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STRATEGY

HOW TO CREATE, PURSUE AND DELIVER A WINNING STRATEGY

FIFTH EDITION

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FT **Guides**

STRATEGY

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Praise for the fourth edition of *The Financial Times Guide to Strategy*

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'The new "evolutionary" section of Corporate Strategy is fascinating and great fun to read'

***Marcus Alexander**, Strategy Professor, London Business School* total corporation and think about its CORE COMPETENCIES, and then decide which BUSINESS SEGMENTS to enter.

The issue is, where does competition really occur? Is it at the level of whole corporations, or between business units within different corporations? Michael Porter states bluntly: 'Corporations don't compete, business units do.'

But Michel Robert of the resource-based view disagrees: 'It is companies that compete and not business units. In fact, what will determine a business unit's ability to compete is determined even before that business unit is formed.'

Robert goes on to assert: 'Successful companies are those that can leverage their unique set of capabilities (driving forces and areas of excellence) across the largest number of products and markets.' He quotes a number of examples, mainly of Japanese companies, where the key expertise is technological and extends across different product applications. For instance, Honda's real skill is in motors – specifically in multilevel cylinder heads with self-adjusting valves – and these skills are deployed across quite different markets – motorcycles, cars, lawnmowers and power generation equipment. In the United States, Hewlett-Packard's key competency is in instrumentation technology, used in a large range of markets from oscilloscopes to cardiac analysers; Northern Telecom Switches has a key skill in digital switch technology, which is used in PBXs, in hybrid analogue-to-digital switches, and also in fully configured offices.

Although in my account I have folded in the idea of core competencies (in Chapter 5) to take account of what underpins competitive position, the resource-based school would say that I have put the cart before the horse. If we can define the core competency or competencies, they say, we will know where we should focus, and we can then hive off or sell businesses that do not fit the core competencies.

My verdict is that the resource-based view is perfectly legitimate and it makes some good points. The companies cited by Michel Robert have generally been successful, quite possibly as a result of a top-down resource approach. I do not, however, find this a very satisfactory approach for most practical businesspeople, for three reasons:

1 It is more difficult to define a corporation's core competencies objectively than it is to observe where the corporation is strong in its individual competitive segments, measured in terms of its relative market share, trend in

market share, and return on capital. Competitive strength is the verdict of the market and has a great deal of objective reality. To say, for example, that Hewlett-Packard has a core competency in instrumentation technology does not take us very far in deciding where to focus.

2 As a matter of fact, Michael Porter is more often right than Michel Robert: competition occurs more frequently at the level of business units than whole corporations. Honda competes against Yamaha in motorcycles, and against Toyota, General Motors and Ford in cars; Yamaha doesn't make cars and the car-makers don't make motorcycles. Honda's approach based on its core competency may be valid, but it still has to take account of different competitors in individual segments, and only a segment-based positioning approach can do this. To focus exclusively on the core competency runs the risk of ignoring competition where this does not coincide with the company's own approach (which is nearly all of the time) – a very dangerous policy.

3 The resource-based approach blurs the distinction between Business Unit Strategy and Corporate Strategy. I will comment more on this in a moment, but the practical disadvantage for business unit managers with the resource-based approach is that they either have to wait for the corporation to sort out its view on its core competencies (which may take for ever), or they have to treat their own business unit as a separate mini-corporation, and work out their own core competencies, regardless of those of the whole corporation. This is not necessarily a bad thing, but unless the corporation is willing to split itself up according to differences in core competencies, it is likely to lead to conflict between the Centre and the business units. A bottom-up resource-based view is likely, in my view, to present a more honest and valid picture of a corporation's real core competencies than the top-down approach favoured by most resource-based theorists. Yet the bottom-up view is likely to be too polyglot and variegated to ever lead to an integrated, holistic view of corporate competencies, which is what the resource approach is gunning for.

My overall view is that the resource-based view has a valid point, especially for small and simple corporations. There is not necessarily an inconsistency between the resource-based and the positioning schools: it is just a pragmatic decision on whether to start at the top or the bottom. If you start at the top, you either have to de-emphasise, demerge or sell the activities that don't fit the overall core competencies. If you start at the bottom, with a positioning approach, you should be extremely mindful of the core competencies that underpin your strong positions; you should nurture and deepen those core competencies and make them more difficult for competitors to imitate; and you should think carefully about new business segments where you can deploy those competencies, preferably where you can avoid competition altogether, or, as a second prize, where you can establish leadership in the new segment.

In Part 2 I go beyond both schools of thought, developing an 'ecological' theory of strategy.

The boundaries between Business Unit Strategy and Corporate Strategy

This is really an extension of the resource-based versus positioning debate. Do you treat the division or SBU (Strategic Business Unit) as an autonomous corporation or sub-corporation, or do you start with the whole corporation, or at least the whole SBU? To the extent that you start with the whole corporation or a bigger part of it, you will need to work out the overall Corporate Strategy first. To the extent that you start at the bottom with a positioning approach, you are in effect ignoring the overall Corporate Strategy or putting it on hold for the moment. The boundary between Business Unit Strategy and Corporate Strategy is not as clear-cut as I have presented it in Part 1; it is often blurred and messy.

For example, unless we have each SBU as a self-sufficient mini-corporation, with its own balance sheet and control of its own cash flow and financing, there must be a central process of resource allocation, either at the divisional or corporate level. Therefore, the division may have to exercise some of the functions of 'the Centre', and, in effect, have a Corporate Strategy. In a way, Randy Mayhew of UTC is in fact a Centre manager: he has to allocate resources across his segments, he has to nurture his core competencies, he has to lead and motivate, he has to be a catalyst for corporate learning, and he has to control budgets and cash flows at a 'mini-central' level before reporting to his head office. I discuss these points further in Part 2. For the moment, just remember that the boundaries between the role of the Centre and the roles of the business units are permeable and to some extent subjective, and certainly not as clear-cut as Part 1 implies.

Planned strategy versus emergent, crafted and evolutionary strategy

'Strategic planning' has an old-fashioned, Stalinist ring to it. In the 1970s, multinational corporations built up huge planning departments at head office: General Electric had 200 such planners, and also bought in large amounts of strategic consulting to bolster these meagre resources. It was widely recognised, in time, that such efforts did more harm than good. They took power and initiative away from the operating managers, and increased the power of the Centre. In 1983 the new chief executive of General Electric, Jack Welch, wisely dismantled the whole department.

More recently, the whole idea of 'strategic planning' has come under attack, regardless of who does the planning. Partly this is because it is recognised that it is difficult to predict the future, and to plan for it implies lack of respect for the chance occurrences of life. It is better to 'go with the flow' and respect market feedback than to stick to a plan that won't work. Partly, it is the related idea that strategy should be 'crafted' rather than 'planned': it should be a creative and intuitive interaction between the firm's aspirations and results in the marketplace. This view, eloquently extolled by Henry MINTZBERG, the Canadian academic, claims that planning necessarily involves overdefinition and categorisation of business reality, which is fluid and constantly evolving. Data-gathering and analysis are the key to planning, Mintzberg says, whereas the true key to good strategy is sensitivity to market opportunities, the creation of superior products and service, and the crafting of strategy by those at all levels in the organisation.

Mintzberg really does have a point. I am all in favour of strategy that emerges from the lower reaches of the organisation, as a result of trial and error and continual experimentation. I do not believe that strategy has to be written down or incorporated into fancy charts with masses of numbers as back-up. The best strategy is one that is simple and that everyone can remember. But my experience as a consultant has convinced me that one effective way of getting the debate on strategy going – and casting a great deal of light on a firm's real strengths, very quickly – is to go through the sort of exercise described in Part 1. The value of the exercise is not so much in the data and analyses generated – though these do have some value – as in the concepts that lie behind the framework. It's all very well for a professor of strategy to dream about crafting strategy as he goes along. He'd probably make a good job of it, because he knows the basic concepts. For the rest of us, structure helps. But the structure is only a guide and a beginning; and we can layer on top of it all the good things that Mintzberg extols.

Strategy as art rather than science

Another related debate is, is there really such a thing as 'management science'? Are there general rules, or is business just 'one damn thing after another'? If business is really a science, then strategy textbooks, professors of management, business schools, rational analysis, and billions of dollars spent on young and inexperienced, but formidably intelligent, consultants – all these things make sense. If business is really just an art, with no general rules, then experience, judgement and luck are all that matter.

I steer a middle course on this. I'm very influenced by the idea from chaos theory that business is 'fractal', which basically means 'the same pattern but with infinite variety'. Coastlines, clouds, trees and leaves are all fractal. Each one is different, but recognisably similar. If you've observed vast stretches of coastline, you stand a better chance of knowing which way it will go beyond the horizon; but you may still be wrong. Rules of thumb about business are useful, but they are more useful when they are specific to particular types of business. Each business is different, but some are more similar than others. Market share is nearly always of some value, but more valuable in particular types of business than in others. Competitive advantage, by definition, is always useful, but the ways of establishing competitive advantage are manifold. Observation of what works well is usually a better method of identifying competitive advantage than a priori theorising. There is a symbiotic relationship between thinking and action, between analysis and observation, between mental models and experience, between theory and intuition. Ultimately, though, decisions are generally made by intuition. 'Were that not true,' as Bruce HENDERSON observed, 'all problems would be solved by mathematicians.'

PART 2

CORPORATE STRATEGY