# SMASH

## Using Market Shaping to Design New Strategies for Innovation, Value Creation, and Growth

This page intentionally left blank

# SMASH

## Using Market Shaping to Design New Strategies for Innovation, Value Creation, and Growth

BY

**Suvi Nenonen**
**Kaj Storbacka**
*University of Auckland Business School, New Zealand*

United Kingdom – North America – Japan – India – Malaysia – China

Emerald Publishing Limited
Howard House, Wagon Lane, Bingley BD16 1WA, UK

First edition 2018



**British Library Cataloguing in Publication Data**
A catalogue record for this book is available from the British Library

ISBN: 978-1-78743-798-2 (Print)
ISBN: 978-1-78743-797-5 (Online)
ISBN: 978-1-78743-839-2 (Epub)

# CONTENTS

# ACKNOWLEDGMENTS

Kaj insists on cultivating an image of book-writing à la Swedish film director and author Ingmar Bergman's writing process – months of toil on a far-flung Scandinavian island with the company only of our interior muses. But while we write from homes on offshore islands both in New Zealand and in our native Finland, the process of realizing the volume in your hands has been anything but a solitary endeavor.

We are firm believers in what we call theorizing *with* managers, rather than merely about them. As social scientists, we see little point in detaching managers from knowledge creation; we would much rather make and shape our new ideas and frameworks in partnership with them. Therefore, our first and most fundamental thanks belong to those 37 companies who welcomed us in and shared their experiences through the four "SMASH – Strategies for MArket SHaping" consortia projects in Finland, New Zealand, Singapore, and Sweden. From A to Z, the 37 companies are: Affecto, Aktia, Beca, Blunt Umbrellas, Comptel, Designer Textiles, Fletcher Building, Fonterra, Griffin's, Heartland Bank, Huhtamäki, IAG, Icehouse, Inspecta, K. Hartwall, Kiwibank, Lemminkäinen, Lobster Exporters New Zealand, MetService, New Zealand Trade & Enterprise, Normet, NZ Post, OP Group, Outotec, ReGen, Relacom, Spring Sheep Dairy, Tamro, Texus Fibre, Tru-Test, Turners & Growers, Uponor, Villa Maria, Vodafone, Wärtsilä, YLE, and Zespri.

The four consortia projects would never have taken shape and held together, though, without the robust and responsive organizational backbone of the institutions we work in. Our deepest thank-yous are therefore also extended to Talent Vectia Ltd, The University of Auckland Business School, and Hanken & SSE Executive Education Ltd.

The foundational research for this book has been financially supported by the Royal Society of New Zealand and their Marsden Fund grant (grant number UOA1333). During this research project, we had the privilege of studying in detail 21 successful market shaping firms in the four economies through a series of 82 interviews. Those companies and their executives are the unnamed heroes of this book. And to the extent we had muses, these were they: the insights from the research project have inspired many of the ideas we present in this book. Here is also the place to thank our wonderful research project team for their stellar and unstinting work: Dr. Charlotta Windahl, Dr. Catherine Frethey-Bentham, Mattie Wall, Joel Allen, and John Lim, we owe you more than you can imagine.

Academic work always stands on the shoulders of giants, past and present. Looming particularly large for us is the late Professor Robert F. Lusch, who was a continuous inspiration for us and directly influenced the last chapter of our book. Our collaborations and conversations with several individuals have been vital to the evolution of our own thinking over the last 10 years: Dr. Melissa Akaka, Professor Luis Araujo, Professor Roderick J. Brodie, Professor Pennie Frow, Professor Hans Kjellberg, Professor Cristina Mele, Professor Kristian Möller, Professor Adrian Payne, Professor Jaqueline Pels and Professor Stephen L. Vargo.

Research and writing also require safe and stimulating intellectual homes. We are deeply grateful to the former Dean, Professor Greg Whittred, and former Associate Dean, Professor Jilnaught Wong, for welcoming us to New Zealand and The University of Auckland Business School. Thank you for trusting us and opening so many metaphorical doors for us. In Finland, two people in particular have provided us platforms to test and develop our frameworks. Tom Lindholm, CEO of Talent Vectia, and Kaj Åkerberg, Business Development Manager at Hanken & SSE Executive Education: thank you for believing in us, year after year.

On the writing side, we want to thank our brilliant and devoted freelance editor, David J. Thompson. David is not only masterly at the micro tasks of turning our "Finglish" into proper sentences, but he is also our most trusted macro critic of logic, structure, and flow … or lack thereof! All the flair and wit in the following pages have also flowed from David's pen. We may have done the heavy lifting of figuring out what we wanted to say, but David's magic made it both lucid and, we hope, enjoyable.

Finally, no amount of research or writing would have sufficed without connection to a publisher! One of the legends of marketing, Professor Jagdish N. Sheth introduced us to Jeanne Glasser Levine, President of Pub Zone Consulting, who was instrumental in making that connection. And as the final link between us and the reader, Charlotte Maiorana, Senior Editor and Nick Wolterman, Assistant Editor at Emerald Publishing deserve the last word of thanks.

Lest that list forgets anyone: we are deeply grateful for *all* the support we have received. And in case we share the love too widely: while we owe most of the insights that follow to others, any errors, of course, are completely our own.

Suvi Nenonen and Kaj Storbacka
Krokö and Waiheke Island
August 2017

# PREFACE

*Time and again, in one company and one country after another, our consultancy and research experience hammers home one point: What makes or breaks strategy is whether managers "get" something so overarching it mostly escapes attention: the very nature of markets.*

*For, whilst markets are the core concept of economics and commerce, they have so far been overwhelmingly glossed over or misunderstood by orthodox strategy. But in 2018, business has crossed a threshold of complexity where a correspondingly complex market view becomes indispensable.*

## FOUNDATION: MARKET VIEWS MAKE OR BREAK STRATEGY

Today, only by getting the nature of markets as *complex adaptive systems*, can firms hope to read and respond to their environment? More enticingly, only by learning to operate, and co-operate, in complexity, can they take part in proactively adapting that environment to themselves – instead of reactively adapting themselves to the environment? And therein lies the strategy's new prize, which turns established strategy paradigms on their head. Mastering the collaborative dynamics of complex market systems enables Strategies for MArket SHaping — SMASH. Market shaping unleashes value gains from greater market size, efficiency, and profitability which dwarf the zero-sum wins eked out in market-share increments by traditional competitive strategy.

The importance of market views – in other words, why readers should even care – crystallizes from our opening pair of case histories: the puzzling fall of Nokia Mobile Phone and the dazzling rise of Uber. Infamously, Nokia plummeted from sure market leader to a fire sale of its mobile phone business line in a few short years. Yet, conventional explanations for the demise of Nokia Mobile Phone miss the forest for the trees. Those explanations overlook the secret lurking in plain sight by seeking answers at the firm level: failures of Nokia's leadership, or failures in product-related competitive advantage against industry rivals, causing loss of product market share.

Ironically, Nokia CEO Stephen Elop raised his eyes to the market level and glimpsed the true explanation in the leaked Burning Platform memo from 2011. He concluded: "Our competitors aren't taking our market share with devices; they are taking our market share with an entire ecosystem. This means we're going to have to decide how we either build, catalyze, or join an ecosystem." Elop's ecosystem epiphany, of course, was too little, too late. But he can hardly be faulted for that. What really stands out is that Nokia went *from hero to zero because it did everything by the book* – a strategy playbook complete with an implicit view of markets that had passed its use-by date.

If Nokia was the model student following all the rules of the doomed old school, Uber Technologies Inc. doesn't just represent the new school; it's unschool. The online ride-sharing company, with its game-changing app that lets riders hail, track, and pay for a cab online, and its alleged non-workforce of mere partner drivers, is shaking up market institutions and flouting the rules of the old taxi-scape. Uber understands that markets are shapeable, makeable systems. It's a born market-shaper – and one of the most radical.

## ORTHODOX STRATEGY STATES NO VIEW OF MARKETS, BUT IMPLIES A POOR VIEW

The case histories generalize. Nokia represents the received view of markets and strategy, while Uber gestures toward an intuited, but as yet unarticulated, alternative. For decades, the received wisdom of management strategy has largely skipped over articulating any theory, or view, of markets. However, by working backwards we can deduce the views it implied. Our text dubs these as the poor views.

The standard playbooks still weighing down managers' bookshelves have taught a single meta-formula of strategic success. Broadly, the formula goes: Analyze your market to identify opportunities, find your unique position, and create a master plan to outwit your competition.

Working backwards, this strategic posture makes assumptions, assertions, and approximations about markets, which imply that markets are either very simple, like a supply and demand graph, or utterly incomprehensible.

Variously:

- The market is externally given: from whence it came, we cannot know. The exception is that occasionally a heroic outlier launching a breakthrough technology manages to conjure into being an entire new market.
- Market opportunities are precursors to strategy. The non-heroic majority of firms are stuck with the market they've chosen, and must adapt their firm to the opportunities that they find.
- Market dynamics are deterministic. They can be analyzed, predicted, and operated on using the everyday mechanical logic of cause and effect.
- Markets are synonyms for the aggregate demand for products – hence phrases like "the mobile phone market." What this view leaves out is the value created when customers use the product.

- Markets are industries. Consequently, we create institutions that limit our ability to look beyond the boundaries of the industry: statistics that measure the growth of the industry, and trade associations that stabilize the market.

None of these premises is true, and many are incompatible.

## Poor Market Views Impoverish Your Strategy Playbook

To strategize on this basis is to build strategy on sand. In most cases, the operating environment is so inherently unpredictable that market analyses aren't worth the pixels they're written in. The poor views impoverish strategy from every angle:

- They make strategy reactive and defeatist because markets are supposedly given.
- They doom firms to compete for market share in a zero-sum competitive game.
- Their very dominance kills the hallmark of good strategy: originality.
- Finally, they miss the main chance: to unleash value that is orders of magnitude greater than market-share increments. In other words, they miss *market shaping*, achieved by adapting markets to the firm, not vice versa.

If these poor market views and the strategy built on them are so deficient, why do they still prevail? We argue they have persisted partly because of sheer incumbency; partly through self-reinforcing definitions in the data on markets and industries; and partly for the lack of an articulated alternative. But the day of reckoning has come in one field after another as markets have crossed a threshold of complexity. Globalization, digitalization, and network effects render the old models of markets and strategy obsolete.

## A RICH MARKET VIEW REQUIRES SYSTEMS THEORY

Drawing on the transdisciplinary science of systems theory, and combining insights from biology, psychology, and sociology as well as economics and management, we offer the rich reality of markets as complex adaptive systems. That's "complex" like an ecosystem or a society, rather than merely "complicated" like the flight deck of a Dreamliner. Indeed, as frequent fliers, we're delighted that airplanes still obey mechanical cause and effect. But complex systems don't. They can be neither controlled nor safely predicted. Markets as systems constantly evolve; partly by random "emergence," partly by the deliberate market shaping efforts of the likes of Uber and its smart entrepreneurial cousins. Consequently, the firm is part of the market, rather than the market being external to the firm.

Markets are complex systems of exchange for the purpose of co-creating value. More precisely they create what classical-era economics called "use value" to the customer. Use value is as opposed to our standard neoclassical metric: exchange value, which is really price. Yet boosting use value – which is limitless – can ultimately boost exchange value, markets, and profits.

The complex systems' view of markets has always been true but only recently become essential. Recognizing markets as complex systems spells strategic implications. Notably, just as markets are socially constructed, so they can be reconstructed by social methods. And while they cannot be predicted or controlled, they can be *influenced* by market players.

## THE BOOK REBUILDS STRATEGY ON THE RICH VIEW OF MARKETS

Rooted in the richness of market systems, the book therefore traces the three main resulting shifts in strategic thinking: (1) from firm focus to context focus, where the relevant context is our definition of the market; (2) from competing and winning to value creation and cooperation; and (3) from analysis, prediction, and planning to non-predictive strategizing and experimentation.

The book weaves these three strands together into a cohesive strategic framework – market shaping. Market-shaping strategies acknowledge that much of firm performance, both turnover growth and profitability, is explained by the markets where a firm operates. Crucially though, strategic choices go beyond market selection, entry and exit; markets are malleable and therefore firms can – and should – actively seek to shape them in their favor by value-creating coalitions.

## KEY CONTRIBUTION: AN EASY, ACTIONABLE FRAMEWORK FOR MARKET SHAPING

Market shaping is not entirely new. Research by Boston Consulting Group and McKinsey suggests that 9% of firms already engage in market shaping. However, most of them do so intuitively. Therefore, their methods are hard to replicate. What is new – and the book's key contribution – is systematizing and articulating a universal, teachable, and actionable framework for understanding and shaping markets. Whereas traditional strategy skipped glibly over the subject, SMASH recognizes markets as strategy's necessary foundation and then rebuilds.

Crucially too, our framework is one that any firm can grasp and practice. It does not take traditional market power and resources, or intuitive genius, to understand markets as complex systems and to shape them to your own benefit. As a master metaphor and structural device, we use the colorful, reader-friendly diagram of a market Fan, comprising four layers plus a core. The Fan groups and orders the 13 elements of markets we've identified that savvy market shapers of any size can influence, in closely explained and topically illustrated ways, to reshape the whole.

# 1

# YOUR STRATEGY PLAYBOOK HAS EXPIRED

*What is market shaping? And what, exactly, is "the market" anyway?*

*Stunningly, strategy has never adequately defined one of its central institution, the market. Old playbooks got away with a hodgepodge of assertions, assumptions and approximations. But the undeniable complexity of modern markets confronts us with the truth. Markets are elaborate, evolving ecosystems – think biology, not machinery. Today, strategy must embrace complexity or die.*

*Market shaping is the first strategy to embrace and exploit the truth about markets. It elegantly distils their complexity. And it shows how any firm can then turn strategy on its head – by adapting the market to the firm instead of the firm to the market, opening up untapped value in the process. The value market shaping unlocks defines strategy's new "main chance."*

## NOKIA: FROM HERO TO ZERO BY DOING EVERYTHING BY THE BOOK

In 2007, Finnish multinational Nokia was the darling of the global mobile phone market. CEO Olli-Pekka Kallasvuo smiled from the cover of *Forbes* magazine, and felt secure enough to dismiss Apple's new offering, the iPhone, as a "niche product" which wouldn't "in any way necessitate us changing our thinking".[1] Few would have questioned him.[2]

Nokia kept notching up successes for several years, but remarks such as this came back to haunt it when everything seemed to go wrong at once and the company nosedived. In September 2013, the once-mighty brand sold its mobile phone business to Microsoft for 5.4 billion euros. A paltry sum, when only six years earlier Nokia's annual operating income from the same business was over 5 billion euros. What reduced the uncontested market leader to a fire sale of its main business line?

The demise of Nokia, or more precisely Nokia Mobile Phone, is an epic saga, with many twists and turns over two decades before the final reversal. To grasp it properly, we need to analyze both its rise and its fall – both the "hero" and the "zero" chapters.[3]

## Hero – Best Products and Most Efficient Supply Chain

Let us begin at the beginning. Nokia stepped onto the world stage as a key player in influencing the development of the Global System for Mobile Communications Standard. You'll know it by its more household abbreviation: GSM. GSM paved the way to the second generation of digital mobile telephony – called 2G.

The first GSM phone call was made in 1991 on a network built by Telenokia and Siemens with a phone built by – you guessed it – Nokia. In 1993, Nokia became the only mobile phone manufacturer whose entire GSM phone range supported Short Message Service, or SMS. (SMS refers of course to "txts," the add-on that became a killer app of mobile telephony and rewrote our language like a bad, vowel-less Scrabble hand in the process.) This, just a year after the first SMS message was sent. And as early as 1996, Nokia provided a smart phone with Internet connectivity: the Nokia 9000 Communicator.

The late 1990s and early 2000s were the golden years for the mobile phone manufacturers. Double-digit growth was spurred by the rivalry between the main players: Nokia, Sweden's Ericsson, and Motorola from Illinois. By the mid-2000s, Nokia was on top. Success stemmed largely from its super-efficient supply chain, affordable and reliable phones, the fastest ramp-up process for the new mobiles (hugely important in a business with 18-month product lifecycles), and the widest range from which operators worldwide could select models for their local consumers.

In 2000, the market entered a transition stage. Over the next few years, 2G would gradually be phased out and 3G phased in. Put simply, whereas 2G brought mobile telephony from analog to digital, 3G deserves credit for bringing voice and data fully under the same standard. The growth rates of mobile phone users and Internet users, and a convergence of digital technologies, sent telco operators into a bidding frenzy, especially the Europeans. Operators spent over 125 billion USD on 3G licenses.

Nokia understood that 3G was the next big thing in mobile telephony and threw itself into this third generation hoping history would repeat. Certainly, the early days showed promise. In 2002, Nokia became the first mobile phone manufacturer to launch a 3G handset. The same year saw the first Nokia smart phone to sport a built-in camera: the 7650. The company followed this up in 2003 with its mobile game deck N-Gage, which combined a portable game console with a mobile phone. And Nokia's first music phone hit the market in 2005.

Anecdotally, it also seems that Nokia's engineers had showcased a touch-screen phone in-house as early as 2000,[4] but the company halted development because its market research predicted consumers would prefer keyboards to touch screens. And you would trust your company's consumer insight when it had researchers on the ground in every continent not inhabited primarily by penguins.

Yet, the 3G market was proving an unpredictable beast. In 2000, Nokia erred wildly with a forecast of over 300 million mobile phones connecting to the mobile Internet within two years. The true figure came in at just 1% of that. Sure, the 3G handsets were more expensive than their 2G predecessors, but this hardly explained the slow adoption. Something else was at play, and it was weighing down Nokia's ascendancy.

What hid the downturn in Nokia's fortunes due to 3G was that, during the transition, 2G of course continued to run alongside it. Luckily, Nokia's 2G handsets were still selling like hot cakes. That was perhaps why Kallasvuo could make his airy dismissal of the iPhone in January 2007, for that year was the zenith of Nokia's fortunes thanks to the continuing, albeit waning, success in its 2G market. Consolidated turnover of 51 billion euros, operating profit of almost 8 billion euros, cash reserve of nearly 7 billion euros, market share of 37.8%[5] of the global mobile phone market, hefty investments in R&D (11% of turnover) and the most efficient supply chain in the industry.

## Zero – Expiry of Nokia's Strategy Playbook

How, then, to explain the nosedive and that humiliating sale to Microsoft six short years later? You've probably heard some of the conventional accounts. It was Icarus syndrome: Management grew arrogant, flew too high, crashed, and burned.[6] It was consumer preferences: underestimating the importance of aesthetics and a smooth user experience à la Apple. It was sluggishness in updating the operating system: hanging on to the old-fashioned Symbian for too long, and failing to develop MeeGo fast enough. It was hesitation introducing the touch screen. And so on.[7]

None of these explanations withstands scrutiny. For starters, Nokia's management stayed substantially unchanged, and always took cutting-edge advice from top-drawer recruits and world-class management consultants. More's the pity, but Nokia itself didn't much change.

Consumer preferences weren't to blame either. Until 2011 Nokia was still the clear market leader in mobile phones, with 23.8% market share.[8] And the rival who eventually overtook it was Samsung, not Apple. Finally, if you disaggregate, the company's decline started well before the iPhone débuted.

We believe conventional explanations for the demise of Nokia Mobile Phones miss the forest for the trees. They look for answers at the firm level: in failures of Nokia's leadership, or failures in product-related competitive advantage against industry rivals, causing loss of product market share.

If you stand back, a bigger picture emerges – one defined by what we'll expound as complex markets. Recast thus as a tale of two markets, Case Nokia Mobile Phones reveals a firm with essentially constant strategy tracking a rise during the 2G market boom, then a slowdown after 3G arrived, and eventually a fall as 2G phased out and 3G took over. Could there have been something radically different about the 3G operating environment that stopped Nokia from successfully replaying its winning strategies from the 2G environment? Was there something about the 3G market for which the company and its strategy were fundamentally unprepared?

Stephen Elop was recruited from Microsoft to succeed Kallasvuo as CEO. In the notorious "burning platform" memo of 2011,[9] Elop confided what he thought had gone wrong. The memo was never meant for public consumption, but leaked to the press. To our mind, the core of the memo is a completely new definition of the market – both Nokia's own market and markets in general: "The battle of devices has now become a war of ecosystems, where ecosystems include not only the hardware and software of the device, but developers, applications, ecommerce, advertising, search, social applications, location-based services, unified communications and many other things. Our competitors aren't taking our market share with devices; they are taking our market share with an entire ecosystem. This means we're going to have to decide how we either build, catalyze or join an ecosystem."

Elop saw past product markets and viewed markets as ecosystems of interdependent actors. He saw that these systems go beyond mere products or "devices"; that their dynamics dwarf uncoordinated, unilateral company strategies such as Nokia was following; and that such systems can be deliberately shaped – or in Elop's words "built" or "catalyzed" – as well as just joined in a me-too fashion.

Nokia had contributed to the emergence of the 2G market by actively engaging – together with competitors – in the creation of the GSM standard. However, the 2G market was less complex than 3G. It required relatively few actors to create value to the end users: the handset manufacturers, the producers of the telecommunication networks and the companies operating those networks. The GSM standard used for 2G meshed these neatly together: The consumer could rely on getting her calls and SMS messages regardless of the brand of her mobile phone, her and her friends' telco operators, and the manufacturers of their networks.

But the 3G standard introduced data into the picture and made the market ecosystem inherently more complex. What kind of content and data-based services should be made available to 3G phones? Who would create that content? How would the IP rights to this content be enforced? How could existing content, such as television shows, be rendered compatible with mobile phones and their small screens? How should operators charge their customers for data? How would operators even measure data usage?

Nokia tried to apply the old, 2G market rules (such as first mover advantage and focus on the quality and numbers of devices) to the new 3G market game. However, the more complex, volatile new market had taken the old market playbook past the point where it could function at all, even as an approximation; it revealed the limits of the old book and its old view of markets.

What really stands out in all this is that Nokia did far more right by the traditional[10] strategy playbook than it ever did wrong. The failure of Nokia was nothing less than the failure of the playbook itself. *Nokia went from hero to zero precisely because it did everything by the book – a book that had passed its use-by date.*

## Nokia's Expired Playbook May Be Your Book!

Why should that concern you? Because we're talking here about essentially the same playbook that is still, today, repeated as variations on a theme between the covers of the myriad strategy, management and marketing titles on your bookcase and ours. Roughly, that book says: Position your firm to the best market, hopefully a growing one, then plan and execute a long-term strategy to adapt the firm to that market by cultivating a competitive advantage, and so compete for the holy grail of market share.

Now, the traditional playbook is a useful volume as far as it goes, with some genuine insights, but it is flawed and becoming less workable by the month. In particular, it is increasingly compromised by its inherited picture of markets. For the traditional book is based on a theory about markets that is fatalistic, incomplete, often circular, and at times plain contradictory. That theory was always flawed at a deep level in the ways just listed, just as the systemic theory that we're going to replace it with was always more correct. We've said that in the mobile telephony context, 3G took the old playbook past the limits where it could function. But exactly how did the old view continue to pass as viable for so long, and how does it continue to do so today?

We see several explanations for the persistence. First, particularly in simple and stable contexts, it contained just enough truths to be of some use. Second, its weaknesses were not stresstested often or severely enough to throw the whole theory into question – market-shaping exceptions like Apple under Steve Jobs could be put down to freaks of nature. This situation lasted while the majority of markets remained fairly static and their workings approximated mechanistic laws of cause and effect. By contrast, 3G and other 21st-century markets with their exponential network effects have assumed a positively ecological level of complexity and global connectedness: Think biology or sociology, not machinery. Third, no really well-developed and validated alternative theory was circulating in the mainstream. Fourth, the now-emerging theory of markets as complex systems is just that: more complex. It should be no surprise, then, that managerial applications wishfully cleaved to the simpler *status quo*. We all secretly wish for easy solutions to wicked problems, don't we? Nowadays, as the markets of the 21st century increasingly resemble 3G more than 2G in complexity, unpredictability, and malleability, the old theory and the playbook based on it will serve you less and less well and leave you more and more exposed to the increasing number of companies that have intuited ecosystems thinking, the way Nokia was exposed to Apple. And in the book you're holding, of course, we seek to supply the missing alternative theory and step-by-step advice on how to put it into practice. We're aiming to make the intuition systematic and learnable. Like so often in life, the first step in learning the right way to do things is to unlearn the wrong way – the old playbook. But before we weed out and unlearn the bad theories and practice one by one, let's sneak a peek inside that – so far exclusive, intuitive – club of the market shapers and makers. These are the outlier firms. The exceptions that prove the rule. The few which have somehow managed to build their strategies on rock, not sand. Unsurprisingly, most club members are either helmed by the founding entrepreneurs or at least deeply entrepreneurial in their culture. They're also more likely to be found in disrupted industries. Often they are the disruptors themselves. More specifically, market shapers and market makers draw on a cohesive set of characteristics and strategic plays of 14 designable market "elements" which we're going to hang our academic and consulting hats on and which you in the field can apply. At the heart of that set, of course, is market-level thinking. It's the level of strategizing beyond company, competition and product which Nokia CEO Stephen Elop glimpsed too late: "building, joining, or catalyzing" entire "ecosystems"; adapting the market, not *to* the market.

Now, you'll already have spotted an obvious candidate for such a positive case story: that "freak of nature," Apple. We'll take Apple's story as read. But to mix things up a bit let's sample another sector. This sector lies beyond pure digital wizardry, where the rubber literally hits the road: urban transport and the brilliant, brazen bad boy on the block, Uber.

## UBER: TRANSFORMING TRANSPORT BY INTUITIVE MARKET SHAPING

If Nokia was the model student following all the rules of the doomed old school, Uber Technologies Inc. doesn't just represent the new school; it's unschool. The online ride-sharing company, with its game-changing app that lets riders hail, track, and pay for a cab online, and its alleged nonworkforce of mere "partner" drivers, is shaking up market institutions and flouting the rules of the old taxi-scape. The very word Uber, slang drawn from the German for super, breathes unbridled ambition. It's a born market shaper – and one of the most radical.

Co-founding entrepreneurs Travis Kalanick from California and Canadian Garrett Camp dreamt up the concept one snowy winter's night in Paris in 2008. The pair were frustrated trying to hail a cab during some down time from a LeWeb conference, but their minds were on the taxi problem back in their city of residence, tech hub San Francisco. They kicked around ideas like splitting the costs of a Mercedes S-class and a driver between themselves before cottoning on that they could tap existing private car owners. UberCab (as originally christened) was founded in 2009. It went into beta launch in 2010, road tested in New York and later that year débuted in San Francisco. Swatting down fines and cease and desist notices for operating like an unlicensed taxi company, Uber (with newly streamlined name) and its budget option UberX soon spread through the United States, Europe, and Asia. The funding snowballed with the popularity. It now operates in over 60 countries.

Characteristically for market shapers, Uber's founding entrepreneurs are still at or close to the helm, with Kalanick and Camp as CEO and chair, respectively. And it's hard to imagine a more entrepreneurial motto than Kalanick's "Always be hustling." Uber's disruptive, too, from tip to toe. But the company made it to the magic 50-billion-dollar valuation faster than Apple or even Facebook. How did they pull it off?

Back in Paris, Camp had muttered that you ought to be able to hail a ride at the tap of a button. Now, the button-tapping was clearly going to involve an app, and Uber's app is crucial. It's a whole new way of bringing together passengers and drivers. Yet the definitive market-shaping innovation was the structural shake-up which the tech leveraged: reconfiguring constituent parts of the old taxi and private car systems into a new market shape. For notably, the other constituents of the new market already existed: cars, drivers, passengers, smartphones. Only, their functions were about to change. Private car owners would begin moonlighting as chauffeurs. Their vehicles would morph from household convenience to revenue-earning asset. Unlike taxi drivers, these drivers would be – very pointedly, for the regulators' attention – partners setting their own hours rather than employees. Meanwhile, would-be passengers could now track their rides' arrival in real time almost like taxi dispatchers, and with a wonderful sense of control, through the latest addition to their smartphones' bank of apps. All of which revolutionized the value to Uber's users compared with traditional taxi services.

To signal the enhanced experience, the users would be nicknamed "riders." Echoing "drivers" on the other side, this appellation differentiated Uber users from traditional clients or passengers of a taxi company. It added a soupcon of the cooperative camaraderie of carpooling which befitted the democratized sharing economy model. The company's marketing still plays up such peer-to-peer virtues. For one, it promotes its nonprofessional drivers as "people just like you" – presumably as opposed to uniform-clad taxi company drones whose main interest is that you not muss up the upholstery. The company went beyond true peer-to-peer, though, by interposing their brokerage and organization. Yet Uber were still turning owners of private cars into paid providers much the way that Airbnb was simultaneously turning couch owners into landlords. After several iterations Uber had re-envisioned the urban transport space and, to borrow Elop's words, catalyzed the ecosystem of riding cars.

Meanwhile, digitalizing and centralizing the financial transaction out of the hands of the drivers and customers and into the app and the credit card companies have enabled Uber's (in)famous "surge pricing." When the demand for rides surges above driver availability due, say, to sudden inclement weather, a sporting event or even simply a public holiday, Uber ups its fares in that area to a new market-clearing price. The premium pumps up supply, as drivers already on the road nearby and others who were resting flock to the happy hunting ground. Simultaneously, the premium dampens demand as lower-price users pay drop out. The risk, of course, is to passenger goodwill. For riders, surge pricing is price gouging by another name. At time of writing, Uber was apparently trialing upfront price quotes and ditching the lightning icon and fare multiplication notice from its screen to at least paper over the organized opportunism.[11]

For the most part, the company has actively courted goodwill and trust from both riders and drivers. Besides the financial incentives to the two groups of cheaper (nonsurge) rides and a second income, respectively, Uber touts the safety that comes with transparency. Vulnerable riders like tourists are less likely to get taken for a figurative ride financially, or worse, since in theory at least passengers' ratings of their drivers will report and effectively constrain dodgy operators. Conversely, drivers can guard against bad apples in the back seat by checking their colleagues' rating of the next intended passenger.

Like other members of the market-shaping club, Uber has advertised its new vision for the market as delivering wins all round. We'll take the win to Uber itself as given. The other obvious beneficiaries are drivers and riders. Society and the economy are also cited as gaining – from better access to transport, more mutually beneficial driver–rider exchanges and even from fewer drunk drivers. And indeed Uber has propelled both overall market growth and efficiency. Cars are earning more often, and less often either sitting idle or taking up lane space under-occupied.[12] Uber itself has also grown considerably. In 2015, the company's revenue was estimated at around $2 billion.[13] Such lightning growth has come with a price, though. It is widely believed that Uber is losing money. This may or may not be a good thing, and draws frequent comparisons to Amazon's early years.[14] Nevertheless, investors appear to be keeping faith in Uber and its strategy. In 2016, the valuation of the company weighed in at a whopping $68 billion.

So far, this Uber fairytale has omitted one group loudly crying foul. That is the old incumbents: licensed taxi drivers, taxi companies, and their industry associations. Like that bad boy at school, Uber has eaten their lunch. They accuse it of piracy. On their side, often, the incumbents have their jurisdiction's law and the government. And to them, Uber has not merely sailed close to the wind or danced a jig on the head of a legal pin with its redefinition of what look remarkably like taxi services. Rather, it has ploughed a corporate juggernaut through the law. Indeed, among intuitive market shapers we've analyzed, Uber has taken the most radical, brazen approach to molding its market's rules of engagement. Where other firms might have courted lawmakers and industry associations, Uber has tried to harness sheer market forces and public popularity to pressure for regulatory acceptance. Apparently it's counting on its hefty war chest for legal fees.[15]

Now, unlike Nokia, Uber didn't need to bridge an old and a new reality – a (2G) world where the old playbook could get by and a (3G) world where only a new one would suffice. Uber was moving into an essentially empty space. What's more, it struck when the iron was hot. The Great Recession was biting. Many future riders and drivers were on their beam ends. And the jurisdictions where Uber was trialing were consciously looking for new economic ways of being.

But like fellow intuitive shapers, Uber knows markets will continue to change. Rather than let the grass grow under its feet, the corporate is actively probing to find the next big disruptions in transportation. Setting aside for the moment more exotic ventures into pizza delivery and helicopter rides, Uber is therefore especially targeting electric cars, driverless cars, and the twilight of our car-owning culture itself. Thus, riders can already insist on an electric car in some locations, and the 2016 UberGREEN pilot project collaborated with electric car providers BMW and Nissan. In 2015, Kalanick tweeted that the entire Uber fleet would be driverless by 2030[16] – and safer for it.[17] And car-owning riders might gladly surrender their second-biggest asset as more of a liability once Uber or similar operators can free them of parking hassles, paperwork, mechanics' and insurance bills and the need to dedicate a fraction of their home to a roller-doored concrete shrine to the automobile.

None of this is to claim that Uber will become the General Electric of the 21st century. Nor is it to endorse what may be seen as borderline-bullying tactics. You will have caught wind of the company's string of PR disasters, from surge pricing during Hurricane Sandy and a hostage-taking in Sydney, Australia, to allegations of a sexist culture and even rape, plus questions over the security of users' data.[18] Then there's the ill will and sometimes highly disruptive strikes[19] of taxi and minicab competitors, in certain instances vindicated by their governments. In August 2016, our made-in-America star also announced that it would merge Uber China with the local rival Didi Chuxing, effectively throwing in the towel on its Chinese operations. Perhaps most ominously, disaffected drivers have started asking: Is Uber working for us or are we working for Uber?[20] And of course the only thing the media love to talk up more than a meteoric success story is a fall from grace.

Yet, after Uber, the transport market will never be the same – other players have already started following the trend of "Uberification" – and its membership of the club of intuitive market shapers is assured. We can do one better than observe club members, though, nose-pressed to the glass. With a few more pages' unpicking of where the traditional strategy playbooks went wrong and the intuitive minority went right, you'll be able to start practicing market shaping for yourselves.

## POOR MARKET VIEW MAKES FOR POOR STRATEGY

Time and again, our study of business success and failure hammers home one point: Bad, old theories or views about markets are the biggest limit on strategy today. Not "getting" markets is why Nokia Mobile Phones failed and why conventional accounts for its demise flop in a similar fashion. It's also why innovators such as Uber are able to shape their markets right around the globe.

Pretty much all the traditional strategy playbooks are founded on poor theories of markets. In fact, they barely reveal a coherent theory worthy of the name, or even a definition. What they offer is a hodgepodge of assertions, assumptions, and approximations. Management strategy isn't the only offender. Most mainstream commerce and economics as taught and practiced for the last 30 years share the same weakness. As Nobel economics laureate Douglass North observes:[21] "It is a peculiar fact that the literature on economics contains so little discussion of the central institution that underlies neoclassical economics – the market."

Ironically, even marketing, which you could be forgiven for thinking would distill some wisdom on the subject, lacks a robust, realistic, useful definition, and theory of markets.[22]

Successive generations of strategy playbook repeat bad or incomplete theories – myths and half-truths – about markets like articles of faith, or supply only partial corrections. The persisting mistakes are so built into our language, our mindsets, our definitions, and even our data that we hardly notice them. But again, *you need to know where you're going wrong before you can go right.* So, if you'll forgive us for dwelling on the negative, we've identified the cardinal errors about markets which are alive and well and misleading business strategy today.

## Markets Are Not Industries!

Both managers and media often reduce the context in which they operate from a "market" to an "industry," as though the two were interchangeable. We call this reduction the industry view of markets. Whatever managers mean by, say, "the steel market" (and more on the flaws of such phrasing in a moment), they feel equally happy to refer to as "the steel industry." And in market reports we hear that the "construction industry" is taking a hammering, as it were, or "the airline industry" is taking off.

Latching onto industries as the relevant concept of the firm's context, and a powerful explanatory factor, is not without justification. For a century, economics and its sub-field industrial organization have said that industry structure explains much of a firm's performance, especially firm growth. Recent, more managerial studies back that up. In 2007, McKinsey & Company looked at turnover growth among some 200 large companies around the world in various sectors from 1999 to 2005.[23] The companies' annual topline growth averaged 8.6%. Of that, fully 5.5% came from industry growth, with 3% from mergers and acquisitions activity – which is likewise industry level – and a bare 0.1% from growth in market share. So industry-level effects massively dominated market share effects. Industry growth and mergers and acquisitions activity explained nearly 80% of the growth differences in this cohort, versus just 20% from market share changes up or down.

Moreover, in 2013, a much bigger McKinsey study of 2,888 companies looked beyond growth effects and investigated industry influence on economic profitability. Now, standard theory assumes economic profit is the product of firms' own actions. Yet, industry again accounted for a handsome 40% of the effect. So the context where the firm operates seems to explain its performance – both topline and bottom line – to a large extent.

The problem with the industry view is that industries – implicitly defined above as a group of firms providing similar products or services – make for a woefully incomplete conceptualization of markets. The industry view tells us something about production and competition but nothing about customers, let alone any wider ecosystem such as Nokia's Stephen Elop glimpsed too late and Uber's Travis Kalanick and Garrett Camp grasped all along. Yet, without customers, the slickest industry's production is worth nothing! Additionally, the industry perspective leaves little room to influence a firm's fortunes: You may streamline your production processes and devise shrewd competitive strategies, but the industry determines your fate – and it lies outside your sphere of influence.

## Don't Think Product Markets, Either!

The commonest (mis)conception of markets, however, is what we call the product market view. We all implicitly espouse this when we toss off phrases like "the mobile phone market." Folk often tack on a place, as in "the mobile phone market *in China*," so we'll also sometimes refer to this as the product-geography view, but it's essentially the same beast. Likewise, formulae that incorporate the who-to, like "the mobile phone market among young consumers," are really only the same beast in drag. So often does the beast in its three forms (product; product + geography; and product + customer segment) rear its head in strategy discourse that we'll often abbreviate the whole lot to "the product view." Oh, and coming back to mobile phones again, "products" are what Nokia CEO Stephen Elop meant by "devices" when he said: "Our competitors aren't taking our market share with devices; they are taking our market share with an entire ecosystem."

In its defense, the product view is not one-eyed like the industry view. It acknowledges, or at least waves at, the supply side, before focusing on demand. But demand, despite being the product view's primary focus, features only in the form of customers. This still critically over-simplifies the picture. Specifically, as you'll recall from ECON: 101, the product market view is fond of reducing the mysteries of markets to a two-dimensional supply-and-demand graph. This model abstracts from all the complexity to leave only buyers, sellers, product, and price. Yet, in one of a howling host of internal contradictions, the product view then seems to forget it's just an abstraction and acts as if this graph were a reliable proxy for the market. Suddenly, the market is reduced to a meager price-setting mechanism. Making a breathtaking leap of faith, that mechanism holds other things equal and considers all the outside factors it can model are sufficiently unusual to merit the name "shocks." The trouble is – and trust us on this one – other things are never equal, and "external" factors are routine, not shocking.

There's a more insidious problem with the product view. Its over-simplification tips us into a flawed metric of demand and a very incomplete concept of value. The balance between supply (producers) and demand (customers) determines both the price of the product and how many products are being exchanged. When you multiply the quantity of product being exchanged by the price, you get something that the classical economists (the 19th-century forebears of today's neoclassicals) would have called *exchange value*. But if you think exchange value adequately measures the size of the market, think again.

To paraphrase Oscar Wilde: The product market view turns us into cynics who know "the price of everything and the value of nothing."[24] Exchange value based on price is just one measure of value (or of market size). An equally important concept for strategists is its forgotten classical counterpart, *use value*.[25] Use value is the value experienced by the customer; the utility of the product or service; its power to satisfy needs and wants. Use value is created – surprise, surprise – when a customer uses a product. Customers engage in value-creating processes in order to achieve their own goals, and they use their own resources and capabilities in these processes. To increase this value creation, customers interact with suppliers in a market in order to access suppliers' resources, typically packaged in the form of products. Hence, according to the use-value perspective, the goal of a supplier is not so much to produce valuable things to be exchanged as it is to help customers to create value for themselves.

Far from splitting hairs, we believe the classical distinction between exchange and use value remains key. As the distinction got lost, we all ended up equating value with exchange value. This was another dangerous simplification, and again a supply-centric one. With it we not only come back full circle to the idea that market just means aggregate demand for a product plus a wave at supply; we literally reduce markets – the central concept of all economics and the economics-based disciplines, including strategic management – to sales figures. Suddenly markets are just yesterday's sales figures spat out by a black box.

Yet, firms forget use value at their peril, for exchange value is merely a reflection of use value, as no one will pay more than a product is worth to them. And while exchange value is an abstract figure outside the average, price-taking firm's reach, use value can be innovated and boosted by the firm in countless, lucrative ways. Imagine if Uber had treated the value in its market as purely the fixed number of dollars a passenger would exchange for a conventional taxi ride. By adding the convenience and sense of control from its app, the company could entice far more people to ride with it thanks to their extra use value, and during peak periods customers were even prepared to pay the surge premium and thus exceed ordinary taxi exchange value.

### Circularity: Available Data Bias Us Toward the Product Market View

Market views and data related to these get distinctly circular. Just as the dominance of data about *markets as industry* biases us into equating a firm's context with industry, so a dominance of data about *product markets* biases us into equating markets with the exchange value of products. Measuring markets in terms of product sales is so institutionalized that other measures are seldom to be seen. Starting from industrial classification and national statistics, the dominant paradigm is to use products or product categories as the organizing idea.

It turns out industries are the only context-level classification for which detailed, comprehensive empirical data are readily available. By contrast, there are just no data to measure the size of markets according, say, to the use value they generate. How, for example, would Uber have measured the extra use value created by its uber-convenient, empowering app – other than by running this as a real-world experiment and watching?

Granted, a hole in the data can't make our case. But it is certainly conceivable that the correlation between industry growth and firm growth could be picking up demand-side causes. Hence, perhaps the growing and profitable industries are just serving growing and profitable markets.

Another institution reinforcing the product-based market views is stock market analysis (the analysts all work to neoclassical economist precepts). Strikingly, studies show that analysts fail to put a value on uniqueness in strategies or market definitions.[26] As a result, capital markets systematically discount uniqueness in their choice of companies to invest in. This, in turn, puts pressure on companies to stick to myopic choices when it comes to markets and strategies, as the analysts' models do not comprehend more creative ones. As it would seem obvious that uniqueness drives economic rents and company value, it is clear that capital markets are in need of new thinking tools as well.

## The Poor View Impoverishes Strategy from Every Angle

Little do the industry and product views of markets tell us about where markets come from or how they evolve. Instead they serve up a gruel of deterministic models such as the product life-cycle model. This blandly holds that you launch a new product to the market and it goes through a series of stages: introduction, growth, maturity and decline. Tough luck if you are in a declining market. And too bad, also, if such models don't withstand empirical scrutiny.[27]

All this is classic *black box* thinking. It says the market is an incredibly important device whose workings firms can never fathom. Indeed, the thinking is almost mystical. And if markets are mystical or unfathomable, firms cannot predict them or influence them. That makes them *given*: exogenous or external to the firm.

Whatever is given or external, strategists won't waste energy trying to influence. So, the flawed industry and product market views lead strategists to try nothing proactive regarding this incredibly important thing, the market. Let's look in more detail at how such poor market views impoverish strategies from every angle – the ways in which they build strategies on sand.

*Market opportunities as precursors to strategy*. The traditional competitive strategy playbook starts with plays to scan the external and given market for opportunities for business development, or to "do industry analysis," if you prefer that term. These opportunities form the input to the company's strategy process, whose whole point becomes planning how to realize them. In essence, the identified market opportunities are precursors of strategy. This thinking forms the flaky backbone of the many management practices grouped under the term "market orientation." Market orientation shakily prescribes that companies should acquire, share, and utilize knowledge about customers and market conditions. The utilization means that the company should adapt to changes in the market, by improving products and customer service.

*Adapting to the market is defeatist and reactive*. That buzzword "adapt" – and the same would apply to "agile" – is putting it too favorably, though. We reckon any theory saying markets are black boxes which hugely influence the firm but which can't be influenced or even properly understood by the firm is, if nothing else, *defeatist*. It should not be a boast to be market driven. As Professor Robert Burgelman[28] of Stanford describes such a *reactive* mode, "Being market driven is for wimps! Firms with ambitious strategies drive the market." Apple, Uber, and the other intuitive market shapers have understood this.

*Adapting to the market through market orientation only ekes out small gains*. Market orientation[29] says firms should learn about customers and market conditions to improve their products and customer service. But the benefits of that are circumscribed by the narrow definition of markets: "How many mobile phones can be sold per year [in China, to the youth market, and so on], and what kind of mobile phones do consumers prefer?" What's more, the McKinsey studies we discussed above show that market share gains are a very inefficient way to raise topline growth – and many executives know painfully well that those last extra market share percentage points are likely to destroy your bottom line.

*Competing for market share when everyone defines their market by product is zero-sum.* By definition a theory that tells you to compete for market share reduces your strategy to a zero-sum game. That limitation is built into not only the words "share" and "compete" but also the poor market view itself. Whole markets/industries get defined around products, so you have the insurance market, the petroleum market and so on. But since every company in the market uses the same market definition, they automatically start to view each other as competitors. And because you're defining the market in terms of the current product (rather than, say, customers and their value creation), there are scant opportunities to grow the market. *Ergo*, you end up with a self-fulfilling prophecy that competitive strategies are inevitable.

*Any narrow view that everyone subscribes to dooms your strategy to be unoriginal.* There's another point to do with the ubiquity of the received industry and product views of markets. If everyone subscribes to the same view, and that view is narrow, then your strategy ends up being "me too," unoriginal – and plain boring. Yet, is originality not the hallmark of good strategy?

*The obsession with industries and products ignores the real competition.* Meanwhile, as psychologist and Nobel prize–winning behavioral economist Daniel Kahneman would remind us, we are always prone to WYSIATI thinking: What You See Is All There Is.[30] Dwelling on industries, your own products and rivals who supply similar ones biases you toward overrating the importance of these factors. Often your customers could satisfy their needs without your product at all. For example, the real competition for a movie theater doesn't come from other movie theaters but from alternative ways of spending a couple of hours of free time: meeting a friend for coffee, reading a book, going to a cooking class. In this kind of reality, how effective are traditional competitive strategies that consider the industry boundaries sacred?

*The obsession with exchange value misses the opportunities of growing use value*. The exchange value focus overlooks the goldmine of business opportunities that resides precisely in use value – over on the demand side of the market which the industry view omits and the product view misunderstands. Because use value always sets the maximum exchange value (again, who would pay more than the value they gained?), you can increase the size of your market by creating more use value. In theory, there are unlimited opportunities for use-value creation. You can improve your current product or introduce new ones to generate more gains for your customer or "reduce his pains."

*Bottom line: the standard view misses the main chance – market-level changes and market shaping*. The bottom line is that traditional strategy practice based on poor market views misses the main chance for strategy: changes at the market level, and in particular deliberate market shaping. Standard strategy thinks small; market-shaping thinks big. As Nokia saw, changes at the market level swamp unilateral changes at the firm level. The assumption of standard competitive strategy is that you have to adapt your firm to the market and then compete for a slice of the market pie. As we'll continue to say, the insight of market shaping is that, with the right knowledge and timing, you can often adapt the market to your firm, bake a much bigger pie in the process, and carve yourself a much more ample and mouth-watering portion.

### Grains of Truth in the Poor Market View

As we said when first describing the demise of Nokia as the demise of the traditional business strategy playbook, the received wisdom is by no means totally wrong. It's just incomplete and therefore likely to lead to Nokia-type failure as soon as market conditions get highly complex or volatile, as they did in the 3G mobile telephony market and increasingly do elsewhere. Despite these shortcomings, the restricted market view based on industries or the exchange value of products contains several grains of truth.

First, the standard view does hold that it is easiest to grow in a growing market. This is true. Second, it is also true that firms can to some extent choose which markets they operate in (short of shaping the market) and that in rare circumstances a breakthrough product or technology will allow the innovating firm to create a whole new market. However, it is far from the whole truth.

For the whole truth, we need a comprehensive theory of markets and a comprehensive practical repertoire of strategy, so that we are no longer seeing markets through one eye and making strategy with one hand tied behind our back.

## EMBRACE THE RICH REALITY OF MARKET SYSTEMS

Let's pause to take stock. The previous sections marked where Nokia Mobile Phones and almost everyone else have been stuck: the traditional strategy playbook with its generic, deeply flawed views of markets. We explored those views and how they lead to all sorts of poor strategic practice. Now for the good news. As we saw from the Uber example, it is possible to approach markets and strategy in another way. This section sets out in glorious technicolor the rich reality of markets as systems for value creation.

And the next section shows how this market view leads to the new practice of market shaping.

To fill the gaps left by the incompleteness and inadequacy of those poor market views, we've gone back to basics. And we've drawn on many disciplines: not only management, economics, and marketing, but also sociology and psychology. This takes us well beyond the narrow neoclassical economics or 1950s industrial organization view of markets. We wanted a market view that would hold for all markets at all times; not only, say, Nokia's 2G market but also its 3G market. So it had to be a general model. Of course it had to be the best fit for the evidence of how markets actually work, so as to explain and predict as much as possible. We also required it to be learnable and useable so that strategy could exploit its insights.

We reckon our market view below delivers on all those things. We call it the rich reality because it captures real markets and is rich in both description and strategic possibilities. And although we and others have articulated many parts of this view in isolation, we believe that no one has articulated all the main parts, let alone put them together as a unified vision with actionable managerial tools.

## Markets Are Complex Adaptive Systems

Markets are a classic case of a complex adaptive system (CAS). Mathematicians developed CASs as a distinct category between systems that are ordered but very complicated, like the flight deck of a modern airliner, and outright chaotic systems, like weather, which is subject to the famous "butterfly effect." Other CASs include the brain, your family, any biological ecosystem, and the economy. The "adaptive" bit means the system is constantly evolving and adapting, not that you have to adapt to it.

We boldly call this theory the rich reality. It has always been true, and was already more complete than the old industry and product views even while they remained serviceable. Ever since markets started racing up the exponential curve of complexity, the way mobile phones crossed that threshold of complexity from 2G to 3G, the system view is *the only map of markets that will work*.

You'll recall Nokia CEO Stephen Elop's burning platform memo and his epiphanous but belated glimpse of "ecosystems." The latter word captures a lot about the rich reality of markets. To be picky though, it might still sound as if you and your firm have to adapt to the ecosystem, because natural evolution is all about adapting to the ecosystem and then competing in it. Trouble is, that's the whole idea we're leaving behind. The notion of natural evolution might in turn leave little room for design, whereas market shaping refers to a kind of interplay between design and spontaneous evolution. Finally, our theory of adapting the market is win-win. So whereas evolution sounds "dog-eat-dog," you could say almost our theory is in this respect just the reverse! The term we prefer is CASs. We turn to those now.

A CAS is an entity comprising many diverse parts, both living agents and nonliving things. ("Adaptive" means the system is constantly evolving and adapting, not that you have to adapt to it.) The parts depend on each other through dense interconnections. Together they behave as a unified whole. However, the whole is more than the sum of the parts, and you can't predict its behavior or properties from theirs. Unlike rigid or mechanistic systems, even very complicated ones, CASs *don't obey simple laws of cause and effect*. They have no center, let alone a central control mechanism; no master *control* at all. However, they are subject to *influence* and a *degree* of prediction. The shape of a CAS continually evolves from a combination of deliberate design influence and random "emergence." Positive and negative feedbacks, respectively, amplify or dampen the effect of stimuli on the system.

**Markets in a Nutshell**

Markets are CASs of exchange for the creation of value, which includes use value to consumers. Markets subsume industries and add multiple layers of designable elements. Rather than obeying ordinary laws of cause and effect, markets constantly evolve from both emergence and deliberate design: deliberate shaping.

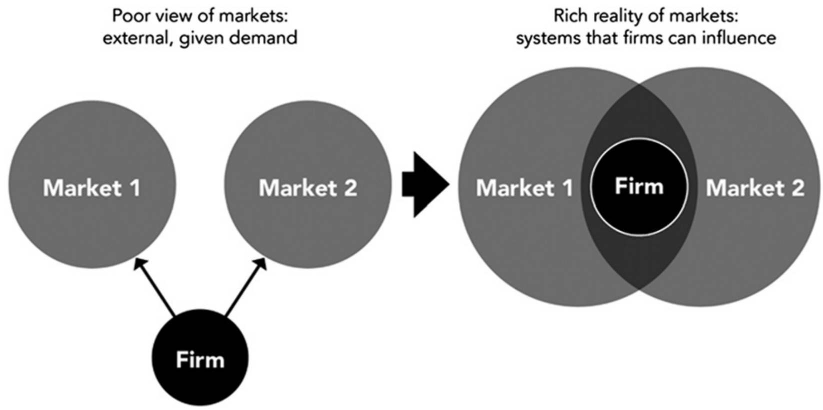
## What the System View Tells Us about Markets: Emergence, Design, and More

Because CASs don't obey ordinary laws of cause and effect, we have to throw out the simplistic view of markets as supply-and-demand curves. Also heading for the trash can is the old, linear view of strategy as a detailed master plan drawn up in phase one and executed in phase two.

On the other hand, CASs are no longer a total mystery, or a black box. They're not impenetrable, just complex! And you and I successfully navigate complex social systems every day, by using our social intuitions. At some level, we intuit the workings of social groups like the family, the neighborhood, or workplace politics.

The firm is one of the agents or actors, *inside* the market system. Although CASs don't follow ordinary cause and effect in a way that even an expert consultant can predict, they are amenable to a degree of influence by their parts, and those include the firm. Figure 1.1 illustrates the difference between the poor and rich view of markets. The left-hand side of the diagram represents the old view. Markets 1 and 2 are "out there," outside the firm's sphere of influence and containing a given demand. All that the firm can do is choose which one to enter. On the right-hand side we see the new, subtler, and richer view. The firm is part of its

**Figure 1.1. From Poor Market View to Rich Reality of Markets.**




market and exerts some influence over it. These market systems are partially overlapping, and sometimes a firm may choose to be part of – and influence – several systems at the same time.

As we'll shortly elaborate, in our theory markets coalesce from a growing and increasingly sophisticated network of buyers, sellers, competitors, distributors, other actors, and material and immaterial infrastructure, plus much more. Had you spotted that this theory also accounts for market formation and change, which the old, fixed views couldn't? CAS tells us that markets will continually evolve – and that we'll have to deal with it! So, markets have complex but comprehensible histories (origin stories, if you like) and futures. They do not pre-exist as eternal givens. Neither do they pop magically into and out of existence, nor are they fixed while they're around. The statistics and other data traditionally used as portrayals of the market are merely a snapshot, like a still from a movie, which also only captures certain dimensions and is disappointingly black and white. Sure, the numbers from yesterday represent yesterday's market, but do they represent today's? Timing will become everything.

## The *Function* of a Market System Is Exchange, for the *Purpose* of Value Creation

Specifically, markets are CASs *of exchange, for the creation of value*. And we do need to be very specific about that. Common definitions which include exchange but omit use-value and the value creation aspect sound curiously zero-sum, as though the same resource is simply being shuffled around the system in a grand version of the children's birthday game pass-the-parcel. Even saying, as people often do, that exchange in markets occurs to create value, glosses over the fact that value comes in two main flavors, and that creation really means co-creation. Just as markets divide into supply and demand, *so does value divide into exchange value to the supplier and use value to the customer/user*. In a firm-focused, production-centric view such as the traditional business strategy approach, value too easily comes to mean what is really only exchange value – the value to the producer or seller – or, worse still, the price.

Since we are writing strategy for firms not customers, we are of course *ultimately interested in the exchange value the producer can achieve*, and price is how it is denominated. You'll recall from our dissection of the product market view and later comments that *what dictates exchange value is use value: the value to the customer*, or (better put) the user. A user will willingly pay a higher price if she can get more use value out of the product. So use value should be integral to the firm's market view, and any way to increase use value offers potential gains in exchange value right back. This is where co-creation comes in. The firm's product is only one component in the customer's use value. Consider cars for instance. Greenhouse gases and traffic jams aside, the car is a magnificent invention. But without other components of the customer's value creation – roads, fuel, fuel stations, traffic rules, driving instruction, and so on – it actually has no value.

## Markets Are Socially Constructed, so You Can Reconstruct Them, too

Markets are social systems.[31] As far as we know, there are no markets without humans. Man is the trading animal, and a market is a microcosm of society. The parts that make up market systems are human agents and human creations.

The original meaning of market as the bustling town marketplace of yore – “Ye Olde Markete,” if you will – made the human side clear. Picture that marketplace and you picture the beating heart of a community where people came together to exchange things in order to get value they couldn’t get by themselves. Think: colorful and very human bazaar, not: drab, automated stock exchange.

Today, the parts of a market system are still human agents and their creations. It’s just easy to forget this in all the abstract talk about price mechanisms, mathematical models and supposedly natural, rather than human-made, laws of supply-and-demand and market forces. These are all highly depersonalized, as though they were “given” scientific truths and humans’ only involvement was in discovering them. But we’ve seen these supposed truths are incomplete and flawed. That’s hardly surprising, since they’re trying to pin down messy human behavior. Plus, they’re human postulates themselves. Even these abstract concepts are created by us humans. (The same goes for our CAS theory – only, ours doesn’t contradict itself and is a far better fit with reality!) Similarly, human made are the other aspects of market systems: the networks of people, the physical marketplace, and its rules and conventions and language, to name but a few.

The key point for us is that, being socially constructed, markets *can be consciously reconstructed*. Because humans can be persuaded, incentivized or, where laws or sheer market power are involved, coerced by other humans, the firm has a means of influencing the human agents and their creations. This is how you can turn social reconstruction to your advantage.

Fundamentally, viewing markets as shapeable systems suggests that *opportunities are not precursors* of strategy; rather they *are outcomes of deliberate efforts to shape markets*. As companies engage in market shaping activities, opportunities occur and companies need to be nimble at capturing the value from these. This indicates that finding a sustainable competitive advantage may not be that important.[32] What is important, however, is that companies have a contingency plan to deal with the upcoming prospects for an expansion of available resources or possible constraints created by other actors in the market.

Additionally, this line of reasoning recommends a change in the unit of analysis: We should not make strategy for a company – we should make strategy for the system. Furthermore, strategy ought not to be viewed as winning a zero-sum game; nor ought the focus to be on competing.[33] On the contrary, it should clarify how the company can engage in collaborative activities with market actors (suppliers, customers, and partners) in order to improve the creation of the use value. Companies that can promise improved value creation for several actors simultaneously are the ones most likely to be successful in shaping their respective markets. The job of the market leader is not to increase own market share at the expense of others, but rather about creating a positive sum game where many market actors grow the market together.

## Putting It All on the Table: Rich and Poor Views, Side by Side

As discussed in the previous sections, there are some fundamental difference in the poor view(s) of markets and the rich, systemic view. These differences also translate to serious differences in firms' strategies, measures of success, and types of innovations pursued by these firms. Figure 1.2 summarizes these differences.

## THE PAY-OFF: STRATEGIES FOR MARKET SHAPING

The pay-off to all the theory above is that it enables you to become a market shaper. In an age of acronyms, we've dubbed our strategies for market shaping "SMASH" for a couple of reasons. First, they're iconoclastic: These strategies smash the icons of old market views and old strategic wisdom. They flip the adaptation process on its head, by saying Adapt the market to your firm, not vice versa. And second, they offer enormous, largely untapped potential for growing entire markets and their profitability to the benefit of many market actors. To use a quaint phrase, we think this makes them pretty smashing; and hopefully a smash hit with your firm!

### What Is Market Shaping Anyway?

Let's back up a moment. The commonest question executives ask when we present our findings is: "What is this market shaping that you are so worked up about?" (Admittedly, we have paraphrased the question more tersely than polite clients and attendees put it, but we reckon we've captured the intent.)

Changing the definition of markets from mere exchange mechanisms to a system fostering value creation is not just semantics or purely academic debate. Think about the implications. We're claiming that, like any other human-made systems, market systems can be changed by companies, governments, and even singular individuals. This line of reasoning is radically different from mainstream strategy thinking, and opens up two exciting new options for strategists and managers.

First, if your company is operating in a market with dismal growth and profitability, you don't have to accept this as the natural world order and adapt accordingly. The near-universal imperative to adapt or die has missed the boat. If you follow the timing and techniques set out in this book, you can, under many

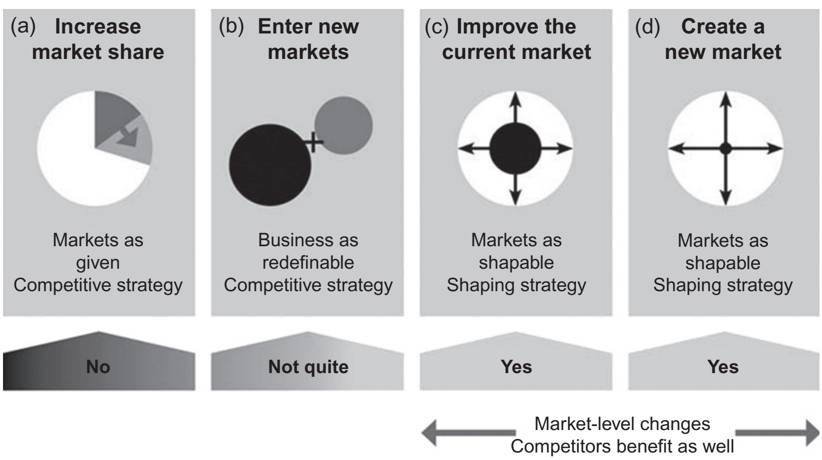
**Figure 1.2. The Poor, Restricted View of Markets versus the Rich, Systemic View.**

| Poor, restricted view | | Rich, systemic view |
|---|---|---|
| Markets defined around industries and/or products. | **Definition of markets** | Markets defined as complex adaptive systems. |
| Suppliers and customers in a value chain. | **Market structure** | A system of market actors (organizations, individuals) with interactions fostering value creation. |
| Exchange value: the value that is extracted by the supplier when selling a product. | **Value focus** | Use-value: the value that is created when a product is used in the customer's value creating process. |
| The market is external to the company. Markets are given and their development is deterministic. | **Market versus firm** | The market system is an outcome of actions by market actors. Markets are plastic and malleable. |
| A company's job is to adapt to the market, i.e., opportunities are precursors of strategy. | **Market opportunities** | A company can influence market development, i.e., opportunities are created by strategy. |
| Company level competitive strategy – how the company positions itself against competitors. | **Role of strategy** | System-level value-creating strategy – how the company supports the value creation of customers and other actors in the system. |
| To find sustainable competitive advantage. | **Ultimate goal** | Continuous renewal (as competitive advantage is always transient). |
| Product market share. Shareholder value. | **Key measurement of success** | Stakeholder/shared value. |
| Technological and product innovations | **Innovation** | + business model innovation, management innovation, and market innovation. |

circumstances, innovate ways to improve the market system so that it creates more, sometimes dramatically more, value to the end customer – and pocket at least a share. Second, you can also create entirely new market systems around your novel, but currently uncommercialized, business idea or technological innovation. In fact, it seems that taking an active stance in creating the surrounding market systems for new inventions helps de-risk commercialization projects considerably. We call these two new strategic options, improving existing market systems and creating new ones, market shaping. Figure 1.3 juxtaposes these two market shaping options against the more traditional strategic moves related to markets.

The four panels left to right in Figure 1.3 show four scenarios moving from not market shaping at all to market shaping. Panel (a), taking markets as given and eking out market share, is the opposite of market shaping, because it adapts the firm to the market. Panel (b) is close but no cigar: You redefine your business by looking at other geographies or offering totally new products or services, but still assume the market is given and unchangeable.

**Figure 1.3. What Counts, or Does Not Count, as Market Shaping.**



Panel (c) is pure market shaping: taking your existing market and remolding it.

Panel (d) is a special case of market shaping: market creation. Building on the theoretical insight that, unlike poets, markets are not only born but also made, this strategy takes a new product or service and aims to consciously attract or build the elements of a fully functioning market around it. Importantly, this entails more than just commercialization or "putting the product out there" and hoping a fully fledged market pops spontaneously into life. You will need, for instance, to deal with new norms and infrastructures – just as launching a car would be unprofitable or downright pointless without suitable legal and physical components, like roads, in the system.

### Market-shaping Strategies in a Nutshell

Market shaping is an original, evidence-based management strategy and method of innovation that reworks your markets to fit your firm, not the other way around. Market shaping can be used to create completely new market systems (for instance, around new-to-the-world technologies) as well as to improve existing market systems. Market-shaping strategies are the practical application of viewing markets as systems for fostering value creation.

*Terminology: Market shaping includes market making*. Note that we see market making as a special case of market shaping. That's because claiming that any market is brand new is slippery. A newly made market could arguably be considered a rather advanced evolution of a previous market system (or systems), at least recycling its (or their) elements. However, there will be times where it's useful to distinguish making from the rest of shaping. At such times, we will expressly refer to market making. Otherwise, from now on, please take it as read that market shaping includes market making.

## FAQs about Market Shaping

In addition to "What is this market shaping anyway?," executives typically ask us several other questions. Hence, before we go any deeper into the processes and tools related to market shaping strategies, let's rattle through the FAQs.

*What are the main ingredients for shaping markets?* This is a question that it takes the rest of the book to answer fully. There is no single formula and no linear progression of steps. It's about a continuous cycle. And there's a degree of art to it as well as science. Broadly though, market shaping begins with re-focusing your business definition, which also acts as your frame on the market, so that you can see the rich reality of your market system, and training it on the slice of the universe of possible markets which you want to start with. You then need to envisage a new shape for that market system that would benefit your firm more, by capturing a share of extra use value you'll help create (in other words, co-create) for customers. Whichever other players it requires to effect the change, you'll need to appeal to them by offering a share in the value creation as well. This involves pitching a win-win-win "story" or narrative about your proposed new shape. And you'll need to time the whole intervention to strike when the market is "hot" and malleable.

*How is market shaping strategy different from the traditional strategy playbook?* Strategies for market shaping (SMASH) differ from mainstream strategic thinking in four ways:

1. Being based on the rich reality of markets as complex systems, market-shaping strategies acknowledge that markets are human-made systems, and thus shapeable.
2. They actively seek to influence market systems, either by improving existing ones or by creating entirely new ones. Therefore, the strategic options are no longer limited to adapting and competing for more market shares.

3. As a result, market shaping brings about value-creating market-level changes.
4. Due to this, market shaping will benefit more actors in the system than just the market shaper – sometimes even the competition!

Anticipating the sound of readers wincing, we recognize that the last point is a painful realization for the ultra-competitive among our number, which we're guessing is a fair few. But keep your eyes on the prize that matters, your firm's absolute prosperity, and don't let the reflex for rivalry and head-to-head competitive plays cloud your better judgment. Given that firm performance is largely contextual, defined by your markets, market-shaping strategies will often net you greater growth and profitability obliquely than traditional competitive strategies could have. If you're not in touch with your inner altruist, you can at least treat spin-offs to the competition as a means to an end.

*Do any firms already practice market shaping?* According to recent Boston Consulting Group research,[34] only 9% of firms currently use market-shaping strategies. As far as we know, none of them use an integrated, systematic explanation of market shaping. We conclude they are practicing market shaping mostly intuitively. Having studied both the scholarly literature and the hundreds of firms we have partnered with for research or consulted for, we have consciously compiled replicable examples of market shaping in all sorts of settings for you to learn from. In the Nokia example, Apple was market shaping. Uber, as we saw, is all about market shaping. Spotify and IKEA are also other good examples you might be familiar with. But you'll meet more than 20 successful market-shaping firms in the course of the book.

*Which firms could practice market shaping? Can I?* We have developed market shaping as an integrated, systematic method. Any firm can do it. You don't have to be a giant corporation, a genius, or a jet-owning rich lister. You don't need market power in the traditional sense of monopolies and oligopolies. In fact, being big can hinder creative thinking of the kind a new strategy requires if the great idea gets tangled up in the red tape of internal processes. However, you need a good idea – a vision about how to shape your market into a better re-incarnation of that market – because market shaping works only if you are truly able to improve the market. And remember, "improving" means improvement to others as well, not just to you.

*Which environments and which markets lend themselves to market shaping?* Just as our view of markets applied to all markets, so the practice of market shaping can work in all markets. However, you'll see there are certain times and conditions which make any particular market more or less shapeable. Striking when the iron isn't hot could be unproductive. The good news is that we'll share with you our new range of special thermometers to take the temperature of the market iron.

In future, the practice of market shaping will probably only get more crucial as ongoing systemic changes such as globalization, the information revolution, urbanization, climate change, and population and lifespan growth increasingly carry markets across a threshold of complexity and instability that the standard playbooks cannot cope with. In terms of the Nokia example, expect lots more of 3G markets and lots less of 2G!

## The Strategic Baby and the Bathwater

As we rewrite the strategy playbook, we are not throwing out the old one entirely. It offers many useful plays and even a few insights into the nature of markets, notably that it is easiest to grow in a growing market. We are not claiming that market shaping is the only way of doing strategy. On the contrary, market shapers will continue to deploy traditional strategies too. For instance, they will continue to invest in innovating technology and products. But armed with an understanding of market shaping, they will see more risks and opportunities, will time their moves better, and will less likely find the rug pulled out from under them by the market shaping plays of other firms (or governments or other organizations) the way Nokia did. And there are going to be a time and place for traditional competitive strategies when companies compete for market shares, but these strategies are limited to those periods when markets are "cold" and unshapeable, or when the current market system fits nicely with your strategy and thus is playing to your strengths. Lastly, seeing the rich reality of markets systems will alert you to market-level movements and their power to either swamp or buoy unilateral strategic actions. So, even if you're not trying to shape markets yourself, at least you'll now notice which way the tide is going. Plus, you'll be privy to the information that active market-shaping firms will enjoy and thus be able to anticipate some likely market-shaping attempts.

## MAKING THE RICH VIEW ACTIONABLE: INTRODUCING THE "MARKET FAN"

If we take a simple-sounding market like the market for cars and look at it more closely in the light of social constructedness and exchange for value creation, we reveal far, far more parts and agents to the system than just the car, the seller, and the buyer. For starters, cars have no use value unless people know how to drive them, so drivers are a key actor, and driving is a core *actor competency*. There also has to be an infrastructure of roads and petrol stations, parking lots, and so on. There have to be *other actors* including service providers such as mechanics and tire repairers – even, dare we say, second-hand car salespeople and parking wardens. And as you'll know all too well if you've ever driven in one of the more lawless foreign jurisdictions, you really need commonly agreed traffic *rules* and driver norms about respecting them vehicle manufacture *standards* and *institutions* to enforce them. Plus, it wouldn't hurt to have automobile associations, lobbies for safety features like the original (Ralph) Nader's Raiders of the 1970s, and media in which to learn about the best cars on offer or how to avoid dogs and lemons, and of course there must be forums to connect buyers and sellers. Some kind of language or representation will also develop comprising not only the terms of the trade but also, for instance, road maps.

Incidentally, remember also that from a use-value perspective what you're creating is not cars but what people use them for. So it would be better to rechristen the market for cars as "the market for automobility."[35]

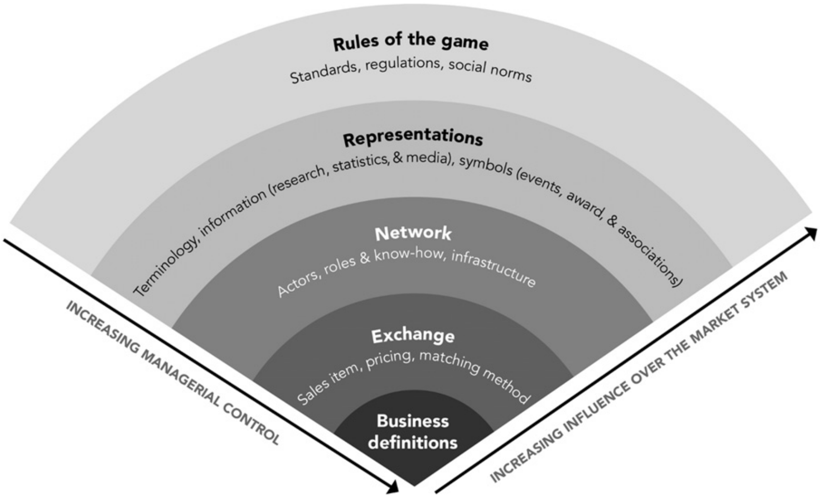
Now, you could just throw a big circle around all those components, draw lines between them, and call it the market for automobility – but that may not be very useful. We've gone much further and built up an illustration of a generic market called the Fan.[36] The Fan identifies all the parts and agents that can be influenced or shaped (designable elements) and systematically groups them into related layers. And you'll see that among these elements are many of the features which the product market view would have called the nonmarket environment or considered noncommercial concerns.[37] By saying all these features are "nonmarket" and "noncommercial" features, the company misses the point that they are all part of one, integrated system – the market system – and this whole system has huge power to enrich strategy. The Fan reveals that they are all bound up together.

The Fan looks beyond the blinders of the seller–buyer duo of the standard view to see the duo as part of a larger system of actors co-creating value. As you can see, there are five layers nested around the focal firm trying to influence its market. The closer the layers are to the center, the more managerial control the firm has over the design elements. However, the further away from the center the layers are, the more leverage the design elements have over the whole market system, if the firm's influence does succeed in reaching them. The layers are: (1) the core: the *business definition* that the focal firm is using when acting in and perceiving a market; (2) the *exchange* process by which the focal firm defines its product or services, their prices and finds customers; (3) the *network* that supports the exchange process and customers' use practices; (4) the *representations* that are used to symbolize the market; and (5) the *rules of the game* that guide all interactions in the market. In addition to the business definition design element, we identified two to three elements on the five outer levels that are potentially amenable to reshaping or design. This gives a total of *13 designable elements* that the focal firm can try to manage or influence.

*Business definition – a designable element in itself.* The innermost layer, the business definition, is the lens or frame through which the firm sees the rest of the layers and so is crucial. *Your business definition decides how many of the elements you recognize as being designable and how well you understand the ways they can be designed, as well as which slice of the overall universe of possible market you are going to position to.* Because the business definition is so crucial to seeing the market and its possible reconfigurations, it gets the whole of Chapter 2 to itself. We won't say any more about it now (Figure 1.4).

*Exchange layer – designable elements: sales item, pricing and matching method.* The firm must decide exactly what product or service it is offering and agree on a pricing logic, which means more than just "how much." For instance, is a news publisher selling hard-copy newspapers or the same content but online and diced and sliced? If online, will it go entirely behind a pay-wall, or offer parts free but with extra content for a charge (the freemium model), be pay per view, subscription, or fully free to the reader but with advertisements? Although a bystander to a transaction may see a widget being handed over for cash, what's valuable to the customer isn't the widget itself so much as a property right in it. The different property rights that the customer is really after include the right to access or use the widget temporarily (hire) or

**Figure 1.4. The Market Fan: Illuminating the Systemic Markets.**




indefinitely (outright sale) and the right to earn money from using the widget (say the widget is an input you use to produce "wodgets"). "Exchange" also involves the method of connecting sellers and buyers, which gets so sophisticated it won Alvin Roth a share of the Nobel in 2012. Roth came up with ingenious ways to more efficiently match suppliers and consumers in various contexts from kidney transplants to school choice, by making it safe for them to reveal confidential information or such basics as giving them more time to decide from multiple alternatives.

*Network layer – designable elements: actors, their roles and know-how, and infrastructure.* A market ecosystem consists of a network of actors, each with their own roles and know-how and with established relationships between them. Together they rely on an infrastructure for the market. Securing that there are competing alternatives in the market might sound like something a firm would want to shut down, but this is exactly the kind of false conclusion you get from the flawed assumptions about markets in the traditional playbook. A 2002 study[38] found that sales of innovations really took off only after an increase in the number of firms providing the innovation, and not just because more firms had sniffed the opportunity. A market-shaping firm might be well advised to foster competition, partly to legitimize the new market as a valid opportunity. Our findings suggest that the network goes beyond a firm's immediate value chain, sometimes including non-commercial actors such as industry associations and public interest groups. An obvious element to work on is the competency of your customers, for instance teaching seniors computer literacy so they will want to buy your computers. Infrastructure means physical or technical structures that support usage of your products or services. Work is still in its infancy, but one study has looked at the impact of the grocery cart on American supermarkets.[39] Our full-worked example above, the market for cars/automobility, discussed the role of roads. From the physical highway to the technical information superhighway is a small step.

*Representations layer – designable elements: terminology, information such as statistics and media outputs, and symbols such as industry events and awards*. We have seen in our discussion above how availability of market statistics can form what we conceive the market to be. Market representations are arrangements of coherent but simplified illustrations of what a market is and how it works. In the healthcare market (which itself used to be labeled medical care), the shift in labels from patient to client has aimed to make the user feel empowered rather than passive and the provider sound, and (especially in the case of doctors with God complexes or state monopolies suspected of taking patients for granted) genuinely act, more accountable. Market research sometimes aims disingenuously despite the objective label which that profession in turn gives itself – research – to destabilize markets. Media are very important for picking up emerging markets. Most markets also enjoy symbols that establish them more firmly and convincingly in our mental landscapes, a process we call "legitimizing" them. Industry events, awards, and associations are the prime examples, and these, too, provide opportunities for shaping. Consider the Academy Awards for the motion picture industry. Should they also honor artistic achievement in the games sector too, as the BAFTAs have since 1998?

*Rules of the game layer – designable elements: standards, regulations, and social norms*. The actions of the players in the market ecosystem are guided by formal and social norms. There are activities on-going in all markets whereby these norms emerge or are consciously created. Lobbyists flock to Capitol Hill, and retired Congressmen and -women in turn emerge through the revolving doors of power as highly paid lobbyists, because influencing legal norms can change everything: keeping or abolishing a tariff against cheap Asian electronics, voting a beef and cattle farming subsidy in or out, or getting supplements like "Dr Dave's Miracle Antioxidant Super-berry Juice" included or excluded from the definition of healthcare for FDA purposes. Anyone who has tried to play a DVD only to be told their machine is the wrong zone knows how the big players influencing norms can carve up the world. Social norms are less often in writing – but just as powerful as the written ones.

*Each setting of the Fan in a particular market is a snapshot in time*. You'll recall that market systems change over time. The particular setting or configuration of specific elements of the Fan at a given time in a particular market provides only a snapshot of the system. It artificially freezes the system at one point in what is actually a never-ending process of evolution. That said, as an aid to strategy, the Fan is enormously powerful, as we shall soon see, when we examine it from the core outwards.

## The Rest of the Book

Working from the core out, the Fan also supplies the structure for the next two chapters of our book. All the action in Chapter 2 takes place at the core with your business definition – the sole element you completely control. With a series of tools, exercises, and exemplary cases, we show why being critically aware of, and then optimizing, your business definition not only boosts growth and productivity but also frames your market more clearly and positions you better for actual market shaping. Market shaping proper begins in Chapter 3. There, with many more real-life examples, we give you practical guidance on how to explore and exploit the 12 elements in the remaining 4 layers of your market Fan: exchange, network, representations, and the rules of the game. For all these elements are by definition susceptible to a degree of influence and design by market shapers, as well as spontaneous emergence.

In Chapter 4, we bring all these designable elements together. We show how you can turn separate shaping actions into a cohesive market shaping strategy. This craft requires the right timing and a win-win-win arrangement. Additionally, we will present and scrutinize several generic market shaping moves – ready for you to be adopted in your markets. Finally, in Chapter 5, we'll take you through the leadership qualities of a market shaper.

## TAKEAWAYS FROM CHAPTER 1

- The strategies in the traditional playbook are built on sand. *Poor views of markets have made for poor strategy*. We've inherited both simplistic and mystical views of markets, riddled with contradictions and kept alive by self-reinforcing definitions behind our data.
- The fact is, markets are not simply industries! Industries alone are useless – supply with no demand. And adding in a sliver of demand (the customer) for a specific product, plus maybe a place, still misses the big picture. So there are no product markets either!
- The poor view impoverishes strategy from every angle. It makes strategy reactive and defeatist because *markets are allegedly "given" – fixed and unfathomable – yet somehow also as simple as supply-and-demand graphs*. It dooms firms to compete for market share in a *zero-sum game*, but ignores the real competition. It kills originality. And it misses the main chance: *to adapt markets to the firm, not vice versa*.
- Drawing on biology, psychology, and sociology as well as economics and management, we offer the rich reality of *markets as complex systems*. That's "complex" as in ecosystems and societies, rather than merely "complicated" as in machines. The complex system view tells us markets don't obey mechanical laws of cause and effect and can't be controlled or frozen in time. *They constantly evolve, partly by unpredictable emergence*.
- Markets are complex systems of exchange for *the purpose of co-creating value, specifically use value to the customer*. And when it comes to use value, the sky is the limit. That's use value as opposed to our standard metric: exchange value – aka price. Yet growing use value can ultimately grow exchange value, markets, and profits.
- The complex view of markets has always been true. The poor views scraped by only while the world itself was radically less complex. Given globalization, technological revolution, exponential network effects, and disruption-as-the-new-normal, *the complex view is the only map that will work in the 21st century*.

- Because market systems are socially constructed, you can reconstruct them, too. For, alongside random emergence, *markets evolve also by deliberate design*, or reconstruction. Other firms will design your market if you don't!
- The pay-off for all our theorizing is design writ large: SMASH. Making new markets and molding existing ones both count as market shaping. And in answer to other frequently asked questions (FAQs): *Although under 10% of firms currently shape markets, any firm can learn to be a market shaper*; but certain market phases and environments will prove riper than others.
- To make the complexity orderly and actionable, our Fan diagram divides markets into a core and four layers. The core is your firm's business definition, which also frames its perception of the layers. See Chapter 2 for this.
- Moving outward, the exchange, network, representations, and rules of the game layers of the Fan consist of another 12 designable elements. You have less influence over successive layers, but greater impact if your influence succeeds. See Chapter 3 for this.