



## **STRATEGY PAPER - How the Resource-based and the Dynamic Capability Views of the Firm Inform Corporate-level Strategy**

**This paper explains that the resource-based view essentially addresses issues of competitive strategy, but by integrating some arguments from its evolutionary version, the dynamic capability view, it can be extended to inform our understanding of corporate-level strategy. We concentrate on the issue of value creation from corporate centres and ask how the centre can possess or provide resources. The primary dynamic capabilities identified by Teece, Pisano and Shuen (1997) are elaborated into six distinct modes of resource creation. Each mode is considered in relation to a set of organizational design parameters. We then propose resource-creating configurations that are congruent with respect to the modes and the required states of the design parameters. We point out areas of tension that are likely to arise if corporations try to combine different modes of resource creation. We conclude that corporate centres may possess resources but must display dynamic capabilities otherwise they will destroy shareholder value.**

### **Introduction**

The resource-based view (RBV) of the firm (Barney, 1986, 1991, 2001b; Wernerfelt, 1984) has received a great deal of recent attention and questions about its utility have been raised (Barney, 2001a; Priem and Butler, 2001). Whether one is an opponent or an advocate of the RBV is perhaps not of prime interest; what is perhaps more important is to suggest how it could be clarified, improved and developed. In this paper, to use Priem and Butler's (2001, p. 22) words we try to 'specify its likely contributions to knowledge'. In particular we establish some of the boundaries of application of the RBV to investigate aspects of value creation by corporate headquarters. That is, we attempt to identify some of the contexts to which the resource-based view can be applied, because, as argued by Barney (2001b, p. 649), it may be helpful to 'understand that the resource-based view can be applied in several different ways, and that the way it should be applied depends mostly on the empirical context of the application'.

In order to do so and further our understanding of 'the full implications of resource based logic for the sustained strategic advantages of firms' (Barney, 2001a, p. 52), we explore in this paper whether the resource-based view primarily informs our understanding of competitive strategy or corporate strategy. We conclude that RBV applies in essence to competitive, rather than corporate strategy. It provides insights into strategy issues at the level of the strategic business unit (SBU) or individual firm. However, there are grounds for extending the perspective to address corporate-level concerns. The evolutionary version of the resource-based view, the 'dynamic capability view' (Eisenhardt and Martin, 2000; Teece, Pisano and Shuen, 1997), i.e. 'capability building' in Makadok's (2001) terms, provides valuable insights into how SBU and corporate-level activity can create new resources. The value of

the dynamic capability argument is recognised by Barney (2001a, 2001b) who admits that it is important to analyse sustainable competitive advantage in a dynamic fashion, and as highlighted by Helfat (2000), the dynamic capability view needs development. This would suggest that an attempt to integrate arguments from the dynamic capabilities literature with the established resource-based view might be valuable in advancing both approaches (Williamson, 1991).

We assume initially that a corporation consists of two levels of activity. At the lower level there are a number of semi-autonomous SBUs engaged in the production of goods and services. Although the SBUs may be related in some ways, we assume that they supply different groups of products to different markets. At the higher level we have the corporate centre or headquarters, which is not involved directly in the provision of products. Its role is to oversee, support or augment the primary activities of the SBUs. This is in line with Grant (1995), who views competitive strategy as the ways in which a single-business firm or an individual business unit of a larger firm competes within a particular industry or market, and, corporate strategy as the ways in which a corporation manages a set of businesses together. Towards the end of the paper we relax this assumption of a clear delineation of roles between the SBUs and the centre as we explore various resource-creating strategies.

The context of applicability of the resource-based view and the dynamic capability view is our first concern. The first part of the paper explains why RBV should be considered to be essentially addressing competitive strategy. The second part explores DCV and focuses on the value-adding role of the corporate centre. We address both where the dynamic capability argument augments the resource-based view and



where it can specifically be applied to competitive and corporate strategy. We also focus our attention on corporate resource-creating processes and the consequent strategies that can be derived from the dynamic capability perspective. We elaborate the dynamic capabilities identified by Teece, Pisano and Shuen (1997) into six modes of resource creation. We then introduce Mintzberg's (1979) organizational design parameters in order to explore the structures and processes required for each mode to be enacted. Finally, we argue that each mode required a distinct configuration, and that trying to combine modes is likely to cause tensions and compromises that the centre would need to manage.

### **Corporate strategy**

The corporate strategy literature is undoubtedly very rich and in this paper we do not aim to cover this extensive literature. Our attention is focused on corporate strategy, but within the confines of RBV and DCV. However, despite this caveat we recognize that some readers may feel that we have overlooked some relevant prior work. Although we refer to Goold and Campbell's (1987) work on strategic management styles, and Goold, Campbell and Alexander (1998), Campbell, Goold and Alexander (1995a) and Prahalad and Hamel's (1990) research on parenting theory, they are not given an extensive treatment. Similarly, we have not incorporated the RBV literature on diversification (e.g. Kor and Mahoney, 2000; Mahoney and Pandian, 1992; Robins and Wiersema, 1995). We have done so consciously because we wanted to provide a distinct argument, and as such we have avoided fighting our battle on several fronts, to concentrate on one primary idea. Goold, Campbell and Alexander's (1994, 1998) publications have been central to understanding why corporate strategy matters, and what the influence of the centre can be (Bowman and Helfat, 2001). They have provided us with a range of prescriptions that should help corporate managers avoid destroying value and develop a parenting advantage. Our purpose is to contribute specifically to the resource-based view of the firm. This is why we have reviewed RBV narrowly, concentrating on its original version and we have compared it to the dynamic capability view (DCV). However, some authors have argued that there is one broad resource-based view that incorporates several views which all share the same basic assumptions about how organizations outperform others and hence can be seen to be under the same RBV umbrella (Barney, 2001b).

Bowman and Helfat (2001) argue that corporate management by itself cannot build core competencies' and 'in theory corporate management and corporate strategy have an impact on but do not fully determine corporate influence on profitability' (2001, P. 4). They imply that RBV is not primarily about corporate strategy. In what follows we proceed to build on this argument.

### **The resource-based view of the firm and competitive strategy**

In this section we explain why RBV should be regarded as a theory of competitive strategy. In order to do so we begin with a reminder of the core principles of the view and then we provide a clarification of the criteria that define a resource. This is necessary, because, as argued by Priem and Butler (2001), one of the main weaknesses of RBV is the lack of precise definitions and rigorous arguments.

The resource-based view of the firm examines the link between the internal characteristics of a firm and firm performance (Barney, 1991). The core principles are that an organization can be regarded as a bundle of resources and that resources that are simultaneously valuable, rare, imperfectly imitable and non-substitutable — the VRIN conditions (Barney, 1991), are a firm's main source of sustainable competitive advantage. This means that RBV locates the source of superior profitability inside the firm. Rents accrue to the resources controlled by the firm that meet the VRIN conditions. These rents lead to super normal profits when captured by the firm rather than by resource suppliers (Barney, 1991; Dierickx and Cool, 1989; Peteraf, 1993; Rumelt, 1984; Wernerfelt, 1984).

In what follows we consider each of the VRIN conditions, underlining the aspects most relevant to our purpose, which is to show that RBV is fundamentally addressing issues of competitive strategy.

#### *Valuable*

A resource is valuable to the firm if it generates rents that can be captured by the firm (Bowman and Ambrosini, 2000; Priem and Butler, 2001). Resources can enable a firm to be lower cost than rival firms, or they may enable the firm to differentiate its products or services. This also suggests that through shifts in demand, resources can become redundant irrespective of any deliberate management activity, and through inappropriate management interventions, such as downsizing, resources can be destroyed. Resources can also cease being valuable as rent generators through competitor imitation or substitution (Barney, 1986). This is highlighted by Peteraf (1993), who explains that to be valuable a resource must not only generate rents but ex-ante limits to competition also need to be present in order to prevent costs from offsetting the rents. Ultimately for rents to accrue there must be a revenue stream involved. Even if the resource enables the firm to be lower cost, the costs that are being reduced are part of a set of activities that ultimately deliver saleable products or services.

Before progressing onto the second of the VRIN conditions, it is worth noting that in most RBV contributions, resources are assumed to be valuable. In other words, 'resource' means 'valuable resource', i.e. 'resource that generates rents' (this



could be argued to introduce some circularity into the theory). In what follows we will hopefully avoid confusion by calling resources that are not rent creating, 'assets'.

#### *Rare*

The relative scarcity of a resource means that a firm that possesses a rare resource can generate either superior margins or superior sales volumes from an equivalent cost base to competitors. As implied such a resource is not commonly found across other competing firms. If it was common, it should be regarded as an entry asset, an easily available non-rent generating asset.

The V and R criteria are about the identification of resources at a point in time. The next two VRIN criteria address the sustainability of the rent streams flowing from these resources. They are the two main ex-post limits to competition.

#### *Inimitable*

The more difficult it is for competing firms to replicate the resource, the longer-lived will be the rent stream accruing to the resource. Inimitability results from the presence of isolating mechanisms (Rumelt, 1984) such as causal ambiguity, information asymmetries or social complexity. These mechanisms protect the organization's resources from imitation and preserve the stream of rents accruing to them. Judging inimitability requires insight into the nature of the resource, and how it was created. A thorough knowledge of the firm's history may be required, given the path-dependent nature of many resources (Reed and DeFillipi, 1990; Rouse and Daellenbach, 1999). Causal ambiguity internal to the firm may mean even managers cannot readily comprehend the nature of their firm's resources.

#### *Non-substitutable*

A resource is said to be non-substitutable if it cannot be easily replaced by another resource that delivers the same effect. Assessing substitutability requires an understanding of the use value of the resource (Bowman and Ambrosini, 2000). This implies that the role the resource plays in the value-creation process needs to be well understood. It is only then that it may be possible to discern alternative or substitute ways in which the effect could be achieved.

Identifying valuable and rare resources in a firm implies that judgements about resource value must be linked directly to the current profit streams of the firm, and the rarity of the resource can only be judged through a thorough knowledge of competing firms. As argued above, judgements about inimitability and non-substitutability require foresight, combined with some understanding of how the particular resource was created. These last two conditions are problematic, because resources may generate causal ambiguity

as a result of their complexity or tacitness for instance (Lippman and Rumelt, 1982; Reed and DeFillipi, 1990). Moreover, luck (Barney, 1986) or serendipity can play an important part in resource creation. In other words identifying VRIN resources needs an in-depth understanding of the firm to untangle the mystery of the sources of sustainable competitive advantage (Rouse and Daellenbach, 1999, 2000). To conclude, resources that pass the VRIN test are involved in delivering competitive advantage to the firm, by either delivering product advantages perceived by customers or they confer process advantages that result in lower unit costs. As such, they generate rents and contribute to the firm's super normal profit.

Assuming that the product or services sold by the firm are created in SBUs and that rent-generating resources are situated at the SBU level, we can deduce that resources are primarily SBU level constructs, intimately connected to product markets. As Priem and Butler explain, the RBV deals with the 'business level question of how to compete' (2001, p. 23). RBV is essentially a static theory (Priem and Butler, 2001). It concentrates on identifying resources at one point in time, and addresses how these resources may have been created. However, a recent extension of RBV, the dynamic capability view (Eisenhardt and Martin, 2000; Teece, Pisano and Shuen, 1997) addresses the processes of future resource creation. The dynamic capabilities view (DCV) focuses on the capacity an organization facing a rapidly changing environment has to create new resources, to renew or alter its resource mix. If we assume that resources are situated primarily at SBU level, processes that reshape and augment these resource bundles can conceivably operate both at SBU level, and at corporate level. Clearly, SBUs themselves are likely to have their own dynamic capabilities. Without these capabilities SBUs are unlikely to be able to sustain advantage. However, in what follows we suggest that the primary ways in which the corporate centre can add value can be explored from a DCV perspective. So although SBUs may well have dynamic capabilities of their own, these may be significantly enhanced by different capabilities enacted at the corporate level.

#### **The dynamic capability approach and corporate strategy**

The essential differences between a corporate structure and a single firm is that the corporation typically comprises more than one line of business, and that there is usually a distinction made between business-level (SBU) activity, and activity performed at the centre. If corporate-level activity is to be valuable, it must in some way impact positively on the profitability of the organization (e.g. Goold, Campbell and Alexander, 1994; Kay, 1993). One way the corporate level can contribute is if it performs dynamic capabilities.



The dynamic capability approach focuses attention on the firm's ability to renew its resources in line with changes in its environment. Dynamic capabilities refer to the firm's ability to alter the resource base by creating, integrating, recombining and releasing resources (Eisenhardt and Martin, 2000). They may involve processes of coordination, replication, learning and reconfiguration (Teece, Pisano and Shuen, 1997). In these two major contributions to the DCV, Teece, Pisano and Shuen (1997) and Eisenhardt and Martin (2000), they make no clear distinction between capabilities performed at corporate rather than SBU level.

Dynamic capabilities are built rather than bought in the market, and they are embedded in the organization (see Makadok, 2001 for an elaboration of this point). These capabilities are likely to be path dependent routines (Eisenhardt and Martin, 2000) and as such they may resist imitation by rival corporations.

However, if we relax our clear distinction between the role of the centre and SBUs, the centre may also possess resources. This suggests that there is a possible blurring between SBU level competitive strategy issues, and corporate-level strategy. The more challenging role of the centre is the creation of new resources, where the centre displays dynamic capabilities. However, because the processes of resource creation are not well understood, and because the identification of rent generating resources is problematic, we have to examine the processes of asset creation. Because of causal ambiguity we cannot be certain that particular activities that the centre engages in will result in the creation of true resources that pass the VRIN tests. Instead, we explore activities that should create assets for the corporation, and that may result in new resources being created, that is resources that generate rents.

In what follows, we examine these assets and resource creation possibilities, grouping this exploration under the headings of reconfiguration, leverage, learning and integration. For brevity we refer to resource creation, with the understanding that the processes considered may produce assets rather than resources.

#### *Reconfiguration processes*

Reconfiguration processes transform and recombine assets and resources. A common form of resource creation through reconfiguration is consolidation, which usually occurs after an acquisition or merger. Here, like activities are usually centralized and rationalized, thus conferring a cost advantage on SBUs which use these resources. The result is normally resource creation at the centre. Alternatively, the centre can reconfigure the SBUs to allow one SBU to exploit economies of scale and scope, which other SBUs can benefit from. For the consolidation to be successful the activities that are combined must be performed in similar ways across the units, and the

activity must be capable of being decoupled from other operational processes at SBU level. So although the resource is normally controlled and managed at the centre, it confers advantage on the SBUs. As an aside we could note that if support services offered at the centre do not confer a cost or effectiveness advantage they might just as well be provided within SBUs. Moreover, if SBU managers deem the corporately provided activities as not suitable for their needs, and therefore they have to duplicate these costs at SBU level, the centre activity is actually destroying value.

Decoupled activities might include, for instance, finance functions or public relations. The more operationally integrated the consolidated activity is, the more blurred will be the distinction between corporate and SBU levels. So where there are scale economies to be had in core activities like marketing, selling and manufacturing, these activities may need to be tightly coupled to SBU activity (Thompson, 1967). What constitutes core activity is clearly determined by the overall mission of the corporation.

Thus we need to distinguish between two forms of reconfiguration: consolidation of support activities, and reconfiguration to achieve scale economies in core processes, because they each have different implications for the design of the corporate structure. Moreover, it may be that reconfiguring activities enables one SBU to create a scale resource that others can benefit from, i.e. reconfiguration may result in resource creation within SBUs as well.

Once the new resource is created through centralization, the dynamic element of the process has ceased. The challenge for the corporate centre is then to repeat the process. Hence we see some corporations in the continual drive for acquisitions of similar businesses in order to increase the utilization of the existing stock of resources (Penrose, 1959).

#### *Leveraging existing resources*

The centre can assist in resource creation by leveraging existing resources. This may be done by extending the scope of the resource into other SBUs or market domains, or by what Teece, Pisano and Shuen (1997) describe as replication. The centre may for instance directly control a strong brand that could be extended across a wider range of products. Extending the resource in this way may be done at low cost, probably at lower costs than those required by an individual SBU to build a brand from scratch. The centre would need to display expertise in knowing how the brand adds value, identifying where else it could operate as a resource and to manage the required changes in a way that did not diminish the value of the brand. Despite the centre being active in manipulating the brand resource, the brand has no value separate from produced products or services to which it is attached in the perceptions of the customer. This



implies that although the manipulation of the brand could be directed and controlled from the centre, the brand only performs as a resource at SBU level. However, rather than the brand being leveraged, it might be brand-development expertise that is replicated. This special know-how possessed by an individual or a group, which in its current setting generates rents for an SBU, could be transferred to another SBU, or newly acquired activities could be located alongside the resource to benefit from it. Although resources may display causal ambiguity to competing firms, it may nevertheless be possible for managers inside the corporation to develop insights into these knowledge resources.

The role of the centre is to identify the nature of the resource, to recognize new opportunities where the resource may confer advantage, and to implement the necessary organizational changes, or create the conditions whereby the resource can be transferred.

In making judgements about where to leverage resources the centre is dealing with issues of diversification. Resource leverage is a form of related diversification (Collis, 1996; Robins and Wiersema, 1995), but the term 'related' may not pertain to the traditional notions of products and markets. An efficient quality system, an expertise in real-estate acquisition or a strong corporate image may confer advantage across a range of SBUs operating in quite different product markets. Culture, as a resource, can be leveraged almost inadvertently through the socialization of employees in particular 'ways of doing things', which they then disseminate as they move across the SBU landscape.

The insight to know which processes or know-how to leverage is critical. In some cases the dominant acquiring firm may impose inferior systems on the acquired firm. So an existing resource may be leveraged in two ways: either the application or scope of the resource is extended into other domains of the corporation, or the resource is replicated. In order for replication to occur the resource must be capable of being understood, thus it cannot be causally ambiguous to managers inside the corporation (although it would still be ambiguous to those external to the firm).

### *Learning*

Learning is 'a process by which repetition and experimentation enable tasks to be performed better and quicker' (Teece, Pisano and Shuen, 1997, p. 520). This dynamic capability has spawned a literature all of its own (e.g. Coopey and Burgoyne, 2000; Lahteenmaki, Toivonen and Mattila, 2001; Senge, 1990). Learning obviously occurs at all levels in the structure, but the centre can indirectly influence the learning processes in SBUs by:

- encouraging SBUs to devote resources to innovation;
- allowing SBUs time to explore new ideas;
- introducing into SBUs new perspectives and knowledge;
- encouraging experiments and tolerating failures;
- establishing dialogue across SBUs;
- funding R&D at SBU level.

However, it is possible that a quite different governance regime may provoke learning within SBUs, rather than support or encourage learning. If we bear in mind that resources exist where firms or SBUs have a competitive advantage over rival firms, it may be that relative advantage can be created through the elimination of organizational slack. For example, where SBUs are subject to tough performance controls that can only be achieved through the ruthless elimination of waste activities and costs, compared to competing firms enjoying more relaxed governance regimes they may have created a cost advantage. Obviously, this type of régime may well deter expenditure on future-oriented activities like R&D and training.

So we can identify two learning strategies, both driven from the centre, which may result in the creation of new resources: one that operates through a supportive culture, and another that provokes resource creation through tough controls.

### *Integration*

This type of dynamic capability concerns the firm's ability to coordinate and integrate its resources and assets. This capability is akin to Henderson and Clark's (1990) architectural knowledge or Miller and Shamsie's (1996) systemic knowledge. It relates to the 'ways in which the components are integrated and linked together into a coherent whole' (Henderson and Clark, 1990, p. 11). Examples of such integration and coordination processes include new product development in which managers form multi-functional teams combining various skills, expertise and assets to create new products. Integration can also be about integrating resources from external sources such as suppliers or customers, they are routines allowing the linking of customers' experience with engineering design or suppliers with production processes. These coordination and integration processes are the main sources of process and product innovation. They involve combining resources in new ways to alter the firm's resource base. While this process may lie within single SBUs the centre can drive resource creation by recognizing where the congruencies and complementarities exist across the corporation and across the corporation and its clients, by encouraging SBUs to pool their skills and resources with those of other SBUs teams, or by encouraging cross-divisional linkages or interactions with clients to settle existing problems or enhance innovation throughout the corporation.



Thus far we have elaborated the basic dynamic capabilities by which firms alter their resource base into six modes of corporate resource creation:

- reconfiguration of support activities;
- reconfiguration of core processes;
- leverage of existing resources;
- encouraged learning;
- provoked learning;
- creative integration.

### **Design parameters**

In this section we explore the structures and processes that would need to be in place in order for the centre to deliver each of these modes. First, using Mintzberg's concept of design parameters (Mintzberg, 1979) we examine the required states that each mode would require of the following parameters:

- SBU strategic autonomy;
- SBU similarity;
- coordination across levels;
- coordination between SBUs;
- performance measures and SBU orientation.

Although there are other design parameters that may be pertinent to corporate structures e.g. planning processes, we believe these are particularly relevant to the role of the centre in delivering dynamic capabilities.

#### *SBU strategic autonomy*

This parameter refers to the scope and discretion the SBU executives enjoy in determining aspects of SBU strategy. This can be viewed as a continuum of autonomy. At one extreme we would locate the two learning modes: provoked learning and encouraged learning. With provoked learning the SBU executives would be tasked to deliver financial performance, but how they achieved these results could be left to them to decide. The encouraged-learning mode would probably require high levels of strategy autonomy, but the centre may require more oversight of investment decisions e.g. R&D spends.

Reconfiguration leading to the centralization of support services would still permit SBUs to determine most aspects of SBU strategy, but they would be obliged to use, and to follow the policies set by the centralized support functions. Where reconfiguration delivers scale-based resources in core activities to the SBU, it is likely that SBU autonomy would be constrained significantly. Indeed, it may be that SBUs are restricted to sales/service/local marketing activities.

Leveraging SBU resources implies that SBU executives are not able to solely determine the dispositions of SBU resources. Where replication takes place, again SBU executives would be obliged to get involved in the capture of expertise that may be a

unique resource for the SBU, and they would be expected to be open to the introduction of systems and processes developed elsewhere in the corporation.

The creative integration mode, more than the other modes, requires SBUs to view themselves as component parts of the corporation. We would expect SBU autonomy on many dimensions of strategy to be low where an integration mode predominates.

#### *SBU similarity*

The effectiveness of each mode of resource creation will be moderated by the extent to which the collection of SBUs is similar. However, as we suggested earlier, our concepts of relatedness need to be sufficiently broad to account for the various ways in which corporates can create resources. So for each of the dynamic capabilities we would expect different forms of similarity.

With the learning modes SBUs need not be similar as far as products, markets, core processes or technologies are concerned. As Hanson proved in the 1970s and 1980s, firms can be acquired in diverse fields but they can nevertheless benefit from control regimes viz, batteries, bricks, tobacco, bulk chemicals. However, as we explained above the provoked learning mode is unlikely to foster a longer team, developmental orientation within SBUs. So we might expect provoked learning to be most effective where SBUs are dissimilar in products, markets, and technologies, but they are similar insofar as they do not require substantial investments in order to secure future performance. Where encouraged learning is the preferred mode we would expect SBUs to be similar in their requirements for investments in R&D and other developmental activities. In this way the centre could take a common approach across all SBUs. However, this may cause problems where, for example, a portfolio approach to SBU management is used e.g. 'cash cows', 'stars' etc, where one would expect dissimilarities between the SBUs investment requirements.

Where reconfiguration is effected in support activities, SBUs need to be able to benefit from common support functions like legal, HR, estates etc. Clearly, trade-offs will be made between the corporate benefits of scale economies and the need to meet local SBU requirements. Where reconfiguration delivers scale resources in core processes then SBUs must be similar in respect of their use of these core activities.

Leveraging existing resources requires the SBUs to be similar in their ability to benefit from the resources concerned. Where resources are cloned, or replicated again there would need to be similarities between the SBU strategies and processes. Again, judgements are required with respect to the extent to which



common systems and processes are imposed on SBUs. Where the creative integration mode is employed the SBUs need to have complementary knowledge bases. In this way the knowledge can be shared, and interSBU interactions may create new ideas. These new possibilities would not have been achievable through intra-SBU interactions.

#### *Coordination across levels*

A key parameter in designing corporate structures is the degree of coordination that is necessary for the corporate strategy to be delivered. Mintzberg (1979) argues that the predominant method of coordination adopted in an organization has great influence on many other design parameters. Here we are not so much concerned with the predominant mechanism of coordination, but rather the degree or extent to which coordination must be effected between the centre activity and the SBUs. As with SBU autonomy we can view this as a continuum. We would expect the two learning modes to require little interlevel coordination of activity. Indeed, one would not expect a great deal of communication between the centre and SBUs in either of these modes, with perhaps the provoked learning mode requiring the least communication.

Coordination becomes an issue, though, where reconfiguration is involved. Support activities will need some coordination between the centralized activities and the SBUs, and even more coordination is required where core activities are centralized, or where scale resources have been developed within one SBU for the shared benefit of other SBUs. Leveraging resources requires interlevel coordination and a good degree of cooperation, so some sense of shared mission would be helpful here, but whereas coordination would be ongoing in both cases of reconfiguration, coordination within leverage modes may be more episodic.

With the creative integration mode we would expect extensive coordination between the centre and SBUs. Indeed, we would also expect a regular movement of personnel between levels.

#### *Coordination between SBUs*

The requirement for inter-SBU coordination is determined by the dynamic capability mode adopted. Where provoked and encouraged learning modes are operating there is little need for coordination between SBUs. Reconfiguration of support activities may require some levels of communication between SBUs, but the primary interactions are likely to be between the SBU and the centralized activities. Similarly, scale economies in core activities may require more coordination between levels than between SBUs, but this would depend on what has been centralized, and on whether the SBUs were involved in sequential processes i.e. they were vertically integrated. Clearly, the more vertical integration involved, the more there would be a need for coordination between SBUs. However, this coordination could be remote and of a quasi-market nature

if transfer pricing is used. It is more likely though that reconfigured activities would be in some ways physically interlinked, requiring direct and extensive levels of coordination.

The leverage strategy would require inter-SBU coordination of a more episodic nature, focused at the points where resource leverage is being considered and when it is effected. Creative integration requires ongoing coordination across collaborating SBUs. There would need to be a culture of regular communication and we would expect many informal networks to be established between SBUs.

#### *Performance measures and SBU orientation*

Each mode of resource creation is likely to be associated with a particular relationship between the centre and the SBUs. Central to this relationship are the performance measures the SBU would be judged on. We would expect the provoked learning mode to involve the setting of tough profit targets for a diverse collection of SBUs. Where encouraged learning is the preferred mode we would not expect singular performance measures to be effective. The centre is more likely to use a range of measures, and to vary the targets and messages it gives to different SBUs. With both reconfiguration modes only partial profit accountability can be expected from SBUs as their autonomy is constrained by the requirement to utilize centralised activities or to, for example, sell and service the products supplied by the centralized core. Targets for the leverage modes should encourage the sharing of know-how and the free flow of information.

We would expect that executives in SBUs within the provoked learning mode would identify primarily with the SBU, rather than the corporation. All other modes would require varying degrees of corporate identification at SBU level, varying from the least in the encouraged learning mode, to the most with the creative integration mode. The essential difference between encouraged learning, and creative integration as resource creation processes is that the latter requires inter-SBU collaboration, and to facilitate this it would be important for SBU personnel to identify strongly with the corporation.

#### *Resource creation configurations*

So far we have elaborated the dynamic capabilities identified by Teece, Pisano and Shuen (1997) into six distinct modes of resource creation. Then we explored the implications of each of the modes for design parameters we believe are particularly pertinent to corporate level strategies. In this final section we introduce the notion of configurations into the argument (Miller, 1986; Mintzberg, 1979). Following on from our discussion of the states of the design parameters required by each mode we set out six configurations. These are feasible structures that could deliver one mode of resource creation.



Each configuration is coherent in that the required states of the design parameters are mutually consistent and supportive. We conclude by arguing that corporations have to choose between these modes of resource creation. The argument developed by Goold and Campbell (1987) applies here. As for their management styles, each configuration will require different organizational processes, divisions of responsibilities, SBU and centre competences etc. and therefore in many cases corporations are unlikely to be able to adopt more than one configuration. We will discuss exceptions later on.

Where corporations try to enact combinations of modes, our framework can be used diagnostically. For example, should a corporation wish to combine a leverage replication mode within a predominant encouraged learning mode we can see where some of the tensions or compromises are likely to occur. It may be that only a subset of SBUs can benefit from resource replication, as the possible sites for replication are likely to be limited. This may lead to a restructuring of related SBUs into divisions, to better facilitate the replication processes between related SBUs, and to appropriately incentivize the subsets. We can also see that some mode combinations would require almost irreconcilably contrasting states of particular design parameters. Where provoked learning is the prevailing mode it would be very difficult to encourage almost any corporately orientated behaviour among SBU executives, focused as they must be on short-term SBU performance.

We accompany each of the configurations with illustrations from real corporations (for those interested in following up on these examples, where indicated \* they can be accessed from the European Case Clearing House). We also depict each configuration with a figure, highlighting where the created resources reside. Finally, we have also tried whenever possible to relate them to Goold and Campbell's (1987) styles, and Ghoshal and Bartlett's (1998) framework. There is no exact match as our proposed configurations have been derived from a different theory base, the RBV and DCV perspectives. The only exception is the case of the provoked learning configuration that matches Goold and Campbell's financial control style.

#### *Provoked learning configuration*

In the provoked learning configuration (Figure 1) the centre causes SBU resources to be developed through the setting and administering of tough financial controls. Here the SBUs are provoked into creating resources in order to meet the imposed performance targets. If we assume that resource-endowed firms can be benchmarked against competing firms, the SBUs within this configuration will have reduced levels of organizational slack or X-inefficiency compared to rival firms. Hence they will have lower relative costs, and ceteris paribus will generate more profits.

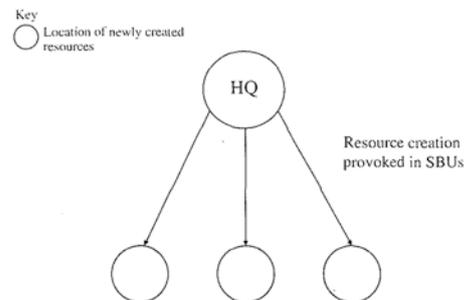


Figure 1. Provoked learning configuration: rewards are based on the achievement of financial targets

Whether these cost advantages can be attributed to specific resources is debatable, however. These resources are likely to consist in the styles and controls operated at SBU level, in response to the targets being set.

The centre is relatively small, there may be a large number of diverse SBUs in the portfolio, and there is no requirement for coordination between SBUs. Relationships between the centre and SBUs will be 'arms length' based on financial performance targets. The emphasis would be on short-term profit performance, the centre would engage in target setting, and in altering the portfolio of SBUs through acquisitions and divestments. Because of the short-term nature of the control system SBUs that require investments in R&D, marketing or training are unlikely to flourish within this régime. This strategy is similar to Goold and Campbell's (1987) financial-control management style. If we refer to Ghoshal and Bartlett's (1998) work on corporations operating in the international business environment, this financial control strategy is likely to be applied by both multinational and global corporations. Both these management styles are about control and setting profit targets.

There are numerous examples of corporations that followed such a strategy. One can cite Sunbeam, whose headquarters maintained tight control over all their business units; Magna, where discipline and incentives were developed to maximize profits; or Tyco whose core approach was financial control, using the financial system to push responsibility and accountability down through the corporation.

#### *Encouraged learning configuration*

Here the structure of the corporation would be similar to that required with provoked learning (see Figure 2). However the performance measure and relationships between the centre and the SBUs would be quite different.

The centre would be sensitive to the need for SBUs to invest in the creation of future assets and resources, and the performance measures and targets set would reflect these concerns. We



would expect SBUs within this configuration to be able to devote expenditure to the creation of potential future sources of advantage. Performance measures would need to reflect more than just short-term profitability, and we would expect far more dialogue between the centre and the SBUs compared to the provoked learning configuration. The quality of this interlevel dialogue would be enhanced where the centre had expertise specific to the context of the SBUs. This would indicate that the SBUs in the portfolio would be related in some ways e.g. similar products, technologies, markets etc.

#### *Reconfiguring support activities*

Here the centre reconfigures loosely coupled support activities, and conducts these activities on behalf of SBUs (e.g. legal, finance, estates, PR). If these consolidated support activities confer cost advantages on SBUs, then the centre possesses the resource, which the SBUs exploit. SBUs would need to be similar to the extent that they could all use the centralized support functions, and would need to be limited by specific coordination between the centralized activities and the SBUs (see Figure 3). The centre may have to manage the compromises that SBU executives would have to accept where local SBU requirements were not entirely met by the centralized functions. Performance measures would need to recognize the constraints on SBU freedom to choose, but cost savings should enable SBUs to be more cost competitive.

IBM, Unilever and Newell are examples of companies that employed consolidation strategies to create value. For instance, Newell provided common logistics management, IBM centralized its marketing and Unilever consolidated its communication approach and advertising in general.

#### *Reconfiguring core processes*

Here the centre delivers resources by reconfiguring core processes to exploit economies of scale. The SBUs are highly dependent on these centrally controlled resources, and thus may be only partially profit accountable (see Figure 4). Certainly they would enjoy fewer degrees of freedom in determining strategy compared to SBUs in either of the learning configurations. Indeed, where most core processes are managed centrally the SBUs are severely restricted in their freedom to decide. Both consolidation configurations could be argued to fall to some extent within Goold and Campbell's (1987) strategic-planning management style stereotypes as they describe the corporate centres that follow such approaches as being 'masterplanners'. If we follow Ghoshal and Bartlett's approach, they can be seen to relate principally to the global or centralized business model that Japanese corporations typically followed in the mid-1960s to capture global scale economies. There are numerous corporations that have opted for this scale strategy e.g. Procter & Gamble, with centralized product development and product manufacturing. Ikea followed the

same strategy when centralizing store design and manufacturing and Birds Eye did so when centralizing their cold stores.

#### *Leverage configuration*

In the leverage configuration, the centre creates new SBU resources through either replication, or by extending the scope of a resource (see Figure 5). Here there are no resources as such at the centre, only the dynamic capability to leverage resources from one SBU into others. SBUs would need to be similar to the extent that they could benefit from leveraged or collocated resources. Performance measures would need to reflect efforts made by SBUs to leverage their resources or assets, or to incorporate new assets into their own operations. SBUs would be required to coordinate to facilitate resource or asset leverage, and if know-how is replicated the codification processes may require coordination with a centralized techno-structure (Mintzberg, 1979). One could note that know-how developed in one SBU may, through competitor imitation cease to be a resource, however it may be transferable to a new SBU context where it would be able to function as a resource. If we follow Ghoshal and Bartlett's (1998) analysis, this proposition can be seen to relate to the international business model that American corporations typically followed post-World War II. More recent examples would be CAE, whose headquarters acted in a coordinating capacity, and Watcom that encouraged leveraging by facilitating the flow of information across the corporation through informal structures and flexible communication channels.

#### *Creative integration configuration*

Here the centre encourages and facilitates SBU learning that leads to product or process innovation. The centre may be aiming to set up 'webs of collaboration' (Eisenhardt and Martin, 2000) across the corporation and between the corporation, its clients and suppliers. Again as with the leverage strategy, the centre possesses no resources, but it does enact the dynamic capability of engendering dialogue and interchange between SBUs which creates new knowledge resources (see Figure 6). This strategy can be linked to Ghoshal and Bartlett's (1998) idea of the transnational corporation, which is about integration, flexibility learning and interdependence. Fishery PT followed this strategy by setting up and integrated information systems to keep employees around the world connected and by having integrated marketing and operations. SAP followed this strategy and so did Johnson & Johnson when facilitating the collaboration of the different units when required, and by encouraging the re-use and the development of existing SBU technologies and processes. 3M's culture embeds creativity within SBUs and across the corporate landscape.

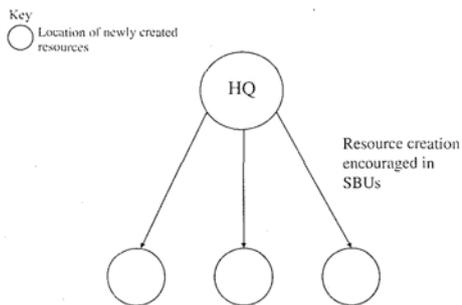


Figure 2. Encouraged learning configuration: rewards are based on financial and non-financial measures

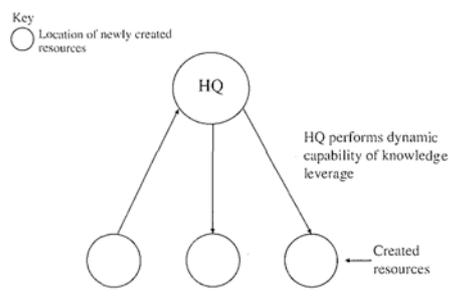


Figure 5. Leverage configuration

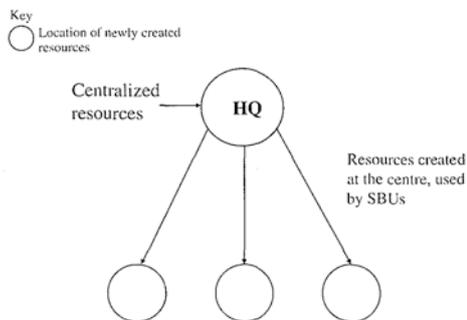


Figure 3. Reconfiguration of support activities configuration

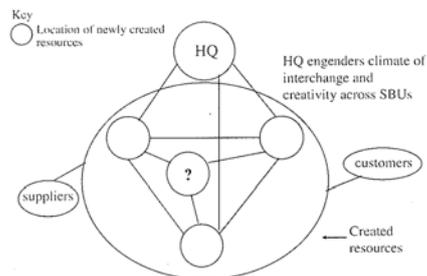


Figure 6. Creative integration configuration: resources may be created within SBUs or they may result in new SBUs being established

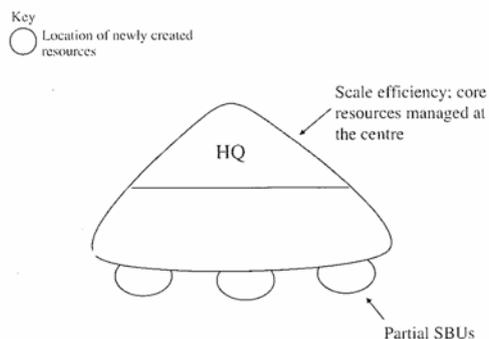


Figure 4. Reconfiguration of core processes configuration

### Configurations as strategies

These six configurations can be viewed as alternative corporate strategies. They are potentially realizable corporate strategy options that are coherent with regard to the relationships between the asset-creation aims of the strategy and the required structures and processes. Because of this coherence the usual problems involved in realizing intended strategies, the problems of implementation, may be reduced. This is because the configurational approach identifies both 'ends', and to quite an extent it determines the 'means' as well.

By examining the different required states of the design parameters we have also identified areas of potential conflict, compromise and tension should a corporation wish to combine different modes of resource creation. For example, where the corporation is trying to provoke learning through controlling SBU financial performance, and it is simultaneously looking to reduce costs through centralizing some support functions there is likely to be tension and some resentment at SBU level. This may be focused on the requirement of SBUs to use centralized functions, thus constraining their autonomy, whilst



simultaneously the centre is holding the SBU executives accountable for profit performance.

Similarly, creative integration may be combined with encouraged learning, and although the prevailing culture would foster learning, it may well result in some confusion at SBU level about the extent to which executives can be held accountable for local SBU performance. Pro-yoked learning will not sit comfortably with any modes that require collaboration and sharing between SBUs, or between the centre and SBUs. Indeed, provoked learning is most likely to be the predominant realized strategy if it is combined with any other mode, because the pressures to hit short-term financials are likely to drive out any collaborative behaviour, or investments of time and energy in longer-term, more speculative activities.

However, we cannot rule out circumstances where the corporation is able to combine apparently conflicting modes. For example, the culture and values socialized into executives may encourage behaviours, which would deliver local SBU performance and broader corporate imperatives. In some sense any structural anomalies or tensions can be overcome if there is a collective will to work around them. It is likely that these corporate capabilities would be path-dependent, highly context specific and possibly causally ambiguous externally and internally. As such the ability to creatively combine modes in these socially complex ways would be a source of enduring corporate advantage.

### **Conclusion**

Using the dynamic capability perspective we have shown that RBV could be extended to apply to corporate-level strategy. The argument suggests that, where a multi-business corporation has a distinct centre, separated from SBU-level processes, the centre can only be justified on one of two grounds:

- either the centre provides resources; or
- the centre has processes that create resources (in Teece, Pisano and Shuen's (1997) terms, the centre possesses dynamic capabilities).

If the centre provides support services for the SBUs that can be delivered centrally at a lower cost or more effectively than they could be by the SBUs themselves, then these services are a resource for the SBUs. Alternatively, the centre enacts processes that result in resource creation within the SBUs. Putting it more starkly, for the centre to be valuable it must either be a resource, or create resources in SBUs. In order to create new resources the centre can essentially adopt six configurational strategies that may be mutually exclusive. This is because each strategy is likely to call for a particular combination of organizational structures and processes, which

raises questions about whether two or more resource creation strategies can coexist in the same structure. This issue could benefit from some further exploration. Expressed differently to create value corporations will have to choose the configuration that will allow them to develop a parenting advantage (Campbell, Goold and Alexander, 1995a). This choice will depend on the current characteristics of the corporation, the nature of the market place, the competition etc. The key though as argued by Campbell, Goold and Alexander (1995b) is maybe to have value-creation insights, which means a thorough understanding by the centre's managers based on their unique experience and knowledge about how to improve the performance of the SBUs.

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**Source: British Journal of Management, Volume 14, 2003**

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