



# **The Leader's Guide to Scenario Planning**

*The world's most successful organisations are making bolder decisions and building resilience in a world of faster, broader and uncertain change. Their secret? Scenario Planning: strategic logic and imagination for designing better futures.*

This guide to Scenario Planning provides answers to questions for leaders and their organisations contemplating the use of Scenario Planning:

1. What is Scenario Planning?
2. Why Scenario Planning?
3. How does Scenario Planning work?
4. When should Scenario Planning be used?
5. Who uses Scenario Planning?
6. What are the benefits of Scenario Planning?

#### **What is Scenario Planning?**

Scenarios are plausible, compelling yet surprising stories that describe how the future might pan out. They weave together changes in technologies, markets, politics, social values and drivers of change in the form of a “storyline.” Scenarios are not predictions, nor options from which a preferred choice should be made. Rather, they are examples distilled from many possible futures.

They serve to challenge preconceptions about the future – since shifts to new environments are always disruptive. The natural inclination of managers is to work from what is known. Scenarios force us to look at what is not very well-known, and what cannot be controlled.

As Art Kleiner (1999) explained: “Scenario Planning forces us to learn to see more clearly the possible worlds in which the unimaginable, the unthinkable, the ungodly, and the unpredictable actually come to pass. If we can feel our way around in them in our imaginations for a while, then we can prepare ourselves for whatever future does come to pass.”

Scenario Planning is used in three broad contexts:

1. Directional strategy – “given the future scenarios, what’s our best course of action?”
2. Contingency planning – “what risks and opportunities is the organisation not considering at present?”
3. Learning and team building – “what should be our company’s shared vision?”

## Why Scenario Planning?

Scenarios provide a way for the organisation to 'rehearse the future', to be better prepared and able to adapt as changes unfold.

Scenario Planning's basic value proposition is that superior performance – indeed survival of the organisation – depends on anticipating and responding to discontinuities, innovations and new trends. A resilient organisation is one that is better positioned to respond to evolving threats and opportunities.

Since the future cannot be measured, scenarios are a way to inform conjecture. And at the heart of conjecture lies a conversation that allows unconventional questions to be asked, bold new hypotheses framed, and different ways of doing things imagined.

### *Strategy in a low predictability environment*

Quantitative forecasting – economic and financial models – does not perform well in a low predictability environment, since their assumptions and structure are derived from past history. And history can be a very imperfect guide to the future. That is why under conditions of low predictability, multiple, potentially contradictory views of the future are a better way to represent knowledge than any quantitative model – no matter how sophisticated – and a better means to communicate the strategic issues.

The ability to anticipate the unexpected and develop responses is not just a valuable add-on to corporate planning practice, but potentially the single most important factor for business success in a volatile environment. Scenarios provide a framework for making decisions now – but with the medium and long-term risks and opportunities in mind.

### *Scenarios create a dialogue between risk and opportunity*

If uncertainty creates difficulties for managers, the flip-side is that this uncertainty must create opportunities for those companies best positioned to cope with it. Great opportunity can often be found in the most "risky" areas, while new risks emerge from every resource investment.

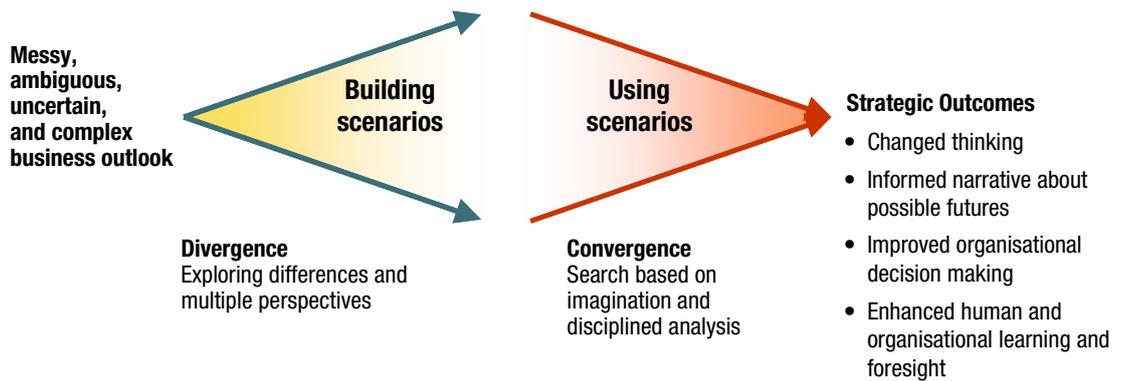
Scenarios challenge preconceptions about the future. They aim to highlight opportunities and challenges that might be overlooked in the rush to address short-term issues. Scenarios help remove the constraint of 'here and now' imperatives; and overcomes the blandness, narrowness and inward-focus of inquiry that pervade many strategic planning exercises.

Scenarios aim to overcome innate biases in decision making such as risk aversion. They challenge fundamental assumptions. A good scenario describes what it's like to deal with the external forces of change, and call upon the organisation make difficult decisions, and take action despite risks. Scenarios enable groups to think the unthinkable, speak the unspeakable, breaking out of established frameworks ('mental boxes') and open up questions that otherwise might be dismissed as heresy. And so they overcome the problem of 'groupthink' which is the suppression of ideas that are critical of the 'direction' in which a group is moving.

### How does Scenario Planning work?

The essence of the scenario process is that you research current trends and emerging developments. You determine which are predictable, which are uncertain, and which uncertainties are most influential. You base the scenarios of the future on those uncertainties, and spend time understanding the implications of those scenarios. Exhibit 1 shows the two main phases in scenario planning: building scenarios and using scenarios.

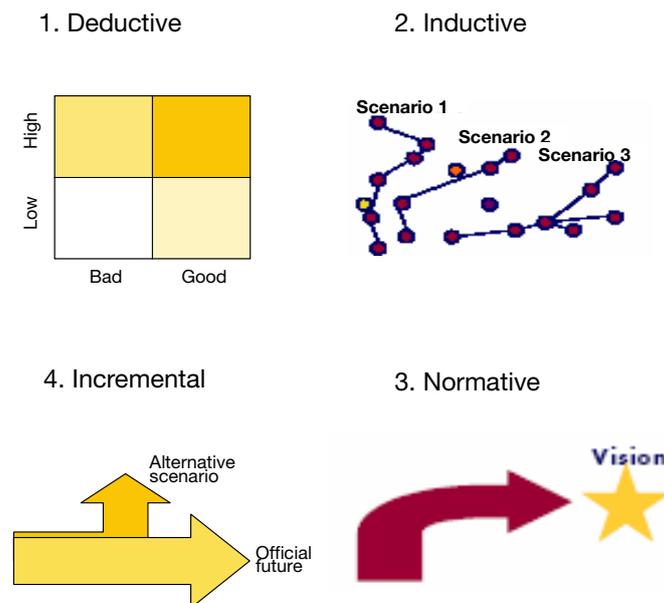
Exhibit 1 – The process of building and using scenarios



### Building the scenarios

Each scenario plot should be different, yet relevant to the focal question. Following Davis (2002), Exhibit 2 shows the four kinds of structures for building scenarios.

Exhibit 2 - The four kinds of structures for building scenarios



The four kinds of structures for building scenarios are:

1. The deductive approach is based on the two most critical uncertainties which then become the axes of a 2 x 2 scenario matrix.
2. The inductive approach clusters different events or trends that are typical of an overarching theme, and so develop a composite but consistent picture.
3. The normative approach sets up an 'end-state' scenario that is either desirable to achieve or to avoid, and then the team identifies what sequence of events might lead to the realisation of this outcome.
4. In the incremental approach the team maps out the details of "the official future" and then looks for ways that the future could deviate from that path, by reversing one or a few critical assumptions that underpins the official future.

### *Using the scenarios*

Once scenarios have been crafted, the most crucial step begins: testing the company's strategies against the scenarios, addressing the following questions. What should the company be doing under each scenario? What actions are common to all scenarios—the "no regrets" strategy? What actions work under one scenario, but are very risky under another scenario? What is the essence of the underlying formula for the organisation's success, given the range of scenarios?

The scenarios are used to develop a strategic roadmap and portfolio of initiatives to address the uncertainties and the opportunities. These initiatives may be implemented over different time frames: short term (next two years), medium term (three to five years) and long term (five years and beyond), and might include the following:

- Decisions on investments and 'real options' that build robustness against the range of scenarios;
- New capabilities which are needed, and existing capabilities which need updating;
- Initiatives to increase speed of adjustment and flexibility;
- Changes in the nature of the dialogue between key stakeholders – customers, investors, policy makers, regulators, and so on;
- Formation of new alliances and partnerships.

### *Who should be involved in a Scenario Planning program?*

A Scenario Planning program requires a group of one to two dozen people drawn from inside and outside the organisation; for example upstream and downstream stakeholders, knowledge holders, and the "curious and the creative" personalities.

Scenarios are a "deep dive" process, so they are best undertaken outside of the hustle and bustle of day-to-day business demands. Adequate time is needed for the process which often extends over many weeks or months. By investing time in the development of shared mental maps the organisation will be able to adapt more quickly, flexibly and coherently to strategic change.

There are common mistakes which should be avoided in constructing scenarios:

- Putting all the good news in one scenario and all the bad news in another;
- Best-case, worst-case, and status quo scenarios;
- Developing unrealistic, implausible scenarios.

What's needed for the scenario process to succeed is an exploratory attitude, to suspend disbelief and explore different perspectives; and a diversity of perspectives to enrich the scenarios and the strategic conversation that result.

Scenarios must be defined at the right level. Scenarios are best when they focus at a level one step more general than the decisions that need to be made, when they focus on the relevant environment for those decisions.

### When should Scenario Planning be used?

Strategy starts with identifying the changes ahead. This is why Scenario Planning is often used at the start of the strategic planning cycle. It aims to capture the bigger picture before the more detailed quantitative planning is done.

Another approach is to use Scenarios in a separate, opportunity-driven process; for example when major decisions need to be tested for robustness. Or to identify new and innovative growth options for the organisation, by providing a platform for testing specific strategies.

Scenarios are also used to assess of long-term objectives – providing concrete descriptions of a range of futures helps stimulate debate about alternative objectives.

Normative scenarios – how we would *like* the future to turn out – can be used to push an organisation or a community toward a specific perspective; in other words a better future, based on a broad dialogue and joint problem solving.

Environmental scanning enables the organization to learn about and take a position on specific assumptions on which strategy is based.

Scenario Planning is used in leadership development and coaching to stimulate personal inquiry. Building the skills of the next generation of leaders is achieved by helping them envision what their industry may look like in the decades ahead.

### Who uses Scenario Planning?

Bain & Company's Survey of Management Tools and Trends records that over 40% of corporations globally use some form of scenario or contingency planning.

Industries where scenario planning is mainly used include energy and power, finance and banking, infrastructure, I.T., logistics, science and technology, oil and gas, pharmaceuticals, telecommunications and tourism.

Corporations mentioned in the media as users of Scenario Planning include BHP-Billiton, BP, BA, British Telecom, DaimlerChrysler, Electricité de France, Electrolux, Cable and Wireless, General Electric, Honeywell, IBM, Motorola, Royal Dutch-Shell, UPS and Zurich Financial Services.

In addition to corporate and business unit strategy, scenario planners explore topics such as market scanning and new market entry, competitive strategy,

business investment decisions, mergers and acquisitions, country risk assessment, innovation and R&D priority setting, new product development, executive leadership and organisation development.

### *General Electric's "dreaming sessions"*

In 2005 GE announced a sweeping new strategy – "Ecomagination" – to promote its new "clean" technologies. The company plans to double its revenues from 17 clean-technology businesses, ranging from renewable energy and hydrogen fuel cells, to water filtration and purification systems, to cleaner aircraft and locomotive engines. To get there, GE is doubling its research spending on clean products.

Before launching the new strategy, GE invited bosses from various industries to two-day scenario planning workshops – described as "dreaming sessions" by GE's CEO Jeff Immelt. Customers were asked to imagine life in 2015 and the energy systems they would need. GE took away a clear message from these scenario workshops: rising fuel costs, ever tighter environmental regulations and growing consumer expectations will translate into demand for cleaner technologies.

### *Public Scenario Planning*

In the public sector and not-for-profit sector, Scenario Planning has been used to explore the future of education, e-Government, defence, environment and climate change, health, philanthropy, public administration, science and technology, and transportation. Users of Scenario Planning include the Australian Business Foundation, Business Council of Australia, CSIRO, the European Commission, Governments of Australia, Brunei, Queensland, Singapore, Scotland, South Africa and the United States.

A vital role for public Scenario Planning is to achieve greater policy alignment between multiple agencies and improve coordination.

### *Applying scenarios in public planning - The Mont Fleur Scenarios*

In 1994, the fledgling democracy of South Africa witnessed a unique collaboration of people in a scenario planning exercise known as the Mont Fleur project. It took place in the middle of a complex period in South Africa when the nation was unsure of how to make the transition away from apartheid.

The Mont Fleur scenario planning program brought together a diverse group of stakeholders of over twenty community workers, politicians, trade unionists, academics, economists and senior business executives. This cooperative, multi-stakeholder scenario planning process had a big and broad influence by facilitating fundamental progress in a rapidly changing environment.

Participants in the recent World Economic Forum's Engineering & Construction Scenarios to 2020 has this to say about scenario planning:

*"We live in a world that is full of uncertainty, and the scenario process lets us tackle that uncertainty head-on in a systematic way that will help us make our resource allocation decisions – and our response to unfolding events – more robust and effective."* Ralph Peterson, Chairman and Chief Executive Officer, CH2M HILL.

*“The scenario project has helped us to identify critical issues and uncertainties that have the greatest potential to impact our company and our industry over the next decade.”* Steve Hanks, President and Chief Executive Officer, Washington Group International.

*“The scenario program asks and studies what is most likely to happen and what has already happened that can create the future. It is a wonderful tool that can enable businesses to make their future.”* Ajit Gulabchand, Chairman and Managing Director, Hindustan Construction Company Limited.

### What are the benefits of Scenario Planning?

In summary scenario planning can benefit organisations in three ways:

1. Scenarios provide a solid foundation for strategy development in a dynamic environment where there is change, opportunity and uncertainty ahead
2. By educating decision makers about the alternative ways in which the future might unfold, it can help them to better prepare the organization for change
3. An explicit use of scenarios helps the executive team to adjust course in the light of events. The better the scenarios, the less frequent these surprises will be and the more successful the strategy.

The benefit of scenario planning results from more skilful action within a changing business environment – by identifying weak signals of big change ahead. Firms can achieve higher returns through more creative strategic planning that builds organizational capabilities to adapt to a changing environment.

The ability to cut through a world of information overload and uncertainty – in other words, foresight – will be among the most important requirements for organisations in the decade of uncertainty ahead. Scenario Planning helps an organisation adapt more successfully by providing:

- Early warning system. Scenarios provide a context for interpreting news and events, and help organizations keep ahead of the game. The better the scenarios, the less frequent the surprises and the more successful the strategy.
- Changed thinking. It “stretches the mind,” producing insights by the disciplined synthesis of otherwise scattered facts;
- Informed narrative about possible futures. It bounds uncertainty, by showing the range of possible futures – and reduces complexity by identifying interdependencies.
- Improved organisational decision making. It facilitates evaluation of potential actions, by placing them in a concrete setting;

Scenarios can help you build support for new initiatives, and foster openness to new perspectives. An organisation skilled at creating, acquiring, and transferring knowledge, and at modifying its behaviour to reflect new knowledge and insights, is one that will succeed in the decade of dramatic change ahead.

No longer a luxury that only the largest of organisations can support, Scenario Planning is an essential framework and process for all organisations navigating their way in a world of faster, broader and uncertain change.

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**Strategis  
Partners**

## About the Author

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Jay Horton, Founder and Managing Director of Strategis Partners, is a leading adviser to Companies and Governments in Asia and Australia on strategic management issues, including scenario planning, capital investment decision making and real options analysis, and corporate strategy.

During his twenty year management consulting career, he has worked with clients in Australia, Canada, China, Japan, Hong Kong, New Zealand and South East Asia.

Jay has played a number of leadership roles, including as a Partner of PricewaterhouseCoopers, McKinsey & Company, and Managing Director of management consultancy ORG Pty Ltd.

Jay is a regular guest lecturer at the Australian School of Management, the Sydney University School of Business & Economics, Australian School of Business at the University NSW, and the Macquarie Graduate School of Management.

Jay's qualifications include Master of Economics from Australian National University, a Bachelor of Engineering from James Cook University, and Fellow of the Australian Institute of Company Directors. He is a member of the Institute for Operations Research and Management Science.

## Contact us

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**Sydney:**

Level 57, MLC Centre  
19-29 Martin Place  
Sydney, NSW 2000  
Phone: +612 9238 6886

[info@strategispartners.com.au](mailto:info@strategispartners.com.au)

[www.strategispartners.com.au](http://www.strategispartners.com.au)

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