Theories of Strategy

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> Practical men, who believe themselves to be quite exempt from any intellectual influences, are usually the slaves of some defunct economist. Madmen in authority, who hear voices in the air, are distilling their frenzy from some academic scribbler of a few years back.
>
> (Keynes 1936: 383)

Introduction

[. . .]

Theories are important. They contain our basic assumptions about key relationships in business life. Theories tell us what to look out for, what our first steps should be, and what to expect as a result of our actions. Saving us from going back to first principles at each stage, they are actually short-cuts to action. Often these theories are not very explicit or very formal. Whether building from experience or from books, we all tend to have our own private assumptions about how things work, how to get things done. Providing the basic grounding for our behaviour, Argyris (1977) calls these assumptions 'theories of action'.

The danger of these theories is forgetting we have them. As Keynes (1936) implies, those who boast of their commonsense approach to management are very probably just following the ill-informed, half-forgotten, pseudo-scientific nostrums peddled to them in their early careers. Drawing upon his work with American senior managers, Argyris (1977) warns that nothing is more dangerous than to leave underlying assumptions hidden. Until we surface our implicit 'theories of action', we cannot test their accuracy and amend them to the conditions of the day. Those who do not actively confront their underlying assumptions are condemned to be 'prisoners of their own theories' (Argyris 1977: 119).

The point of this chapter, then, is to make explicit the assumptions that underlie . . . theories of strategy. Each theory holds very different views about our

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human capacity to think rationally and act effectively. They diverge widely in their implications for strategic management. By directly confronting these differences, you should be better able to test your own 'theories of action' and to decide finally which basic theory most closely matches your own experience and needs.

[. . .]

The Classical approach to strategy

For Classicists, profitability is the supreme goal of business, and rational planning the means to achieve it. Dominant in the mainstream textbooks, the Classical approach draws wide disciplinary and metaphorical support. Its notions of strategy formulation are informed by the economics of eighteenth-century Scotland, while its assumptions about strategic implementation appeal back to the militaristic ideals of Ancient Greece.

For all this, the Classical approach to business strategy is still novel. The beginnings of a coherent discipline only emerged in the 1960s, with the writings of business historian Alfred Chandler (1962), theorist Igor Ansoff (1965) and the businessman Alfred Sloan (1963). These three men early established the key features of the Classical approach: the attachment to rational analysis, the separation of conception from execution, and the commitment to profit maximization.

Alfred Sloan, former President of General Motors, defined the fundamental strategic problem as positioning the firm in those markets in which maximum profits could be earned. In his great biography *My Years with General Motors*, Sloan laid down the Classical profit-orientated goal of strategy:

> the strategic aim of a business is to earn a return on capital, and if in any particular case the return in the long run is not satisfactory, the deficiency should be corrected or the activity abandoned. (1963: 49)

Sloan's (1963) biography chronicles in detail the development of the measures and methods by which, with as much cold objectivity as he could summon, he pursued this strategic aim over four decades at General Motors. Among the innovations he helped to pioneer were return on investment criteria, the decentralized divisional form and the separation of 'policy' from operations.

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Sloan's example was highly influential. The prolific author and management consultant Peter Drucker worked for General Motors between 1943 and 1945, when the company employed half a million people. He subsequently publicized Sloan's management structures and style in two books, *The Concept of the Corporation* (1946; republished in 1973) and *Big Business* (1947). Igor Ansoff too was much impressed by Sloan, citing his statement on the strategic aim of business at the head of the first chapter of his *Corporate Strategy*, the first ever strategy textbook (a generation later, Grant 1998: 16) reproduced the same statement in his first chapter). Sloan was also closely connected with the first academic researcher of

strategy, historian Alfred D. Chandler. Chandler (1962) took General Motors as one of his four central case studies in his historical account of the evolution of strategy and structure in American business; his research was financed by the Sloan Research Fund; and he was himself – full name Alfred Du Pont Chandler – connected to the family which owned a quarter of Sloan's General Motors (the Du Pont company supplied the second of his four cases).

It may not be surprising, then, that Chandler shares Sloan's faith in the superiority of the top-down, planned and rational approach to strategy-making. Chandler's (1962) own influential definition of strategy has all the characteristics of Classical strategy thought: the emphasis on the long run, the explicit and deliberate conception of goals, and the logical cascading of actions and resources from original objectives. According to Chandler, strategy is

> the determination of the basic, long-term goals and objectives of an enterprise, and the adoption of courses of action and the allocation of resources necessary for those goals. (1962: 13)

The central problem of the companies Chandler studied was how to build the organizational structures that would allow top management to focus on their strategic responsibilities. The basic reason for the success of the multidivisional structure that all four of his companies adopted in the first half of this century 'was simply that it clearly removed the executives responsible for the destiny of the entire enterprise from the more routine operational activities and so gave them the time, information, and even psychological commitment for long-term planning and appraisal' (Chandler 1962: 309). Thus was strategy formulation and control confirmed as the prime task of the top manager, strategy implementation as the responsibility of the operational managers in the divisions.

Sloan, Chandler and Ansoff did not, of course, dream up the concept of strategy from scratch. Ansoff (1965: 105) links his notion of strategy directly to both military practice and academic economics. Since then, economistic ideas about rational optimization, and militaristic expectations of hierarchical command, have continued to resonate in Classical thinking about strategy formulation and implementation.

Indeed, Bracker (1980) traces the concept of strategy to the Greek word *strategos*, 'a general', which in turn comes from roots meaning 'army' and 'lead'. Apparently, the link between military and business practice came early, when Socrates consoled Nichomachides, a Greek soldier who had lost an election to the position of general to a mere businessman. According to Bracker (1980: 219), Socrates explained to Nichomachides that the duties of a general and a businessman were equivalent: both involve planning the use of one's resources in order to meet objectives.

It is not clear that Nichomachides was consoled by this view, but anyway this military concept of business strategy was lost with the fall of the Greek city-states. There is no direct line of descent to modern business: Hoskin (1990) emphasizes the disjuncture between Greek military theory, tactical and partial in fact, and modern business strategy, long term and comprehensive in aspiration. None the less, as Hoskin (1990) finds, many of the earliest managerial systematizers of American business shared military origins, in particular training at the officer cadet school of West Point in the first half of the nineteenth century. Even today, when business strategy can claim a substantial and independent body of experience, military imagery continues to influence contemporary strategy analysis, as can be seen in the popularity of such books as James's (1985) *Business Wargames*. Certainly, the military metaphor reinforces several typical features of Classical approaches to strategy.

At the centre of the military tradition of strategy is the heroic yet slightly isolated figure of the general himself. Presiding at the top of a rigid hierarchy, it is the general who ultimately makes the decisions. From Alexander to Rommel, individual genius is critical to victory. Plans are conceived in the general's tent, overlooking the battlefield but sufficiently detached for safety. These preconceived plans are executed according to commands transmitted through obedient hierarchies to the officers and their men at the front: it is not for them to reason why, but simply to execute their orders. The men are sent to do battle, and the objective is simple: victory. Conflict, not co-operation, is the norm. The epitome of this coolly detached, sequential approach to strategy was General Colin Powell, chairman of the Joint Chiefs of Staff during the Gulf crisis. Asked how he planned to retake Iraqi-occupied Kuwait, he said: 'Our strategy for dealing with this [Iraqi] army is simple: first we are going to cut it off, then we're going to kill it' (*Sunday Times* 13 January 1991).

For the Classical theorists, this military model is complemented by an intellectual inheritance from economics. Indeed, the first academic application of the notion of strategy to business was made by two mathematical economists, von Neumann and Morgenstern (1944), in their *Theory of Games and Economic Behavior*. Since then, as Rumelt et al.'s (1991) recent view makes clear, economics has supplied the strategy field with many basic techniques and concepts – most notably Michael Porter's (1980) industry structure analysis and Oliver Williamson's (1985) concept of transaction costs in business organization. However, the most pervasive contribution of economics to strategy is the philosophical core of assumptions summed up in the ideal type of 'rational economic man' (Hollis and Nell 1975).

The ideal of rational economic man projects strategy as the product of a single entrepreneurial individual, acting with perfect rationality to maximize 'his' economic advantage. Von Neumann and Morgenstern (1944) placed this singular figure right at the heart of their conception of strategy as an elaborate 'game' of move and counter-move, bluff and counter-bluff, between competing yet interdependent businesses. Rational economic man was a necessary device. Only this reduction of the firm to a unique decision-maker would allow them to ignore internal organizational complexities; only this endowment of super-rationality would permit the sequence of mathematical calculations necessary to follow through the logics of the game.

Smuggled into Classical strategy thinking with the baggage of economics, the individualistic ideal of rational economic man goes back at least to the hard-headed economics of eighteenth-century Scotland. Hollander's (1987: 312) account of classical economics reveals how the fundamental principles of orthodox strategy thought were already present in the writings of Adam Smith. The profit-maximizing assumption is merely the economic expression of Smith's sad belief that self-interest was 'inherent in the very nature of our being'. Consequently, Smith asserted in his *Wealth of Nations* that 'each individual is continually exerting himself to find out the most advantageous employment of whatever capital he can command' – or, translated into the terms of modern accounting, each individual firm is continually exerting itself to maximize return on investment. According to Smith, our pursuit of this self-interest is governed by what he called 'prudence'. This notion of 'prudence' embodies the dual principles of 'reason' (the ability to foresee consequences and to discern advantage) and 'self-command' (the readiness to abstain from short-term opportunism in order to benefit more substantially in the long run) (Hollander 1987: 315–16). It is exactly these principles of eighteenth-century 'prudence' that are at the heart of modern long-term strategic planning.

[. . .]

The more pragmatic and self-conscious Classical thinkers hesitate over some of the economists' abstractions and the militarists' metaphors (see Grant 1998: ch. 1). Yet echoes of both continue to linger in the orthodox textbooks. Henry Mintzberg's (1990) recent critique of strategic management orthodoxy exposes this subtext with painful clarity.

By careful analysis of key texts, especially those associated with the Harvard Business School, Mintzberg (1990) identifies what he terms the 'basic premises' of Classical thought. The first premise, that strategy formation should be a controlled conscious process of thought, derives directly from the notion of rational economic man. The premise that responsibility for control and consciousness must rest with the chief executive officer – 'THE strategist', as Mintzberg (1990: 176) puts it – reflects both the individualism of economics and the military notion of the solitary general at the tip of the pyramid of command. Military notions of command also inform the premise that strategies emerge from the decision-making process fully formulated, explicit and articulated: strategies are in a sense orders for others to carry out. Thence too comes Mintzberg's (1990) last premise, that implementation is a distinct phase in the strategy process, only coming after the earlier phase of explicit and conscious formulation. It is this which underlies the image of the strategist as general in his tent, despatching orders to the front. The actual carrying-out of orders is relatively unproblematic, assured by military discipline and obedience.

In sum, the Classical approach to strategy places great confidence in the readiness and capacity of managers to adopt profit-maximizing strategies through rational long-term planning. Accordingly, the Classic texts from Ansoff (1965) to Grant (1998) furnish us with an abundant technology of matrices, formulae and flowcharts. The 'seat-of-the-pants' managerial style of William Durant at General Motors is banished to the past. Flattered by the image of Olympian detachment, lured by the promise of technique-driven success, managers are seduced into the Classical fold.

Evolutionary perspectives on strategy

Evolutionary approaches to strategy are less confident about top management's ability to plan and act rationally. Rather than relying on managers, they expect markets to secure profit maximization. Stressing competitive processes of natural selection, Evolutionary theorists do not necessarily (prescribe rational planning methods; rather, they argue that whatever methods managers adopt, it will only be the best performers that survive. Managers need not be rational optimizers because 'evolution is nature's cost–benefit analysis' (Einhorn and Hogarth 1988: 114).

Evolutionary theorists often make an explicit parallel between economic competition and the natural law of the jungle. Bruce Henderson, founder of the Boston Consulting Group, complains:

> Classical economic theories of competition are so simplistic and sterile that they have been less contributions to understanding than obstacles. These theories postulate rational, self-interested behavior by individuals who interact through market exchanges in a fixed and static legal system of property and contracts. (1989: 143)

According to Henderson, these postulates are too abstract and unrealistic. Competition is not a matter of detached calculation but a constant struggle for survival in an overpopulated, dense and steamy jungle. He concludes (1989: 143): 'Human beings may be at the top of the ecological chain, but we are still members of the ecological community. That is why Darwin is probably a better guide to business competition than economists are.'

In fact, many economists had reached a similar conclusion long before Bruce Henderson. R.C. Hall and Hitch's (1939) simple field enquiries had discovered that business practice was far from that prescribed by the ideal of rational economic man: not only did managers fail to set output at the theoretically profit-maximizing level where marginal costs exactly equal marginal revenues, but they had no idea what their marginal cost and revenue curves were anyway. Economists adjusted to this business stupidity by letting the markets do the thinking.

Thus Alchian (1950) appealed directly to the biological principle of natural selection to propose an evolutionary theory of the firm that downgraded managerial strategy and emphasized environmental fit. The most appropriate strategies within a given market emerge as competitive processes allow the relatively better performers to survive and flourish, while the weaker performers are irresistibly squeezed out of the ecological niche. The evolution of industries typically follows

the pattern of the French and United Kingdom automobile industries illustrated in Figure 2.1. As a new niche opens up, it is initially flooded by new entrants, but then overpopulation drives a process of fierce competition that allows only the most 'fit' to survive (Hannan 1997). As Milton Friedman (1953) famously argued, it hardly matters if managers do not rationally profit-maximize so long as competitive markets ensure that only those who do somehow achieve the profit-maximizing position will survive over the long run. Markets, not managers, choose the prevailing strategies within a particular environment.

The Evolutionary economists initially emphasized competition in product markets as the means of winnowing out inefficient competitors. Unfortunately, as critics such as Penrose (1952) were quick to remark, many large contemporary firms dominate the markets that are supposed to discipline them, with sufficient oligopolistic power to be well buffered against competitive pressures. For these companies, strategy is about selecting markets, rather than being selected by markets. More recent elaborations of Evolutionary theory (e.g. Pelikan 1989) have therefore emphasized other markets, especially managerial labour markets, the market for capital and the market for corporate control, as selecting the best performers for survival. In this broader view, incompetent managers are eliminated as they fail to get promoted or hired, as they find themselves unable to get

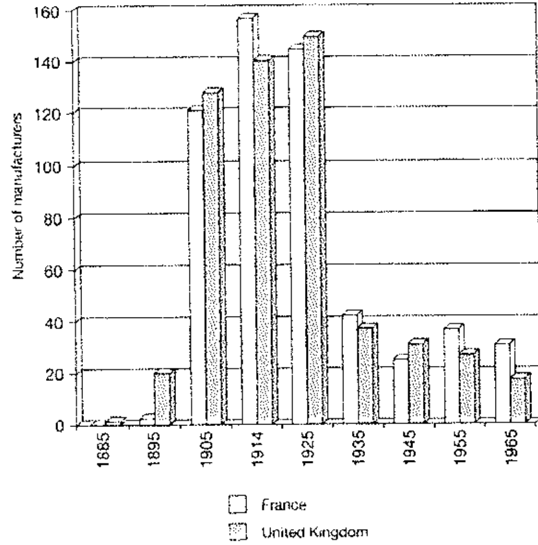

Figure 2.1 ***Populations of automobile manufacturers in France and the United Kingdom, 1885–1965*** **(Hannan 1997)**

bank loans, or as falling share prices provoke either shareholder revolt or hostile takeover. Thus, by one market or another, the pressure for profit maximization is maintained.

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Evolutionary theory has some intriguing implications for managerial strategy. Henderson (1989) draws directly from the biological 'principle of competitive exclusion' established by the Russian biologist Gause in 1934. Gause had found that when he put two small organisms of the same genus but different species in a jar with a limited supply of food, they would survive; however, if the two organisms were from the same species, with exactly the same amount of food, they would die. Coexistence is impossible if organisms make their living in an identical way. Henderson's (1989) conclusion is that business survival in a competitive environment depends on strategies of differentiation.

The challenge for strategy is that many Evolutionary theorists doubt the capacity of organizations to achieve differentiation and adaptation in a deliberate and sustainable way. As the dinosaurs found, complex biological organisms usually adapt more slowly than their environments. Human organizations are often the same. Drawing on Processual insights into the difficulties of managing change, Evolutionary theorists emphasize the limited capacity of organizations to anticipate and respond purposively to shifts in the environment. Aldrich (1979) argues that environmental fit is more likely to be the result of chance and good fortune, even error, than the outcome of deliberate strategic choice. Alchian (1950) too warns against overestimating the power of strategy. For him, firms are tossed about by unpredictable and uncontrollable market forces. Like plants which flourish because the wind blew their seeds onto the sunny side of a wall, business success is generally the result of happenstance – just being at the right place at the right time.

> Among all competitors, those whose particular conditions happened to be most appropriate for testing and adoption will be 'selected' as survivors . . . The survivors may appear to be those having *adapted* themselves to the environment, whereas the truth may well be that the environment has *adopted* them. (Alchian 1950: 213–14; emphasis in the original)

Indeed, investing in long-term strategies can be counter-productive. Organizations maximize their chances of survival in the short term by achieving perfect fit against their current environment. In a competitive environment, flexibility is evolutionarily inefficient. Strategy is too expensive; the investor in long-term strategies of innovation, diversification and change can always be undercut by the short-term, inflexible, low-cost producer. Competitive markets thus introduce a bias to strategic conservatism. According to Hannan and Freeman (1988: 25), 'Organizational selection processes favour organizations with relatively inert structures, organizations that cannot change strategy and structure as their environments change.'

Evolutionists not only insist that markets are typically too competitive for expensive strategizing and too unpredictable to outguess. They also hold that

markets are too efficient to permit the creation of any sustainable advantage. In a competitive environment, elaborate strategies can only deliver a temporary advantage: competitors will be quick to imitate and erode any early benefits. Classical techniques in particular are unlikely to deliver permanent superiority. The market for such knowledge is too perfect. As McCloskey observes:

> formal methods will not earn abnormally high profits for long. The formality makes them easy to copy. Going to business school is not a way to acquire immense wealth, because it is too easy get in. (1990: 128)

The market ensures that everybody else has access to Michael Porter's (1985) writings on competitive advantage too.

For Evolutionists, then, strategy can be a dangerous delusion. Except for the minority of firms with significant market power, the prosaic conclusion of Oliver Williamson (1991: 87) is simply that 'economy is the best strategy'. The only real comparative advantage is relative efficiency. Managers must concentrate on their costs, especially the 'transaction costs' of organizing and co-ordinating. Williamson writes:

> a strategizing effort will rarely prevail if a program is burdened by significant cost excesses in production, distribution or organization. All the clever ploys and positioning, aye, all the king's horses and all the king's men, will rarely save a project that is seriously flawed in first-order economizing respects. (1991: 75)

Williamson's advice, then, is not to get distracted from the basics.

If deliberate strategizing is ineffective, then what matters is an abundance of diverse new initiatives from which the environment can select the best. Hannan and Freeman's (1988) 'population ecology' perspective suggests that overall efficiency can best be secured by ensuring a steady stream of new entrants into any organizational population, from which the relatively ill-adapted are ruthlessly selected out. Rates of new firm formation and failure, therefore, are equal and complementary indicators of economic health and dynamism. Thus the helter-skelter rise in the number of business failures in the United States – multiplying eightfold between 1980 and 1997 (Figure 2.2) – merely reflects the more effective natural selection processes brought about by competitive markets. The rise in new business start-ups over the same period has kept the American economy's 'gene pool' refreshed and replenished. It is little use trying to prop up and reform existing underperformers. Firms that are poorly adapted to current conditions should simply make way to let new businesses try their chances at achieving environmental fit. Market convert Tom Peters (1992: 618) actually applauds high business failure rates.

The Evolutionary perspective clearly has rather gloomy implications for strategy. Certainly, differentiation is a sound principle within a competitive environment, but it is doubtful whether this can be achieved deliberately or permanently. The construction of grand long-term strategies may be so much vain distraction; managers would do much better to get down to the modest business of making sure that what they do now is done as efficiently as possible. If managers must attempt to anticipate change, then they would be wise not to try to outguess the market by investing heavily in a single major plan. The most effective approach may be to experiment with as many different small initiatives as possible, to wait and see which flourish and which fail, and then to build on the successes whilst ruthlessly eliminating the failures. It was this Darwinian approach that guided Sony in its strategy during the 1980s, when it launched more than 160 different Walkman versions in the American market, never retaining more than about twenty versions on the market at the same time (Sanchez and Sudharshan 19 2). The Evolutionary advice, then, is that, in searching for the best strategy, it is best to let the environment do the selecting, not the managers.

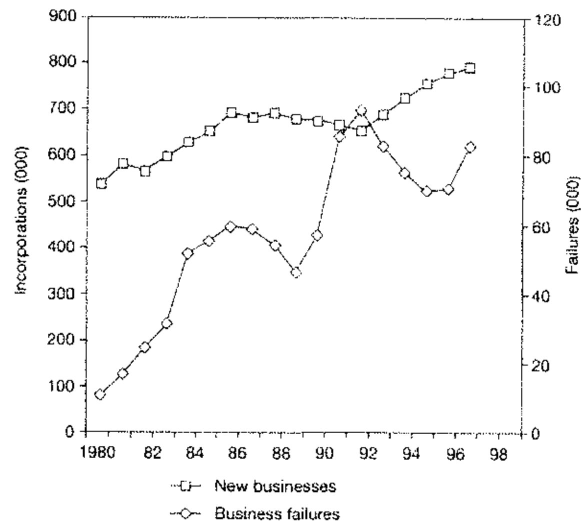

Figure 2.2 ***Darwinian America: business starts and failures in the United States*** **(Economic Report to the President; www.dnb.com: note expanded coverage 1984 onwards)**

Processual approaches to strategy

Processual approaches to strategy generally share the Evolutionary scepticism about rational strategy-making, but are less confident about markets ensuring profit-maximizing outcomes. For Processualists, both organizations and markets are often sticky, messy phenomena, from which strategies emerge with much confusion and

in small steps. Indeed, they argue that it is to the very imperfections of organizational and market processes that managers owe their strategies and competitive advantages. The best Processual advice is not to strive after the unattainable ideal of rational fluid action, but to accept and work with the world as it is.

The foundations for the Processual approach were laid by the innovative work of the American Carnegie School – most prominently, Richard Cyert, James March and Nobel Prize-winner Herbert Simon. Together, they advanced a model of strategy-making that is still being restated with radical claims to novelty more than four decades later. Rejecting the specious unit of rational economic man on the one hand and the perfections of competitive markets on the other, they were led to take the internal complexity of organizations seriously. Here they uncovered two of the themes that have now become fundamentals of Processual thought: the cognitive limits on rational action, since extended by Henry Mintzberg (1987, 1994) in particular; and the micro-politics of organizations, developed by Andrew Pettigrew (1973, 1985).

Aiming for a more psychologically realistic theory of human behaviour, the Carnegie School emphasized the limits of human cognition. Rational economic man is a fiction: in practice, people are only 'boundedly rational' (Cyert and March 1963). By this they mean that we are unable to consider more than a handful of factors at a time; we are reluctant to embark on unlimited searches for relevant information; we are biased in our interpretation of data; and finally we are prone to accept the first satisfactory option that presents itself, rather than insisting on the best (March and Simon 1958; Cyert and March 1963). Even momentary consideration of our everyday behaviour will probably confirm the basic plausibility of these assumptions. The result is that the environmental scanning, data analyses and calculated comparisons of strategic options advocated by Classical theorists of strategy tend always to be flawed and incomplete. This is just human nature.

The micro-political view of organizations was established by the Carnegie School's recognition of the individual interests represented in any enterprise. Firms are not united in optimizing a single utility, such as profit. Rather, they are coalitions of individuals each of whom brings their own personal objectives and cognitive biases to the organization. Organizational members bargain between each other to arrive at a set of joint goals more or less acceptable to them all. The bargaining process involves both many compromises and what Cyert and March (1963: 31) describe as 'policy sidepayments' in return for agreement. For example, the Production Director may accept a reduced investment programme in order to secure at least some new machines this year, while supporting the Technical Director's bid for a new research and development initiative in electronics just to keep her on-side. Strategy is thus the product of political compromise, not profit-maximizing calculation.

The combination of political bargaining and bounded rationality strongly favours strategic conservatism. The need for change will only be imperfectly recognized, and anyway change is suspected because it is likely to set off a period of internal civil war until a new 'dominant coalition' is established (Cyert and March 1963). Strategic behaviour therefore tends to become entrenched in the 'routines' and 'standard operating procedures' imposed by political exigency and cognitive limits. Rather than perfectly rational strategies, organizations opt simply for 'adaptive rationality', the gradual adjusting of routines as awkward messages from a dynamic environment eventually force themselves on managers' attention.

Cyert and March (1953) argued that firms can get away with these slow adjustments because, contrary to the views of the more stringent Evolutionists, markets are in fact typically quite tolerant of underperformance. Firms often enjoy sufficient market power to be able to earn reasonable profits without maximum effort. Shareholders are unable to detect this underperformance because, like everybody else, they are not rational or informed enough to know. Thus firms can build sufficient 'organizational slack' to buffer themselves against the need for strategic change, delivering just enough profits to keep everybody reasonably happy. In this sense, firms 'satisfice' rather than profit-maximize (Cyert and March 1963: 41).

This modest view of organizations and the people who run them has significant implications for strategy. The Processual perspective radically downgrades the importance of rational analysis; it limits the search for strategic flexibility; and it reduces expectations of success. In practice, strategy-makers do not strive ceaselessly for the optimal solution, but satisfy themselves with following the established routines and heuristics of the organization. Indeed, as Nelson and Winter (1982: 133) observe, 'according to the concept of strategy that has been developed by a number of investigators associated with the Harvard Business School, the fundamental heuristic imperative for top management is: Develop a strategy'.

But strategy statements themselves can become routinized heuristics, working to constrain the field of opportunity and guiding decisions into established paths. Say Nelson and Winter, in strong Processual mood:

> it is quite inappropriate to conceive of firm behavior in terms of deliberate choice from a broad menu of alternatives that some external observer considers to be 'available' opportunities for the organization. The menu is not broad, but narrow and idiosyncratic; it is built into the firm's routines, and most of the 'choosing' is also accomplished automatically by these routines. (1982: 134)

Strategies are not chosen; they are programmed.

Strategies, then, are a way in which managers try to simplify and order a world which is too complex and chaotic for them to comprehend. The regular procedures and precise quantifications of strategic planning are comforting rituals, managerial security blankets in a hostile world. Thus Weick (1990) tells the story of a Hungarian detachment that got lost in the Alps during military manoeuvres. As it snowed for two days, the soldiers despaired and laid themselves down to die in the frozen wilderness. Then suddenly one of the soldiers found a map in his pocket, the detachment took heart, and they marched confidently out of the mountains. Safe back at camp, they discovered the map was of the Pyrenees. For Weick (1990),

strategic plans are often like this map: it does not matter much if they are wrong, so long as they give managers the confidence and sense of purpose to act. If the firm sits waiting for the right map, it will freeze; if it gets up and moves, it will somehow or other find direction, acquire experience and make its own opportunities (Box 2.1).

> **Box 2.1**
>
> **Surfing the edge of chaos**
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> The notion of 'emergence' in strategy finds increasing support in 'chaos theory', the new science of complex adaptive systems. This new science is concerned with how order tends naturally to spring from chaos. It doesn't take precise planning from the top, only a few simple rules guiding action from the bottom.
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> Brown and Eisenhardt (1999) give the example of 'boids' – a computer simulation of autonomous, bird-like agents. Something remarkable happens when these mindlessly moving agents are given just three simple rules: try to maintain a minimum distance from other objects, including other boids; try to match the velocity of nearby boids; and try to move to the centre of the mass of nearby boids. Regardless of their starting positions on the screen, and of the number and positioning of obstacles, the boids always end up doing the same thing: forming a flock. There's no need for leaders: order emerges naturally from myriads of small adaptive adjustments.
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> The point about being on the 'edge of chaos' is to have enough structure to allow for patterns to emerge, but not so much as to cause inflexibility and cost. The American company 3M allows scientists to do whatever they like with 15 per cent of their time, but within a framework that insists on taking 30 per cent of sales from products less than four years old while imposing tough targets for profit and growth. Innovative ideas – such as the Post-it or Thinsulate – bubble up from below but fall into place within a coherent strategic frame. Surfing on the edge of chaos means riding the wave – never falling behind and never falling in.
>
> *Sources*: Brown and Eisenhardt 1999; Pascale 1999

In this way, the Classic sequence of formulation first, implementation second, gets reversed: strategy is discovered in action (March 1976). Alfred Sloan's (1963) distinction between 'policy creation' and 'policy execution' begins to blur. Doubting top managers' capacity to prescribe effective strategies in the splendid isolation of their executive suites, Mintzberg (1987) proposes the metaphor of strategy as 'craft'. The craftswoman is intimately involved with her materials: she shapes her clay by personal touch, imperfections inspire her to artistic improvisation, hands and mind work together in a process of constant adaptation. So should it be with strategy. In a world too complex and full of surprises to predict, the strategist needs to retain the closeness, the awareness and the adaptability of

the craftsperson, rather than indulging in the hubris of grand long-range planning. For Mintzberg, crafting strategy is a continuous and adaptive process, with formation and implementation inextricably entangled.

This view of strategy is an unglamorous one: hands get dirty, steps are small and there are few bold lunges into the unknown long term. But this slow progress is not to be despised. As Lindblom (1959) claimed, there is 'a science of muddling through', involving cautious comparison of successive options and careful maintenance of consensus. The gradual adaptive approach to strategy has its own rationality, which Quinn (1980: 89) terms 'logical incrementalism'. The superior rationality of logical incrementalism lies in its acceptance of our own bounded rationality: 'Smart strategists appreciate that they cannot always be smart enough to think through everything in advance' (Mintzberg 1987: 69). Honest about his or her limits, the logical incrementalist is committed to a process of experimentation and learning.

The incrementalist approach is not necessarily a tactical one. It may be informed by an underlying logic, or 'strategic intent', that is both sufficiently clear to provide a sense of direction and sufficiently broad to allow flexibility and opportunism along the way, as for instance Komatsu's ambition simply to 'encircle Caterpillar' (Hamel and Prahalad 1989). More radically, Mintzberg and Waters (1985) suggest, the underlying strategic logic may be perceived only after the event. Strategies are often 'emergent', their coherence accruing through action and perceived in retrospect. Thus Intel's famous switch from the Dynamic Random Access Memories (DRAMs) market to its new role as a dominant player in microprocessors was achieved during the 1980s through an accumulating series of incremental investment decisions that had consistently valued the prospects of the new business more highly than the old. Yet all the while the company's explicit strategy and self-definition was still to be a 'memory company', its original business. As late as 1985, one-third of the research and development budget was still devoted to the 'strategically important' memory business, even when the company had been reduced to a negligible 2 to 3 per cent market share. As Chief Executive Officer Andy Grove observed: 'Don't ask managers "What is your strategy?" Look at what they do!' (Burgelman 1996: 423).

This incremental approach to strategy is reinforced by Processualists who emphasize the stickiness of external markets. For the 'resource-based' strategy theorists (e.g. Grant 1998), market imperfections inhibit the opportunity-maximizing strategies proposed by Classicists. The resources with which firms compete are not all to be bought and sold in markets according to the shifting matrix of strategic opportunities and threats (Collis and Montgomery 1995). Resource-based theories of the firm stress how a firm's resources include tacit skills, patterns of co-operation, and intangible assets that take time and learning to evolve. These resources cannot be traded, changed or imitated with ease (Box 2.2). The origin of a firm's competitive advantage, therefore, lies in what is unique and embedded in its resources – these constitute its core, distinctive competences (Grant 1998).

Box 2.2

The knowledge resource

In today's knowledge-based economy, superior knowledge is likely to be the most valuable resource of all. Knowledge is valuable precisely because it is hard to manage and hard to trade. Most useful knowledge is tacit, not easily captured in managerial databases or imitated by competitors. Knowledge resides inside the heads of lower ranking staff, not in the files of top management. Knowledge is dynamic in unpredictable ways – experience and events are always adding to it, regardless of formal efforts at research and development. Knowledge is hard to trade, because the acquirer cannot know its value until it is actually used. Knowledge is often highly immobile, because embedded in the routines, culture and teams of a particular organization. For all these reasons, the value of knowledge is unlikely to diffuse away through normal processes of market competition and exchange.

Equally, all these knowledge characteristics impose constraints on the strategy process. Especially in knowledge-intensive firms, such as professional services or new technology enterprises, strategy is as likely to emerge bottom-up as top-down. After all, it is at the bottom where the knowledge lies and is continuously recreated. Top managers ignore this source of value in their strategy process at their peril.

Sources: Conner and Prahalad 1996; Tsoukas 1996; Zack 1999

In other words, the sources of sustainable superior performance lie internally, in the capacity to exploit and renew distinctive resources, rather than externally, in simply positioning the firm in the right markets. Strategy involves building on core competences, not chasing each and every opportunity. Hamel (1991: 83) accuses: 'the traditional "competitive strategy" paradigm (e.g. Porter 1980), with its focus on product-market positioning, focuses on only the last few hundred yards of what may be a skill-building marathon'. However attractive market opportunities might be, entry strategies will fail in the implementation if the firm lacks the requisite skills and resources internally or underestimates the difficulty of acquiring them externally. What matters in strategy, therefore, is the long-term construction and consolidation of distinctive internal competences. In this view, strategy becomes a patient inwardly aware process, rather than the fluid externally oriented pursuit of opportunity emphasized by Classical industry structure analyses.

Thus the Processualist focus on the imperfections of organizational and market processes yields at least four conceptions of strategy radically different from the Classical perspective: strategy may be a decision-making heuristic, a device to simplify reality into something managers can actually cope with; plans may just be managerial security blankets, providing reassurance as much as guidance; strategy may not precede action but may only emerge retrospectively, once action has taken place; strategy is not just about choosing markets and then policing performance, but about carefully cultivating internal competences. Many of the confident precepts of the Classicists are put in jeopardy: suddenly, it seems that goals are slippery and vague, long-term policy statements vain delusions, and the separation of formulation from implementation a self-serving top management myth.

For the pure Processualists of the Carnegie School, all this means that strategy is inescapably about satisficing, settling for less than the optimal. But more managerial Processualists turn the messy reality of organizations and markets to advantage. In practice, the technical sophistication of the Classicists amounts to naive idealism. It is above all by recognizing and accommodating real-world imperfections that managers can be most effective. Giving due attention to implementation, exploiting imperfect markets to build distinctive competences, cultivating flexibility for incremental adaptation – these are really the means to maximum performance.

Systemic perspectives on strategy

Against the sometimes nihilistic propositions of Evolutionary and Processual theorists, Systemic theorists do retain faith in the capacity of organizations to plan forward and to act effectively within their environments. Where they differ from the Classicists, however, is in their refusal to accept the forms and ends of Classical rationality as anything more than historically and culturally specific phenomena. Systemic theorists insist that the rationales underlying strategy are peculiar to particular sociological contexts.

A central tenet of Systemic theory is that decision-makers are not simply detached calculating individuals interacting in purely economic transactions, but people rooted deeply in densely interwoven social systems. Granovetter's (1985) notion of social 'embeddedness' captures the sense that economic activity cannot be placed in a separate rarified sphere of impersonal financial calculation. In reality, people's economic behaviour embedded in a network of social relations that may involve their families, state, their professional and educational backgrounds, even their religion and ethnicity (Swedberg et al. 1987; Whittington 1992). These networks influence both the means and ends of action, defining what is appropriate and reasonable behaviour for their members. Behaviour that may look irrational or inefficient to the Classical theorist may be perfectly rational and efficient according to the local criteria and *modus operandi* of the particular social context.

Systemic theorists propose, therefore, that firms differ according to the social and economic systems in which they are embedded. They are not all perfect profit-maximizers, as they choose to be in Classical theory and they are obliged to be in Evolutionary theory. But nor are they just the particularistic organizations of the Processual perspective, whose idiosyncrasies are the product of internal limits and compromises. In the Systemic view, the norms that guide strategy derive not so much from the cognitive bounds of the human psyche as from the cultural rules of

the local society. The internal contests of organizations involve not just the micro-politics of individuals and departments but the social groups, interests and resources of the surrounding context. The variables of the Systemic perspective include class and professions, nations and states, families and gender.

Important, therefore, to Systemic theory are differences between countries' social systems and changes within countries' social systems. As Whitley (1999) has shown for southeast Asia, prevailing forms of business may vary widely according to the local interplay of state, familial and market structures. Thus, in South Korea, a traditionally strong state has promoted the creation of the vast chaebol conglomerates; in nearby Taiwan, by contrast, the combination of an exclusionary Kuomintang state with the peculiar culture of Chinese family business has created an entrepreneurial economy of small and medium-sized firms, loosely linked by familial networks. Whitley (1991: 24) concludes: 'different kinds of enterprise structures become feasible and successful in particular social contexts, especially where cultures are homogeneous and share strong boundaries with nation states'. For all the contemporary talk of globalization, the peculiarities of local histories and local societies still matter.

Indeed, most large companies are hardly global at all. The Gestrin et al. (2000) survey of more than 200 Fortune Global 500 large corporations finds that on average roughly 60 per cent of their turnover and their assets were still concentrated in their home markets. Growth in international turnover and assets had been slow throughout the 1990s and the profit share from overseas had been disproportionately weak even before the Asian crisis of 1997–98. The world's largest international engineering conglomerates illustrate the point: only 41 per cent of General Electric's sales in 1999 were outside the United States, 35 per cent of assets and just one-third of profits (www.ge.com); at Hitachi, just 30 per cent of 1999 sales were outside Japan, 17 percent of assets, but, so depressed was the Japanese market, 69 per cent of profits (www.hitachi.co.jp). In Hu's (1992) sceptical phrase, companies like these are not so much global multinationals as domestic companies with international subsidiaries.

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Thus even the largest multinationals can retain strong local character. As Walker (1988: 395) observes, in its image and management style 'General Motors remains a thoroughly Midwestern company.' Apple is very Californian. IKEA is Swedish. Companies – whether as competitors, customers, partners or suppliers – vary widely according to their local contexts. Rather than rising above their origins, even multinationals may be deeply influenced by the industrial cultures, class structures, politics and professional biases of their home nations.

Indeed, the very notion of 'strategy' may be culturally peculiar. Arising in the particular conditions of North America in the post-war period, the Classical conception of strategy does not always fit comfortably in other cultures. Pascale (1982) reports that the Japanese do not even have a phrase for 'corporate strategy'. 'Strategy' has strong connotations of freewill and self-control, but many cultures prefer to interpret events less as the product of deliberate human action, and more as the result of God, fate, luck or history (Boyacigiller and Adler 1991). For example, fundamentalist Muslims see life following a path pre-ordained by God, while the Chinese often explain events in terms of 'Joss', a combination of luck and fate. To these deterministic cultures, the idea of 'strategy' embodies a voluntarism that is entirely alien. Boyacigiller and Adler's (1991) analysis suggests that Classical notions of strategy are the product of a historically peculiar coincidence between the American 'can-do' culture and the steady growth and 'Pax Americana' of the 1950s and early 1960s. Strategy as a managerial practice developed in a context of cultural voluntarism and economic and political security that was uniquely favourable to long-term strategic planning.

The American origins of the strategy concept may also constrain our understanding of what strategy involves. Wilks (1990) finds that the Anglo-Saxon cultures of the United States and the United Kingdom are biased towards an individualistic free-enterprise model of strategy that denigrates explicit reliance upon the state. By contrast, the traditional nationalism of the French and German states, and the developmental role of the Japanese state, have given to the Anglo-Saxon world's major competitors industrial cultures in which the enlisting of state resources is seen as a natural and important part of strategic management (Wilks 1990). Thus national approaches to strategy can be heavily distorted by what is locally regarded as culturally legitimate.

From this perspective, the Classical and Evolutionary emphases on markets and profitability, to the exclusion of state resources and national interests, are simply the product of very particular historical and social circumstances. This is not to say that they are necessarily 'wrong'. The current sociological appreciation of the 'institutional environments' of organizations (Meyer and Rowan 1977; DiMaggio and Powell 1983) highlights the social pressures to conform to local forms of rationality. American business works within a culture which respects profit, values technical procedures and regards the free market as an article of faith. In this context, any individual business-leader who repudiates outright the forms of Classical strategy-making risks losing his or her credibility in the face of auditors, customers, financial markets and governmental regulators, all of whom can exert considerable influence on success. Whether or not formal planning in the Classical mode is economically effective, if that is how key elements of the institutional environment expect business to be done, then it is sociologically efficient to at least go through the motions. The rationality of the Classical approach to strategy may be a social construct, but nevertheless it is one that it can be dangerous to ignore.

Yet it remains important to be clear how particular conceptions of strategy reflect and reinforce the limitations of a particular society. Indeed, Shrivastava (1986) goes so far as to allege that the whole discipline of orthodox strategic management actually constitutes a self-servingly conservative political ideology. He points to how the Classic theorists' normative emphasis on top-down management and profit maximization as the ultimate unifying goal serves to reproduce the conditions of hierarchically organized capitalist society in general. The firm is typically represented as a 'co-operative system' (e.g. Barnard 1938), for whom the

arrogation by top management of goal-setting and decision-making is merely a matter of administrative efficiency. Classical techniques of environmental analysis take the existing structures of society for granted and tend anyway to focus specifically on market factors, downplaying the relevance of social, cultural and political demands on the organization. Thus Michael Porter (1980: xix) blithely relegates his assumption of profit objectives to a footnote, and concentrates his industry analysis on five sets of economic forces amongst which government and labour are almost entirely lost.

Shrivastava (1986) concludes that orthodox strategic management is not a neutral, objective, scientific discipline, but an ideology that serves to normalize the existing structures of American society and universalize the goals of its dominant elite. Because it is designed to preserve the status quo, Classical strategic management traps strategists within a particularly narrow range of strategic options. To invoke state resources, or to challenge the top-down logic of strategic orthodoxy, is to play dangerously with the established social order.

The ideologies guiding strategy in different countries can be influenced strongly by different cultural traditions around the world. The American culture is hard-nosed and individualistic. In repeated surveys of international executives, Hampden-Turner and Trompenaars (1993) report that American attitudes stand out consistently from many of their competitors'. When asked whether the only goal of a company was profit, 40 per cent of American executives answered yes, against only 8 per cent from Japan and 11 per cent from Singapore. In a structured comparative analysis of American and South Korean managers' strategic decision-making criteria, project cash flow and return on investment were amongst the top three for the Americans. For the Koreans, it was sales growth and market share that were critical: cash-flow and return on investment ranked tenth and eleventh out of thirteen possible criteria (Hitt et al. 1997). In its understanding of what matters in strategy, the United States is clearly something of an outlier. But it is American practice and American research that dominate strategy textbooks world-wide.

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More than culture is involved in defining local approaches to strategy. Differences in strategy are so enduring, and patterns so hard to change, because they are also founded on real economic, social or political conditions. Recent analyses have explored the implications for strategy of different ownership structures in particular. The detached and relatively diffuse relationships between shareholders and their companies that are taken for granted in the Anglo-Saxon economies are unusual elsewhere round the world (Scott 1997). In the Germanic economies – Germany itself, Austria, Switzerland and to a lesser extent the Netherlands and Scandinavia – banks and other financial institutions play a central and interventionist role, with long-term relationships. For example, Deutsche Bank was a prime mover in bringing its two clients together to create the merged company Daimler Benz in 1926, and three-quarters of a century later, it was still the largest shareholder in the new DaimlerChrysler company, holding 12 per cent in 1999 (Gall 1995; www.daimlerchrysler.com). Deutsche Bank also has a 9 per

cent stake in the great German insurance company, Allianz, which reciprocates with a 5 per cent stake in the other direction. Although changes in German corporate law may prompt an unravelling, at the end of the twentieth century Allianz still occupied a central place in German capitalism, with substantial stakes in key utility companies, major chemicals and engineering companies, as well as the leading financial institutions. Not very much happens in German business without the Allianz or its allies having a say.

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In China, on the other hand, 34 per cent of the nation's output and no less than 110 million workers are accounted for by state-owned firms (Bruton et al. 2000).

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Theorists of a new 'managerial capitalism' (Marris 1964; Berle and Means 1967) suggest a growing split between ownership and control within large Western companies. Since the 1920s, firms have increasingly been governed by professional managers rather than by their true owners. These theorists accuse managers of running their firms in their own interests, sacrificing profitability for the perquisites of growth. From this Systemic perspective, then, Alfred Sloan's Classic goal of maximizing return on investment has been superseded by managerial objectives such as security, empire-building, high rewards and high status. Abundant evidence for such managerial self-interest can be found in studies of top management compensation. The continuous upward spiral of chief executive rewards in America, despite chronically poor economic performance, certainly does not suggest that top management is as unselfishly dedicated to shareholders' interests as Classical theory likes to think.

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For practising managers, then, the special advantage of the Systemic approach lies in its heightened sociological sensitivity. By alerting individual managers to the key elements of the social systems in which they work, the Systemic approach can widen the search for resources and deepen the appreciation of competitors. Every strategist should analyse his or her particular social characteristics, and those of his or her immediate social system, in order to grasp the variety of social resources and rules of conduct available (Whittington 1992). Managers can thereby free themselves from exclusive reliance on the capitalist resources of ownership and hierarchy, and open up the political resources of the state, the network resources of ethnicity or, if male, the patriarchal resources of masculinity. Sociologically sensitized, managers can also play reflexively on the ideological resources of their profession – exploit the Classical apparatus of strategic management not just for its technical answers but also for the enhanced legitimacy won by glossy display. The value of a MBA can lie in its packaging as much as its content. As for competitors, no presumptions should be made about their strategies without analysis of their social as well as industry structures. In planning moves and counter-moves, Systemically aware managers will not assume that competitor logics are the same as their own. In international competition

in particular, competitors' political power may be as important as their market power.

To conclude, the Systemic perspective challenges the universality of any single model of strategy. The objectives of strategy and the modes of strategy-making depend on the strategists' social characteristics and the social context within which they operate. From this perspective, the Classical approach emerges as culturally highly specific – after all, it originated in just two large American companies, Du Pont and General Motors, controlled by a single family during the 1920s. It may work well in certain contexts, and often the appearances at least of Classical rationality may be required anyway, but it will not translate everywhere. To insist on a socially alien form of strategy-making – whether in a Japanese *keiretsu* or a patriotic American business – is to court disaster. Moreover, to assume that your competitors or customers operate according to the same model of strategy as yourself risks substantial strategic miscalculation. A state-backed Chinese enterprise or a growth-oriented managerially controlled firm will not respond to competitive signals in the same way as a Classically run business; and, in any stand-off with an Anglo-Saxon profit-maximizer, both are likely to hold out much longer. The main message of the Systemic perspective, then, is that strategy must be sociologically sensitive.

Conclusions

The four approaches to strategy introduced in this chapter differ widely in their advice to management. The Classical school confidently prescribes a rational, detached and sequential approach, offered as a universal norm. The Evolutionary and Processual perspectives are more cautious, each sceptical of strategists' capacity to direct strategy effectively in this rational hierarchical way. For Evolutionists, environmental change is typically too fast, too unpredictable and too implacable to anticipate and pre-empt; their advice is to concentrate on day-to-day viability while trying to keep options open. Processualists doubt whether either organizations or markets work with the ruthless efficiency that Classicists and Evolutionists respectively claim, and incline therefore towards patient strategies of incremental adjustment and cultivation of core competences. Finally, Systemic theorists take a more relativistic stance, insisting that both the ends and means of strategy depend on the character of prevailing social systems, and that therefore even the hyper-rationality of the Classical school may be appropriate in some social contexts – but only some.

The main characteristics of the four approaches are summed up in Table 2.1. For the Classical school, strategy should be formal and explicit, its objective unambiguous profit maximization. Evolutionists generally agree on the second part – for high profitability is essential to survival – but regard efforts to secure this through extravagant long-term strategies as so much futile distraction. Efficiency is the Evolutionists' watchword. Processual theorists too dismiss Classical formality, seeing strategy as 'crafted', its goals vague and any logic often only emerging in retrospect. But where Processualists find economic irrationality, Systemic analysts search for other rationalities: for them, modes of strategy are deeply embedded in particular social systems, and their processes and objectives may be perfectly rational according to the criteria of the locally dominant groups.

The main focus of each of these approaches varies accordingly. For the Classical school, success or failure is determined internally, through the quality of managerial planning, analysis and calculation. The Processualists are inward-looking too, concerned with political bargaining processes the adjustment of managerial cognitive biases and the building of core skills and competences. The two other approaches emphasize the external. Evolutionists stress the determining impact of markets, and the Darwinian processes of natural selection. Systemic theorists argue that, to understand what is really going on within the organization and amongst competitors, the strategist must be sociologically sensitive.

Table 2.1 *The four perspectives on strategy*

	Classic	Processual	Evolutionary	Systemic
Strategy	Formal	Crafted	Efficient	Embedded
Rationale	Profit maximization	Vague	Survival	Local
Focus	Internal (plans)	Internal (politics/cognitions)	External (markets)	External (societies)
Processes	Analytical	Bargaining/learning	Darwinian	Social
Key influences	Economics/military	Psychology	Economics/biology	Sociology
Key authors	Chandler; Ansoff; Porter	Cyert and March; Mintzberg; Pettigrew	Hannan and Freeman; Williamson	Granovetter; Whitley
Emergence	1960s	1970s	1980s	1990s

Table 2.1 also associates each approach with the particular decades of their emergence (cf. Mintzberg et al. 1998). The Classical approach, with its emphasis on planning and analysis, had its heyday in the 1960s, a time of steady growth and American economic and technological confidence. Faith in planning was dented hard by the largely unforeseen oil shocks of 1974 and 1979 (Wilson 1990), leaving the field open for both the Processual stress on bounded rationality and the Evolutionary awe for market forces. Evolutionary arguments gained still greater resonance with the popularity of free-market economics during the 1980s.

The most recent arrival is the Systemic approach to strategy. Although firms have always differed in their objectives and contexts, the closing of the twentieth century and the opening of the new have forced a sharper appreciation of difference. The end to the stark opposition between capitalist America and the communist Soviet bloc has allowed a more nuanced appreciation of the different textures of market economies and the rich variety of their linkages with the rest of society. The former communist economies have themselves bred a wide variety

of capitalisms – from the wild Mafia capitalism of Russia to the deliberate 'red capitalism' of China. The dramatic successes – and occasionally equally dramatic failures – of Asian economies have drawn attention to the very different social structures that underlie their business systems. Even in the West, privatization has brought into the economic sphere organizations that must compete, yet which also operate with complex social and economic motives and rely upon many non-market resources. The profit-maximizing entrepreneurs and competitive markets of the textbooks are not the only reality with which strategists must contend. Competitive strategy in complex environments requires a Systemic sensitivity to the diversity of contemporary economic practices.

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