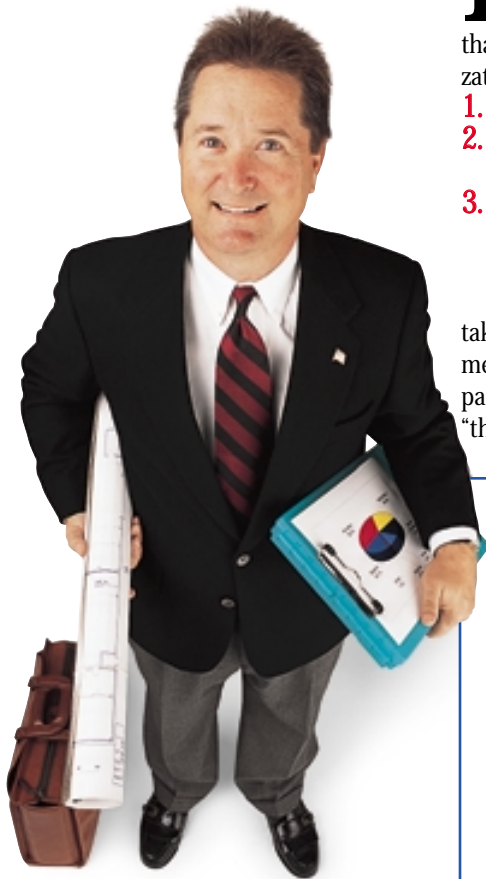


Business basics: what and how

by Art Raymond
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Every business owner and senior manager is responsible for answering three key questions that guide the activities of their organization:

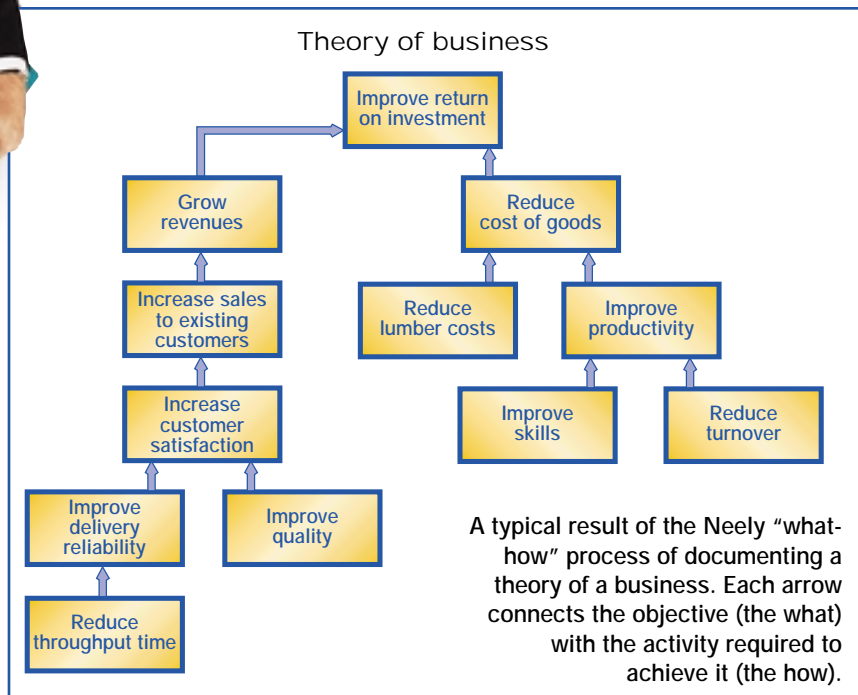
1. Who are their customers?
2. What is their offering — the products and services they sell?
3. How is the company enticing those customers to buy its offering and making a profit?

The answers to these questions, taken together, form what management guru Peter Drucker calls a company's theory of the business. A good "theory" provides a company's employ-

ees a clear definition of who to sell to and who not to sell to, plus which products to offer and which not to offer. More importantly, the theory guides decisions on the 'how' — what to do and what not to do to satisfy customers while making a profit.

Developing a theory

All companies need a clear theory of business. How do you go about documenting the theory of your business? One useful method is the Neely "what-how" process. This was named for Dr. Andy Neely, a management professor at the Universi-



ty of Cambridge.

You need a large sheet of paper or whiteboard plus two post-it notes, one labeled WHAT and the other HOW. Next assemble your senior management team. Stick the WHAT post-it on the whiteboard and ask the team what they are trying to achieve. Most managers first answer with a financial objective like "making an 8 percent operating profit" or "improving the company's value." Record the first response, move the HOW post-it beneath that entry, and ask your team how they propose to achieve that result. Multiple hows are typical at this point in the process. For instance, team members may indicate the needs to grow revenues, improve quality and reduce cost of goods. One at a time place the WHAT post-it above the reply, move the HOW post-it below the entry, and again ask how they propose to achieve that result.

Continue this process until you have developed a hierarchy of whats and hows. The illustration shows a typical result. Each arrow connects the objective (the what) with the activity required to achieve it (the how).

During the process you may find it useful to develop "whats" in four key areas of your business:

1. Financial — What financial targets must you meet? One of these "whats" is typically the primary objective of the business and thus should be located at the top of your graphic.
2. Customer — What must you do to satisfy your customers?
3. Process — What activities must you excel at?
4. People — What human resources must be developed?

Testing your theory

Once you have a first draft theory of your business, test the relationships between the whats and hows. Do your hows actually result in your whats? For example, the management team must decide whether or not improving quality will actually result in increased sales to existing customers. Keep working through the relationships until the assumptions underlying your theory fit.

Updating your theory

All great companies have a great theory of their business. But over time the world changes. Different customers may become the right customers. New products may become the right products. These changes demand a new priority of activities that determine how the business is con-

ducted. With these changes even the greatest companies may find their theory of business broken.

Take IBM in the early '80s. Big Blue at that time believed that the future of computing lay with powerful mainframes. After all, the company had bet its existence on the System *continued*



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raymond's view

360. Then came the personal computer. IBM initially thought that the lack of computing power, speed and storage would condemn the PC to novelty status. But the marketplace spoke otherwise, and thousands of Apples found their way into homes and businesses. Seeing a crack in the theory of its business, IBM quickly refocused assets on developing a better PC. That version, powered by Intel processors and driven by Microsoft operating system, became the industry standard.

Stay alert

To prevent obsolescence in the theory of your business, stay alert by:

- ▶ **Abandoning products, customers and core activities that don't contribute to your success.** You must question every element of your business at least annually. If you were not already selling a product or supplying a customer, would you invest in those activities now?
- ▶ **Watching the edge of your radarscope.** You not only need to know what your present customers want. You must study your non-customers. For most companies non-customers greatly outnumber customers. New opportunities may abound outside your traditional markets.

Utilizing your theory

The process of developing a theory of your business will focus you on the activities that are critical to success. As a result your theory will direct investment of your time and money on what matters most, the drivers of profitability. You simply must have every activity in your company supporting

The who and what

What comes first in building the theory of your business? Customers — the who? Or products and services — the what? Two schools of thought offer answers to that question.

Proponents of a market-driven business believe that the customer's needs and priorities come first. Under this philosophy managers (1) identify the who and then spell out (2) the distribution channel that delivers the needs of those customers, (3) the product/service offering that meets those needs — the 'what', (4) the inputs/materials required to create the offering, and finally (5) the assets vital to converting the inputs.

Starbucks recognized that the priorities of coffee buyers were shifting from low price to quality (taste). They then focused on a new distribution method, the café and its offering — a combination of coffee and the café experience. Once the

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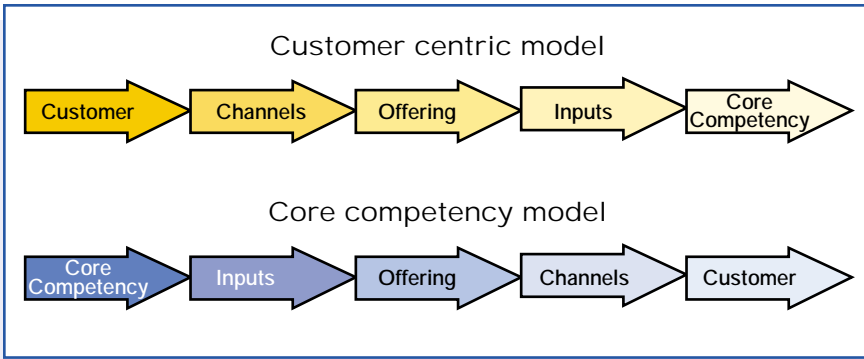


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Is your business based on the customer or core competency? Proponents of market-driven business believe customers needs come first, and everything builds on that. Others believe a business starts with a narrow set of skills.

customer and the product were proven, the company scaled up its store business and then branched into grocery stores.

Others believe that a business starts with a narrow set of skills and knowledge that creates value for the customer. These assets are commonly referred to as core competencies. With this philosophy managers find (1) ways to convert the core

competencies into an offering and (2) then find customers who value that product/service.

Honda exemplifies success under the core competency banner. That company has leveraged its expertise in engine design and manufacture into products serving markets as diverse as lawn and garden, marine, and motorcars.

Which philosophy is best for you?

the primary objective through a real cause-and-effect relationship.

To guide employees' behavior managers must align their organization with their whats and hows. A sound theory can provide that discipline if its assumptions are publicized throughout the work force. In the next Raymond's view we will explore how you can continuously teach your whats and hows to your employees.

Bottom line

Putting your whats and hows on paper won't revolutionize your company overnight. But the process of documenting the theory of your business can force you to question the relevance of your assumptions and activities to today's world. Real business success comes from good ideas that are implemented, and then continuously nurtured. Good ideas don't implement themselves. The what-how process can help you get past simply thinking and on to the real doing. ▲

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