Book Reviews

Gary C. Biddle, Editor

The University of Hong Kong

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Over the past two decades, shareholder activism has become an important element of the corporate governance landscape, with hedge funds and private equity firms starting to play an increasingly prominent role. Although hedge fund and private equity activism is widely discussed, it remains poorly understood, with scarce large-sample empirical evidence on the firms that these activists target, their strategic objectives, and the performance effects from their initiatives. Anecdotal evidence suggests that fund activism has achieved a certain degree of success in reshaping target firms, encouraging restructurings, mergers, and dividend recapitalizations, and the replacement of management and board members. Yet critics and regulators question whether hedge fund and private equity activists benefit shareholders, with numerous claims that their interventions destroy value by distracting managers from long-term projects.

Institutional Investor Activism: Hedge Funds and Private Equity, Economics and Regulation is a collection of essays wherein leading corporate governance scholars examine various aspects of the activism model adopted by now-prominent hedge funds and private equity firms, their strategies, performance, economic consequences, as well as the regulatory framework in which they operate, with important implications for both accounting research and pedagogy.

This book consists of an introduction and 20 chapters that you can read collectively or reference selectively as described below. The chapters originated from presentations made at the Activist Investors, Hedge Funds and Corporate Governance Conference organized by the European Corporate Governance Institute, the University of Amsterdam Center for Law and Economics, and the Vanderbilt University School of Law in March 2007.

Part I of the book (Chapters 2–4) reviews the evolution and state of shareholder activism in the U.S. and Europe. Chapter 2 (by Stuart L. Gillan and Laura T. Starks) summarizes the history of shareholder activism in the U.S., from the SEC’s adoption of Rule 14a-8 in 1943, through the initiation of pension fund activism in the mid-1980s and the emergence of hedge fund activity in the last 30 years. In reviewing related empirical studies, the authors highlight a lack of consistent evidence on the corporate effects of shareholder initiatives. While some studies have found positive short-term market reactions to announcements of certain kinds of activism, there is little evidence of significant changes in the business activities and long-term performance of companies targeted by shareholder initiatives. The recent emergence of hedge fund activism has provided some evidence of significant performance gains, but the long-term effects warrant more research. In Chapter 3, Lucian A. Bebchuk critically evaluates the current U.S. legal regime, accusing the system of failing to provide shareholders with effective directorial powers. The author presents statistics of director electoral challenges over the period 1996–2005. These challenges amounted to a total of 118, across all years, equivalent to less than 12 challenges per year. Bebchuk identifies procedural expenses, uncertainties regarding rival slates of directors, and the prevalence of staggered boards as primary impediments to electoral challenges and he advances various proposals for reforming directorial elections. These reforms include, among others, granting shareholders a periodic right to replace directors, instituting a default rule of majority (rather than plurality) voting, and confidential voting. According to the author, these reforms would provide shareholders additional powers to effectively monitor and replace directors. Chapter 4 (by Peter Cziraki, Luc Renneboog, and Peter G. Szilagyi) discusses shareholder activism in Europe. Compared to the U.S., empirical studies have been limited by data availability, and by the fact that European countries often have very diverse legal provisions governing shareholder access to proxy proposals. Analyzing a
sample of shareholder proposals across nine European countries between 1998 and 2008, the authors show that, relative to the U.S., shareholder proposals remain much less frequent in Europe, especially in continental Europe. The authors attribute these results to legal disparities, such as the binding nature of shareholder proposals in most European countries compared to the non-binding nature in U.S., as well as differences in activism costs. Moreover, although proposal submissions are usually preceded by a careful selection process, shareholder proposals in Europe are usually unsuccessful and accompanied by significantly negative market reactions.

Part II (Chapters 5–12) focuses on activist hedge funds, their ownership strategies, and the economic consequences from their interventions. In Chapter 5, Marcel Kahan and Edward B. Rock discuss the implications of the rise of hedge fund activism for corporate governance and control. The authors start the chapter by analyzing the differences between hedge funds’ activism and the more moderate forms of activism of traditional institutional investors. They highlight significant differences in incentives, regulatory impediments, conflicts of interests, and business strategies. The investment strategies of hedge funds often involve taking high stakes in companies in order to become activist, rather than becoming involved ex post (e.g., as a result of a failed portfolio investment). The authors then discuss potential problems that are generated by hedge fund activism, such as instances in which the interests of activist hedge funds conflict with those of other shareholders or result in excessive short-termism. The authors conclude that, at the current stage, no regulatory intervention is warranted since hedge funds usually need the support of other, less short-term oriented, constituents to affect corporate policies, and that market forces and incentive devices adopted by companies may address short-termism problems more effectively than regulation. Chapter 6 (by John Armour and Brian Cheffins) provides a different perspective by identifying the various features on the demand and supply sides of the market for corporate control hedge funds that have come to dominate the 2000s. Their list of supply-side causes includes the post-tech bubble decline in stock prices and a concomitant climate of dissatisfaction within the traditional institutional investor community. On the demand side, cheaper and ready credit lowered hedge funds’ financing costs and facilitated defensive accommodations by targets. Amour and Cheffins predict that hedge fund activism will remain a prominent feature of U.S. corporate governance in the near future.

In Chapter 7, Marco Becht et al. present the results of a detailed case study of a U.K. pension fund, the Hermes UK Focus Fund. The authors take advantage of having unlimited access to the fund’s confidential records for the period 1998–2004 to study its positions, trades, asset values, and returns. The authors find that most of the fund’s engagements were conducted through direct contact with firm executives and other institutional holders, as opposed to shareholder proposals at a company’s annual meeting. Using different categories of engagement objectives (e.g., selling non-core divisions and assets, limiting diversifying investments and acquisitions, replacing the firm’s CEO) and degrees of hostility, the authors next relate the achievement of the fund’s engagements to measured abnormal returns. The authors find that the achievement of the fund’s objectives prompted significant positive returns around their announcement dates, with mean (median) abnormal returns of 5.30 percent (3.69 percent). They conclude that the case provides the first substantive evidence that private engagements by activist funds can result in substantial returns to outside shareholders.

In Chapter 8, Alon Brav et al. use a large sample of hedge fund engagements for the 2001–2006 period to answer other important questions about the functioning and value effects of hedge fund activism. The authors argue that the new form of activism that hedge funds engage in differs significantly from previous activist efforts. Hedge funds are more flexible, incentivized, and better positioned to act as informed monitors compared to traditional institutional investors. When studying the impact of hedge fund activism, the authors find that the market reacts favorably to intervention announcements. The filing of a Schedule 13D, which reveals an activist fund’s investment in a target firm, results in large positive abnormal returns, in the range of 7 percent to 8 percent, during the [−20 to +20 trading-day] announcement window. When examining cross-sectional variations in abnormal returns, the authors find that the largest returns come from activist hedge funds that target significant changes in the firm’s business strategy (such as refocusing and spinning-off non-core assets) and are associated with improvements in target firms’ subsequent operating performance. The authors conclude that their results challenge the premises of proposals that require increased hedge fund regulations. Similar conclusions are reached in Chapter 9, in which April Klein and Emanuel Zur analyze data on 151 hedge fund confrontational activist campaigns and a comparison sample of 154 other entrepreneurial activist campaigns over 2003–2005. The comparison group consists primarily of private equity funds, venture capital firms, and asset management groups. The authors find that the two groups differ significantly in the companies they target and the post-13D filing strategies they follow. Hedge fund activists target more profitable and financially healthy firms and appear to be primarily concerned about free cash flow problems at the firms. In contrast, other entrepreneurial activists most frequently demand changes in target firms’ operating strategies, by requesting significant cuts in R&D and capital expenditures. Despite these differences, both types of activism campaigns record significantly positive market reactions around the initial 13D filing dates (i.e., 10.2 percent and 5.1 percent average abnormal returns for hedge fund and other activists’ targets, respectively) and high success rates in achieving their objectives. The authors conclude that hedge funds and other entrepreneurial activists represent a form of intervention that can contribute to long-term shareholder value creation.
Chapter 10 (by Henry T. C. Hu and Bernard S. Black) discusses problems generated by equity and debt decoupling. A first pattern of equity decoupling occurs when investors have voting rights that are greater than their economic interests in the firm. A second pattern, which the authors term “hidden-morphable ownership,” occurs when investors’ economic interests in the firm are greater than their voting rights, but can be quickly transformed to entail voting ownership as well. The authors argue that the proliferation of equity derivatives made “hidden-morphable ownership” cheaper, facilitated stealth takeovers, and created large hidden ownership positions in U.S. public companies. As for equity decoupling, debt decoupling can take many forms, with credit default swaps, other credit derivatives, and debt securitization permitting formal ownership of debt claims to be decoupled from economic exposure to the risk of default or credit deterioration of the firm. The authors argue that widespread debt decoupling can have important negative externalities, such as impeding financial restructurings, re-negotiating loan conditions, and the “freezing” of debtor-creditor relationships.

Chapters 11–12 investigate the forces underlying the recent changes in the bankruptcy reorganization process in the U.S. and the effects of hedge funds’ active participation on the nature and outcomes of the reorganizations. Chapter 11 (by Douglas G. Baird and Robert K. Rasmussen) discusses the problems stemming from the strategic activities of hedge funds that specialize in distressed debt. These actors, according to the authors, have radically changed the traditional scheme of bankruptcy reorganization, a system originally designed on the assumption that stable creditor groups coalesce around identifiable and common interests. Strategic hedge funds acting as major creditors can disrupt the committee representation system, with hedge fund involvement often leading to alliances with the firm’s managers that are against the interests of the classes of creditors. Baird and Rasmussen term these dynamics the “anti-commons problem.” In Chapter 12 Wei Jiang, Kai Li, and Wei Wang investigate more closely the role of hedge funds in bankruptcy code Chapter 11 cases. Using a sample of 474 cases over 1996–2007, the authors show that about 90 percent had an active involvement by hedge funds. This result is consistent with practitioners’ assertion that hedge funds have become the most active investors in the distressed debt market, generating approximately 50 percent of the annual trading volume in distressed debt, about 30 percent of the trading volume in leveraged loans, and 25 percent of the trading volume in high-yield bonds. The authors also find that hedge funds’ choice of distressed targets often reflects not only their firm-picking skills, but also their desire to be actively involved in the firm’s reorganization, and that the large presence of a hedge fund increases the likelihood of a successful case. These results suggest an overall positive effect from hedge funds acting as unsecured debt holders.

Part III (Chapters 13–14) investigates the structure and development of the private equity sector. In Chapter 13, Steven N. Kaplan and Per Strömberg offer an overview of the evolution of private equity activities over time. The authors start the chapter by describing the components of a typical leveraged buyout transaction, where a private equity firm buys majority control of an existing or mature firm. This arrangement is distinct from venture capital firms that typically invest in young or emerging companies, and do not obtain majority control. The chapter then reviews the empirical evidence on the effects of the changes in, e.g., the firm’s capital structures and management incentives that private equity investors typically introduce. This evidence suggests that private equity activities, on average, create economic value. In Chapter 14, Ludovic Phalippou reviews the past literature on the performance of private equity funds and replicates the results from these studies using a sample 392 U.S. buyout funds from the Preqin dataset. The authors find that the positive and significant average public market equivalent (PME) of 1.20 they find when using the Vanguard S&P 500 index as a benchmark, is comparable to the findings from prior studies, but that the results are very sensitive to the choice of the benchmark. As a result, it remains unclear whether the implications drawn from previous research remain valid.

Part IV (Chapters 15–21) provides an overview of current legal regimes. Chapters 15–17 look at the treatment of hedge funds and private equity funds under the current regulatory frameworks. Chapter 15 (by Douglas Cumming, Na Dai, and Sofia Johan) discusses potential agency problems associated with hedge fund management and the rationales for regulation around the world. While hedge funds are hardly regulated in the U.S., other jurisdictions often implement different and more onerous regulatory requirements. A central issue considered in this chapter is whether hedge funds practice regulatory arbitrage to facilitate riskier portfolio strategies. The results from a study of hedge fund strategies, fund flows, and reporting behavior the authors conduct across 24 countries offer little support for the view that hedge fund managers are actively involved in regulatory arbitrage. Chapter 16 investigates the mechanics of the recently adopted European Union Alternative Investment Fund Managers (AIFMs) reporting and transparency directives and offers some preliminary observations on their effectiveness. Chapter 17 (by Joseph A. McCahery and Erik P. M. Vermeulen) takes a closer look at the new European directives and their effects on investors’ commitment to private equity funding and the compensation arrangements between investors and fund managers. The authors argue that the new requirements will prompt significant changes in private equity limited partnership agreements, with investors getting more investor-favorable compensation terms and more control over the funds’ investment decisions.

Chapters 18–19 review the recent developments under U.S. securities law. In Chapter 18, Lucian A. Bebchuk and Robert J. Jackson, Jr. discuss a recent petition submitted to the SEC that advocates tightening the rules that govern the disclosure of blocks of stock in public companies. The authors argue that the SEC should not proceed with changes to these rules before
undertaking a comprehensive examination of their economic implications for investors, since available empirical evidence provides no basis for concluding that the tightening of disclosure thresholds would protect investors from the risk of outside block-holders capturing a control premium at shareholders’ expense. In Chapter 19, J. E. Fish examines proposed changes to Rule 14a-11 (i.e., federal proxy access rule), and makes a case for the tension between the federal requirements for the exercise of shareholder director nominating rights and the state law principles upon which the SEC purported to ground those rights. In Chapter 20, John C. Coffee lists the lessons learned from the recent proxy fight case initiated by Third Point LLC against Sotheby’s board. The chapter suggests new modes of drafting “poison pills” that raise the bar against activist intervention. The final chapter (by the book’s editors) reviews the content of the book and proposes a list of challenging questions for future research.

This book suits many audiences. It is an excellent resource for financial and governance researchers who are interested in understanding the recent developments in the activism model adopted by hedge fund and private equity firms, as well as empirical challenges to studying the effects from activists’ interventions on corporate governance and performance outcomes. It also informs on the recent calls for stricter regulatory frameworks in the U.S. and Europe. Researchers, executives, and regulators alike will find this a highly informative book to provide cogent institutional details without being overly technical. It also informs teaching by highlighting the increasingly prominent roles of hedge funds, equity firms, and their activist interventions in shaping corporate governance, including accounting policies, disclosures, and informativeness. Overall, I strongly recommend this book to anyone who is interested in developing an understanding of the advent and inner workings of hedge fund activism, a new reality in corporate governance.

FRANCESCA FRANCO
Assistant Professor of Accounting
London Business School


Managerial accounting is about value creation, but typically we start one step too late. Optimizing organizational performance makes less sense if we are fine-tuning something that should not be done in the first place, or for which potential is largely dissipated. We might rather begin by asking what endeavors will create more value, and optimize them. For years I have looked for a book to inspire students, from undergrads to seasoned executives, to begin with this first step of value creation and apply design thinking continually both to new products and to new and valuable business models in a rigorous and risk-reducing manner. Having recently assigned these books in a managerial accounting course as prologues to my usual text, I attest that they combine compellingly with managerial accounting content.

In Designing for Growth (D4G), co-authors Jeanne Liedtka of the Darden Graduate School at University of Virginia and Tim Ogilvie, CEO of Peer Insight, extend Silicon Valley’s “IDEO-style” design thinking and rigor to creating businesses versus products. Together with co-author Rachel Brozske, VP of Allison Partners and lecturer at Darden, they recently crafted a clever companion Field Book that provides step-by-step templates for value creation that they call “growth.” D4G is about working smart versus working hard or in usual ways. It is about finding ways to make money ahead of saving it. It is about optimizing business models versus organizational structures or incentives, which, while enormously important, create even more value when applied to regularized value-creating innovation. It is about hard-headed, structured, disciplined, and rigorous design thinking based on accounting numbers versus giddy and grandiose daydreaming. It is about viewing the firm as a portfolio of established business lines that design thinking innovations, by design, render obsolete.

Things that I like about D4G are its pointed and pithy prose pitched for managers versus designers, punctuated with cameos of real-world successes and failures. Featured design thinking case studies include Proctor & Gamble (P&G), Apple, Ikea, Mayo Clinic, Google, Pfizer, AARP, Kaiser Permanente, Darden and Siemens, with Kodak (digital photography) and IBM (voice recognition initially) providing poignant missed design thinking opportunities. Personal experiences are shared by those who have applied design thinking or have tried, complete with descriptions of their challenges, frustrations, and tips that they discovered. In other words, it is not theoretical or design-jargon-laced, but practical. An intuitive and sequentially referenced master graph of the design process depicts four stages and ten tools of design thinking, highlighting where you are in
the process as you read. Chapters describing each tool include “Try at home” exercises that reinforce and confirm its application, which, depending on your course design, you can select as homework or group-work assignments. At barely 200 pages, D4G is a half-day read, perfect for busy student (and flight) schedules.

To illustrate the power of design thinking, consider the case of P&G. As a world leader in consumer goods, P&G assembled teams of world-leading experts in the formulation and marketing of floor-cleaning detergents, including specialists in: detergent chemistry, cleaning effectiveness, scents, color, shelf-life, packaging, trade names, marketing audios, and visuals. With this expertise, P&G attained top-ranked market shares. Then someone asked the design question of whether customers wanted better floor-cleaning detergents or rather cleaner floors. Instantly, P&G realized that many customers do not have the time, contexts, or implements to employ floor-cleaning detergents. In fact, in many countries, precious water that is needed for drinking cannot be spared to clean floors. And yet, they want clean floors, too. This led P&G to ask design questions of what is their reality, how might P&G solve their problems, and how can P&G serve them profitably? P&G discovered that in many cultures, floors are cleaned with sticky mops and not water-based detergents. Applying this design thinking, P&G created the runaway bestseller, Swiffer, a product invented in the middle ages if not before, and now hugely popular for both dusting and floor cleaning in countries with and without abundant water. As Swiffer also illustrates, design thinking precedes and embraces operational optimization based on accounting numbers, which are elemental to its success.

D4G is a well organized in color-coded and easy-to-locate sections. It begins with an overview of The Why and How of Design Thinking (Section I), followed sequentially by sections that elaborate on four key questions or stages of design thinking: What is? (Section II); What if? (Section III); What wows? (Section IV); and What works? (Section V). Each section contains associated chapters that describe ten design tools (reviewed, in turn, below). As an end-of-book bonus, project management aids (PMAs) are provided. These are not design tools, but rather “communications protocols that successively link the design thinking process to the established project management structures of the organization,” namely, a Design Brief PMA aiding the management of What is?, Design Criteria aiding the management of What if?, Napkin Pitch aiding What wows?, and a Learning Guide aiding What works? thinking. In other words, the PMAs help implement design thinking.

What are these four key questions of design thinking about? They begin with framings of empathy (with customers, not staff), invention (to solve customers’ problems), and iteration (to get it right). Is this accounting? Absolutely! Or should be! As said in D4G, “In business, we have tended to start the growth conversation with constraints: the constraints of budgets, of ease of implementation, of the quarterly earnings focus that Wall Street dictates,” and “we’ve built mind-sets and skill sets attuned to dealing with predictability and control,” where most “business’s obsession with analysis is best suited for a stable and predictable world.” Our world? Stable? Predictable? Certainly not! “Managers need to accept that their basic belief that ‘analysis equals reduced risk’ is just plain wrong in the face of uncertainty. Hiding in your office using questionable numbers from the past to predict the future is just about the riskiest thing you can do.” By comparison “design is tailored to dealing with uncertainty.” Put another way, design versus control thinking is subjective versus rational, better versus best, do versus plan, experiment versus numerate, customer emotion versus logic, novelty versus certainty, and iterative versus abstract. In conditions of uncertainty? You choose. Great business design, as is quoted from Richard Buchanan of Carnegie Mellon, “occurs at the intersection of constraint, contingency, and possibility.” Central Park’s iconic design was won by the out-of-box three-dimensional thinking of placing city streets underneath.

D4G rightly emphasizes that design thinking also depends on rigorous business analysis for several good reasons including: novelty does not necessarily create value; value creation needs profit capture; just because we can does not mean we should do something. Thus, it takes both a well-structured process and good accounting data to reliably create value-enhancing business models. Following this reasoning, D4G poses four basic questions reflecting four stages of the business model design process: What is? explores current reality; What if? envisions a new future; What wows? makes some key choices; and What works? takes us into the marketplace. Visually in a master diagram and in accompanying text, D4G further distinguishes between divergent versus convergent thinking. Divergent thinking in the What is? and especially What if? stages looks broadly and expansively “so as to not be trapped by our usual framing and pre-existing set of solutions. After generating a set of concepts, we reverse the process by converging, progressively narrowing down our options to the most promising” in the What wows? and especially What works? stages. Accounting data are subordinate in the former and preeminent in the latter so as to promote both divergent and convergent thinking.

Perhaps surprisingly, D4G argues that pie-in-sky prognostications are not the place to start in creating value. Instead, What is? thinking steps away from the crystal ball, as “All successful innovation begins with an accurate assessment of the present, of current reality.” Nor is conformist thinking helpful, as “A lot of managers throw away all kinds of opportunities for growth before they even get started by framing the problem too narrowly.” “There is a deluge of low-quality information available from sources like the Internet. But high-quality information usually requires field research.” Also to be avoided is proselytizing new proposals. “The primary objective in this exploratory stage is not to build a ‘business case’ for any particular idea. That comes later. The purpose here is to generate ideas—not evaluate them.”
What if? is about imagining possibilities. “Having synthesized the data and identified emerging patterns, ideas begin to pop into our heads” and “it is time to move from the data-based exploratory stage to the more creativity-focused thinking. Setting jargon aside, this is where traditional thinking often falters, by starting with budgets and other constraints that discourage breakthrough thinking.

What works? is about finding the sweet spot by applying the scientific method and hypothesis testing, particularly of assumptions, where “the goal here is not uncovering the ‘truth’ [and] making better choices under conditions of uncertainty.” As D4G observes, “All design is essentially hypothesis driven.” Following hypothesis testing, rapid “low-fidelity” prototyping of models just good enough to share helps mistakes happen faster in order to discern what is working effectively.

What is? is time to get real. “There is no more effective way to reduce the risks of any growth initiative than to engage customers in designing it.” A “learning launch” is explicit about what both confirming and disconfirming data will look like in “fast feedback” cycles.

To facilitate a selective reference and assignments, here is a synopsis of Chapters 3–12 that sequentially describe D4G’s design thinking tools 1–10. Not listed but included in each chapter is an enumerated step-by-step guide for implementing each tool, complete with hints for enhanced effectiveness:

Chapter 3 describes the “meta” tool of Visualization, meta because it applies to all of the other tools. As a natural precursor to doing, Visualization engages mirror neurons that permit us to imagine physical movements and expressions without asking our muscles to enact them. Visualization significantly reduces project risk by projecting for common commitment what a textual description might conjure up differently in each of our own minds’ eyes, painted by our own training, experiences, and perceptions. Concurrent with Visualization is story-telling to create a cause (versus solving a problem) that excites and unites people. D4G suggests that to sell a challenge, show how the current state is more dangerous than anything, depict a frame of mind to take it on, define a reference fellowship, provide a chance to discuss tensions, and begin to raise possibilities. Design thinking is already underway.

To promote What is? thinking (Section II), Chapter 4 suggests the tool of Journey Mapping, where you walk a mile in your customers’ shoes and experience their interactions with your product or service. “Journey mapping gets you closer to customers’ lives, to their problems and frustrations, as you seek to understand how to create value for them. This knowledge is the most important input to the search for profitable growth.” “Along the way you are looking for the emotional highs and lows and the meaning that the experience holds for the customers. These are the key to identifying value-creating innovations.”

Behaviors to watch for during this ethnographic trek are confusion, overexertion, pain points, appropriation for a new purpose, and skipped steps. To depict customers, D4G suggests crafting personas, which for Darden’s M.B.A.s were Mainstream, Mature Ticket-Punchers, Happy Wanderers, and Map-Makers, then mapping the journey of each to reveal innovation opportunities.

Chapter 5 describes the What is? tool of Value Chain Analysis of business partners. “From it emerge important clues about your partners’ capabilities and intentions and your firm’s vulnerabilities and opportunities.” D4G advises looking for offerings that are executable, scalable, create value for you, customers, and partners, that are hard for competitors to copy, and hard for suppliers to expropriate. Not so much new here for business school content, except for seeing Value Chain Analysis as part of the design thinking process, rather than as a stand-alone technique.

Chapter 6 culminates What is? thinking by applying Mind Mapping to discern patterns in data collected from customers, suppliers, partners, and operations and to begin generating ideas. Mind Mapping helps avoid pitfalls of learning nothing from data or disagreeing about ideas they suggest and forming a “common mind” view, which is why it must be a “team sport” of “inner detective” (Sherlock Holmes) thinking. A Mind Mapping technique recommended by D4G is to open an “art gallery” of data, invite “shoppers,” offer (group) tours, pick out “good stuff,” and identify related insights, connections, evaluation criteria, and clusters of consensus.

To transition into divergent What if? thinking (Section III), Chapter 7 recommends the tool of Brainstorming, pausing to elucidate on why people hate it, and solutions. Listed are: Poor framing (don’t ask people to think “out of the box” and instead give them a box and ask structured questions); Usual suspects say usual things to push pet projects; Devolution into critiques and criticism (so withhold all judgments, and enforce it); Makes work for no use (so first get give them a box and ask structured questions); Usual suspects say usual things to push pet projects (so keep groups small and right for the session.

Chapter 8 concludes What if? thinking with the tool of Concept Development, a process of choosing the best ideas from Brainstorming, assembling them into detailed solutions, and then evaluating them using both customer and business criteria. In contrast to diverse brainstorming groups, Concept Development works best with a dedicated core team evaluating ideas against design criteria to distill (say) 200 ideas to 12 concepts to 3 customer trials to 1 concept deployment. D4G advises from experience to look for groupings rather than standouts, as “Clever combinations trump the lone ‘killer idea’ every time.”
Progressing to What works? thinking (Section IV), Chapter 9 describes the tool of Assumption Testing, which first identifies and then begins to test using thought experiments, key assumptions upon which a concept’s success hinges. Assumption Testing “acknowledges that any new business concept is actually a hypothesis” based on assumptions that must hold in order for the hypothesis to be true, and that “the sooner you find the fatal flaw in a new concept, the sooner you can either fix it with your inventiveness or move on to a more promising concept.” Key to using this tool is identifying generic business tests a new concept must “pass” in order to move forward (value test, execution test, scale test, defensibility test) and sorting data into three categories: what you know, what you don’t know and can’t, and what you don’t know but could, paying special attention to data that could prove you wrong. This is a time for evaluative discipline and not salesmanship.

Chapter 10 describes the complementary tool of Rapid Prototyping employed concurrently with Assumption Testing to iteratively experiment, test, and refine a concept. “In prototyping, you give your concepts detail, form and nuance—you bring them to life.” From experience, D4G advises to “Build prototypes early and often.” “Play with your prototypes, don’t defend them.” “Show, don’t tell.” “Sooner is better than later.” “It is all about minimizing the I’ part of ROI.” And as also admitted, “It is easy to prototype a new toothbrush, harder to prototype a new business model,” so “start small and simple.”

Progressing to What wows? convergent thinking that intersects “customers want it,” with “firms can produce it,” and “economics can sustain it” (Section V), Chapter 11 describes the tool of Customer Co-Creation, which the authors see as “one of the most significant ways to de-risk a growth project.” “In our Six Sigma world, which values perfection and polish, we tend to get anxious about showing customers unfinished, unpolished ‘stuff.’ Get over it. Innovation is about learning, and customers have the most to teach you.” D4G suggests that, whereas it is easy to fall in love with your creations, let the customer judge and do 80 percent of the talking. As an example insert, page 163 provides a sample “Invitation to a Co-Creation session” that could be sent to a customer.

Chapter 12 describes the tenth tool of a Learning Launch, whereby “an experiment [is] conducted in the marketplace quickly and inexpensively. It forms a bridge between customer co-creation and commercial rollout,” “incorporating both a physical and time dimension,” “when you are ready to ask customers to put some skin in the game.” “Design with a sharp focus on key assumptions measured by confirming and disconfirming data, and affordable loss.” Prudently, D4G advises, “Have a backup plan for everything.” Then importantly, return to the start and do it all again, continually, deliberately, by design.

Commendably, D4G doesn’t stop here. Section VI, entitled Leading Growth and Innovation in Your Organization, provides follow-ups on featured innovators to reveal who succeeded, who did not, and why, like Built to Last but fast. The authors also offer “Five Tips for Getting It Right on Your First Try” and “Ten Tips for Innovating with Speed” to help those applying design thinking achieve improved outcomes. These are beyond an Appendix that presents the “Project Management Aids” mentioned above, a reference “List of Universal Human Needs” to facilitate ethnographies, and a collection of helpful further readings.

Finally, and what made D4G click for my students, is the newly released Field Book that makes design thinking even easier to implement. The Field Book is spiral bound for laying flat, filling in, and spin-around easy viewing on creation team tabletops. Its six parts are Four Key Questions (as above), Steps from Identify Opportunity to Design the On-Ramp, Tools (as above and embellished), Templates, Resources, and, importantly, an Example Project with the templates filled in for a health-enhanced workforce at a $2.5 billion multinational.

Are D4G and its Field Book perfect? Of course not. No books are. One could quibble with some jumps of logic, assumed knowledge, and a need for rapid updating of examples. But then, they are books, not Internet sites, and their brevity appeals to an Internet generation. If you ask whether they substitute for or complement current managerial accounting content, my view is neither. I rather see them as an inherent part of managerial accounting that is essential for students to consider. Why? Because value creation relates as much and more to innovation than to optimizing pre-existing operations. Said another way, the application of design thinking to continually evolve business models, as informed and optimized by accounting data and techniques, is a compelling mindset for every enterprise, for profit and not. Should we leave this vital first step of value creation to another discipline? I think not, and these books can help to make value-creating design thinking an integral component of managerial accounting.

GARY C. BIDDLE
PCCW Professor, Chair of Accounting
The University of Hong Kong

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