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Corporate Strategy in a "VUCA" World

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In a VUCA world, one that is volatile, uncertain, complex, and ambiguous – as many would characterise today's global environment – strategy matters more than ever. That is because strategy is an integrated set of coherent choices about an organisation's goals.

Strategy aligns and reinforces corporate goals. It defines where the board and management decide to "play" and how they would play to win. Finally, it focuses on what management systems and resources are needed to achieve corporate goals.

The challenges companies face in a VUCA world demand a filter to separate opportunities from distractions, and strategy helps management make good decisions about what to do. Just

as importantly, good strategy directs management about what not to do.

Resource allocation, investment positions, performance expectations, and the design of organisational structures – all these are underpinned by a set of assumptions about the organisation's industry, competitors, customers, and other factors. The key to good strategy is agility and flexibility around these factors.

The volatility of the current business environment calls for a periodic review of working assumptions. When they change – and they do constantly and rapidly – organisations need to recheck the choices they made based on those assumptions, and adapt them if necessary.

How often strategy should be reviewed depends on the "clock speed" of the industry. The clock speed of the technology sector, for example, is much faster than that of many other industries.

CLARIFYING THE ROLE OF BOARD AND MANAGEMENT

It is a constant debate among governance experts on exactly where the board's role and management's role in strategy begin and end. Quite apart from drawing the line between the roles of the board and management, it is more important that the roles are complementary and each has a clear understanding as to the balance that should be struck.

In general, management is responsible for setting, refining, and executing strategy while the board provides oversight and guidance for the direction of the strategy, and weighs its inherent risks.

Part of the board's responsibility is to clearly set appropriate expectations for management's strategy. The board should not set the bar too low – by not demanding a strategy and simply allowing

management to develop ad hoc initiatives without the context of overall strategic goals. Nor should the board set it too high – with unrealistic expectations for the organisation based on its starting point and resources.

In a productive relationship, the board asks purposeful questions that legitimately probe and advance the right strategy, and it does so without grandstanding or attempting to "one-up" management.

DEFINING THE RISK APPETITE

The board is the organisation's chief risk steward. As such, it is responsible for defining the entity's risk appetite, and how risks are managed and mitigated. The organisation's strategy must therefore be viewed within the context of the risks the organisation bears together with its stakeholders.

A 2014 risk management study by Deloitte showed that 38 per cent of the top 1,000 global public companies suffered share-price declines of more than 20 per cent relative to the MSCI Global 1000 index over the last 10 years. The study found that many of these "value-killer losses" were caused by low-probability, low-frequency, and high-impact events.

This suggests the need for companies to consider scenarios of low-frequency events that could create "tail risks" when setting strategies. While risks cannot be eliminated, companies can better prepare for them. Scenarios and models can be built to explore how companies will fare and how to deal with value-killer events.

Boards should encourage management to stress-test their capacity to respond to different scenarios where a bundle of events, correlated or uncorrelated, occur concurrently. While the past is not necessarily a prelude to the future, a well-governed enterprise can build on the knowledge of prior value-killer risks to help model its strategy in

a way that allows the company to better manage and respond to existing and future value-killer risks.

In reviewing its strategic portfolio, the company therefore needs to weigh the risks associated with them under the different scenarios that change these portfolios. The board and management need to weigh, for example, when and how the company should get out of one business or venture into another, and the impact such moves may have on the organisation's basket of risks.

In a VUCA world, directors and management tend to underestimate the risk of keeping the status quo – namely, staying with the current direction and makeup of the organisation. Curiously, they also tend to overestimate the risk of doing something different. Just because the risks associated with the current business activities are known, it does not mean they are any less than the risks associated with doing something different.

Volatility, uncertainty, complexity and ambiguity – these corporate realities are current and pervasive. The challenge of setting strategy is greater than it has been before. But the risks of not establishing a strategy are also greater, not forgetting that risk appetite is a crucial part of strategy. ■