





Where Have All the 10-Year Strategies Gone?

Short-term thinking has become the strategy of choice for many executives as they fixate on today's breakneck speed of change. While short-term strategies can deliver an immediate impact, in the race to stay on top in uncertain times, the undisputed champions are those who take the long view.

IN 1996 TWO-TIME CHAMPION MICHAEL SCHUMACHER, one of the best Formula 1 drivers in the world, signed with Ferrari, a team considered a joke by most in the racing industry. Ferrari, having not won a championship in 17 years, was in chaos. But signing Schumacher was part of a long-term strategy by Ferrari CEO Luca Cordero di Montezemolo to restructure every aspect of the company—from car design to engineering and reliability to sponsorship and staff.

In the short term, it didn't work out very well. After Schumacher's engine blew up at the 1996 French Grand Prix, wasting his \$1 million-per-race salary, team principal Jean Todt offered his resignation. But Montezemolo was not swayed by such short-term setbacks, even as they continued over the next four years. Within nine years, Schumacher had won more races and

championships than any driver in history, making Ferrari the world's undisputed Formula 1 leader.

How many business strategists follow Ferrari's lead, developing and sticking to long-term strategies? Lately, not very many. Obsessed with the ever-increasing pace of change and its impact on soaring rates of "hypercompetition," many executives we've talked to believe it pointless to invest in strategic thinking beyond one to three years; indeed, a five-year strategy is considered long term.

We have a problem with that.

The Paradox of Time

Recently, we researched the length of time organizations typically employ when formulating their strategies.¹ We found that about two-thirds of companies have a strategy horizon of four years or less. Another 30 percent have plans of five to six years, and only 6 percent of companies in our survey have a strategy that stretches beyond six years (see figure 1).

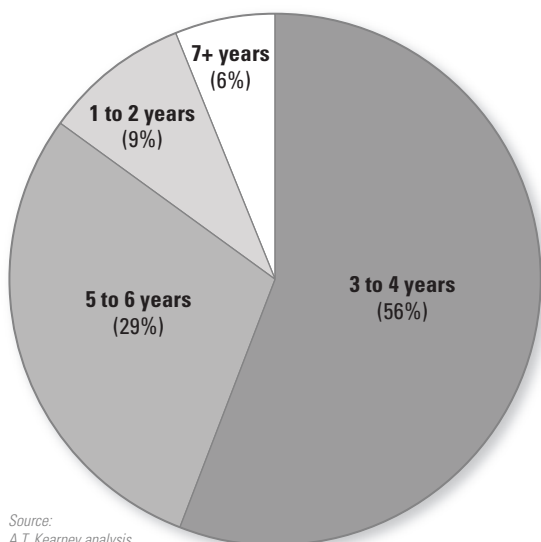
The result is hardly surprising: Most companies see longer-term strategies as too beset by uncertainty. Only short-term strategies can have a *real* impact on business. Yet this logic hides a paradox: Continually planning for the short term leads to "temporal myopia," in which industry changes that genuinely erode long-term competitive position are missed.

For example, for 15 years now, telecommunications companies have used "convergence" as a reason to eschew long-term thinking in favor of shorter-term strategies aimed at staving off erosion of fixed-line revenues—and many of those telcos have, in the long run, failed to transform their businesses to deal with convergence. Similarly (and over the same time frame), most bricks-and-mortar retailers have been aware of the emergent threat of online retail, but have

FIGURE 1

Two-thirds of companies have a strategy horizon of four years or less

Companies by strategy horizon (%)



Source:
A.T. Kearney analysis

¹ The authors sought evidence of considered thinking based on a stated time frame, but not necessarily any strict formal planning such as detailed P&Ls and balance sheet projections.

seen this threat as far off in the future and instead have focused on shorter-term strategies involving store locations, operations and merchandising. As a result, they realized an immediate impact but failed to position their companies to deal with online alternatives—the now-bankrupt Borders is the most obvious example.

*We fear change and hyper-competition **only because of hindsight bias**—our ability to see the past as inherently more logical and predictable than the future.*

A big part of the problem is the separation of the terms short and long in the planning process. As soon as you make this distinction, long-term trends recede permanently into the distance. As soon as you start thinking about multiple, discrete horizons, you start marching down a path where you run the risk that those horizons will never converge. But tomorrow's long-term trend will eventually become today's short-term reality.

Common Reasons for Short-Term Thinking

Why the obsession with short term? There are many reasons, some of them well known. They include:

Incentives. Mounting empirical evidence demonstrates that when executives are given short-term incentives, such as stock options,

they focus on short-term objectives (and, consequently, on improving short-term performance). The opposite is also true: Long-term incentives drive long-term performance improvements.

CEO contracts and tenures. As has been widely reported, the average tenure of a CEO is declining. What is less well known is that firms with shorter CEO contracts tend to have shorter-term objectives that may lead to value-destroying behavior, such as under-investing in future capabilities. One recent study suggests that if your investment strategy chooses firms with longer CEO contracts and sells those with shorter contracts, your yield will go up about 10 percent per year.² For example, in his later years as CEO of Marks & Spencer, Richard Greenbury set an ambitious \$1.6 billion (GBP£1B) short-term profit target for the retailer. In pursuit of the goal, however, he underinvested in existing

stores, IT and training, which contributed to the company's later poor performance and his ultimate downfall.

Market expectations. Analysts and fund managers base stock assessments on quarterly earnings, rather than long-term growth. CEOs point to this market behavior to rationalize their own obsessions with earnings. This vicious circle threatens efforts to build long-term capabilities that drive long-term growth. This is also why private equity firms are often considered better owners of assets than public companies—they can patiently, quietly turn them around outside of the market's gaze.

Commitment to flexibility. The lack of flexibility inherent in long-term strategic commitments is thought to hamper risk management (though it embodies a misunderstanding, discussed later). So firms with little appetite for

² Xu, M., *CEO Employment Contract Horizon And Myopic Behaviour*, Unpublished Working Paper, INSEAD, Fontainebleau Cedex, France, June 2009

risk prefer to commit to the flexibility of blowing in the wind.

The curse of more information. Which pieces of information have a real impact on your business? Answering that question conservatively, by assuming that all of the increasingly available information is relevant, can lead to mistaking tactical decision making for strategic decision making.

The rise of the “emergent strategy” paradigm. Two increasingly influential approaches to strategy have been “learning by doing” and “setting strategy from the front line.” Both are sometimes an excuse for refusing to think in the longer term about strategy.

All of these factors contribute to a fixation on the short term. However, there is an even more important contributor—and it’s not altogether valid.

The Deeper Problem: Misperceptions of Change

At a deeper level, our short-term obsession reflects a fundamental human dynamic. As Bill Gates said, “We always overestimate the change that will occur in the next two years and underestimate the change that will occur in the next 10.” First, we tend to mistake “noise” for significant shifts. For example, recent research suggests that the impact of competition has not changed much in 20 years, and the impact of hypercompetition may have been overstated.³ Further, we tend to “misperceive” the dynamics of the rare, genuinely significant shifts. A small number of industries (estimated to be about 20 percent) are indeed undergoing hypercompetitive, radical, rapid change. But it usually takes 10 years or more to unfold.⁴

³ McNamara, Vaaler and Devers, “Same as it Ever Was: The Search for Evidence of Increasing Hypercompetition,” *Strategic Management Journal* 24: 261–278 (2003)

⁴ Anita McGahan, *How Industries Evolve: Principles for Achieving and Sustaining Superior Performance* (Harvard Business Press, 2004)

⁵ Our research was based on a small but representative sample across eight industries; however, we believe the results are a good indication of a wider trend. For that reason, A.T. Kearney is now launching a broader survey on the relationship between planning cycles and TSR.

We fear change and hypercompetition only because of hindsight bias—our ability to see the past as inherently more logical and predictable than the future. We look backward and forget how frightened and paralyzed we were by what turned out to be meaningless blips; then we look forward and perceive every blip as a game-changer. Yet not everything that fills daily news headlines (or the daily diaries of CXOs) is truly strategic.

Other disciplines seek to overcome these temptations toward thinking only in the short term. For example, the conventional wisdom in financial investing is: “It’s time *in* the market, not the timing *of* the market.” Can you imagine a financial advisor saying that given long-term uncertainty, you should optimize your finances only for the short term and adjust your portfolio at every sign of volatility? Likewise, experts in government policy always urge a longer-term horizon to manage the vagaries of economic cycles, complex budgets and large-scale infrastructure projects. Shouldn’t business strategists do the same?

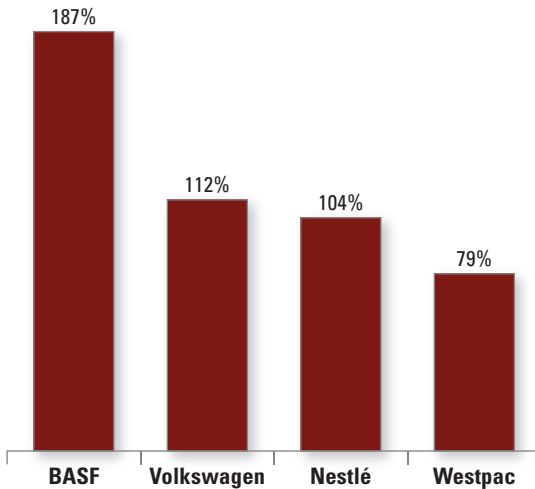
The Rewards of Long-Term Thinking

Not all companies are stuck in a short-term cycle. In fact, leading corporations in a variety of industries and countries do think strategically over the very long term. They typically set their strategy horizons at up to 10 years or more, so they can build capabilities and advantage. And this perspective pays off: Companies such as Nestlé, BASF, Volkswagen and Westpac have considerably higher total shareholder returns (TSR) than their peers (*see figure 2*). In fact, our research found that the longer the

FIGURE 2

Companies with a 10-year or longer strategy horizon outperform industry peers

Cumulative 10-year TSR above peers¹

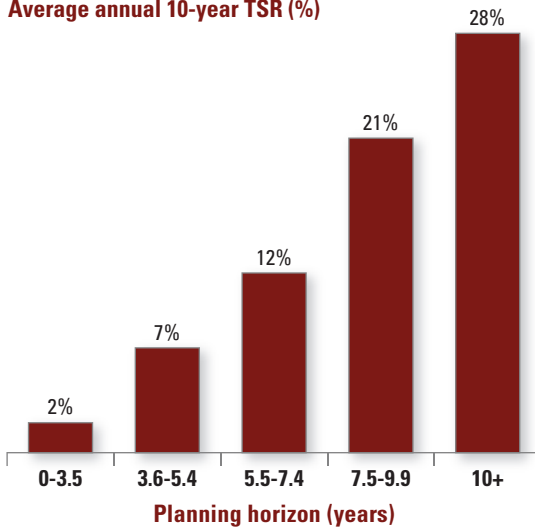


Note: Total shareholder returns (TSR) from 1 January 2000 to 31 December 2010; absolute TSR difference to equally weighted peer portfolio (peers based on Bloomberg)
Source: A.T. Kearney analysis

FIGURE 3

A longer strategic planning time frame generates higher total shareholder returns

Average annual 10-year TSR (%)



Note: TSR is total shareholder returns; companies were selected based on availability of 10-year TSR, from 1 January 2000 to 31 December 2010.
Source: A.T. Kearney analysis

strategic horizon, the higher the long-term TSR (see figure 3).⁵

Obviously many factors drive performance, and we don't claim a direct causal link between longer-term planning and superior performance in and of itself. Rather, thinking longer term creates an environment that can help shape these other performance-enhancing factors. And these companies have all the attributes necessary to drive superior performance (see sidebar: *Long-Term Thinking Pays Off for BASF, Nestlé, Volkswagen and Westpac on page 23*).

Following are some of the factors:

Building strategic capabilities. With a forward-looking view, a company can take the time to invest in genuine transformation to build profound new strategic capabilities, allowing the strategy to match the life of the asset.

Aligning tactics. Having a long-term horizon doesn't mean that you ignore short-term strategies. Rather, a long-term strategy *informs* the short term, providing a framework for mergers and acquisitions, guidance for R&D investments, and a context for organizational changes.

Creating real differentiation. Longer horizons further the development of truly distinct positions in the market rather than spiraling into incremental tactics and competitor tit-for-tat that are characteristic of shorter horizons.

Shaping industries. Business cycles are generally believed to play out over a course of seven to 11 years. Thus a longer-term perspective helps an organization think not only about its position within the industry, but also about how it will take advantage of longer-term industry changes to shape the industry.

Managing risk and uncertainty. The way to deal with the uncertainty of the immediate future is to look far into the distance. Managing uncertainty requires understanding when and how those large, long-term trends will finally collide with today's short-term business realities.

Creating shared value. The mantra today is *big tent* as we look beyond profits to create shared value for our firms, our value-chain partners, the broader community and the environment. This perspective often requires time to deploy, so it's not surprising that the leaders in shared value creation, such as Nestlé, are committed to formulating longer-term strategies.

Essentially, even as we plan for the immediate impact of today's short-term challenges, we cannot ignore the large and growing advantages that come with forward-thinking strategies.

Lifting Your Gaze: Setting a Long-Term Strategy

So how does an organization, starting into the short term, lift its gaze to establish a longer-term strategy horizon? We suggest the following steps:

Overcome cultural resistance. In our research for this article, many strategists at companies with extended horizons cited cultural resistance among the biggest issues they face. To overcome such resistance requires first understanding management's current strategic biases, then resetting key performance indicators and incentives and adjusting reporting to reflect the new emphasis on long-term objectives. You must also ensure that the organization's values—including the way it formulates and assesses business cases—are aligned to lasting objectives.

Reset the long-term vision and objectives. Next, start *really* thinking about the *long* term. This does not mean projecting profit-and-loss statements out 10 years; it means understanding the desired future position and

taking an outside-in view of industry changes. The vision and objectives are not necessarily about specific market positions, but rather the general capabilities that must be built and exploited across undefined markets. For example, Google (another practitioner of long horizons) could not have predicted 10 years ago which of its applications would be most popular today. But it had a well-defined vision and objectives regarding its extraordinary capability in data analytics.

*A long-term strategy informs the short term, **providing a framework for mergers and acquisitions, guidance for R&D investments, and a context for organizational changes.***

Identify required long-term capabilities. An organization must be good at something in order to go the distance. Capabilities typically take considerable time to build, especially if barriers to entry are to be erected. Thus you need to have a clear view of the general capabilities to be built and exploited over time. And even in a world that rewards "dynamic capabilities," this does not mean they will be built overnight.

Combine short- and long-term perspectives. In our experience, the best approach is to think about strategy over time in a connected logical continuum. Your strategy extends from the future to the present. Conversely, it extends from the present to the future. Draw a line of

sight from the capabilities needed to meet your long-term objectives to those necessary in the short term. Then manage a portfolio of short- and long-term requirements simultaneously, with an understanding of how they relate to (and reinforce) each other.

Keep an eye on “mega trends.” A long-term perspective is not static, but will continually evolve as it is shaped by the macro or

“mega trends” that transform the future environment. To understand potential implications on the organization, the trends must be monitored continually.

Bring employees and shareholders along. Don't just think about a 10-year perspective—talk about it. The more you can share your ambitions, the more employees and shareholders can become invested in helping

Long-Term Thinking Pays Off for BASF, Nestlé, Volkswagen and Westpac

Fearing the uncertainty of the future in an era of rapid change, many companies fixate on the short term and end up paying the price. Four companies take a different view: All are committed to developing long-term strategies—and all achieve significantly higher total shareholder returns than their peers.

BASF, the global chemical company, depends on mega-trend assessments in setting its future strategies. For example, in 2009, when the company's trend analysis found that two-thirds of future growth in the chemical industry would come from Asia Pacific, it launched its “Asia Pacific Strategy 2020” as a core plank in its global growth strategy. The company had short- and long-term strategies. The short-term: Invest €2.3 billion over five years to increase sales to Asia Pacific by 2 percent on average per year. The long-term: Generate 70 percent or roughly €20 billion in global sales from Asia Pacific by 2020.

Nestlé, the Swiss consumer goods company, does strategic planning based on fundamental

trends that are expected to shape its industry over 10-plus years, taking into account aging consumers, low-income consumers and the increasing availability of information. All categories and regions must anchor their three- to five-year business plans in this strategic direction. For example, Nestlé's recent acquisitions in health-related businesses fulfill its strategy around aging consumers. The company has non-negotiable principles of financial performance and focuses on long-term operating models, competencies and human resources development—and it shares these “rules of the game” through all management levels.

Volkswagen, the German auto giant, unveiled its most recent 10-year strategy in 2009. Entitled “Strategy 2018,” it unequivocally aims to position the Volkswagen Group as a global economic and environmental leader among automobile manufacturers. The company has articulated a clear goal to be the “most successful and fascinating automaker in the world” through a variety of strategic objec-

tives, including becoming an innovation leader, maintaining its focus on the environment, becoming the employer of choice and improving customer satisfaction. Volkswagen is not afraid to think ahead—it has set a number of quantitative metrics 10 years out, including return on sales and unit sales targets.

Westpac, the Australian financial services leader, has made long-term strategy a priority after a series of events in the late 1980s and early 1990s brought it to the brink of insolvency. Since then the company has focused intently on the long term, with a strategy to achieve industry leadership underpinned by a prudent credit policy. The current strategy set in 2009 has a time horizon of about 10 years and involves forming deep, long-term customer relationships and making significant investments in building capabilities. The strategy is about long-term transformation. As CEO Gail Kelly told *The Australian* last year, “We are all about sustainability... It's not what analysts or others say in a quarter or a half.”

to achieve them (and analysts and shareholders can adjust earnings expectations). Not everyone will like the shift. Inevitably some changes will be required; the employees and stakeholders who remain will be better committed to the organization.

Be disciplined and stay the course.

Finally, thinking ahead and anticipating the future will require persistence and discipline in the face of short-term setbacks. For example, BASF persisted with its research into genetically modified organisms despite constant public and political opposition in Europe—a move that paid off when the EU recently approved Amflora, a genetically modified potato that produces biodegradable starch for packaging.

The Catch: Dealing With Uncertainty

Great, you may be saying, I've never denied the benefits of long-term thinking. But how can it account for short-term uncertainties? Rest assured, we understand that there are uncertainties. But we believe that organizations can best address them within the broader context of a long-term strategy; indeed, many tools and approaches have already been developed for this purpose. These fall into two broad categories—those that seek to *adapt* to industry changes, and those that actively seek to *shape* the industry in which the company plays.⁶ Some of the more relevant ones include the following:

How to adapt to industry changes:

- **Discovery-driven strategy.** Invest small amounts of money in select strategic projects to obtain the information necessary to learn and invest more confidently in the future.

- **Corporate venturing.** Develop and nurture new ideas in a sheltered environment away from the limelight, mimicking the conditions created for startups by venture capital firms.
- **Options-based approaches.** Identify and pursue multiple, sometimes contradictory, strategies simultaneously so as to take an “option” on the various possible outcomes. As the future becomes clear, some options are exercised while others are eliminated.

Don't just think about a 10-year perspective—talk about it. The more you can share your ambitions, the more others can become invested in helping to achieve them.

- **Wargaming and game theory tools.** When the future is contingent on the actions of competitors within a relatively narrow set of parameters, develop scenarios to understand the range of outcomes.
- **Scenario planning.** In an approach pioneered by Shell, formulate possible futures based on key defining uncertainties over the planning horizon. The resulting scenarios are assigned a probability and monitored to understand which is most likely to happen.
- **Analogies and pattern recognition.** Used in situations of true ambiguity, these tools can help establish a way to think about the problem by drawing on potentially similar or analogous problems in other contexts.

⁶ For a discussion of strategy tools for dealing with uncertainty, see the Executive Agenda article, “Playing on the New Strategy Chessboard” at www.atearney.com.

How to shape your industry:

- *Blue oceans.* Move beyond traditional competitive tactics to create entirely new uncontested market spaces or “blue oceans” in which competition is irrelevant.
- *Preferred futures.* Envision an ideal future and then work back from the present to build capabilities to make it happen.
- *Creativity and innovation.* Redefine an industry through game-changing insights, bold ideas and product innovation.

In short, many tools are available to deal with strategic uncertainty. Indeed, most of them are not only compatible with long-term strategic planning, but are also *required* for the organization to be thinking far into the future.

These Are the Terms for Future Success

The short term is important. As a yardstick, it measures near-term stock performance and execution capability. You should certainly keep your eyes on short-term performance, but only within the context of the long term. If you expect your organization to be around for longer than three to five years, and if you accept the wisdom that most business cycles last anywhere from seven to 10 years—and that even drastic change can take more than 10 years to transform an industry—then you’re already primed to create the optimum environment for tomorrow’s sustained success even as you adeptly address the issues of today. 🗣️

Consulting Authors

MAURICE VIOLANI is a principal in the strategic growth practice. Based in the Melbourne office, he can be reached at maurice.violani@atkearney.com.

CHARLES PERRARD is a principal in the operations practice. Based in the Paris office, he can be reached at charles.perrard@atkearney.com.

JOCHEN KAEMPFER is a consultant based in the Sydney office. He can be reached at jochen.kaempfer@atkearney.com.

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PUBLISHING ADVISOR
Wayne Boley

EDITOR
Patricia Sibo

DESIGN
Kevin Peschke

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