OMIGOSH – *Integrating Strategy, Governance and Ownership*

Many comment that New Zealand companies often struggle to maintain a strategic approach. John Mendzela asks why

In 1999 I developed a report on strategy and governance for the IoD, based on interviews with over 20 successful medium-sized companies. Most were exporters. The findings were mixed, and included an unexpected third topic:

- strategic management skills were variable but far from absent
- opinion about governance divided sharply. Some companies did not have or want a board; others found their external directors highly valuable. Differing expectations about strategic management roles had sometimes led to a lack of added value from the board. In particular, many boards had been ineffective in sponsoring strategic change
- ownership issues had often tended to impede progress or divert management.

How Much Has Changed Since Then?

In strategy and governance, perhaps less than we like to think.

A simple exercise at IoD workshops demonstrated the problem. Directors from different institutions were asked to pair up and briefly outline the nature, current situation and future goals of their organisations. Each then privately identified the three-to-five key indicators of strategic performance that he or she would expect to be measured, monitored and reported for the other's directors. Typically, we found that in reality only one or two of those indicators was being reviewed in some way. Often none were!

With clients, I expect to tackle strategy and governance issues in an integrated way. Strategic thinking needs to be practical and tangible, with continuing processes that monitor performance against strategy. If not, then we get the strategically ineffective board that many interviewees identified.

Does Every Business Need a Board?

A board is not cheap, and without good strategic processes it may not add great value. So governance roles and skills, not a governance structure, is what matters.

But often the greatest challenge may be related to ownership. That can take many forms. Let's first imagine a sole-owner business growing over a generic life path:

- **O**perations – the owner is the operator. Management and governance are barely conscious
- **M**anagement – the owner engages capable operators, and steps back from operations to focus on management
- **I**ntuition – the owner engages capable managers, and steps back further to focus on strategic management. Many owners will do that informally but well. Others will struggle
- **G**overnance – the owner engages capable advisers and directors, and starts to think of the business as an entity distinct from its owner
- **O**wner**SH**ip – the owner starts to think about how value should be realised, or transferred to others who can add further value.

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Ownership succession is essential to realise the value that has been created.

But where 'this business is my life…' applies, it is easy to go no further right now. So thinking about ownership change comes too late. Too much value remains dependent on the original owner, and is never realised.

For an owner, the key strategic questions should be about the value of the business and what makes up that value. Financial results are of course the starting point, but the analysis also needs to consider the company's current and future strategic positioning, markets, people, technical capability, customers and contracts.

New Zealand is a small society with inherently limited business ecology. The sole owner scenario is commonplace. But ownership challenges that limit strategic success can take many forms. And those challenges can become opportunities. By aligning strategy, governance and ownership, a business can combine nimbleness and scale.

To take some examples from client experience:

- governance for a successful family company can be structured to recognise ownership interests and add independent professional skills. In fact the right chair is likely to become a trusted adviser and mentor for the owners.
- a technology business growing in scope and scale is likely to leave behind some of the original owners who prefer a lesser level of intensity or a lower risk and return profile. Measuring the value of the business to develop risk and return scenarios can help identify who wants to "play at the next table", and make win-win ownership reconfiguration easier.
- an adventurous sole owner who enjoys start-up and breakthrough growth can sell a maturing business to someone more managerial, but retain an investment stake and reinvest some proceeds in new ventures.

In each of those cases, 'owner' becomes a distinct value-adding business role, not just a property right. But ownership alignment is needed in less personal situations too:

- professional service businesses rely mainly on individuals. Mechanisms can be developed to spread ownership amongst key shareholder-employees, without losing the advantages of unified management and governance.
- geographic and market realities require many mature New Zealand businesses to choose between stable profitability and a much higher risk profile. Some owners may face potential conflicts of scope. So governance needs to analyse alternative strategies in terms of risk preferences and "go/no-go" areas.
- a co-operative company can shape its strategy around the "multiple hats" of the co-operative model. Ownership strengths can be exploited but a board will allow fresh and creative thinking.
- public ownership is more than a political question. To do its job properly, a board needs to look through its cosmetic or conflicting mandates and insist that owners clarify and prioritise their ownership objectives. Tension is likely! Often a targeted strategic analysis or project investigation can help.

What About Investment Issues?

Realistic strategic capitalisation is vital, but changing ownership is much more than a financial transaction. Again the scale of New Zealand makes generic models much less applicable.

Yes, a conventional "venture capital" path whereby external investors finance a business through the stages of seed, start-up and expansion can work for some enterprises. But more often, an overseas business with complementary activities can add greater and more targeted ownership value. Careful structuring can combine the advantages of personal ownership and corporate financing.

And public listing is unlikely to add value for most Kiwi companies. They are simply too small for those complications and costs. Publicity may initially seem gratifying, but it becomes a distraction. Most seriously, a strategy that needs patient ownership readily becomes compromised. Businesses lose strategic focus and momentum after listing as their boards struggle to meet optimistic promises or reassure investors.

So What's the Lesson?

For most businesses, thinking carefully about strategy leads to questions about governance, which in turn leads to questions about ownership. But approached that way around, the process is inefficient and probably ineffective. Alignment through reverse engineering will be difficult. Many private companies will do better by beginning with an ownership plan, not a strategic plan.

Ownership, governance and strategy should be considered as an integrated package from the outset. The goal should not be some generic Best Practice in strategy or governance, but the combination of good practice with customisation to specific circumstances that achieves Right Practice for Us.

John Mendzela has advised or directed a wide range of New Zealand companies. He developed and presented the IoD's strategy training some years ago. Further resources on strategy for New Zealand companies are available at www.mendhurst.com