The Five Steps All Leaders Must Take in the Age of Uncertainty

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Business leaders increasingly find themselves in unfamiliar territory marked by high levels of uncertainty and instability, a slowing global economy, and shifting political realities. Global economic policy uncertainty has tripled since 2000 and continues to accelerate. Our own research shows that this systemic uncertainty feeds into corporate decision-making. Companies are more exposed than ever to economic and political feedback, and their performance swings are increasingly due to noncompetitive effects. This phenomenon affects players across entire industries and, in the extreme, can threaten their very survival.

Take the U.S. retail industry, for example. Over the last several decades, companies like Walmart, The Gap Inc., and many others successfully played a global cost arbitrage game by taking advantage of labor cost differences, low trade barriers, and IT advances. As we know today, such sourcing strategies have unleashed economic, social, and political feedback effects, culminating in strong political backlash. Retailers now face the possibility of a border adjustment tax, which, if implemented, could wipe out a substantial proportion of the industry’s profits.

The examples are manifold and not limited to the United States. Consider utilities in Europe, where companies underestimated the social demand and resulting political support for renewable energy. The top 10 European energy utilities lost 40% of their market value since their peak in 2007 — the top 3 lost as much as 75%.
Political and macroeconomic forces are shaping the business environment as never before. The implications for corporate strategy and leadership are profound.

**Change in Perspective Needed**

We believe business leaders need a new mental model to better understand the complex interplay between companies, economies, and societies. To do so, they must shift their focus to the broader business and social ecosystems in which their companies are embedded. These ecosystems are *nested complex adaptive systems*: multilevel, interconnected, dynamic systems hosting local interactions that can give rise to unpredictable global effects and vice versa. Acknowledging the unpredictability, nonlinearity, and circularity of cause-and-effect relationships within these systems is a notable departure from the simpler, linear models that underpin traditional mechanistic management thinking.

What does a nested ecosystem look like? Companies are part of industries and markets — business ecosystems — that are embedded in local and national economies, which in turn are interwoven with societies. Changes at lower levels (for example, the sourcing practices of U.S. retailers) influence higher-level systems (such as the economic value and social status of manufacturing skills in society), which then reshape policy (border tax proposals, for example) and thus the fates of subsystems — namely, companies. A new systems-based mental model will help leaders to understand, adjust to, and, within limits, shape these feedback dynamics. We see it as a prerequisite to maintaining competitive advantage.

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**A New Leadership Paradigm**

Business leaders need to master the art of shaping systems, rather than just operating within them. This means not merely extending their current game, which typically focuses on the company, the resources it controls, and its immediate competitors, suppliers, and customers. They need a completely new set of priorities and capabilities. Leaders can take these five steps to effectively shape the extended system in which they participate.

1. **Observe and understand the broader system.** First, leaders need to mentally situate their business in the context of a wider system that includes consumers, ecosystem partners, media institutions, and policymakers. This means understanding the key players and their interests and mapping out the important relationships among them. Often, opportunities for and threats to the business become visible only by considering the broader system beyond traditional industry boundaries.

   The music industry in the 2000s is a classic case of what happens when business leaders fail to see the bigger ecosystem picture. Record labels faced with new digital competitors were on a downward spiral and unable to muster the systemic response to break out of it. Eventually, it took an industry outsider, Apple Inc. founder Steve Jobs, to lead (nearly) all major music labels onto one platform, and with it open a viable path to new digital revenues.

2. **Master the art of intervening in the system.** Next, leaders need to learn how to intervene effectively in a
complex adaptive system. A common managerial mistake is to limit oneself to direct leverage points. Instead, seemingly softer indirect points can often provide more leverage in complex systems. One example: the “Intel Inside” campaign. Before Intel Corp. changed its messaging in the 1990s, chip manufacturers solely marketed to their direct users — design engineers at computer manufacturers — but as the market matured, chips were in danger of becoming commoditized. By finding an indirect but more powerful leverage point — the end consumer — Intel was able to change the role that chip manufacturers play in the IT value chain and assume a leadership role in the industry. In that process, Intel grew its value by more than 40 times.  

3. Orchestrate collaboration in the system. Leading in a system requires striking a balance between the often-conflicting needs of companies and the broader system that they constitute. To do so, leaders must foster mutualism and trust among the companies. In practice, this requires not just modeling the right behaviors by creating value for the overall system but also actively surfacing and resolving tension within the system. Active conflicts, such as between nongovernmental organizations and large companies serving similar constituencies, can lead to productive information exchange and activity; these interactions, while stressful, typically help both sides improve and sharpen their value proposition, whereas unsurfaced tension increases the risk of deeper disruptions down the road. Healthy systems require both collaboration and small, manageable conflicts.

4. Foresee and manage systemwide risks. Because of the increasing interconnectedness and interdependence of companies, many corporate risks present themselves to the entire system rather than to individual companies. To manage systemwide risks, leaders must be able to detect potential threats to the system’s health and have the courage to preemptively change practices to avert them. This means that they need to play the roles of antennae that sense changing political, social, and technological signals; articulate the risks these developments bring; and also act as disruptors to prod other stakeholders in the system to adopt new behaviors, even when the direct benefits to their own companies are not clear or immediate.

Take the suffering U.S. textbook industry. Some of its systemwide woes come from technological substitution, but a more fundamental challenge is that the entire sector has been impervious to persistent warning signals about its lack of openness and anachronistic pricing practices. As a result, the industry now faces a host of competition and substitutions, ranging from open-access journals to massive open online courses.

5. Lead with a new mindset. Leaders cannot rely only on formal authority or a chain of command when working on their system. Instead, they need to leverage more informal ways of exercising leadership that can transcend organizational boundaries. We have seen some leaders rely on superior visionary abilities to exercise thought leadership in an industry; others leverage their ability to convene and build trustful relationships. Ultimately, these actions transform leadership from a position of authority into an activity that can create broader influence. This transformation requires, at its root, a mindset shift from thinking in reductionist models of company performance toward more holistic models of system performance. Those who manage this shift are bound to create an
advantage for their company as well as their wider ecosystem.

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References

1. See, for example, the Global Economic Policy Uncertainty Index at http://policyuncertainty.com.


3. BCG analysis comparing the relative performance effects of noncompetitive factors (political/regulatory exposure) and competitive factors (e.g., profitability, EBIT [earnings before interest and taxes] margin). The importance of noncompetitive factors has increased relative to competitive ones (from 0.4x to 0.6x) and even exceeds competitive factors in financial services (~1.4x).


5. BCG analysis based on S&P CapitalIQ.

6. BCG analysis based on S&P CapitalIQ. Intel share price grew from $0.81 to ~$34.20 (end of June 2017).
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