertainty, commitment, bias, conviction and execution. Most strategies pass fewer than four.

McKinsey's Advice

McKinsey, in a 2011 article, made the valid point that executives too often treat strategy as a procedural exercise or set of frameworks rather than a way of thinking through problems. Their advice is direct. Do not look for the newest strategy fad or business guru. Instead, take your strategy and stress-test it against ten rigorous tests. 1

In true McKinsey style, they applied rigor to what seems like a qualitative exercise. They ran the tests by 700 strategists and 2,100 executives. They found that most company strategies pass fewer than four of the ten tests. This is fascinating and not entirely surprising. Strategy is hard, and most organizations settle for planning rather than genuine strategic thinking.

Apply What You Already Know

Keep it simple and consistent rather than piling more concepts into your head. A simple analogy illustrates the point. Everyone knows what causes obesity: too many calories and not enough exercise. Yet more than 50 percent of Americans are considered obese. Knowing is not enough. Strategy, like health, requires your head, heart and hands working in alignment.

Test One: Will Your Strategy Beat the Market?

This is the main question. Is your company able to harness some competitive advantage, an economic moat, which allows it to create and keep more value than competitors? Think of

Porter's classic five forces framework. 2 Suppliers, buyers and substitutes can all eat away at your profits. What is keeping your share of profits safe?

The goal of strategy is to create and sustain competitive advantage. It is not about beating your competition. It is about winning at the game you have set out to play. Play your own game, not someone else's out of fear of missing out. Markets drive reversion to the mean, meaning top performers tend to get worse and bottom performers tend to improve over time. Operational efficiency is not strategy.

Test Two: Does Your Strategy Tap a True Source of Advantage?

Without a mini-course on strategy theory, consider a few key questions. Do you have a positional advantage in your industry? Do the right customers seek you out? Do you have control over valuable resources such as patents, process knowledge or management? Have you bundled activities together so it is hard for competitors to mimic you? Causal ambiguity is a real advantage. When competitors cannot understand why your approach works, they cannot copy it.

Test Three: Is Your Strategy Granular About Where to Compete?

In marketing we learn about segmentation, targeting and positioning. McKinsey argues that companies do not segment enough. They urge you to think deeply about customer, geographic and product-using segments. Companies need to de-average their approach to different markets. The days of mass-market strategy are dead. Any executive who talks about customers and markets generically is committing heresy in today's environment.

Test Four and Five: Ahead of Trends and Privileged Insights

Does your strategy put you ahead of trends? This test is self-explanatory but frequently failed. Does your strategy rest on privileged insights? This is a fancy way of asking whether you have unique information, data, analysis and insights. There is a sea of data, but that is the obvious field all competitors look through. Find out what is happening at the edges of the industry and pick up the weak signals buried in the noise.

McKinsey suggests rigorous brainstorming on what key questions could dramatically disrupt, change or challenge your business. This leads to the next test about uncertainty.

Test Six: Does Your Strategy Embrace Uncertainty?

In this volatile, uncertain, complex and ambiguous world, you cannot predict anything with certainty. 3 That said, uncertainty is not binary. It is not simply know or do not know. McKinsey characterizes four levels of uncertainty. Level one offers a reasonably clear view of the future, a range of outcomes tight enough to support a firm decision. Level two presents identifiable outcomes for which a company should prepare. Level three represents possible outcomes as a probability distribution rather than discrete points. Level four features total ambiguity where even the distribution of outcomes is unknown.

This is the fundamental difference between strategic planning and genuine strategy. Customers can do whatever they want. Rivals and new entrants get a vote. They hire smart people too. There is enormous uncertainty, so leaders must be realistic about it.

Test Seven: Does Your Strategy Balance Commitment and Flexibility?

A market-beating strategy will focus on just a few crucial, high-commitment choices to be made now, while leaving flexibility for other choices to unfold over time. This is the point. If we agree on the first six tests, then it comes down to making good decisions, smart bets and building a strong culture for emergent strategy decisions. Management is a practice, not a formula, framework or fancy diagram. Are you consistently making better decisions more quickly than the competition?

Major on the majors and minor on the minors. Focus your analysis and worry on the most important decisions and commit to them. For other details and lower-level issues, respond flexibly and stay opportunistic. Get the big things right.

Test Eight: Is Your Strategy Contaminated by Bias?

Without further reading, the answer is yes. McKinsey goes through a list of potential biases, all things learned in business school. Over-optimism, anchoring, loss aversion, confirmation bias, herding and champion biases. What is in our heads can often work against us. Reed

Hastings, co-founder of Netflix, explains that chief executives need to farm for dissent. It is too easy for leaders to surround themselves with people who always say yes. That is poison for decision-making.

Test Nine: Is There Conviction to Act?

This is perhaps the biggest failure of most corporations. They do not stick to one strategy long enough to really know whether it works. Since the average chief executive tenure is a few years, someone is always coming or going from the executive suite. Imagine a football team with a revolving door of players. How much coordination would they have? Catherine Cook observed that if you are not making mistakes, you are not making decisions.

Test Ten: Have You Translated Strategy Into Action?

This test is self-explanatory but critical. A strategy that lives only in a presentation deck has no value. It must connect to concrete actions, resource reallocation and operational changes. The gap between strategy formulation and execution is where most value is lost. Translate your strategy into clear steps that people at every level can understand and act upon.

The Head, Heart and Hands Framework

Long lists are hard to remember. A practical grouping fits the worldview that solving problems requires head, heart and hands. The head covers analysis, data, facts and logic. Do you have a true advantage based on unique insights, or are you just downloading analyst reports? Do you have a culture of intellectual honesty and aggressive curiosity, or is it a stew of politics? Are you diligently looking for leading indicators through messy real-time information?

The heart covers passion, drive and founder's mentality. Are you committed to your plan yet flexible enough to adjust? Are you wedded to old strategy that is not working? Would your target customers say that you understand them better than competitors? If you were 25 years old, would you want to work here?

The hands cover implementation and change management. Is your strategy easy to implement? When the company wants to take action, how many meetings are needed? Is your employee engagement high enough to catalyze customer engagement? Do you have a culture of managing risk or leading change? Strategy ultimately succeeds or fails not in the boardroom but in the daily decisions and actions of everyone in the organization.

- 1How Strategy Champions Win
- 2Porter's Five Forces Analysis
- 3VUCA

Summary

Strategy is hard, which is why consistently beating the market is difficult. The ten tests require head for analysis, heart for commitment and hands for implementation. Focus on the major decisions, commit deeply to a few choices and maintain flexibility for the rest.