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).*

Fred Reichheld: Customer centricity and the strategic power of embracing the "Golden Rule" in business
Brian Leavy

Few have done more to advance the cause of a customer-first approach than Fred Reichheld, pioneer in the area of customer loyalty economics and creator of the Net Promoter Score (NPS), the predominant framework for measuring customer experience. In his latest book on NPS, *Winning on Purpose: The Unbeatable Strategy of Loving Customers*, co-authored with Bain colleagues, he aims to show how customer capitalism can promise not only economic advance but also help to further humanize and elevate the world of business.

Strategy & Leadership: How did you first become interested in "loyalty economics"?

Fred Reichheld: Early in my career I began noticing companies like Enterprise Rent-A-Car, USAA, Chick-fil-A and others across a range of sectors with great performance that couldn't be explained by existing strategic or economic frameworks. The common denominator: these firms were earning superior loyalty from their customers and employees—and their profitable growth was remarkable.

S&L: Can you outline how your perspective on Net Promoter Score, and your goals for it, has evolved?

Reichheld: At first, I viewed NPS as an improved metric for measuring the quality of a customer relationship—a statistic based on the customer's likelihood to recommend a product or service to a friend, family member or colleague. NPS, implemented correctly, reveals a lot about how consistently a company lives up to its purpose of enriching customers' lives.

S&L: *Winning on Purpose* argues that "there is one (and only one) purpose that generates long-term prosperity for a business" and that is "to enrich the lives of customers." Why this and not profits?

Reichheld: When profits become purpose, companies will pursue many options to boost accounting profits. When leaders inspire team members to embrace the mission of enriching customers' lives they help their teams lead lives of meaningful service.

S&L: Finally, why do you believe that the customer-centric model will be more important than ever in an AI-intensive Digital Era in which bots and algorithms are increasingly dominating company-consumer interactions?

Reichheld: Digital innovations hold enormous promise for improving the lives of customers and employees. Microsoft Teams for example let us boost personal productivity while eliminating much of the need for commuting and travel. But digital tools must embrace the right objective which is to help employees enrich the lives of customers.

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In the digital age, the combination of technology and radical management practices drives competitive advantage

Stephen Denning

In November 2011, management guru Gary Hamel declared boldly in a *Financial Times* interview, “I am willing to stake my reputation that we will see more dramatic change in the way management is organized in the next 10 years than we’ve seen in the last 60 or 70.”

Almost exactly ten years later, the *Financial Times* management columnist, Andrew Hill, published his conclusion that not a lot had changed. According to Hill, “a manager from 2011, or 1991, or even, frankly, 1961” would still feel right at home in the office of 2021. Hill acknowledges that change is happening in the form of “management fashions,” though mainly in obscure firms,

Large-scale management change is already here

Those conclusions don’t match reality. The fact is that Hamel’s “radical management innovations” are already staring us in the face, not in a couple of tiny obscure foreign firms, but in the success of the most valuable firms in the world.

They are obvious, not only in the five largest companies—Apple, Alphabet, Amazon, Microsoft and Tesla, with a combined market capitalization of some $9 trillion—but also in smaller digital winners that are growing fast, including AirBnB, AMD, Deere & Company, Meta, NVIDIA and Shopify.

Whether traditional management thinkers want to recognize it or not, we are already living in a new economic age—with radically different management practices that are driving the growth of the economy. The current new age has been triggered by combining extraordinary new technologies and new management principles. The new age has different economic dynamics, different management principles, different social consequences and different political implications, as compared to the industrial era.

The radical new management principles

The new management principles – instead of focusing on internal efficiency and outputs—is characterized by an obsession with creating value and favorable outcomes for customers and users. Instead of leadership located solely at the top of the organization, leadership and initiative that create fresh value are nurtured throughout the organization.

In the current era, managers whose careers thrived in hierarchical corporations are now spending frantic days and sleepless nights trying to understand the new technologies and grasp the new realities of managing them in a volatile, uncertain, complex and ambiguous world. They are discovering that it is not just technology that generates great innovation: it is the combination of exponential technology and new management principles that makes the difference.

Innovative firms with a total value of more than half the economy are being run with a radically different management mindset, principles and skills. It’s just that some analysts – like *Financial Times* management columnist Andrew Hill, and many of his peers – are ignoring transformation change in the most dynamic half.

Isolate and SEAL: two steps to designing an innovative and potent business model

Sayan Chatterjee

All successful innovative business models eventually change their industry value chain. But ascertaining the relative significance of operational changes to the business model is often not obvious in the planning stage. Some changes to operations seem unremarkable but have a profound effect on competitive advantage. Take, for example, Southwest Airline's decision to fly only one type of plane, or Aldi supermarket leaders' decision to have checkout clerks be seated instead of standing.

A systematic and repeatable process – Isolate and SEAL – can enable strategists to identify such potentially game-changing operational actions that will support significant business model innovations.

Instead of trying to decide "what to do" to create an operational advantage, businesses attempting to innovate "should first identify the core objective that operationalizes the winning profit logic." For Southwest this is a 15-minute gate turnaround. For Aldi supermarkets the core objective is to speed up shopping in general and specifically for clerks to check out 40 items per minute, which they can do faster when seated.

To identify and deliver the most potent operational objectives, a company seeking to innovate its business model will need to deconstruct all the elements in its existing industry value chain to see if each one helps or hurts in delivering its core objective.

The two-step Isolate and SEAL process formulates the actions needed into a strategic model.

Step 1 – Isolate: split the value chain's elements into its component parts.

Step 2 – SEAL: Reconstruct the value chain using the four actions that effectively deliver the core objectives (Shift in space and time, Eliminate, Alter/Add, Leverage).

Not all the actions are needed at every stage and some actions are interdependent. The process may need to go through a few cycles to ensure alignment between the core objectives and a final value chain process that the business can execute.

- Shift – in space and time– the sequence in which the business carries out the industry value chain components.
- Eliminate some components that are not needed to deliver the core objectives.
- Alter or Add some of the components.
- Leverage the output from one component to facilitate the Alteration or Shifting possibly by combining components.

Once the primary value chain components are isolated, next decide what SEAL actions would help make them happen.

Profit logic that satisfies desired customer outcomes

Isolate and SEAL processes enable leaders to identify actions that can operationalize the profit logic. If these actions to achieve core objectives result in a value chain that is executable by the company then profitability is a likely outcome.

The end-to-end process is demonstrated using a historical review of the emergent strategy that produced the highly successful business model of Southwest Airlines.

When and how to use a fighter brand to combat a low-price entry

Daniel Deneffe and Herman Vantrappen

New market entrants often attempt to take away share from incumbent companies by launching low-priced products or services targeted at price-sensitive customers. Those incumbents may try to win back lost customers by launching so-called "fighter brands."

A fighter brand is designed to combat, and ideally eliminate, low-price competitors while protecting an organization's premium-price offerings. The track record of fighter brands, however, is quite dismal. They have often been shut down or repositioned within a couple of years after launch. But strategists should not give up on a fighter brand strategy altogether; under certain conditions a fighter brand can be effective, if it is correctly positioned.

A concrete decision-making framework will help managers think through the specific design of a fighter brand.

The framework takes managers through four steps:

1. Clarify that the objectives of the fighter brand are to increase overall returns by profitably by winning back customers from the low-priced entrant while minimizing the negative impact – or "cannibalization" – of profits earned from the company's flagship product.
2. Verify that the company is serving two customer segments clearly distinct from each other in terms of price sensitivity – "low" and "high."
3. Decide which features, if any, should be removed or added to the fighter brand to differentiate it from the low-priced entrant's offering. The notion of must-have features –"must-haves" – is at the core of the fighter brand framework.
4. Decide upon the other dimensions of the marketing mix for the fighter brand::
   - The brand to use, and whether it should have any association with the umbrella brand of the company's flagship product.
   - The price to charge relative to the low-priced entrant's product.
   - The sales channel and promotion to use relative to those for the company's flagship product.

The finding

Many companies have become reluctant to develop fighter brands, given that most fighter brands fail to achieve their objectives. The proven framework offered shows, however, that if a company's strategists can identify at least one unique must-have feature for the value segment with high certainty, and remove it from the fighter brand targeted at the price segment, the risk of cannibalization is minimal.

Tools the board can use to prevent an M&A synergy trap

Mark L. Sirower and Jeffery M. Weirens

Boards are routinely given a board book that reviews the strategy and valuation of the M&A deal that management is promoting. But are they asking the right questions or having the right discussions? This is a critical concern given that so many bad deals make it out of the boardroom. Directors need more and better information about proposed deals before they cast their votes.

Several simple analytical tools and a set of questions can help boards drive more informed discussions about potential deals.

A helpful set of four analysis tools

1. Shareholder value at risk (SVAR)

Before committing to a major deal, both parties will need to assess the effect on each company's shareholder value should the synergy expectations embedded in the premium fail to materialize.

The use of cash versus stock as the method of payment has profound ramifications for the shareholders of both acquiring and target companies and a substantial impact on SVAR.

2. The PMI Board Pack

Post-merger integration (PMI) is a highly complex process. The pace, importance and sheer number of decisions that will need to be made for a merger far outstrip the normal rate of decision-making.

The PMI Board Pack is designed to help the board ensure that senior management is ready to avoid the common pitfalls of PMI. Before a deal is approved by the board and announced publicly, senior management should present the following five essential elements:

- A PMI process calendar showing phasing of activities and decisions.
- The key top-level shaping decisions to be made up front.
- A tailored integration approach that is clearly articulated.
- The structure, teams and resourcing to deliver the PMI.
- The business plan that delivers the performance promises for the deal.

3. The Meet the Premium Line and Plausibility Box

Short-term earnings accretion to the acquirer remains one of the most popular thresholds in judging whether or not to do a deal. It's also typically the first order of business in investor presentations. The importance of the MTP Line for senior management teams and boards is straightforward: Deals whose combination of percentage cost reductions and percentage revenue enhancements put them below the line should be avoided—or at least put under more scrutiny.

4. The Capabilities/Market Access Matrix and the Synergy Mix

The next step in the analysis is to consider whether the proposed combination of cost and revenue synergies—even if that data point falls within the Plausibility Box—makes operating sense, given the strategic intent of the deal and the assets the transaction brings together.

Implementing this approach may seem challenging, but it translates to some minimum basic considerations for directors. Before approving a deal and recommending it to shareholders, directors should ensure that senior management offers a clear business case and has an operating model—and a plan— in place. And, knowing this, senior executives must be prepared to withstand such scrutiny.

Five strategic tech and talent trends for 2022 and beyond

Haynes Cooney, Anthony Marshall and David Zaharchuk

Over the past year, the IBM Institute for Business Value (IBV) surveyed and interviewed tens of thousands of executives, employees and consumers around the world to learn what high-performing organizations are doing differently, and where executives are making the biggest bets. Technology and talent initiatives are top priorities for the coming year. Executives are learning how to redefine how humans and technology work together.

As open innovation, ecosystem partnerships and integrated customer experiences become increasingly important, here are five extensively researched trends that executives can explore to help prepare for a future characterized by disruption and change.

Trend 1: Digital transformation has become a way of life

Many executives have realized that transformation is a journey. Rather than working toward a perfect end state, they're focused on making their organizations more responsive. They see technology playing a key role in building resilience and adaptability, ranking it the top external force that will impact their businesses in the near term.

Trend 2: Tech adoption should reshape business operations

Rather than rolling out isolated innovations that streamline individual workflows, executives must focus on building integrated systems that revolutionize business models.

Trend 3: Security needs strengthening to underpin sustained innovation

As companies expand their cloud footprint to enable remote work, integrate supply chains and streamline customer experiences, they must also evolve their approach to cybersecurity.

Trend 4: Sustainability and transparency are urgent priorities

Many companies have a sizable information gap they need to bridge. While our 2021 research found that 9 out of 10 companies say they will be working on various sustainability initiatives across the enterprise, another study found that only 1 in 3 of consumer companies are measuring their progress.

Trend 5: Human capital is increasingly precious and scarce

The “Great Resignation” is picking up pace. A record-breaking 4.3 million Americans quit their jobs in August 2021. More than half (56 percent) of those that voluntarily changed companies this year cited the need for more flexibility as a key reason for making the switch, while nearly one-third said they wanted to work for a company that better fits their values.