SUMMARY

- The primary reason a firm uses a corporate-level strategy to become more diversified is to create additional value. Using a single-or dominant-business corporate-level strategy may be preferable to seeking a more diversified strategy, unless a corporation can develop economies of scope or financial economies between businesses, or unless it can obtain market power through additional levels of diversification. Economies of scope and market power are the main sources of value creation when the firm uses a corporate-level strategy to achieve moderate to high levels of diversification.
- The related diversification corporate-level strategy helps the firm create value by sharing activities or transferring competencies between different businesses in the company's portfolio.
- Sharing activities usually involves sharing tangible resources between businesses. Transferring core competencies involves transferring core competencies developed in one business to another business. It also may involve transferring competencies between the corporate headquarters office and a business unit.
- Sharing activities is usually associated with the related constrained diversification corporate-level strategy. Activity sharing is costly to implement and coordinate, may create unequal benefits for the divisions involved in the sharing, and can lead to fewer managerial risk-taking behaviors.
- Transferring core competencies is often associated with related linked (or mixed related and unrelated) diversification, although firms pursuing both sharing activities and transferring core competencies can also use the related linked strategy.
- Efficiently allocating resources or restructuring a target firm's assets and placing them under rigorous financial controls are two ways to accomplish successful unrelated diversification. Firms using the unrelated diversification strategy focus on creating financial economies to generate value.
- Diversification is sometimes pursued for value-neutral reasons. Incentives from tax and antitrust government policies, low performance, or uncertainties about future cash flow are examples of value-neutral reasons that firms choose to become more diversified.
- Managerial motives to diversify (including to increase compensation) can lead to overdiversification and a subsequent reduction in a firm's ability to create value. Evidence suggests, however, that many top-level executives seek to be good stewards of the firm's assets and avoid diversifying the firm in ways that destroy value.

- Managers need to consider their firm's internal organization and its external environment when making decisions about the optimum level of diversification for their company. Of course, internal resources are important determinants of the direction that diversification should take. However, conditions in the firm's external environment may facilitate additional levels of diversification, as might unexpected threats from competitors.

REVIEW QUESTIONS

1. What is corporate-level strategy and why is it important?
2. What are the different levels of diversification firms can pursue by using different corporate-level strategies?
3. What are three reasons firms choose to diversify their operations?
4. How do firms create value when using a related diversification strategy?
5. What are the two ways to obtain financial economies when using an unrelated diversification strategy?
6. What incentives and resources encourage diversification?
7. What motives might encourage managers to overdiversify their firm?

EXPERIENTIAL EXERCISES

EXERCISE 1: WHAT'S MY CORPORATE-LEVEL STRATEGY AND HOW DID I GET THIS WAY?

Your text defines corporate-level strategy as "actions a firm takes to gain a competitive advantage by selecting and managing a group of different businesses competing in different product markets." However, these actions are dynamic and longitudinal—they evolve over time. How did Ford Motor Company or IBM arrive at the corporate-level strategies they use today, and what are those strategies?

Part One

Form teams of four or five students and select a publicly traded firm, preferably one that has been in existence for a few decades. A comprehensive listing of all U.S. publicly traded firms may be found at the Investor Guide Web site (http://www.investorguide.com/stock-list.php) as well as links to each firm's homepage and other financial data. You will also want to access the firm's SEC filings, which could be available at your library or through the Securities and Exchange Commission's Web site at http://www.sec.gov/edgar.shtml.

Part Two

Complete a poster that can be displayed in class. Your poster should represent the firm and its evolution as far back in its history as you can get on one poster. The goal is to highlight the firm's beginnings, its acquisitions and divestiture activity, and its movement from one corporate-level strategy to another. You will need to do some extensive research on the firm to identify common linkages between operating units.

Be prepared to answer the following questions:

- How has the firm's corporate-level strategy evolved over time?
- What is the current corporate-level strategy and what links, if any, exist between operating units?
- Critique the current corporate-level strategy (e.g., too much diversification, too little, just right, and why).

EXERCISE 2: WHAT DOES THIS ANNOUNCEMENT MEAN?

Form 8K of the Securities and Exchange Commission is often called the current report due to the SEC requirement that companies must report or announce any major events that shareholders should know about. Many times the reporting is rather common such as the departure of an executive or changing of the firm's auditor. However, an important firm notification on their 8K filing is due to the announcement of a merger or acquisition which, as mentioned in the preceding chapter, has a significant impact on corporate level strategy.

This exercise requires teams of students to analyze 8K filings in the last 12 months. You can find many sources of this information but a good place to start is your university library. Contact your reference librarian for databases and financial analysis sites that will help you efficiently identify some good candidates. Teams are to pick one 8K filing that represents a firm's announced acquisition. It does not particularly matter if the acquisition was consummated, as the announcement in and of itself is sufficient. Once the team has identified the acquisition they must be prepared to at a minimum answer the following questions in the form of a presentation to the class:

1. Describe the acquiring firm in terms of its corporate level strategy.
2. Analyze the firm's press releases regarding the announced acquisition. How is the firm categorizing the event?
3. Describe the target in terms of its corporate level strategy.
4. Now analyze the announced acquisition in terms of its new corporate level strategy. How do you categorize the proposed entity? Does this match with press reports?
5. Rate the acquisition. Does this combination of two firms make sense in your team's opinion?

VIDEO CASE

THE ROAD TO DIVERSIFICATION
Barry Diller/Senior Executive/IAC

Barry Diller, once the chairman and CEO of Paramount Pictures and Fox and intrigued by interactive commerce, purchased QVC only to lose it in other business acquisition attempts, particularly his bid to purchase Paramount. Losing the bid to own Paramount as well as other organizations, Barry Diller purchased QVC competitor HSN and began an interactive conglomerate from financial services to matchmaking services such as Match.com. Along the way, Diller discovered that his many businesses related to one another and united all his brands under one corporate headquarters. Barry Diller, driven by vision and the ability to grasp new and difficult concepts, insists that IAC/InterActiveCorp is a brand-by-brand endless multiproduct company similar to Procter & Gamble.

Be prepared to discuss the following concepts and questions in class:

Concepts

- Corporate-level strategy
- Levels of diversification
- Value-creating diversification
- Operational and corporate relatedness
- Related and unrelated diversification
- Motivations to overdiversify

Questions

1. Describe Diller's corporate-level strategy.
2. Describe IAC's level of diversification.
3. What do you think was Diller's reason to diversify?
4. Is Diller's approach value-creating diversification? Why or why not?
5. Explain how IAC businesses and brands are related. Do they have related diversification?
6. Is Diller in a position to overdiversify?