Strategy Matters

By Susan Webber

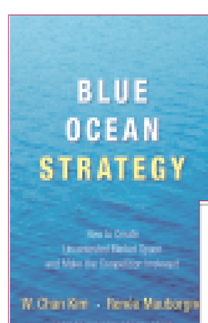
Blue Ocean Strategy
How to Create Uncontested Market Space and Make the Competition Irrelevant
By W. Chan Kim and Renée Mauborgne
Harvard Business School, $27.95

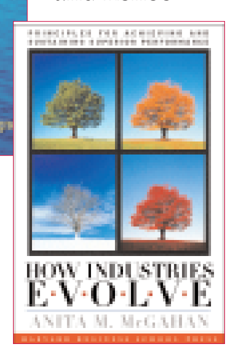
How Industries Evolve
Principles for Achieving and Sustaining Superior Performance
By Anita M. McGahan
Harvard Business School, $35.00

Perhaps I'm jaded, but too seldom does business writing grab my attention. A thought-provoking exception was a 2004 *Financial Times* article by John Kay on obliquity. In essence, it said, in complex systems that we can influence, pursuing goals indirectly is better than a straightforward approach, since we do not understand the totality well enough to plot the right path. Thus people who seek to be happy are rarely the happiest, and companies out to maximize shareholder value are less profitable than those targeting more complex objectives.

*S*USAN *W*EBBER *is founder of Aurora Advisors, a management-consulting firm based in New York and Sydney. She reviewed* Anti-Americanism *in the May/June 2004 issue.*

Boston University strategy professor Anita McGahan and her INSEAD counterparts W. Chan Kim and Renée Mauborgne are out to capture readers' imaginations. In particular, *Blue Ocean Strategy* is, forgive the pun, a corporate wet dream: *Follow our prescription and you will pull free of competitors.*





Needless to say, it's not that simple, and in trying to make it so, McGahan, Kim, and Mauborgne push their claims far beyond what their findings support; their frameworks are presented as universally applicable guides to action. In each case, the clear objective is to produce a landmark work with the same impact as BCG's cows-and-stars framework or Michael Porter's five-forces model. The authors would have done better to understand what their theories really proved, and the limits of their applicability. Their aspirations—the desire to break new ground—actually undermine each work, one dramatically, the other in subtle ways.

Kim and Mauborgne's *Blue Ocean* examines a crucial topic—how can businesses escape their competitive confines and find virgin territory? It focuses on companies that have created new markets and presents tools for identifying and pursuing market opportunities. Using the metaphor of open water, the book contrasts red oceans of bloody, contested, known markets with blue oceans of "untapped market space, demand creation, and the opportunity for highly profitable growth."

It's not all smooth sailing, though. The authors' first damning failing is a tendency to force facts to fit their thesis. They point to established, mature innovators, depicting the companies as if they took their current shape at an early stage. It doesn't work like this, of course. Progress is typically incremental and experimental. But the authors' narratives often collapse a series of initiatives into a dramatic leap, realizing a fully formed corporate vision, like Athena springing full-grown from Zeus's forehead. For example, *Blue Ocean* describes Bloomberg's dual flat-panel screens, analytics, and online shopping as if they were present from the outset. In fact, these features were beyond the scope of the then-available technology! Similarly, the authors present Southwest Airlines as a pioneer of discount air travel, when it improved on earlier ventures, particularly People Express. Other examples cited, such as Dell Computer and Wal-Mart, are contradicted by the better-researched *How Industries Evolve*.

The authors too often rewrite business history to serve their ends. For example, to prove that, "Failing to address the concerns of employees . . . can be expensive," Kim and Mabourgne claim, "When Merrill Lynch's management, for example, announced plans to create an online brokerage service, its stock price fell by 14 percent as reports emerged of resistance and infighting." Sorry, but markets care about bottom lines, not employee morale. Merrill had been a longstanding holdout against cannibalizing its lucrative traditional brokerage business, and the online launch was an admission that its old pricing model was unsustainable. Internet consultant Clay Shirky commented at the time: "When a company can cut its prices 70% and still be three times as expensive as its competitors, something has to give. Usually that is the company's stock price."

More obvious is the authors' assertion that Henry Ford perceived difficulty of driving and unreliability as the main obstacles to broad adoption of the automobile. Huh? Ford saw price as the big barrier; the other issues were secondary.

Second, *Blue Ocean*'s frameworks are not particularly useful. Most are simplistic, long on feel-good and short on rigor. To illustrate, the Blue Ocean Idea Index is supposed to weed out duds by rating new products on utility, price, cost, and adoption (as in, ease of). Self-assessment exercises like this are a garbage-in, garbage-out process. New Coke would undoubtedly have been rated favorably by Coca-Cola's managers.

Third, the book is larded with jargon: "The grid pushes companies not only to ask all four questions in the four actions framework but also to *act* on all four to create a new value curve."

How Industries Evolve is less muddled and more helpful than *Blue Ocean*, though its thesis is substantially more difficult to summarize briefly. Based on a statistical analysis of more than seven hundred companies, McGahan classifies industry development into four categories—Progressive, Creative, Intermediating, and Radical. (She maintains that every industry fits into one and only one of her categories.) Which path an industry follows depends on whether its core assets or core activities are threatened.

To illustrate, in Progressive change, which holds for discount retailers and commercial airlines, neither core assets nor core activities are in jeopardy. A company's success, McGahan argues, depends on developing and adhering to an industry model that is visible and well-recognized. Here, she recommends benchmarking and building capabilities incrementally, rather than via acquisition.

By contrast, in industries facing

Sorry, but markets care about bottom lines, not employee morale.

Radical change, such as landline-telephone manufacturing and overnight letter delivery, both core assets and core activities are under attack. In this case, she advocates curtailing investment and milking existing assets and relationships.

McGahan's analysis, and the scope of her study—to say nothing of her association with Harvard strategy guru Michael Porter—almost guarantee that *How Industries Evolve* will become a fixture in MBA programs. But it is less clear that it will be as widely used in practice.

The book's major shortcoming is that it revolves around McGahan's "four sizes fit all" model. Although she works through some options under her typologies, they are usually limited, binary choices (e.g., when to lead rather than follow). As a result, her construct is dogmatic and deterministic. She asks readers to accept that their choices are circumscribed, but she never proves her central thesis—that companies that break her rules are doomed to fail. McGahan simply asserts, for example, that "many of the most noted retail dot-coms . . . got into trouble because they attempted to change the structure of industries on Progressive paths." She refers to her statistical analyses and twenty-five in-depth case studies, but never divulges her methodology. And even though she frequently cites examples, they are typically brief references, illustrative rather than persuasive.

A related weakness is that her book is comprehensive at the expense of utility. She operates at a high level of abstraction when most strategic analysis occurs on a less lofty plane. By contrast, even though Porter's industry-forces framework was a high-level paradigm, he covered a great deal of practical ground, discussing strategy formulation in specific contexts and providing many valuable tools, checklists, and ideas.

Sadly, the reach of *How Industries Evolve*—like that of *Blue Ocean Strategy*—exceeds its grasp. Strategy is a well-tilled field, and saying something that is both new and broadly applicable is no small feat. Indeed, one of the most useful business books in recent years, Malcolm Gladwell's *The Tipping Point*, is a general-interest examination of the propagation of trends, yet its nuanced discussion of human behavior adds a new dimension to strategic thinking. The dictates of obliquity suggest that to improve this discipline, the best path may be an end run. ♦

Our Man In the IRS

By Theodore Kinni

Many Unhappy Returns

One Man's Quest to Turn Around the Most Unpopular Organization in America
By Charles O. Rossotti
Harvard Business School, $26.95

"Were you ever in the military, and if you were, did you volunteer for a suicide mission?" a reporter asked Charles Rossotti on his nomination as IRS commissioner in July 1997. Rossotti, whose book details his five-year stretch as the first businessman—after fifty years of tax professionals—to lead the Internal Revenue Service, calls the question "snide" and doesn't record his answer.

In fact, the job does seem like a suicide mission. By 1997, the IRS had the "largest number of customers and the lowest approval rating of any institution in America."

Worth Noting

Integrity Is All You've Got

And Seven Other Lessons of the Entrepreneurial Life
By Karl Eller
McGraw-Hill, $24.95

Eller gives it all away on page 18: "The secret of a successful businessperson is to leverage each failure into a bigger success." His career as executive and entrepreneur, redefining the business of outdoor advertising, is testament to that. Before *Integrity* even gets to the successes, Eller candidly discusses his career failures—"I was ruined financially, professionally, and publicly by the failure of Circle K"—and explains how he was able to pick up the pieces and start again.

Integrity energetically recounts Eller's career—his crashes and comebacks, his decisions and deals—while offering guidance to those interested in following in some, if not all, of his footsteps. Sometimes Eller's rah-rah counsel is too commonsense to be of use or even interest ("When you negotiate, make sure you get what you need, but don't be greedy"), but it's always sound, and the book nicely balances advice and autobiography.

Eller's enthusiasm for entrepreneurship is undeniably heartfelt. "Big risks, nagging problems, occasional failure—all of these loom ahead," he writes. "The downside is acceptable for one compelling reason: entrepreneurs have fun. So much so that any other life doesn't feel like living."

Conspiracy of Fools

By Kurt Eichenwald
Broadway, $26.00

New York Times reporter Eichenwald writes corporate-crime chronicles that read like thrillers—a narrative pace necessary to make it through yet another book about what went wrong at Enron, much less a 750-page book. But even though every potential reader already knows the story's outline, few who open *Conspiracy of Fools* will easily put it down. Eichenwald is a masterful writer, smoothly blending authoritative reportage with lively yet realistic dialogue, and he spins out this tale of woe beautifully.

The author begins the saga in the mid-1980s, with a now-familiar cast of villains, and methodically carries it through Andy Fastow's dark schemes, Enron's transition from conventional energy company to market manipulator, *Fortune*'s cover-story exposé, political scandal, bankruptcy, and the public humiliation of Jeff Skilling and Ken Lay. Eichenwald doesn't blame crime, per se, for Enron's doom—rather, he targets "[s]hocking incompetence, unjustified arrogance, compromised ethics and an utter contempt for the market's judgment."

One wishes that the book's focus were a bit broader than one company's implosion—after all, the author promises "a portrait of an America in upheaval . . . the story of a wrenching period of economic and political tumult as revealed through a single corporate scandal." But few could ask for a better, or more readable, chronicle of that single corporate scandal.

No Place to Hide

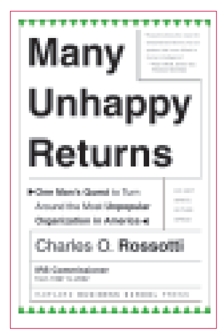
By Robert O'Harrow Jr.
Free Press, $26.00

O'Harrow, a *Washington Post* reporter, is hardly the first journalist to pull back the curtain of the data-mining industry, but he's the first to show how high-tech databases are combining consumer information and national-security surveillance to create "a public-private security infrastructure" that threatens this nation's traditions "of individual privacy, autonomy, and civil liberties." Eschewing libertarian rhetoric about privacy, the author explains who has access to purportedly confidential police files, which companies' supercomputers process credit reports, and just why identity theft "is almost laughably easy to commit, and terribly difficult to prevent."

Some of the information is collected for marketing reasons, some ostensibly for national security, some for pur-

The agency, which hadn't been reorganized since 1952, was a train wreck driven by illegal collection quotas and virtually continuous crisis response. Its archaic information systems, which held the tax records of 132 million people and 6 million businesses, were so old that the only programmers who knew how to keep them running were retiring. Worse, the latest IT modernization initiative had just been declared a $4 *billion* failure.

Rossotti's first job was to switch the IRS's modus operandi from a reactive approach to a proactive one. Apparently, every time more bad news surfaced, the IRS and its political bosses simply promised to fix the problem without any regard to whether a solution was feasible. Rossotti assigned a team to tabulate these promises and duly received a list that exceeded "five thousand line-item recommendations." He winnowed those down to 157 objectives—low-hanging fruit that could be gathered in twelve to eighteen months.



At the same time, he created a restructuring plan—the first since 1952—and adroitly built a coalition of supporters that helped get it signed into law in July 1998. Interestingly, the Clinton administration, which had hired Rossotti to create just such a change, opposed the plan. It feared that it might lose control over IRS management and, with it, some of the executive branch's power. According to Rossotti, Clinton made a show of signing the bill only after its passage became inevitable.

The IRS reform bill enabled Rossotti to restructure the agency's convoluted organizational structure. Instead of regional fiefdoms trying to administer a tax code too big for any one organization to get its arms around, the IRS followed what is becoming today's standard business model. It was recast into four specialized operating divisions by taxpayer "customer" category: wage and investment income, small business and self-employed, large and midsize business, and tax-exempt and government entities.

Rossotti also paid careful attention to rebuilding the morale and standards of the IRS's 100,000 employees. Buffeted by years of scandals and often viewed as ogres by the general public, the IRS workforce was clearly shell-shocked. Rossotti found that, while suspicious, most employees welcomed both leadership and change. Further, once they became convinced that the plan was real, they happily embraced it.

Unlike many CEO memoirs and turnaround tales, *Many Unhappy Returns* pays careful attention to drawing out and articulating the larger lessons. In this case, they usually reiterate change-management tenets we've heard often over the years: Be inclusive, open, and honest; get the right people in the right jobs; measure the right things; lead from the frontlines; and, importantly, the real limits are the systemic ones—mainly, the exceptionally unwieldy and ever-changing tax code, which the IRS does not write but must enforce.

Rossotti acknowledges that his power to create systemic change was limited and says that he explicitly refused to discuss his ideas on tax reform while commissioner out of fear that it would compromise his ability to work effectively with Congress and the administration. Here, he breaks his silence and devotes a chapter to tax reform.

His prescription will disappoint advocates of radical schemes, such

Theodore Kinni is editor of The Business Reader Review *and has authored or ghostwritten eight business books, including, most recently,* No Substitute for Victory: Lessons in Strategy and Leadership From General Douglas MacArthur. *His last article was "Faith at Work," the Nov/Dec 2003 cover story.*

as a flat tax or a national sales tax in lieu of income tax. Rossotti suggests that there is little hope of eliminating the 83,000-plus pages of tax code. (He discovered that even the IRS doesn't know exactly long it is.) Instead, he offers a three-step plan to patch the big potholes. First, he argues, the tax filing for 70 percent of taxpayers could be greatly simplified by clarifying and reducing the regulations covering family provisions and savings accounts, and abolishing "the ominous and obsolete alternative minimum tax." Second, he recommends the legislative abolition of tax shelters existing solely to hide billions in taxes rightfully owed by corporations and wealthy individuals. Finally, he says that the IRS could capture some $230 billion in unpaid taxes if the White House simply provided the agency the funds it needs to do its job.

It's hard to believe that the executive branch is starving the agency that provides it $2 trillion per year in income, but Rossotti lays the lion's share of the blame for the IRS's problems at 1600 Pennsylvania Ave, regardless of which political party is in residence. In our nation's capital, political power is a prime determinant of budget dollars, and, perhaps unsurprisingly, the ever-unpopular IRS has none. As a result, its budget is anemic, with few advocates for increases. "Incredibly," writes Rossotti, who always appears stunned when reporting that the government doesn't operate like a business, "the OMB [Office of Management and Budget, the White House budgetary arm] tries to appear fiscally responsible by neglecting the collection of its revenues and accounts receivable!"

Rossotti's tenure featured one notable failure: ironically, in the one area in which he was eminently suited for the job—the agency's troubled IT initiative. In nominating as commissioner the co-founder, chairman, and CEO of American Management Systems Inc., a billion-dollar IT consulting firm, Bill Clinton clearly hoped that Rossotti would apply his expertise in large-scale implementations to finally resolve the IRS's IT problems.

But Rossotti had his work cut out for him: He found an organization with "no fewer than 130 separate computer systems, running on 1,500 mainframe and midrange computers from twenty-seven vendors and comprising about eighteen thousand vendor-supplied software products and fifty million lines of custom computer code." Worse was the fact that an RFP for a fifteen-year modernization project was already in the works and predicated on an organizational structure that Rossotti intended to radically revamp.

In December 1998, a year after Rossotti took office, the agency awarded the $8 billion prime-contractor contract to Computer Sciences Corp. The work didn't go as smoothly as he'd hoped. "As I left the IRS in November 2002," he writes, "the IRS's technology program was a lot better than I had found it, but it was still a work in progress." He neglects to mention that in December 2003, a year after he left office, the IRS Oversight Board reported that five years in, the IT modernization program was already running 40 percent over budget and was as much as twenty-seven months behind schedule.

So what's the final verdict on Rossotti's tenure? Aside from the continuing IT dilemma, which is no small matter, he did successfully set the IRS on a path to modernization. In the first five years, he created fundamental change in structure, culture, and customer service. The IRS's customer-satisfaction numbers are significantly higher, and the agency is substantially more responsive. The IRS is still widely disliked, but think about it—if you sent your customers big bills with similarly tenuous and often-contentious connections to services received, yours might not be much better. ♦

poses to be named later. But few of us are aware of much of this collection or analysis, or what it might be used for. And no one seems sure who's in charge of all the information pouring in from security cameras and credit bureaus and websites and subway MetroCards and supermarket scanners, since the government has outsourced the work to a variety of firms that are accountable to no one.

There's no need for artificial melodrama in O'Harrow's survey of the information industry. After reading *No Place to Hide*, you'll think twice about handing over your Social Security number to some website or clerk.

Charming Your Way to the Top
Hollywood's Premier P.R. Executive Shows You How to Get Ahead
By Michael Levine
Lyons, $22.95

Talk about a simple formula for success: *Be charming.* PR guru Levine begins by pointing out something that's obvious but often overlooked—whether in entertainment, politics, business, or anything else, "charm pays." Charm smooths over problems, helps you get noticed, even makes you stand out ("It can become part of your brand: the charming bookstore, the charming insurance company, the charming computer solutions provider").

Levine lumps different things under the heading of "charm"—charisma, friendliness, courtesy, competence—and implies that sincerity is optional: "Charm means *making the other person believe you care*." The important thing is to add charm to every aspect of your life—for success, charm is "an *absolute necessity*." For better or, more likely, worse, he's probably right.

To get the most out of *Charming Your Way*, look past Levine's italics, his occasionally grating "keep smiling!" tone, and his less-than-helpful celebrity-based material, including a superfluous photo section. Of course, if you're currently at the top, you don't need this book—you must be pretty damn charming already. *Keep smiling!*

—Matthew Budman