KPPM organisational strategists

Why Strategies Fail

Human beings are still hardwired for survival on the African savannas

In 2003 Charles Roxburgh at McKinsey wrote an important article *Hidden flaws in strategy*, which explains how our natural instincts can lead to bad decisions. As strategists, KPPM is constantly looking to simplify and explain the process, and to avoid Roxburgh's eight mistakes:

1. Overconfidence

Humans are overconfident of our ability to make accurate estimates and unable or unwilling to reveal our ignorance. This leads to 'overoptimism' where we forecast better outcomes than the facts would indicate. Overconfidence and overoptimism are dangerous tools in strategic planning as they are unrealistic and imprecise. To counter this:

- Test a wider range of options
- Downgrade your most pessimistic scenario (remember we err on the side of optimism)
- Build in flexibility - be sceptical of certainty

2. Mental accounting

Surprisingly we treat money differently depending where it comes from, where it is kept and how it is spent, we are likely to be less critical of spending on new ideas than on core business.

- Treat every dollar the same, no matter where it comes from or how it is used
- Decisions should be judged on the same criteria, don't reclassify to make an idea acceptable

3. The status quo bias

People would rather leave things as they are - they are more concerned about the risk of loss than excited by the prospect of gain. But the right strategy can be to 'hold on', so when is the status quo good, and when is it inaction?

- Adopt a radical view of all big decisions, don't be afraid to sell, change or move on
- Subject 'do nothing' options to the same rigour as change options

4. Anchoring

One of the most peculiar wiring flaws is anchoring. Present the brain with a number and then ask it to make an estimate of something completely unrelated, and it will anchor its estimate on the first number. This works very well in negotiating if you name a high figure first, but is dangerous if you're anchored to the past (e.g. a belief that stocks will always rise).

- Analyse trends in the context of the last 20-30 years, not the last 2-3

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5. The sunk cost effect

This failure is often called "throwing good money after bad" and it's hard to avoid – we would rather spend another $10,000 to complete an uneconomic $100,000 project than write off the $100,000 – once we're anchored at $100,000 an extra 10% doesn't seem so bad.

- Apply the full rigour of analysis to the extra incremental investment
- Be prepared to kill experiments early, jettison the losers and concentrate on the winners
- Use gated funding, only release additional funds when targets have been reached

6. The herding instinct

The desire to conform is a fundamental human trait. Warren Buffett said "Failing conventionally is the route to go; as a group, lemmings may have a rotten image, but no individual lemming has ever received bad press", yet great strategies break away from the trend.

- Find unique sources of strategic advantage – the new and unusual
- Look outside your industry
- Be prepared to kill failing strategies early

7. Misestimating future hedonic states

People find it hard to estimate how much pleasure or pain they will feel if their circumstances change dramatically, yet evidence shows that they adapt quickly and their level of pleasure (hedonic state) ends up broadly where it was before. For example, frontline staff often resist a takeover or merger even when they are frustrated with the current management.

- Approach change with a dispassionate and unemotional view, this is where KPPM comes in, we can see the situation from the outside – once you've made your plans, use empathy in the rollout
- Keep things in perspective, Field Marshall Slim said "In battle nothing is ever as good or as bad as the first reports of excited men would have it", good advice

8. False consensus

People tend to overestimate the extent to which others share their views, beliefs and experiences. Do you recognise these:

Confirmation bias: seeking out opinions and facts that support our own beliefs and hypotheses

Selective recall: remembering only facts and experiences that reinforce our assumptions

Biased evaluation: the quick acceptance of evidence that supports our ideas while contradictory evidence is subjected to rigorous evaluation (and almost certain rejection), for example questioning the motivation or competence of critics

Groupthink: the pressure to agree with others in team-based cultures

False consensus leads to overlooking important threats and persisting with doomed ideas. Tackle false consensus head on, by:

- Creating a culture of challenge, valuing open and constructive criticism
- Ensuring role models have strong checks and balances – use independent reviews
- Instead of asking for agreement about an idea, ask for equal and opposite hypotheses

For the full article, see
The McKinsey Quarterly: May 2003