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Humanizing strategy

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ABSTRACT

In this article, we apply our latest thinking on knowledge to provide insights on how to reconceptualize strategy to cope with a VUCA world, epitomized recently by COVID-19. We demonstrate that business leaders must draw on phronesis, or practical wisdom, for strategy to become more future-oriented, society-focused, dynamic, and human-centric. Using in-depth case studies, we show how companies will survive in the long run if they start with a moral purpose, and end by offering value to customers, contributing to society, living in harmony with nature, and creating a new and better future. We came up with six practices that enable business leaders to create new and better futures, citing evidences from neuroscience. We conclude that humans should be at the center of strategy, driving future-making with the help of digital-led automation. Reconceptualizing strategy based on this “inside-out” approach, the reward to the company is resilience, longevity, and sustainability.

Introduction

The future may look hazy, but humans have the uncanny ability to sniff the wind, sense what lies ahead, and deal with uncertainty in order to make a better future in which to live. More than 50 years ago, Peter Drucker stated that we may not be able to predict the future, but we can “make” the future. His immortal quote has recently been backed up by neuroscience. Research about the brain has discovered that humans have an uncanny ability to see the world not only as it is, but also as it could be. We think “what if” and can, therefore, make our own future using our imagination and instinct.

In order to adapt to the new realities of our VUCA (volatile, uncertain, complex, and ambiguous) world, we draw on two research areas close to us. The first is knowledge creation, a subject we have been conducting research for a long time. The second is strategy, a subject we have been teaching at business schools both in the U.S. and Japan.

In this article, we apply our latest thinking from our research on knowledge (and now on wisdom) to provide insights on how to reconceptualize strategy for this day and age of unpredictability. We argue that strategy must become more future-oriented, society-focused, dynamic, and human-centric:

• The goal of strategy should be about making a better future, not only about generating superior financial returns.
• Maximizing the common good should be equally important to strategy as maximizing shareholder value.
From knowledge to wisdom

We postulated in our 1995 book, The Knowledge-Creating Company, that new knowledge is created by converting explicit knowledge to tacit knowledge and vice versa through an interactive process known as SECI (Socialization, Externalization, Combination, Internalization).1 Our research on knowledge creation gave rise to a whole new view of the organization – not as a machine for processing information – but as a living organism.

In that book, we emphasized the importance of the lesser-known of the two knowledge types – tacit knowledge – in creating organizational knowledge. Both explicit and tacit knowledge reside in an individual, or to use Peter Drucker’s words, in the “head” and “hand” of an individual. When knowledge management became popular in the late 1990s, however, managers and executives in the West tended to accord more value to explicit knowledge. To use a metaphor, explicit knowledge is the tip of the iceberg and tacit knowledge is the much larger base lying at the bottom of the ocean. The expression, “If we only knew how much we know” by Michael Polanyi (1996), a scientist and philosopher, points to this important body of knowledge we call tacit knowledge that lies deep under water invisibly and unconsciously.

The advent of the Internet brought with it digital-led automation, such as machine learning, Big Data, data analytics, Cloud computing, Artificial Intelligence (AI), Internet of Things (IoT), Augmented Reality (AR), and much more. Digital-led automation is making data, information, and knowledge – especially explicit knowledge – more abundant, open, and connected:

- Knowledge is becoming free, limitless, personalized, and shareable (“Just Tweet it”)
- Data, information, and knowledge are becoming indistinguishable
- The Internet, combined with social media and mobile technology, is creating a hyper-linked world

The buzz over AI has given rise to the belief by some that Singularity – the term Ray Kurzweil coined for the moment AI will supersede humans – will be at hand. The idea is that the computer will become so powerful that it will be able to deal with any challenge we throw at it or solve all of the world’s problems. That certainly has not taken place yet. Why? From a knowledge perspective, it is because AI does not have tacit knowledge embedded in it; it is all about explicit knowledge.2 In trying to solve a problem, our tendency is to rely on explicit knowledge and linear causation, even when the messy world we live in defies logical thinking.

Practical wisdom atop knowledge

To adapt to this messy world, we needed to draw on a third, often forgotten kind of knowledge called phronesis that Aristotle talked about 2400 years or so ago. It is interpreted as experiential knowledge that enables us to make prudent judgments in a timely fashion, and to take actions guided by values, principles, and morals. Among practitioners, it is better known as practical wisdom.

In 2019, we published The Wise Company as a sequel to the original book. We have come to realize that knowledge is of no value unless it is put into practice. We listened to an old Japanese proverb, “Knowledge without wisdom is a load of books on the back of an ass.” Thus, our research focus evolved from knowledge to wisdom, which explains why the title of our books evolved from “The Knowledge-Creating Company” to “The Wise Company.” We are reinforcing our research by putting wisdom atop knowledge.3

To understand wisdom better, think of “mother’s wisdom.” All of us have a mother and almost all of us gained mother’s wisdom by living with her, by watching from behind her, by being scolded by her, and by being told over and over again, to be honest, not to tell a

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1 Knowledge is created through two interactive processes in SECI. For one, two types of knowledge – tacit and explicit knowledge – interact with each other in the epistemological dimension. For another, people who create knowledge interact with each other – within a team, within an organization, and inter-organizationally – in the ontological dimension. While we had the two dimensions in mind, in reality, we didn’t incorporate the ontological dimension in the original SECI Model (Nonaka and Takeuchi, 1995). Consequently, we described the SECI process only in terms of the epistemological dimension as a conversion from tacit and explicit and vice versa: 1) Socialization: from tacit to tacit. 2) Externalization: from tacit to explicit. 3) Combination: from explicit to explicit. 4) Internalization: from explicit to tacit.

2 In 1983, Roger Schank, an educator, wrote an influential book Dynamic Memory, which focused on artificial intelligence. In 1999, he wrote Dynamic Memory Revisited, which focused on human intelligence, and reached a similar conclusion as ours – education should not be about explicit knowing but about doing things.

3 As a side note, the tentative working title of our sequel book was actually “The Knowledge-Practicing Company,” but we did not follow through with it, thinking it reflected linear thinking. We concluded that replacing Creating with Practicing was too logical and deductive for this messy world we live in today, which is why we decided to make an inductive jump by replacing the centerpiece of our title, namely Knowledge with Wisdom.
lie or cheat, not to be greedy, not to be a nuisance to others, and more. We remember mother’s wisdom because we heard her words repeatedly and ceaselessly. It did not come to us in the form of a formula, a theorem, or manual. Mother’s wisdom is appealing because it combines insights, self-sacrifice, love, and social understanding.

Mother’s wisdom is passed down generations through stories, through narratives, and becomes part of our life through practice, through action. Whereas knowledge becomes obsolete the minute it is created, mother’s wisdom endures over time. In Japanese, we go back a generation and refer to mother’s wisdom as “grandma’s wisdom package.” It is similar to the wisdom that has been passed down generations among the Indigenous communities worldwide. Because of this resilient quality, wisdom serves as a countervailing force in this world of high-velocity change.

We also realized that knowledge creation alone is insufficient for knowledge to be useful. Creation can get us new knowledge, but not the wisdom to use it properly. For knowledge to be useful, we concluded that knowledge creation has to be paired up with knowledge practice. Knowledge creation is about acquiring, accessing, accumulating, codifying, and storing knowledge. It can be embodied in new products, new technologies, new systems, new methods, new organizational structures and other forms of innovation. Knowledge practice, on the other hand, is about applying knowledge, putting it to use, disseminating it, and converting it into action.

Both mother’s wisdom and practical wisdom come to us through practice and are long-term in focus. There is a difference, however, on how scalable mother’s wisdom is compared to practical wisdom. Mother’s wisdom enriches her children, and other children around her, but practical wisdom applies more broadly, having an impact on individuals, companies, communities, and society at large. Similarly, practical wisdom elevates the knowledge creation and knowledge practice process that starts at the individual level to the societal level over time.

In the new book, we made the process more dynamic by adding a third dimension – time – to the original SECI Model and converted it into a three-dimensional model called the SECI Spiral Model (see Fig. 1 below). The SECI Spiral, as the name indicates, comes from the spiraling up of the SECI process over time. We did mention that organizational knowledge creation is a spiral process in the original book, but only in passing. We featured the spiral aspect of the SECI process more prominently in the new book to show how knowledge is created, amplified, and practiced over time repeatedly and ceaselessly.

Although not depicted clearly in Fig. 1, SECI starts with Socialization at the individual level. A dynamic interaction takes place between knowledge creation and knowledge practice within one horizontal round of SECI from Socialization to Internalization. This dynamic interaction also creates a vertical spiral movement to higher levels of ontology – from the individual level to the society level. Knowledge creation is carried out collectively by individuals, teams, and organizations as they interact with the external environment.

Not shown explicitly in Fig. 1 as well, companies make use of “creative routines” – or kata as they are called in Toyota – to adapt dynamically to the changing external environment. At Toyota, kata is defined as “a means for keeping your thoughts and actions in sync with dynamic, unpredictable conditions” (Rothen, 2010: 16). This definition suggests that although the conditions surrounding an organization are always changing dynamically, the company can develop creative routines to remain adaptive and future-focused. One of these practices is called “Thinking Two Levels Above,” which forces employees out of their silos and compels them to take a broader view. Just as the view of the landscape changes as the climber goes from the foot of the mountain to the top, this kata encourages employees to imagine what it would be like to view the world higher up in the mountain and to think “what if” about the future (Nonaka and Takeuchi, 2019; Osono et al., 2008).

Without going into details, we want to point out three features of the SECI Spiral Model. First, notice how knowledge that is created at the individual level becomes organizational knowledge, then spirals up to the inter-organizational or community level and eventually to the society level.

We use the “spinning top” as a metaphor to illustrate the dynamic nature of the knowledge creation/practice process. If the top spins with enough velocity, it will defy the forces of gravity to maintain its balance against shocks and crises coming from the external environment. For companies, that is equivalent to maintaining resilience and being sustainable. The top will fall over if it stops spinning, which, for companies, means death.

Second, we also want to draw attention to the vertical arrow in the middle, which represents practical wisdom. Companies need practical wisdom as the driving force to continue spinning so that they can make a contribution to society. As Tadashi Yanai, the CEO of Fast Retailing that operates UNIQLO stores worldwide, pointed out:

(S)ociety only recognizes companies, and permits them to survive, if they have some contribution to make from the moment a company is born. It is an instrument of the public. In other words, if companies aren’t improving society in some way, society will quickly shut them down (Nonaka and Takeuchi, 2019: 101).

Third, look at how the tip of the vertical arrow is pointed a little bit towards the right in Fig. 1. The arrow, however, can be pointed

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4 The multi-dimensionality of the SECI Spiral Model depicted in Fig. 1 works as follows. The base, shown on the horizontal axis, is made up of tacit and explicit knowledge, which represents the two ends of the epistemological dimensions. The ontological dimension is shown on the vertical axis, where each SECI cycle moves up to a higher-level ontological base, from the individual level to the organization, to the inter-organizational, the community, and finally, societal levels. The model shows that the knowledge base becomes enlarged when SECI goes through one horizontal cycle, as well as when SECI spirals up to higher ontological levels over time.

5 As shown in Fig. 2 (Nonaka and Takeuchi, 2019: 62), individual knowledge is socialized and externalized into team knowledge; team knowledge is combined into organizational knowledge; and organizational knowledge is internalized back into (upgraded) individual knowledge, while interacting with the environment throughout the conversion process.
to any direction. In other words, a company has the discretion to choose the direction it wants to move in the future. The future is wide open, 360° to be exact. Practical wisdom serves as the driving force that directs the company to choose a unique future. The future-we-want-to-make should reflect the beliefs and ideals of the company’s founder or successor, as we will see in the case of HondaJet below.

The HondaJet story

Making the future a reality requires a long time. To illustrate, let’s look at Honda’s foray into business jets. Soichiro Honda, the founder of Honda Motor, was infatuated with airplanes since his childhood days and eventually became a licensed pilot. He made it clear to everyone in the company after his success with motorcycles that he wanted to create a future in which anyone, including himself, would be able to fly an easy-to-handle and low-priced aircraft. That was his dream. As an indication of how much he wanted his vision to become a reality, the first motorcycle the company produced in 1948 was named the Honda Dream, which came with the image of a wing as its product mark on the side of the main body. Every Honda motorcycle to this day carries that wing mark.

The founder’s dream became a reality in December 2015, when the Honda Aircraft Company in Greensboro, North Carolina delivered the first small business jet to its customer in the U.S. It took the company 29 years to commercialize what industry sources described as the fastest, most energy efficient, highest altitude-reaching, quietest, largest main-cabin, largest cargo-hold, and sexiest-
looking jet in its class. The rest is history. In less than two years, the $4.85 million HondaJet became the best-selling small business jet in the U.S.A.

Seven generations of CEOs at Honda who succeeded the founder kept Soichiro’s dream alive. It was, however, a secret that only the CEO and a handful of engineers inside the company knew. Michimasa Fujino, the CEO of the Honda Aircraft Company who spearheaded the HondaJet project since its launch, was one of them. Soichiro did not even know. To make sure that the project would remain a secret, Fujino spent most of his time developing HondaJet in the U.S. He met Soichiro once, only in passing in the men’s room at a research center in Japan, but they did not exchange words. Fujino confided that he regretted not being able to tell Soichiro, who had already been retired by then, that the future the founder had envisioned would soon become a reality. Fujino followed strict orders from successive CEOs not to tell anyone about the project, but he couldn’t help feeling remorseful since Soichiro passed away few years after their silent encounter.

According to the above story, Soichiro had a dream, while Fujino made it happen. Since we used the words dream and vision interchangeably, we could also say, Soichiro had a vision, while Fujino made it a reality. Vision, as we see it, addresses the question, “What kind of a future do we want to create?” Both dream and vision are about the future, but they are about the future “we” want to create. Thus, they are both subjective and personal. Fujino also confided that the future he wants to create may not be what the founder had in mind. Having lived in the U.S. a long time, the future he wants to create is one in which American executives would be spending less time on air travel, including time at airports, and more time with their families. To go back to Fig. 1, that means the arrow may be pointing in a different direction for Honda Aircraft Company in the U.S. today as compared to the direction that the founder had in mind 70 years ago.

**Two approaches to strategy**

Most business schools around the world do not currently teach strategy with the future-we-want-to-make in mind. We would like to change that, but before we dive into doing so, let’s make sure we have a common understanding of what is currently being taught in a basic strategy course.

At the Harvard Business School, we define strategy as an “integrated set of choices” which positions a firm “in an industry” so as to generate superior financial returns “over the long run.” The foundation of strategy – what we call “blocking and tackling” to use an American football metaphor – is taught in our classroom (and now using Zoom) along the following three modules:

1. External environment (corresponds to “in an industry” above)
2. Internal activities (“integrated set of choices”)
3. Competitive dynamics (“over the long run”)

We make use of analytical frameworks that Michael Porter developed in *Competitive Strategy*, a book published in 1980, to enable students to size up the external environment (Five Forces framework), configure internal activities (Value Chain framework), and anticipate/respond to competitive dynamics (Competitor Analysis framework). If firms do these analyses right, they will most likely be able to come up with strategic positionings that generate superior, sustainable returns (*Porter, 1980; Porter and Takeuchi, 2000*).

This analytical process utilizes what we call an “outside-in” approach to strategy. Strategy is being taught by:

- first analyzing what lies outside the firm – industry structure and the competitive field (external environment)
- then choosing what to do and what not to do inside the firm (internal activities)

The outside-in approach has served us well over the years. The fact that *Competitive Strategy* is still used as a strategy textbook at hundreds of business schools around the world is a tribute to its intellectual rigor. The more amazing fact is that a revised edition of this book has never been published.

Instead, revisions have been made in the form of articles published in the *Harvard Business Review*. For example, Michael Porter responded to the criticism that thinking only about making our shareholders happy is too narrow by co-authoring “Creating Shared Value.” The CSR article was published eight years before the Business Roundtable in the U.S. issued a statement in 2019 that shareholder value is no longer everything. The message coming from 181 CEOs of the Business Roundtable was very clear – making other stakeholders (customers, employees, suppliers, and communities) happy is equally important. As Tadashi Yanai noted, “Ultimately, the company’s goal must be to make people happier … if you are always chasing money, you’ll never catch it.” (*Nonaka and Takeuchi, 2019: 101*).

**“Inside-out” approach to strategy**

We live in a time of flux and fluidity, when the pace of change is more unrelenting that in the past. It’s a tough world out there. To survive, strategy has to become more about future-making. To do so, companies have to adopt what we call an “inside-out” approach to strategy. In the HondaJet story, recall how the founder’s dream (inside) created a new future aimed at improving society at large (outside).

Our inside-out approach to strategy contrasts not only with the outside-in approach mentioned above, but also with prior approaches that focused on the “inside” as consisting of resources (resource-based view) or competencies (competency-based view). In our inside-out approach to strategy, the beliefs and ideals of the founders (or successors in the company) serve as the starting point. It
focuses on the origin of the firm, not what it has as its asset. As we see it, strategy is sparked by something subjective and personal, like dreams, gut feel, intuition, insight, imagination, inspiration, and other forms of tacit knowledge. We believe strategy originates from the heart, not from Big Data and analysis, as many consultants contend. Starting from the individual drive to make a difference in the world, strategy moves out to the societal level and into the future, as depicted in the SECI Spiral Model.

One of the fundamental questions in strategy is, “Why do firms differ?” The most likely response from the followers of the outside-in approach is, “Because they have different value chains or activity systems.” From our perspective, however, firms differ because they envision different futures. They differ because people in charge of formulating and executing strategy choose a unique future they want to create. Viewed in this way, strategy is about future-making.

Strategy is still about making a choice. In addition to "running a different race" and choosing "what not to do," which we learned from the outside-in approach, strategy is also about choosing a unique positioning with regards to the future we want to make. With practical wisdom as the driving force, the goal is directed outside, namely, to make the future world a better place in which to live. The future must extend beyond the narrow interest of the company. It must be about pursuing the common good. Only then will companies start to think of themselves as social entities that have been charged with a purpose to create lasting benefits for society. Doing so will also recover the founding agenda of the social sciences, which is to improve the human condition.

You can hear the cynics groan. That’s too idealistic, they may argue. But in *The Wise Company*, we wrote:

(C)ompanies must create a new future in order to survive. Those futures can no longer be extensions of the past; they must be leaps of faith. Leaders cannot be content analyzing situations using empirical data and deductive reasoning; they must also make inductive jumps according to their ideals and dreams. If they aren’t idealistic, they simply can’t create new futures (*Nonaka and Takeuchi, 2019: 23*).

An endorsement of the inside-out approach to strategy came from *Fast Company*, a business magazine, which raised the following question to the cynics: “What if an inside-out strategy creates more creative, resilient companies than those following the old outside-in approach?” (*Safian, 2014: 74*).

The payoff of the inside-out approach to strategy, which is widely practiced among Japanese companies, lies in the end result it brings. It comes in the form of resilience, longevity, and sustainability. Japanese companies have been criticized for not being sufficiently capitalistic – not maximizing shareholder value, not laying off employees to reduce costs, not paying compensation that will incentivize top management, and the like in the short run. But history has shown that it pays to have a long-term view. An estimated 20,000 of the 1.24 million companies in Japan have been operating for over 100 years, and about 1200 Japanese companies have been in business for more than 200 years; around 600 companies more than 300 years; and about 30 have survived for more than 500 years. And five companies have lived for more than 1000 years (*Funabashi, 2013: 274–275*).

**Six practices to make a better future**

In the remainder of the article, we examine what is it about humans that drives them to make inductive jumps into the future. We will discuss six practices that humans have carried out to make strategy become more human-centric and future-focused:

- Coping with complexity
- Adapting dynamically to reality
- Embracing “dynamic duality”
- Empathizing with others
- Narrating stories
- Living with nature

Wherever possible, we will cite evidences from recent neuroscience research that the body plays a pivotal role in how our brain works. The traditional view in brain science, known as the brain-bound view, took the stance that the brain is solely responsible for our thinking and cognition. By contrast, the “embodied cognition” view has shown that the mind must be understood in how it interacts with the physical body and the outside world (*Varela et al., 1993*).

**Coping with complexity**

The real world, to use the words of David Sax “isn’t black and white. It isn’t even gray. It is multi-colored.” He goes on to say in *The Revenge of Analog* that it is “infinitely textured, and emotionally layered. It smells funky and tastes weird, and revels in human imperfection” (*Sax, 2016: xviii*). Humans do not live in an air-tight closed world that Siri and Alexa live in, says Brandt and Eagle, a composer and a neuroscientist. Our world is open and has “porous borders that leak future. We balance an understanding of our present reality against an imagining of the future. We constantly peer over the fence of today into the vistas of tomorrow” (*Brandt and Eagleman, 2017: 250*).

Our mind is fluid – free to wonder around, to think laterally and randomly, and to make new combinations. Neuroscientist Christof Koch observes that the human brain is part of a complex integrated system in which the brain, the body, and the world operate as a dynamic system. As a result, our consciousness has “the ability to combine data from different sensors to contemplate and plan a future course of action,” says Koch (*Koch, 2012: 129*).
Adapting dynamically to reality

We have known that companies and managers possess the ability to adapt to the environment and even shape that environment, thanks to the work of David Teece on “dynamic capabilities” (Teece, 2009). As mentioned briefly earlier, companies rely on creative routines – or *kata* as referred to in Toyota – to adapt dynamically to the changing reality. Examples of these practices in Toyota include: “Ask why five times,” *kanban* (the card about components sent along the production line), *yokoten* (best practices sharing) and *jidoka* (automation).

We now know that the brain, once thought to be static, is always changing. Keith Yamashita of SY Partners, who worked closely with Steve Jobs at Apple, recently reported that the brain changes its shape in several ways: (a) by creating new neural pathways and disrupting old ones, (b) by shrinking specific parts of the brain and growing others, and (c) by lighting up particular brain regions, making it easier and more natural to switch a region depending on contexts.

In *Strategy: A History*, Lawrence Freedman, a historian of military strategy, argues that strategy must adapt to change using “soap opera” as a metaphor (Freedman, 2013). In soap operas, new characters constantly come into play and the plot lines unfold in different directions over a series of episodes, oftentimes deflected by chance events. Unlike a three-act play with a definitive ending, each episode is self-contained with no prescribed ending. We cannot predict when, where, and how the central characters and their circumstances change throughout the series. The plot in a soap opera must therefore have a built-in freedom of movement. Freedman contends that strategy is similar to a soap opera as they both have to adapt dynamically to the ever-changing reality.

Embracing “dynamic duality”

There is a strong propensity in the West to view the world in an “either/or” model. This intellectual tradition can be traced to Descartes and the Cartesian split. To use the A/B analogy, A is pitted against B, resulting in a “A versus B” setup. This intellectual tradition is reflected in the debates over dualism – such as mind versus body, subject versus object, rationality versus empiricism, materialism versus idealism, and much more. In management, it is represented by debates over machines versus humans, analytics versus intuition, economic versus societal value, exploration versus exploitation, egoism versus altruism, etc.

Take the classic “body versus mind” dualism as an example. Humans, through practice, can turn it into a “body and mind” duality. A *Fortune* editorial piece on skiing, says it all:

> You can plan one or two decisions in advance, but readiness to make an instant adjustment is always required, as everything around you is swiftly and constantly changing. In the flow, you have no time for reflective or analytical thinking. Your body needs to work in concert with the mind absolutely, simultaneously, and unconditionally (Herman, 2015: 30).

Thanks to recent findings in neuroscience, you can now kiss the Cartesian split good-bye. We have known all along that humans, compared to other living creatures in the animal kingdom, have an enormous cortex, in particular an outsized prefrontal cortex. We are now finding out that the prefrontal cortex can be trained to pay attention, absorb details, and think clearly through practice. In other words, the brain can be trained to take a divergent phenomenon, as those mentioned above, and convert it into a “both/and” setup through training.

Empathizing with others

To cultivate wisdom, humans have to empathize with others. Research in both philosophy and neuroscience is backing up our contention that humans have mastered this unique quality and practice it every day.

The German philosopher Edmund Husserl (1859–1938), who laid down the foundations of phenomenology, conducted research on how subjectivity can be shared among multiple individuals, known as intersubjectivity (Nonaka and Takeuchi, 2019). He argued that intersubjective experiences stem from empathizing with others, where intentional acts to other subjects are recognized and understood by “putting yourself in someone else’s shoes.” Husserl called this mechanism of empathy “pairing.” When two individuals become paired with one another, the narrow egoism that separates the two dissipates, making them feel as if they are directly connected to one another.

Recent studies in neuroscience show that empathy – or acting together, cooperating, and caring about others – is facilitated by basic brain functions (Nonaka and Takeuchi, 2019). For example:

- Studies on the activities of the medial prefrontal cortex present evidence that the human ability to understand other people’s minds occurs at the pre-cognitive level, that is, even before such a consideration is recognized consciously.

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6 According to Teece, dynamic capabilities refers to the particular (non-imitable) capacity business enterprises possess to shape, reshape, configure, and reconfigure assets so as to respond to changing technologies and markets and escape the zero profit condition. Dynamic capabilities relate to the enterprise’s ability to sense, seize and adapt, in order to generate and exploit internal and external enterprise-specific competences and to address the enterprise’s changing environment.

7 Keith Yamashita, “Neuroplasticity: We Can Change Our Brain,” an unpublished document prepared for Global Treehouse by SY Partners. Yamashita is the founder and chairman of SY Partners, which has more than a quarter of a century history of helping leaders and organizations transform with its base in San Francisco and New York.
• Research shows that empathetic feeling triggered by someone’s pain involves anterior insula and cingulate cortex.
• Discovery of the mirror neuron system in the human brain has opened up the possibility that “mimicking” others might play a critical role in understanding the intersubjective experiences with others.
• Scientific evidence suggests that people with active insulæ – the body sensation center – tend to have high empathy.

Although empathy is facilitated inside the brain, it needs a ba for it to expand beyond the individual level. In Japanese, a ba – which literally translates as place, space, or field – refers to the context in which relationships are forged and human interactions take place. Think of it as a temporal container for creative interaction, where the space, time, and context can be physical, virtual, or cognitive.

Empathy lays the foundation for anyone to know anything about others and the world in which we live, involving all five senses of the body, not just the brain. Emphasizing with others is synonymous with sensing and understanding others not just on a shallow intellectual level but on a deep, emotional level. To empathize on a deep level, we need to develop sharp bodily senses and cultivate compassion in our hearts that can capture the feelings of others. When we sense the feelings of others as if we are having such feelings on our own, only then can we create a sense of “us” with others. That’s what the practice of “putting yourself in someone else’s shoes” means.

Narrating stories

Stories become a prism through which humans live. Call them narratives, scripts, plots, novels, metaphors, cognitive maps, or soap operas, they define how we live. Stories are the way we understand life and imagine “what could be.” The more vivid the stories we tell of what is possible “out there,” the clearer the future becomes. As James Kerr pointed out in Legacy:

… the leader begins to bring the story to visceral life across as many channels as possible. In this way, language becomes the oxygen that sustains belief. In this way, leaders rewrite the future (Kerr, 2013: 154).

Business leaders and politicians – as well as journalists, filmmakers, and YouTubers – all know the power of stories, but novelists are a league of its own when it comes to writing epic stories. Business schools and other disciplines teach us that we should empathize with others, but “only literature offers this constant practice in doing so,” according to Gary Morson and Morton Schapiro in Cents and Sensibility. The stories that great novelists write cannot be understood through deductive logic, they contend:

Human lives do not just unfold in a purely predictable fashion the way Mars orbits the sun. Contingency, idiosyncrasy and choices – all of which allow for alternatives – play an important role (Morson and Schapiro, 2017: 9–10).

In addition to literature, history helps humans to envision “what could be done” in the future. History is the story of human activities that allows us to look back at historical events from the present, interpret and reconstruct the past, and create possible futures. History explains the “why” by describing the causality between the past and the present and the “how” as in “how has this come to be.”

Living with nature

Putting humans at the center of strategy enables us to live in harmony with nature, which has been around a long, long time – over four billion years. In our view, we homo sapiens (or “wise man” in Latin) have been plagued these days with short-termism and over-planning. Take strategic planning as a case in point. In most companies, it only covers a three- or five-year time span. Worse, a plan seldom touches our heart. Imagine Martin Luther King giving the “I have a plan” speech instead of the “I have a dream” speech. Remember what we pointed out earlier – that strategy originates from our heart.

Remember also what we mentioned earlier – brain research has discovered that humans can see the world not only as it is, but also as it could be. We have the ability to run simulations. Brandt and Eagleman, the composer-neuroscientist pair, observed that the world we live in is “the product of what-ifs built atop one another generation after generation” (Brandt and Eagleman, 2017: 245).

As natives of Japan, we are heartened by efforts to live in harmony with nature. For example, Shinto priests at the Ise Grand Shrine have been planting and rebuilding the shrine every 20 years for the last 1300 years to celebrate the renewal and the cyclical quality of nature. As this example illustrates, the practice of “oneness of self and nature,” which is one of the most important characteristics of the Japanese intellectual tradition, is still alive and kicking. Only through oneness with nature can we build a lasting future.

Reconceptualizing strategy

How do we reconceptualize strategy? We recommend making the following three fundamental changes. For companies living in a world of high-velocity change, where discontinuity is the only constant and uncertainty is the only norm, doing nothing is not an option. Not making changes will mean death. To survive, new routines are in order.

First of all, companies need to put humans at the center of strategy. Adopt an inside-out approach by letting humans formulate strategy by starting with beliefs, ideals, and intuition. Since we now know from neuroscience that the body and brain are connected, let

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8 Joichi Ito, “Resisting Reduction: A Manifesto,” in Joichi Ito (ed.) Resisting Reduction: Designing Our Complex Future with Machines (Cambridge, MA: MIT Press, pending) p. 11.
humans make use of their experiential knowledge to make strategy a way of life for all employees. Let humans be in the driver’s seat to deal with unpredictability since the brain has the ability to combine data from different sensors to contemplate a future course of action and handle unexpected and novel situations. Scientific evidence makes it clear that the brain urges humans to empathize with others, so let humans come up with “what-if” options. Let humans be in charge of pursuing the common good to ensure survival.

Second, pound the message into everyone’s head that strategy should be driven by practical wisdom. Based on our definition earlier, there are two dimensions to practical wisdom: 1) taking actions guided by values, principles, and morals, and 2) making “here and now” judgment calls. On the one hand, strategy must constantly pursue what is good for the company as well as for society. It must constantly pursue the “common good,” making people happier and improving society in some way. On the other hand, strategy needs to be dynamic and agile. Companies have to make judgments knowing that everything is contextual, make decisions knowing that everything is changing, and take actions knowing that everything depends on doing so in a timely fashion. Doing both at the same time – constant and dynamic – is the challenge facing strategy. This tension keeps everyone engaged in ensuring that the top keeps spinning continuously.

Third, make future-making the mission of strategy. Because the future is hazy, unpredictable, and leaky, strategists need to rely on story-telling in order to clarify where the company is headed. Narratives become a set of beliefs that bind the organization together, a plot that everyone in the organization can follow. Using narratives, strategy serves as a script for all employees about what the company stands for and what kind of legacy it wants to leave behind. Thinking of the future makes strategy focus on the long term. As the HondaJet story exemplified, making the future you want to create takes time. Thus, strategy is not about creating a three-year or a five-year plan. It is about making your vision, defined as “what kind of a future do we want to create?” into reality. That may take generations. To avoid short-termism, companies need to formulate strategy with the future in mind as well as with nature in mind. If you succeed in making a new future, a better future, the reward to the company is resilience, longevity, and sustainability.

Wise capitalism

We argued in this article that no company will survive in the long run if it does not start with a moral purpose, and end up offering value to customers, contributing to society, and living in harmony with nature. We close by raising the following questions: (1) Will the old notion of capitalism survive? (2) Is it time for us to evolve into a new form of capitalism in order to adapt to the new realities of our VUCA world, especially in light of what is taking place around the world with the COVID-19 crisis today?

In The Wise Company, we pointed out that capitalism, especially as practiced in Wall Street today, typically pits business and society against each other. This divisiveness has given rise to a system based on (a) maximizing shareholder value, quarterly earnings, executive compensation and incentives, (b) reducing costs by laying off employees or moving businesses offshore, (c) putting off concerns of climate change, global warming, and other environmental issues, and (d) strengthening legal compliance through the U.S. Sarbanes-Oxley Act and the like.

In July 2019, David Teece invited both of us to an international conference in Edinburgh, Scotland. The topic of the conference was on “reshaping capitalism and the global order.” It was held at the home of Adam Smith, the founder of capitalism, who passed away in 1790. At the end of the two-day conference at Panmure House, which Nonaka attended, the following declaration was signed by over 80 participants:

The first declaration of Panmure House urges international leaders to base their policies and decision-making on a set of common principles, as espoused and formulated by Adam Smith, which cherish the required values of an ethically-based liberal democratic system, a moral commitment to the well-being of our communities, and affirm responsibility to protect economic social and political freedoms, and resources, wisely avoid unintentional consequences, follow the rule of law, favor markets and prices as guides to resource allocation and a long-term view of private and private investment to support inclusive economic growth and prosperity for all.9

A month later, in August 2019, 181 CEO members of the Business Roundtable in the U.S. signed a new mission statement, as mentioned earlier. For more than two decades, it explicitly put shareholders first, but its new mission talks first about delivering value to customers, followed by employees, suppliers, communities, and lastly by shareholders. A Fortune article, “America’s CEOs Seek a New Purpose for the Corporation” explains why the switch was necessary. It talked about the changing economic, social, and political contexts in the U.S., which moved towards widening economic inequality and deepening mistrust of business in the last two decades.

These two events pre-dated the corona virus crisis, which means that we have been concerned about reshaping capitalism and the global order as well as about mistrust and divisiveness in the U.S. even before the outbreak of COVID-19. In 2019, we lived in a world where complexity was already a way of life, but with corona virus, the world has become even more unpredictable. The pandemic has not only aggravated our concerns; it is calling to question whether or not the old form of capitalism will survive. If capitalism were to survive the crisis we are facing today, it has to evolve into a new form of capitalism – call it wise capitalism – which will be based on phronesis.

The two of us are hoping to write about wise capitalism next. We wrote “The Wise Leader” ten years ago, The Wise Company last year, so why not Wise Capitalism next? Our vision is to write about a system in which the “new normal” becomes:

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9 Steve Denning, “A Roadmap for Reshaping Capitalism,” an unpublished report of The New Enlightenment Conference, held on July 1–2, 2019 at Penmure House, Edinburgh Scotland. p. 8.
• Living in harmony with society
• Having a social purpose in earning profits
• Pursuing the common good as a way of life
• Having a moral purpose in running a business
• Living in harmony with nature
• Evaluating performance based on resilience, longevity, and sustainability

Given these values, principles, and morals, we hope to create a narrative for a better future where divisiveness will be replaced with inclusivity, mistrust with empathy, and egoism with altruism. That's too much to expect, you may say. But we need new futures to survive and those futures must be leaps of faith into the vistas of the unknowable tomorrow. To repeat, we need to make inductive jumps according to our ideals and dreams. Who knows, we may have to “humanize” capitalism as well.

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Ikujiro Nonaka received his BA in political science from Waseda University in 1958, and MBA and PhD in Business Administration from the University of California, Berkeley in 1968 and 1972, respectively. Professor Nonaka was appointed a Xerox Distinguished Faculty Scholar of the University of California in 1997, Professor Emeritus of Hitotsubashi University in 2006, and University Professor of Waseda University in 2013.

Professor Nonaka was the Dean of the Graduate School of Knowledge Science, Japan Advanced Institute of Science and Technology, from 1997 to 2000. Previously he was Professor (1982–95) and Director (1985–98) at the Institute of Business Research, Hitotsubashi University. His earlier academic career included positions at Nanzan University and the National Defense Academy’s Faculty of Social Science.

Professor Nonaka’s primary research interest is to establish and disseminate the theory of knowledge-based management of companies, communities, public administration, and the nations, in order to facilitate ongoing, sustainable knowledge creation and innovation. As part of this work, he has conducted comparative research on leaders and on knowledge-creating processes in companies and organizations, and of leaders, around the world. Accordingly, he is known globally as the ‘guru’ of Knowledge-based Management, having proposed concepts and theories on organizational knowledge creation processes and leadership since the 1980s. His academic works include the SECI Model for the organizational knowledge creating process, the concept of Ba and the dynamic model of organizational knowledge creation process, the concept and abilities of wise leadership and phronesis (practical wisdom), and historical imagination and idealistic pragmatism.

Professor Nonaka has won wide-ranging recognition for his work in developing the theory of Knowledge-based Management. In 2002, Professor Nonaka was conferred with a Purple Ribbon Medal by the Japanese government, and elected a member of the Fellows Group of the Academy of Management in the United States, becoming the first Asian scholar among the Group’s members. Professor Nonaka was ranked number 20 in the Wall Street Journal’s “Most Influential Business Thinkers (May 5, 2008).” In Autumn (2010), he was conferred with the Zuiho-sho, or The Order of the Sacred Treasure, Gold Rays with Neck Ribbon, for outstanding achievement, and long service and contributions to education. In June 2012, Professor Nonaka received the Eminent Scholar Award from the Academy of International Business (AIB). In November 2013, he was presented with the Lifetime Achievement Award by Thinkers50, which is given to someone who has had a long-term impact on the way people think about and practice management. He was elected as a member of the Japan Academy in January 2016. Professor Nonaka received the Lifetime Achievement Award from the Haas School of Business at the University of California, Berkeley, on November 3, 2017, during the school’s annual gala.

Professor Nonaka has published many books and contributed numerous articles to management journals as well as other media both in Japanese and in English. Selected publications include: The Essence of Nation Management, Nihon Keizai Shimbun Shuppan-sha, 2014 (with co-authors); The Essence of Great Judgements, Diamond-sha, 2014 (with S. Ogino); The Grammar of Knowledge Creating Management for Prudent Capitalism, Toyokeizaishimpo-sha, 2012 (with N. Konno); Managing Flow: A Process Theory of the Knowledge-based Firm, Palgrave Macmillan, 2008 (with co-authors); The Essence of Strategy, Nihon Keizai Shimbun-sha, 2005 (with co-authors); Hitotsubashi on Knowledge Management, John Wiley & Sons, 2004 (with co-authors); The Essence of Innovation, Nikkel BP-sha, 2004 (with co-authors); Enabling Knowledge Creation: How to Unlock the Mystery of Tacit Knowledge and Release the Power of Innovation, Oxford University Press, 2000 (with co-authors); The Knowledge-Creating Company, Oxford University Press, 1995 (with H.Takeuchi); Strategic vs. Evolutionary Management: A U.S.-Japan Comparison of Strategy and Organization, Amsterdam: North-Holland, 1985 (with co-authors); “The Wise Leader” Harvard Business Review, May 2011 (with Hirotaka Takeuchi); “The Theory of the Knowledge-creating Firm: Subjectivity, Objectivity and Synthesis,” Industrial and Corporate Change, 14(3) 2005 (with R.Toyama); “Toward Middle Up/down Management: Accelerating Information Creation,” Sloan Management Review, Spring 1998; “Creating Organizational Order out of Chaos: Self-renewal in

10 As a matter of fact, in 2019 the World Economic Forum suggested to stop using the word “capitalism” and replacing it with “talentism.”
11 We are grateful of Professor Robert M. Grant of Bocconi University, Department of Management and Technology, for his helpful comments in reviewing this paper.
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Hirotaka Takeuchi currently teaches courses in the MBA and Executive Education programs. He is also Chair, Board of Trustees of International Christian University and Professor Emeritus of Hitotsubashi University.

Professor Takeuchi received a BA from International Christian University in Tokyo, Japan, and an MBA and PhD from the University of California, Berkeley. Professor Takeuchi’s first faculty position at Harvard was in the Marketing Unit from 1976 to 1983. Starting in 1983, he taught at Hitotsubashi University in Tokyo and served as the Founding Dean of its business school from 1998 to 2010. He returned to Harvard Business School in 2010 and serves as the Faculty Chair for Japan. Prior to his academic career, he worked at McCann-Erickson in Tokyo and San Francisco and at McKinsey & Company in Tokyo.

Professor Takeuchi’s research has focused on the knowledge creation process within organizations, the competitiveness of Japanese firms in global industries, and the link between strategy and innovation. He is the author or editor of 16 books, including The Knowledge-Creating Company: How Japanese Companies Create the Dynamics of Innovation co-authored with Ikujiro Nonaka (which won the 1995 Best New Book of the Year Award in the business and management category from the Association of American Publishers), Can Japan Compete? co-authored with Michael Porter, and Extreme Toyota: Radical Contradictions That Drive Success at the World’s Best Manufacturer co-authored with Hitotsubashi professors Emi Osono and Norihiko Shimizu (which won the Best 30 Business Books by Soundview Executive Book Summaries in 2008). His recent Harvard Business Review articles are The Wise Leader (May 2011) and Embracing Agile (May 2016).

Professor Takeuchi has received recognition in several business magazines over the years. Business Week voted him as one of the top 10 “management school professors in demand for in-house corporate education programs” in the world (1993) and recognized him as one of “The Stars of Asia: 50 Leaders at the Forefront of Change” (2001). Fortune introduced him as “among the intellectual leaders of the younger, globally-minded generation that is coming to power in Japan (1996).” Fast Company selected him as one of the “Most Creative People in Business” (2016).

Professor Takeuchi is or has been a member of the board of directors of Mitsui & Co, Daiwa Securities, ORIX, Integral, and three start-up companies, all based in Japan. He is also a director/trustee of several non-profit organizations, including Japan Society of Boston, Nonaka Institute of Knowledge, Ark Hills Club, International Christian University, and HLAB. He is is or has been an adviser to Fast Retailing, All Nippon Airways, NTT DoCoMo, World Economic Forum, Japan Association of Corporate Directors, Japan Football Association, among others. He has been a member of a number of committees and councils formed by government agencies in Japan, including the Cabinet Office; Ministry of Economy, Trade and Industry; Ministry of Finance; Ministry of Education, Culture, Sports, Science and Technology; and Ministry of Land, Infrastructure and Transport and also a member of the editorial board of Japan Marketing Journal, Journal of Knowledge Management, and Hitotsubashi Business Review.