Horizontal Strategy in a Diversified Corporation

By

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ABSTRACT

Competition in the business world is becoming harsher as markets shrink due to the financial crisis of the late 2000s. Firms have to leverage their core competencies to survive by attracting more customers and attaining more efficient operations. In such circumstances, diversified corporations that run multiple businesses have opportunities to differentiate themselves by implementing horizontal strategies. Unfortunately, a horizontal strategy never happens spontaneously. There must be strong control and solid process to realize synergy. Furthermore, there are no generalized or standardized methods for developing and implementing a horizontal strategy. Executing this kind of corporate strategy is very difficult in the real world.

However, if the firm could establish a solid infrastructure to implement a horizontal strategy, it would be a sustainable competitive advantage that could not be easily imitated. In fact, there are many firms that enjoy synergy by implementing a horizontal strategy using various approaches. They differentiate their products and services, reduce operating costs, attract and involve customers, and create high barriers to prevent invasion by rivals. A horizontal strategy is a powerful business tool that enhances a firm’s capabilities and increases its corporate value.

In this thesis, I will investigate several historical theories of horizontal strategy and attempt to integrate their core concepts. I will examine four actual diversified corporations to determine how they utilize their horizontal strategy, while also identifying their critical driving forces and challenges. Then I will propose a practical process for creating and implementing a horizontal strategy. In my proposal, I will also recommend appropriate evaluation system and strong leadership because the lack of them frequently results in failure.

Thesis Supervisor: Arnoldo C. Hax
Title: Alfred P. Sloan Professor of Management Emeritus
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1.1 Purpose of Thesis

In recent years, business competition has become harsher in virtually every industry. Particularly after the financial crisis of the late 2000s, most markets became smaller, and firms were forced to become more competitive in order to attract customers. Most managers have for years been making great effort to generate competitive advantage in their business units, but it is more difficult for a single business unit today to create and maintain sustainable competitive advantage.

What, then, will create sustainable competitive advantage for the future? I believe the answer is a synergistic approach to creating added value among multiple business units within the firm. I use the term “horizontal strategy” to express this synergistic approach, and I use “synergy” to express additional value generated by executing a horizontal strategy (details are provided in Chapter 2). Every single business unit can take advantage of synergy to generate competitive advantage, and it can be sustained because skills and know-how are generated by its horizontal strategy. In many cases, rival companies will find it hard to develop a similar strategy over a short amount of time, and it would be difficult to imitate.

In general, horizontal strategy is regarded by business management as quite difficult to implement. Considerable research abounds documenting the fact that many mergers and
acquisitions fail because they do not generate synergies among the parties. A wide variety of people work in each business unit, surely giving each unit a unique culture. A successful horizontal strategy requires combining and mixing these different elements, and a firm will need strong leadership to realize it. Arnoldo Hax and Nicolas Majluf (1996) note: “Horizontal strategies do not tend to emerge spontaneously” (p. 226); and further: “It will not materialize unless there exists a determined will to make it happen” (p. 226). Michael Porter (1985) states:

The failure of synergy stemmed from the inability of companies to understand and implement it, not because of some basic flaw in the concept. . . . Even in instances where companies possessed a genuine opportunity to harness synergy, they often failed because the tools for analyzing it were lacking or they could not overcome the substantial organization problems of implementation. (p. 318)

These authors agree that horizontal strategy and synergy generation are difficult to implement.

The purpose of this thesis is to identify and suggest methods for overcoming the difficulties that face a diversified corporation when it tries to execute a horizontal strategy. I am employed by Kirin Group, Japan’s largest food and beverage corporation, and have been there for more than 15 years. Kirin is a diversified corporation that runs multiple businesses, including beer, wine, whiskey, soft drinks, pharmaceuticals, foods, and so on. Kirin is acting to generate synergies among its business units, but sufficient success has not yet been achieved.

In this thesis, I will define and discuss the concept of synergy, investigate several case studies, and propose a pragmatic horizontal strategy process for creating sustainable
competitive advantage. I believe this thesis will offer clues that can help Kirin attain sustainable competitive advantage, and it can assist managers in any corporations who are struggling to generate synergy.

1.2 Thesis Structure

There are six chapters in the thesis. The first chapter introduces the thesis, and describes its purpose and basic structure.

Chapter 2 defines terms and clarifies key words and ideas to avoid ambiguity and misunderstanding.

Chapter 3 considers the historical perspective. I research several theories, including those of Michael E. Porter, Jay B. Barney, Arnold C. Hax, and others. At the end of the chapter, I will try to integrate the ideas from these sources to create a framework for developing a horizontal strategy.

Chapter 4 investigates four active diversified corporations in an effort to understand how they create and implement a horizontal strategy. I will compare the challenges in each corporation with the theories presented in Chapter 3.

Chapter 5 presents a proposal for creating and implementing a horizontal strategy in a diversified corporation. I provide practical processes, organization, evaluation system, and leadership skills needed for a successful horizontal strategy.
Finally, in Chapter 6, I conclude with a summary and some observations. Figure 1-1 illustrates the basic thesis structure.

Source: developed by author.

**Figure 1-1 Basic structure of this thesis**
CHAPTER 2
DEFINITIONS

In this chapter, I will define key words and ideas used in the thesis.

2.1 Diversified Corporation

I use the phrase “diversified corporation” to mean a company that runs businesses in multiple industries simultaneously. In other words, if the company launches a new business that belongs in a different industry from its original business, the company becomes a diversified corporation.

Diversified corporations typically adopt one of several organization styles, as shown in Figure 2-1. It could be a single company containing two or more business units (Type A in Figure 2-1); it could be one main company that runs a primary business and one or more subsidiaries that each run other businesses (Type B in Figure 2-1); it could be one pure holding company that focuses on managing corporate strategy, with two or more subsidiaries that run actual operational businesses (Type C in Figure 2-1). In each case, I use the phrase ‘corporate function’ to express the various headquarters’ roles that are dedicated to group management, and the phrase ‘business unit’ to express each operational business entity.
Figure 2-1 Corporate function and business units in several organizations

There are several reasons why companies diversify. Hiroyuki Itami and Tadao Kagono (2003) suggest there are three main reasons for diversifying a business: economy of scale, dispersion of risk, and economy of growth (p. 93). "Economy of scale" means cost reduction achieved by sharing activities among multiple business units. "Dispersion of risk" means avoiding the risk of environmental change, which is expected to decrease by having multiple business units. "Economy of growth" means the economic advantage that growth itself brings about. For instance, growth changes cost structure positively because hiring more young workers lowers average labor costs. In another example, growth gives positive psychological energy to employees, and this energy is a driving power of the company.

Hax and Majluf (1996) discuss several alternatives for how companies can grow (see Figure 2-2). They state there are two alternatives for diversifying a business—related and unrelated—and call unrelated diversification a conglomeration (p. 206). However, in Itami's (2003) perspective, unrelated diversification has the advantage of dispersion of risk and economy of growth.
Identifying unrelated diversification is a big problem. According to Jay B. Barney (2006), there are several motivations for a company to diversify its business, and he shows the relationships between motivation of diversification and type of diversification (see Figure 2-3). In my view, although unrelated diversification certainly has some advantages, it would never of itself create a sustainable competitive advantage because of the factors Itami cites (‘Dispersion of Risk’ and ‘Economy of Growth’) as well as those cited by Barney (‘Risk Reduction’, ‘Tax Advantage’, ‘Exploiting Market Share’ and ‘Firm Size and Employee Incentives for Diversification’). All are easy for rival companies to imitate. For this reason, I would agree with Hax and Majluf: unrelated diversification is a conglomeration.

Source: Hax and Majluf (1996), p. 205. Adapted by author

**Figure 2-2 Alternatives for growth**
Consequently, I will focus specifically on related diversified corporations, and will use ‘Diversified Corporation’ as a related diversified corporation.

<table>
<thead>
<tr>
<th>Motivation</th>
<th>Related Diversification</th>
<th>Unrelated Diversification</th>
</tr>
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<tbody>
<tr>
<td>Operating economies of scope</td>
<td></td>
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</tr>
<tr>
<td>• Shared activities</td>
<td>X</td>
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<td>• Core competencies</td>
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<td>Financial economies of scope</td>
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<td>• Internal capital allocation</td>
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<td>• Tax advantages</td>
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<tr>
<td>Anticompetitive economies of scope</td>
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<tr>
<td>• Multipoint competitive</td>
<td>X</td>
<td></td>
</tr>
<tr>
<td>• Exploiting market share</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>Firm size and employee incentives for diversification</td>
<td>X</td>
<td></td>
</tr>
</tbody>
</table>


Figure 2-3 Relationships between motivation for diversification and type of diversification

2.2 Synergy and Horizontal Strategy

The ‘synergy’ is one of the most critical issues for a diversified corporation. To define ‘synergy’, I must first define ‘horizontal strategy’, which is used here as the process of creating synergy. Hax and Majluf (1996) define it this way: “Adding value beyond the simple sum of independent business contributions” (p. 225). Robert S. Kaplan and David P. Norton (2006) define it as, “Add[ing] value to its collection of business units and shared-service units” (p. 5). Porter (1985) expresses it as “combining different but related businesses could create value” (p. 318). I quote these three definitions because each of them contains critical keywords.
I believe horizontal strategy should be implemented by independent business units, as Hax and Majluf define. I also believe that horizontal strategy should be pursued by all corporate entities including shared-service units, as Kaplan and Norton claim. In addition, I believe that horizontal strategy should be executed by combining related businesses, as Porter expresses. Therefore, I define ‘Horizontal strategy’ as the following: Adding value beyond the simple sum of independent but related business units and shared-service units by combining their assets and capabilities. I replaced Porter’s word “businesses” with “assets and capabilities” because assets and capabilities are only resources we can combine in the business.

Now “synergy” can be defined as follows: The difference between corporate value and the simple sum of the value of business units and shared-service units. Figure 2-4 illustrates definitions of ‘synergy’ and ‘horizontal strategy.’

![Figure 2-4 Definition of ‘synergy’ and ‘horizontal strategy’](image-url)
2.3 Why Should a Diversified Corporation Generate Synergy?

One may wonder why a diversified corporation has to generate synergy. There are plenty of diversified corporations in the world, but not all intend to pursue a horizontal strategy. If a diversified corporation is sufficiently profitable, and management and the employees are happy, then one would suppose that corporation would not have to think about synergy. However, if they do not pursue any synergies, why form a corporation in the first place? Even if there is no synergy in the corporation, there is overhead required to manage the business units. Why not break up the corporation and make each business unit independent and thus eliminate the overhead? Porter (1985) observes: “Without horizontal strategy, there is no convincing rationale for the existence of a diversified firm because it is little more than a mutual fund” (p. 319). Forming corporation but not pursuing a horizontal strategy is completely inefficient. It destroys corporate value, i.e., stockholder value, particularly in the advanced economic environment of developed countries. Taking the economic perspective of stockholders, I believe diversified corporation should generate synergy.

In addition, as described in Chapter 1, competition among companies is getting harsher. Management is required to create sustainable competitive advantage in order to attract more customers and win the competition. Synergy—especially one generated by a carefully designed horizontal strategy—would be a strong sustainable competitive advantage because it is not yet generalized and commoditized. If one could establish a systematic process of horizontal strategy in the corporation, it would be valuable, rare, and hard for
rivals to imitate. Hax and Majluf (1996) state: “For many organizations, the appropriate pursuit of horizontal strategy becomes one of the most critical ways to establish a superior competitive position” (p. 225). David A. Aaker (2001) notes,

Synergy between strategic business units can provide a sustainable competitive advantage that is truly sustainable because it is based on the characteristics of a firm that are probably unique. A competitor might have to duplicate the organization in order to capture the assets or competencies involved. (p. 194)

Therefore, as the competitive perspective from management’s viewpoint, I believe a diversified corporation should generate synergy.

Synergy often brings innovative products or services that one single business unit would have difficulty producing. For instance, Apple combines its powerful design skill with a strong digital music capability and conventional cellphone technology, to develop its innovative and highly successful product, i-Phone. Kirin combined its brewing know-how with its soft drink technology to launch an alcohol-free (0.00%) beverage that duplicates the taste of beer. These examples show that synergy can expand the range of products or services, and contribute to customer satisfaction. As a marketing perspective from the customer viewpoint, I believe a diversified corporation should generate synergy.

The reasons why diversified corporations should generate synergy are summarized in Figure 2-5. This figure represents my proposed ‘Principle of Value Creation’ using synergy.
Figure 2-5 The Principle of Value Creation

Source: developed by author.
CHAPTER 3
HISTORICAL CONSIDERATIONS

For years, many researchers have devoted themselves to various facets of business strategy. In 1959, the McKinsey Award was established by the *Harvard Business Review*, and every year thereafter, the award has been conferred on the most excellent research of the year. Past winners include Peter F. Drucker, Michael E. Porter, Gary Hamel, Clayton M. Christensen, Henry Mintzberg, and others.

Over time, the theory of business strategy has evolved in different ways. But I believe there exists universal fundamentals that support various ideas. In this thesis I will try to focus the spotlight on the fundamentals of horizontal strategy that exist in an ocean of management arguments. This chapter investigates some historical theories and draws a larger picture of the principle of horizontal strategy.

3.1 Porter’s Framework
3.1.1 Overview

I investigated Michael Porter’s framework seeking to understand his main points. He is one of the strongest and most popular researchers of business strategy. Although his famous frameworks—Five Forces, Value Chain, and Diamond of National Advantage—were proposed some years earlier, they remain viable as basic models and foundations for many business people worldwide. For this reason, I begin the chapter with his research.

In the simplest term, Porter proposes that firms should study the external environment by using the Five Forces framework; then examine their internal strengths and weaknesses using the Value Chain framework; and then select an attractive industry to compete and pursue a cost leadership strategy or a differentiation strategy in each activity of the value chain. Figures 3-1 and 3-2 provide the basic framework of the Five Forces framework and the Value Chain framework.

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1 Most of my knowledge about Porter’s work is based on these books and articles: Competitive Strategy (1980), Competitive Advantage (1985), On Competition (2008), and “Towards a dynamic theory of strategy” (1991).
Figure 3-1 Five Forces framework

Figure 3-2 Value Chain framework
These frameworks are powerful when used to plan a single business unit strategy. However, when considering a horizontal strategy, another approach should be taken. Porter (1985) states:

Business strategy charts the course for a firm’s activities in individual industries, while corporate strategy addresses the composition of a firm’s portfolio of business units. . . . Horizontal strategy provides for explicit coordination among business units that makes corporate or group strategy more than the sum of the individual business unit strategies (pp. 318-319).

Porter clearly differentiates business strategy and corporate strategy, positioning horizontal strategy as the core of the corporate strategy. He provides four concepts for corporate strategy: (1) Portfolio Management, (2) Restructuring, (3) Activity Sharing, and (4) Skill Transfer (2008: 147-159). While the first two concepts do not require coordination among business units, the latter two definitely need horizontal coordination. In Porter’s view, Activity Sharing and Skill Transfer are the key factors of horizontal strategy. He often emphasizes the importance of coordinating interrelationships among business units. In this context, coordination of interrelationships indicates Activity Sharing and Skill Transfer. In summary, Porter believes that Activity Sharing and Skill Transfer are two critical concepts needed to generate synergy in a diversified corporation. Figure 3-3 shows Porter’s view of horizontal strategy.
3.1.2 Porter’s Horizontal Strategy: Activity Sharing

Porter (1985) states, “A business unit can potentially share any value activity with another business unit in the firm, including both primary and supporting activities” (p. 326). In fact, because coordination of activity sharing is an easier way to generate synergy, many diversified corporations try to implement some kinds of activity sharing. The concept of shared-service unit is an example of activity sharing. Some diversified corporations have a central R&D organization whose activities are shared by multiple business units. Some utilize collaborative procurement to purchase common raw materials cheaper by increasing the purchase volume. As activity sharing mainly reduces unit cost, it could be a competitive
advantage for every participating business unit. Figure 3-4 shows the principle of activity sharing.

![Activity Sharing Diagram](image)

**Activity 1:** Both business units decrease the activity cost.

**Activity 2:** Business unit A takes charge of activity and business unit B stops activity. Total cost of activity decreases.

**Activity 3:** Business unit A halves the activity cost while business unit B doesn’t change. Total cost of activity decreases.

Source: developed by author.

**Figure 3-4 Principle of activity sharing**

On the other hand, activity sharing always involves a cost. Porter (1985) identifies three types of cost: (1) cost of coordination, (2) cost of compromise, and (3) cost of inflexibility (p. 331). Sometimes these costs become high enough that they discourage managers from
implementing activity sharing. Such costs should be removed or reduced by designing a careful system of horizontal strategy. I will argue this point in Chapter 5.

3.1.3 Porter’s Horizontal Strategy: Skill Transfer

If one business unit in a diversified corporation has some type of know-how, and if the know-how could be utilized in other business units to enhance their competitive strength, then the know-how should be transferred. This could include marketing skills, effective production processes, an effective human resource management system, and so on. Whatever it is, if it is effective in other business unit, then it should be transferred. Porter (1985) notes: “The transference of generic know-how can occur anywhere in the value chain” (p. 350). By transferring skills from one business unit to another, a diversified corporation can raise its business capability. Moreover, a transferred skill sometimes evolves in the different environment so that it can, in turn, be transferred to the original business unit.

Unlike sharing tangible assets, skill transfer has infinite possibilities. For example, the effect of production-line sharing is limited because there are physical limits to the capacity of the production line. One business unit could make use of the production line when another business unit is not producing anything. Two business units could not use the same production line simultaneously, which is the obvious limitation of sharing a tangible asset. On the other hand, skill transfer is the sharing of intangible know-how. Two different business units could use the same marketing skill or efficient production process
simultaneously. In this sense, skill transfer has huge potential for a diversified corporation.

Figure 3-5 shows the principle of skill transfer.

Skill 4: Transferred from business unit B to business unit A.
Skill 5: Transferred from business unit B to business unit A.
Skill 5': Skill 5 evolves in business unit B and is transferred back to business unit A.

Source: developed by author.

Figure 3-5 Principle of Skill Transfer

I found that skill transfer has not been implemented either sufficiently or systematically. I believe this is true because skill transfer is quite difficult to identify. Since skills are intangible, managers have trouble knowing how to handle it, and cannot tell if it is been transferred. Porter (1985) says, "The transference of know-how is subjective and the
benefits of doing so often are hard for managers to understand when compared to tangible interrelationships” (p. 353).

As I mentioned above, however, skill transfer has huge potential for synergy generation, that is, increasing corporate value. Therefore, we have to identify or develop a systematic process for driving skill transfer. I will discuss this point in greater detail in Chapter 5.

3.2 Resource-Based View

The Resource-Based View (RBV) is another representative and popular theory in the research on business strategy. I investigated RBV to understand its main approach.2

3.2.1 Overview

While Porter stresses ‘attractiveness of industry’ and ‘positioning in the industry’, supporters of RBV emphasize the firm’s ‘internal resources’. Robert Grant (1991) states that resources are the basis of a firm’s capability (in his definition, capability is a team of resources), and it is capabilities that create competitive advantage and bring profitability to the firm (pp. 118-19). Barney (2006) sees resources and capability as being interchangeable; Collis and Montgomery (2004) call it “organizational capabilities” and distinguish them from resources. In this thesis, I will use these terms in accordance with Grant’s definition. He

2 Most of my knowledge about RBV is based on these books and documents: Gaining and Sustaining Competitive Advantage by Barney (2006); Corporate Strategy: A Resource-Based Approach by Collis and Montgomery (2004); and “The resource-based theory of competitive advantage: Implications for strategy formulation,” by Grant (1991).
claims: “The resources and capabilities of a firm are the central considerations in
formulating its strategy: they are the primary constants upon which a firm can establish its
identity and frame its strategy, and they are the primary sources of the firm’s profitability”
(p. 133). Barney (2006) says, “[The] resource-based view of the firm . . . focuses on the
idiosyncratic, costly-to-copy resources controlled by a firm – resources whose exploitation
may give a firm a competitive advantage” (p. 133). The idea that the resources of a firm are
the central foundation of competitive advantage is the core concept of RBV.

RBV has long been criticized as a theory that lacks practical implementation. In 1990s,
however, Grant proposed a strategic framework that shows how to identify resources,
capabilities, and competitive advantage (see Figure 3-6). Subsequently, Collis and
Montgomery introduced their Corporate Strategy Triangle (see Figure 3-7), which combined
RBV theory with practical strategy. Although there is not yet a single dominating framework,
RBV is a promising model for considering business strategies.
4. Select a strategy which best exploits the firm’s resources and capabilities relative to external opportunities.

3. Appraise the rent-generating potential of resources and capabilities in terms of:
   (a) their potential for sustainable competitive advantage and
   (b) the appropriability of their returns.

2. Identify the firm’s capabilities: What can the firm do more effectively than its rivals? Identify the resources inputs to each capability and the complexity of each capability.

1. Identify and classify the firm’s resources. Appraise strengths and weaknesses relative to competitors. Identify opportunities for better utilization of resources.

5. Identify resource gaps which need to be filled. Invest in replenishing, augmenting and upgrading the firm’s resource base.

Source: Grant (1991), p. 115. Adapted by author

**Figure 3-6 Grant’s framework**


**Figure 3-7 Corporate strategy triangle**
3.2.2 RBV: Horizontal Strategy

Porter’s framework and the RBV framework provide different viewpoints for planning a single business unit strategy. However, they offer similar viewpoints when we consider a horizontal strategy. As shown earlier in Figure 2-3, Barney classifies motives for diversification into four categories: Operating Economies of Scope, Financial Economies of Scope, Anti-competitive Economies of Scope, and Firm Size and Employee Incentives for Diversification.

Operating economies of scope are what corporate management should pursue by implementing horizontal strategy. Barney (2006) defines ‘Shared Activities’ and ‘Shared Core Competences’ as two elements of operating economies of scope (p. 343). This idea is similar to what Porter calls “Activity Sharing” and “Skill Transfer” in the horizontal strategy. I will investigate Barney’s two elements in detail in this section.³

3.2.3 RBV: Shared Activities

The concept of shared activities is similar to Porter’s activity sharing. Barney (2006) notes, “Shared activities can add value to a firm by reducing costs or by increasing the willingness of customers to pay” (p. 344). In contrast to Porter’s position, Barney states that shared activities could increase sales, and Barney explains its mechanism by showing ‘product

³ Three other categories of motivation for diversification correspond to one of Porter’s other corporate strategies, Portfolio Management and Restructuring, but as I mentioned in Section 3.1, they are not a horizontal strategy.
bundles’ and ‘exploiting the strong, positive reputations’. Since we generally see the benefit of shared activities as cost reduction, his explicit indication gives us a fresh viewpoint.

3.2.4 RBV: Shared Core Competencies

The concept of shared core competencies, as proposed by Barney with regard to a horizontal strategy, is similar to Porter’s concept of skill transfer. The phrase ‘core competence’ was introduced by Gary Hamel and C. K. Prahalad in a 1990 article in *Harvard Business Review*. They define it as, “[T]he collective learning in the organization, especially how to coordinate diverse production skills and integrate multiple streams of technologies” (pp. 79-91). Core competence definitely indicates intangible skills developed in the organization. Thus, sharing core competencies among business units literally means transferring skills between business units. Barney (2006) states, “Core competencies enable firms to have lower costs or increase their customers’ willingness to pay . . . compared to firms without these competencies” (p. 350). Clearly, he believes that core competencies (skill transfer) will bring competitive advantage to a diversified corporation.

3.2.5 RBV: Competitive advantage

One of the unique characteristics of RBV is the idea of creating sustainable competitive advantage. RBV sees internal resources as the foundation of a firm’s capability. Two or more resources can be used to conduct some activities, which is called capability. Capabilities that are superior to those of rival firms are defined as competitive advantage.
What is unique is the test method used by RBV when it identifies sustainable competitive advantage over other competitive advantages. Like Porter, RBV values sustainable competitive advantage for competition against rivals.

Here I will introduce Grant’s test method and compare it with Barney’s test method. Grant (1991) identifies four conditions that mark sustainable competitive advantage: durability, transparency, transferability, and replicability (pp. 123-128) – meaning sustainable competitive advantage should be durable, should not be transparent to rivals, should not be transferable to rivals, and should not be replicable within rivals. Of all competitive advantages, only those that satisfy these four conditions are identified as sustainable competitive advantage, and they are the core strengths of a firm looking for future sustainable growth.

Barney’s framework is called VRIO: Value, Rarity, Inimitability, and Organization. He says that a firm should ask four questions to analyze sustainable competitive advantage: whether competitive advantage is valuable, rare, inimitable by its rivals, and whether there is proper organization to leverage competitive advantage (2006, pp. 138-150). It is striking that Barney includes Organization in his framework. He understands that it is people and organizations that realize sustainable competitive advantage; if there is no appropriate organization, any advantage will not be effective. Clearly, I must consider ‘Leadership and Organization’ when I propose a pragmatic process of horizontal strategy. I will discuss this point further in Chapter 5.
It is relatively easy to apply RBV to create horizontal strategy. Shared activities means creating capabilities by mixing tangible resources of business units. Shared core competencies means creating capabilities by mixing intangible resources (skills) of business units. Of all the capabilities created, those that satisfy Grant’s or Barney’s test are called sustainable competitive advantage. Thus, creating capabilities and sustainable competitive advantage is the process of horizontal strategy in RBV, and created capabilities are the foundation of synergy. Figure 3-8 shows horizontal strategy in RBV.

If resources are tangible, the process creating capability is called sharing activities. If resources are intangible, the process creating capability is called core competences.

Source: developed by author.

Figure 3-8 Horizontal strategy in RBV
3.3 **Hax's Framework and Delta Model**

In this section, I investigated Arnoldo C. Hax theory and framework known as the Delta Model to understand the key points of this approach.  

3.3.1 **Overview**

Hax proposes the Delta Model as a framework and methodology to help managers make effective corporate and business strategies and to identify the firm’s existing competencies. Hax’s framework integrates the RBV and Porter frameworks by adding customers’ and complementors’ perspectives to the model. Hax introduces ten axioms of strategy (so-called “Haxioms”) (2010: pp. 10-13). Of the ten Haxioms, the first, third, and seventh present his theory well. He values customer bonding and makes it a top priority in the strategy. He repeats the importance of love for customers, and he is against war with rivals. His framework is quite simple and practical, which highlights the matches of customer value proposition and competencies of the firm. In this section, I will begin by discussing the Delta Model and Hax’s pragmatic strategic process, then I will investigate the horizontal strategy of this theory.

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4 My knowledge of this theory is based on these books: *The Strategy Concept and Process* by Hax and Majluf (1996), and *The Delta Model* by Hax (2010).

5 #1: “The center of strategy is the customer”; #3: “Strategy is not war; it is love”; #7: “The foundations of strategy are two: Customer Segmentation and Customer Value Proposition, and the Firm as a Bundle of Competencies.”
3.3.2 Delta Model and Strategic Process

The Delta Model framework expresses three strategic options: ‘Best Product’, ‘Total Customer Solution’, and ‘System Lock-in’, which firms can utilize to realize customer bonding. Hax uses a triangle shape to display these options, and puts one option in each corner of the triangle. These three options are not tradeoffs, but the firms could take multiple options at the same time. Hax (2010) notes: “A sophisticated strategy plays simultaneously in every corner of the triangle, depending on the way you choose to serve the heterogeneous diversity of your customers” (p. 15).

He also defines eight strategic positions associated with the three options. Surprisingly, Porter’s two strategic positions, Low Cost and Differentiation, are associated with the Best Product option, a starting-point of eight positions. Hax stresses that Porter’s two strategic positions are not sufficient to create strong customer bonding, and has added six additional strategic positions. Figure 3-9 shows the Delta Model with all eight strategic positions.
Hax’s theory has five stages: Customer Segmentation and Customer Value Proposition, Existing and Desired Competencies of the Firm, Mission of the Business, Strategic Agenda, and Monitoring the Strategy Execution. He calls them ‘Strategic Tasks’ (2010, pp. 186-189).

There are two unique ideas in Hax’s theory. First, he puts customers at the center of the strategy. Porter puts competition (or competitors) at the center. RBV puts resources (or the corporation) at the center. It is interesting that all three share each component of the 3C model, but because Hax believes strategy should include love for customers and customer bonding, his importance is on the customers’ perspective. Second, he provides various
practical models, based on ‘The Strategic Agenda’ and ‘Monitoring the Strategy Execution’. These are helpful for managers trying to make corporate/business plans in the real world.

The Delta Model and Hax’s theory spotlight the demand and supply aspects of the business. This seems similar to Porter’s framework and the RBV, but is actually quite different because Hax focuses more on how to attract customers, not on matches of external environment and internal strengths and weaknesses. In this sense, Hax’s theory provides a fresh perspective and complements what was missing in the other frameworks.

### 3.3.3 Horizontal Strategy in Hax’s Theory

Hax and Majluf (1996) lay out ten tasks for corporate strategy as shown in Figure 3-10. Horizontal strategy is one of these tasks. The authors say: “One could argue that horizontal strategies are the primary sources for corporate advantage of a diversified firm. It is through the detection and realization of the existing synergy across the various businesses that significant additional economic value can be created” (p. 187). They position horizontal strategy as the core of corporate strategy, noting, “The pursuit of horizontal strategy is a central task for corporate management” (p. 226).
Figure 3-10 Fundamental elements of the definition of corporate strategy: the ten tasks

Source: Hax and Majluf (1996), p. 190. Adapted by author
Hax and Majluf show ‘Identification of sources of interrelationships’ and ‘Configuration/Coordination of activities of the value chain’ as the action programs of horizontal strategy (pp. 231-239). Their methodology is so practical that managers should be able to understand and implement it easily. Figure 3-11 shows an example of identification, and Figure 3-12 shows an example of configuration and coordination. By using these forms, a firm can detect and leverage interrelationships among business units and realize synergy.

![Figure 3-11 Example of ‘Identification of sources of interrelationships’](image)

<table>
<thead>
<tr>
<th>VALUE-CHAIN ACTIVITIES</th>
<th>Molyb</th>
<th>Nick</th>
<th>Tungsten</th>
<th>Copper</th>
<th>Ld/Zn</th>
<th>Silver</th>
<th>Specialty Metal</th>
<th>Iron</th>
<th>Alum</th>
<th>Magn</th>
<th>Oil &amp; Gas</th>
<th>Fert</th>
<th>Coal</th>
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<tbody>
<tr>
<td>Product R&amp;D</td>
<td>X</td>
<td>X</td>
<td>X</td>
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<td>Process R&amp;D</td>
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<tr>
<td>Purchasing of Raw materials</td>
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<tr>
<td>Transportation of Raw materials</td>
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<tr>
<td>Exploration</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td></td>
<td>X</td>
<td></td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
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<td>X</td>
<td></td>
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<tr>
<td>Mining Technology and Mining Operation</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
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<tr>
<td>Know-how</td>
<td>X</td>
<td>X</td>
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<tr>
<td>Marketing</td>
<td>X</td>
<td>X</td>
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<tr>
<td>Sales</td>
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<td>X</td>
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<tr>
<td>Distribution</td>
<td>X</td>
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</tbody>
</table>

Note: X indicates sharing

<table>
<thead>
<tr>
<th>ACTIVITIES OF THE VALUE</th>
<th>CENTRALIZATION CONFIGURATION</th>
<th>HIGH COORDINATION</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>ADVANTAGES</td>
<td>DISADVANTAGES</td>
</tr>
<tr>
<td>R&amp;D</td>
<td>• Go down the learning curve faster</td>
<td>• Failure to respond to heterogeneous local product needs</td>
</tr>
<tr>
<td></td>
<td>• Gain scale and scope</td>
<td>• Failure to respond to government requirements in some countries</td>
</tr>
<tr>
<td></td>
<td>• Gain protection against leakage of technology to outsiders</td>
<td>• Better serve multinational buyers</td>
</tr>
<tr>
<td>Components manufacturing</td>
<td>• Gain scale economies</td>
<td>• Transport and storage costs</td>
</tr>
<tr>
<td></td>
<td>• Go down the learning curve faster</td>
<td>• No hedge against the risks of single site</td>
</tr>
<tr>
<td></td>
<td>• Unable to encourage nationalistic purchasing</td>
<td>• Failure to respond to competitors</td>
</tr>
<tr>
<td>Assembly</td>
<td>• Better quality control</td>
<td>• Higher costs</td>
</tr>
<tr>
<td></td>
<td>• Failure to respond to heterogeneous local product needs</td>
<td>• Flexibility in responding to competitors</td>
</tr>
<tr>
<td></td>
<td>• Failure to respond to local government requirements</td>
<td>• Respond to changes in comparative advantage among countries</td>
</tr>
<tr>
<td></td>
<td>• Failure to encourage nationalistic purchasing</td>
<td>• Government restrictions on flows of goods and information</td>
</tr>
<tr>
<td>Testing and quality control</td>
<td>• Some economies</td>
<td>• Failure to differentiate product in final production stages to address local market segments</td>
</tr>
<tr>
<td></td>
<td>• Some learning curve effects</td>
<td>• Failure to encourage nationalistic purchasing</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Failure to respond to government requirements</td>
</tr>
<tr>
<td>Marketing, distribution, and sales</td>
<td>• Standard marketing policies worldwide</td>
<td>• Failure to respond to heterogeneous local product needs</td>
</tr>
<tr>
<td></td>
<td>• Solidify brand reputation worldwide</td>
<td>• Failure to encourage nationalistic purchasing</td>
</tr>
<tr>
<td></td>
<td>• Failure to respond to government requirements</td>
<td>• May not respond well to heterogeneous local conditions</td>
</tr>
</tbody>
</table>

Source: Hax and Majluf (1996), p. 238. Adapted by author

Figure 3-12 Example of 'Configuration and coordination of activities of the value chain'
Hax and Majluf support Porter’s classification of interrelationships—‘Tangible Interrelationships’, ‘Intangible Interrelationships’, and ‘Competitor Interrelationships’. Since Tangible Interrelationships are similar to Activity Sharing in Porter’s definition, and Intangible Interrelationships similar to Skill Transfer, the mechanism for generating synergy of Hax and Majluf’s theory is almost the same as Porter’s. Figure 3-13 shows Hax and Majluf’s principle of horizontal strategy.

![Figure 3-13 Hax and Majluf’s Principle of Horizontal Strategy](image)

Source: developed by author.
3.4 Other Theories

In this section, I also examined the frameworks of Hiroyuki Itami and Tadao Kagono, David Aaker, and the Boston Consulting Group.6

3.4.1 Itami and Kagono’s Theory

As mentioned in Chapter 2, Itami & Kagono (2003) developed three categories for classifying the reason for a firm’s diversification; Economy of Scope, Dispersion of Risks, and Economy of Growth. Of these categories, Economy of Scope is the horizontal strategy that a diversified corporation should pursue, because other two categories are somewhat attainable by diversification itself. The authors state: “Among those three logics of diversification, the most important one is economy of scope. We can say that this logic always exists behind most successful cases of diversification” (p. 98).

The authors describe two economic effects arising from economy of scope: Complementary Effect, and Synergistic Effect. Complementary Effect is an additional combination result, which the authors call “making 2 from 1+1” (p. 98). For instance, one business unit can produce its products by using the production line of another business unit when it is not in use. Thus, two or more business units utilize one physical resource by complementing each other. Synergistic Effect is the result of multiple combinations, and the authors call it “making 3 by 1+1” (p. 99). For example, a beer manufacturer can apply its

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6 Most of my knowledge of their theories comes from these books: Management Seminar by Itami & Kagono (2003); Developing Business Strategies by Aaker (2001); BCG Strategy Concept by BCG & Mizukoshi (2003).
accumulated biotechnology to produce medical products. Both the beer business unit and
the medical business unit leverage the firm’s common skill, biotechnology, but neither
interferes with the other. Itami and Kogono say:

While the complementary effect is a shared physical resource, the
synergistic effect is sharing informational resources. There is a usage limit
in physical resources. On the other hand, there is no physical usage limit
with informational effect. We believe the synergistic effect is more valid
and efficient than the complementary effect (p. 99).

Obviously, the complementary effect corresponds to Activity Sharing in Porter’s concept,
and the synergistic effect corresponds to Skill Transfer. Figure 3-14 shows the horizontal
strategy of Itami and Kagono’s theory.
Figure 3-14 Horizontal strategy in Itami and Kagono's theory

Source: developed by author.
3.4.2 Aaker’s Theory

Aaker’s view of horizontal strategy is ‘Exporting or Exchanging Assets and Competencies’ (2001, p. 232). He introduces three steps. First is identifying transferable resources and skills, and he gives some examples: brand name, marketing skills, capacity in sales and distribution, manufacturing skills, and R&D skills (pp. 233-237). This is not much different from what Porter calls Skill Transfer, or what Barney calls Shared Core Competencies.

The second step is identifying a business region where conventional resources are applicable. He says “One fruitful exercise is to examine each asset for excess capacity... If a diversification can use excess capacity, a substantial, sustainable cost competitive advantage could result” (p. 233). As he explains, this step focuses on using excess capacity, similar to what Porter calls Activity Sharing, or what Itami & Kagono call Complementary Effect.

The third step is ascertaining the need for organizational integration. Aaker claims, “Many efforts at achieving synergy falter because of implementation difficulties” (p. 233). As Barney emphasizes the importance of organization, and Hax & Majluf indicate configuration and coordination of activities of value chain as action programs of horizontal strategy, Aaker suggests that organizational treatment is a big step toward horizontal strategy. Figure 3-15 shows horizontal strategy in Aaker’s theory.
3.4.3 The Boston Consulting Group Theory

Boston Consulting Group (BCG) is an innovative consulting firm that has introduced various strategic concepts to the world. One of their classic corporate strategic concepts is
Product Portfolio Management (PPM), developed in 1970s, but still a basic management theory of corporate strategy. PPM expresses business units by two dimensions, industry growth ratio and relative market share. All business units are classified into one of four quadrants: Star, Cash Cow, Problem, and Dog. The basic idea is that a firm should take cash from its Cash Cow and invest it into Problem in order to develop a future Star. At the same time, the firm should consider getting out of any business classified as Dog. Ideally a firm maintains a good balance Star, Cash Cow, and Problem business units. Figure 3-16 is a diagram of PPM.

![Figure 3-16 Diagram of PPM](image)


**Figure 3-16 Diagram of PPM**

However, by itself PPM is not a horizontal strategy. While it is definitely a task of corporate function, there are no interrelationships among business units. The authors explain the transition of the corporate role and portfolio management as evolving from ‘Traditional Headquarters’ through ‘Autonomic Company’, ‘Portfolio Company’, to
'Synergistic Company' (pp. 165-168). They believe that Synergistic Company is an evolved form of 'Portfolio Company', calling its foundation 'Organizational Platform'. By their definition, Organizational Platform is an infrastructure for generating synergy by cross-fertilizing human resources, technologies, know-how, brand, and so on—unlike a conventional portfolio company that focuses on cross-fertilizing just cash (p. 168).

I see that Organizational Platform corresponds directly to horizontal strategy, and the idea of cross-fertilizing various factors is similar to Activity Sharing and Skill Transfer in Porter's framework. Figure 3-17 shows the transition of the corporate role and portfolio management.

![Figure 3-17 Transition of corporate role and portfolio management](source: BCG & Mizukoshi (2003), p. 166. Adapted by author)
3.5 Integrating the Historical Works

In this section, I will try to integrate the various frameworks discussed in this chapter. Figure 3-18 shows the resulting picture of horizontal strategy.

First, the diversified corporation needs to evolve from a Portfolio Company to a Synergistic Company, just as BCG & Mizukoshi suggested. The corporate function should pursue synergy by implementing a horizontal strategy. There are two approaches: Activity Sharing and Skill Transfer. Although the various frameworks use different terms, all would be consolidated into these two approaches.

However, Activity Sharing and Skill Transfer are not sufficient to successfully accomplish horizontal strategy. There should also be organizational alignment. Kaplan & Norton (2006) state: “Enterprises enjoying the greatest benefits from their new performance management systems are much better at aligning their corporate, business unit, and support unit strategies, and this indicates that alignment . . . produces dramatic benefits” (p. 3). Therefore, I added configuration and coordination of the organization as one more task in horizontal strategy – just as Hax & Majluf and Aaker also suggest.

Finally, the corporate function must identify its sustainable competitive advantage by testing interrelationships realized by a horizontal strategy, using Grant’s or Barney’s frameworks.
Source: developed by author.

**Figure 3-18 Combined picture of horizontal strategy**
In this chapter, I will research four diversified corporations, seeking to identify the features of their horizontal strategy and the challenges facing each one. I will conclude the chapter by considering the possibilities and difficulties of implementing a horizontal strategy in each of the firms.

4.1 GENERAL ELECTRIC

4.1.1 Overview

General Electric (GE) is one of the world’s top firms, and has maintained that status for more than 100 years. In 2010, GE was ranked among Fortune magazine’s listing of the Most Admired Companies in the world for the fifth consecutive year. GE is the only company listed in the Dow Jones industrial Index today that was included in the original index in 1896. In 2010 GE had revenues of more than $150 billion; over 300,000 employees; and customers in 160 countries.

GE is one of the largest diversified corporations in the world, with six major divisions: Energy, Capital, Home & Business Solutions, Health Care, Aviation, and Transportation, with more than 100 business units worldwide (see Figure 4-1). Sometimes GE is criticized as
conglomerate, i.e., an unrelated diversified corporation with no synergy. Jeffery Immelt, Chairman and CEO of GE, responds to such criticism by saying:

Our businesses are closely integrated . . . They share leading-edge business initiatives, excellent financial disciplines, a tradition of sharing talent and best practices, and a culture whose cornerstone is absolutely unyielding integrity. Without these powerful ties, we could actually merit the label ‘conglomerate’ that people often inaccurately apply to us. That word does not apply to GE. What we have is a company of diverse benefits whose sum is truly greater than the parts. (Magee, 2009, pp. 189-190).

David Magee (2009) notes: “To grow in GE’s infrastructure segment, for example, Immelt implemented a vertical business strategy, creating cross-company teams from GE businesses like rail, water, energy, and finance to find common ground among unified selling and multilateral solutions” (p. 189).
Looking around the world, especially at developing countries and the vast number of people living there, we know that energy, water, and healthcare are critical issues that require solutions. Many possibilities exist for horizontal strategies that GE could implement between its Energy and Healthcare divisions (and the many business units under these two divisions). Actually, GE does implement the possibilities. Magee says “Perhaps only GE has the resources to do the full job, offering one-stop shopping in infrastructure because of its size and depth,” and he continues, “Immelt’s strategy is that GE will grow from within through internally generated means at two to three times the world gross domestic product” (p. 84). GE is a related diversified corporation that implements its horizontal strategy through the strong leadership and commitment of its CEO.

4.1.2 Horizontal Strategy at GE

Magee (2009) notes, “GE’s culture has long emanated from the strength of its beating heart, found at the company’s leadership training center in Crotonville, New York” (p. 56). The Welch Leadership Training Center (WLTC) is at the core of GE’s culture. It was founded in 1956 as an employee training facility, but in 1981, soon after Jack Welch became CEO, he positioned WLTC to be the central part of the firm, responsible for accelerating change from within and effectively supporting GE employees. Noel Tichy, who led the radical transformation of WLTC with Welch, says that Welch revitalized the curriculum, faculty, staff, and facilities at WLTC, while seeking to convey a message to thousands of managers (p. 100). Welch restructured WLTC as a place where employees from the business units could cultivate common values and objectives in one place. Teamwork at corporate level,
nurtured in WLTC, can be seen in the development of GE’s wind-power business. Magee cites this typical case of skill transfer in GE:

Lyons [chief engineer of GE Global Research] led the technologies effort, drawing upon GE engineering talent from around the world, regardless of discipline. In aviation, he found material experts familiar with lighter-weight products for turbine blades. In GE’s rail business, Lyons used experts who know how to make gearing systems operate at peak efficiency. In the United States and Germany he put industrial designers to work, while in places like Bangalore and Shanghai he found company researchers to build analytical models and conduct high-end simulations of wind turbines in use, revealing improvements needed and progress made” (p. 57).

Another example of skill transfer is GE’s imagery analysis technology, which was originally developed in the healthcare imaging division, and was then applied to scanning baggage for the security business. Since managers are familiar with managers in other GE divisions because of their mutual experience with WLTC, these kinds of skill transfers are executed routinely at GE.

WLTC became the world’s first internal business school, and has produced many world leaders for 50 years. GE invests about one billion dollars annually on training and education programs even during severe business downturns. Clearly, the WLTC and leaders trained there are competitive assets for GE.

In my view, the core concepts of GE’s horizontal strategy are ‘Human Resources’ and ‘Learning Culture’. We can easily understand the level of GE’s leaders by seeing the fact that Jim McNerney, Chairman, President and CEO of Boeing, comes from GE, the fact that Frank Blake, Chairman and CEO of Home Depot, comes from GE, the fact that Robert Nardelli,
former Chairman and CEO of Chrysler, comes from GE, and so on. *Fortune* ranks GE well up on its list of the world’s best companies when it comes to leaders. Leaders who could become CEO of large corporation are trained internally, and they collaborate routinely through their mutual experiences at WLTC. Immelt says, “Success in today’s dynamic world is based less on how much you know than how quickly you can learn” (Magee, p. 167). As Magee puts it:

> If change is the driving force pushing GE forward, then learning is the fuel that makes it go. Dating back to the company’s earliest days, learning has been a core theme and practice inside the organization. GE, for instance, promoted leaders from within as far back as the early 1900s on the premise that shared knowledge gained along the way made them far more valuable to the company than the hiring of someone without that advantage (p. 167).

Welch says “Learning, . . . It’s all about learning” (p. 168), and the expanded training program at WLTC has dramatically increased shared knowledge among employees.

### 4.1.3 GE’s Approach and Framework

From the viewpoint of Porter’s horizontal strategy, GE implements its skill transfer by leveraging its super-competitive human resources as a catalyst.

From the viewpoint of RBV, GE implements shared core competencies (i.e., human resources and learning culture) through experiences gained in the WLTC.

From the viewpoint of Hax’s horizontal strategy, leaders in GE are collaborating to identify the possibility of both tangible and intangible interrelationships.
The common point among all three frameworks is human resources. GE practices its horizontal strategy through the horizontal collaboration of exceptional leaders to cross over the barrier of divisions. The existence of WLTC is a symbol of its core competence, and GE's continuing investment in its employee training is bolstered by a commitment of top management to a sustainable horizontal strategy.

GE is continually evolving its core competencies. Immelt reformed the corporate R&D organization (Global Research Center) as a nerve center of the firm, similar to the WLTC. Noel Tichy said that Immelt aroused excitement and energy with the concept of R&D and results sharing (Magee, 2009, p. 108). This may sound obvious and straightforward, but it is actually quite difficult to implement at the corporate level, especially in a huge corporation like GE. Confrontations among business units, competition among leaders, differences of culture, and the Not-Invented-Here Syndrome (NIHS) are all barriers that can prevent skills from being transferred. As all managers in the world know these kinds of difficulties, people praise GE for its competencies and accomplishment.

4.2 VIRGIN GROUP

4.2.1 Overview

Virgin is a global diversified corporation based in the UK. Richard Branson, CEO of Virgin, started the company in 1968, and today it has expanded into music, theater, airlines, railway, finance, space travel, and so on, and it is still actively seeking new business categories (see Figure 4-2). The umbrella company, Virgin Group, is a holding company
consisting of more than 300 companies worldwide, employing approximately 50,000 people in 30 countries.

Virgin is often perceived as a conglomerate, a simple aggregation of unrelated firms. But Branson responds: “We offer our customers a Virgin experiences, and we make sure that this Virgin experience is a substantial and consistent one, across all sectors of our business” (2008, p. 43). Virgin adds specific value to its individual firm by controlling its core competence, i.e., the Virgin brand. Virgin generates synergy by implementing its unique horizontal strategy.

Source: Virgin website, 2011.

Figure 4-2 Virgin Companies
4.2.2 Virgin’s Horizontal Strategy

The core of Virgin’s horizontal strategy is its brand. Haru Miyazaki (2007), CEO of Haru Design Consulting, describes the Virgin brand as “perfectly differentiated.” Conversely, without the Virgin brand, a single business unit would no longer belong to Virgin Group.

The Virgin brand appeals to many people because of its youthful image. Customers see Virgin as brave young newcomer trying to wrestle against conventional giants to save customers from greedy exploitation. Likewise, the Virgin brand promises fun and respectful hospitality—ultimate products and services at reasonable prices, and a better-than-expected shopping experience for customers. Branson knows this, noting: “Over the years the Virgin brand has earned the reputation of being bold and unafraid. Isn’t it extraordinary how few brands communicate fearlessness?” (p. 187). Most customers understand what the Virgin brand brings to the table, so they are inclined to purchase the range of Virgin products and services. According to Branson, “Virgin’s success is primarily down to the consistent way it’s delivered on its brand proposition” (p. 126).

The CEO’s direct control team scrutinizes all groups and prioritizes issues to carry out promises made to customers. As Branson sees it: “They enjoy the advantages of doing business under the Virgin umbrella, and in return they agree to protect the integrity of the brand. If they don’t, then we can legally withdraw the name” (p. 86). Virgin knows that its brand is its best core competence, able to bring enormous success to the firm; it also knows that continuing to satisfy customers via its brand is the only way to develop the corporation further.
4.2.3 Virgin’s Approach and Framework

Virgin implements skill transfer as its horizontal strategy. ‘Skill’ in this regard is defined as the ‘Virgin Brand’ and ‘Promise to Customers’. However, Virgin knows that just adding its name to a company is not sufficient. There must be a specific situation in which the Virgin brand is well recognized, there must be special know-how to announce the launch of new business spectacularly, there must be unique method to allow managers’ autonomy while acquiring centripetal force at the same time, and so on.

From the perspective of Itami’s horizontal strategy, Virgin realizes a ‘synergistic effect’. Every business unit takes advantage of the Virgin brand and its ability to get things done.

From the perspective of Aaker’s horizontal strategy, Virgin is good at ‘identifying business regions where conventional resources are applicable’. In this regard, resources are the ‘Virgin brand’ and ‘Promise to Customers’.

Virgin is an atypical diversified corporation. Its business units are not related physically, they do not collaborate directly, but they are related conceptually and spiritually. Virgin is implementing its horizontal strategy through its brand. This comment from Branson expresses the essence of Virgin:

Publicity is absolutely critical. You have to get your brand out and about, particularly if you’re a consumer-oriented brand. You have to be willing to use yourself, as well as your advertising budget, to get your brand on the map. A good PR story is infinitely more effective than full-page ad, and a damn sight cheaper. I have an absolute rule. If CNN rings me up and wants to do an interview with me, I’ll drop everything to do it. Turning down the chance to tell the world about your brand seems just crazy to me. (p. 63)
Here, Virgin knows its competence and way of enhancing it.

4.3 PROCTER & GAMBLE

4.3.1 Overview

Procter & Gamble (P&G) is the largest consumer goods manufacturer in the world. It has three main businesses: Beauty and Grooming, Health and Well-Being, and Household Care. Its businesses run in more than 180 countries (see Figure 4-3).

![P&G Corporate Structure Diagram]

Source: P&G website, 2011. Adapted by author

Figure 4-3 P&G Corporate Structure

P&G is a profitable firm, with 20.3% operating income ratio (P&G, 2010, p. 76) which is astonishing for this industry. Innovation is the backbone of P&G’s management, and
consumers are positioned at the center of innovation. A. G. Lafley, former Chairman and CEO of P&G, states: “The overarching or guiding principle for game-changing innovation that delivers sustained organic growth and profits is placing the consumer or customer at the center of this framework. While many say they are “customer-centric,” few actually put the customer as boss in the center of the innovation process” (2008, p. 10). P&G conducts its strategy with a concentrated mind and has reaped successful results. In 2010, Fortune listed P&G as number six among the world’s most admired companies, praising its innovation and focus on the consumer.

4.3.2 P&G’s Horizontal Strategy

Figure 4-4 illustrates what P&G calls its ‘core strengths’. All strengths here would be competitive advantage of P&G, but in my view, ‘Innovation’ and ‘Consumer Understanding’ are outstanding than other strengths compared to any other firms in any industry, just as Fortune applauds. I will argue these two strengths in this section as the key factors of P&G’s horizontal strategy.
Innovation is P&G’s corporate-level skill, not a skill of one specific business unit. P&G defines innovation to include the business model, supply chain, concept, and cost reduction; it is not restricted to products, technologies, and services. Likewise, P&G puts the same priority on incremental innovation as on disruptive innovation. Lafley notes:

> Innovation is P&G’s lifeblood and is at the core of our business model. Every day, more P&Gers are involved in innovation. Consumers expect P&G brands to improve their lives with new innovations. Retail customers count on P&G innovation to grow their business and create value. P&G investors and shareowners look to innovation as an indicator of overall future financial performance (p. 7).

What is surprising is that P&G sees innovation as an integrated management process, not an incidental invention. P&G unites philosophy, objective, strategy, organization, system, leadership and culture to develop the process. During the innovation implementation process, they focus on building an innovation portfolio for sustainable growth. That is one
reason why P&G acquires Wella AG (a German cosmetic company), Gillett (a US personal care products company), and other firms. Lafley believes:

These acquired brands become platforms for future innovation and engines for future sustainable growth. They . . . strengthen some of P&G’s core strengths. Most important, these acquired brands and categories are beneficiaries of future business model, business process, and new-product innovation. (p. 75)

P&G intends to use these acquired firms to transfer its competence and to generate innovation, in addition to obtaining new products, technologies, and know-how. Moreover, P&G incorporates innovation into its daily operations. P&G sets broad definition for innovation to encourage employees to feel that innovation is accessible and realizable.

P&G has developed a repeatable and measurable method consisting of five elements for transforming ideas to results: Flow of Ideas, Selection and Green-lighting of Ideas, Nurturing, Go to Market, and Killing Ideas (Lafley, pp. 167-172). This process penetrates into the full range of entire P&G’s businesses to become the foundation that differentiates P&G’s products, services, and operations across all its business units.

‘Consumer Understanding’ is another P&G core competence. Their motto, “The consumer is boss”, is not only policy, it is a concrete and systematic strategy positioned at the center of innovation. Tsukuru Kasahara (2009) wrote, ”Lafley . . . succeeded in making [the slogan] “The Consumer is Boss’ penetrate throughout the entire corporation as an essential paradigm shift.” In order to please consumers when they buy a product and use it, P&G innovators try to see the world from the consumers’ viewpoint, and identify innovative possibilities. Lafley himself said: “In 2002, P&G created specific consumer immersion programs, Living. It enables employees to live with consumers for several days in their
homes, eat meals with the family, and go along on the shopping trips” (p. 48). Many firms say that customer focus is their philosophy, but not many actually implement that philosophy as radically as P&G, which spends over $10 billion annually on consumer research—almost double the industry average. P&G understands consumers not with their head, but with their heart. This is the reason why P&G can connect innovation with profit. Immelt says “Innovation without a customer is nonsense; it’s not even innovation” (Magee, p. 21). P&G’s two core strengths, ‘Innovation’ and ‘Consumer Understanding’, are tightly connected for generating new value to consumers.

‘Consumer Understanding’ is a key commonality among all the P&G business units. For instance, when P&G acquired Hugo Boss, a German fashion brand, in 1992, they transferred P&G’s ‘Consumer Understanding’ skill to Hugo Boss. Researchers lived with a group of men, accompanied them shopping in department stores, attended a fashion show with them, followed them in restaurants and nightclubs. By applying the knowledge gained to new product development, Hugo Boss succeeded in generating innovations, and has expanded its sales and profits far more than the industry average since 1992.

4.2.3 P&G’s Approach and Framework

From the perspective of Porter’s horizontal strategy, P&G implements skill transfer. They transfer their ‘Innovation’ and ‘Consumer Understanding’ skills as a process to new business they launch or acquire.
From the perspective of RBV, P&G implements shared core competencies. One characteristic is that the two competencies are always combined; ‘Innovation’ cannot stand without ‘Consumer Understanding’, and vice versa.

From the perspective of Hax’s horizontal strategy, P&G clearly identifies its intangible interrelationships and does an excellent job of configuring and coordinating the transfer of skills. Lafley found, “While each individual core strength is important and provides a source of competitive advantage in its own right, the real power and the biggest edge comes from combining P&G’s strengths in ways that deliver more consumer, customer, and shareholder value” (p. 100). He says elsewhere: “The effect has been not only to improve our performance in each unique core strength, but also to create real competitive advantage from their combination” (p. 14).

P&G is implementing its horizontal strategy around two core competencies, ‘Innovation’ and ‘Customer Understanding’, and generating consumer value and synergy.

4.4 KIRIN GROUP

4.4.1 Overview

Kirin Group is the largest food and beverage manufacturer in Asia. It has three main businesses: alcohol, soft drinks & foods, and pharmaceuticals, all functioning primarily in Asia and Oceania. Figure 4-5 shows Kirin sales by segment.
Kirin has had diversified businesses for 30 years. It has invested almost $10 billion to acquire shares of a Japanese pharmaceutical company, a Japanese wine company, an Australian beer company, an Australian dairy product company, a Filipino beer company, and a Singaporean soft drink company for several years. Kirin’s primary motive for expanding its business was to obtain sufficient scale to compete with global giants in the food and beverage industry, such as Anheuser-Busch Inbev, Heineken, Coca Cola, or Nestle.

Kirin has talked about the existence of synergies among its business units for years, but it basically left synergy generation to spontaneous collaborations between subsidiaries, except for the launch of its shared-service unit, which provides administrative services to some business units.

In 2009, Kirin announced a new business strategy, and launched a ‘Cross-Company Team’ (CCT) in Kirin Holdings Company. Developed as an organizational infrastructure to generate synergy, it was the beginning of Kirin’s full-scale horizontal strategy.
4.4.2 Kirin’s Horizontal Strategy

For years, Kirin did little about managing the integrated actions of its horizontal strategy. Management and headquarters expected voluntary collaboration among the business units to generate synergy; they encouraged the subsidiary leaders, but did not manage their actions. However, little synergy was actually created. It was not the fault of the business units. They put forth strong efforts to collaborate and in fact generated small synergies at the field level.

Rather, the fault lay with the headquarters corporate function. In this regard, Hax and Majluf (1996) note: “Horizontal strategies do not tend to emerge spontaneously” (p. 226), so synergy was not generated because there was no strong central control of the corporate function.

In 2009, Kirin launched eight CCTs: Sales & Marketing, Production & Distribution, R&D, Procurement, Business Integration, Asset Reduction & Cash Flow Management, Human Resource Infrastructure, and IT. The directors of Kirin Holdings directly manage the CCTs, and the CEO chairs monthly cross-CCT meetings. This is a strong commitment by management to lead the actions and generate synergy.

Kirin believes it can establish corporate-level competitive advantage by leveraging the CCT activities. A Kirin’s internal document states:

If we can establish solid process to generate synergy, it would be competence of building business portfolio and corporate management, because we can expand investment options through enlarging scope of investment premium. Otherwise, if we cannot generate synergy more than
investment premium, we would decrease corporate value (conglomerate discount). (Kirin internal document, 2008)

CCT is Kirin’s key to establishing a solid process for generating synergy and gaining competitive advantage.

Every CCT consists of members from corporate function and from related business units. Issues are discussed in CCT meetings and approved in cross-CCTs meetings. Some issues are hard to implement because not all business units gain equal benefit from the actions. It is possible that one business unit must accept a cost increase in order to achieve a cost reduction across the entire firm. In the past, this kind of difficult issue was neglected due to a lack of central control. However, now that CCTs are managed directly by the CEO and directors of Kirin Group, the difficult issues can be resolved, perhaps with the arrangement of performance evaluations. Today, I can say that Kirin has established a solid basis for a horizontal strategy.

Kirin classifies horizontal strategy into ‘Cost Synergy’ and ‘Sales Synergy’. Cost Synergy corresponds to Activity Sharing in Porter’s view, and Sales Synergy corresponds to Skill Transfer. The Kirin internal document states:

Profits from synergy can be divided into 2 concepts. First, sales synergy, which leverages comparative advantage by crossing complementary resources; second, cost synergy, which leverages economies of scale, the experience curve, and economies of scope by consolidating overlapping resources (Kirin internal document).

Kirin understands that cost synergy is much easier to implement than sales synergy, so it instructs all CCTs to focus on cost synergy first. Management knows that the CCTs need
small but real successes that demonstrate their ability to generate synergy and encourage employees.

Kirin set a goal of ¥20 billion (almost $235 million dollars) total cost reduction by 2012—almost 10% of operating income. As of 2011, the company is steadily producing good results, having already realized a ¥15 billion cost reduction at the end of 2010.

In addition to cost synergy, marketing and the R&D section also collaborate to develop innovative products by combining technologies. Among these are:

- ‘Hyoketsu’, a ready-to drink cocktail mix, developed by combining Kirin’s alcohol technology with its soft drink technology. Hyoketsu has experienced explosive sales, and is leading brand in the cocktail category.
- ‘Kirin Free’, the world’s first completely alcohol-free beverage with a beer taste, was developed by combining Kirin’s beer technology with its soft drink technology.
- Combining its beer and wine technologies enabled Kirin to launch ‘Tanrei Alpha’, a beer with wine overtones.
- Kirin combined Japanese tea flavoring technology with its Australian soft drink technology to produce a new tea-flavored beverage in Australia.

Because Kirin has various technologies for almost every beverage category, there are still many possibilities for developing innovative products by sharing technological skills and know-how.
Kirin’s product line includes various kinds of beverage, beer, wine, shochu (Japanese distilled spirits), sake, whisky, tea, coffee, juice, energy drink, carbonated drink, and milk. This is ‘Horizontal Breadth’ corresponds to the Delta Model. In the beverage category, Kirin provides one-stop shopping for customers. In addition, Kirin beer salespeople often visit restaurants to offer not only beer products, but also wine, whisky, shochu, and soft drinks. As it is convenient to procure various beverages from one single company from the viewpoint of restaurant owners, ‘Horizontal Breadth’ could be considered as synergy which brings value to customers and Kirin.

4.4.3 Kirin’s Approach and Framework

From the perspective of Porter’s horizontal strategy, Kirin implements both activity sharing and skill transfer. Its CCT strategy corresponds to activity sharing, and its technology mixing corresponds to skill transfer. Kirin distinguishes between sales synergy and cost synergy, and executes its horizontal strategy step by step, working from easier to more difficult.

From the perspective of Hax’s horizontal strategy, Kirin tries to identify and coordinate possible interrelationships on the basis of CCT activity. Each CCT is a flexible and agile organization that can be applied to planning and implementing under the strong leadership of top management.
From the perspective of Itami’s horizontal strategy, Kirin pursues both complementary effect and synergistic effect. As Kirin has already developed synergistic products like Hyoketsu and Kirin Free, there are many possibilities for synergies, as Itami claims.

Kirin has just begun developing and implementing its horizontal strategy, and results are not yet sufficiently defined. But the firm knows it must generate synergy through a systematic horizontal strategy in order to increase its corporate value. So it established the unique infrastructure, CCT. I believe the Kirin’s approach will evolve even more in the future.

4.5 Discussion of Each Firm’s Approach to Horizontal Strategy

I investigated four diversified corporations to understand their approach to horizontal strategy. In this section, I sum up each firm’s approach and clarify possibilities and challenges facing each one. Based on those discussions, I will suggest an approach for Kirin that will generate more sustainable synergy to enhance its corporate value.

4.5.1 GENERAL ELECTRIC

GE has implemented the most robust and sustainable horizontal strategy of the four firms in my case study. It leverages human resources as the force driving its horizontal strategy. Itami and Kagono (2003) explain: “A corporation is an aggregation of people. Corporate activity is shaped through organizing people and encouraging them to execute teamwork” (p. 238). They explain people’s decision-making process by stressing the significant influence of fundamental factors (see Figure 4-6).
What GE does is drill its employees in fundamental factors to help them make accurate decisions. This becomes the solid basis of GE’s horizontal strategy. Leaders and managers are strictly trained in the WLTC to acquire GE’s values and way of thinking. Magee (2009) states, “GE’s top 189 executives have been on average in the past decade to at least 12 months of leadership training at the Crotonville center” (p. 78). Highly trained and motivated leaders collaborate in various business regions. Collaboration is not a special event, but rather a routine. It would be almost impossible for other companies to imitate this capability over a short period of time because GE has already taken decades to develop this ability. Although its human resource training process could be imitated, it would be impossible for other firms to imitate the knowledge and skills accumulated over half a century, as GE has done. In this sense, human resources, the development process, and accumulated know-how are definitely GE’s sustainable competitive advantage.
The big challenge facing GE is personnel management. Welch (2005) emphasized the importance of a strict but anti-bureaucratic evaluation system (p. 120). Since human resources are one of GE’s core competences, the firm must maintain a fair personnel management system, otherwise, people would become discouraged and leave the company. From all appearances, GE has established a good system and put it into practice successfully. But maintaining and abiding by it is sometimes difficult. A CEO cannot monitor everything, so strong internal discipline and observation are essential.

4.5.2 VIRGIN

Virgin has implemented the most unique horizontal strategy of the four corporations. Its key shared resources are its powerful ‘Virgin Brand’ and its authentic ‘Promise to Customers’. Aaker (2001) notes: “[An] established brand name . . . makes developing awareness, trust, interest, and action all easier. Many firms have built large, diverse businesses around a strong brand” (p. 232). Aaker positions brand as one of the resources to be transferred. In this sense, Virgin seems to be walking the high road.

From the perspective of the Delta Model, however, Virgin is heavily focused on the strategic option of ‘Total Customer Solution’ in its horizontal collaboration. Virgin depends on its strong brand both in positive and negative ways. That is, if one business unit harms the Virgin brand in any way, it affects all business units immediately. Customers would feel betrayed by Virgin Group as a whole, not just by the single business unit at fault, and Virgin
would run the risk of losing business. If this happened, the Virgin empire would fall apart because there is nothing else that connects them horizontally.

Therefore, the challenge facing Virgin is to reduce the risk of impact that would occur if its brand were denigrated in some way. Branson (2008) says he is ready: “Virgin turns out to be ready for the storm as well. Because its risks are spread, the failure of one part – even a major part – will not ruin the whole” (p. 44). But the risk of brand defamation could not be dispersed, particularly in a strongly recognized brand like Virgin. One way to reduce the risk would be to find other ways to implement a horizontal strategy. For example, sharing assets or skills among the business units would strengthen interrelationships and tighten business associations that connect the Virgin brand. The point is to create a scheme that prevents business units from breaking apart even if the value of the Virgin brand decreases, even if only temporarily.

Another significant challenge facing Virgin is the crucial relationship between Richard Branson and the Virgin brand. Many customers identify the Virgin brand specifically in terms of Branson himself. Miyazaki (2007) notes, “Richard Branson is the brand icon of Virgin Group. In addition to his showmanship, he understands the motives of customers at a deep level and acts as the primary spokesperson for the Group”. The Virgin brand (and its innate promise) is the company’s sole core competence, but it cannot be allowed to disappear with the retirement of Branson. Decoupling Branson from the Virgin brand and setting the brand on its feet is an urgent need for Virgin’s sustainable horizontal strategy.
4.5.3 P&G

P&G implements the most well-balanced horizontal strategy of the four corporations. From the perspective of Hax’s Delta Model, P&G pursues a strategy of System Lock-in by innovating virtually all aspects of its business processes; it implements Total Customer Solutions by positioning its consumers as the core of the strategy; and it executes the Best Product option by enhancing its innovation capability to differentiate its products.

As discussed in section 4.3, P&G developed a systematic innovation process and incorporates it into daily operation. The consumer is positioned at the center of this innovation process. As Lafley (2008) puts it: “We’re spending far more time in context with consumers – living with them in their homes, shopping with them in stores, and being part of their lives” (pp. 13-14). Thus, P&G literally sees its all operations from the consumers’ standpoint. By leveraging its core competencies, ‘Innovation’ and ‘Consumer Understanding’, the company differentiates its products, continually reinvents and improves its consumers’ experience.

P&G proudly points to ‘Brand Building’ as one of its core strengths. This skill is built by consumer research and a strong ability to develop innovations. There is a strong reinforcing loop among ‘Consumer Understanding’, ‘Innovation’ and ‘Brand Building’, as shown in Figure 4-7. P&G is known for its powerful marketing capability. The mechanism for generating marketing capability is supported in this reinforcing loop. This is why P&G is perceived to be a ‘Reservoir of Talent’. Talented people are developed through its repeated implementation of core competencies, which are shared by all P&G business units.
The challenge facing P&G is to train and retain a certain number of innovation leaders. Lafley observes: “Leaders of innovation are made, not born”, and “If a company wants to place innovation at the center of its business, developing innovation leaders is not optional” (p. 276). P&G knows that strong leadership is essential for maintaining its innovative culture. If the firm established a systematic process for developing innovation leaders and encouraged them to collaborate in daily operation, I believe it would obtain sustainable competitive advantage through its horizontal strategy. Maintaining the positive reinforcing loop shown in Figure 4-7 is also important. It could easily turn negative if one element goes wrong. Maintaining its ‘Innovation’ and ‘Consumer Understanding’ skills and preserving the positive reinforcing loop will be the significant role of innovation leaders.
4.5.4 Kirin

Kirin faithfully implements its theory of horizontal strategy, and organized CCTs as the foundation of that strategy. CCTs pursue cost synergy first and try to share the activity. The Marketing and R&D sections pursue a sales synergy and collaborate by transferring skills. Since Kirin’s business units are strongly related, there is huge potential for generating various kinds of synergy. Kazuyasu Kato, Chairman of Kirin Holdings, often says, “If we do not collaborate, we will not remain a corporation” (Kirin Internal document). Kirin’s 2010-2012 mid-term business plan illustrates this position clearly (see Figure 4-8).

Source: Kirin 2009 Annual Report

Figure 4-8 Kirin’s 2010-2012 Mid-term Business Policy
As I mentioned in section 4.4, Kirin invested almost $10 billion to acquire several businesses for some years past. This period was positioned as a quantitative expansion stage, which means the firm sought to acquire enough scale and diversity to compete with its global rivals. But quantitative expansion is not sufficient to gain competitive advantage. Rather, the firm understands that it must create additional value by leveraging the resources that have been acquired.

Kirin has positioned fiscal years 2010-2012 as a qualitative expansion stage, which means generating synergy by implementing a horizontal strategy. Seiji Miyake, CEO of Kirin Holdings, says, “My personal belief is that reform cannot happen until people are aware of sectionalism and move to break such barriers” (Kirin 2009 Annual Report, p. 5). Kirin is committed to this position and will pursue synergies.

Because Kirin has just begun implementing its horizontal strategy, it has focused on the Best Product strategic option as defined in Hax’s Delta Model. Then, what kind of progress can Kirin make in the future? I can get clues from horizontal strategy of other three corporations; human resources, brand, and customer-focused innovation. First, Kirin should enhance its human resource development. Surely, Kirin is trying to do it, and is expanding employee training at corporate level in recent years. However, trained people are still dominated by its main business unit, Kirin Brewery, and majority of employees who work in Kirin’s headquarter, Kirin Holdings, would come from Kirin Brewery. In order to pursue horizontal strategy, Kirin should open a gate of development for all business units. Similar to GE’s WLTC, Kirin’s training should be where people can experience collaboration through
live course materials. The amount of training should also be increased. In GE’s case, its top executives receive more than 12 months of training over 10 years. The average Kirin executive receives much less than half of that amount.

Kirin’s biggest challenge with regard to human resource is diversity, specifically people from other countries. The great majority of Kirin’s employees in its domestic business units are Japanese. Therefore, people in the Australian business units, which earn more than 20% of sales, should be much more involved to Kirin Holdings and in its major business units in Japan and other Asian countries. To achieve a sustainable horizontal strategy supported by continual collaboration among highly skilled managers (as happens in GE), Kirin should put more priority on human resource development and diversified alignment, and incorporate development and alignment process into its horizontal strategy.

Second, Kirin should rethink its brand strategy. The company website states that “Kirin aims to raise the brand value of “KIRIN” as a brand of trust, a brand at the front line of innovation . . . . Management believes that the KIRIN brand can act as a unifying force for the Group” (Kirin Group Vision 2015). In fact, Kirin is a strong brand in Japan, and an especially trusted symbol. However, the Kirin brand is not yet well-recognized in overseas markets. Kirin has to decide whether to enhance the Kirin brand globally or to leave that path to concentrate on establishing its individual brands locally, region by region. If Kirin selects a global brand strategy, it should consider a horizontal strategy that leverages shared recognition within the Kirin brand, just like Virgin. It would allow Kirin to launch new
businesses, or expand business into new areas where it will be more easily accepted by new customers.

Kirin’s biggest challenge with regard to brand is penetration to local customers. Although there is no “magic wand” for accomplishing that, one strategy is a “brand community”, which Harley-Davidson has adopted. Brand community is organized by enthusiastic users who sympathize with and adopt the lifestyle, action, and values that are connected to a specific brand. Susan Fourniew (2010) says, “Brand community is not a part of marketing strategy, but it should be a part of corporate strategy”. In addition, Roland Rust, Valarie Zeithaml, and Katherine Leomon found that “many firms lose their customer-focused policy by too much weight on brand. It is important to consider centering brand around customers and not to lose trusted customers”. Based on these points of view, Kirin should set brand strategy at the center of its Total Customer Solution strategic option described in the Delta Model.

Third, Kirin should enhance its innovation skill with its customer-relationship skill, following the example of Procter & Gamble. Kirin’s twin strengths that need to be developed are ‘Technology Expertise’ and ‘Customer Relationship Excellence’ (Kirin website). It could also be read as “Kirin will strengthen customer relationship to make technological innovation,” which corresponds well to this issue. Kirin’s corporate conduct code, The Kirin Way, discusses a “customer-focused approach” and “Innovation,” which directly correspond to this issue. Kirin has been seeking capabilities like those I have identified at P&G, and Kirin is realizing appreciable new skills. I believe the P&G approach, particularly its effort to
assimilate with consumers, is an excellent example that should be included in Kirin’s future evolution.

The biggest challenge with regard to innovation and customer relationship is horizontal development. These are skills that major business unit should enhance and transfer horizontally, and these correspond to the ‘Skill Transfer’ in Porter’s horizontal strategy, and to ‘Sales Synergy’ in Kirin’s definition. As mentioned in section 4.4, Kirin’s CCTs now focus on ‘Cost Synergy’. But in the future, they will have to tackle ‘Sales Synergy’ in order to pursue further possibilities. The firm understands there would be no spontaneous skill transfer, and that there should be strong control by the corporate function to create synergy. Therefore, establishing a solid system for generating and transferring skills is critical for Kirin.

In conclusion, I believe Kirin has enormous potential for creating a process of human resource development, enhancing its brand, and developing customer-centered innovations. I would add ‘Creating a Process’ to my suggestion because it is critical for gaining sustainable competitive advantage. By developing and implementing these options, I believe Kirin can achieve a balanced and sustainable horizontal strategy for the future.
In order to create and implement a horizontal strategy, there should be a systematic process in place, otherwise, synergy will not be generated. Porter puts it this way:

Without an explicit horizontal strategy, there will be no systematic mechanism to identify, reinforce, and extend interrelationships. Business units acting independently simply do not have the same incentives to propose and advocate strategies based on interrelationship as do higher level managers with a broader perspective. (1996, p. 368)

In this chapter, I will propose a comprehensive approach for diversified corporation to create and execute horizontal strategy from the viewpoint of process, evaluation system, and leadership.

5.1 Steps for Creating and Implementing Horizontal Strategy

First, the process should be practical. This sounds obvious, but the reality is that many conceptual processes in a firm are just meaningless rules that are never implemented. Second, created horizontal strategy should be concrete. It should be shared in the firm and should be understood by employees as a guide for what they have to do next. Third, the results should be monitored and evaluated by top management. The content of the strategy should be adjusted depending on the firm’s situation. The external and internal environments change quickly, and firms do not know whether their strategy will be appropriate in a few months. A proper feedback system is critical in the process. Finally, and
most importantly, the strategy should be implemented properly. Larry Bossidy, Ram Charan, and Charles Burck (2009) declare, “Execution is the great unaddressed issue in the business world today. Its absence is the single biggest obstacle to success and the cause of most of the disappointments that are mistakenly attributed to other causes” (p. 5). A well-designed organization and strong leadership are absolute requirements for carrying out the horizontal strategy.

From these perspectives, I propose a seven-step process to create and implement a horizontal strategy for a diversified corporation. Figure 5-1 illustrates this process. I explain each step in this chapter.

Source: developed by author.

Figure 5-1 The 7-Step Process for Creating a Horizontal Strategy
5.1.1 Step 1: Current Reality

The first step is to understand the current state of the firm’s horizontal strategy. The key question to be asked in this step is, “What horizontal collaboration are we implementing now?” Some diversified corporations will not have implemented any horizontal collaboration; some will be executing some sort of horizontal collaboration and attempting to evolve it to a higher level. Regardless, understanding where the firm stands currently is important for creating a practical horizontal strategy. If the firm perceives its current situation wrongly, the strategy that is created will be faulty and unworkable.

Reviewing past actions and observing results are two main tasks in this step. Besides planned horizontal strategy, sometimes there is specific horizontal collaboration at the field level. Determining what types of horizontal collaboration are going on and how they are working is the first step to be taken by the corporate function. In addition, knowing the firm’s rivals or the target corporation’s horizontal strategy is also important. The ancient Chinese philosopher Sun Tzu said: “If you know the enemy and know yourself, you need not fear the result of a hundred battles.” I believe that a clear understanding of the current situation is critical for any strategy.

5.1.2 Step 2: Possible Interrelationships

The second step is detecting possible interrelationships among business units. The firm should examine every potential interrelationship that it could pursue. Porter (1985) confirms this when he says: “Examine value chains of each business unit for actual and
possible opportunities for sharing. . . . After identifying tangible interrelationships, the next step is to seek out intangible interrelationships. This involves the isolation of value activities in which a firm has valuable know-how that might be useable in other business units” (pp. 368-371). Listing all possibilities is important, but avoiding an overestimate is equally important. Aaker (2001) talks about the fact that “synergy is too often simply assumed when in fact it . . . is vastly overextended” (p. 237), calling it “the mirage of synergy.” If the management overestimates synergy and suggests an excessive number of interrelationships, then pursuing a horizontal strategy often just results in a cost increase.

There are two ways to prevent failures caused by overestimation. First is to be conservative when estimating possible interrelationships. Second is to implement the strategy while monitoring it carefully, and immediately stop or change course when it becomes apparent that has taken a wrong turn. This second way corresponds to ‘Emergent Strategy’, which I will discuss further in Step7.

In order to detect possible interrelationships, I suggest using the chart proposed by Hax and Majluf (see Figure 5-2). This chart detects the pairs of business units that have appropriate interrelationships, and is suitable to examine mutual exclusivity and complete exhaustiveness.
### Wholesale Distribution

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<th>Raw Material</th>
<th>Tissue &amp; Papers</th>
<th>Disposable Diapers</th>
<th>Coffees</th>
<th>Cake Mixes</th>
<th>Shortening</th>
<th>Chips/Peanuts</th>
<th>Drinks</th>
<th>Cosmetics</th>
<th>Oral Care</th>
<th>Soap-Shampoos</th>
<th>Detergent</th>
<th>Chemicals</th>
<th>OTC Drugs</th>
<th>Prescription Drugs</th>
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<tr>
<td>Cellulose</td>
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**Key:** * denotes sharing of wholesale distribution activities across business units. A,B,C,D identify clusters of sharing of activities across business units.

### Raw-Materials Procurement

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### Research and Development

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<th>Coffees</th>
<th>Cake Mixes</th>
<th>Shortening</th>
<th>Chips/Peanuts</th>
<th>Drinks</th>
<th>Cosmetics</th>
<th>Oral Care</th>
<th>Soap-Shampoos</th>
<th>Detergent</th>
<th>Chemicals</th>
<th>OTC Drugs</th>
<th>Prescription Drugs</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cellulose</td>
<td>A Tissue</td>
<td>A Diapers</td>
<td>Coffee</td>
<td>Cake</td>
<td>Shortening</td>
<td>Chips</td>
<td>Drinks</td>
<td>Cosmetics</td>
<td>Oral</td>
<td>Soap</td>
<td>Detergent</td>
<td>Chemicals</td>
<td>OTC</td>
<td></td>
</tr>
</tbody>
</table>

Source: Hax and Majluf, 1996, pp. 234-235

**Figure 5-2 Tangible Horizontal Interrelationships Among Business Units – P&G**
5.1.3 Step 3: Prioritization

The third step is considering how to prioritize several interrelationships in order to implement the strategy. Management is generally inclined to set too many goals that they want to pursue simultaneously—all of which they believe their employees can do. But as Heike Bruch and Jochen Menges (2010) indicate, it is difficult for employees to implement many horizontal strategic actions at one time:

If management requires employees to work in accelerated pace everyday for months, it would deplete employees’ energy and worsen the business performance... Doing business with an oppressive pace not only deprives employees of motivation, but also disperses the focus of corporate activities. (p. 76)

Because management and corporate function generally have available capacity, they tend to set too many goals, with multiple horizontal strategic actions. Often the pace is too accelerated pace for business units. Management has to prioritize possible interrelationships and indicate the appropriate amount of action that should be implemented.

The only task in the third step is to select several actions to realize the interrelationships identified in the second step. In other words, management should postpone other possible interrelationships. That may sound irrational, but if we understand that implementing a horizontal strategy and generating synergy are extremely difficult issues for the firm, we can see that pursuing all possible interrelationships simultaneously would be overloading and far too resource-consuming. Management must instead focus on meaningful
interrelationships. If they achieve them, then they will be ready to realize new interrelationships.

One question to be asked is this: How should the firm prioritize interrelationships? I suggest that they choose easier and faster ones to implement, not more profitable ones, because success examples are required to encourage employees. The faster the firm succeeds in generating synergy, the more employees become motivated. Small but fast results will be superior to larger, slower results.

5.1.4 Step 4: Mission

The fourth step is to state the mission of the horizontal strategy, that is, deciding concrete actions and communicating them to employees. For example, Kirin launched eight CCTs—Sales & Marketing, Production & Distribution, R&D, Procurement, Business Integration, Asset Reduction & Cash Flow Management, Human Resource Infrastructure, and IT for cost synergy by activity sharing. These eight actions demonstrate Kirin’s intention to pursue cost synergy. Decisions about the kinds of actions to include depend on effectiveness and ease. In order to achieve success quickly, choosing straightforward actions first is the better approach. There are two important points: first, examine both customer (demand side) and firm’s business competencies (supply side); and second, clarify the specific kind of transformation the firm needs. Hax (2010) points out, “What we want to generate at this [creating mission] stage of the planning process is a redefinition of our business strategy, an objective assessment of where we are and where we want to go” (p.
93). Deciding horizontal strategic actions in terms of these perspectives is extremely fruitful for the firm.

Management should express in simple terms what the firm intends to do, and then share it repeatedly with employees. P&G’s former CEO, A. G. Lafley (2008), often communicated with his employees this way: “Our business is pretty simple . . . . The consumer is our boss, and we have to win with her at two moments of truth, day in and day out . . . . And we have to win both moments of truth millions of times a day in more than 180 countries worldwide” (p. 34). Kirin made the decision to focus on reducing costs and generating cost synergy from 2010 to 2012, and shared this decision with employees and shareholders. The key issue is helping all employees understand what the firm is willing to do with its horizontal strategy. The explanation should be simple. Business strategy is often described using management terms or obscure words. It is completely non-sense. The content of the strategy needs to be understood by all employees. Particularly horizontal strategy should be understood by employees with different cultural values within wide range of business units. Abstract expressions or complicated wordings can cause misunderstandings. Michael Jacobides (2010) states:

Top management has to write an acting script ... indicates how the firm can increase corporate value by business units strengthening each other ... and by corporate function controlling these relationships ... management of headquarter can clearly announce the way how the firm generates additional value.

In this regard, management should be expert at educating and encouraging employees, otherwise the firm will not achieve maximum strength through employee motivation.
A brilliant tool for expressing horizontal strategy is Kaplan and Norton’s Balanced Scorecard. The authors describe their four-perspective framework this way:

The four-perspective framework for business unit strategies turns out to extend naturally for developing an enterprise Balanced Scorecard... The corporate headquarters aligns the value-creating activities of its business units – enabling them to create more benefits to their customers or to lower total operating costs – beyond what they could achieve by themselves if they were operating independently. (2006, p. 7)

Figure 5-3 shows the four perspectives for an enterprise scorecard.

<table>
<thead>
<tr>
<th>The Enterprise Scorecard</th>
<th>Sources of Enterprise Derived Value (Strategic Themes)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial Synergies</td>
<td>• Internal capital management: Create synergy through effective management of internal capital and labor markets</td>
</tr>
<tr>
<td></td>
<td>• Corporate brand: Integrate a diverse set of businesses around a single brand, promoting common values or themes</td>
</tr>
<tr>
<td>Customer Synergies</td>
<td>• Cross-selling: Create value by cross-selling a broad range of products and services from several business units</td>
</tr>
<tr>
<td></td>
<td>• Common value proposition: Create a consistent buying experience, conforming to corporate standards at multiple outlets</td>
</tr>
<tr>
<td>Internal Process Synergies</td>
<td>• Shared services: Create economies of scale by sharing the systems, facilities, and personnel in critical support processes</td>
</tr>
<tr>
<td></td>
<td>• Value-chain integration: Create value by integrating contiguous processes in the industry value chain</td>
</tr>
<tr>
<td>Learning and Growth Synergies</td>
<td>• Intangible assets: Share competency in the development of human, information, and organization capital</td>
</tr>
</tbody>
</table>

Source: Kaplan & Norton 2006, p. 11

**Figure 5-3 The Four Perspectives of an Enterprise Scorecard**

Taking Kaplan and Norton’s definition, if the firm selects human resource development as a driving force of horizontal strategy (like GE), then the ‘Learning and Growth’ perspective will be fulfilling. If the firm selects a customer-centered approach as its main
horizontal strategy (like P&G), then the ‘Customer’ perspective will be fulfilling. And if the firm chooses cost reduction as a major activity (like Kirin), then the ‘Internal Process’ perspective will be fulfilling. It is useful for management to plot the possible horizontal strategic interrelationships presented in Step 2 against each perspective, and show the priority of interrelationships as determined in Step 3 as a part of entire structure.

Unfortunately, however, management often uses balanced scorecard only from the product or service viewpoints. In other words, management tends to focus on a Best Product strategic option in the Delta Model when they try to express the business strategy using a balanced scorecard.

Hax proposes another framework to create a well-balanced strategy. As Figure 5-4 illustrates, he introduces three major business processes: ‘Operational Effectiveness’, ‘Customer Targeting’, and ‘Innovation’, and proposes a matrix of three strategic options and three business processes. This definitely helps management to create and express strategy from balanced viewpoints. It is also a highly useful tool for communication between management and employees to share the horizontal strategy.
STRATEGIC POSITIONING

<table>
<thead>
<tr>
<th>ADAPTIVE PROCESS</th>
<th>Best Product</th>
<th>Total Customer Solutions</th>
<th>System Lock-In</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operational Effectiveness</td>
<td>Best Product Cost</td>
<td>Best Customer Benefits</td>
<td>Best System Performance</td>
</tr>
<tr>
<td>Customer Targeting</td>
<td>Target Distribution Channels</td>
<td>Target Customer Bundles</td>
<td>Target System Architecture</td>
</tr>
<tr>
<td>Innovation</td>
<td>Product Innovation</td>
<td>Customer Service Innovation</td>
<td>System Innovation</td>
</tr>
</tbody>
</table>

Source: Hax, 2010, p. 131. Adapted by author

Figure 5-4 Three Processes to Support Three Strategic Options

5.1.5 Step 5: Goal and Indicators

Summarizing the points so far, the management determines the interrelationships to pursue and expresses the actions to be implemented.

The fifth step is setting a goal for each action and defining performance indicators. As Kaplan and Norton (2006) say “You can’t manage what you don’t measure” (p. 250), management has to set quantitative goal and measurable indicators. Besides financial performance, management can adopt indicators such as capital market indices, cost of capital, asset growth/reduction, risk-related metrics, or operational parameters such as inventory turnover, time for delivery, rejection rate, or average price per customer.
Here, I define ‘goal’ as the final objective to be achieved by the actions, and ‘indicator’ as the checkpoint of each milestone of the action. For example, Kirin’s IT CCT sets its goal to reduce 20% of IT costs by 2012 compared to 2009. It defined several indicators to check whether the actions are on target. One indicator is the amount of cost reduction achieved by 2010. Others are the amount of asset reduction, the amount of reduction in overtime work by IT personnel, progress with IT software consolidation, and so on.

Setting goal and indicators seems quite similar to general business unit strategy. However, horizontal strategy requires alignment of business unit strategies among all the business units involved. Goal and indicators for each action are decided at the corporate level, but they have to be broken down to actions in each business unit. This sometimes brings about conflict because horizontal strategic actions often run counter to the business unit strategy, which typically works toward maximizing its profit. Porter (1985) describes it this way:

Interrelationships are often resisted by some business units because the benefits are or appear to be asymmetric ... differences in the size and strategy of business units often mean that the competitive advantage arising from an interrelationship accrues more to one business unit than another. In some cases, an interrelationship can have a net negative impact on one business unit while being clearly beneficial to the firm as a whole. (p. 386).

Therefore, there should be a proper evaluation system that motivates business units that may be affected. I will discuss this further in section 5.2.
5.1.6 Step 6: Organizations

From Step 1 to Step 5, the firm creates its horizontal strategy including what to do, how to do it, and what to achieve.

The sixth step is to configure the organization so as to carry out the horizontal strategy smoothly. The importance of organization in the strategy is widely discussed in the literature. Barney includes existence of a proper organization as one essential factor of sustainable competitive advantage (as discussed in Section 3.2). Hax and Majluf believe that configuration of value chain and coordination of value activities are critical for horizontal strategy (as discussed in Section 3.3). Aaker states that ascertaining organizational integration is the final step of a horizontal strategy (as discussed in Section 3.4).

There are two kinds of decisions to be made regarding organizational issues. The first is organizing a “control tower” for the horizontal strategy. The second is designing the structure of the business units, whether integrated or decentralized. Both decisions are crucial, but completely different.

For the first decision, management should launch a specific department or project team in corporate function, dedicated to the horizontal strategy. I call this organization the Head Office (HO) of horizontal strategy. HO is the driving force behind horizontal strategy and is responsible for managing the entire process. The owner of HO should be the CEO, and the leader of HO should be one of the corporate operating officers (or someone else at a similar level), because solid authority is needed in order to work as the control tower for the whole corporation.
Within the HO there should be task forces responsible for each action in the horizontal strategy. The owner of each task force should be a corporate director, and the leader should be the manager who is in charge of the relevant action. In each task force, members should be selected from every business unit involved in the action. Kirin’s CCT organization is a good example of this framework (see Figure 5-5). HO is placed in the Corporate Planning Department of Kirin Holdings. The owner of HO is the CEO, and the leader of HO is the managing officer responsible for corporate management. There are eight CCTs under the HO. The owner of each CCT is director in Kirin Holdings. All CCT owners have regular meetings to monitor the progress of every action. The CEO chairs the meeting and coordinates inter-CCT issues if needed. Every CCT consists of multiple business unit members. They are expected to consider and implement issues from a firm-wide viewpoint, and to become a bridge between corporate and the business units.
Source: Internal document, adapted by author.

Figure 5-5 HO and CCTs in Kirin
Second, the firm should implement daily business operations with collaboration from all the business units. There are four types of structures, as shown in Figure 5-6.

Source: developed by author.

**Figure 5-6 Possible Structures of Horizontal Operations**
Type 1 is collaboration among independent sections of business units. Every business unit has its own section, and the sections collaborate to share activities or skills. This option is the most moderate type of collaboration, and is easy to reinstate if it goes wrong. But it also has a risk of conflict and sectionalism, which can arise whenever there is collaboration among different organizations. It may require careful adjustment to maintain effective collaboration.

Type 2 is a centering operation to one business unit. The business unit whose operation is superior to the other business units will take all operations and collect service fees. This option benefits the comparative advantage proposed by David Ricardo. That is, every business unit specializes in its relatively skilled operation and imports other operations from other business units, which is the most effective and efficient operation from an economic viewpoint. But there is a risk that the business unit will prioritize its own operation and neglects the operations of others. Some kind of service agreement between the business units, and a method for enforcing compliance would be required.

Type 3 is a establishing shared-service unit dedicated to a specific operation and collecting service fee from the business units. This option is common in standardized operations such as accounting, payroll, or IT maintenance. Skilled experts can provide equal service to every business unit, and the quality of service would be expected to improve. However, the risk is that the power of the business units exceeds that of shared-service unit, which becomes inefficient or redundant. Business units are inclined to require excessively high levels of service, and a shared-service unit tends to do this as well. So a shared-service
unit could increase overall costs and perhaps deny some benefits of synergy. There should be some type of supervisory system to prevent self-ballooning in a shared-service unit.

In order to avoid the disadvantages of Types 1, 2, and 3, Type 4 is a powerful structure that requires managers and business unit employees to work in a matrix organization. They work for the business unit as well as for the horizontal function. In the corporate function, there should exist managers who work as controller of the horizontal collaboration. By creating this structure, the firm has a specific entity for resolving conflicts among business units, can prevent sectionalism, pursue total optimization, and avoid self-ballooning. Hax and Majluf (1996) suggest “to assure successful implementation, we need to create horizontal mechanisms that cut across the existing organizational units of the firm” (p. 239).

While the Type 4 structure seems to be the ideal form for implementing horizontal strategy, one concern is that it is not easy to make the organization work effectively. Because managers and employees in the business unit have two separate report lines, they might become confused unless there is clear consensus between corporate and each business unit, and a strong and independent mindset in every employee. Some companies with highly hierarchical and/or bureaucratic systems will have to revamp their corporate culture in order to implement a Type 4 structure. But if the firm achieves this organizational structure, it would be a big advantage for executing a horizontal strategy and generating synergy.
5.1.7 Step 7: Monitoring and Fine Adjustment

The final step is monitoring and adjustment. While Steps 1 through 6 are tasks for planning, Step 7 is how to manage execution. Authors in the relevant literature warn about the pitfalls of execution. Roger Martin (2010) says, “Making a distinction between strategy and execution can do great damage to a corporation,” and he warns about the risk of decoupling execution from strategy. Mintzberg et al. writes:

When a strategy failed, the thinkers blamed the doers. ‘If only you dumbbells appreciated our beautiful strategy . . .’ But if the dumbbells were smart, they would have replied: ‘If you are so smart, why didn’t you formulate a strategy that we dumbbells were capable of implementing?’ In other words, every failure of implementation is also, by definition, a failure of formulation. But the real problem may lie beyond that: in the very separation between formulation and implementation, the disassociation of thinking from acting. (p. 189)

Clearly, excellent strategy does not exist without execution. And strategies without execution are not good strategies, they are just failures. In this regard, I have included this step as a part of the process of creating horizontal strategy.

First, the progress of the execution should be monitored regularly, at least once a month. The actions of horizontal strategy easily lag because task force members are busy doing their own tasks in their business units. Since horizontal strategy generally requires tough coordination within the organization, it tends to be left undone without a proper monitoring system. As a practical measure, the HO should provide monitoring sheets and require all task forces to submit one at regular intervals. HO also should organize regular meetings to check progress and discuss issues. Strict monitoring and encouragement of the owners (directors) of task forces are the critical role of the HO owner (CEO). Commitment to
shareholders is a good way to ensure execution. If the CEO has to announce the results and progress of the horizontal strategy to shareholders regularly, it would create effective pressure on the entire firm.

Fine-tuning the horizontal strategy is another key task in Step 7. The critical point of this task is a rotating execution-monitoring-feedback-adjustment cycle. Here, I would incorporate the idea of ‘emergent strategy’ into the horizontal strategy process. Mintzberg et al. write about this:

Deliberate strategy focuses on control – making sure that managerial intentions are realized in action – while emergent strategy emphasizes learning – coming to understand through the taking of actions what those intentions should be in the first place ... The concept of emergent strategy, however, opens the door to strategic learning, because it acknowledges the organization’s capacity to experiment. A single action can be taken, feedback can be received, and the process can continue until the organization converges on the pattern that becomes its strategy. (p. 199)

Deliberate strategy and emergent strategy are often regarded as mutually exclusive. However, I believe management should use both to create a better overall strategy. Today’s world is filled with uncertainty, and a predetermined strategy may not be enough to weather a harsh storm. Management has to execute planned activities, monitor results, provide feedback, and adjust the strategy if needed. This is the core concept of emergent strategy. The firm should learn from execution and refocus the strategy regularly, like a guided missile recalculates its course to reach the target. Feedback and strategy adjustment could be the biggest tools for risk management.

On the other hand, there should be a deliberate strategy for pushing forward the organization. In particular, horizontal strategy needs strong centripetal force to coordinate many people and cultures. Without a specific strategy, no one will know what to do or how
to do it. Therefore, management has to combine both deliberate and emergent strategies in order to implement a horizontal strategy, and to do that, an execution-monitoring-feedback-adjustment cycle is essential. As Welch (2005) states, “I know that strategy is a living, breathing, totally dynamic game ... most managers I know see strategy as I do – an approximate course of action that you frequently revisit and redefine, according to shifting market conditions. It is an iterative process” (pp. 165-166), continuous fine adjustment of the horizontal strategy is crucial.

5.2 Evaluation System

One of the most difficult challenges of a horizontal strategy is the lack of an appropriate and fair system for evaluating people. Managers and employees in business units that are involved in the horizontal strategy always encounter a conflict between the performance of the business unit and that of the corporation. If the two worked together, it would be best, but unfortunately that does not always happen.

In order to work more for corporate performance, there should be a specific evaluation system. Bossidy and Charan (2009) state: “Reward the doers; this is a critical part of achieving success that we stressed in Execution” (p. xxviii). In this section, I will discuss how to provide a proper evaluation system and motivate people in the horizontal strategy.
5.2.1 Conflicts between Corporate Performance and Business Unit Performance

If there were no conflicts between corporate performance and business unit performance when implementing a horizontal strategy, things would be much easier. The corporate function would just have to provide a good environment for managers and employees in the business units to work harder. But, in fact there are numerous conflicts between corporate performance and business unit performance.

A typical example is skill transfer between two business units. In general, a transfer of skills is beneficial for the receiving company but does not bring any advantage for the transferring company. The transferring company often has to send skilled managers to the receiving company in order to export capabilities and educate people, which sometimes creates problems for the transferring company.

Another example is consolidating production facilities. When Company A takes over all the production done by Company B, and Company B stops its production, total production cost is expected to decrease due to an increase of utilization ratio and economy of scale. However, Company B has to tolerate the pain of shutting down the factory, dismissing employees, losing control of production, and losing accumulated production know-how. Even if Company B achieves some cost reduction, the cost for pain exceeds the gains at least for a few years. The managers of Company B have to endure some conflict over the total cost reduction (corporate performance increase) and cost increase of their business unit (business unit performance decreases). Porter (1985) calls this conflict ‘Asymmetric Benefits’ and says:
Many of . . . the organizational impediments to achieving interrelationships are based on the perceived conflict between interrelationships and equity . . . interrelationships can conflict with equity in the minds of some managers. Interrelationships can yield differing benefits to the business units involved. Interrelationships also imply that managers should have different degrees of autonomy, differing objectives, and differing bases for incentives (p. 392).

Management cannot escape these kinds of conflicts between business units when trying to implement a horizontal strategy. Management should face the conflicts and should not fear them. This is why Hax and Majluf (1996) say “it [horizontal strategy] will not materialize unless there exists a determined will to make it happen” (p. 226).

5.2.2 An Evaluation System in Horizontal Strategy

Corporate incentive plans often exacerbate the difficulties of implementing interrelationships by indirectly penalizing managers for pursuing them. Business units often lack any positive incentive to participate in interrelationships. They see little gain in changing the way they perform activities to facilitate sharing or transferring know-how, both essential to a successful interrelationship” (Porter, 1985, p. 388).

An appropriate evaluation system is a necessary part of horizontal strategy. It should motivate managers and employees in business units to collaborate with other business units, and it should reward them for their effort and execution.

Itami (2003) describes five types of incentives that firms can offer people: Material Incentive (work for monetary compensation), Evaluative Incentive (work for a high evaluation in the organization), Human Incentive (work for an attractive leader), Ideal Incentive (work to support a philosophy and values), and Self-realizing Incentive (work for accomplishment). He says, “When we consider that the firm’s basic nature is an economic
organization, the most important incentives of all would be Material Incentive and Evaluative Incentive” (pp. 302-303). And since compensation is generally based on the result of an evaluation, I believe a proper evaluation system that satisfies employees’ Evaluating Incentive is a key factor in a successful horizontal strategy.

From Porter’s perspective, an appropriate evaluation system is essential for horizontal strategy. And from Itami’s perspective, the evaluation system is the foundation of every incentive. Then, what kind of evaluation system is required? The answer is clear: one that evaluates the contribution to other business units and the corporation, even if it worsens the performance of a single business unit. I will suggest three approaches to a successful evaluation system.

**Approach 1** is to evaluate managers and employees based on the corporate performance. Generally, people in business unit are evaluated by individual performance and/or the business unit’s performance. I suggest that corporate performance be incorporated into evaluations. For instance, managers would be evaluated 40% by individual performance, 30% by the business unit’s performance, and 30% by corporate performance. This would encourage managers and employees to work for the benefit of the corporation, not just for their business unit.

**Approach 2** is to directly evaluate the contribution to other business units. To do this, some individual performances should be judged based on implementation of the horizontal strategy. For example, managers are evaluated 40% by the business unit’s performance, and 60% by individual performance; and half of the individual performance is evaluated by
contributions to other business units through implementation of the horizontal strategy. This approach directly evaluates the implementation itself, and motivates people to execute the horizontal strategy.

Approach 3 is to lower the performance goal based on the amount of loss due to horizontal strategy that benefits other business units but worsen one’s own business unit. For example, if the profit of a business unit is expected to decrease 10% by implementing the horizontal strategy, that amount would be eliminated from the original performance goal. Although it is difficult to estimate quantitative loss, this approach is the most straightforward and comprehensible. If the loss of performance did not affect their evaluation, employees would not lose their motivation to implement horizontal strategy.

Figure 5-7 illustrates these three approaches. They are not mutually exclusive. A firm could adopt all three approaches at the same time. Providing this type of evaluation system is important for executing a horizontal strategy, and such an evaluation system would represent a strong commitment by management to achieve the horizontal strategy.
Current System
Score would lower

Without Horizontal Strategy
- Individual Performance
- Business Unit Performance

With Horizontal Strategy
If business unit performance declines, the evaluation of managers (or employees) would come down. Therefore, total evaluation would decrease.

Approach 1
Incorporate corporate performance

With Horizontal Strategy
Even the evaluation of business unit performance comes down, the evaluation of corporate performance would increase much more. Therefore, total evaluation would increase by executing horizontal strategy.

Approach 2
Individual performance includes execution of horizontal strategy

Without Horizontal Strategy
- Individual Performance
- Business Unit Performance

With Horizontal Strategy
Even the evaluation of business unit performance comes down, the evaluation of individual performance would increase much more. Therefore, total evaluation would increase by executing horizontal strategy.

Approach 3
Adjust original criteria

Without Horizontal Strategy
- Individual Performance
- Business Unit Performance

With Horizontal Strategy
Criteria of business unit performance comes down. Therefore, total evaluation would not decrease by executing horizontal strategy.

Source: developed by author.

Figure 5-7 Three Approaches for an Evaluation System
James Kouzes and Barry Posner (2007) note: “They need emotional fuel to replenish their spirits. They need the will to continue and the courage to do something they have never done before” (p. 281). An appropriate evaluation system gives encouragement, will, and motivation to managers and employees who are venturing into the difficult world of horizontal strategy.

5.3 Leadership

One more key factor to implementing horizontal strategy is leadership. Since horizontal strategy is executed by many people from different business units, strong leadership is needed to hold everyone together and achieve the goal. In addition to the CEO and top management, HO managers have to exert leadership, because realistically it is they who work up and down the corporation and push the entire horizontal strategy forward. As Ram Charan (2009) notes: “Being a leader in tough and uncertain times means always anticipating the next challenge and building the fortitude and skills to face it” (p. 127), leadership requires a strong will and heart.

Itami (2003) says that leaders have three faces: face to outside, face to upside, and face to downside. Face to outside means connecting to the external world as a representative of the group. Face to upside means negotiating with the top management as a representative of the group. Face to downside means leading members as the top of the group. Itami defines leadership as face to downside (p. 373). Figure 5-8 shows the three faces of leaders. In this section, I will discuss leadership needed by managers of an HO in order to lead a
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5.3.1 Source of Leadership

What are the qualifications of good leaders? What characteristics do people require leaders to have? Kouzes and Posner (2007) indicate four leadership qualities: honest, forward-looking, inspiring, and competent (p. 29). Itami says, “True sources of leadership would be personal magnetism, reliable decision, and rightfulness” (2003, p. 382). Drucker claims, “Manager needs skill in getting his thinking across to other people as well as skill in finding out what other people are after” (1954, p. 346). There are various views of what
makes a good leader, depending on the viewpoint one takes, but I believe the views cited above can be consolidated into two core sources—reliability and communication ability.

Reliability grows out of basic qualities such as honesty or morality, and personal skills such as forward-looking or decisive. Basic qualities which are obtained through self-discipline evolve into reliability. Personal skill plays a role in increasing a leader’s reliability and is obtained through experience and determination. In general, people do not like to obey others, particularly a leader who belongs to other group. Therefore reliability is essential to reassure people that they will be treated fairly.

The ability to communicate has multiple aspects: presenting, acting, inspiring, coaching, listening, understanding, encompassing, networking, and so on. Drucker notes,

The manager has a specific tool: information. He does not “handle” people; he motivates, guides, organizes people to do their own work. His tool – his only tool – to do all this is the spoken or written word or the language of numbers. No matter whether the manager’s job is engineering, accounting, or selling, his effectiveness depends on his ability to listen and to read, on his ability to speak and to write. (p. 346)

In order to execute horizontal strategy, leaders have to convince a broad range of people with different backgrounds and a variety of values. Sufficient and appropriate communication encourages people to work together. HO managers often have to take the brunt of an attack by business units, so communication skills are vital for persuading and satisfying employees.

In addition to reliability and communication ability, leaders must have a cross-cultural understanding if they work in a global corporation. People differ by race and culture, and if a leader does not understand cultural differences among members of an international team,
it is quite likely the goal will not be achieved. Fons Trompenaars and Charles Hampden-Turner (1997) write:

In every culture in the world such phenomena as authority, bureaucracy, creativity, good fellowship, verification and accountability are experienced in different ways. That we use the same words to describe them tends to make us unaware that our cultural biases and our accustomed conduct may not be appropriate or shared. . . . What is most important to consider, however, is not what they are and where they are found physically, but what they mean to the people in each culture . . . the essence of culture is not what is visible on the surface. It is the shared ways groups of people understand and interpret the world” (p. 3).

It is difficult for leaders to acquire a deep understanding of the culture of every business unit member, not least because what is important is invisible and tacit. However, leaders need to make efforts to know about cultural and racial differences, and to coordinate those differences with respect for each culture. In these circumstances, I believe reliability and communication ability would play significant role to lead people and achieve the goal. Reliability such as honesty or rightfulness would be universal quality. Communication ability would be a strong tool to show respect for different culture and clear up misapprehension even if leaders break taboo unconsciously. Here, feedback and learning is essential. Like emergent strategy, leaders could deepen and improve cross cultural understandings by practicing and experiencing.

5.3.2 Approach to Organization

In addition to sources of leadership, leaders should understand the dynamics of organizations. Deborah Ancona, Tom Kochan, John Van Maanen, and Eleanor Westney (2005) talk about three classic lenses on organizations, the strategic design lens, the political
lens, and the cultural lens. According to these authors, the strategic design lens looks at how the flow of tasks and information is designed, how people are sorted into roles, how these roles are related, and how the organization can be rationally optimized to achieve its goals. The political lens looks at how power and influence are distributed and wielded, how multiple stakeholders express their different preferences and get involved in (or excluded from) decisions, and how conflicts can be resolved. The cultural lens looks at how history has shaped the assumptions and meanings of different people, how certain practices take on special meaningfulness and even become rituals, and how stories and other artifacts shape the feel of an organization.

Within the same corporation, these three lenses would function differently depending on how they are applied to each business unit. They write that “A failure to consider multiple perspectives represents an incomplete analysis,” and they emphasize the balance of analysis using the three lenses. That is, as people in any organization move not only by designed rules, but also by political power and by cultural background, leaders have to pay attention to all three perspectives and take actions depending on the organization’s situation.

Generally, managers in corporate function tend to see the organization primarily through the strategic lens, because they place considerable value on discipline and rule in order to keep a rein on the corporation. There is a pitfall, however, as many HO managers find that people do not move as they wish. In such cases, they should remember to utilize the political and cultural lenses. This means finding allies in the business unit, discovering the
key person who has a major impact on the decision-making process, and understanding people’s social behavior and language. HO managers should try to see beliefs, morals, laws, or custom that exist in the business unit, as these often become the breakthrough for resolving a situation. Mintzberg (1998) defines ‘The Power School’ and ‘The Culture School’ as parts of ten schools of the strategic management, and notes “Hold power up to a mirror and the reverse image you see is culture. Power takes that entity called organization and fragments it; culture knits a collection of individuals into an integrated entity called organization. In effect, one focuses primarily on self-interest, the other on common interest” (p. 264). Leaders should understand that in addition to strategic issues, political power and cultural behavior are important dynamics in organizations, and they are critical to successful strategic management.

5.3.3 Developing the Next Generation of Leaders

Horizontal strategy and its implementation is not temporary or one-time activity. It must be executed continuously into the future, otherwise current competitive advantage will disappear, and the firm will quickly lose its competencies.

In order to implement a horizontal strategy sustainably, today’s leaders must work now to develop new leaders who can work as a future horizontal strategy. Lafley (2008) talks about P&G’s approach to developing leaders: “For the process of innovation to be sustainable, it is imperative to have a systematic methodology for developing these unique people as a continuous process” (p. 272). James Collins and Jerry Porras (1994) state: “It is
not the quality of leadership that most separates the visionary companies from the comparison companies. It is the continuity of quality leadership that matters – continuity that preserves the core” (p. 173). They put forward one strong message: sustainable development of competitive leaders is critical for sustainable growth of the firm, and development of new leaders is one of the most important missions of current leaders. It is surely important for leaders to implement horizontal strategy and generate synergy, and leaders should be evaluated from this regard, but if they fail to make it sustainable, their performance will be regarded as lacking the finishing touch.

One practical approach to development is arranging for young and promising people to be assistants to the leader. Itami notes, “Dividing the role of leadership or setting assistant has not been discussed in the theory of leaders, but it is crucially important in the real business world” (pp. 389-391). He defines four functions of an assistant: complementing the leader’s shortfalls, supporting the leader in every respect, criticizing the leader if needed, and enlarging the leader’s will to get things done. I agree with Itami’s belief that training an assistant is beneficial for both the leader and the organization. However, I also believe it is important for the development of leaders to come. As assistant works closely with the leader, it is a good opportunity for the leader to educate and transfer his skills. Likewise, it is beneficial to the assistant to experience the tasks of leader and acquire a leadership skillset. By implementing a system of assistants, firms can build an ample pipeline of leaders.

I will conclude this chapter by quoting Peter Drucker, who emphasizes the importance of development:
Just as no one learns as much about a subject as the man who is forced to teach it, no one develops as much as the man who is trying to help others to develop themselves. Indeed, no one can develop himself unless he works on the development of others. It is in and through efforts to develop others that managers raise their demands on themselves. The best performers in any profession always look upon the men they have trained and developed as the proudest monument they can leave behind. (p. 189)
In recent years, particularly after the financial crisis in the late 2000s, competition in the business world is getting more harsh and fierce. In a complicated and uncertain business environment, firms are competing just to survive. One key to doing this is creating new value that attracts customers. Value should be sustainable, otherwise it can be imitated by rivals and will never be a competitive advantage that wins customers.

Horizontal strategy is one of the most powerful ways to generate sustainable value, what I call synergy. Synergy is, in general, hard for rivals to replicate, for two reasons. First, synergy is generated by combining two or more businesses. For a rival to copy the synergy, the rival would have to replicate the same business structure in their firm. Second, synergy is generated by a systematic and complicated horizontal strategy. There is no standard or established way to execute horizontal strategy; rather, it requires advanced organizational capability because different businesses and people rarely collaborate spontaneously without strong control from the corporate function. This capability is intangible and often forms a compound body comprised of strategy, competence, culture, and history. It is difficult to replicate in other firms. In this regard, horizontal strategy and synergy are a great source of sustainable competitive advantage.
In Chapter 3, I examined several historical theories to better understand the fundamental principle of horizontal strategy. It can be defined in many ways depending on the perspective, but it is best defined by three key phrases: Activity Sharing, Skill Transfer, and Organizational Alignment.

In activity sharing, business units share one or more activities in the value chain. This is the easiest and most fundamental method of horizontal strategy and is suitable for diversified corporations that try to generate synergy for the first time.

In skill transfer, business units share intangible capabilities with each other. Because these capabilities are hard to retain within a single business unit, they become a competitive advantage against rivals if they are leveraged to generate new value for customers.

In organizational alignment, the firm forms a control tower for the horizontal strategy and considers optimal structures for its business units. Some activities may be consolidated, and some might be conducted independently. In any case, the organization structure is critical to executing the horizontal strategy and realizing synergy. Figure 3-18 (refer back to Chapter 3) illustrates my view of horizontal strategy.

In Chapter 4, I investigated real applications of horizontal strategy. Many diversified corporations are implementing horizontal strategies, but I chose four examples: General Electric, Virgin Group, Procter & Gamble, and my own employer, Kirin Group. The horizontal strategies of these four firms are unique to each company.
GE’s horizontal strategy is based on strong human resources and the process of human resource development, into which the company has invested one billion dollars per year for decades.

Virgin is leveraging its powerful brand to enhance every business unit in the group.

P&G shares its core competences, especially its systematic consumer-focused policy and innovation process, among all its business units.

Kirin has begun methodological actions recently, and is currently focused on the Low-cost and Differentiation strategic positions that are part of the Delta Model.

I cited specific challenges for the future of horizontal strategy in each firm. In particular, I examined possible approaches that Kirin might pursue in the future by learning from the examples of GE, Virgin, and P&G. Although this consideration was done for Kirin Group, I believe it has use for any diversified corporation.

In Chapter 5, I proposed a comprehensive process of developing and implementing horizontal strategy. The process should be practical and simple enough to be executed. I showed seven detailed steps for creating and implementing horizontal strategy as illustrated in Figure 5-1.

In addition to the seven steps, I discussed the importance of an evaluation system and leadership as part of the horizontal strategy. Even if there is a good strategy and suitable organization to execute it, people would not respond well without a proper evaluation system and strong leadership. The purpose of adopting an appropriate evaluation system is
to prevent deteriorating motivation among managers who belong to business units that may not benefited from executing the horizontal strategy. The performance of a business unit sometimes runs counter to that of the corporation, so an appropriate evaluation system will increase the likelihood of executing a horizontal strategy.

Likewise, leadership is crucial. It is not the system that move people, but rather strong leadership, especially when there are people with diverse values and cultures. Furthermore, in order to make horizontal strategy sustainable, continuous leadership development is essential. I discussed this in detail in the last section of Chapter 5.

I began this thesis by defining ‘diversified corporation’ as an entity that does business in multiple industries simultaneously. Now, however, I understand that the concept of horizontal strategy can be applied to a global corporation that is pursuing a single business in multiple countries, such as Coca Cola or Heineken. The concepts of activity sharing and skill transfer are applicable to these corporations in the same way, because even though the industry is the same, the business may need to be run differently from country to country or region to region. In order to execute activity sharing and skill transfer, corporations have to configure and coordinate their organization along the lines discussed in this thesis. There must be solid process, an appropriate evaluation system, and strong leadership to realize collaboration. Pankaj Ghemawat (2007) proposed an “adding value scorecard”, which stresses the importance of adding volume, decreasing costs, differentiating, improving industry attractiveness, normalizing risks, and generating and deploying knowledge in global strategy (p. 75). Each component of the adding value scorecard is, surprisingly, quite similar
to that of horizontal strategy. I found many commonalities between the mechanism of horizontal strategy and that of global strategy. Likewise, the RATs and CATs framework of internalization proposed by Donald Lessard (2011) would be applicable to a firm’s diversification. Activities and skills of the diversified corporation should be relevant, complementary, appropriate, and transferable in order to implement an effective horizontal strategy. In this regard, the ‘global diversified corporation’ has many more possibilities for generating synergy by applying horizontal strategy to global or international strategy.

Today’s business environment is changing dramatically, and businesses face increasing uncertainty. It is today’s leaders who will create new value. It is we who will execute new strategy. It turns on us whether the firm will survive.

I end by quoting Alfred P. Sloan, Jr., former CEO of General Motors and the original supporter of the MIT Sloan Program: “Each new generation must meet changes . . . the work is only beginning . . . . The work of creating goes on.” (1990, p. 444)
REFERENCES


