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Getting strategy wrong—and how to do it right instead

Too many companies equate strategy with hitting financial goals. They underestimate the difficulty—and the value—of the real thing.

by Richard P. Rumelt

The word "strategy" means an approach to dealing with a difficult challenge, especially that of competing with a clever opponent. To have a strategy is to have an approach to overcoming critical obstacles and difficulties. However, through many years of working with companies, government agencies, and the military, I have too often seen strategies that are actually a toxic mix of wishful thinking combined with a jumble of incoherent policies.

In 2016, an S&P 500 company I'll call Royalfield gathered 25 of its senior executives in a hotel ballroom for what was billed as a strategy discussion. I was there to give a prelunch talk on strategy and had been invited to spend the day with the group and join them for dinner.

The chief financial officer spoke first and showed clips from Marvel's *Thor* movie to dramatize the financial report. A key point was that the company's debt burden was becoming a constraint, so investments had to be carefully controlled if return on equity was to be preserved.

The chief executive officer spoke next, armed with PowerPoint slides presenting what he called the Strategic Commitment and the Success Score Card (SSC). He reminded the group that the strategic commitment grew out of a key acquisition made three years earlier and defined the newly expanded scope of the business. It comprised a description of the market being served and the admonition that the company's products would "provide its customers with the most effective solutions to their needs." It would also aim to "provide a high level of service" for its products.

The SSC for the whole of Royalfield was specified as a 15 percent annual growth in earnings and a 15 percent return on equity. These targets were somewhat higher than the company's recent financial record. The CEO ended with a quote from 19-year-old Katie Ledecky, who had won five Olympic gold medals in swimming: "Set goals that, when you set them, you think they're impossible. But then every day, you can work toward them, and anything is possible."[1]

During a break, uplifting music played. Each participant received a handsome marble desk weight commemorating the strategy retreat.

After lunch, the four business unit managers each presented their individual SSCs. Each offered targets for sales growth, profit rate, return on investment, and market share, along with strategies for achieving these targets. There were references to key customers and certain product improvements, but the basic language had been preset by the CEO: the language of financial performance. Their strategies, therefore, boiled down to promising to find new customers, somehow cutting costs, and keeping investment in check to boost return on equity.

The CEO's system of defining the SSCs in largely financial-performance terms shaped the options they considered and shifted strategic thinking away from technology, product, customer, and competition and toward tactics for achieving targeted accounting results. There was no serious consideration of how the contradictory demands for increased sales and reduced costs would be reconciled.

Why had these well-trained, highly paid executives chosen this approach? One way to understand Royalfield is to recognize that the CEO's almost daily experience was explaining the company's financial results to investors, Wall Street analysts, pension and hedge funds, Royalfield's board, and the Securities and Exchange Commission. His personal incentive package was framed against accounting results and stock-market returns. Thus, the world he inhabited had been engineered to make the SSCs his personal problem.

Another way of understanding Royalfield is that the company leadership had accepted the pop-culture notion that strategy is a broad statement about purpose and values. A vague strategic commitment replaced having a real strategy. With strategy seemingly addressed by the strategy commitment, the company's strategy retreat centered on what executives saw as the real work—the setting of financial-performance targets.

Some of Royalfield's strategic challenges seemed fairly evident. The company was still organized by regions, while the industry had become global. The technology it had invented and successfully deployed in the past had been equaled—and, in places, surpassed—by a competitor's inventions. The company's engineering group was competent but slow to act, responding to its own internal sensibilities rather than to competitive issues.

When, over drinks before dinner, I raised some of these issues with the CEO, he held out his hand, palm forward, asking me to stop. "I don't want to hear negative things about the team. I don't want them distracted from the SSCs."

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[1] Katie Ledecky Quotes, BrainyQuote.

I did not work with Royalfield again. In the years since that event, each of the company's competitors grew faster, and the share losses were greatest in Royalfield's core business. These losses were clearly due to the company not keeping pace with the technologies offered by competitors. Yes, Royalfield cut expenses so that its net profit margin improved. But its growth rate fell behind that of its industry, and its market share dropped by 30 percent as competitors won sales by targeting key customer segments.

Royalfield had significant strategic issues that it should have faced in order to move forward. It did not do this, because the company's leaders misunderstood the meaning and purpose of strategy itself. Instead of facing and resolving challenges, leadership asked operating managers to create strategies for achieving certain arbitrary financial outcomes.

The sad truth is that Royalfield is not an isolated case. Today, I and many other researchers and consultants have observed that too much corporate work on strategy has devolved into setting financial-performance goals rather than developing solutions to important and often imminent difficulties. Is it any surprise that most senior executives are disappointed with the outcomes of their strategy process? A McKinsey survey found that 70 percent of executives surveyed did not like their company's strategy process and 70 percent of board members didn't trust the results of that process.[2] Other surveys have corroborated these findings.

A common complaint is that strategic plans don't work out or guide actual operations. Some years ago, I asked then-CEO Robert Eckert about strategy at Mattel. Smiling, he said, "We do a great job of strategic planning. The problem is implementation." Eckert's observation expresses an unavoidable fact: plans cannot predict competitive outcomes. Or, as Mike Tyson so eloquently put it: "Everyone has a plan until they get punched in the mouth."[3]

At many businesses, nonprofits, and government agencies, so-called strategy exercises do not produce strategies—because they are designed to do something else. In commercial settings, they are often attempts to predict and control financial outcomes, nothing more than a form of budgeting. The process may glance at broader issues, but it quickly centers on financial targets and then budget allocations. In nonprofits and government agencies, the strategy activity often develops a list of ambitions that passes as "strategy." What is missing are the elements giving strategy its bite: a realistic assessment of the obstacles blocking or slowing forward progress and a mix of policies and actions designed to focus organizational energy on surmounting these obstacles.

Why strategy is hard: Gnarly challenges

Real strategy work is hard. It is hard because serious strategy situations are much more complex than decision situations. They are what I call *gnarly*, resisting easy resolution.

Gnarly situations do not present easy-to-identify answers; they don't even present readily identifiable choices. Rather, they present multiple issues where the underlying forces

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[2] Survey conducted in 2014, referenced in Chris Bradley, Martin Hirt, and Sven Smit, *Strategy Beyond the Hockey Stick*, Hoboken, NJ: John Wiley & Sons, 2018.
[3] Mike Tyson's reply to reporter asking about Evander Holyfield's fight plan, Associated Press, August 1987.

and logic at work are not immediately obvious. Is the engineering issue at Royalfield due to a lack of training, not enough spending, overlapping divisional responsibilities, poor leadership, a combination of the above, or something else altogether?

In a gnarly situation, clear choices must be searched for and designed or imagined. Many of the most apparent alternatives—invade or blockade, acquire BuyCo or not—have been posited with artificial clarity by shortsighted staff or parties with vested interests. There are almost always other ways to proceed.

Making matters more complex, especially in areas of public policy and defense, real-life leaders do not have a neat economist's single measure of value. Instead, they are faced with a bundle of conflicting ambitions—a group of desires, goals, intents, values, and fears—that cannot all be satisfied simultaneously. Forging a sense of purpose from this bundle is part of the gnarly problem. Making matters most complex is the fact that the connection between potential actions and actual outcomes is unclear.

A gnarly challenge is not solved with analysis or the application of preset frameworks. A coherent response arises only through a process of diagnosing the nature of the challenges, framing, reframing, chunking down the scope of attention, referring to analogies, and developing insight. The result is a design, or *creation*, embodying purpose. I call it a creation because it is often not obvious at the start, the product of insight and judgment rather than an algorithm. Implicit in the concept of insightful design is that knowledge, though required, is not, by itself, sufficient.

The way through a gnarly challenge may not seem clear at first but working to grasp the structure of the challenge is often the best way of seeing a path through. As a number of problem-solving researchers have found, "at the least, problems must be deeply analyzed before an insight solution can be achieved."[4] Writing about how hard design problems are solved, industrial-design specialist Kees Dorst nicely described zeroing in on the heart of a difficulty:

> *"Experienced designers can be seen to engage with a novel problem situation by searching for the central paradox, asking themselves what it is that makes the problem so hard to solve. They only start working toward a solution once the nature of the core paradox has been established to their satisfaction."*[5]

The skilled strategist recognizes the heart of a challenge as the thing blocking an easy solution. Attention is drawn to it because it hints at leverage—that if we could only just move the keystone, the whole wall can be breached.

The crux principle

To execute strategy well, one must consider the logic of challenges instead of wished-for end states. At a moment in time, a properly configured strategy is a mixture of policy and

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[4] Mark Beeman and John Kounios, "The cognitive neuroscience of insight," *Annual Review of Psychology*, January 2014, Volume 65.

[5] Kees Dorst, "The core of 'design thinking' and its application," *Design Studies*, November 2011, Volume 32, Issue 6.

action designed to surmount a high-stakes challenge. (Were the challenge not high stakes, it would not be called strategic.) It is not a financial goal, or a plan for hitting a financial goal, or a wished-for end state, or a long list of priorities. A dynamic strategy is designed to be a way forward that deals with particular obstacles and barriers to progress. It is not static but rather is renewed as new challenges and opportunities appear and as older challenges are surmounted. Strategy is continued, ongoing problem solving.

Given a set of gnarly challenges, three strategic skills can define the path forward. The first is judgment about which issues are truly important and which are secondary. The second is judgment about the difficulties of dealing with different issues. And the third is the ability to focus, to avoid spreading resources too thinly or trying to do everything at once. In combination, these three skills lead to what I call *the crux*—the most important part of a set of challenges, the part that is *addressable*, which has a good chance of being solved through focused, coherent action.

As an example, the entrepreneur Elon Musk is passionate about populating Mars. He imagined promoting this idea by sending a small payload there. In 2001, Musk had tried to buy an old rocket but was unhappy with the style of bargaining and how the price tripled during the negotiations. He began to look at the challenge of cost—why did it cost so much to put payloads into orbit? He was quick so see that the high cost was because rockets were not reusable. There was no cheap way to return to Earth through the furnace-heat of blasting back through the atmosphere at 18,000 miles per hour. Was there a way around this problem, the Achilles heel of the old space shuttle? Then Musk had an insight: fuel was a lot cheaper than vehicles. It might make sense to avoid the huge complexity of super-high-heat reentry by carrying more fuel and using it to slow the rocket's return to Earth. Like many old science fiction stories, Musk imagined a rocket that would turn around and slow down by firing its engine, leading to a soft landing. No violent reentry furnace would char the outside of the vehicle. The process could be automated, as well—no need for a human pilot. The key would be engineering a rocket engine that could reliably start and stop and accurately throttle and direct its power. With this insight, soft reentry became the crux challenge for SpaceX.

It took years of engineering and tests, but in 2015 the SpaceX Falcon 9 became the first rocket to ever gain orbit, turn around and fire its engines for a slow reentry, and softly land on its tail. By 2018, the Falcon 9's cost per pound into low-Earth orbit was 23 times cheaper than the old space shuttle. Its bigger brother, the Falcon Heavy, cut the Falcon 9's cost per pound in half.

For another example of discerning a crux, consider Marvel, which in 1999 had just come out of bankruptcy with a comic-book business, a toy business, and a huge debt burden. The company had an avid following among comic-book readers but no general audience. Much of the debt was paid off by licensing characters for toys and games. The next opportunity seemed to lie in having Marvel characters anchor feature films. Yet there was a classic chicken-and-egg problem: studio licensing offers were low because there had yet not been a successful major film based on Marvel characters. And because there had been no major feature film, the characters were largely unknown outside the comic-book crowd. While Marvel had 4,700 comic-book characters, Hollywood was chiefly interested in just Spiderman and the X-Men.

After licensing Spiderman to Sony Pictures and X-Men to Fox for very low fees, Marvel president Kevin Feige worked on the problem of making the rest of the Marvel characters worth something. This challenge became the crux of a strategy as he devised a plan for a large group of Marvel characters to all inhabit the same fictional "universe." Using this idea, Marvel raised money from Wall Street to pay for an independent studio. Its first successful film, *Iron Man*, has been followed by 27 more feature films (and 11 TV series), many of which star the same set of characters: Iron Man, Thor, Captain America, the Winter Soldier, Black Widow, Hawkeye, Vision, Black Panther, and so on. Marvel was acquired by Disney in 2009, which continues to develop the Marvel Cinematic Universe.

The force of coherence

The most ancient and still crucial element of strategy is focus. In military terms, it is the concentration of force on an opponent's weakness. More generally, it is the coordinated application of resources and effort to an important yet addressable challenge. Strategic focus means bringing sources of power to bear on a selected target. If the power is weak, nothing happens. If it is strong but scattered and diffused across targets, nothing good happens. If power is focused on the wrong target, nothing good happens. But when power is focused on the right target, breakthroughs occur.

An example of focus is Bolero. After the United States entered World War II in 1941, General George C. Marshall, US Army chief of staff, brought Major General Dwight D. Eisenhower into a top position in war planning. On March 25, 1942, Eisenhower presented his strategy, code-named Bolero. The strategy's chief element was an invasion across the English Channel (Operation Roundup). In justifying this difficult challenge as the crux, Eisenhower had to reject proposals to add American troops to the Russian front, to focus on the Mediterranean, to come up through Spain, or to come down through Scandinavia. In Bolero, he insisted on a focus on securing the United Kingdom and keeping Russia in the war. The focus on this priority was evident when he wrote, "Unless this plan [Bolero] is adopted as the central aim of all our efforts, we must turn our backs upon the Eastern Atlantic and go, full out, as quickly as possible, against Japan."[6] General Marshall and President Roosevelt agreed, and after a briefing in London, so did Winston Churchill.

Surprisingly, one month later, President Roosevelt caved to Navy and Australian pressure and announced a commitment of 100,000 soldiers and 1,000 aircraft to Australia. The move would have shattered the coherence of Bolero. General Marshall went to the White House and confronted Roosevelt. He told the president that if he wanted to defend Australia, there should be a "complete abandonment" of Bolero. Historian J. E. Smith wrote:

> *"FDR was sometimes too quick off the mark, and this time he recognized that he had overstepped. As he often did when caught out, he dissembled. 'I did not issue any directive to increase our forces in Australia,' he wrote Marshall. Roosevelt said he merely 'wanted to know if it were possible to do so. I do not want Bolero slowed down.'"*[7]

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[6] Memorandum for the chief of staff, "Critical points in the development of coordinated viewpoint as to major tasks of war," March 25, 1942, 1 War Years, 205–7; as quoted and referenced in Jean Edward Smith, *Eisenhower: In War and Peace*, first edition, New York, NY: Random House, 2012.

[7] The subquote is from Maurice Matloff and Edwin Marion Snell, *Strategic Planning for Coalition Warfare, 1941-1942 [--1943-1944]*, 1953, Volume 3, Washington: Office of the Chief of Military History, Department of the Army.

One sees how coherence is easily lost. The cost of coherence is saying no to many interests with reasonable values and arguments.

The experience of McGraw Hill is an example of how coherence can pay off. Founded in 1888, by 2009, McGraw Hill had become a publishing conglomerate. It published *BusinessWeek*, *Architectural Record*, and *Aviation Week*, owned broadcasting divisions, published the greatest number of education books in the United States, and ran the Standard & Poor's credit rating agency. Within it were numerous committees and interconnections among the publishing, education, and financial-information businesses. The overabundance of such links added costly complexity by mixing executives with very different kinds of experience. In addition, the company's Standard & Poor's subsidiary was drawing intense scrutiny for the credit ratings it had given many subprime mortgage bundles. Many observers thought that the temptation to ditch that business was obvious. But, after thinking it through, company leaders chose to go in the opposite direction. They decided to center the company on financial data rather than paper publishing.

In the next few years, McGraw Hill sold *BusinessWeek* to Bloomberg, sold its broadcasting operations, and sold the entire education business. It sold off a host of publications and its J.D. Power survey division. The company changed its name to S&P Global and focused exclusively on financial-information services. With a coherent concentration on the high-profit, fast-growing market for financial data, benchmarks, and analytics, S&P Global's market value has grown at an average of 23 percent a year since 2012.

Facing the facts about strategy

A strategy is a way to overcome selected difficulties. It is not a wish list of wonderful possible outcomes.

The art of strategy is not the art of decision making—that discipline assumes that you have been handed a list of possible actions to choose among. The art of strategy is also not the process of finding your one true goal and passionately pursuing it with all your heart and soul in everything you do—that is what some call monomania. Nor is the art of strategy the act of setting higher and higher performance goals for people and using charisma, carrots, and sticks to push them to attain those goals—that presumes that someone somewhere knows how to find a way through the thicket of problems the organization actually faces.

To create a strategy, one needs to embrace the full complex and confusing force of the challenges and opportunities being faced.

To create a strategy, one has to develop a sense for the *crux* of the problem—the place where a commitment to action will have the best chance of surmounting the most critical obstacles.

To create a strategy, one needs to be persistent and avoid the temptation to grab the first glimmer of a pathway through the thicket of issues.

To create a strategy, one must balance a host of issues with its bundle of accompanying ambitions—the purposes, values, and beliefs that stakeholders wish to support.

To create a strategy, one must keep actions and policies coherent and aligned, instead of nullifying efforts by pursuing too many different initiatives or conflicting purposes.

These facts are rarely written or spoken about with honesty. We are told that strategy is about having an advantage (obviously!)—that it is about having a long-term vision of where you want to be. We are told that by adopting method X or mindset Y the average business can become as successful as the very best.

However, the honest fact is that we do not live in Lake Wobegon, and the majority of organizations cannot be above average. The honest fact is that some situations are irretrievable and offer no clever way out. The honest fact is that organizations cannot change direction on a dime. The honest fact is that some situations are so locked up with competing political interests that there is not enough executive power anywhere to break the logjam. Strategy is not magic.

What is true is that to meet a challenge, one should first work to comprehend its nature. You cannot improve a failing school system unless you have a clear idea about why it is failing. To supply shoppers with a better shopping experience, you need to know about their wants, habits, and needs, as well as the technologies that can help you sell once you've learned their preferences. Don't start with goals—start by understanding the challenge and finding its crux. Q

Richard P. Rumelt is professor emeritus at UCLA Anderson School of Management and the author of the forthcoming book *The Crux: How Leaders Become Strategists* (Public Affairs, 2022).