

# *The Role of Intelligence in Formulating Strategy*

Jan P. Herring

**S**uccessful business strategies are inherently dependent on the skills of the corporate strategist and the company management team's ability to implement the strategies. However, like the chef who is creating the epicurean meal, the strategist is also dependent on the ingredients that he has to work with—in essence, his strategy can be no better than the information from which it is derived. The more comprehensive and prescient that information, the more likely the strategy is to be successful.

Two basic categories of information are required for strategy formulation: (1) information and data about your own company's resources and capabilities and (2) relevant information about the company's total external environment, including customers, competitors, the industry structure, and various competitive forces that shape the markets in which your company competes. The completeness and accuracy of the two sets of information vary considerably.

Most companies possess the information about their own capabilities and resources with a reasonable degree of completeness. And many companies have relatively good information about their customers, depending on how much they choose to spend on market research. But only a few firms allocate sufficient resources to collect and analyze the information on the competition and those external forces and factors that affect their industry's competitiveness.

It is this latter set of information that is generally defined as competitive or business

intelligence. No matter how much you spend in gathering and developing this information, you will never be able to produce business intelligence with the same degree of precision, nor need you, as that about yourself. Nevertheless, the effectiveness of your strategies will be directly related to the comprehensiveness and timeliness of this business intelligence.

During the Desert Storm campaign, General Norman Schwarzkopf depended heavily on intelligence about the Iraqi military forces, the number and capabilities of their weapons, and their deployment to formulate his strategy and battle plan. Once he launched the campaign, he relied on real-time intelligence about the enemy's response to adjust the implementation of his plan. In addition, he had purposely created a different perception about his battle plan in the minds of the Iraqi military leaders by revealing to them (their intelligence units) what he wanted them to know. Thus, intelligence played a very important role in formulating the strategy, executing it, and enhancing its chances of successful implementation.

Few corporate strategists make such comprehensive use of competitor or business intelligence. Their intelligence inputs are often assumed or static, having been derived from outdated and incomplete public and secondary information sources. This situation may stem from the poor state of intelligence in US companies; however, I also believe that it is because most American bus-

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iness strategists do not appreciate nor fully understand the effect that competitors or the competitive environment will have on their strategy's success.

At its simplest, a strategy can be defined as the way(s) an organization plans to use its resources (i.e., capital, manpower, and technology) to achieve its goals and objectives. Most business strategies define what that company expects to achieve and only superficially factor in the competition and its plans and intentions. In fact, companies that have tried to factor in competitive intelligence more explicitly seldom have good business intelligence concerning the competitors' current and future intentions—much less complete intelligence about the competitors' current capabilities.

In addition, few of the companies that I have observed possess the type of intelligence organization necessary to gather and use the *real-time* intelligence necessary to both measure their competitors' responses and to make tactical adjustments based on that new intelligence. As a result, the implementation of their strategies is static, at best; if successful, it is because the competition either does not know or does not care whether the company is implementing a particular strategy.

This situation is particularly true among US companies. This form of "positioning" strategy begins to suffer severe repercussions when US companies use their static strategies to compete with companies that take competitive intelligence and competitive strategies more seriously. Japanese companies, in particular, find this behavior by US firms puzzling—but, nevertheless, take full advantage of their competitors' poor intelligence capabilities.

#### **THE ART OF COMPETITIVE STRATEGY FORMULATION**

Dr. Fumio Hasegawa, a Japanese planner and futurist for the Shimizu Corporation, describes the six basic strategies used by Japanese construction companies in his book, *Built by Japan*. He specifies them as transnational expansion, new business development, integrated engineering construction,

development projects, technology development, and financial management. However, it is the combinations in which these six strategies are used to produce integrated strategies that are of interest.

In describing how one composes such combined strategies, he cites the Chinese military strategist Sun-Tzu: "There may be only five different tones, but all their variation must be listened to . . . In military strategy, there are only orthodox and unorthodox strategies, but all of their variations must be studied." Dr. Hasegawa goes on to describe the Japanese development and application of such strategies. He states that competitive strategies may take either of two major directions: a head-on collision with a rival for greater share of the market or a move into a business where there is little or no competition. He specifies several principal strategy objectives such as gaining superiority, reducing potential retaliation, and avoiding competition, each of which requires a considerable amount of intelligence about current and potential competitors.

It is clear that without such intelligence, the formulation of these sophisticated strategies could not be accomplished. Although his description of the strategy formulation process is relatively simple, what it portends for US construction companies in regard to future competition is compelling—if they are listening.

Dr. Hasegawa's book, which was originally written in the mid-1980s and translated into English in 1988, was somewhat prophetic in identifying the coming nature of cooperation and competition among Japanese and foreign companies. In addressing the large construction markets in Japan, his identification of future potential competitors of Japanese construction companies was even more prescient. He identified large makers of electrical machinery, steel products, and ships as becoming increasingly active in the construction market. Some were already heavily involved as contractors, such as Mitsubishi Heavy Industries, Nippon Kokan, and Mitsui and Company, along with Ishikawajima-Harima Heavy Industries.

Somewhat surprisingly, he identified

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Toyota Motor Co., the automobile maker, as a new force in house building, and one with a long-term view of developing housing operations as a major business line. This is particularly true in the area of automated housing, which will include information and communications equipment that are likely to become integral parts of house design and operation.

He states that, in all probability, competition with such companies will intensify in most areas of the construction market, including houses, factories, and office buildings, plus the prospective fields of energy, marine, and space development projects. This example demonstrates the breadth of competitive intelligence that a Japanese company requires in its strategy formulation, its dependence on both current and future intelligence, and the analytical insight that they provide.

One area of Dr. Hasegawa's strategy development process, his "Strategies to Avoid Competition," deserves special attention. It is this form of strategy that Japanese companies have used most successfully. Gathering intelligence about competitors that use this approach is much more difficult, particularly if the competitor is employing it as an entry strategy, using both low-profile activities and good security to cover the company's actual operations and intentions.

Dr. Hasegawa states that, above all, avoiding competition is the most effective strategy. Such strategies, however, are usually two-sided, requiring both cooperation

and competitive activities. The second is building barriers to newcomers. By properly setting up appropriate barriers, consisting mainly of two types—controlling critical resources and the use of regulatory restrictions—one can control and exclude foreign competition. The third type is cooperative strategies. Properly executed, these strategies make partners of potential competitors; in the Japanese view, this is probably the most effective approach.

Each of the three types require greater intelligence about the competition and the competitive environment than most US corporations are currently capable of providing. Therein lies the Japanese advantage in creating and implementing more sophisticated and effective competitive strategies vis-à-vis their US competitors.

#### **POSITIONING STRATEGIES VERSUS PROACTIVE STRATEGIES**

Most US companies create overall business strategies based on the concept of "set-piece" game theory, aimed at achieving the optimum market position vis-à-vis their competition. Once the actual game begins, however, the US companies' managers and strategists are generally left to their own devices to gather the competitive intelligence necessary to execute subsequent moves. The dynamics of the game often overtakes them, and they find that their strategies become both out of date and inappropriate for the prevailing conditions. As long as the competition is conducted over relatively long time periods (over months and years, for example), they have adequate time to respond to competitors' actions.

But when the game speeds up and the competition is able to make multiple moves quickly, their strategies are frequently two and three steps behind the competitors. As long as they are competing against players using the same rules, the need for real-time intelligence is not high, since both seem to operate in the same timeframe and the competition also requires less timely intelligence.

Two examples demonstrate this situation. The first is the US auto industry. As long as domestic companies were competing among

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and competitive activities. He identifies three principal means of developing and applying these strategies.

The first is entry into less-competitive markets. This provides the company enough time and opportunity to develop the appropriate market skills before entering into

themselves, their planning, design, production schedules, and actual competitive cycles closely matched one another. Intelligence was easily gained and assimilated over a matter of months and years, allowing each company to make adjustments in its technology, manufacturing, and competitive strategies.

However, once Japanese companies entered the market, practicing the "avoid competition" quiet-entry strategy to achieve market position, the game was set for an entirely different form of competition. New designs, different technologies, and more rapid product entry all tended to change the time frame in which intelligence had to be gathered and assimilated. US auto companies were unprepared for this change in the rules of competition.

The Japanese entered the game with not only better intelligence about their competition but a greater understanding of how the US companies competed. It was like a chess game being sped up from making moves in minutes to having to make the same moves in seconds. Neither US management nor the type of intelligence available to it permitted the Big Three to operate at such a quick pace.

A similar situation took place among US defense companies when one firm recognized that, by changing the rules of the game, it could increase its chances of winning because it would be the only company that had prepared to play by the new rules. In the early 1980s, the Raytheon Co. perceived that future defense purchasers would be driven by increasingly low-cost considerations. This meant that by possessing low-cost manufacturing capabilities, Raytheon could achieve a distinct advantage over its competitors. But first it had to change the rules of the game.

This was done by a clever and well-prepared strategy: using both sound financial logic and political clout, the company persuasively argued that the Defense Department would receive better products at lower costs if it opened up its weapons procurement to multiple sources—in effect creating marketplace competition in what had traditionally been a single-source environment.

Raytheon's strategy was successful. The

Navy, in particular, changed the rules to accommodate multiple-source competition and reaped considerable budgetary benefit from lower-cost weapons procurement. Not surprisingly, only Raytheon had prepared both its manufacturing and component supply systems to produce what to many seemed unrealistically low bids. However, those bids were based on sound and well-proven manufacturing and production technologies and procedures.

Once again, better intelligence concerning the competition and its limited production capabilities, along with insightful intelligence concerning the government decision makers' needs to manage the overall procurement process, resulted in an appropriate strategy that gave Raytheon a unique competitive advantage—one it would take years for the competition to overcome.

#### **SIX ROLES OF INTELLIGENCE IN STRATEGY FORMULATION AND IMPLEMENTATION**

Good intelligence, by itself, will not make a great strategy. But successful strategies are derived from good intelligence concerning a company's total business environment, including the competition. That intelligence must describe both the company's current competitive situation and its most likely future competitive environment. The role of intelligence in the formulation and implementation of strategies falls into six basic categories:

**Describing the Competitive Environment.** Intelligence analysis must define the current competitive environment in which the company competes. An intelligence assessment must be made of those forces and factors that make up the company's competitive environment, including competitors, customers, products, the industry structure in which they all perform, and the various types of competition, such as price, performance, and technology. It should be noted, however, that this description differs from the one provided by the marketing department. Combining these

*Avoiding competition is the most effective strategy.*

two environmental assessments (competitive and market) provides the basis for a dynamic analysis of how particular competitive situations are likely to evolve. (I describe this combined situation as a competitive response model—how competitors are likely to respond to your company's product offerings.)

**Forecasting the Future Competitive Environment.** The intelligence department can either provide (or contribute to) a

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forecast of the company's business future, particularly the competitive environment that the company is likely to find itself in (the selected future time frame). The most appropriate intelligence product for this purpose is what is called a *business intelligence estimate*, which might describe the company's future competitive environment as being one entirely different from the business environment that it competes in today.

For example, automotive component suppliers that had competed aggressively among themselves to serve General Motors were either being absorbed by or became partners with larger subsystem suppliers at GM's Saturn plant. The GM purchasing department had concluded that it could no longer afford the cost and time required to manage the various individual component providers. Therefore, it changed the procurement rules to require vendors to supply the total subsystem, including all the components, or to join a group that could supply the entire component assembly, thus creating an entirely new competitive environment. (This situation first occurred in the consumer electronics field and will eventually find its way into other industries, including consumer goods and the food and beverage industry.)

**Challenging the Underlying Assumptions—Asking the Right Questions.** A very important role for intelligence is in identifying and challenging the underlying assumptions (economic, political, technological, as well as market and customer-related) that affect the company strategist's thinking. Often these assumptions are implicit and strategists will not even realize they are basing their strategies on them.

An example of this involved a major electronics manufacturer that conducted a costly and comprehensive global market forecast every other year. For the most part, its industry had been stable, and major changes in the marketplace took place over a period of two to three years. However, during the formulation of the corporate long-range plan during one of the other-year periods, the basic assumption that the market growth forecast had not changed appreciably was made; this had been the procedure for the last seven or eight years, and there was no obvious reason to question it at that time.

The intelligence department, however, had been monitoring individual competitors in various geographical regions of the world and had noticed a significant decline in the purchase of components and subsystems throughout the Asian-Pacific region. As a result, the intelligence department questioned the basic assumption that the industry's market growth would continue at the last estimated percentage.

This certainly caused a lot of consternation on the part of the marketing department. Who was this intelligence analyst to question the experience and judgment of marketing? After all, they tracked all the market data and kept detailed statistics on sales of their own products more completely than any intelligence analyst (which was true, and no one questioned those data). However, the corporate strategist, after listening to the two arguments, decided it would be worth several hundred thousand dollars to at least review the current market situation and its impact on the last forecast.

The results were surprising: an independent market research company concluded that the industry's market growth was going to be less by a factor of at least one-third and that

the usual two-year forecast was invalid for the current time period. The downward revision of this market forecast was significant because the company's overall growth and revenue goals were set by this single factor. Had the company planned to continue to grow at the original rate during this period of downturn, it would have had to significantly increase both marketing and product development costs in order to achieve the expected sales growth. Had they not recognized this situation, there would have been a companywide shortfall in the projected business revenues, which could have been disastrous. Intelligence had caused the right question to be asked—at the right time.

**Identifying and Compensating for Exposed Weaknesses.** The intelligence department can be used to identify and assess a company's own weaknesses and vulnerabilities, something that it typically is required to do for the competition. This ability is particularly valuable when a company is about to launch a new strategy or enter a market or business that it has never participated in before. It is during these times that company weaknesses become vulnerabilities, because the competition is likely to have assessed the newcomer's strengths and weaknesses and will exploit those weaknesses that are truly vulnerabilities.

The well-prepared company entering such new business arenas should understand its own weaknesses before the competition does and take appropriate actions to either correct them or formulate a strategy that does not expose them in ways that might make the company vulnerable.

**Using Intelligence to Implement and Adjust Strategy to the Changing Competitive Environment.** Once the company's new strategy has been formulated and tested, it will go through two distinct phases of implementation. The first phase is during its initial implementation, when competitors begin to sense and react to the strategy's salient features. Good intelligence on how the competitor is responding and adjusting to the strategy's initial implementation is very valuable, both to test its effectiveness

and to begin making adjustments that compensate for any countermeasures the competition is likely to initiate. This initial implementation phase typically lasts for a few months.

After the competition has had time to gather and analyze intelligence on the strategy and the customers' response to it, an intelligent competitor is likely to initiate the second phase, developing a more complete and appropriate set of actions to counter your strategy. The competitor's range of options varies from a totally new strategy of its own to the development of effective counterstrategies (or in some cases, when the competitor wants to attack your new business or product directly, a countermeasure program).

The effectiveness of each will be heavily dependent on the competitor's ability to gather and analyze the appropriate intelligence about your company. It is during this period that greater emphasis should be placed on your company's counterintelligence and security efforts. The more effective these are, the longer your new strategy is likely to remain viable.

The intelligence that you gather during these two distinct phases of implementation are critical to the long-term viability of your new strategy. Comprehensiveness, timeliness, and objectivity are required in both collection and analysis of such competitor intelligence. Yet understanding how other players in the competitive environment are responding, including the customer, suppliers, and governments, when regulatory issues are involved, is just as important. Few US companies are capable of conducting such effective business intelligence operations and thus formulating the appropriate ongoing business plans necessary to continually adjust their strategy to the changing competitive environment.

**Determining When the Strategy Is No Longer Sustainable.** Once a successful strategy has been put in place and it has survived the initial phases of implementation, it is imperative that the company's business intelligence unit establish an ongoing intelligence collection and reporting program to

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monitor the competitor's actions. Eventually, the competitor will either produce a new product, develop an appropriate counterstrategy, or find other ways to overcome your new business strategy. Deriving early indications of such competitor actions make it mandatory for you to both detect and understand the nature of the competition's response. Your strategy should be constantly reviewed, and when intelligence indicates that strategic or major changes are taking place within your competitor's organization or product offerings, an intelligence assessment should be made of their potential impact on both your current performance and future plans.

The ability of your company to sustain its strategy's effectiveness over time will depend directly on how well you monitor and understand your competitor's actions. Therefore, intelligence plays a critical role not only in the formulation of strategy and its implementation, but in its viability. Senior executives and strategists will ultimately determine whether the strategy is sustainable or a new one is necessary. Good competitive intelligence will help them make that determination before it is too late.

#### **USING INTELLIGENCE TO CREATE EFFECTIVE STRATEGIES**

Both strategic and tactical intelligence are critical to the effectiveness of a company's business strategies. Strategists must make full use of business intelligence in the formulation of competitive strategies to craft a truly competitor-sensitive strategy and to monitor the competition's resulting market activities and counteractions. Even if your company's strategies are formulated without the explicit use of business intelligence, you should at least understand your competitors' intent regarding your customers; otherwise, be prepared to continually adjust your strategies as the competitive environment is influenced by competitor actions intended to achieve objectives that are similar to yours.

Although it seems inconceivable that companies would take this "non-intelli-

gence" approach to strategy formulation and implementation, many US companies do. For those interested in using business intelligence in strategy formulation and implementation, the following is a brief checklist:

- Make intelligence an explicit input in your strategy-formulation process, including identifying and challenging underlying assumptions.
- Consider whether the new strategy requires you to assess your company's weaknesses and vulnerabilities; if so, assign the task to the intelligence department.
- Have the intelligence department assess the competitor's likely responses to your new strategy or product entry before actual implementation; adjust the strategy or plan accordingly. (Consider war-gaming as one possible way of doing this: it is interesting, fun, and provides the appropriate results.)
- Analyze your own strategy so that you might identify which strategic features will directly influence your competitors. Prepare ahead of time to monitor and analyze these features so that any major changes resulting in the competitor's actions can be detected and their results measured.
- Prior to strategy implementation, establish appropriate intelligence collection and monitoring capabilities so that the competitor's initial and secondary responses can be detected and analyzed in real time; link the intelligence reporting directly to the managers in charge of the related operations and the strategists (if different). Assess your need for security and counterintelligence operations; put them in place before strategy implementation.
- Assign the intelligence department the continuing responsibility of challenging the strategy's viability and producing the evidence to support any assessment that it is no longer viable. ■

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