Strategic Management Center

Virtual Members Meeting

18th November 2021

Minutes of Meeting

In attendance:

Nicola Adams	BP
Paul Barrett	Babcock
Wouter DeKlein	Shell
Subha Dutta	Shell
Stuart Farmer	ABF
Ananth Gopalakrishnan	Shell
Yitzchak Grant	DS Smith
Amie Hows	Shell
Alan Line	ABF
Alex Manisty	DS Smith
Gabriel Ratcliffe	ABF
Shoubhik Roy	Shell
Robert Stoddard	BP
Brian Wilks	Shell
Paul Titcombe	Atkins

From the Strategic Management Center:

Stephen Bungay
Andrew Campbell

Stephen Bungay: Agile Strategy

The theme of agility is now on the agenda of many companies, but it is far from clear what 'agility' means, particularly at the level of strategy. The purpose of this meeting was to explore what an agile strategy could be, and to offer a way of understanding it against the background of the work ASMC has done on strategy execution and uncertainty. Since the last meeting on this theme, Stephen has worked with some Members to develop the approach further, and that work was featured in the course of the afternoon.

Stephen began by summarizing the results of a report published in April about the current state of agile practices. Most companies in the survey had some experience of agile. It is becoming the new norm in IT processes, but although it is spreading beyond IT the report mentions that inconsistent processes and internal cultures are impeding the adoption of agile methodologies. Despite this, as many as 70% of Fortune 500 companies are trying to introduce agile at scale, often in combination with an approach known as DevOps, which is designed to overcome silos and extend the reach of agile practices beyond their origins in software development. The main benefits cited are speed and quality.

Stephen questioned whether the spread of agile practices could result in an agile strategy, and suggested that the agile community were trying to achieve results in areas that agile practices were not designed for.

At their core, agile practices involve setting up semi-autonomous teams which modify their output rapidly based on feedback from a customer. The 'agility' is a function of the ability of a team to respond to the feedback by changing the product it is developing. It is a method for innovation, which is effective when there is a product or outcome to be delivered to a user or customer. Strategy is not a product and it does not have a customer.

However, calls for strategy to be agile are growing. Stephen began by asking: 'What could an agile strategy be?' and suggested that it would involve rapid iteration cycles to respond to emerging effects rather than rapid product modifications to respond to user feedback. The principle is analogous, but the approach would be different, and the success of the result would not be a function of speed to market and customer satisfaction, but the extent to which the formulation of the strategy allowed the organization to adapt to changing circumstances.

One member commented that Stephen's account of recent developments sounded very sceptical. Stephen clarified that agile practices create a lot of value in the right context and he is not trying to pour cold water on them. The evidence that agile practices work well in software development is compelling. He is simply questioning whether spreading them everywhere is a good idea and whether scaling them up to cover a large number of teams will in itself make strategy agile. His first hypothesis is that it would not.

At this point, Stephen asked the group what experiences they had had with agile practices:

1. One member commented that they had used agile techniques to develop strategy in a very functional organization. This changed the way they set priorities and they then set up squads around the priorities so that resources could be shifted towards them more rapidly. They are also interested in building agility into strategic plans when the uncertainties are large.

2. Another Member company has had mixed experiences. One condition of success seems to be that a team is working towards a shared end-point. They developed strategies in Germany and India using an agile approach, cycling hypotheses round 60-70 people across upstream and downstream businesses and iterating. This worked well. However, it did not work so well for corporate strategy where different teams were working on

different aspects of the strategy to different timeframes, which meant that a scrum-type rhythm did not work.

3. The key question is what you are trying to achieve. If you understand that, bringing all the necessary skills together, developing a minimum proposition and testing it so that you don't over-engineer can be effective. A kanban board can help, but what matters is applying the principles of agile rather than any specific technique.

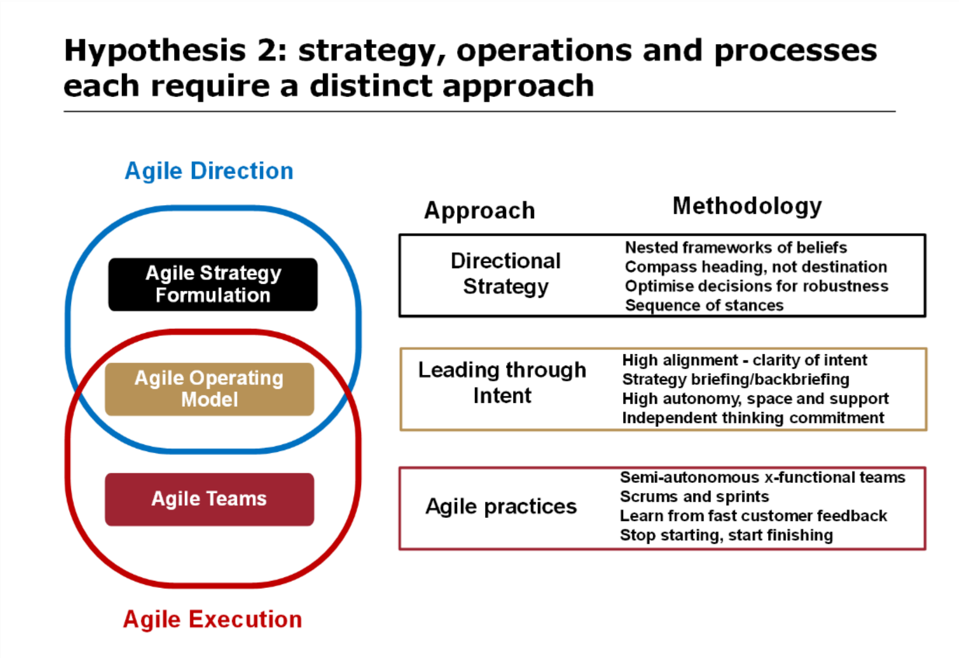
4. That was echoed in further comments from the same company. The most valuable thing is having points at which you stop and assess whether what has been done is working so that you have a natural point of reflection, instead of starting out on a journey and just keeping on going. However, scepticism is well-placed because agile practices can be misapplied. For example, if you have a two-week sprint on work that has a much longer lead time, nothing will move on a kanban board for a long time, and this can de-motivate people. It fails when fast feedback loops are not a given.

With the experience of Covid-19, executives found themselves confronted with an unexpected, sudden and radical change in the environment. In the face of that, many needed to re-position their businesses at speed, and were held back by established processes. Some needed to 'pivot', but found the experience painful. The question then is what it would take to make an organisation agile, in the sense of being quick and responsive to changes in the situation, and whether agility can have value at the level of strategy.

This suggests that an 'agile strategy' would be one that sets direction in such a way that the organization can adapt rapidly in the course of execution. That implies that it should form a framework for decision-making that enables rapid decisions to be taken at the operational level. As the comments above suggest, agile practices need a shared goal and framework, which is what strategy can provide. The strategy can be developed in an agile way, but once set it would not itself constantly change but would allow operations to do so. That implies that the strategy could be translated into a set of more specific decision-making frameworks nested in each other, allowing a stepped response to unforeseen events. Rather than responding to customer feedback, the organization would respond to events in the external world, meaning that it would have to establish an appropriate operating rhythm to monitor changes in the environment.

So an agile organization needs a strategy which provides agile direction and agile execution. Agile direction would create room for rapid course adjustment and agile execution would be based on an operating model that enabled the organisation to respond. Parts of the operation may use agile practices, but neither the way strategy is formulated nor the way in which operations are conducted would necessarily involve agile techniques such as scrums and sprints.

Stephen's second hypothesis is that that the work ASMC has done on strategy in uncertainty which has resulted in an approach know as 'directional strategy', and on strategy execution which has resulted in the approach known as 'leading through intent' could form the basis of what might be called an 'agile strategy'. Rather than competing with agile practices they complement them by creating the context within which those practices can be deployed most effectively. This approach depends on distinguishing three distinct levels:



Agile practices can be applied to appropriate processes within an agile operating model based on 'leading through intent'. Leading through intent involves creating high alignment by using a process of briefing and backbriefing, and giving people as much autonomy as possible to adjust their actions as the situation changes (see Stephen's book 'The Art of Action'). In order to allow such an operating model room to have traction, 'directional strategy' formulates strategic direction as a compass heading consisting of sets of beliefs, with stances changing over time and decisions optimized for robustness.

Adaptation is possible at each of the three levels. Agile practices adapt to customer feedback, leading through intent adapts actions to changes in the situation and directional strategy adapts stances to changes in the strategic environment. This raises the question of the nature of change at each level, and how you can decide how radical the adaptation should be.

Prompted by some comments made by a Member at the last meeting, Stephen introduced the idea of 'pace layering'. This idea originated with the architect Frank Duffy about the different rates at which the elements of buildings become obsolete and decay. It has been taken up by the American thinker Stewart Brand in an article from 2018 called 'How Complex Systems Learn'. The basic idea is that in a complex system, there are different layers which change at different rates, but interact with each other at their interfaces.

A business is a complex system and Stephen suggested that there are three relevant layers of change which can be understood as an ocean. On the surface is the weather which is fast changing, unpredictable, but transitory. Being visible it gets most of the attention. Just below the surface are currents which are continuous, form recurring patterns and change more slowly. These surface currents are invisible but can felt. Below these are deep ocean currents that are enduring but shift slowly. They are imperceptible, but very powerful.

Pace layering: the environment as an ocean

Factor	Perception	Impact: time	Impact: force
Weather	Visible	Fast changing, unpredictable	Transitory
Surface currents	Felt but invisible	Continuous, recurring	Strong, but can be countered
Deep ocean currents	Imperceptible	Enduring, shifting	Very powerful, overwhelming

The three layers are independent, speed up and slow down, but interact and affect each other

The challenge is to distinguish the three layers, so that you do not respond to surface weather by making long term commitments, and do not to ignore deep ocean currents because they are invisible. In the words of Stewart Brand, 'fast gets all the attention, slow has all the power'. We need to be *responsive* to the weather, *adapt* to surface currents and be ready to embark on *transitions* as deep ocean currents shift. In broad terms, agile practices allow us to respond to the weather, leading through intent allows us to adapt to surface currents and directional strategy allows us to transition as deep ocean currents shift.

Identifying to which layer changes in the environment belong cannot be exact, and requires judgement as well as research. However, relevant questions to ask might include: 'what is the historic pace of change?', 'has it reached a point at which the pace could speed up?', 'how enduring is it?' and 'is it driven by a deeper level change?'

To take the realm of technology as an example, we might categorise launching an app as a response to the weather, applying AI in parts of the business as an adaptation to a surface current and moving to a digital platform as a transition due to a deep ocean current. The three layers interact. If we have already made the transition to digital, introducing AI is easier and creating new apps can be done quickly. Our responses to deeper levels enable us to be more agile at more shallow ones.

Translating the metaphor into business examples

Factor	Technology	Supply chain	Environment	Competitors
Weather	Apps	Capacity constraints	Health foods	New products/ services
Surface currents	AI	Supplier relationships	Food sources	New entrants
Deep ocean currents	Digital	Supply chain configuration	Carbon footprint	Disruptive business models

Appropriate responses are different

(Another example not mentioned in the meeting might be hydrogen. Research into the use of hydrogen as a fuel has been going on for decades. Its potential has long been recognized but the technical and economic hurdles have taken a long time to overcome. Over the last 2-3 years, a tipping point has been reached, and now the use of hydrogen as a fuel in applications in which electrification is difficult or impossible constitutes a surface current. That implies that investing in some capability which would allow a business to be a player somewhere in the long and complex green hydrogen value chain would be a sound move in principle, whatever setbacks or problems may arise (i.e. the weather conditions on the surface). An investor can take confidence in that from the deep ocean currents concerning energy, where a slow but inexorable shift has taken place from cost and convenience to carbon-free as the main driver of use. Had that deep ocean shift not taken place, hydrogen would probably still be seen as a difficult and expensive marginal product.)

One Member took us through a series of decisions made in the business which can be mapped onto the ‘pace layer’ model above.

The business had long been advocating the use of re-cycled paper to make cardboard. 80% of its volume is recycled. One decision taken in relation to that was to sell a very profitable plastics business, in line with the ‘Blue Planet’ trend, which was understood to be a surface current rather than a change in the weather.

However, China was changing the market for virgin paper which was also consolidating so, for the first time, the company bought a virgin paper mill at a high price. At the time, they were excoriated for doing so, but now there is a global shortage it looks like a wise move. What might have been dismissed as a change in weather conditions was more like a shift in the surface currents.

One decision also criticized at the time was getting in to e-commerce very early. This was driven by the identification of a deep ocean current. It now seems obvious, but most of their competitors were put off by the very high cost of entry. The company was able to pick up a deep ocean current before others did because every few years it runs scenarios designed to identify them.

One further deep ocean current is on the agenda now. Re-cycling paper is a carbon-intensive process. If you make paper from trees, you burn the bark to dry the paper. If you re-cycle you have to add heat from a hydrocarbon like gas. So the issue now is how to de-carbonise the process, and that is a current that lies deeper than re-cycling. It is also possible that the plastics industry will have a resurgence with re-usable packaging. The fundamental issue is the carbon footprint.

Acting on deep currents can be unpopular because people who are only observing the surface weather cannot understand the logic for doing so. However, this example shows how identifying and responding to deep currents makes it easier to respond to shallower ones and may indeed be a condition of being able to do so. Today, the company's customers are increasingly wanting to deal with them as e-tailers, and it has started a webshop for small retailers. Their ambition is to be leaders in e-commerce and the easiest company to do business with. They also have to address cross currents – recycling vs reuse vs carbon, each of which can affect the impact of the other. But navigating this is only possible because the North Star is clear.

After the break Stephen used the example of a Danish regional bank called Sydbank to explain how formulating a directional strategy can allow a rapid response to circumstances.

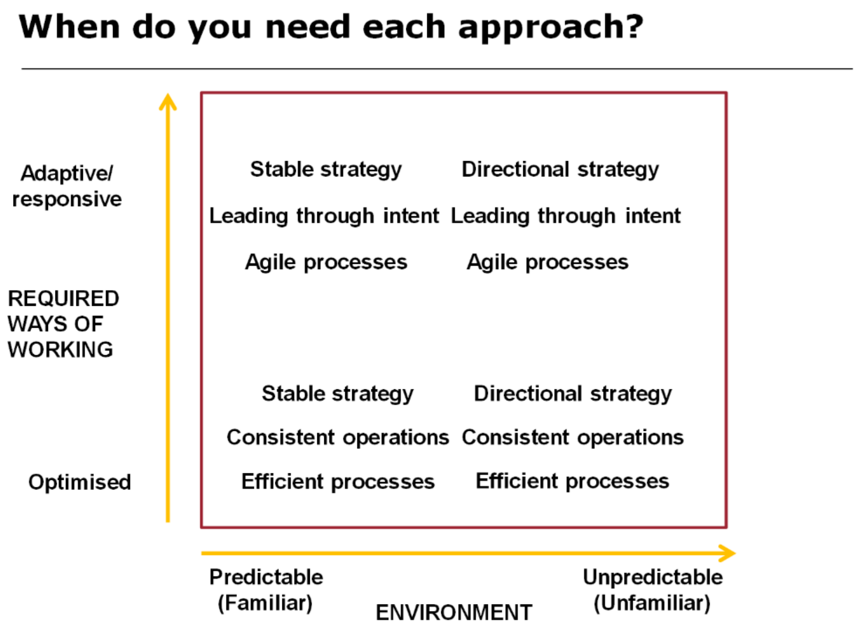
In 2019, he held a workshop with Sydbank's top executives to re-formulate their strategy as a high-level intent based on 10 core beliefs. Each belief consisted of an observation about the environment, followed by a statement of what they intended to do as a result and a contrasting statement about what they were not going to do. For example, the first was: 'Trust in corporations is eroding – therefore we will put ethics before profit and not push products which will cause problems for our customers'. The belief was founded on consumer surveys conducted in the light of a wave of banking scandals. The otherwise empty phrase 'we will put ethics before profit' was giving meaning by the 'and not' statement that they would not push products which were not in their customers' interests.

A second belief was that currently revenue from standard transactions would decline. This was because Denmark was experiencing negative interest rates. Whilst many competitors were reacting to this by entering new product areas, Sydbank declared that it would seek to strengthen existing customer relationships and grow with their needs, and not enter areas in which they had no experience.

The ten beliefs were published in the 2020 annual report. Each of them can be tested as time goes on and they are at different levels. With rising inflation the period of negative interest rates is probably ending. It was a local weather condition. However, the principle of growing with the core customer group of Danish SME's is more enduring, a deep ocean current in their business. The biggest market for most of their customers is north Germany. Last year, as other Danish banks consolidated and closed down branches in Hamburg and Bremen, Sydbank bought them up because it enhances their ability to serve their core customers. Similarly, when a small private bank became available for acquisition, Sydbank acted quickly and beat rivals wanting to buy it because it enabled them to offer personal services to the owners of SME's. Both of these decisions were easy to make because of the high-level framework laid out in their statement of beliefs.

In order to adjust course rapidly in the context of a framework of beliefs, a business needs an agile operating model such as that offered by 'leading through intent'. The high-level framework is made more specific at each level of the hierarchy until concrete actions are specified. As everybody has an area of freedom to make independent decisions, those actions can be changed as the situation changes.

The question then becomes under what circumstances directional strategy, leading through intent and agile processes are appropriate. Stephen has worked with another Member to develop a way of positioning the businesses in their portfolio according to their need for agility at each of the three levels. The result was this matrix:



In the bottom left would be established businesses needing constant small adjustments, and in the top left established ones with a challenged business model. On the bottom right would be businesses in a volatile or disruptive environment that nevertheless needed to maintain the efficiency of established operations. Only in the top right is agility a requirement at all levels. Here one would find many new businesses such as Spotify. They attract a lot of attention, but should not be a model for everyone all of the time.

One of the Members then took us through some examples from the company's portfolio. One business is in the top left. Its underlying principles are very predictable but it needs agile processes and operational agility to respond to rapid, unpredictable changes at the surface, which is this case is literally the weather.

Another is in the bottom left. There has been little change for a long time and advantage is about honing efficiency. However, there are signs that this business may be moving upwards and to the left as consumer behaviour and the role of different distribution channels change.

A third business is fashion retail, and this is in the top right. It does not use the language of agility, but every layer is unpredictable and the business is in fact very responsive both to deep currents such as environmental and social impact, and ephemeral surface changes in fashion. Operationally, there is a lot of experimentation and people have high levels of autonomy.

The meeting concluded with some overall comments from various members:

- This has been very interesting and given me some new lenses to look through. I must think about how to divide up the organization into different layers.

- I used to work at Mars, whose core business is largely in the bottom left of this matrix - if you are trying to sell more Mars bars how agile do you need to be? Pet care was different though, as it was a direct-to-consumer business. How close you are to the customer may be a driver of the need for agility. Looking at the needs of the portfolio makes me wonder how you can find an MD who can manage businesses in different segments.

- We do have cultural resistance in places where more agility is needed. It is helpful to make the needs explicit, but managing opposite requirements is difficult. Stephen suggested that in such circumstances it is usually best to separate the businesses or parts of the business in order to avoid a compromise which will serve nobody. It is difficult, but it can be done. One extreme example is the Mercedes F1 team. Their a race team is clearly bottom left, needing extreme efficiency in pit stops, but the design team, where creativity is the key to success, is top right. The needs of both are fully recognized and both understand that they depend on each other for success, but need to behave very differently. The overall company culture and values provide a way of bringing them together as one team without imposing common behaviour patterns.

Future meetings

The next Members' Meeting will be held from 14.00 – 16.30 on 17th March 2022. The subject will be 'From Reset to Thrive – Growing through Uncertainty' and will be led by Rebecca Homkes. A full list of 2022 dates will be sent shortly.