

Immediacy of Strategic Uncertainties

Events or trends associated with strategic uncertainties may have a high impact, but such a low probability of occurrence that it is not worth actively expending resources to gather or analyze information. Similarly, if occurrence is far in the future relative to the strategic-decision horizon, then it may be of little concern. Thus, the harnessing of tide energy may be so unlikely or may occur so far in the future that it is of no concern to a utility company. Finally, consider the reaction time available to a firm compared with the reaction time likely needed. After a trend or event crystallizes, a firm needs to develop a reaction strategy. If the available reaction time is inadequate, it becomes important to reinvest and anticipate emerging trends and events better so that future reaction strategies can be initiated sooner.

Managing Strategic Uncertainties

Figure 5.4 suggests a categorization of strategic uncertainties for a given business. If both immediacy and impact are low, then a low level of monitoring and analysis is recommended. If the impact is thought to be low but the immediacy is high, the area may merit monitoring and analysis. If the immediacy is low and the impact high, then the area may require more in-depth monitoring and analysis and contingent strategies may be considered but not necessarily developed and implemented. When both immediacy and potential impact of the underlying trends and events are high, then an in-depth analysis will be appropriate, as will be the development of reaction plans or strategies.

Scenario Analysis

Scenario analysis can also help firms deal with strategic uncertainties. The difference between impact analysis and scenario analysis is that instead of investing in more information search and analysis to reduce uncertainty, the firm creates a small number of environmental scenarios, assesses their likelihood and impact, and then uses this analysis to develop or test potential strategies.

There are two types of scenario analyses. In the first type, strategy-developing scenarios, the object is to provide insights into future potential environments and then use these insights to evaluate existing business strategies and stimulate the creation of new ones. Such analyses can help create contingency plans to guard against disasters—an airline adjusting to a terror incident, for example, or a pharmaceutical company reacting to a product safety problem. They can also suggest

		Immediacy of Threats	
Impact of Threats	High	Low	High
	Monitor and analyze; long-term contingent strategies outlined	Monitor and analyze in more depth; perform scenario analysis and develop contingent strategies in depth	Monitor and analyze for changes; outline a short-term response
Low	Monitor for changes; low investments		

Figure 5.4 Impact Analysis

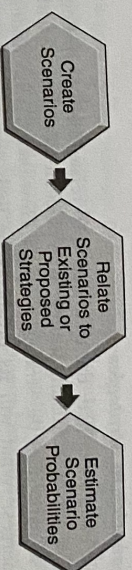


Figure 5.5 Scenario Analysis

investment strategies that enable the organization to capitalize on future opportunities caused by customer trends or technological breakthroughs.

In the second type of analysis, decision-driven scenarios, a strategy is proposed and tested against several scenarios.³⁶ The goal is to challenge the strategy, thereby helping to make the go/no-go decision and suggesting ways to make the strategy more likely to withstand environmental forces. If the decision is to enter a market with a technology strategy, alternative scenarios could be built around variables such as marketplace acceptance of the technology, regulations, and competitor response.

In both analyses, a scenario analysis will involve three general steps—create scenarios, relate those scenarios to existing or potential strategies, and assess the probability of the scenarios (see Figure 5.5).

Step 1: Create Scenarios

Strategic uncertainties can drive scenario development. The impact analysis will identify the strategic uncertainty with the highest priority for a firm. This source of uncertainty should be the focus of the scenario. A manufacturer of a medical imaging device may want to know whether a technological advance will allow its machine to be made at a substantially lower cost. A farm equipment manufacturer or ski area operator may believe that the weather—for example, whether a drought will continue—is the most important area of uncertainty. A server firm may want to know whether a single software standard will emerge or if multiple standards will coexist. The chosen uncertainty could then stimulate two or more scenarios.

When a set of scenarios is based largely on a single strategic uncertainty, the scenarios themselves can usually be enriched by identifying related events and circumstances. Thus, an inflation-stimulated recession scenario would be expected to generate a host of conditions for the appliance industry, such as price increases and retail failures. It is sometimes useful to generate scenarios based on possible outcomes: optimistic, pessimistic, and most likely. The consideration of a pessimistic scenario helps test existing assumptions in a firm's strategic plan. The "what-if" exercises in a scenario analysis provide a nonthreatening way to consider the possibility of clouds or even rain on the picnic.

Often several variables are relevant to the future period of interest. The combination can define a relatively large number of scenarios. For example, a large greeting-card firm might consider three variables as important: the success of small boutique card companies, the creation and sharing of e-cards, and the nature of future distribution channels. The combination can result in many possible scenarios. Experience has shown that two or three scenarios are the ideal number with which to work; if a larger number is used, the process becomes unwieldy, and any value is largely lost. Thus, it is important to reduce the number of scenarios by creating a small set that ideally includes those that are plausible/credible and those that represent departures from the present substantial enough to affect strategy development.