

INTELLIGENT STRATEGY

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Introduction

This article focuses on designing strategy as an on going process, building in adaptation, learning, and creativity. The current economic news from Russia is good, but reality is that things will change. So the concern here is with strategy as a self adaptive process that enables organizations to respond appropriately to new, and often unexpected events. Looked at from another angle, the subject matter is the problem of sustaining performance (measured by competitive advantage, competitiveness, or just survival) into the long term.

Von Hayekⁱ identified the key weakness of central planning as the near impossibility and the huge cost to the central planning agency, of accumulating the information required to balance supply and demand for all the goods and services produced in a modern economy. His solution was decentralization: allowing individuals with knowledge of local circumstances to deal with the problems of matching supply and demand through markets. In the language of information technology, markets are distributed information systems.

The problem of markets is two fold. Both affect Russia profoundly. The first is that markets need the institutions of capitalism to function properly (laws, regulations, traditions). Institutions take time to create, and they do not emerge spontaneously as a result of actions like privatisation. The naivety the foreign advisersⁱⁱ of *Perestroika*, was to assume that they would emerge spontaneously: Russia still bears the cost of this assumption. The second problem of markets is that they are distributed information systems, but they are not intelligent. Organizations are required to design strategies intelligently. How can this be done?

Organizations are affected by sudden shifts in circumstances that arise from complex interactions between variables, rather than simple cause and effect relations. In the next section, the variables affecting the changing state of the Russian economy are sketched. Governments should think of strategy in terms of continuous adaptation: that is as a *self adaptive* process, at every level in organizations and institutions, that

enables society to take advantage of new events. The last section of the paper discusses intelligent strategy, a *self adaptive* or *autocatalytic* process, in terms of the Enneagram (illustrated in Figure 2 below). The Enneagram, an ancient symbol of Chaldean origin, is found in the traditions of Christianity, Zoroastrianism, Buddhism, and Sufism. In the early twentieth century, it was expounded by the Russians G.I. Gurdjieff and P.D.Ouspensky (see Bennett, 1966), and currently it is used in some personal development programmes, notably at the Academy of National Economy.

I define strategy as a continuous attempt, by an organization, (business enterprises, governments, or any organizations for that matter) to reconcile objectives with i. the opportunities presented by the business environment, and ii. capabilities. As a result of this adaptive process, economies and businesses evolve. Figure 1 illustrates the definition of strategy.

INSERT FIGURE 1 NEAR HERE

The strategy triangle

The business environment might be described as the *system state* of an organization. It describes where it is now, and reflects historic as well as current factors - economic, social, political or technological. An organization's capabilities consist of i. the resources at its disposal, and ii. the effectiveness with which it can connect, or network these resources (human and physical capital, raw materials, and less tangible capital tied up in its reputation, brands, and image). Resources constitute a stock of assets: connections turn these assets into intelligence - distributed intelligence. Distributed intelligence is shared learning. In the current *system state* of the global economy, is their distributed intelligence because this determines the ability of organizations to adapt and evolve. "*The only thing that gives an organization a competitive edge- the only thing that is sustainable- is what it knows, how it uses what it knows and how fast it can learn something new.*"ⁱⁱⁱⁱ The quotation applies equally to governments and to businesses. Currently it is applied to new economy organizations, but I suspect it has always been so. *How to learn? How to encourage and spread learning in organizations?* These are questions I will return to in the last section. First let us look at the state of the Russian economy - the macroeconomic aspects of the Russian business environment or *system state*.

The state of the Russian economy

The main indicators of recovery in Russia are good. Lower inflation should continue, rising annually at between 15-16%; mostly as a result of a stable exchange rate, and in spite of the inflationary effects of the recent utility price rise. A rate of economic growth of 4% is expected, as a result of good external trade performance and high domestic demand. This is the highest annual growth rate since the fall of communism. Important economic reforms by the Russian government, especially the reform of personal taxation and social security, should help to create the institutions needed in a market economy. The new economic programme is likely to win the approval of the IMF and World Bank, thus providing encouragement for inward investment into Russia.

Reservations about Russian government exist, especially due to events in August 2000, but the international view is mostly positive. The move towards radical reform is seen to have Mr Putin's active support. The main factors driving the performance of the Russian stock market are the rapid rise in the price of crude oil, positive response to government economic reforms, the closing of the London Club restructuring deal, and the immanent upgrade of Russia's credit rating. Confidence in the domestic economy has been reflected in the performance of the Russian stock market and especially in telecommunication and utility stocks.

KEY INDICATORS	1998 (actual)	1999 (actual)	2000 (expected)	2001 (expected)
GDP growth (real)%	-4.9	3.2	4.0	4.0
Inflation %	27.7	85.8	17.9	14.0
Unemployment %	13.3	14.2	13.8	12.4
Refinancing rate (end of year)%	58.0	55.0	24.0	20.0
EPS growth %	na	na	207.2	10.2
P/E ratios	na	24.9	8.1	7.4
Current Account balance (billion US\$)	2.4	25.0	33.0	21.0
FDI inflow (billion US\$)	1.2	0.7	4.0	7.0
Gross external Debt gross (billion US\$)	180.0	185.4	179.4	181.1
External debt service(billion US\$)	21.6	22.0	22.0	22.0
Exchange rate/US\$ (average)	9.9	24.7	28.9	31.3

Source ABN-AMBRO

Some statistics of the past and forecasts for the future are included in Table 1. A falling refinancing rate reflects lower inflationary expectations. Earnings per share growth (EPS growth) and price earnings ratios (P/E ratios) reflect reasonably optimistic expectations about the future performance both of Russian companies and of the economy as a whole. Positive current account balances are expected, as well as moderate increases in inflows of foreign direct investment (FDI).

The future

Of course no detailed exact blueprint for future strategy exists. One certainty is that things will change in surprising and unexpected ways. The Russian stock market will continue to be affected by political uncertainties, and volatility in major world markets. The high price of oil may not last. Indeed the high oil price may trigger a major recession in the West, comparable to that brought about by the oil price shock of the early 1970's^{iv}. Generally major stock markets appear to be overvalued in terms of price earnings ratios and since stocks make up a major component of personal wealth, especially in the USA, a fall in stock prices could bring about a downward spiral in demand, trade, and economic growth. On the other hand if the optimists are right, innovation and growth in the new economy ICT industries (information and telecommunications) may bring about the end of the capitalist business cycle. Rather unlikely, but a possibility.

Summarising the last paragraph, there are many scenarios. We can forecast reasonably accurately for the short term. Data on expectations in Table 1 is likely to be fairly accurate at least for one year ahead. The reality is that things are uncertain. So learning and adaptation by organizations, businesses or governments, is needed to achieve competitiveness and growth.

The Enneagram

It is impossible to derive a detailed blueprint for policy: Kolmogorov^v entropy spells out the theoretical basis why not: *the further we project into the future, the less useful is current information*. Practical experience of Soviet planning provides a real life example why not. But we can say something useful about the strategic process.

One framework for doing this is provided by the Enneagram. The Enneagram has an ancient tradition. It can be and has been applied to processes of learning and

adaptation perhaps for hundreds of years. I have used it in many consultancy and research situations. Here it is applied to the creative process of developing strategy in the face of uncertainty.

The strategy process can be broken down into a number of stages:

- Deciding objectives
- Deciding on finance
- Considering alternative strategies and alternatives
- Choosing a strategy
- Implementing the strategy
- Adapting the strategy as circumstances change.

Obviously, a complete essay, or even series of books could be written on each stage. Since organizations and their environments are complex; affected by interdependent factors, both internal and external, that produce non-linearity and unpredictability, procedures for designing strategy must build in the potential for learning and adaptation.

INSERT FIGURE 2 NEAR HERE

The Enneagram

The Enneagram should be thought of as a creative tool. It is defined by the dynamic pattern that follows the sequence 1,4,2,8, 5,7,1,4,2 . I have embedded the strategy triangle (Figure 1) in that shape. Note that the sequence spells out the irrational number derived from the fractions, $1/7$ (0.42851), $2/7$ (0. 85142), $3/7$ (0.4285714), and so on. Also note that the shape is divided into two linked sections defined by 1,4,2, on the circle and 8,5,7. The first part is concerned *recognizing potential*; aligning feasible objectives with alternative scenarios for policy. The second part is concerned with *realizing potential* through choice, implementation, and adaptation. Linkage between the two parts is provided by adaptation/alternative scenario axis, (8,2) and the implementation/objectives axis (7,1): learning requires adaptation to alternative scenarios as time unfolds, and adjustment of aims in the light of attempts at implementation. The Latin root of the English word intelligent is *intellegere, to choose between-* in this case, between objectives and scenarios..

Traditionally the Enneagram is a mandala, a pattern for contemplation, linking *Being*, that is, individual and social enlightenment, with *Becoming*, that is, change. Whereas markets are, according to Hayek, distributed information systems, the Enneagram is concerned with distributed learning, and self adaptation to new circumstances.

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ⁱ F.A. von Hayek, (1945).

ⁱⁱ See for example Jeffrey Sachs (1990,1994)

ⁱⁱⁱ Prusak, (1996), quoted in McKelvey (2000).

^{iv} This happened as a result of the Arab embargo on oil exports after the Arab Israeli War.

^v See Prigogine (1980)