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"The most interesting business book of 2011 … read it principally for its profound yet common-sense approach to business"

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"There are many books on strategy but none as good and thought-provoking as Richard Rumelt's *Good Strategy/Bad Strategy*. This is a wonderful book, full of fresh ideas and practical advice, written in a clear and engaging way. It will change the way we teach and practice strategy."

—**Professor Costas Markides**, Robert P Bauman Chair in Strategic Leadership, London Business School

"Richard Rumelt's book, *Good Strategy/Bad Strategy*, is a must-read. It articulates the fundamentals of strategy and is exceptional in its depth and breadth of case illustrations and understanding on strategy. A book like this can only be written with many years of research and deep thought on the practice of strategy. I highly recommend this book to anyone interested in the field of strategy."

—**W. Chan Kim**, BCG Professor at INSEAD and co-author of *Blue Ocean Strategy: How to Create Uncontested Market Space and Make the Competition Irrelevant*

RICHARD RUMELT is one of the world's most influential thinkers on strategy and management. *The Economist* profiled him as one of twenty-five living persons who have had the most influence on management concepts and corporate practice. *McKinsey Quarterly* described him as "strategy's strategist", and "a giant in the field of strategy". Rumelt has always challenged dominant thinking: in 1972, he was the first person to uncover a statistical link between corporate strategy and profitability. He received his doctoral degree from Harvard Business School and holds the Harry and Elsa Kunin Chair at the UCLA Anderson School of Management. He is a consultant to small firms such as the Samuel Goldwyn Company and giants such as Shell International, as well as to organisations in the educational and not-for-profit worlds. *Good Strategy/Bad Strategy* was shortlisted for the *FT* & Goldman Sachs Business Book Award 2011.

RICHARD RUMELT

GOOD STRATEGY BAD STRATEGY

The difference and why it matters

PROFILE BOOKS

This edition published in 2017

First published in Great Britain in 2011 by
PROFILE BOOKS LTD
3 Holford Yard
Bevin Way
London WC1X 9HD
www.profilebooks.com

First published in the United States of America in 2011 by
Crown Business, an imprint of the Crown Publishing Group,
a division of Random House, Inc., New York

1 3 5 7 9 10 8 6 4 2

Printed and bound in Great Britain by
CPI Group (UK) Ltd, Croydon, CR0 4YY

A CIP catalogue record for this book is available from the British Library.

ISBN 978 1 78125 617 6

eISBN 978 1 84765 746 6

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INTRODUCTION

OVERWHELMING OBSTACLES

In 1805, England had a problem. Napoléon had conquered big chunks of Europe and planned the invasion of England. But to cross the Channel, he needed to wrest control of the sea away from the English. Off the southwest coast of Spain, the French and Spanish combined fleet of thirty-three ships met the smaller British fleet of twenty-seven ships. The well-developed tactics of the day were for the two opposing fleets to each stay in line, firing broadsides at each other. But British admiral Lord Nelson had a strategic insight. He broke the British fleet into two columns and drove them at the Franco-Spanish fleet, hitting their line perpendicularly. The lead British ships took a great risk, but Nelson judged that the less-trained Franco-Spanish gunners would not be able to compensate for the heavy swell that day. At the end of the Battle of Trafalgar, the French and Spanish lost twenty-two ships, two-thirds of their fleet. The British lost none. Nelson was mortally wounded, becoming, in death, Britain's greatest naval hero. Britain's naval dominance was ensured and remained unsurpassed for a century and a half.

Nelson's challenge was that he was outnumbered. His strategy was to risk his lead ships in order to break the coherence of his enemy's fleet. With coherence lost, he judged, the more experienced English captains would come out on top in the ensuing melee. Good strategy almost always looks this simple and obvious and does not take a thick deck of PowerPoint slides to explain. It does not pop out of some "strategic management" tool, matrix, chart, triangle, or fill-in-the-blanks scheme. Instead, a talented leader identifies the one or two critical issues in the situation—the pivot points that can multiply the effectiveness of effort—and then focuses and concentrates action and resources on them.

Despite the roar of voices wanting to equate strategy with ambition, leadership, "vision," planning, or the economic logic of competition, strategy is none of these. The core of strategy work is always the same: discovering the critical factors in a situation and designing a way of coordinating and focusing actions to deal with those factors.

A leader's most important responsibility is identifying the biggest challenges to forward progress and devising a coherent approach to overcoming them. In contexts ranging from corporate direction to national security, strategy matters. Yet we have become so accustomed to strategy as exhortation that we hardly blink an eye when a leader spouts slogans and announces high-sounding goals, calling the mixture a "strategy." Here are four examples of this syndrome.

- The event was a "strategy retreat." The CEO had modeled it on a similar event at British Airways he had attended several years before. About two hundred upper-level managers from around the world gathered in a hotel ballroom where top management presented a vision for the future: to be the most respected and successful company in their field. There was a specially produced motion picture featuring the firm's products and services being used in colorful settings around the world. There was an address by the CEO accompanied by dramatic music to highlight the company's "strategic" goals: global leadership, growth, and high shareholder return. There were breakouts into smaller groups to allow discussion and buy-in. There was a colorful release of balloons. There was everything but strategy. As an invited guest, I was disappointed but not surprised.

- A specialist in bonds, Lehman Brothers had been a pioneer in the new wave of mortgage-backed securities that buoyed Wall Street in the 2002–6 period. By 2006, signs of strain were appearing: U.S. home sales had peaked in mid-2005, and home price appreciation had stopped. A small increase in the Fed's interest rate had triggered an increase in foreclosures. Lehman CEO Richard Fuld's response, formalized in 2006, was a "strategy" of continuing to gain market share by growing faster than the rest of the industry. In the language of Wall Street, Lehman would do this by increasing its "risk appetite." That is, it would take on the deals its competitors were rejecting. Operating with only 3 percent equity, and much of its debt supplied on a very short-term basis, this policy should have been accompanied by clever ways of mitigating the increased risk. A good strategy recognizes the nature of the challenge and offers a way of surmounting it. Simply being ambitious is not a strategy. In 2008, Lehman Brothers ended its 158 years as an investment bank with a crash that sent the global financial system into a tailspin. Here, the consequences of bad strategy were disastrous for Lehman, the United States, and the world.

- In 2003, President George W. Bush authorized the U.S. military to invade and conquer Iraq. The invasion went quickly. Once the army-to-army fighting stopped, administration leaders had expected to oversee a rapid transition to a democratic civil society in Iraq. Instead, as a violent insurgency gathered momentum, individual units of the U.S. military fell back on running "search and destroy" missions out of secure bases—the same approach that had failed so badly in Vietnam. There were numerous high-sounding goals—freedom, democracy, reconstruction, security—but no coherent strategy for dealing with the insurgency.

  The change came in 2007. Having just written the *Army/Marine Corps Counterinsurgency Field Manual*, General David Petraeus was sent to Iraq, along with five additional brigades of troops. But more than the extra soldiers, Petraeus was armed with an actual strategy. His idea was that one could combat an insurgency as long as the large preponderance of civilians supported a legitimate government. The trick was to shift the military's focus from making patrols to protecting the populace. A populace that was not in fear of insurgent retaliation would provide the information necessary to isolate and combat the insurgent minority. This change, replacing amorphous goals with a true problem-solving strategy, made an enormous difference in the results achieved.

- In November 2006, I attended a short conference about Web 2.0 businesses. The term "Web 2.0" purportedly referred to a new approach to Web services, but none of the technologies involved were really new. The term was actually a code word for Google, MySpace, YouTube, Facebook, and various other new Web-based businesses that had suddenly become very valuable. At lunch, I found myself seated with seven other attendees at a round table. Someone asked me what I do. I briefly explained that I was a faculty member at UCLA where I taught and did research on strategy—and that I was a consultant on the subject to a variety of organizations.

  The CEO of a Web-services company was sitting directly across from me. He put down his fork and said, "Strategy is never quitting until you win." I could not have disagreed more, but I was not there to argue or lecture. "Winning is better than losing," I said, and the conversation turned to other matters.

The key insight driving this book is the hard-won lesson of a lifetime of experience at strategy work—as a consultant to organizations, as a personal adviser, as a teacher, and as a researcher. A good strategy does more than urge us forward toward a goal or vision. A good strategy honestly acknowledges the challenges being faced and provides an approach to overcoming them. And the greater the challenge, the more a good strategy focuses and coordinates efforts to achieve a powerful competitive punch or problem-solving effect.

Unfortunately, good strategy is the exception, not the rule. And the problem is growing. More and more organizational leaders say they have a strategy, but they do not. Instead, they espouse what I call *bad strategy*. Bad strategy tends to skip over pesky details such as problems. It ignores the power of choice and focus, trying instead to accommodate a multitude of conflicting demands and interests. Like a quarterback whose only advice to teammates is "Let's win," bad strategy covers up its failure to guide by embracing the language of broad goals, ambition, vision, and values. Each of these elements is, of course, an important part of human life. But, by themselves, they are not substitutes for the hard work of strategy.

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The gap between good strategy and the jumble of things people label "strategy" has grown over the years. In 1966, when I first began to study business strategy, there were only three books on the subject and no articles. Today, my personal library shelves are fat with books about strategy. Consulting firms specialize in strategy, PhDs are granted in strategy, and there are countless articles on the subject. But this plentitude has not brought clarity. Rather, the concept has been stretched to a gauzy thinness as pundits attach it to everything from utopian visions to rules for matching your tie with your shirt. To make matters worse, for many people in business, education, and government, the word "strategy" has become a verbal tic. Business speech transformed marketing into "marketing strategy," data processing into "IT strategy," and making acquisitions into a "growth strategy." Cut some prices and an observer will say that you have a "low-price strategy."

Further confusion is created by equating strategy with success or with ambition. This was my problem with the Web-services CEO who claimed "Strategy is never quitting until you win." This sort of mishmash of pop culture, motivational slogans, and business buzz speak is, unfortunately, increasingly common. It short-circuits real inventiveness and fails to distinguish among different senior-level management tasks and virtues. Strategy cannot be a useful concept if it is a synonym for success. Nor can it be a useful tool if it is confused with ambition, determination, inspirational leadership, and innovation. Ambition is drive and zeal to excel. Determination is commitment and grit. Innovation is the discovery and engineering of new ways to do things. Inspirational leadership motivates people to sacrifice for their own and the common good.[1] And strategy, responsive to innovation and ambition, selects the path, identifying how, why, and where leadership and determination are to be applied.

A word that can mean anything has lost its bite. To give content to a concept one has to draw lines, marking off what it denotes and what it does not. To begin the journey toward clarity, it is helpful to recognize that the words "strategy" and "strategic" are often sloppily used to mark decisions made by the highest-level officials. For example, in business, most mergers and acquisitions, investments in expensive new facilities, negotiations with important suppliers and customers, and overall organizational design are normally considered to be "strategic." However, when you speak of "strategy," you should not be simply marking the pay grade of the decision maker. Rather, the term "strategy" should mean a cohesive response to an important challenge. Unlike a stand-alone decision or a goal, a strategy is a coherent set of analyses, concepts, policies, arguments, and actions that respond to a high-stakes challenge.

Many people assume that a strategy is a big-picture overall direction, divorced from any specific action. But defining strategy as broad concepts, thereby leaving out action, creates a wide chasm between "strategy" and "implementation." If you accept this chasm, most strategy work becomes wheel spinning. Indeed, this is the most common complaint about "strategy." Echoing many others, one top executive told me, "We have a sophisticated strategy process, but there is a huge problem of execution. We almost always fall short of the goals we set for ourselves." If you have followed my line of argument, you can see the reason for this complaint. A good strategy includes a set of coherent actions. They are not "implementation" details; they are the punch in the strategy. A strategy that fails to define a variety of plausible and feasible immediate actions is missing a critical component.

Executives who complain about "execution" problems have usually confused strategy with goal setting. When the "strategy" process is basically a game of setting performance goals—so much market share and so much profit, so many students graduating high school, so many visitors to the museum—then there remains a yawning gap between these ambitions and action. Strategy is about *how* an organization will move forward. Doing strategy is figuring out *how* to advance the organization's interests. Of course, a leader can set goals and delegate to others the job of figuring out what to do. But that is not strategy. If that is how the organization runs, let's skip the spin and be honest—call it goal setting.

■ ■ ■

The purpose of this book is to wake you up to the dramatic differences between good strategy and bad strategy and to give you a leg up toward crafting good strategies.

A good strategy has an essential logical structure that I call the *kernel*. The kernel of a strategy contains three elements: a diagnosis, a guiding policy, and coherent action. The guiding policy specifies the approach to dealing with the obstacles called out in the diagnosis. It is like a signpost, marking the direction forward but not defining the details of the trip. Coherent actions are feasible coordinated policies, resource commitments, and actions designed to carry out the guiding policy.

Once you gain a facility with the structure and fundamentals of a good strategy, you will develop the parallel ability to detect the presence of bad strategy. Just as you do not need to be a director to detect a bad movie, you do not need economics, finance, or any other abstruse special knowledge to distinguish between good and bad strategy. For example, looking at the U.S. government's "strategy" for dealing with the 2008 financial crisis, you will see that essential elements are missing. In particular, there was no official diagnosis of the underlying malady. So, there can be no focus of resources and actions on a cure. There has only been a shift of resources from the public to the banks. You do not need a PhD in macroeconomics to make this judgment—it follows from understanding the nature of good strategy itself.

Bad strategy is more than just the absence of good strategy. Bad strategy has a life and logic of its own, a false edifice built on mistaken foundations. Bad strategy may actively avoid analyzing obstacles because a leader believes that negative thoughts get in the way. Leaders may create bad strategy by mistakenly treating strategy work as an exercise in goal setting rather than problem solving. Or they may avoid hard choices because they do not wish to offend anyone—generating a bad strategy that tries to cover all the bases rather than focus resources and actions.

The creeping spread of bad strategy affects us all. Heavy with goals and slogans, the national government has become less and less able to solve problems. Corporate boards sign off on strategic plans that are little more than wishful thinking. Our education system is rich with targets and standards, but poor in comprehending and countering the sources of underperformance. The only remedy is for us to demand more from those who lead. More than charisma and vision, we must demand good strategy.