

13 Implementing Corporate Strategy: Managing the Multibusiness Firm

Some have argued that single-product businesses have a focus that gives them an advantage over multibusiness companies like our own—and perhaps they would have, but only if we neglect our own overriding advantage: the ability to share the ideas that are the result of wide and rich input from a multitude of global sources. GE businesses share technology, design, compensation and personnel evaluation systems, manufacturing practices, and customer and country knowledge.

—JACK WELCH, CHAIRMAN AND CEO, GENERAL ELECTRIC COMPANY, 1981–2001

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Introduction and Objectives

The key feature of the multibusiness firm is that—whether organized as business units, divisions, or subsidiaries—they comprise a number of separate businesses that are coordinated and controlled by a corporate headquarters. These businesses may be organized around different products (e.g., Samsung Electronics), different geographical markets (e.g., McDonald's), or different vertical stages (e.g., Royal Dutch Shell). While the individual businesses are responsible for most business-level decisions, both strategic and operational, the headquarters is responsible for corporate strategy and issues that affect the company as a whole.

The three previous chapters have addressed the three key dimensions of corporate scope: vertical integration, international expansion, and diversification. In relation to all three, the critical issue has been whether the diversified company can create value by operating across multiple businesses. However, value is only realized if the benefits from exploiting these linkages are not outweighed by the additional costs of managing the multibusiness company. This raises several issues. How should corporate strategy be formulated and linked to resource allocation? How should the corporate headquarters coordinate and control the businesses? What roles and leadership styles should corporate managers adopt? Under what kind of governance structure should corporate managers operate? To answer these questions, we must look closely at the activities of the corporate headquarters and its relationships with the businesses.

By the time you have completed this chapter, you will be able to:

- ◆ Comprehend the primary strategic role of corporate managers: creating value within the businesses owned by the company.
- ◆ Apply the techniques of portfolio analysis to corporate strategy decisions.
- ◆ Understand how the corporate headquarters manages the linkages among the different business units within the company.
- ◆ Appreciate the tools and processes by which the corporate headquarters influences the performance of its individual businesses.
- ◆ Understand how corporate managers can stimulate and guide strategic change.
- ◆ Recognize the governance issues that impact the work of managers within the multibusiness corporation.

The Role of Corporate Management

Common to decisions over vertical integration, international expansion, and diversification is the basic condition that the benefits from extending the scope of the firm should exceed the administrative costs of a larger, more complex corporate entity. This

implies that the formulation and implementation of corporate strategy are inseparable: decisions over corporate scope must take account of both the benefits and the costs that arise from extending (or reducing) corporate scope which depend upon how corporate strategy is implemented. To investigate these benefits and cost, we need to direct our attention to the mechanisms through which multibusiness corporations create value for the businesses they own.

In this chapter we shall focus on four activities through which corporate management adds value to its businesses:

- managing the corporate portfolio
- managing linkages across businesses
- managing individual businesses
- managing change in the multibusiness corporation.

The four sections that follow consider each of these activities, establish the conditions under which they create value, and specify what this implies for the role of the corporate headquarters.

Managing the Corporate Portfolio

The simplest form of multibusiness company is one that assembles independent businesses under common ownership and neither intervenes in their management nor exploits linkages between them. The corporate executives in this type of company are engaged in portfolio management: buying and selling businesses and managing the allocation of capital among them. Can such portfolio management add value to a set of businesses in excess of the cost of the corporate headquarters and transaction costs of acquiring and disposing of businesses? Ask Warren Buffett, the foremost exponent of portfolio management who has built Berkshire Hathaway out of 65 mostly unrelated acquisitions (see Strategy Capsule 13.1).

For portfolio planning to create value, the essential requirement is for corporate management to be adept at spotting undervalued companies (that is, to be better than the stock market in recognizing the long-term profit potential of certain companies) and to be better than capital markets at allocating capital among different businesses. The more efficient are the financial markets, the less scope there is for portfolio management wizards such as Warren Buffett.

Even if it is not their primary source of value creation, portfolio management—determining which businesses the company should be in and managing resource allocation among them—is an important corporate management function for all multibusiness companies. For this purpose, *portfolio planning matrices* are a widely used strategy tool among multibusiness firms. By showing the strategic positioning of a firm's different businesses, they can be used to analyze their value-creating prospects (see Strategy Capsule 13.2).

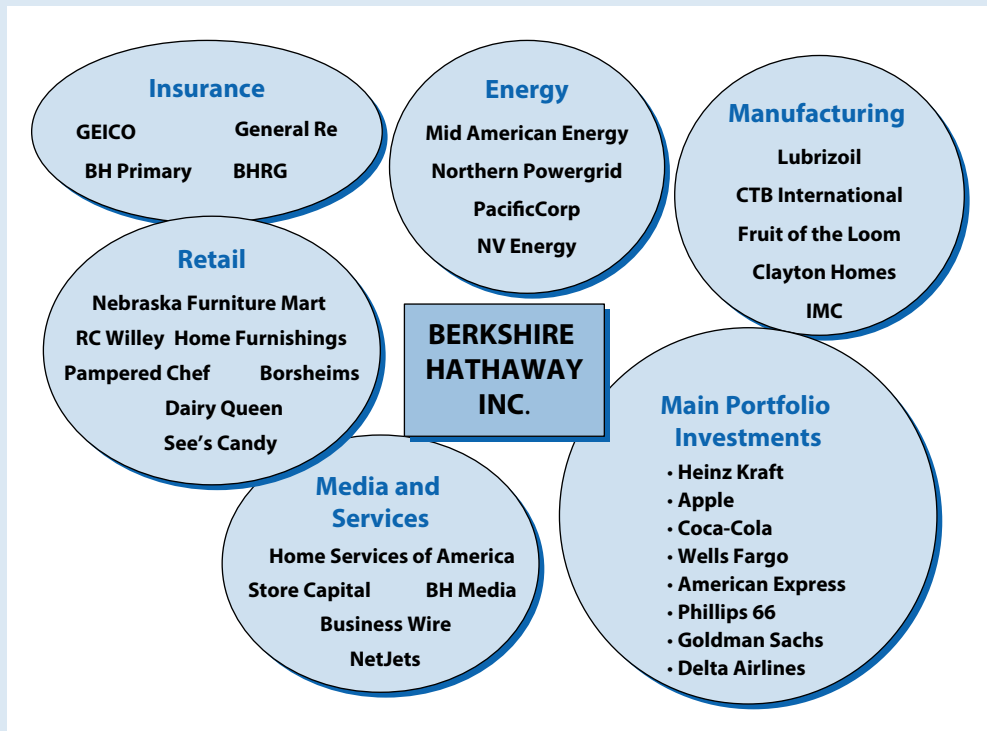
STRATEGY CAPSULE 13.1

Berkshire Hathaway, Inc.

Berkshire Hathaway comprises 63 operating subsidiaries (some of which are shown in Figure 13.1) and a headquarters in Omaha, NE, that comprises 25 employees. It is America's third biggest company by revenue with profits second only to Apple. It follows a simple portfolio management strategy that has been executed since 1970 by its 86-year-old chairman and CEO, Warren Buffett. That strategy involves selecting companies that possess a "wide moat" (=sustainable competitive advantages), that compete in industries with sound

long-term prospects, and whose stock market valuation is sufficiently low to permit a sizable upside potential. Buffett's stock picking ability is reinforced by rigorous capital allocation: "We move huge sums from businesses that have limited opportunities for incremental investment to other sectors with greater promise. Moreover, we are free of historical biases created by lifelong association with a given industry and are not subject to pressures from colleagues having a vested interest in maintaining the status quo."

FIGURE 13.1 The Warren Buffett portfolio: Some of Berkshire Hathaway's businesses



Managing Linkages Across Businesses

In relation to vertical integration, international strategy, and diversification (Chapters 10, 11, and 12), we established that the main opportunities to create value arise from exploiting the linkages between businesses. These include the benefits from sharing and transferring resources and capabilities and avoiding the transaction costs of markets. Most multibusiness firms are organized to exploit resource and capability linkages in two areas: first, through the centralization of common services at the corporate level and, second, through managing direct linkages among the businesses.

Common Corporate Services

The simplest form of resource sharing in the multidivisional company is the centralized provision of corporate functions and common services. These include corporate management functions such as strategic planning, financial control, treasury, risk management, internal audit, taxation, government relations, and shareholder relations. They also include business services that are more efficiently provided on a centralized basis, such as research, engineering, human resources management, legal services, management development, purchasing, and any other administrative services subject to economies of scale or learning.⁴

In practice, the benefits of the centralized provision of common services and functions may be disappointingly small. Cost savings from eliminating duplications may be offset, first, by the propensity for corporate staffs to grow under their own momentum and, second, by the weak incentives for corporate staffs to meet the needs of the businesses. Part of the problem is that the corporate headquarters serves two distinct purposes: providing the businesses with leadership and control and providing them with support services. Hence, a growing trend has been for companies to separate their corporate headquarters into a *corporate management unit*—responsible for supporting top management in strategic planning, finance, and communication—and a *shared services organization*—responsible for supplying common services such as research, recruitment, training, and information technology to the businesses.

By 2017, the majority of large multibusiness corporations in North America and Europe had established shared service organizations. Most of these comprised three or more functions the most common of which were information technology, human resource management, real estate and facilities management, and legal services. Increasingly, shared service organizations offer services that span national borders. The location of these global shared service centers is influenced by the cost and skills of local human resources.⁵

Procter & Gamble's Global Business Services organization employs 7,000 people in six "global hubs": Cincinnati (US), San Jose (Puerto Rico), Newcastle (UK), Brussels (Belgium), Singapore, and Manila (Philippines). Through scale economies and standardizing systems, it has reduced the cost of business services by over \$800 million. In addition to traditional support services, Global Business Services improves decision making in P&G's businesses through innovations such as virtualization (e.g., replacing physical product mock-ups with virtual reality applications), internal collaboration and decision support tools, and real-time digital capabilities.⁶

STRATEGY CAPSULE 13.2

Portfolio Planning Matrices

Portfolio planning techniques were developed by Boston Consulting Group, McKinsey & Company, and Arthur D. Little when addressing the challenges faced by General Electric at the end of the 1960s in managing its 46 divisions and 190 businesses.

The basic idea of a portfolio planning matrix is to position graphically the different businesses of a multi-business company in relation to the key strategic variables that determine their profit potential.

The GE/McKinsey Matrix uses the two primary drivers of profitability that we identified in Chapter 1 (see Figure 1.5): market attractiveness and competitive advantage. The GE/McKinsey matrix measures industry attractiveness by combining market size, market growth rate, return on sales, potential for margin growth, and international potential. A business unit's competitive advantage combines market share, return on sales relative to competitors, and relative position in terms of quality, technology, manufacturing, distribution, marketing, and cost.¹ Figure 13.2 shows the basic strategy implications concerning the allocation of capital to each business.

The Boston Consulting Group Growth-Share Matrix is a simplified version of the GE/McKinsey matrix. It uses rate of market growth as proxy for industry attractiveness and relative market share (the business unit's market share relative to that of its largest competitor) as an indicator of competitive advantage. The four quadrants

of the BCG matrix predict patterns of profits and cash flow and indicate strategies to be adopted (Figure 13.3).²

The Ashridge Portfolio Display is based upon the concept of parenting advantage.³ It recognizes that the value-creating potential of a business not just dependent upon the characteristics of the business, but also on the characteristics of the parent. Hence, the focus is on the fit between a business and its parent company. The positioning of a business along the horizontal axis of Figure 13.4 depends upon the parent's potential to create profit for the business by, for example, applying its corporate-level management capabilities, sharing resources and capabilities with other businesses, or economizing on transaction costs. The vertical axis measures the parent's potential for value destruction by the costs of corporate overhead or a mismatch between the management needs of the business and the management systems and style of the parent.

These different portfolio planning matrices each have their advantages and disadvantages as well as generic limitations:

- ◆ The McKinsey and BCG matrices are both intended to indicate the future profit potential for the business, yet they utilize data drawn from the past.
- ◆ The McKinsey and BCG matrices ignore linkages between businesses, yet such synergies between businesses tend to be major sources of multibusiness companies' value creation.

FIGURE 13.2 The GE/McKinsey portfolio planning matrix

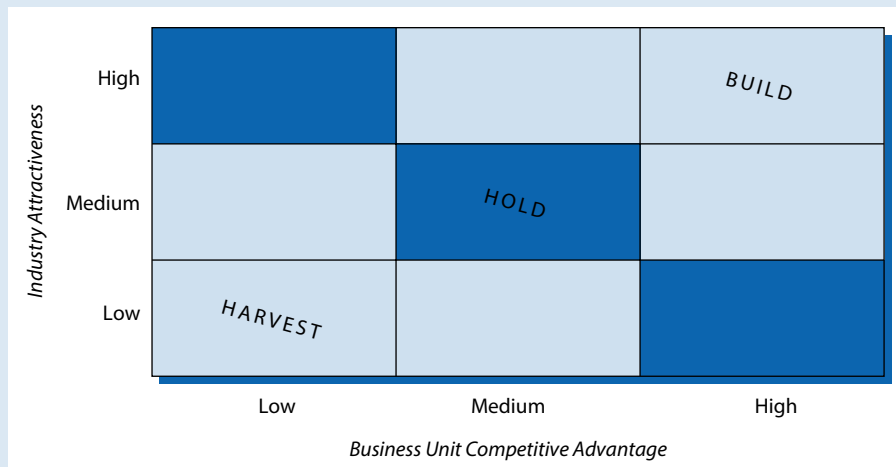
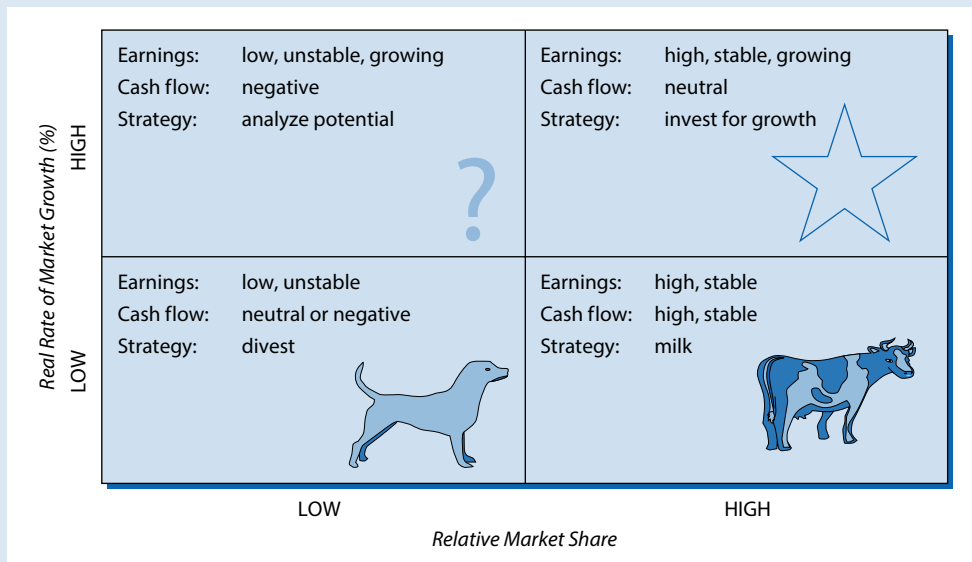
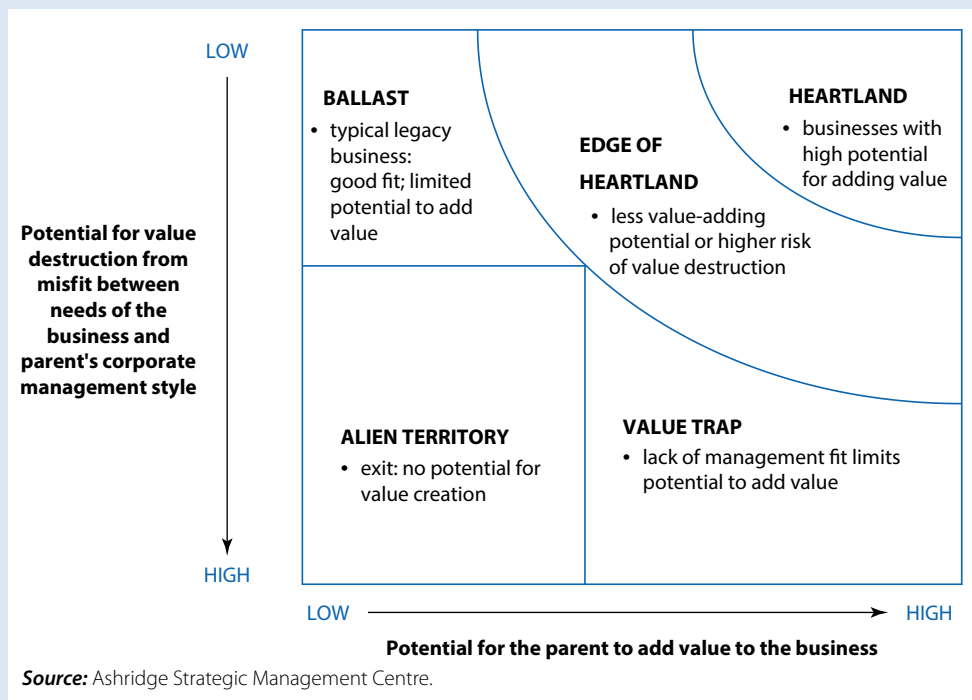


FIGURE 13.3 The BCG growth–share matrix**FIGURE 13.4** Ashridge portfolio display: The potential for parenting advantage

- ◆ All the matrices encounter problems of market definition—for example, in the BCG matrix, is BMW's auto business a “dog” because it holds less than 2% of the world auto market or a “cash cow” because it is the market leader in the luxury car segment?
- ◆ The Ashridge matrix recognizes the role of strategic fit and synergy, but encounters problems of complexity and subjectivity—neither of the dimensions lend themselves to quantification.

Transferring and Sharing Resources and Capabilities among Businesses

Exploiting economies of scope doesn't necessarily mean centralizing resources and capabilities at the corporate level. In most multibusiness companies, the major source of synergy is from sharing resources and transferring capabilities between businesses. To identify the potential for sharing resources and capabilities, Michael Porter advocates comparing the value chains for different businesses to see where there are similarities both between individual activities or in the overall configuration of the different value chains.⁷ Such similarities can be exploited in two ways:

- *Transferring resources and capabilities:* In the previous chapter we observed that organizational capabilities can be transferred between businesses: LVMH transfers its design and brand management capabilities among its luxury businesses, General Electric transfers its turbine expertise between jet engines and electrical generators. Similarly with intangible resources: Virgin transfers the use of its brand name among its many businesses; W.L. Gore transfers its proprietary technology relating to expanded PTFE polymer across its business units. Michael Porter notes that sharing skills and know-how is "an active process ... that does not happen by accident or by osmosis ... support of high-level management is essential."⁸ The main impediments to the transfer of best-practices within companies appear to lie in deficiencies in the relationships across intra-organizational boundaries.⁹
- *Sharing activities:* When different business units have activities that use similar tangible and human resources, there may be major economies from combining them. Samsung Electronics has global design centers in Seoul, Tokyo, Beijing, Delhi, London, San Francisco, and Sao Paulo which serve all Samsung's business units.¹⁰ Ford Motor Company's transition from a geographical to a more functional organizational structure (see Chapter 11, Strategy Capsule 11.3) reflects its desire for cost savings through consolidating design, purchasing and manufacturing.

Implications for the Corporate Headquarters

The more closely related are a company's businesses, the greater are potential gains from managing the linkages among those businesses and the greater the need for an active role by the corporate center. Thus, in vertically integrated petroleum companies (such as Royal Dutch Shell or Eni) or companies with close market or technological links (such as IBM, Procter & Gamble, and Sony), corporate staffs tend to be much larger than at companies with few linkages among their businesses. Berkshire Hathaway, which has almost no linkages among its businesses, has a corporate staff of about 25. Prior to its 2015 split, Hewlett-Packard, with about the same sales but much closer linkages between its divisions, had over 2000 employees at its Palo Alto head office. When business units share common resources or capabilities, the corporate headquarters is likely to be closely involved in developing and deploying those resources and capabilities. For example, both Pfizer and Corning each have strong corporate R&D departments, while Virgin Group's corporate team is heavily involved in managing the Virgin brand.

Developing and sharing organizational capabilities implies an important role for knowledge management. In industries such as beer, cement, food processing, and telecommunication services, internationalization offers few economies of scope in

shared resources, but does offer important opportunities for transferring innovation and know-how among national subsidiaries.

Exploiting linkages between businesses imposes costs which can easily outweigh the benefits generated. Even straightforward collaborations, such as cross-selling between different businesses, have yielded disappointing results, especially in financial services.¹¹ A comparison between conglomerate companies and vertically-integrated paper companies found that the heavier coordination requirements of the paper companies resulted in greater involvement of head office staff in divisional operations, larger head office staffs, more complex planning and control devices, and a lower responsiveness to change in the external environment. By contrast, conglomerate companies made little attempt to exploit operating synergies, even if they were present.¹²

Managing Individual Businesses

In the portfolio management approach to corporate strategy, the corporate headquarters' primary role is as an *investor*: making acquisitions and divestments and allocating investment funds among the different businesses. In managing linkages among the businesses the essential role of the corporate headquarters is as a *coordinator and orchestrator of synergies* between businesses. However, the corporate headquarters may be involved more directly in adding value to its individual businesses by *improving their management*. Andrew Campbell and his associates refer to this direct influence of corporate headquarters on the individual businesses as "vertical value-added" achieved through "stand-alone influence" (i.e., it is not dependent upon exploiting synergies among the businesses). There are many types of intervention through which corporate management can improve the performance of the businesses they own: replacing business-level managers, controlling budgets, guiding strategy, setting performance targets, facilitating external relationships (e.g., with governments and investors), providing advice and guidance, and managing the corporate culture.¹³

We focus upon just three of these mechanisms: direct corporate involvement in business level management, strategic planning, and performance management and financial control.

Direct Corporate Involvement in Business-level Management

There is overwhelming evidence that performance differences between companies are vast and are caused primarily by differences in the quality of management.¹⁴ Hence, there is scope to create value by improving the management practices of poorly managed companies. A *restructuring strategy* is one in which a parent company intervenes to install new managers, change strategy, sell off surplus assets, and possibly make further acquisitions in order to achieve scale and market presence. For the strategy to create value requires that management is able to spot companies that are undervalued or offer turnaround potential to then make strategic and operational interventions to boost their performance. A further requirement, observes Michael Porter, is the willingness to recognize when the work has been done and then dispose of the restructured business.¹⁵

Restructuring was once associated with the strategies of conglomerate companies, most of which have disappeared from the corporate sectors of North America and Europe. Their role as restructurers has passed to private equity groups. Firms such as Carlyle Group, Kohlberg Kravis Roberts, Blackstone, and Apollo Global Management

in the United States and CVC Capital Partners and BC Partners in the United Kingdom create investment funds organized as limited partnerships that acquire full or partial ownership of private and public companies. Value is created through financial restructuring (primarily increasing leverage), management changes, and making strategic and operational changes. Private equity firms have also been involved in acquiring very large public companies. 3G Capital's acquisitions of Heinz and Kraft points to the potential for restructuring interventions to radically boost profit margins (see Strategy Capsule 13.3). On average, private equity funds have generated returns that exceed those of the stock market, although the gap has narrowed.¹⁶ Whether private equity firms create value on a more broadly defined basis is less clear; it is likely that the gains to investors have been financed by employees, taxpayers, and communities.

Restructuring may also involve not just individual companies, but entire industries. The merging of Heinz and Kraft by 3G Capital and its subsequent attempt to acquire Unilever, suggests intent to consolidate the entire processed foods sector. 3G's role in consolidating the global beer industry around Anheuser-Busch InBev—with its 21% share of the world beer market—offers a precedent.

For most multibusiness companies, involvement by corporate-level management in the strategic and operational decisions at the business level is less intrusive than that implied by a restructuring approach. Multibusiness companies with superior financial performance over the long term tend to have close communication and collaboration between the business and corporate management. For example:

- Exxon Mobil Corporation has been the most profitable of the world's petroleum majors for the past 50 years. At the core of ExxonMobil's renowned financial

STRATEGY CAPSULE 13.3

3G Capital's Restructuring of Heinz-Kraft

3G Capital is a Brazil-based private equity firm founded in 2004. In 2013, it partnered with Berkshire Hathaway to acquire the US food processing company. Heinz, then two years later merged Heinz into Kraft Foods. Between 2013 and 2017, Heinz-Kraft has undergone massive organizational and operational changes.

3G's initial interventions were replacements of management. At Heinz, 3G fired 11 of the top 12 executives in a single day; at Kraft, 10 top executives were quickly dismissed. Cost cutting measures at Kraft ranged from the symbolic—eliminating office refrigerators, selling corporate jets, requiring all employees to fly coach—to the substantial—closing seven plants in North America, eliminating some 2,600 jobs, and selling the Chicago corporate campus. Plant closures and layoffs induced favors from governments and unions: cities and states offering Heinz-Kraft incentives to keep plants

open and unions offering concessions on pay and conditions. 3G's management processes include "zero-based budgeting," every expense item must be justified in each accounting period; measurable, transparent annual goals for each employee; and rapid advancement for high-performing young talent.

The impact on profitability has been remarkable: in 2017, Heinz-Kraft's operating margin was 30%—double what it was in 2012—and far ahead of rivals General Mills, Campbell Soup, Kellogg, Unilever, and Nestle.

3G's attempt to acquire Unilever in 2017 has made Heinz-Kraft's rivals increasingly wary of their vulnerability—most boosting their cost cutting efforts to support their share prices.

Sources: "The Lean and Mean Approach of 3G Capital," *Financial Times*, May 7, 2017; "Kraft's Heinz Recipe – Buy, Squeeze, Repeat," *Fortune* (February 1, 2017).

discipline, strategic acuity, and operational effectiveness is a management system that combines rigorous implementation of company-wide financial and operational procedures, a close relationship between the president of each of the 10 global businesses and a member of the five-person management committee, and a powerful corporate culture that has been described as “relentless,” “ruthless,” “Texan,” and “cult-like.”¹⁷

- Danaher Corporation adds value to its 27 companies in life sciences, dental care, and environmental systems through applying its Danaher Business System which “guides what we do, measures how well we execute, and creates options for doing even better” and “drives every aspect of our culture and performance.”¹⁸ The system comprises Toyota’s principles of lean production and continuous improvement, the extensive use of closely-monitored performance metrics, and a company-wide commitment to using innovation to solve customers problems.¹⁹
- Kering, the Paris-based luxury and lifestyle group that includes Gucci, Bottega Veneta, Yves St. Laurent, Puma, and other fashion brands, has a corporate center that nurtures creativity, diffuses corporate values such as environmental sustainability, women’s empowerment, and developing diverse talent, while closely monitoring performance and replacing subsidiary CEOs and creative directors when it deems necessary.²⁰

The downside of direct corporate involvement in business-level decisions is its potential to undermine the autonomy and motivation of the general managers of those businesses. Authoritarian, highly-interventionist CEOs can be very successful (as in the case of Steve Jobs at Apple) or very unsuccessful (as in the case of Carly Fiorina at Hewlett-Packard). Universally true, however, is that centralization of initiative and decision-making authority adversely affects the responsiveness and adaptability of the organization as a whole. A key challenge of managing the multibusiness firm is to design a management system that allows business-level managers to benefit from the expertise and perspective of corporate managers while sustaining their initiative and motivation and exploiting their superior knowledge of their own businesses. Two management systems can assist in this task: strategic planning systems and performance management systems.

The Strategic Planning System

In most multibusiness companies, the corporate center establishes overall corporate goals and priorities, then within this framework, the business units develop their business strategies. It is then the role of corporate managers to appraise, amend, approve, and then integrate these business-level strategies. The challenge is to design a strategy-making process that reconciles the decentralized decision making that is essential to fostering flexibility, responsiveness, and a sense of ownership at the business level with corporate management’s ability to apply its knowledge, perspective, and responsibility for the interests of shareholders and other stakeholders. Common to the success of ExxonMobil, Siemens, and Unilever is a strategic planning system that supports a high level of decision-making autonomy at the business level, motivates business leaders toward high performance, shares knowledge between corporate and business levels, and reconciles business initiative with overall corporate control. The typical strategic planning cycle is outlined in Chapter 6 (“The Strategic Planning System: Linking Strategy to Action”).

Criticisms of Strategic Planning Since the early 1980s, the strategic planning systems of large firms have been bombarded by criticism. We observed in Chapter 1 that Henry Mintzberg claimed top-down, formalized strategic planning to be ineffective since it separated strategy formulation from strategy implementation and failed to take account of uncertainty or the need for flexibility and creativity. These deficiencies may explain the observation that, for many large companies, strategy is formulated outside the strategic planning system. Marakon consultants Mankins and Steele observe that the rigidities of formal planning cycles mean that “senior executives ... make the decisions that really shape their companies’ strategies ... outside the planning process typically in an ad hoc fashion without rigorous analysis or productive debate.”²¹ Mintzberg’s criticism of the divorce of strategy formulation from strategy implementation is reinforced by surveys that show that deficiencies in strategy execution processes are the biggest challenge that senior executives face.²²

Improving Strategic Planning Systems Proposals to increase the effectiveness of the strategic planning processes of large, multibusiness companies have focused on three types of initiative.

Emphasize critical strategic issues. Richard Rumelt observes that:

“A strategy is a way through a difficulty, an approach to overcoming an obstacle, a response to a challenge. If the challenge is not defined, it is difficult or impossible to assess the quality of the strategy... if you fail to identify and analyze the obstacles, you don’t have a strategy. Instead, you have a stretch goal or a budget or a list of things you wish would happen.”²³

McKinsey consultants point to the need to begin the strategy process by “deliberately, thoughtfully identifying the strategy issues that will have the biggest impact on future business performance.”²⁴ A key problem, according to a study by Bain & Company, is that strategic issues are obscured by an emphasis placed on financial targets. Companies that separated strategy development from budgetary planning reported bolder, more inspiring ambitions and clearer choices over where to play and how to win.²⁵

Adapt strategic planning to meet a company’s specific needs. Different companies face different strategic decisions and decision contexts which require different strategic planning processes. Companies in slow moving, mature industries such as processed foods, earth-moving equipment, and airlines can utilize traditional strategic planning systems that emphasize incremental change and utilize performance targets. Companies in e-commerce and information technology need strategic planning systems that foster alertness to technologies and business models that may disrupt their businesses. Companies’ strategic planning cycles should match the needs of their businesses. According to McKinsey & Company, business units whose performance is satisfactory and face a stable business environment do not need to undertake a full-blown strategy review each year. Conversely, businesses in fast moving sectors need to review their strategies continuously.²⁶

Systematize strategy execution. Effectiveness in executing strategy must go beyond budget setting. To link strategic planning more closely to operational management, Larry Bossidy and Ram Charan recommend using *milestones*—specific actions or intermediate performance goals to be achieved at specified dates. These can “bring reality to a strategic plan.”²⁷ As we noted in Chapter 2, the *balanced scorecard* offers a means of cascading high-level strategic plans into specific functional and operational targets for different organizational units. Building this approach, Kaplan and Norton propose the use of *strategy maps* to plot the linkages between strategic actions and overall goals.²⁸ To be effective, performance targets must be embedded into human

resource management so that appraisal metrics and compensation incentives reflect strategic goals. Connecting strategic planning to its implementation may require a broader role for strategic planning units. Kaplan and Norton recommend upgrading strategic planning units into *offices of strategy management* that, not only manage the annual strategic planning cycle, but also oversee the execution of strategic plans.²⁹

Performance Management and Financial Control

Most multibusiness companies have a dual planning process: strategic planning is concerned with the medium and long term; financial planning and control typically concentrate upon a two-year horizon. The first year of the strategic plan normally includes the performance plan for the upcoming year comprising an operating budget and strategy targets that relate to market share, output growth, new product introductions, and employment levels which are often expressed as specific strategic milestones. Annual performance plans are agreed between senior business-level managers and corporate-level managers. Targets are monitored on a monthly and quarterly basis to provide early detection of deviations from targeted performance. At the end of each financial year, they are probed and evaluated in performance review meetings held between business and corporate management. Capital expenditure budgets tend to be longer term—usually extending over the entire three to five year strategic planning period.

Companies whose management systems are heavily orientated towards demanding financial and operating targets typically use powerful individual incentives to create an intensely motivating environment for divisional managers. Creating a performance-driven culture requires unremitting focus on a few quantitative performance targets that can be monitored on a short-term basis. PepsiCo CEO Indra Nooyi observed: “We are a very objective-driven company. We spend a lot of time up front setting objectives and our guys rise to the challenge of meeting those objectives. When they don’t meet the objectives, we don’t have to flog them because they do it themselves.”³⁰

In industries in which investment horizons and the lag between strategic decisions and their outcomes are longer, the challenges of reconciling short- and medium-term targets with longer-term company performance is more difficult. The performance management system of BP, the UK-based petroleum company, was identified as a contributory factor in the tragic accidents at its Texas City refinery and Deepwater Horizon drilling platform (see Strategy Capsule 13.4).

Strategic Planning and Performance Control: Alternative Approaches to Corporate Management

Although many companies implement their strategic plans through setting performance targets, ultimately, strategic plans and performance targets represent alternative mechanisms of corporate control. Strategic planning involves exerting corporate control over the strategic decisions made by the businesses. Performance management, on the other hand, involves establishing performance targets for the businesses, then allowing the managers of the business the freedom to make the decisions needed to attain the required performance.

The distinction between these two approaches is between *input* and *output* control. A company can control the inputs into strategy (the decisions) or the output from strategy (the performance). Although most companies use a combination of input and output controls, there is a tradeoff between the two: more of one implies less of the other. If the corporate HQ micromanages divisional decisions, it must accept

STRATEGY CAPSULE 13.4

Performance Management at BP

Under the leadership of John Browne (CEO 1995–2007), BP became the most decentralized, entrepreneurial, and performance focused of the petroleum majors. Brown's management philosophy emphasized three principles:

- ◆ BP operates in a decentralized manner, with individual business unit leaders (such as refinery managers) given broad latitude for running the business and direct responsibility for delivering performance.
- ◆ The corporate organization provides support and assistance to the business units through a variety of functions, networks, and peer groups.
- ◆ BP relies upon individual performance contracts to motivate people.

The CEO was responsible for presenting the five-year and annual corporate plans to the board for approval.

The goals, metrics, and milestones in corporate plans were cascaded down in the plans for each segment, function, and region. These same goals and metrics were reflected in individual performance contracts. A performance contract outlined the key results and milestones an employee was expected to achieve that year. Progress against targets and milestones in an employee's performance contract were a key determinant of annual bonuses. Performance contracts were the key mechanism for delegating annual plans into commitments by individual leaders. The performance contracts set goals for financial, operational, strategic, and HSSE (health, safety, security, and environmental) performance that were high, but not so high that they couldn't be achieved.

Source: Adapted from *The Report of the BP US Refineries Independent Safety Review Panel*, January 2007, with permission from BP International.

the performance outcomes that will result from this. Conversely, if the corporate HQ imposes rigorous performance targets, it must give divisional managers the decision-making freedom for their attainment.

This implies that, in designing their corporate control systems, companies must emphasize either strategic planning or financial control. This distinction was observed by Goold and Campbell in their study of the corporate management systems of British multibusiness companies.³¹ *Strategic planning companies* emphasized the longer-term development of their businesses and had corporate HQs that were heavily involved in business-level planning. *Financial control companies* had corporate HQs that emphasized short-term budgetary control and rigorously monitored financial performance against ambitious targets, but had limited involvement in business strategy formulation—this was left to divisional and business unit managers. Table 13.1 summarizes the key features of the two styles.

Over time, the trend has been for companies to make increasing use of financial control in managing their businesses. This has occurred even in capital-intensive sectors with long time horizons, such as petroleum, where strategic planning has become increasingly oriented toward short- and medium-term financial targets.³² However, since the financial crisis of 2008–2009, increasing criticism has been levied against short-term shareholder value maximization. Whether this will lead to an increasing emphasis on longer-term strategic planning remains to be seen.

TABLE 13.1 Characteristics of different corporate management styles

	Strategic planning	Financial control
<i>Business strategy formulation</i>	Businesses and corporate HQ jointly formulate strategy The HQ coordinates strategies of businesses	Strategy formulated at business unit level Corporate HQ largely reactive, offering little coordination
<i>Controlling performance</i>	Primarily strategic goals with medium- to long-term horizons	Financial budgets set annual targets for ROI and other financial variables with monthly and quarterly monitoring
<i>Advantages</i>	Effective for exploiting (a) linkages among businesses, (b) innovation, (c) long-term competitive positioning	Business unit autonomy supports initiative, responsiveness, efficiency, and development of business leaders
<i>Disadvantages</i>	Loss of divisional autonomy and initiative Conducive to unitary strategic view Tendency to persist with failing strategies	Short-term focus discourages innovation and long-term development Limited sharing of resources and capabilities among businesses
<i>Style suited to</i>	Companies with few closely related businesses Works best in highly competitive, technology-intensive sectors where investment projects are large and long term	Highly diversified companies with low relatedness among businesses Works best in mature, low-tech sectors where investment projects are relatively small and short term

Source: Based on M. Goold and A. Campbell, *Strategies and Styles* (Oxford: Blackwell Publishing, 1987) with permission of John Wiley & Sons, Ltd.

Managing Change in the Multibusiness Corporation

The shifting priorities of corporate managers have had important implications for the strategic management of multibusiness companies. During the last two decades of the 20th century, the priority shifted from growth to the creation of shareholder value. This resulted in the restructuring of diversified corporate empires through outsourcing and refocusing. During the present century, especially since the financial crisis of 2008–2009, the greatest challenge has been enhancing responsiveness to external change and accelerating the pace of organizational evolution.

Disillusion with the shareholder value maximization model, diminishing returns to cost cutting, and the need to create new sources of value have resulted in profound shifts in the corporate strategies of multibusiness companies. Increasingly, large multibusiness companies have sought to identify opportunities for innovation, for new product development, and for exploiting linkages—both internally between their businesses and externally with other companies. Corporate headquarters are concerned less with the problem of control and more with the challenges of creating value within and between their individual businesses. The *parenting* concept reflects this growing emphasis on business development and the quest for new sources of value. One of the greatest challenges for the corporate management is to facilitate adaptation to change

STRATEGY CAPSULE 13.5

Reformulating Strategic Planning at IBM

IBM is an evolutionary wonder. It has successfully transitioned from tabulating machines to mainframe computers, to personal computers, to networked information technology, to cloud computing. During the past two decades, it has also changed from a hardware to a software and services company. Under its past three CEOs, IBM's pace of evolution accelerated, assisted by IBM's processes for making and implementing strategy.

Under transformational CEO's Lou Gerstner and Sam Palmisano, IBM recreated its strategic planning system around processes for identifying and responding to emerging opportunities and threats. This IBM Strategic Leadership Model includes systems for sensing new opportunities:

- ◆ The technology team meets monthly to assess emerging technologies and their market potential.
- ◆ The strategy team comprising a cross section of general managers, strategy executives, and functional managers meets monthly to review business unit strategies and recommend new initiatives.
- ◆ The integration and values team comprises 300 key leaders selected by top management. The team is responsible for companywide initiatives called "winning plays" that cut across IBM's divisional boundaries.
- ◆ "Deep dives" are conducted by ad hoc teams to explore specific opportunities or issues and may result in recommendations to enter a new area of

business or to exit from a particular technology or product market.

The initiatives arising from these processes are then acted on by the three main executing vehicles:

- ◆ *Emerging business opportunities (EBOs)* are business development processes that protect new business initiatives from the financial rigor applied to more conventional projects. EBOs were established to develop Linux applications, autonomic computing, blade servers, digital media, network processing, and life sciences.
- ◆ *Strategic leadership forums* are three- to five-day workshops facilitated by IBM's Global Executive and Organizational Capability Group. Their purpose is to transform strategic initiatives into action plans and to address pressing strategic issues, such as poor performance, in specific business areas. They are initiated by a senior manager and overseen by the strategy team.
- ◆ *The Corporate Investment Fund* finances new initiatives identified by the integration and values team or by EBOs.

Source: J. B. Harreld, C. A. O'Reilly, and M. L. Tushman, "Dynamic Capabilities at IBM: Driving Strategy into Action," *California Management Review* 49 (Summer 2007): 21–43.

by large, multibusiness companies. (Strategy Capsules 13.5 and 13.6 illustrate how the corporate centers of IBM and Samsung Electronics have built adaptive capability. These companies, together with other exemplars of responsiveness to changing business conditions—such as Microsoft, Siemens, Philips, Haier, and Johnson & Johnson—point to three ways of facilitating corporate adaptation:

- *Counteracting inertia:* As we noted in Chapter 8 ("The Challenge of Organizational Adaptation and Strategic Change"), organizations resist change. Multibusiness corporations, because of their greater complexity, are especially subject to

STRATEGY CAPSULE 13.6

Samsung Electronics: Top-down Initiatives that Drive Corporate Development

Samsung is the biggest of South Korea's *chaebols*—groups of companies linked by cross-shareholdings and controlled by a founding family. The Samsung group comprises 83 companies. The biggest company is Samsung Electronics, the world's largest electronics company in terms of sales. The head of the Samsung group, and chairman of Samsung Electronics, is Lee Kun-hee, son of the founder Lee Byung-chull and father of Jay Y. Lee, president of Samsung Electronics.

The rise of Samsung Electronics is the result of a series of corporate initiatives that were ambitious, focused, long-term, and driven by intense top-down commitment—and capital investment. In 1982, Samsung Electronics resolved to become world leader in memory devices—it achieved this in DRAM chips in 1992. In 2004, its semiconductor investments began focusing on flash memories, where it also established global leadership. Between 2000 and 2009, it established itself as the world's biggest producer of batteries for mobile digital devices, similarly with flat-panel televisions.

These successes involved massive commitments of resources to technology (Samsung receives more US patents than any other company except IBM), manufacturing (for semiconductor production Samsung built the world's biggest fabrication complex), design (design centers in five cities of the world), and the Samsung brand. Its resource deployments have been supported by a culture and working practices that support high levels of coordination and commitment. Samsung's culture is nourished by tales of outstanding endeavor, including constructing a four-kilometer paved road in a single day

to ensure that Samsung's first integrated circuit plant could open on time.

Central to Samsung's success is a new product development process supported by a knowledge management process that allows development teams to exploit the expertise of the entire company. In April 2009, the Visual Display Division of Samsung Electronics' Digital Media Business had just completed work on a high-resolution LED TV when it was required to roll out a high-definition, 3-D television within a year. Within a week, the two task forces assigned to the project scoured Samsung Electronics' Test and Error Management System (TEMS) of information on every product development project undertaken at the company to identify know-how within Samsung that might assist the new project.

Samsung Electronics' top-down drive continues. In 2010–2011, CEO Lee Kun-hee announced 10-year plans to build major new businesses in solar panels, LED lighting, electric vehicle batteries, biotechnology, and medical devices. During 2014 to 2018, the strategic priorities were to transition Samsung from hardware to software and services and build strength in automotive systems, digital health, and industrial automation. By acquiring Harman International in December 2017, Samsung indicated its willingness to use acquisitions to build new areas of business.

Sources: "Samsung: The Next Big Bet," *Economist* (October 1, 2011); *Samsung Electronics*, HBS Case 9–705–508 (revised 2009); "Samsung Electronics' Knowledge Management System," *Korea Times* (October 6, 2010).

organizational inertia. One aspect of this is the difficulty that companies experience in reallocating resources among their existing businesses in response to external change and internal performance differences. Not only do multibusiness companies tend to maintain the same allocation of capital expenditures to their individual businesses from year to year, but there is also a bias toward equalizing capital expenditures to each business.³³ This is despite the fact that

those companies that did achieve higher levels of capital reallocation outperformed those which did not.³⁴

- *Adaptive tension:* At General Electric, Jack Welch, CEO from 1981 until 2001, created a corporate management system that decentralized decision making to business-level managers but created a level of internal stress that counteracted complacency and fostered responsiveness to external change and a constant striving for performance improvement. The role of the CEO as a catalyst for change and driver of outstanding performance is also evident in the leadership styles of Steve Jobs at Apple and Jeff Bezos at Amazon.
- *Institutionalizing strategic change:* As we have already noted, companies' strategic planning systems are seldom sources of major strategic initiatives: the impetus for major strategy redirection usually comes from outside formal strategy processes. The IBM case example shows that strategic planning systems can be redesigned as systems for sensing external changes and responding to the opportunities these changes offer—in other words, building *dynamic capability* at the corporate level.
- *New business development:* The compression of industry lifecycles means that multibusiness companies are under increasing pressure to revamp their business portfolios. The barriers to releasing mature and declining businesses lie principally in management psychological and organizational politics: once a company has decided to exit a sector, the divestment is typically applauded by the stock market (e.g., GE's sale of its domestic appliance business or HP's decision to spin off its PC and printer business). Developing new businesses represents a bigger challenge. A few companies are able to build whole new businesses on internally developed new products (e.g., 3M), new technology (e.g., Google, Amazon), or new entrepreneurial initiatives (e.g., the Virgin Group). Some companies have established *corporate incubators* for nurturing new startups: Royal Dutch Shell's GameChanger and Google's Area 120 are examples.³⁵
- *Top-down, large-scale development initiatives:* Throughout this book, we have pointed to the key role of strategic intent—top-down strategic goals—in unifying and motivating organizational members. In some companies, linking such strategic intent to specific projects and programs has been an especially powerful vehicle for corporate development. The rise of Samsung Electronics to become the world's largest electronics company has been on the basis of a small number of hugely ambitious development projects that have involved massive commitments of finance, human ingenuity, and effort.

Adaptation to changing circumstances also requires timing. Intel's former CEO, Andy Grove, emphasizes the importance of CEOs identifying *strategic inflection points*—instances where seismic shifts in a firm's competitive environment require a fundamental redirection of strategy. For Intel, key inflection points included: transition from DRAM chips to microprocessors as its core business, its choice of its x86 microprocessor architecture, and its 1994 decision to replace its faulty Pentium chips at a cost of \$475m.³⁶

Finally, managing change in large organizations also requires providing people with the security and certainty to allow them to leap into the unknown. Some of the companies that have been most effective in adapting to change—IBM, Philips, 3, and HSBC—have done so while emphasizing the continuity of their heritage and identity. Creating a sense of identity is more challenging for a company that spans several businesses than for one whose identity is determined by the products it offers

(e.g., McDonald's or De Beers). It goes beyond “strategic relatedness” and “dominant logic” and embraces vision, mission, values, and principles. For example, the French-based multinational Danone has undergone multiple transformations before emerging as a dairy products and baby foods company, yet has provided continuity through its commitment to a set of enduring business principles that have emphasized employee welfare and corporate social responsibility.³⁷

Governance of Multibusiness Corporations

So far, our discussion of the multibusiness corporation has focused on the means by which the corporate headquarters can create value. What we have not discussed is: value for whom? This takes us to the issue of *corporate governance*—the system by which companies are directed and controlled—or more formally:

Procedures and processes according to which an organization is directed and controlled. The corporate governance structure specifies the distribution of rights and responsibilities among the different participants in the organization—such as the board, managers, shareholders and other stakeholders—and lays down the rules and procedures for decision-making.³⁸

The reason corporate governance is an important issue is because of the separation of ownership from control in large companies, which gives rise to the *agency problem*: the propensity for managers (the agents) to operate companies in their own interests rather than in the interests of the owners (see the discussion of “The Cooperation Problem” in Chapter 6). Although corporate governance is an issue for all companies whose owners are not directly engaged in managing the company, it is especially acute in large public corporations, almost all of which comprise multiple businesses. Indeed, in the multibusiness company the problem of agency is compounded by the separation not only of the shareholders from corporate management but also of corporate management from business-level management.

Let us examine three key issues of corporate governance in relation to large, multibusiness firms: the rights of shareholders, the responsibilities of boards of directors, and the role of corporate management.

The Rights of Shareholders

The tendency for companies to be operating in the interests of their senior managers—whose personal goals tend to be the aggrandizement of their wealth, power, influence, and status—rather than in the interests of their owners is primarily a problem for public companies where, typically, ownership is dispersed among thousands of shareholders. Hence, in most countries company law seeks to protect shareholders' interests through establishing their rights to elect and remove members of the board of directors, to share in the profits of the company, to receive company information (including audited financial statements), and to sell their shares.

However, even with these protections, shareholders' incentives to exercise their governance rights are weak: if each shareholder owns only a small fraction of a company and these shares only account for a small fraction of the shareholder's total wealth then the costs of active engagement are high relative to the likely returns. Disgruntled shareholders typically sell their shares rather than oppose the incumbent management team.

The short-term orientation of most shareholders further discourages activism: over the past 40 years the average holding period for US equities has fallen from seven years to seven months.³⁹ At the time of Kraft's highly contentious takeover of British chocolate maker Cadbury, about 30% of Cadbury's shares were owned by hedge funds.⁴⁰

Mechanisms to limit shareholder power include issuing shares with differential voting rights. This allows the founders of companies and their families to exercise effective control despite owning a minority of shares. At News International, Rupert Murdoch and family owned 12% of the company but controlled 40% of the votes. After Facebook's IPO, Mark Zuckerberg owned 18% of the company but controlled 57% of the votes. Shares with differential voting rights are primarily a defense against hostile takeover. Managers as well as founders tend to oppose takeovers, since they are likely to lose their jobs. Hence the use of "poison pill" defenses that penalize hostile takeovers.

The Responsibilities of Boards of Directors

The board of directors, according to *OECD Principles of Corporate Governance*, has the responsibility to "ensure the strategic guidance of the company, the effective monitoring of management by the board, and the board's accountability to the company and the shareholders."⁴¹ This requires that:

- board members act in good faith, with due diligence and care, in the best interest of the company and its shareholders;
- board members review and guide corporate strategy, major plans of action, risk policy, annual budgets, and business plans; set and monitor performance objectives; oversee major capital expenditures; select, monitor, and compensate key executives; ensure the integrity of the corporation's accounting and financial reporting systems; and oversee the process of disclosure and communication.

However, there are several impediments to the effectiveness of boards of directors in exercising oversight and strategic guidance:

- The dominance of the board by executive directors. Among many companies (including many US and UK corporations), the top management team are also board members, hence limiting the board's role in providing independent oversight of management. Such overlap also occurs when the roles of board chair and CEO are held by a single person—a feature of one-half of Fortune 500 corporations in the United States, though less common in Europe. The weight of evidence points to the advantages of splitting the roles; however, in general it is the competence of the individuals who do the job that is more important than the structural arrangements.⁴²
- Boards have become increasingly preoccupied with compliance issues with the result that their role in guiding corporate strategy has shrunk.

Dominic Barton, global managing director of McKinsey & Company, argues that, if boards are to become effective agents of long-term value creation, they must devote much more time to their roles, need to have relevant industry experience, and should have a small analytical staff to support their work.⁴³

The harshest criticisms of board oversight have been in relation to management compensation. From 1978 to 2013, the compensation of US CEOs, inflation-adjusted,

increased 937% compared to 10.2% for the average worker compensation over the same period.⁴⁴ The paradox is that the massive payouts to CEOs have been the result of compensation systems designed to align management goals with those of shareholders', especially through the grant of stock options and emphasis on performance-related bonuses. As Table 13.2 shows, the highest-paid CEOs were not always those who delivered exceptional returns to their shareholders. Poor alignment between executive compensation and shareholder value is often the result of linking bonuses to short-term performance, failing to correct for overall stock market movements, and incentives for creating shareholder value not being matched by penalties for its destruction.⁴⁵

Governance Implications of Multibusiness Structures

In the multibusiness corporation, decision-making responsibilities are divided between a corporate headquarters and the individual businesses—typically through a multidivisional structure. As we saw in Chapter 6 (Strategy Capsule 6.1), the multidivisional form was a key development in the emergence of the modern corporation. What are the implications of this structure for corporate governance?

For organizational economist Oliver Williamson, the widespread adoption of the multidivisional structure (or “M-form”) was a result of its advantages both in combining centralized direction and localized adaptation and in overcoming the problems of corporate governance that affect large public companies.⁴⁶ The multidivisional form facilitates corporate governance in two ways:

- *Allocation of resources:* Resource allocation within any administrative structure is a political process in which power, status, and influence can triumph over purely commercial considerations.⁴⁷ To the extent that the multidivisional company can create a competitive internal capital market in which capital is allocated according to past and projected divisional profitability and projects are subjected to a standardized appraisal process, it can avoid much of this politicization.

TABLE 13.2 The highest-paid CEOs of 2016

Rank	CEO	Company	Direct compensation 2016 (\$m)
1	Thomas Rutledge	Charter Communications	98
2	Leslie Moonves	CBS	69
3	Robert A. Iger	Walt Disney	41
4	David Zaslav	Discovery Communications	37
5	Robert Kotick	Activision Blizzard	33
6	Brian Roberts	Comcast Corp.	33
7	Jeffrey L. Bewkes	Time Warner	33
8	Virginia Rometty	IBM	32
9	Leonard Schleifer	Regeneron Pharmaceuticals	28
10	Stephen Wynn	Wynn Resorts Ltd.	28

Source: Equilar

- *Agency problems:* Given the limited power of shareholders to discipline and replace managers and the weakness of boards to control management, the corporate head office of a multidivisional firm can act as an interface between shareholders and the divisional managers and enforce adherence to profit goals. With divisions designated as profit centers, financial performance can readily be monitored by the head office and divisional managers can be held responsible for performance failures. Hence, multibusiness companies can be more effective profit maximizers than specialist companies.

STRATEGY CAPSULE 13.7

Governance in Holding Companies

A holding company owns a controlling interest in a number of subsidiary companies. The term *holding company* is used to refer both to the parent company and to the group as a whole. Holding companies are common in Japan (notably the traditional *zaibatsu* such as Mitsubishi and Mitsui), in Korea (*chaebols* such as LG, Hyundai, and SK) and the Hong Kong trading houses (Swire, Jardine Matheson, and Hutchison Whampoa). In the United States, holding companies own the majority of US banking assets.

Within holding companies, the parent exercises control over the subsidiary through appointing its board of directors. The individual subsidiaries typically retain high levels of strategic and operational autonomy. Unlike the multidivisional corporation, the holding company lacks financial integration: there is no centralized treasury, profits accrue to the individual operating companies, and there is no centralized budgeting function—each subsidiary is a separate financial entity. The parent company provides equity and debt capital and receives dividends from the subsidiary.

Although the potential for exploiting synergies between businesses is more limited in the holding company than in the divisionalized corporation, the holding company structure has important advantages for large family-owned companies. The attractiveness of holding companies is that they allow family dynasties to retain ownership and control of business empires that diversify family wealth across multiple sectors. At the same time,

their decentralization allows effective management of the group without the need for the parent company to develop a tremendous depth of management capability.

Thus, the Tata Group, India's biggest business concern with over \$60 billion in revenue and 424,000 employees, is controlled by the Tata family through Tata Sons Ltd, parent company of the group. Among the many hundreds of subsidiaries, several are leading companies within their industries, including Tata Steel, Tata Motors (owner of Jaguar and Land Rover), Tata Tea (owner of the Tetley brand), and Tata Consulting Services. Twenty-seven Tata companies are publicly listed.

In contrast to the public corporations where the key governance problem is the conflicting interests of owners and managers, the governance problems of holding companies relate to the conflicting interests of different shareholders: especially between the founding family and other shareholders. Through its investment company Exor, the Agnelli family controls a business empire that comprises Fiat Chrysler, Ferrari, CNH Industrial, and Juventus Football Club, despite minority ownership of these enterprises. Similarly with the Tata family: cross-shareholdings and shares with differential voting rights allow family control despite minority ownership.

Sources: M. Granovetter, "Business Groups and Social Organization," in N. J. Smelser and R. Swedberg, *Handbook of Economic Sociology* (Princeton: Princeton University Press, 2005): 429–450; F. Amatori and A. Colli, "Corporate Governance: The Italian Story," Bocconi University, Milan (December 2000).

There is not much support for Williamson's "theory of the M-form." At some multi-business companies—such as ExxonMobil, Danaher, Berkshire Hathaway—corporate management is highly effective at pursuing long-term shareholder value maximization. Other multibusiness companies—Enron, WorldCom, Royal Bank of Scotland, and Kaupthing Bank of Iceland—have become vehicles for CEO ambition resulting in the destruction of shareholder value on a massive scale.

Multidivisional companies may also lack the flexibility and responsiveness that their modular structures should, in principle, be capable of. Henry Mintzberg points to two key rigidities: first, highly centralized decision making within each division as a result of divisional presidents' personal accountability to the corporate head office; second, standardization of management systems and styles across the different businesses of the multidivisional corporation.⁴⁸ As already noted, the rigidities of multidivisional companies' allocation of their capital expenditures is indicative of a lack of performance orientation.⁴⁹

The governance issues that multibusiness companies face are highly dependent upon their structures and ownership patterns. As Strategy Capsule 13.7 shows, the other major type of multibusiness company—the holding company—gives rise to different governance issues from the multidivisional corporation.

Summary

While corporate strategies in the form of vertical integration, multinational expansion, and diversification have the potential to create value, ultimately, their success in doing so depends upon the effectiveness with which corporate strategy is implemented. This in turn depends upon the role of the corporate headquarters in managing companies that comprise multiple business units. We have identified four principal types of activity through which corporate management creates value within these companies:

- ◆ *Managing the business portfolio*: deciding which businesses and geographical markets the company should serve and allocating resources among these different businesses and markets.
- ◆ *Managing linkages among businesses*: exploiting opportunities for sharing resources and transferring capabilities comprises multiple activities ranging from the centralized provision of functions to best practices transfer. The key is to ensure that the potential gains from exploiting such economies of scope are not outweighed by the costs of managing the added complexity.
- ◆ *Managing individual businesses*: increasing the performance of individual businesses by enhancing the quality of their decision making, installing better managers, and creating incentives that drive superior performance.
- ◆ *Managing change and development*: although multibusinesses have the key advantage of not being captives of a single industry, exploiting this advantage means the processes, structures, and attitudes that foster new initiatives and create a willingness to let go of the past.

Finally, there is the contentious and perplexing issue of corporate governance. While broad agreement exists over the goal of corporate governance—ensuring that companies pursue long-term value maximization while taking account of the interest of multiple stakeholders—putting in place a system that achieves this goal remains elusive. Establishing corporate systems that are invulnerable to self-serving managers, short-term orientated shareholders, human greed and stupidity, and bureaucratic inertia represents a design challenge that is unlikely to be realized.

Self-Study Questions

1. Unilever—one of the world's leading consumer goods companies—is reviewing its business portfolio in order to address the problems of unsatisfactory growth and profitability. The head of group planning has asked for your advice on the use of portfolio matrices as an initial screen of Unilever's portfolio of businesses. Should Unilever use portfolio analysis and, if so, which portfolio matrix would you recommend: the McKinsey, BCG, or Ashridge matrix?
2. Apply the BCG matrix to the different programs that your institution offers. (You will need to make some informed guesses about market growth rates and relative market share.) Does this analysis offer useful implications for strategy and resource allocation?
3. The discussion of “performance management and financial control” identified two companies where the corporate HQ imposes a strong performance management system on its business units, PepsiCo and BP. To which company do you think a performance management system using financial targets is better suited?
4. Amazon.com, Inc. is under pressure to improve its profitability (between 2015 and 2017 it earned a net margin of 1.4%). Amazon is a highly diversified company engaged in online retailing in 14 different countries, audio and video streaming, the production and sale of mobile electronic devices, web hosting and other cloud computing services, and numerous other activities. Of the four main corporate management roles discussed in this chapter—managing the corporate portfolio, managing linkages among businesses, managing individual businesses, and managing change and development—which offers the greatest opportunities for Amazon's corporate headquarters to create value?
5. Would holding companies (such as Tata Group, Samsung Group, the Virgin Group, and Berkshire Hathaway) be more successful if they were converted into multidivisional corporations (such as General Electric, Philips, and Unilever)?

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