


COMMENTARY



The risk of incrementalism
and the importance of
clear strategy during
periods of uncertainty

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Marakon

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Chairpersons and CEOs are at risk of becoming incremental in their thinking as a natural defense to today's uncertain environment. We observe companies that are at risk of getting stuck given the extreme set of existential risk CEOs and Board members face in managing through today's environment. They may take comfort from managing operational improvements within their control and shy away from bold choices that might deliver competitive advantage by fundamentally altering their strategy.

While performance matters, strategy and planning for the future have never been more important. The agenda for successful companies must move from being internal and operationally focused (the primary orientation during the pandemic), toward understanding and focusing on a new set of opportunities and risks.

Increasing unpredictability

The level of uncertainty and volatility in the financial and geopolitical environment is higher than we have seen in decades. This is reflected in terms of recent capital markets performance (bond volatility materially above stock market volatility) and the challenges facing central banks in setting rate policy. More profound, however, is the clear recognition that we have entered a new cold war. This may have been masked slightly by the immediate and prolonged effects of the pandemic but has become apparent with increasingly strained international relationships between the United States and Europe on the one side and Russian and China on the other.

History tells us that during periods of heightened geopolitical tensions, we are more likely to experience instability and economic damage. Tensions between major trading partners lead to protectionist measures, disrupting supply chains and increasing costs. Globally, collaboration is reduced, thereby stifling innovation, and overall, the sense of instability impacts consumer confidence. The only certainty is uncertainty and continued volatility for the foreseeable future.

The risk of incrementalism

Incremental thinking creates challenges and managerial risks for CEOs and their management teams, as they push against a default mindset of “steady as she goes” that generally takes hold in board rooms during periods of high uncertainty. While it's hard to argue against a “steady as she goes strategy”, it has hidden risks and almost always results in missed opportunities.

Incremental thinking is a mindset in which leaders focus on incremental improvements to existing processes and business models rather than looking for more transformative solutions, or step outs. This type of thinking can be particularly damaging in an environment where the “status quo” constantly shifts, and new challenges and opportunities emerge.

In a volatile environment, incremental thinking can lead to missed opportunities and increased risk. Senior management may become too focused on optimising existing value chains rather than looking for new ways to innovate and adapt to changing conditions or accelerate opportunities that result from major shifts. This can result in missed opportunities to enter new markets, develop new products or services, attract different customers, or adopt new technologies that can help to differentiate the organisation from its competitors.

Moreover, incremental thinking can lead to a failure to recognise and respond to emerging risks. If senior management is too focused on the status quo and incremental improvements, they may not be adequately prepared to address new risks that arise.

To combat the risk of incremental thinking, senior management needs to adopt a more agile and innovative approach to strategy development. They need to be open to new ideas and willing to take calculated risks. They also need to be willing to challenge existing assumptions and be open to new ways of thinking and views about the type of world that exists around them.

In such an environment, having a sound strategy becomes even more important.

Benefits of a clear strategy

A strategy establishes a clear ambition and then sets out a plan of action designed to achieve a particular goal or objective. It provides a roadmap for decision-making and outlines the steps needed to achieve success. In a volatile environment, a clear strategy enables leaders to be proactive rather than

reactive. It helps them to anticipate challenges and opportunities, and to make decisions based on a clear understanding of their goals and priorities.

Tackling uncertainty

Accurately forecasting the future is impossible and the odds of 'guessing it right' are low, particularly during times of high volatility and political unrest. Scenario planning is a critical tool to help leaders think about these macro uncertainties and their potential responses. Organisations often view scenario planning as a 'tick the box' exercise which is delegated to the risk team. In today's uncertain environment organisations need to develop scenarios that are realistic and radical. More importantly, the C-suite needs to be involved in considering the implications and debating the options to mitigate the company's downside risks and to maximise potential opportunities.

Figure 1. Benefits of a clear strategy



Below we highlight key considerations and questions for CEOs and Boards.

- ▶ **Geopolitical conflict.** All companies should identify their geopolitical risk and assess the potential impact. Are assets in certain countries at risk? Is the company exposed to changing regulations? What's the indirect impact of sanctions on supply chains and export controls?
- ▶ **Economic downturn** (e.g. recession or prolonged inflation). Can we improve efficiency to reduce costs? What is driving the cost base and where can discretionary spend be reduced without cutting investment in areas critical for delivering the strategy? What parts of the portfolio are core to the future of the business and what parts could be divested? Are there assets currently trading below their longer-term intrinsic value, that could be acquisition targets?
- ▶ **Climate change** (e.g. physical event or regulatory change). Has a risk assessment and scenario planning been carried out to identify vulnerabilities and plan for mitigating measures? What are the implications for supply chains? Are there opportunities for building resilience in high-risk areas? What could trigger a sudden change in regulation (e.g. physical event or an election)? How can you work with governments to shape future regulation? What are the expectations of key stakeholders (e.g. governments, investors, customers and employees)?
- ▶ **Emerging technologies** (e.g. AI or energy storage). What emerging technologies have the potential to disrupt the current business model? Is the company scanning for new technologies beyond its sector? Can these technologies be embraced or are they a threat?

Closing thoughts

In today's uncertain and volatile environment, companies need to conduct rigorous scenario planning, continually scan the external environment, engage with a broad range of stakeholders and look for signposts that indicate the direction of change. At the earliest sign, CEOs and Boards need to be prepared to act and act quickly. Having a sound strategy is critical to manage through uncertainty. It provides direction, allows organisations to be agile and adaptable, and helps to manage risk. With a clear strategy and staying focused on their goals, organisations can weather the challenging times and position themselves for long-term success. Incremental and tactical improvements are useful but may prove to be inadequate to take advantage of the opportunity and manage risk at this time.

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About Marakon

Marakon is a strategy and organisational advisory firm with the experience and track record of helping CEOs and their leadership teams deliver sustainable, profitable growth. We get hired when our client's ambitions are high, the path to get there is not clear (or taking too long) and lasting capabilities are as important as immediate impact.

We help clients achieve their ambitions for sustainable, profitable growth through:

- Stronger strategies and advantaged execution based on:
 - A better understanding of what drives client economics and value
 - Insight into changing industry dynamics and the context in which clients need to succeed
- A stronger management framework to generate better ideas and link decisions and actions to value
- A stronger organisation with a more focused top management agenda and well-aligned resources
- A more confident and effective leadership team that's focused, decisive and strategic

We have a joint team delivery approach where client ownership and engagement is paramount. Partners are highly engaged in the work product and supported by strong analytical and industry relevant capability. We work as advisers and catalysts in close, trust-based relationships with top management teams.

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