CHAPTER FIVE
THE KERNEL OF GOOD STRATEGY

Good strategy is coherent action backed up by an argument, an effective mixture of thought and action with a basic underlying structure I call the *kernel*. A good strategy may consist of more than the kernel, but if the kernel is absent or misshapen, then there is a serious problem. Once you apprehend this kernel, it is much easier to create, describe, and evaluate a strategy. The kernel is not based on any one concept of advantage. It does not require one to sort through legalistic gibberish about the differences between visions, missions, goals, strategies, objectives, and tactics. It does not split strategies into corporate, business, and product levels. It is very straightforward.

The kernel of a strategy contains three elements:

1. A *diagnosis* that defines or explains the nature of the challenge. A good diagnosis simplifies the often overwhelming complexity of reality by identifying certain aspects of the situation as critical.

2. A *guiding policy* for dealing with the challenge. This is an overall approach chosen to cope with or overcome the obstacles identified in the diagnosis.

3. A set of *coherent actions* that are designed to carry out the guiding policy. These are steps that are coordinated with one another to work together in accomplishing the guiding policy.

Here are some examples:

- For a doctor, the challenge appears as a set of signs and symptoms together with a history. The doctor makes a clinical diagnosis, naming a disease or pathology. The therapeutic approach chosen is the doctor's guiding policy. The doctor's specific prescriptions for diet, therapy, and medication are the set of coherent actions to be taken.

- In foreign policy, challenging situations are usually diagnosed in terms of analogies with past situations. The guiding policy adopted is usually an approach deemed successful in some past situation. Thus, if the diagnosis is that Iran's president, Mahmoud Ahmadinejad, is "another Hitler," war might be the logical implication. However, if he is "another Moammar Gadhafi," then strong pressure coupled with behind-the-scenes negotiation might be the chosen guiding policy. In foreign policy, the set of coherent actions are normally a mix of economic, diplomatic, and military maneuvers.

- In business, the challenge is usually dealing with change and competition. The first step toward effective strategy is diagnosing the specific structure of the challenge rather than simply naming performance goals. The second step is choosing an overall guiding policy for dealing with the situation that builds on or creates some type of leverage or advantage. The third step is the design of a configuration of actions and resource allocations that implement the chosen guiding policy.

- In many large organizations, the challenge is often diagnosed as internal. That is, the organization's competitive problems may be much lighter than the obstacles imposed by its own outdated routines, bureaucracy, pools of entrenched interests, lack of cooperation across units, and plain-old bad management. Thus, the guiding policy lies in the realm of reorganization and renewal. And the set of coherent actions are changes in people, power, and procedures. In other cases the challenge may be building or deepening competitive advantage by pushing the frontiers of organizational capability.

I call this combination of three elements the *kernel* to emphasize that it is the bare-bones center of a strategy—the hard nut at the core of the concept. It leaves out visions, hierarchies of goals and objectives, references to time span or scope, and ideas about adaptation and change. All of these are supporting players. They represent ways of thinking about strategy, stimulating the creation of strategies, energizing groups of people, denoting specific sources of advantage, communicating, summarizing, and analyzing strategies, and so on. The core content of a strategy is a *diagnosis* of the situation at hand, the creation or identification of a *guiding policy* for dealing with the critical difficulties, and a set of *coherent actions*. I will explore the three elements of the kernel one by one.

THE DIAGNOSIS

After my colleague John Mamer stepped down as dean of the UCLA Anderson School of Management, he wanted to take a stab at teaching strategy. To acquaint himself with the subject, he sat in on ten of my class sessions. Somewhere around class number seven we were chatting about pedagogy and I noted that many of the lessons learned in a strategy course come in the form of the questions asked as study assignments and asked in class. These questions distill decades of experience about useful things to think about in exploring complex situations. John gave me a sidelong look and said, "It looks to me as if there is really only one question you are asking in each case. That question is 'What's going on here?'"

John's comment was something I had never heard said explicitly, but it was instantly and obviously correct. A great deal of strategy work is trying to figure out what is going on. Not just deciding what to do, but the more fundamental problem of comprehending the situation.

At a minimum, a diagnosis names or classifies the situation, linking facts into patterns and suggesting that more attention be paid to some issues and less to others. An especially insightful diagnosis can transform one's view of the situation, bringing a radically different perspective to bear. When a diagnosis classifies the situation as a certain type, it opens access to knowledge about how analogous situations were handled in the past. An explicit diagnosis permits one to evaluate the rest of the strategy.

Additionally, making the diagnosis an explicit element of the strategy allows the rest of the strategy to be revisited and changed as circumstances change.

Consider Starbucks, which grew from a single restaurant to an American icon. In 2008, Starbucks was experiencing flat or declining same-store traffic growth and lower profit margins, its return on assets having fallen from a generous 14 percent to about 5.5 percent. An immediate question arose: How serious was this situation? Any rapidly growing company must, sooner or later, saturate its market and have to clamp down on its expansion momentum. Slowing growth is a problem for Wall Street but is a natural stage in the development of any noncancerous entity. Although the U.S. market may have been saturated, were there still opportunities for expansion abroad? Deutsche Bank opined that Starbucks faced a great deal of competition oversees, noting in particular that its 23 remaining restaurants in Australia competed with 764 McDonald's outlets selling McCafe-branded coffee, lattes, cappuccinos, and smoothies.[1] By contrast, Oppenheimer opined, "We would expect that these markets [Europe] are still under-penetrated enough to maintain growth."[2] Was the foreign market saturated?

Or were there more serious problems? Was overbuilding outlets a sign of poor management? Were consumers' tastes changing once again? As competitors improved their coffee offerings, was Starbucks' differentiation vanishing? In fact, how important for Starbucks was the coffee-shop setting it provided versus the coffee itself? Was Starbucks a coffee restaurant, or was it actually an urban oasis? Could its brand be stretched to other types of products and even other types of restaurants?

At Starbucks, one executive might diagnose this challenging situation as "a problem in managing expectations." Another might diagnose it as "a search for new growth platforms." A third might diagnose it as "an eroding competitive advantage." None of these viewpoints is, by itself, an action, but each suggests a range of things that might be done and sets aside other classes of action as less relevant to the challenge. Importantly, none of these diagnoses can be *proven* to be correct—each is a judgment about which issue is preeminent. Hence, diagnosis is a judgment about the meanings of facts.

The challenge facing Starbucks was *ill-structured*. By that I mean that no one could be sure how to define the problem, there was no obvious list of good approaches or actions, and the connections between most actions and outcomes were unclear. Because the challenge was ill-structured, a real-world strategy could not be logically deduced from the observed facts. Rather, a diagnosis had to be an educated guess as to what was going on in the situation, especially about what was critically important.

The diagnosis for the situation should replace the overwhelming complexity of reality with a simpler story, a story that calls attention to its crucial aspects. This simplified model of reality allows one to make sense of the situation and engage in further problem solving.

Furthermore, a good strategic diagnosis does more than explain a situation—it also defines a domain of action. Whereas a social scientist seeks a diagnosis that best predicts outcomes, good strategy tends to be based on the diagnosis promising leverage over outcomes. For instance, we know from research that K–12 student performance is better explained by social class and culture than by expenditures per student or class size, but that knowledge does not lead to many useful policy prescriptions. A very different strategic diagnosis has been provided by my UCLA colleague Bill Ouchi. His book *Making Schools Work* diagnoses the challenge of school performance as one of *organization* rather than as one of class, culture, funding, or curriculum design.[3] Decentralized schools, he argues, perform better. Now, whether the organization of a school system explains *most* of the variations in school performance is not actually critical. What is critical, and what makes his diagnosis useful to policy makers, is that organization explains some part of school performance and that, unlike culture or social class, organization is something that can be addressed with policy.

A diagnosis is generally denoted by metaphor, analogy, or reference to a diagnosis or framework that has already gained acceptance. For example, every student of U.S. national strategy knows about the diagnosis associated with the Cold War guiding policy of containment. This concept originated with George Kennan's famous "long telegram" of 1946. Having served as an American diplomat in the USSR for more than a decade, and having seen Soviet terror and politics at close hand, he carefully analyzed the nature of Soviet ideology and power. Kennan started with the observation that the Soviet Union was not an ordinary nation-state. Its leaders defined their mission as opposition to capitalism and as spreading the gospel of revolutionary communism by whatever means necessary. He stressed that antagonism between communism and capitalist societies was a central foundation of Stalin's political regime, preventing any sincere accommodation or honest international agreements. However, he also pointed out that the Soviet leaders were realists about power. Therefore, he recommended a guiding policy of vigilant counterforce:

> In the light of the above, it will be clearly seen that the Soviet pressure against the free institutions of the western world is something that can be contained by the adroit and vigilant application of counter-force at a series of constantly shifting geographical and political points, corresponding to the shifts and maneuvers of Soviet policy, but which cannot be charmed or talked out of existence. The Russians look forward to a duel of infinite duration, and they see that already they have scored great successes.[4]

Kennan's diagnosis for the situation—a long-term struggle without the possibility of a negotiated settlement—was widely adopted within policy-making circles in the United States. His guiding policy of containment was especially attractive as it specified a broad domain of action—the USSR was, metaphorically speaking, infected by a virus. The United States would have to keep the virus from spreading until it finally died out. Kennan's policy is sometimes called a strategy, but it lacked the element of action. All presidents from Truman through George H. W. Bush struggled with the problem of turning this guiding policy into actionable objectives. Over time, the guiding policy of containment led to NATO and SEATO, the Berlin Airlift, the Korean War, placing missiles in Europe, the Vietnam War, and other Cold War actions.

The power of Kennan's diagnosis can be seen by considering how history might have been different if the situation had been framed another way in 1947. Perhaps the Soviet Union could have been enticed into the world community through a policy of engagement by including it in the Marshall Plan. Or perhaps it wasn't an American problem at all, but an issue for the United Nations. Or perhaps the Soviet Union was a tyranny rivaling Nazi Germany, and the United States should have sought to actively oppose it, undermine it, and liberate its population.

In business, most deep strategic changes are brought about by a change in diagnosis—a change in the definition of the company's situation. For example, when Lou Gerstner took over the helm at IBM in 1993, the company was in serious decline. Its historically successful strategy had been organized around offering complete, integrated, turnkey end-to-end computing solutions to corporations and government agencies. However, the advent of the microprocessor changed all that. The computer industry began to fragment, with separate firms offering chips, memory, hard disks, keyboards, software, monitors, operating systems, and so on. (The vertical disintegration of the computer industry is analyzed in chapter 13, "Using Dynamics.") As computing moved to the desktop, and as IBM's desktop offering became commoditized by clone competitors and the Windows-Intel standard, what should the company do? The dominant view at the company and among Wall Street analysts was that IBM was too integrated. The new industry structure was fragmented and, it was argued, IBM should be broken up and fragmented to match. As Gerstner arrived, preparations were under way for separate stock offerings for various pieces of IBM.

After studying the situation, Gerstner changed the diagnosis. He believed that in an increasingly fragmented industry, IBM was the one company that had expertise in all areas. Its problem was not that it was integrated but that it was failing to use the integrated skills it possessed. IBM, he declared, needed to become more integrated—but this time around customer solutions rather than hardware platforms. The primary obstacle was the lack of internal coordination and agility. Given this new diagnosis, the guiding policy became to exploit the fact that IBM was different, in fact, unique. IBM would offer customers tailored solutions to their information-processing problems, leveraging its brand name and broad expertise, but willing to use outside hardware and software as required. Put simply, its primary value-added activity would shift from systems engineering to IT consulting, from hardware to software. Neither the "integration is obsolete" nor the "knowing all aspects of IT is our unique ability" viewpoints are, by themselves, strategies. But these diagnoses take the leader, and all who follow, in very different directions.

THE GUIDING POLICY

The guiding policy outlines an overall approach for overcoming the obstacles highlighted by the diagnosis. It is "guiding" because it channels action in certain directions without defining exactly what shall be done. Kennan’s containment and Gerstner’s drawing on all of IBM’s resources to solve customers’ problems are examples of guiding policies. Like the guardrails on a highway, the guiding policy directs and constrains action without fully defining its content.

Good guiding policies are not goals or visions or images of desirable end states. Rather, they define a *method* of grappling with the situation and ruling out a vast array of possible actions. For example, Wells Fargo’s corporate vision is this: “We want to satisfy all of our customers’ financial needs, help them succeed financially, be the premier provider of financial services in every one of our markets, and be known as one of America’s great companies.”[5]

This “vision” communicates an ambition, but it is not a strategy or a guiding policy because there is no information about *how* this ambition will be accomplished. Wells Fargo chairman emeritus and former CEO Richard Kovacevich knew this and distinguished between this vision and his company’s guiding policy of using the network effects of cross-selling. That is, Kovacevich believed that the more different financial products Wells Fargo could sell to a customer, the more the company would know about that customer and about its whole network of customers. That information would, in turn, help it create and sell more financial products. This guiding policy, in contrast to Wells Fargo’s vision, calls out a way of competing—a way of trying to use the company’s large scale to advantage.

You may correctly observe that many other people use the term “strategy” for what I am calling the “guiding policy.” I have found that defining a strategy as just a broad guiding policy is a mistake. Without a diagnosis, one cannot evaluate alternative guiding policies. Without working through to at least the first round of action one cannot be sure that the guiding policy can be implemented. Good strategy is not just “what” you are trying to do. It is also “why” and “how” you are doing it.

A good guiding policy tackles the obstacles identified in the diagnosis by creating or drawing upon sources of *advantage*. Indeed, the heart of the matter in strategy is usually advantage. Just as a lever uses mechanical advantage to multiply force, strategic advantage multiplies the effectiveness of resources and/or actions. Importantly, not all advantage is competitive. In nonprofit and public policy situations, good strategy creates advantage by magnifying the effects of resources and actions.

In most modern treatments of competitive strategy, it is now common to launch immediately into detailed descriptions of specific sources of competitive advantage. Having lower costs, a better brand, a faster product-development cycle, more experience, more information about customers, and so on, can all be sources of advantage. This is all true, but it is important to take a broader perspective. A good guiding policy itself can be a source of advantage.

A guiding policy creates advantage by *anticipating* the actions and reactions of others, by *reducing the complexity and ambiguity* in the situation, by exploiting the *leverage* inherent in concentrating effort on a pivotal or decisive aspect of the situation, and by creating policies and actions that are *coherent*, each building on the other rather than canceling one another out. (These sources of advantage are discussed in detail in chapter 6, “Using Leverage.”)

For example, Gerstner’s “provide customer solutions” policy certainly counted on the advantages implicit in IBM’s world-class technological depth and expertise in almost all areas of data processing. But the policy itself also created advantage by resolving the uncertainty about what to do, about how to compete, and about how to organize. It also began the process of coordinating and concentrating IBM’s vast resources on a specific set of challenges.

To look more closely at how a guiding policy works, follow the thinking of Stephanie, a friend who owns a corner grocery store. She does the accounts, manages personnel, sometimes runs the cash register, and makes all the decisions. Several years ago, Stephanie told me about some of the issues she was facing. She was considering whether she should keep prices down or offer more expensive, fresh organic produce. Should she begin to stock more Asian staples for the many Asian students who lived in the area? Should the store be open longer hours? How important was it to have a helpful, friendly staff that gets to know the regulars? Would adding a second checkout stand pay off? What about parking in the alley? Should she advertise in the local college newspaper? Should she paint the ceiling green or white? Should she put some items on sale each week? Which ones?

An economist would tell her that she should take actions that maximize profit, a technically correct but useless piece of advice. In the economics textbook it is simple: choose the rate of output *Q* that provides the biggest gap between revenue and cost. In the real world, however, “maximize profit” is not a helpful prescription, because the challenge of making, or maximizing, profit is an ill-structured problem. Even in a corner grocery store, there are hundreds or thousands of possible adjustments one can make, and millions in a business of any size—the complexity of the situation can be overwhelming.

Thinking about her store, Stephanie diagnosed her challenge to be competition with the local supermarket. She needed to draw customers away from a store that was open 24/7 and had lower prices. Seeking a way forward, she believed that most of her customers were people who walked by the store almost every day. They worked or lived nearby. Scanning her list of questions and alternatives, she determined that there was a choice between serving the more price-conscious students or the more time-sensitive professionals. Transcending thousands of individual choices and instead framing the problem in terms of choosing among a few customer groups provided a dramatic reduction in complexity.

Of course, if both of these customer segments could be served with the same policies and actions, then the dichotomy would have been useless and should be cast aside. In Stephanie’s case, the difference seemed significant. More of her customers were students, but the professionals who stopped in made much larger purchases. Pushing further along, Stephanie began to explore the guiding policy of “serve the busy professional.” After some more tinkering, Stephanie sharpened the guiding policy a bit more, deciding to target “the busy professional who has little time to cook.”

There was no way to establish that this particular guiding policy was the only good one, or the best one. But, absent a good guiding policy, there is no principle of action to follow. Without a guiding policy, Stephanie’s actions and resource allocations would probably be inconsistent and incoherent, fighting with one another and canceling one another out. Importantly, adopting this guiding policy helped reveal and organize the interactions among the many possible actions. Considering the needs of the busy professional with little time to cook, she could see that the second checkout stand would help handle the burst of traffic at 5 p.m. So would more parking in the alley. In addition, she felt she could take space currently used for selling munchies to students and offer prepared high-quality take-home foods instead. Professionals, unlike students, would not come shopping at midnight, so there was no need for very late hours. The busy professionals would appreciate adequate staffing after work and, perhaps, at lunchtime. Having a guiding policy helped create actions that were coordinated and concentrated, focusing her efforts.

COHERENT ACTION

Many people call the guiding policy "the strategy" and stop there. This is a mistake. Strategy is about action, about doing something. The kernel of a strategy must contain *action*. It does not need to point to all the actions that will be taken as events unfold, but there must be enough clarity about action to bring concepts down to earth. To have punch, actions should coordinate and build upon one another, focusing organizational energy.

Moving to Action

INSEAD, a global business school located in France, was the brainchild of Harvard professor General Georges F. Doriot. The INSEAD library holds a bronze statue of Doriot inscribed with his observation "Without action, the world would still be an idea."

In many situations, the main impediment to action is the forlorn hope that certain painful choices or actions can be avoided—that the whole long list of hoped-for "priorities" can all be achieved. It is the hard craft of strategy to decide which priority shall take precedence. Only then can action be taken. And, interestingly, there is no greater tool for sharpening strategic ideas than the necessity to act.

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The president of the European Business Group had a discrete private office in a classic London town home, just west of St. James' Park. I was there to discuss progress on the company's "Pan-European" initiative.

A consumer goods producer, the company had a typically complex international organization. There were country-based marketing organizations; globally run manufacturing operations; and four product development centers, one in North America, one in Japan, one in Germany, and one in the United Kingdom. Product managers were responsible for coordinating activities but had no direct authority. Products tended to be tailored to country or regional differences, partly as a result of some local acquisitions and partly due to perceptions of local differences in tastes.

Senior management believed that the company’s European business was too fragmented. They wanted most of the products offered in Europe to be Pan-European, exploiting greater economies of scale in both production and marketing. Management had spent time and effort communicating the message about a Pan-European product line and had created some mechanisms to bring it about. The heads of the country-based organizations were placed on a Pan-Europe Executive Committee, which met once a quarter. Developers from Germany and the United Kingdom were rotated between the two locations. A New Products group had been created to consult with all departments on opportunities for Pan-European concepts and brands. Part of each executive’s evaluation for promotion was based on his or her contribution to the Pan-European initiative. Despite these measures, nothing much had happened. The German and British developers each claimed that their initiatives were unsupported by the other. The one British-German joint initiative had not been picked up by the rest of the organization.

As we discussed the situation, my client’s frustration was evident. I stopped taking notes, and we both got up and walked over to the window, looking down on the mews houses below. “Suppose,” I said, “that this was really important, really top-priority critical. Suppose you absolutely had to get some Pan-European products developed and marketed in the next eighteen months or everything would collapse. What would you do then?”

“For one thing,” he said, throwing his arms up in mock surrender, “I would close one of the development groups. They spend more time bickering than developing.”

Then he thought for a moment and said, “I just might close both and start over in the Netherlands. There is a market-test office there we could use as a seed. We could take some of the best people from the UK and Germany and start fresh. Still, that doesn’t solve the problem of getting the country managers on board.”

“And the country managers’ lack of enthusiasm is because … ?” I asked.

“Well, each country manager has spent years understanding the special conditions in a country, tailoring products and marketing programs to that country’s local conditions. They don’t trust the Pan-European idea. The French don’t want to waste marketing efforts on products they see as ‘too British’ or ‘too German.’ And there really has not yet been a compelling Pan-European product that all could get behind. If it were already a success in three or four countries, the rest would get behind it. But everyone has their current portfolio of products to worry about.”

“Right,” I said. “Their jobs are running the present country-based system. And you want new Pan-European initiatives. Now, you can use a shoe to hammer a nail, but it will take a long time. Don’t you need a different tool for this task? If it were really important to get this done, I think you know how you would do it.”

“Of course,” he said. “We could have a single group develop, roll out, and market Pan-European products and take full profit responsibility.”

“At the same time,” I added, “you would have to intervene in the country-based system with special budget overrides for this initiative, promotions for people who help it along, and career problems for people who don’t.”

We moved back to the center of the office, and he sat at his desk, a position of authority. He looked at me and said, “That would be a very painful road. Many noses would get out of joint. It would be better to win people over to this point of view rather than force them over.”

“Right,” I said. “You would only take all those painful steps if it were really important to get action on this concept. Only if it were really important.”

It took another nine months for him to decide that the Pan-European initiative was indeed important and move to reorganize European operations. There was no magical solution to his problem of wanting strong country-based marketing, Pan-European initiatives, and no noses out of joint, all at the same time. As long as strategy remained at the level of intent and concept, the conflicts among various values and between the organization and the initiative remained tolerable. It was the imperative of action that forced a decision about which issue was actually the most important.

This executive’s problem was primarily organizational rather than rooted in product-market competition. Yet the kernel of strategy—a diagnosis, a guiding policy, and coherent action—applies to any complex setting. Here, as in so many situations, the required actions were not mysterious. The impediment was the hope that the pain of those actions could, somehow, be avoided. Indeed, we always hope that a brilliant insight or very clever design will allow us to accomplish several apparently conflicting objectives with a single stroke, and occasionally we are vouchsafed this kind of deliverance. Nevertheless, strategy is primarily about deciding what is truly important and focusing resources and action on that objective. It is a hard discipline because focusing on one thing slights another.

Coherence

The actions within the kernel of strategy should be coherent. That is, the resource deployments, policies, and maneuvers that are undertaken should be consistent and coordinated. The coordination of action provides the most basic source of leverage or advantage available in strategy.

In a fight, the simplest strategy is a feint to the left and then punch from the right, a coordination of movement in time and space. The simplest business strategy is to use knowledge gleaned by sales and marketing specialists to affect capacity expansion or product design decisions—coordination across functions and knowledge bases. Even when an organization has an apparently simple and basic source of advantage, such as being a low-cost producer, a close examination will always reveal a raft of interrelated mutually supporting policies that, in this case, keep costs low. Furthermore, it will be found that these costs are lower only for a certain type of products delivered under certain conditions. *Using* such a cost advantage to good effect will require the alignment of many actions and policies.

Strategic actions that are not coherent are either in conflict with one another or taken in pursuit of unrelated challenges. Consider Ford Motor Company. When Jacques Nasser was the CEO of Ford Europe and vice president of Ford product development, he told me, “Brand is the key to profits in the automobile industry.”[6] Moving into the corporate CEO spot in 1999, Nasser quickly acted to acquire Volvo, Jaguar, Land Rover, and Aston Martin. However, at the same time, the company’s original guiding policy of “economies of scale” was fully alive and kicking. A senior Ford executive told me in 2000: “You cannot be competitive in the automobile industry unless you produce at least one million units per year on a platform.” Thus, the actions of buying Volvo and Jaguar were conjoined with actions designed to put both brands on a common platform. Putting Jaguar and Volvo on the same platform dilutes the brand equity of both marques and annoys the most passionate customers, dealers, and service shops. Volvo buyers don’t want a “safe Jaguar”; they want a car that is uniquely safe. And Jaguar buyers want something more distinctive than a “sporty Volvo.” These two sets of concepts and actions were in conflict rather than being coherent.

What about a list of nonconflicting but uncoordinated actions? In 2003, I worked with a company whose initial “strategy” was to (1) close a plant in Akron and open a new plant in Mexico, (2) spend more on advertising, and (3) initiate a 360-degree feedback program. Now these actions may all have been good ideas, but they did not complement one another. They are “strategic” only in the sense that each probably requires the approval of top management. My view is that doing these things might be sound operational management, but it did not constitute a strategy. A strategy coordinates action to address a specific challenge. It is not defined by the pay grade of the person authorizing the action.

The idea that coordination, by itself, can be a source of advantage is a very deep principle. It is often underappreciated because people tend to think of coordination in terms of continuing mutual adjustments among agents. Strategic coordination, or coherence, is not ad hoc mutual adjustment. It is coherence imposed on a system by policy and design. More specifically, design is the engineering of fit among parts, specifying how actions and resources will be combined. (This approach to coherence is the subject of chapter 9, “Using Design.”)

Another powerful way to coordinate actions is by the specification of a proximate objective. By “proximate,” I mean a state of affairs close enough at hand to be feasible. If an objective is clear and feasible, it can help coordinate both problem solving and direct action. (You will find more about this important tool in chapter 7, “Proximate Objectives.”)

Strategy is visible as coordinated action *imposed* on a system. When I say strategy is “imposed,” I mean just that. It is an exercise in centralized power, used to overcome the natural workings of a system. This coordination is unnatural in the sense that it would not occur without the hand of strategy.

The idea of centralized direction may set off warning bells in a modern educated person. Why does it make sense to exercise centralized power when we know that many decisions are efficiently made on a decentralized basis? One of the great lessons of the twentieth century—the most dramatic controlled experiment in human history—was that centrally controlled economies are grossly inefficient. More people starved to death in Stalin's and Mao Tse-tung's centrally planned regimes than were killed in World War II. People continue to starve to death in North Korea today. In modern economies, trillions of decentralized choices are made each year, and this process can do a pretty good job of allocating certain kinds of scarce resources. Thus, when the price of gasoline rises, people start buying more fuel-efficient cars without any central planning. After a hurricane, when there is much to rebuild, wages rise, attracting more workers to the stricken area.

But decentralized decision making cannot do everything. In particular, it may fail when either the costs or benefits of actions are not borne by the decentralized actors. The split between the costs and benefits may occur across organizational units or between the present and the future. And decentralized coordination is difficult when benefits accrue only if decisions are properly coordinated. Of course, centrally designed policies can also fail if the decision makers are foolish, in the pay of special interest groups, or simply choose incorrectly.

As a simple example, salespeople love to please customers with rush orders, and manufacturing people prefer long uninterrupted production runs. But you cannot have long production runs and handle unexpected rush orders all at the same time. It takes policies devised to benefit the whole to sort out this conflict.

On a larger canvas, in World War II, President Franklin D. Roosevelt coordinated political, economic, and military power to defeat Nazi Germany, using the United States' productive capacity to support the Soviet Union, thus allowing it to survive and degrade the Nazi war machine before Americans landed in Normandy. Another element of his strategy, one with great consequences, was to focus the bulk of American resources to first winning in Europe before fully taking on Japan, a complex coordination of forces over time. Neither of these crucial policies would have emerged out of decentralized decision making among the Departments of State and War, the various war production boards, and multiple military commands.

On the other hand, the potential gains to coordination do not mean that more centrally directed coordination is always a good thing. Coordination is costly, because it fights against the gains to specialization, the most basic economies in organized activity. To specialize in something is, roughly speaking, to be left alone to do just that thing and not be bothered with other tasks, interruptions, and other agents' agendas. As is clear to anyone who has belonged to a coordinating committee, coordination interrupts and de-specializes people.

Thus, we should seek coordinated policies only when the gains are very large. There will be costs to demanding coordination, because it will ride roughshod over economies of specialization and more nuanced local responses. The brilliance of good organization is not in making sure that everything is connected to everything else. Down that road lies a frozen maladaptive stasis. Good strategy and good organization lie in specializing on the right activities and imposing only the essential amount of coordination.