Special Report

Forever Blue

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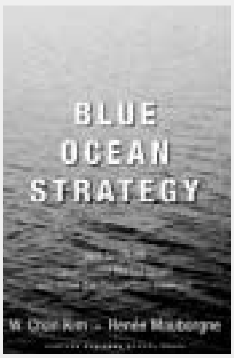

To many in the business world, strategy formulation remains the pinnacle of corporate endeavour. Yet, as business becomes ever more competitive, and growth more elusive, strategy is often little more than a call to reform ranks for the next bloody battle. Orthodox strategy is all about beating the competition – literally, to death.

It is no coincidence that strategic plans are couched in warlike notions. They exhort companies to seize competitive advantage, battle over market share, and struggle for differentiation. The trouble is that if the opposing army is doing the exact same thing, such strategies often cancel each other out or trigger immediate tit-for-tat retaliation. Strategy quickly reverts to tactical opportunism. As the German Field Marshall Helmuth Carl Bernard von Moltke memorably observed: "No battle plan ever survives contact with the enemy." So where should companies turn for a more innovative approach to strategy?

Blue Ocean Strategy claims to hold the answer and, along the way, challenges everything you thought you knew about strategy. The authors, W. Chan Kim and Renée Mauborgne, argue that cut-throat competition results in nothing but a bloody red ocean as rivals fight over shrinking profits. Based on a study of 150 strategic moves spanning more than 100 years and 30 industries, they argue that lasting success comes not from battling competitors, but from creating "blue oceans" – untapped new market spaces with high growth potential, something they call value innovation.

Smart moves

Before diving into the blue ocean it is worth looking around from the diving board. The vista is clear. Those in search of strategic inspiration have traditionally had two alternatives. Either, they started with their industry as the basic strategic building block, or with their company. The former led them towards Michael Porter's Five Forces framework which focuses on industries; while the latter inclined them towards Gary Hamel and CK Prahalad's core competencies which focuses on companies.

Over the last two decades a great deal of intellectual energy has been expended on refining these two worldviews. Yet, both view the world from a purely competitive stand point – they see strategy as a zero-sum game. According to Kim and Mauborgne there's also an intellectual irony underlying both. "There's no such thing as a permanently great company or a permanently great industry. All industries rise and fall as do companies," they explain. "However, there are permanently smart strategic moves."

Kim and Mauborgne are methodical. Their work is characterised by rigorous research and attention to detail. They are also patient. On the strength of their *Harvard Business Review* articles alone, some thought-leaders of their standing would be on their second or third book. Kim

Photo: John Abbott

Kim and Mauborgne: Life on the ocean wave

and Mauborgne are only now publishing their first. *Blue Ocean Strategy* is the culmination of more than a decade of work.

The Korean and American, now based at Insead, wanted to be sure their theories stand up – that they cannot be dismissed as a passing fad or fashion. Nothing has been left to chance. Extending their data back over 100 years took two years of painstaking research. “We have sleepless nights getting the data right,” reflects Professor Kim, a former University of Michigan Business School professor who studied under CK Prahalad and alongside Gary Hamel. Mauborgne, an American, joined intellectual forces with Kim at Michigan.

So what does all this data show? Kim and Mauborgne believe that the business world has been overlooking one of the key lessons of wealth creation in history. Their research indicates that the major source of wealth creation over time is not the industry that a company plays in *per se*. Nor did they find permanently great companies that consistently captured wealth. This contradicts books like *In Search of Excellence, Built to Last,* and *Good to Great,* which seek to distil the characteristics of great companies. Instead they found that an industry’s and a company’s ups and downs are substantially attributable to something they call strategic moves.

“When we first asked ourselves if there is a systematic approach to create blue oceans, we began by looking at the basic unit of analysis used in business literature: the company. However, history reveals that there are no perpetually excellent companies,” they say. “Consider *In Search of Excellence,* the first bestselling business book published in 1982. Within just five years two-thirds of the identified model firms in the book had declined. Likewise, for those sample companies in the book *Built to Last*, another blockbuster business book, it was later found that if industry performance was removed from the equation, many of the companies in *Built to Last* were no longer exceptionally excellent. As Foster and Kaplan point out in their book *Creative Destruction*, the companies listed certainly outperformed their markets, but so did their entire industries.”

So if there is no perpetually high-performing company and if the same company can be brilliant at one moment and wrongheaded another, it appears that the company is not the appropriate unit of analysis in exploring the roots of high performance. Likewise, there are no perpetually excellent industries. Five years ago, for example, people envied companies in the IT industry; today the reverse is largely true.

Kim and Mauborgne’s analysis of industry history revealed that the strategic move, and not the company or the industry, is the right unit of analysis for explaining the creation of blue oceans and the root of profitable growth. “By strategic move we mean, the set of managerial actions and decisions involved in making a major market-creating business offering. The strategic moves we discuss – moves that have delivered products and services that opened and captured new market space, with a significant leap in demand – contain great stories of profitable growth. We built our study around these strategic moves (over 150 from over 30 industries spanning from 1880 to 2000) to understand the pattern by which blue oceans are created and captured and high performance is achieved.”

Consider auto-industry from 1900 to 1940 is instructive. Ford’s Model T, launched in 1908, triggered the industry’s growth and profitability, replacing the horse drawn carriage with the car for American households. It lifted Ford’s market share from 9 to 60 per cent. The Model T, then, was the strategic move that ignited the automotive industry. But in 1924, it was overtaken by another move, this →

→ time by GM. "Contrary to Ford's functional one-colour one-car single model strategy, GM created the new market space of emotional stylised cars with 'a car for every purpose and purse'," explain Kim and Mauborgne. "Not only was the auto industry's growth and profitability again catapulted to new heights, but GM's market share jumped from 20 to 50 per cent while Ford's fell from 60 to 20 per cent."

Then in the 1970s, Japanese car companies created the blue ocean of small, gas efficient autos. In the 1980s, Chrysler created the blue ocean of minivans. All these companies were incumbents. Moreover, the blue oceans made by incumbents were usually within their core businesses. In fact, most blue oceans are created from within, not beyond, red oceans of existing industries. This challenges the view that new markets are in distant waters. Blue oceans are right next to you in every industry. Issues of perceived cannibalisation or creative destruction for established companies also proved to be exaggerated. Blue oceans created profitable growth for every company launching them, start-ups and incumbents alike.

Over the research period, they found a similar pattern in other sectors. In short, the strategic move that matters most to both an industry's long run profitable growth and that of individual companies is the repeated creation over time of new market space that embraces the mass market. Kim and Mauborgne call this "value innovation". Without it, whole industries fade into the sunset and are replaced by those which are more innovative. Without it, companies become irrelevant or are overtaken – as Ford was overtaken by GM in the 1920s.

"Value innovation occurs across industries, across countries, across companies," they say. "It is a universal force. A company, therefore, substantially limits its strategic opportunities and profitable growth potential by narrowly confining its analysis to its own industry. Yet, in most strategy literature, industry boundaries are regarded as central – think of SWOT analysis or Michael Porter's Five Forces."

Rather than viewing strategy as enacted in a landscape of dominant companies or industries, in *Blue Ocean Strategy* Kim and Mauborgne paint a persuasive picture of a commercial world in constant flux, where whole industries rise and then often disappear into oblivion. "Look back to the major industries of 1970 and very few, if any, are now significant," they note. "The big growth industries in the past 30 years have been the computer industry, software, gas-fired electricity plants, mobile phones, and the café bar concept. But in 1970 not one of those industries existed in a meaningful way, and that's just 30 years back. The pattern continues as you dig into the past. The big industries of 1940 aren't those of 1910 and so on. We have a hugely under-estimated capacity to create new industries."

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This, then, is their key message. The number of industries is ever expanding – and the pace is accelerating. The implications for companies are profound. "What we see is that over a 30 year cycle the focus of commerce, where the money is made, shifts 100 per cent," say Kim and Mauborgne. "Some industries die, some persist. But new industries are constantly being created. It is like a galaxy of stars – infinite." Transpose that onto the future, and the obvious conclusion is that the biggest industries today are unlikely to be the biggest industries 30 years hence.

Different not disruptive

Often, of course, the emergence of new industries coincides with the arrival of new technology. So how does the notion of blue ocean strategy differ from the "disruptive technology/innovation" proposed by Clayton Christenson?

Professors Kim and Mauborgne have a ready answer. Disruptive technologies/innovation, they say, is about seizing those customers who are overserved by incumbents in the existing industry. It focuses on disrupting from the low-end to capture down market customers. In contrast, blue ocean strategy is about making incumbents irrelevant by creating uncontested new market space not only within but also beyond existing industry boundaries. When blue ocean strategy speaks of creating uncontested new market space within, however, it does not focus on the low-end like disruptive innovation.

It focuses equally on creating blue oceans at the high-end as in the case of Dyson in vacuum cleaners, Starbucks in coffee, or Polo Ralph Lauren in fashion, at the low-end as is in the case of Curves in fitness or Formule 1 in hotels, or anywhere in between as in the case of Borders and Barnes & Noble in book retailing, or Pret A Manager in take-out food. Hence, when blue ocean strategy speaks of "within" it embraces the whole range of entry points of demand creation. Furthermore, blue ocean strategy differs from disruptive innovation in that it also reaches beyond existing industry boundaries by opening entirely new industry space as in the case of Cirque du Soleil or eBay.

They also have a counter to the charge that blue ocean strategy is inherently more risky. Far from it, they say, blue ocean strategy is about risk minimisation and not about risk taking. Of course, there is no such thing as a riskless strategy. Any strategy, whether red or blue, will always involve risk. Nonetheless, when it comes to venturing beyond the red ocean to create and capture blue oceans there are six key risks companies face: search risk, planning risk, scope risk, business model risk, organisational risk, and management risk. The first four risks revolve around strategy formulation, and the latter two around strategy execution.

Each of the six principles in *Blue Ocean Strategy* expressly addresses how to mitigate each of these risks. The first blue ocean principle – reconstruct market boundaries – addresses the search risk of how to successfully identify, out of the haystack of possibilities that exist, commercially compelling blue ocean opportunities. The second principle – focus on the big picture, not the numbers – tackles how to mitigate the planning risk of investing lots of effort and lots of time but delivering only tactical red ocean moves. The third principle – reach beyond existing demand – addresses the scope risk of aggregating the greatest demand for a new offering.

The fourth principle – get the strategic sequence right – addresses how to build a robust business model to ensure that you make a healthy profit on your blue ocean idea, thereby mitigating business model risk. The fifth principle – overcome key organisational hurdles – tackles how to knock over organisational hurdles in executing a blue ocean strategy addressing organisational risk. The sixth principle – build execution into strategy – tackles how to motivate people to execute blue ocean strategy to the best of their abilities, overcoming management risk.

Winning battles, losing wars

It sounds compelling. So, why isn't every company pursuing a blue ocean strategy? The problem, say Kim and Mauborgne, is that the basis of strategic thinking – and the consulting industry it has spawned – is based on coming up with strategies based on what you can see now. Business strategy is historically intertwined with military notions of strategy. Carl von Clausewitz, a Prussian general, and Sun-Tzu, an ancient Chinese theorist, are still cited as inspirations by the world's managers. This notion of strategy, say Kim and Mauborgne encourages managers to see strategy as a series of battles to be conducted on a neatly defined battlefield. The victor gains ownership of more of the battlefield.

"The war analogy we have used for strategy so far is the wrong one. It is based on an assumption that there's only so much territory that exists," they observe. "So it's been about dividing up that territory. There's been a winner and a loser. But our research shows it's not a zero sum game. You can create new land. Business history shows us that contrary to perceived wisdom, the number of market spaces that can be created is infinite."

Blue ocean strategy, Kim and Mauborgne argue, offers a more reliable route to value creation. This changes the fundamental operating principles of strategy. Consider The Body Shop. In the 1980s, The Body Shop was highly successful. Rather than compete head on with large cosmetics companies, it invented a whole new market for natural beauty products. More recently Body Shop has struggled. But, say Kim and Mauborgne, that does not diminish the brilliance of its original strategic move.

The problem was that The Body Shop didn't realise what made it a brilliant strategic move. Its genius lay in creating a new market space in what was seen as a commodity industry. Once it had carved out its own market, the company focused on mining that new market space. That was effective while few players imitated it. But, as more and more competitors moved into its market space, the company became involved in a bruising battle for market share. This was the wrong strategy.

"Once you have your own market space and imitators follow, you go into classical competitive strategy mode where you focus on milking it, getting your best market share, blocking other imitations and dramatically ramping up and refining your offering", explain Kim and Mauborgne. "But, as other companies' strategies converge on your market, history shows you need to create new market space again and break away."

In their model, strategic success depends on understanding the context and using the right moves at the right time. Strategy becomes a game of tag or leapfrog, rather than a brawl. Crucially, Kim and Mauborgne reject the idea that a company's strategic options are determined by traditional industry lifecycle.

The strategic lesson is clear: "When you take an industry deterministic view of your company you become a victim of that industry. The moment you sit back and say how can we create a new industry then you start to break that cycle. All industries are created not by big resources but by big ideas."

Big ideas also change the way we think about business. ■

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Blue Ocean Strategy: *How to Create Uncontested Market Space and Make the Competition Irrelevant*, by **W. Chan Kim** and **Renée Mauborgne** is published by Harvard Business School Press.