

Flouting Conventional Wisdom

INSEAD scholars W. Chan Kim and Renée Mauborgne say the key to success isn't about your company or industry. It's about smart strategic moves.

BY DES DEARLOVE & STUART CRAINER

Chief executives in search of strategic inspiration traditionally have had two alternatives. They start with either their industry or their company as the basic building block. The former leads them into the familiar if cold embrace of Michael Porter's Five Forces framework, which posits that different industries can sustain different levels of profitability; the latter nuzzles them seductively towards Gary Hamel and C.K. Prahalad's core competencies of companies.

Over the past two decades, a great deal of intellectual energy has been expended on refining these two worldviews. But according to two leading Europe-based academics, an intellectual irony underlies both. "There's no such thing as a permanently great company or a permanently great industry. All industries rise and fall as do companies," say W. Chan Kim and Renée Mauborgne. "However, there are permanently smart strategic moves."



Kim and Mauborgne are based at INSEAD, the elite business school situated in the beautiful forest of Fontainebleau, just south of Paris. They are methodical people, not prone to hysterical outbursts or wild hypotheses. Their work, characterized by rigorous research and attention to detail, is supported by a substantial database—one that extends all the way back to 1850. As scholars, they are also patient. Some thought leaders of their standing would be on their second or third book. Kim and Mauborgne are currently wrapping up their first. When it does finally see the light of day—probably in 2004—it will be the culmination of more than a decade of work.

In the quiet of Fontainebleau, the Korean and American are preparing their challenge to the strategy hegemony. They want to be sure their theories stand up—that they cannot be dismissed as a passing fad. Stretching their data back 150 years has already taken two years of painstaking research. "We have sleepless nights getting the data right," says Kim, a former University of Michigan Business School professor who studied under Prahalad and alongside Hamel.

Mauborgne joined intellectual forces with Kim in Ann Arbor.



The Model-T, launched in 1908, replaced the horse-drawn carriage and lifted Ford's market share from 9 to 60 percent.

So what does all this data show? Kim and Mauborgne believe that the business world has been overlooking one of the key lessons of wealth creation. It's not the industry a company plays in, per se, that leads to wealth creation, according to their research. And they found no permanently great companies that consistently captured wealth. (This contradicts books such as *In Search of Excellence* and *Built to Last*, which seek to distill the characteristics of great companies.) Instead, Kim and Mauborgne found that an industry's and a company's ups and downs are substantially attributable to something they call strategic moves. "By 'strategic moves,' we mean the actions of players in conceiving,

launching and realizing their business ideas. In each strategic move, there are winners, losers and mere survivors,” says Mauborgne.

A snapshot of the auto industry from 1900 to 1940 is instructive. Ford's Model T, for example, launched in 1908, triggered the industry's growth and profitability, replacing the horse-drawn carriage with the car for American households, note Kim and Mauborgne. That move lifted Ford's market share from 9 to 60 percent.

The Model T, then, was the strategic move that ignited the automotive industry. But in 1924, it was overtaken by another innovation, this time by GM. “Contrary to Ford's functional one-color, one-car, single-model strategy, GM created the new market space of emotional, stylized cars with ‘a car for every purpose and purse,’” explains Kim. “Not only was the auto industry's growth and profitability again catapulted to new heights, but GM's market share jumped from 20 to 50 percent, while Ford's fell from 60 to 20 percent.”

Over the 150-year period, the scholars found a similar pattern in other sectors. In short, the strategic move that matters most to both an industry's and a company's long-run profitable growth is the repeated creation of new market space that embraces the mass market. Kim and Mauborgne call this “value innovation.” Without it, whole industries fade into the sunset and are replaced by those that are more innovative. Without it, companies become irrelevant or are overtaken—as Ford was by GM in the 1920s.

“Value innovation occurs across industries, across countries, across companies,” says Kim. “It is a universal force. A company, therefore, substantially limits its strategic opportunities and profitable growth potential by narrowly confining its analysis to its own industry. Yet, in most strategy literature, industry boundaries are regarded as central—think of SWOT (Strengths, Weaknesses, Opportunities and Threats) analysis or Michael Porter's Five Forces.”

Rather than viewing strategy as enacted in a landscape of dominant companies or industries, Kim and Mauborgne paint a persuasive picture of a commercial world in constant flux, where whole industries rise and then often disappear into oblivion. “Look back to the major industries of 1970, and very few, if any, are now significant,” says Kim. “The big growth industries in the past 30 years have been the computer industry, software, gas-fired electricity plants, cell phones and the coffee bar concept. But in 1970 not one of those industries existed in a meaningful way, and that's just 30 years back. The pattern continues as you dig into the past. The big industries of 1940 aren't those of 1910, and so on. We have a hugely underestimated capacity to create new industries.”

This, then, is their big discovery: The number of industries is ever-increasing—and the pace is accelerating. The implications for chief executives and their advisors are profound. “What we see is that over a 30-year cycle, the focus of commerce—where the money is made—shifts 100 percent,” says Kim. “Some industries die, some persist. But new industries are constantly being created. It is like a galaxy of stars—infinite.”

Transpose that onto the future, and the obvious conclusion is that the biggest industries today are unlikely to be the biggest industries 30 years hence.

The trouble is that the basis of strategic thinking—and the consulting industry it has spawned—lies in coming up with strategies based on what you can see now. Business strategy is historically intertwined with military notions of strategy. Carl von Clausewitz, a Prussian general, and Sun Tzu, the ancient Chinese theorist who wrote *The Art of War*, are still cited as inspirations by the world's managers. This notion of strategy, say Kim and Mauborgne, encourages managers to see it as a series of skirmishes to be conducted on a neatly defined battlefield, where the victor gains ownership of more of the battlefield. The competitive environment is static and limited to that which a CEO can perceive at the moment, but doesn't lend him or her a sense of what the future might look like.

“The war analogy we have used for strategy so far is the wrong one: It is based on an assumption that there’s only so much territory that exists,” says Mauborgne. “So it’s been about dividing up that territory. There’s been a winner and a loser. But our research shows it’s not a zero-sum game. You can create new land. Business history shows us that, contrary to perceived wisdom, the number of market spaces that can be created is infinite.”

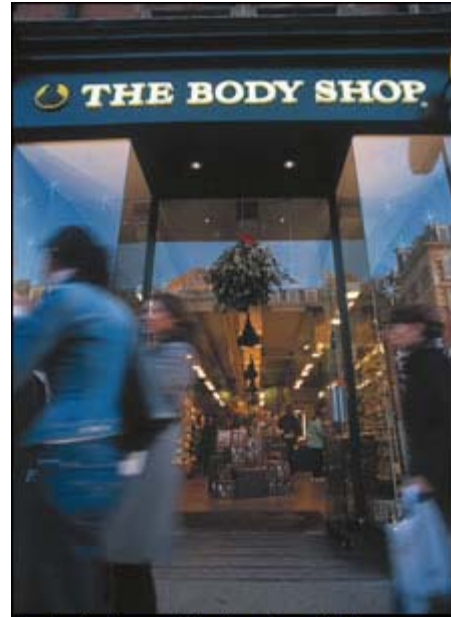
Value innovation, they argue, offers a more reliable route to value creation. This changes the fundamental operating principles of strategy. Consider The Body Shop, which in the 1980s was highly successful. Rather than compete head-on with large cosmetics companies, it invented a whole new market for natural beauty products. More recently, The Body Shop has struggled. But, say Kim and Mauborgne, that does not diminish the brilliance of its original strategic move.

The problem was that The Body Shop did not realize what made its strategic move so brilliant. The company’s genius lay in creating a new market space in what was seen as a commodity industry. Once it had carved out its own market, the company focused on mining that new market space. That was all right when few players imitated it. But as more and more competitors moved into its market space, the company became involved in a bruising battle for market share. This was the wrong strategy.

“Once you have your own market space and imitators follow, you go into classical competitive strategy mode, where you focus on milking it, getting your best market share, blocking other imitations and dramatically ramping up and refining your offering,” explains Mauborgne. “But, as other companies’ strategies converge on your market, history shows you need to create new market space again and break away.”

In their model, strategic success depends on understanding the context and using the right moves at the right time. Strategy becomes a game of tag or leapfrog, rather than a brawl. Crucially, Kim and Mauborgne reject the idea that a company’s strategic options are determined by traditional industry life cycles.

The strategic lesson is clear. Says Mauborgne: “When you take an industry-deterministic view of your company, you become a victim of that industry. The moment you sit back and ask, ‘How can we create a new industry?’ then you start to break that cycle. All industries are created not by big resources but by big ideas.”



Instead of competing head on with large cosmetics companies, The Body Shop invented a whole new market for natural beauty products.