Quick takes

Larry Goodson

These brief summaries highlight the key points and action steps in the feature articles in this issue of Strategy & Leadership*. Larry Goodson, an* S&L *contributing editor, is a veteran strategy consultant based in St. Louis, Missouri. He is a Partner at LDGA Consulting, which offers Lean operations and strategy development services (ldgoodson@msn.com).*

The Imagination Premium: An anticipative performance metric

Rita McGrath, Alex van Putten and Ron Pierantozzi

Most backward looking corporate performance metrics leave a lot to be desired as measures to drive long-term, forward looking decision-making by corporate strategists and CEO's. Adding to the problem is that companies incentivize corporate leaders on the basis of backward looking measures, for instance, on stock price during a given period. Ideally, performance metrics should encourage managers to invest for the long-term even as they experience short-term performance pressures.

As a more forward-looking measure for evaluating companies' prospects and executive success we propose The Imagination Premium.™

The Imagination Premium (TIP) assessing the value of potential growth

The Imagination Premium is a fitting name for the metric because it reflects the intention of leaders to move their companies forward into new business models, markets, technologies and ways of working, either through incremental growth or acquisition.

The value of a company's equity can be thought of as comprising two parts that determine The Imagination Premium.

- The first represents the value a reasonable investor might estimate based on the ongoing streams of profits it generates from operations. This is the Value of its Current Operations [Vo].
- Investors, however, are future oriented. If they believe that a company will enjoy healthy future growth, there is a premium they are willing to pay for the equity of a company that will permit them to participate in that growth. This is the Value of Growth [Vg], or the additional value an investor will attribute to the equity beyond what is reflected in simple cash flow generation from the current business.

The Imagination Premium reflects the ratio between the two – dividing the value of operations by the value of growth. The two components of TIP, the Value of Operations [Vo] and the Value of Growth, [Vg] can be thought of as the steak and the sizzle of a company's offering.

Implications for leaders

The Imagination Premium provides a leading indicator of changing investor sentiment, with potential implications for how executives manage their growth portfolios.

Taking action to boost TIP

One of the first things strategists can do to manage their company's TIP is undertake a portfolio analysis that looks at how uncertain each current investment is, and whether the whole portfolio is one that growth investors will reward with an increased TIP.

A sure strategy for failure is to systemically under-invest in important extensions to the core that can show growth in a 24-36 month time-frame. TIP can provide C-suite executives, boards and their investors with a useful perspective on developing their strategies for the future. Incorporating TIP into a strategic analysis, and monitoring any sudden changes, also provides an early warning in case investors begin to believe a growth strategy is competitively problematic.

Interview
Hubert Joly: The new capitalism formula purpose first, people at the center, then profits

Brian Leavy

Hubert Joly has been widely acclaimed for his leadership of the Best Buy turnaround and transformation over his tenure as CEO from 2012 to 2019. The principles and framework that he developed, and that guided his leadership at Best Buy, are featured in his new book *The Heart of Business: Leadership Principles for the Next Era of Capitalism*.

Strategy & Leadership: You note that *The Heart of Business* is neither a memoir nor a play-by-play account of the turnaround and transformation of Best Buy. What then was your main aim in writing it?

Hubert Joly: This book is the articulation of key leadership principles for the next era of capitalism, and how to put them into practice in both the best and hardest of times. Through all my experiences, I have come to believe—to know—that purpose and human connections constitute the very heart of business.

S&L: In *The Heart of Business* you develop a model called "the purposeful human organization" based around the guiding principle of purpose and people before profit. How does this work in practice?

Joly: That approach is based on a seismic shift from profit to purpose. Business is fundamentally about purpose, people and human relationships—not profit, at least not primarily.

S&L: You say that developing a "noble purpose" for Best Buy to replace the primacy of profit "fundamentally changed our strategy and how we did business." How and why did it make such a difference?

Joly: The resurgence of Best Buy is based on embracing and implementing the principles of putting purpose and people first. In Best Buy's case, enriching people's lives by addressing their key human needs through technology promotes many more activities than just selling consumer electronics. Such a noble purpose also ensures that economic activity is sustainable. In the end, the purposeful human organization approach produces great bottom-line results.

Purpose before profit: unleashing individual and collective "human magic"

Hubert Joly

Over the course of my career, I have learned that so much of what I had been taught about business at business school and as a consultant and young executive is either wrong, outdated or incomplete. I learned that the old top-down approach to management—having a few smart executives first formulate a strategy and its implementation plan, then tell everybody else in the company what to do while crafting incentives to motivate them—rarely works.

While many of these ideas were already fermenting when I was invited to take on the leadership of Best Buy in 2012, I learned an enormous amount from my colleagues there.

The limitations and dangers of financial incentives

I have since come to believe that in today's economy, financial incentives at all levels are no longer the primary driver and motivator of performance, if indeed they ever were.

So if financial incentives do not motivate people to go the extra mile, then what does? In my experience, it starts with one fundamental change in perspective: to view people as a "source" rather than a resource.

Five drivers of exceptional motivation

Best Buy and its people have taught me much about the practical implications of this shift in perspective. I now believe that the recipe for creating such an environment is made of up of five key ingredients:

1. Connecting dreams.
2. Developing human connections.
3. Fostering autonomy.
4. Achieving mastery.
5. Putting the wind at your back.

This environment fosters individual growth and drive, which in turn feeds back into innovation and further business expansion.

Putting purpose and human connections first

Through all my experiences, culminating in the years at Best Buy, I have come to believe—to know—that purpose and human connections constitute the very heart of business.

I believe that business is fundamentally about purpose, people and human relationships—not profit, at least not primarily.

By creating an environment where everyone at the company is energized in support of a unifying sense of purpose and can see their role in its fulfillment, the five ingredients – connecting dreams, developing human connections, fostering autonomy, achieving mastery and putting the wind at your back – will drive engagement.

This is the human dimension that can power corporations as purposeful human organizations. It is also an essential element for the kind of reinvention of business, and reinvigoration of the economic system, around a model of stakeholder capitalism that is so urgently needed today.

Effective storytelling: leadership's magic methodology

Stephen Denning

In these days of disruptive change and difficult to imagine futures, the leadership challenge of inspiring people to adapt and undertake innovation is central. To achieve success, leaders need an understanding of the dynamics of persuasion and the craft of leadership storytelling.

Inspiring people to change through leadership storytelling

Storytelling is of course one of the age-old traditions of the human race. The great leaders throughout history who have won hearts and changed minds often resorted to storytelling.

While storytelling is recognized as a critical success factor in politics, its importance in organizational change is often overlooked.

The mechanics of changing minds through storytelling

The first thing to learn about leadership storytelling is that most stories don't spark an intent to act differently. Research has shown that the stories that do change minds and inspire different behavior tend to have a particular narrative pattern. The key to leadership storytelling is to understand and master this narrative pattern.

The key elements of successful leadership storytelling to inspire change are:

- The story is about an individual with whom the listener can identify.
- The story is about the situation or problem that the communicator seeks to resolve by inspiring the listener to take different action.
- The story is about someone who solved the problem.
- The story is about something that actually happened and so it is credible.
- The leadership story is told very briefly in a minimalist form, so the listener can think, "What if I were to. . ..?" As a result, the story thus imagined is perfectly adapted to the listener's own setting.
- The story, in the space of only a few words, contrasts the situation before the change idea and the situation after the change idea is implemented.
- The story is told with conviction; it is the leader's intensity that is doing much of the work of persuasion.

Today the ongoing reinvention of management to transform workplaces from the boring, sterile, dispiriting cubicles of the 20th century into the lively centers of inspiration and creativity that are needed for the creative economy of the 21st century necessitates the elevation of change-agent storytelling to the central place in leadership that it deserves. Storytelling is more than just a tool. It is a requirement of being a leader. It enables leaders to surmount a humdrum world and get to that realm where profound meaning is revealed.

Open innovation: digital technology creates new opportunities

Anthony Marshall, Jacob Dencik and Raj Rohit Singh

Open innovation, after many years of limited success in large companies, is now driving greater business results than any other type of innovation.

A recent survey conducted by the IBM Institute for Business Value (IBV) indicates that as many as 83 percent of companies see open innovation as important to their future growth strategy. Organizations need to transform their operating model from supporting linear innovation processes to orchestrating complex innovation dynamics within their own organization and across ecosystems.

How digital technology drives open innovation

When data sits within silos or departments of individual units and remains inaccessible for use by others, collaboration and co-creation in both innovation and discovery processes becomes more difficult.

- Cloud. The emergence of cloud – and hybrid-cloud in particular – helps address this integration and collaboration challenge. It allows companies to connect – vastly improving the processes of integrating, moving, sharing and accessing data.
- Artificial intelligence. AI infuses the innovation ecosystem with intelligence, revealing or exploring new insights and accelerating the process of discovery by augmenting and expanding capabilities of all ecosystem participants.
- Advanced Analytics and Internet of Things. Complementary technologies, such as Advanced Analytics and Internet of Things (IoT), improve the possibilities for capturing and making sense of vast quantities of data, which in turn support new innovations and solutions.

- **Blockchain**. Blockchain is to ecosystem workflows what Enterprise Resource Planning software is to internal enterprise processes. It provides the security, transparency, trust and efficiency necessary for interactions and transactions between actors in an ecosystem and functions as a shared system of record for and between all participants.

A transformational way of doing business

Open innovation is not just another way of doing innovation. It constitutes a completely new operating model for organizations. The model harnesses the collective intelligence of employees, partners, vendors and customers in the pursuit of innovation and value.

IBV research indicates that in just the last two years, companies have more than doubled their active creation of and participation in platforms for engaging partners and customers.

Shaping the open innovation journey

The requirements are different, the levers organizations have are different and the value capture requirements are different as well. A brief action guide will help firms advance open innovation strategies:

- Create clarity on strategy and objectives.
- Scale ideation and experimentation.
- Use platforms for innovation dynamics.
- Create a hybrid-cloud technology foundation for open innovation.
- Harness the collective intelligence of ecosystems and augment it with AI.
- Adapt incentive mechanisms, metrics for success and the balance of risk and reward.

What corporate executives can learn from leading value investors

Joseph Calandro Jr and Paul A. Sherratt

Despite differences of opinion regarding what to include as a "top risk" today, many executives agree that 2021 and beyond will likely be a period of uncommonly broad-based risks. The principles of value investing – based on risk management lessons learned from highly successful practitioners – present an approach to corporate strategy and management that is especially relevant in an era of market turbulence.

Research into their successful practices and behaviors can be distilled into six core managerial considerations:

- **Adding cost-effective resource allocation to the strategy tool kit**

The first consideration is one that is generally absent from many definitions of corporate strategy: cost-effective resource allocation.

- **Conservative financing**

A strong balance sheet, defined by little-to-no debt, is a critical enabler of cost-effective resource allocation over time. Having ample cash holdings, along with little-to-no debt, enables cost-effective resource allocation over time.

- **Balancing non-traditional and traditional information**

Strategically approaching global risk often requires investors and executives to act against conventional wisdom and take pains to avoid confirmation bias. The term "confirmation bias" holds that, "people . . .seek data that are likely to be compatible with the beliefs they currently hold."

- **Clarity about the complexity of risk**

Corporate executives are facing an ever broader and increasingly complex array of risks. As a guide to this ongoing struggle, some professional value investors augment formal valuation analyses with behavioral-based insights.

- **Humility in times of uncertainty**

Humility is rarely stated as one of the preferred or most valuable attributes to look for in a CEO, yet the opposite has been identified as an impediment to an executive's effectiveness and success, especially in times of high risk.

- **Focusing on compounded returns**

The "bottom line" of our managerial considerations is the "compounded return," which is a measure of the constant rate of return that is earned over a period of time, rather than a simple annual return measure or stock price. The focus on compounded, rather than short-term, returns is also something observed in successful investors and executives.

Adopting the mindset and practices of a value investor

By extending the traditional definition of corporate strategy to include cost-effective resource allocation and employing the principles and behaviors of leading value investors, corporate executives can be better prepared to meet the ever-expanding array of risks head on, and exploit the advantages that a strong balance sheet provides.

In theory, the prescriptions of value investing appear straightforward, but in practice it takes an active shift in mindset to achieve over time. Executives need to augment their operational skillsets with those of both an astute investor and discerning banker, balance their attention between conventional and non-traditional sources of information, and exhibit the patience and grit to go against the herd and focus on longer-term compounded returns.