



SentinelReward
Your Risk Partner

“Managing Strategic Risk in a
VUCA/TUNA Environment”

“Managing Strategic Risk in a VUCA/TUNA Environment”

Introduction

The world of today is arguably more dynamic and uncertain than any era heretofore. Strategic execution is exposed to highly uncertain environments as the new normal. Thus, entities who want to survive in the medium to long term may need to build enhanced strategy development capability. The author has over 25 years' experience in senior executive roles in financial services across Europe, UK, Asia, and North America. Working in treasury, and capital markets brought exposure to best practice in contingency planning and scenario planning including wargaming techniques. Working in corporate strategy brought exposure to best practice in strategy formulation. This paper contemplates combining this experience and associated learnings to identify an enhanced strategy development process for entities in increasingly uncertain environments. The focus of the paper is to consider the relevance of corporate wargaming considering the prevailing volatile environment and how this tool might be integrated into an enhanced strategy development process.

Uncertain Environment

In the digital era one key element to keep in mind in strategy development is the uncertain environment in which we operate. Traditional planning and forecasting processes are still important but those responsible for strategy implementation would be wise to note the article 'Plotting Strategy in a dynamic world' where Teece et al tell us:

“Companies can no longer rely on traditional forecasting exercises to spot — and capitalize on — emerging threats and opportunities”.

Kodak, Blockbuster Video, Nokia, Blackberry the list goes on, how much better might these companies have fared if they had a strategy capable of surviving the uncertain environments they encountered. More recently we have witnessed Covid 19, and the failures of WeWork and Silicon Valley Bank, and soon a US election that could have ramifications that are extremely hard to predict. Arguably never has it been more important to understand what good strategy looks like in a VUCA environment. Volatility, uncertainty, complexity, and ambiguity look to be only increasing, and the same can be said of the evolution further towards a TUNA environment, turbulent, uncertain, novel, and ambiguous. Professor Stephan Meier in Columbia Business school put it well in saying:

In today's world, there is great uncertainty. With all the rapid change, it can feel like a new world almost every day.

A good starting point to understanding what is required to frame a good strategy in an uncertain environment is the 'Strategy Under Uncertainty' article from Courtney et al, which tells us:

“In order to perform the kinds of analysis appropriate to high levels of uncertainty, many companies will need to supplement their standard strategy tool kit”.

Furthermore, in *Strategy Tools for a Shifting Landscape*, Michael Jacobides notes:

“Identifying characters, describing their roles, and coming up with plots, subplots and story lines offers a simple but rigorous approach to strategy planning”.

Reflecting on these observations, and the experience of the author in the balance sheet strategy area, a question presented. Could the prevailing environment and the authors learnings of the past be complimentary in evidencing a rationale for an enhanced overall strategy development approach. In the next section that notion will be examined further.

Strategic Balance Sheet Management

Over many years the author has been responsible for the strategic management of bank balance sheets, including liquidity, funding, capital optimisation and foreign exchange and interest rate risk management, contingency and disaster planning. Chat GPT will tell you balance sheet management is:

“Managing a company’s assets, liabilities, and equity to optimise financial performance and risk”.

Fulfilling such a role results in having a real influence on the creation of a robust and sustaining strategy for the entirety of a bank entity. One very interesting part of the role was holding responsibility for a bank’s recovery and resolution plan. An actuarial definition of such a plan is as follows:

“A recovery plan identifies options to restore financial strength when the company comes under severe stress. Resolution refers to the situation when a firm is no longer viable and has no reasonable prospect of becoming so”.

It will come as no surprise to the reader that post the Great Financial Crisis (GFC) the requirement to have such a plan in place has become a regulatory imperative for banks. In considering the ‘recovery’ element, one key requirement is to have both a Contingency Funding Plan and Disaster Plan in place. The nomenclature for both these plans is replete, they do what they say on the tin. Best practice demands that such plans are tested on an annual basis, and so over many years the author has been responsible for balance sheet and treasury related scenario planning including wargaming exercises. Examples of simulations executed included deterioration in the European sovereign debt crisis, Brexit and persistent lower for longer interest rates.

In the experience of the author simulations were especially powerful where scenario details were kept entirely confidential from the participants. C-level and senior management were exposed to scenario simulations where executives had to make ‘live’ decisions. Detailed comprehensive preparation was key, as was identifying effective scenarios, Brian Huffman, a Professor of Management put it well in saying:

“Synthesis of something unlikely is much harder than of something likely”.

Identifying unlikely, but plausible scenarios takes a lot of hard work and preparation. Scenario planning is all about being prepared. Implicit to preparation is contemplation. Bank balance sheet management best practice entails a minimum of an annual contingency funding plan review and including a wargaming exercise. In the experience of the author the learnings from such exercises were fundamental. On many occasions senior executives would say things like:

- “I learned so much”.
- “I would never have foreseen such an occurrence”.
- “I was not aware we had that dependency”.
- “We need to eliminate that exposure in light of this exercise”.
- “Count me in for next year’s exercise”.

All the above created a question in the mind of the author. Why not make a corporate wargaming exercise an essential element to the strategy development process and especially so given the growing uncertainty in the corporate environment. The discipline to hold such an exercise on at least an annual basis (if not more) could serve as a real enhancement to overall strategy formulation.

Corporate Wargaming

The term wargaming is derived from the Prussian term Kriegsspiel, the literal translation being ‘war considered as a game’. The author, and likely readers, are in no doubt aware that war is no game, and neither is corporate strategy. It is beyond the scope of this paper to do full justice to a considered analysis of corporate or business wargaming but should the reader desire to do a deep dive into the subject a good place to start would be the book, ‘Winning the Uncertainty Game’ by Daniel F. Oriesek and Jan O Schwarz.

In “The Future of Management”, Gary Hamel defines corporate wargaming thus:

“Corporate wargaming is a disciplined process whereby participants can realistically explore future uncertainties of the competitive environment and create strategic options in a risk-free setting”.

Arguably such a capability is most compelling in an uncertain environment as it strengthens muscle memory ahead of an unpredictable event. Yet the technique does not tend to be used as much as some other classical strategic management approaches and tools such as a PESTEL or SAFe analysis. It is difficult to identify any detailed studies or research on the area, but estimates are that fewer than one in four companies use the corporate wargaming technique. The reason for that may in some part be illustrated by what is required to successfully complete such an exercise, there is a lot of work involved. Nonetheless in the experience of the author, the argument for adopting the corporate wargaming technique is extremely compelling as it hones the strategic radar of senior management. There are three critical stages to successfully set up, structure and perform a corporate wargame simulation.

Preparation and Plan

Preparation is fundamental to an effective corporate wargaming simulation. One key is that senior management, and all participants need to give the exercise the respect it is due and in the experience of the author that typically means the CEO of the entity needs to underline its importance in no uncertain terms. The following needs to be crystal clear:

- Who is required to participate
- What role do they fulfil
- Where will the exercise happen
- What are the objectives of the exercise
- What are the rules of the exercise

Note, the Team who prepare the actual scenario for simulation must do so in a silo away from the exercise participants. Confidentiality is critical, there can be no leakage of any element of the scenario as that would serve to make the simulation less 'real'.

Pre-Briefing Participants

Participants must acknowledge and accept that they will be vulnerable in the exercise, indeed in many ways this is the true power of the practice in creating 'real life what would you do?' moments.

Pre-reading material will be required ahead of the exercise that provides all need-to-know information. It is imperative that participants study this, thus underlining again the importance of buy in. Preparing these materials will take considerable effort and should be done to a high-quality standard thus reinforcing the efficacy of the exercise.

Role-Playing Session

This is where the scenario plays out in real time. Possible scenarios could include, Product launches, Legislative changes, Competitor Actions, Emergence of disruptive technology.

The scenario will be introduced to the group. Participants need to act as if the scenario were real, think critically, anticipate change, and be prepared to adapt.

There will be defined time limit for the exercise. Further information will be introduced to the participant group if it is relevant or relates to consequences of decisions such as, financial impacts, regulatory actions, or media coverage. Note some participants will be in the room but some may also be 'on call'. A facilitator is observing and should only interject if exercise rules are not being followed.

Once the exercise is complete work will begin on the debriefing session, an objective analysis of outcomes where participants can consider lessons learned and potential changes to strategic intent going forwards.

Clearly there is a considerable amount of work to be done to make a corporate wargaming exercise work to optimal effect, a useful time then to consider the benefits and challenges of the wargaming approach.

Benefits

- **Collaboration:** The exercises are powerful in encouraging cross departmental cooperation and communication. The Team sees the benefit of working together effectively.
- **Pressure Test:** Companies can dry run a strategy in a staged challenging (VUCA/TUNA) environment but risk-free laboratory. This can often result in more informed strategic refinement resulting in greater confidence and buy in from the whole team of the final 'proof tested' strategy.
- **Creativity:** Forcing participants to act 'in the moment' often results in innovative outcomes.
- **Culture check:** Live scenarios tend to force out realities you may not have been aware of. Vulnerabilities like a myopic 'group think' approach will tend to be exposed in more stressed environments.
- **Risk Management:** Useful in identifying controls and mitigations for risks that are inherent in the business.
- **Flight Simulator:** Fear of the unknown often weighs on teams, wargaming enables decision testing, learning and experimentation relating to plausible but potentially challenging scenarios in a safe environment. In short it can serve to reduce corporate anxiety in Teams.

Challenges

- **Resource Intensive:** Significant pre and post exercise work is required. Senior management need to be made available and be prepared to be vulnerable in the actual exercise. Many companies will struggle with this type of resource commitment if they have limited capacity.
- **Engagement:** If participants do not engage professionally the exercise will be a failure. Typically, the CEO and senior management will need to underline the importance of engagement which means they need to buy in themselves.
- **Complexity:** Designing scenarios is not easy and does require deep knowledge of the organisation and its environment. Fact can be, and often is stranger than fiction.
- **Confidentiality:** It is imperative that wargaming sessions take confidentiality into account. There are two levels here. Firstly, leakage from the group devising the scenarios would serve to massively undermine the exercise.

Secondly, in these exercises the entity is trying to identify vulnerabilities, and it is imperative that these do not become exposed to competitors until ideally controls or mitigations are devised.

Considering the above many organisations choose to engage external consultants to work with the internal team to execute a wargaming exercise optimally. External specialists can streamline the process given their familiarity with best practice thus saving considerable time recognising resource constraints for the entity. An external party can also assist in providing ideas for risk mitigation, facilitation of the exercise and objective preparation of a debrief. One caveat however is that any external consultant will still need access to key staff in framing the exercise to ensure there is a bespoke informed approach, and senior management will need to participate in the actual exercise.

Corporate Wargaming Exemplars

There is a myriad of different potential ‘use cases’ for corporate wargaming. High level areas of focus include Strategy diligence, Product launch, New Market Entry, Competitor Analysis, Customer Experience, Stakeholder Management, Disaster Planning, the list goes on and on and in many ways is only limited by the informed imagination of the simulation author. By their nature examples of corporate wargames tend to be hard to find due to sensitivity and confidentiality, there are however some useful examples of note.

Danone successfully used corporate wargaming to enhance their strategic thinking around taking a leadership position in the plant-based foods sector. Manuela Borella, a Danone Board Member and VP for Plant Based acceleration noted:

“With the business wargaming sessions we were definitely able to unlock country business units...I would say it has been quite a milestone to really open up a new chapter in strategy”.

Microsoft have often commented in the public domain on their use of red team versus blue team business wargames where the red team are cyber attackers looking to battle a blue team in the Microsoft Office 365 security division.

Cognosis, a London strategy consultancy that has been called in by Diageo, InterContinental Hotels Group and Red Bull to run business wargaming exercises and Pia Kirkland a consultant at Cognosis says:

“Ultimately, it’s used to simulate competitive scenarios to test strategies... The beauty of wargaming is that it enables you to do all those things in a controlled and risk-free environment.”

Shell employed Chris Paton and Quirk Solutions to wargame scenarios around decommissioning the Brent Oil rig in the North Sea to better understand how different stakeholder groups would react. Internal teams fulfilled stakeholder roles in the wargame, such as the fisheries group, the public, environmentalists, and competitors. A Shell project manager noted that the wargame produced more useful output in one day than three months of broader project work around the task. Patton a former Lieutenant Colonel in the Royal

Marines noted that many companies tend to think only about the competitor dimension in business wargaming but that in his opinion, is less than five percent of the most relevant use cases.

The above examples are demonstrable of the potential power of applying a wargaming discipline, and as VUCA evolves to TUNA and indeed beyond, the potential benefits of incorporating a corporate wargaming capability into a strategy development tool kit seem compelling, the next question is how might that work in practice?

Incorporating War Gaming into Strategy Development

Strikingly, in the experience of the author, Strategy Development Frameworks (SDF's) are a rare sight. This is remarkable given every business needs to have a strategy. Creating an SDF for an entity is extremely helpful as it forces the creator to go back to first principles and creates an effective means of enforcing discipline on the strategy development process. An effective SDF should encompass the approach to framing commercial rationale, client/customer deliverables and the capability required to deliver on customer propositions over time. Another critical element to strategy development that should be included in the SDF is a symbiotic Strategy Risk Assessment (SRA). The SRA is a means to sanity check and diligence the strategy of an entity.

It is as a subset to this element, that the author believes, including a corporate wargaming exercise could be most effective. Imagine a strategy forged in the absence of any risk consideration. An arresting thought. Would you wish to invest in an entity with such a myopic approach? The author defines strategic risk management thus:

“The process by which the strategy of an organisation is formally assessed for any potential risks implicit and explicit to that strategy”.

In the experience of the author the best tangible exponent of the effectiveness of strategic risk management is a SRA. In a financial services entity, a comprehensive SRA should include workshops with the lines of business and relevant support functions focusing specifically on the new entity strategy. The SRA would be conducted in tandem with the Banks formal capital, liquidity, and prudential risk assessment activities. Workshops provide the opportunity to consider bespoke strategy scenarios with multi-disciplinary teams and can force out areas for consideration that might not have presented otherwise. This is where the author would suggest there is the opportunity for an additional tangential element concurrently. Namely, a corporate wargaming exercise as part of the overall strategy development cycle thus more fully closing out a thorough diligence of the entity strategy.

In ‘Are you sure you have a strategy’ Hambrick and Fredrickson talk of seven tests to test the quality of your strategy, incorporating environmental, resource, sustainability, consistency, and implementation. Wargaming could provide a means to stress testing some or all these dimensions regarding a final draft entity strategy. Unlike scenario analysis wargaming enables review of behavioural activity and the live interaction of multiple variables. It is not all encompassing but it does contribute to a more comprehensive overall diligence of strategy.

Conclusion

The author argues that in the prevailing VUCA/TUNA environment persisting today that the rationale for including corporate wargaming as part of an entities strategy development cycle has never been more compelling. Over the past two decades the author has witnessed corporate wargaming scenario simulation resulting in more considered strategic intent in the balance sheet management world and believes applying a similar repeatable approach in the broader strategy world is logical. The corporate wargaming approach certainly respects Professor Michael Porter's view that:

"The essence of strategy is choosing what not to do".

An article in the MIT Sloan review 'Using scenario planning to reshape strategic planning', put it very well:

"Rather than trying to predict the future, organisations need to strengthen their ability to cope with uncertainty".

Combining corporate wargaming with scenario analysis is powerful. By its nature this requires the preparation and contemplation of future plausible but uncertain scenarios and then releasing those scenarios into a simulation environment where second order behavioural impacts can be witnessed that would be very difficult to identify otherwise. In summary corporate wargaming is about being prepared. Implicit to preparation is contemplation. The power of corporate wargaming scenarios for strategy decision development is in the contemplation and simulation, not the prediction. It is the contemplation and simulation that typically results in an evolution towards a more robust strategic approach.

In the experience of the author most corporate entities instinctively understand the potential value of wargaming to make strategy development more robust. Unfortunately, they often lack the capacity and expertise to execute on a wargaming exercise. Nonetheless giving the prevailing and increasingly uncertain environment it may well be worthwhile to engage an external consultant who can expedite corporate wargaming execution. Noting that even if an external consultant is employed it is still imperative to recognise that senior management engagement and commitment will be required. By incorporating such an exercise into a strategy development framework and strategic risk assessment there is also a unique opportunity to bring cross departmental collaboration and integrate it into some form of annual or semi-annual corporate event. Frame the strategy, game the strategy, and celebrate ownership and buy in to the strategy.

Bibliography

- Business Wargaming, Chris Patton, Quirk Consulting, YouTube, 2021.
- Courtney, H., Kirkland, J. and Viguerie, P. (1997), Strategy Under Uncertainty, Harvard Business Review, November-December, pp. 67-79.
- Coyne, A, IT News, 'How Microsoft uses Wargames to fight attackers', October 2013.
- Dornbrack, J, Business Leader 'The Art of Business Wargaming', February 2024.
- Frigo, M.L. and Anderson, R.J. Strategic Risk Management: A Foundation for Improving Enterprise Risk Management and Governance. The Journal of Corporate Accounting & Finance, March/April 2011, pp 81-87
- Gardere, N. 'Danone's secret weapon for agile decision-making: Wargaming'
- Hambrick, D. C. and Fredrickson, J. W. (2005), Are You Sure You Have a Strategy? Academy of Management Executive, Vol. 15, No. 4, pp. 51-62.
- Hamel G, "The Future of Management: How to Create an organization to fit the future", 2007.
- Huffman, B. University of Wisconsin-River Falls, "Synthesis of something unlikely is much harder than of something likely".
- Jacobides, M. G. (2010), Strategy Tools for a Shifting Landscape, Harvard Business Review, January-February, pp. 77-84.
- LBS Blog, 'Successful professional wargames'.
- Meier, S, "In today's world, there is great uncertainty. With all the rapid change, it can feel like a new world almost every day", Columbia Business School, 2024.
- Oriesek, D.F, Schwarz, J.O, 'Winning the Uncertainty Game, Turning Strategic Intent into Results with Wargaming', Routeledge, 2021.
- Phadis, S., Caplice, C. and Sheffi, Y. How Scenario Planning Influences Strategic Decisions. MIT Sloan Management Review, Summer 2016, pp23-27.
- Porter, Michael. What is strategy? HBR, November 1996.
- Ramírez, R., Churchhouse, S., Palermo, A. and Hoffmann, J. Using Scenario Planning to Reshape Strategy. MIT Sloan Management Review, Summer 2017. Volume 58, Number 4, pp30-37.
- Teece, D. J., Rospin, P. G. and Cox, D. R. (2020), Plotting Strategy in a Dynamic World, MIT Sloan Management Review, Fall, pp. 28-33.
- Walton, A, Competitive Intelligence Alliance, 'A guide to business wargaming for strategy planning', February 2024.