European refocusing throughout the nineties

By

DANIELLE DEVOGELAER\
KULeuven
Naamsestraat 69
3000 Leuven, Belgium
E-mail: Danielle.Devogelaer@econ.kuleuven.ac.be
Tel: 32-16-32 69 16
Fax: 32-16-32 67 32

Abstract

This paper examines the refocusing activity of multi-business firms in the European Union. Theory and empirical data are offered to argue that diversification has diminished during the 90s, although not as vastly and widespread as we expected. In this paper, we will seek an explanation for the observation that most of the firms we study remain remarkably diversified. Therefore, we investigate the extent and determinants of diversification and refocusing across a sample of 277 leading European manufacturing firms. The results confirm that refocusing happens mainly at firm level. Above that, we refine the general 'refocusing' belief in distinguishing between conglomerate diversification and technology and market concentric diversification. We see that conglomerate diversification decreases throughout the 90s, but that the resource based technology and market concentric diversification are gaining momentum.

\ PhD Candidate in Strategy at KULeuven, Faculty of Economics and Applied Economics, Naamsestraat 69, 3000 Leuven, Belgium.

The author would like to thank Reinhilde Veugelers (KUL, CEPR, ULB, ECARES), Leo Sleuwaegen (KUL, VLGMS), Danielle Gilliot (KUL, VLIR) and Herman Daems (KUL, IESE) for helpful comments.

INTRODUCTION

The purpose of this paper is to present an empirical analysis of the extent and determinants of refocusing[i], using a unique data set covering 227 leading European firms over the period 1987-2000. Compared to the refocusing activity in the States, which continues to receive an extensive scrutiny in the popular press and some academic journals (Shleifer and Vishny, 1991; Cusatis, Miles & Woolridge, 1993; Lang & Stulz, 1994; Markides, 1995 a,b), corporate refocusing has attracted comparatively little academic interest outside the US. As Europe experiences the consequences of an enlarged competitive arena triggered by the Single Market Program (SMP), and hence has to act increasingly responsive to market demands, refocusing is now being placed on the agenda in a lot of European companies.

This paper begins from the position adopted by recent American researchers that during the 1980s and into the 90s a large number of US firms refocused or downscoped[ii] their activities (Liebeskind & Opler, 1995; Comment & Jarrell, 1995; Johnson, 1996). This view marks a change from the steady increase in diversification since the 50s and from the several theoretical justifications for conglomerate diversification that have been advanced. Many organizations have instead chosen to focus on related businesses, technologies or core competencies, where they can more readily add value across the businesses and generate synergy (Thompson, 2001).

This paper reports results from a large-scale investigation of refocusing activity outside the US. The project uses a unique data set of disaggregated firm level data from the Market Share Matrix (MSM) as described in Davies & Lyons (1996). This database is then used to construct measures of refocusing based alternatively upon the number equivalent of entropy, the number of diversified firms and the output share in secondary industries. At first sight this study looks like one of the many studies on refocusing, but what is been done in this paper is quite renewing. First, the impact of the SMP on refocusing decisions is being investigated. As the chosen period covers the start of the European integration process (1992) it is possible to see how refocusing has changed with the European integration and the Single Market Program (SMP). We will study refocusing before, during and after the integration. A second argument is that this paper proceeds with a *European* based study. Main driver is the observation that the literature that has emerged on refocusing is mainly American based research. This is valuable, but as Europe has its own specific regulations and business situations, it is highly advisable to gain a good grasp of the phenomenon from a European viewpoint. The MSM data base at hand will then reveal information on the European multi-business firm strategic decisions on refocusing.

1. THEORETICAL CONSIDERATIONS

There is increasing evidence in the business press as well as in the academic literature (Bhagat et al., 1990; Hoskisson and Turk, 1990; Shleifer and Vishny, 1991; Bowman & Singh, 1993; Cusatis, Miles & Woolridge, 1993; Lang & Stulz, 1994; Comment & Jarrell, 1995; Markides, 1995 a, b; Dennis et al., 1997) that during the 1980s many U.S. firms engaged in corporate refocusing. Markides (1990) estimates that at least 20 percent (and perhaps as many as 50 percent) of Fortune 500 firms refocused between 1980 and 1987. Markides (1990) further estimates that this type of restructuring occurred in only about 1 percent of the firms during the 1960s and 1970s. Although it is assumed that conglomerate firms are refocusing (Lee & Cooperman, 1989; Williams et al., 1988), Hoskisson and Johnson (1992) provide evidence that the majority of firms refocusing are not unrelated diversifiers; rather, they are firms that combine related and unrelated units in their portfolios. Furthermore, Markides (1992b) presents evidence to suggest that refocusing is equally likely among the Fortune 400-500 as it is with the Fortune 100. Corporate refocusing appears to be a widespread phenomenon that is not limited to very large firms[iii]. In concluding, we can state that corporate refocusing has become a commonplace strategy in the US since the early 1980s. What we want to determine then is whether Europe follows a similar refocusing pattern. More in detail, we want to investigate whether the advent of Europe 1992 incited firms to go "back to basics".

2. Hypotheses

In this study, the implications of market integration for the diversification of firms in a European context are being investigated. In the theoretical literature, this has received scant attention. Nevertheless, the hypothesis of "return to core business" has been a popular theme of the corporate strategy literature, as a result of widespread empirical evidence in the US. In this stream of literature it is proven that although a diversification strategy has its merits[iv], it also has major drawbacks. Increasing diversification can lead to a loss of efficiency, competitiveness and most ominous of all, the ability to manage a diverse collection of unrelated products and services. Over time, rapid expansion of a company's product line destroys its competitive ability. Markides (1992b, 1995) found that high levels of diversification result in inefficiencies that may lead to declines in performance. For many companies in many industries that point is now being reached. What we are observing today is the opposite phenomenon. Instead of expansion, companies are getting back to basics. Companies are "refocusing[v]".

One of the drivers of refocusing is the emergence of a more efficient market for corporate control. This follows the general belief that during the 60s and the 70s, managers may have acquired assets in business areas unrelated to the core businesses and competencies of the firm in order to increase their personal wealth or their job security (Marris, 1964; Amihud and Lev, 1981). Although diversification may provide gains for managers, firm value may be destroyed because of lack of economies of scope between unrelated lines of business (Amihud & Lev, 1981); because of possible overpayment in

acquisitions (Morck, Shleifer and Vishny, 1990); and through inefficient investment in, and cross-subsidization of, the ongoing businesses of the firm (Bhide, 1990; Berger and Ofek, 1995). With the increasing efficiency and transparency of external capital markets in the 80s and the appearance of financial high-tech instruments like junk bonds these inflated firms possibly fell victim to hostile takeovers or corporate raiders who make their living through "bust-ups[vi]". This incited highly diversified firms to critically analyze their business portfolios themselves before others had the opportunity to 'bust up' or dismantle their organisation.

Alternative explanations are that firms have become over-diversified to satisfy managerial hubris, and return to the core is the consequence of a tighter control over managers. From a different perspective, Teece, Rumelt, Dosi and Winter (1994) propose a theory which encompasses elements of the resource view of diversification (Penrose, 1959, Wernerfelt, 1984) and of evolutionary economics (Nelson and Winter, 1982). The firm's choice of an optimal strategy (e.g. coherent diversification, conglomerate diversification, specialisation, vertical integration, etc.) depends on a set of firm-specific factors – e.g. the firm's technological and organisational capabilities – as well as on a set of characteristics of the "selection environment". The theory predicts that if the competitive pressure in the selection environment becomes tougher, as is the case in the hypercompetitive[vii] environment of nowadays, the firm ought to re-focus to ensure survival. This hypercompetition or intense state of global competition forces holdings to concentrate on a few industries where they hold a clear global competitive advantage[viii] and abandon unprofitable side-activities, often taken up in the portfolio during times when it was still fashionable to diversify. Veugelers et al. (2001) confirm that low or related diversifiers appear better equipped to compete in a larger and more integrated market. Above that, Veugelers et al. (2001) found that in industries where either advertising or R&D expenditures are important strategic weapons refocusing was significant. This suggests that in these very sectors the competitive pressure has induced firms to refocus towards the core business and to abandon non-leading activities.

Although this observation is in favour of an industry effect of refocusing, Markides (1995) and Collis & Montgomery (1997) show that at any given time, firms are at different places on the path of diversified expansion. Some are just starting out, moving away from their initial businesses. Others are considerably further along, with sets of businesses that may span many industries. Still others are restructuring and divesting businesses. This leads us to believe that refocusing might also be firm specific, and less dependent on the industries in which the firm participates. These points lead to the first hypotheses:

Hypothesis 1*: The advent of Europe 1992 has incited the 'return to the core' movement among leading European firms, although with some delay.*

***Hypothesis 2**: Firm effects are more important than industry effects in explaining refocusing.*

For the third hypothesis, we distinguish four different forms of diversification, namely technology concentric diversification, market concentric, conglomerate and geographical diversification. *Technology concentric* diversification is a diversification strategy whereby the same technology is used throughout the different operations, but each operation has its own distinct market, whereas *market concentric* diversifiers have the same target market ('similarity in customer groups', Farjoun, 1998), but their activities use different technologies (Kitching, 1972). The technology concentric and market concentric diversification forms largely coincide with what Robins and Wiersema (1995) term 'interrelationships among businesses'. *Conglomerate diversification* is coined whenever a mother company acquires or internally develops unrelated business activities. *Geographical diversification* is a diversification strategy whereby a company is present in more than one country (Davies et al., 2001). In fact, a mother company diversifies itself by having her operations spread out in several countries. It is possible to combine one or more of these diversification forms, for example a company can pursue at the same time geographical and conglomerate diversification. Some combination forms are not possible though, for example a company cannot be simultaneously market concentric and conglomerate diversified.

Another categorisation that is popular in the literature is the difference between related and unrelated diversification. Related diversification is pursued if the firm diversifies in related lines of business, technology or core competence. Unrelated diversification is an act of diversification where the company management decides to engage in businesses further afield from the core business, like for example a firm that is active in cars and decides to diversify in publishing (Fiat). Our previous classification is consistent with this one in that technology concentric and market concentric diversification can be seen as related diversification, whereas conglomerate is unrelated diversification. Geographical diversification can in fact be both (see also Davies et al., 2001). This argument suggests a third hypothesis:

***Hypothesis 3**: Refocusing mainly concerns conglomerate or unrelated diversification that is being reversed. Market concentric and technology concentric diversification forms are not disappearing.*

3. DATA AND METHODS

3.1. Data and variables

For this study, we use the MSM, or Market Share Matrix as described in Davies & Lyons (1996). The basic idea of this matrix is to identify a set of "leading firms", and disaggregate their turnover data,

extracted from individual company accounts, using a common industrial classification scheme at a meaningful level of disaggregation. A firm qualifies as a "leader", if it is one of the five largest EU producers in at least one manufacturing industry. For every such firm, the matrix includes:

- estimates of its EU turnover (sourced from within the EU, measured in EUROs), in each industry in which it operates (not only in those where it is a "leader"), and
- disaggregated into the turnovers, in that industry, sourced from production in each member state.

A three-dimensional matrix built on these principles can provide estimates of various structural dimensions. *For any given firm*, it reveals the extent of its diversification across industries. Various dimensions can be constructed, such as the number of sectors in which the firm is active, the importance of production outside the main sector of activity or the weighted sum of shares of production across different sectors (entropy- index).

3.2. Methodology

First descriptive statistics will be presented in section 4, followed by the testing and discussion of our hypotheses.

4. RESULTS

A comparison of the basic dimensions of the time comparable matrices 1987 till 2000 provides a quick guide to the major changes in firm diversification over this period. The evidence suggests that EU firms have reduced their diversification at the expense of industries in which they are not leaders (non-leading diversification). Reduction in diversification has particularly occurred between 1993 and 1997, after the completion of the Single Market Program, and not between 1987 and 1993 when the removal of non-tariff barriers was in progress and most expected to exert its influence over corporate restructuring. This non-linearity suggests that the de-diversification process may have continued in the years after 1997. This is also what we see in table 1: diversification in 2000 has further decreased.

Table 1 - Changes in the matrix between 1987, 1993, 1997 and 2000

	1987	**1993**	**1997**	**2000**
Number of industries	67	67	67	
Number of firms	223	218	223	
Number of diversified firms	175	176	170	
Number of entries	**1079**	**1016**	**810**	
of which:				
Leading	*335*	*335*	*335*	

Non-leading	*744*	*681*	*475*	
Number of entries per firm	**4.84**	**4.66**	**3.63**	
Of which:				
Leading	*1.50*	*1.54*	*1.50*	
Non-leading	*3.34*	*3.12*	*2.13*	

The tables 2 and 3 present the distributions of diversification indices across firms, by comparing the quartiles and extreme deciles of the distributions of NE and R (with firms ranked by diversification). The de-diversification process envisaged in the previous section is confirmed by the changes in means calculated for 2-digit industries (Table 2).

Table 2 - Distribution of diversification across firms, 1987-93-97-2000

(2-digit)

	Number equivalent of Entropy					**Output share in secondary industries**				
	1987	*1993*	*1997*	*2000*	*Change*	*1987*	*1993*	*1997*	*2000*	*Change*
Arithmetic mean values of D										
All Matrix Firms	1.77	1.79	1.60			0.16	0.18	0.14		
Std. Dev.	1.09	1.09	0.86			0.19	0.21	0.19		
Distribution of D across firms										
Decile 9	3.11	3.38	2.67			0.46	0.51	0.46		
Quartile 3	2.18	2.14	1.88			0.28	0.31	0.23		
Median	1.30	1.31	1.26			0.07	0.07	0.06		
Quartile 1	1.00	1.00	1.00			0.00	0.00	0.00		
Decile 1	1.00	1.00	1.00			0.00	0.00	0.00		

Table3 - Distribution of diversification across firms, 1987-93-97-2000

(3-digit)

	Number equivalent of Entropy					**Output share in secondary industries**				
	1987	*1993*	*1997*	*2000*	*Change*	*1987*	*1993*	*1997*	*2000*	*Change*
Arithmetic mean values of D										
All Matrix Firms	2.62	2.60	2.25			0.27	0.29	0.25		
Std. Dev.	*1.95*	*1.72*	*1.44*			*0.24*	*0.24*	*0.23*		
Distribution of D across firms										
Decile 9	4.74	4.77	4.33			0.59	0.64	0.61		
Quartile 3	3.23	3.37	2.72			0.46	0.49	0.43		
Median	2.05	2.03	1.79			0.25	0.30	0.22		
Quartile 1	1.20	1.26	1.13			0.04	0.06	0.03		

Decile 1	1.00	1.00	1.00			0.00	0.00	0.00		

Looking through the indices in Table 2, we find that highly diversified firms decreased diversification more substantially, although the trend is non-linear, with firms displaying first an increase and then a reduction in the mean values. At this level of aggregation, these preliminary findings are nonetheless suggestive of rationalisations that eliminated operations in unrelated or marginal industries.

In Tables 2 and 3 we report summary statistics on 2-digit and 3-digit diversification indices[ix]. Comparing 3-digit and 2-digit industries allows us to provide some evidence as to what extent EU leaders' diversification may be broadly defined as "related" or "unrelated" and to measure whether the apparent re-focusing of operations has occurred via divestment from unrelated activities or if, in contrast, the extent of restructuring led firms to exit from related activities as well[x].

Finally, by comparing tables 2 and 3, it is possible to notice that 3 digit diversification has decreased relatively more than 2 digit diversification, suggesting that firms have exited from both related (i.e. within the same 2 digit industry) and unrelated (i.e. in different 2 digit industries) activities. In general, the overall impression of a remarkable return to the core is somewhat weakened by these findings. Firms have readjusted their corporate structure around a lower number of industries, but have not refocused the output share in their primary industries in any remarkable way. In other words, instead of a *return to core business*, we are documenting a *return to core businesses*.

In what follows, we will dig deeper into these findings and use a better working definition for 'relatedness'. Based on this definition and on the article of Robins & Wiersema (1995) we try to proof that market concentric and technology concentric diversification are gaining momentum. We will also establish whether firm or industry effects prevail in the decision to refocus.

5. SUMMARY AND CONCLUSIONS

6. REFERENCES

Alexander, G. J., Benson, P. G., and Kampmeyer, J. M. (1984). "Investigating the valuation effects of announcements of voluntary corporate selloffs." Journal of Finance, 39, 503-517.

Bass, F. M. (1973). "Market structure and profitability - Analysis of the appropriateness of pooling cross-sectional data." Institute for Research in the Behavorial, Economic and Management Sciences, Krannert Graduate School of Management, Purdue University, West Lafayette, Ind., Paper No. 242.

Bass, F. M., Cattin, P., and Wittink, D. K. (1978). "Firm effects and industry effects in the analysis of market structure and profitability." Journal of Marketing Research, 15(2), 3-10.

Baysinger, B. D. and Hoskisson, R. E. (1989). "Diversification strategy and R&D intensity in large multiproduct firms." Academy of Management Journal, 32, 310-332.

Berger, P. G. and Ofek, E. (1995). "Diversification's effect on firm value." Journal of Financial Economics, 37, 39-65.

Bergh, D. D. and Holbein, G. F. (1997). "Assessment and redirection of longitudinal analysis: demonstration with a study of the diversification and divestiture relationship." Strategic Management Journal, 18(7), 557-571.

Besanko, D., Dranove, D., and Shanley, M. (1996). Economics of Strategy, John Wiley & Sons, Inc. New York.

Bhide, A. (1990). "Reversing corporate diversification." Journal of Applied Corporate Finance , 3, 70-81.

Bowman, Edward H., and Singh, H. (1993). "Corporate restructuring: reconfiguring the firm." Strategic Management Journal, 14, 5-14.

Bradley, M., Desai, A., and Kim, E. H. (1988). "Synergistic gains from corporate acquisitions and their division between the stockholders of target and acquiring firms." Journal of Financial Economics,

21, 3-40.

Brealey, R. A. and Myers, S. C. (2000). Principles of corporate finance, Irwin/McGraw-Hill Boston, Boston (Mass.).

Bronars, S. G. and Deere, D. R. (1991). "The threat of unionization, the use of debt, and the preservation of shareholder wealth." Quarterly Journal of Economics, 231-253.

Brush, T. H. and Bromiley, P. (1997). "What does a small corporate effect mean? A variance components simulation of corporate and business effects." Strategic Management Journal, 18, 825-835.

Butz, D. Free cash flow theory without the cash flow emphasis. Departement of Economics, University of California LA CA. 1990.

Campbell, A. and Goold, M. (1998). Synergy (Why Links Between Business Units So Often Fail And How To Make Them Work) , John Wiley and Sons Ltd.

Campbell, A., Goold, M., and Alexander, M. (1995). "Corporate strategy: the quest for parenting advantage." Harvard Business Review, 120-132.

Chang, S.-J. (1996). "An evolutionary perspective on diversification and corporate restructuring: entry, exit, and economic performance during 1981-89." Strategic Management Journal, 17, 587-611.

Chang, S.-J. and Singh, H. (2000). "Corporate and industry effects on business unit competitive position." Strategic Management Journal, 21, 739-752.

Collis, D. J. and Montgomery, C. A. (1997). Corporate Strategy: Resources and the Scope of the Firm, McGraw-Hill, Chicago.

Comment, R. and Jarrell, G. A. (1995). "Corporate focus and stock returns." Journal of Financial Economics, 37, 67-87.

Daley, L., Mehrotra, V., and Sivakumar, R. (1997). "Corporate focus and value creation: evidence from spin-offs." Journal of Financial Economics, 45, 257-281.

Davies, S., Rondi, L., and Sembenelli, A. "S.E.M. and the changing structure of EU manufacturing, 1987-1993." CERIS Working paper ,(N.5/1998).

Davies, S. W. and Lyons, B. R. (1996). Industrial organisation in the European Union: structure, strategy, and the competitive mechanism, Clarendon Press, Oxford.

Duhaime, I. M. and Grant, J. H. (1984). "Factors influencing divestment decision-making: Evidence from a field study." Strategic Management Journal, 5, 301-318.

Farjoun, M. (1998). "The independent and joint effects of the skill and physical bases of relatedness in diversification." Strategic Management Journal, 19, 611-630.

Gertner, R., Powers, E., and Scharfstein, D. "Learning about internal capital markets from corporate spinoffs." NBER.

Gilson, S., Healy, P., Noe, C., and Palepu, K. (2000). "Analyst specialization and conglomerate stock break-ups." Harvard University, working paper.

Grossman, O. and Hart, S. (1986). "Corporate financial structure and managerial incentives." The economics of information and uncertainty, University of Chicago Press, Chicago.

Hagel III, J. and Singer, M. (1999). "Unbundling the corporation." Harvard Business Review, 133-141.

Hansen, G. S. and Wernerfelt, B. (1989). "Determinants of firm performance: the relative importance of economic and organizational factors." Strategic Management Journal, 10, 399-411.

Hatfield, D. E., Liebeskind, J. P., and Opler, T. C. (1996). "The effects of corporate restructuring on aggregate industry specialization." Strategic Management Journal, 17, 55-72.

Haynes, M., Thompson, S., and Wright, M. (2000). "The determinants of corporate divestment in the UK." Discussion Papers in Economics, University of Nottingham, 00/15.

Hill, C. W. L. and Hoskisson, R. E. (1987). "Strategy and structure in the multiproduct firm." Academy of Management Review, 12, 331-341.

Hoskisson, R. E. and Hitt, M. A. (1990). "Antecedents and performance outcomes of diversification: a review and critique of theoretical perspectives." Journal of Management, 16, 461-509.

Hoskisson, R. E. and Hitt, M. A. (1994). Downscoping: how to tame the diversified firm, Oxford University Press, New York.

Hoskisson, R. E. and Johnson, R. A. (1992). "Corporate restructuring and strategic change: The effect on diversification strategy and R&D intensity." Strategic Management Journal, 13, 625-634.

Hoskisson, R. E., Johnson, R. A., and Moesel, D. D. (1994). "Corporate divestiture intensity in restructuring firms: effects of governance, strategy, and performance." Academy of Management Journal, 37(5), 1207-1251.

Jain, P. C. (1985). "The effect of voluntary sell-off announcements on shareholder wealth." Journal of Finance, 40, 209-224.

Jensen, M. (1989). "Eclipse of the public corporation." Harvard Business Review, 61-74.

Jensen, M. C. (1986). "Agency costs of free cash flow, corporate finance and takeovers." American Economic Review, 76, 323-329.

Jensen, M. C. (1993). "The modern industrial revolution, exit, and the failure of internal control systems." Journal of Finance, 48, 831-880.

Jensen, M. C. and Ruback, R. S. (1983). "The market for corporate control: scientific evidence." Journal of Financial Economics, 11, 5-50.

Johnson, R. A., Hoskisson, R. E., and Hitt, M. A. (1993). "Board of director involvement in restructuring: The effects of board versus managerial controls and characteristics." Strategic Management Journal, 14 (Special issue), 33-50.

Johnson, R. A. (1996). "Antecedents and outcomes of corporate refocusing." Journal of Management, 22(3), 439-484.

Kaiser, K. (1995). "Value creation through corporate restructuring: European divestitures." European Management Journal, 13(2).

Kose, J., Lang, L. H. P., and Netter, J. (1992). "The voluntary restructuring of large firms in response to performance decline." The Journal of Finance, XLVII(3), 891-917.

Kumar, K. B., Rajan, R. G., and Zingales, L. What determines firm size? National Bureau of Economic Research. 1999.

Lang, L. H. P. and Stulz, R. M. (1994). "Tobin's q, corporate diversification, and firm performance." Journal of Political Economy, 102(6), 1248-1280.

Liebeskind, J. P. and Opler, T. C. The causes of corporate refocusing: evidence from the 1980s. UCLA working paper. 1995.

Markides, C. C. (1992a). "Consequences of corporate refocusing: Ex ante evidence." Academy of Management Journal, 35, 398-412.

Markides, C. C. (1992b). "The economic characteristics of de-diversifying firms." British Journal of Management , 3, 91-100.

Markides, C. and Singh, H. (1997). "Corporate restructuring: a symptom of poor governance or a solution to past managerial mistakes? " European Management Journal, 15(3), 213-219.

Markides, C. C. (1993). "Corporate refocusing." Business Strategy Review.

Markides, C. C. (1995). Diversification, refocusing, and economic performance, MIT Press.

Markides, C. C. (1995). "Diversification, restructuring and economic performance." Strategic Management Journal, 16, 101-118.

Meeks, G. (1977). "Disappointing marriage: a study of the gains from merger." Department of Applied Economics, University of Cambridge.

Montgomery, C. A. (1994). "Corporate diversification." Journal of Economic Perspectives, 8(3), 163-179.

Montgomery, C. A. (1982). "The measurement of firm diversification: some new empirical evidence ." Academy of Management Journal, 25(2), 299-307.

Montgomery, C. A. (1985). "Product-market diversification and market power." Academy of Management Journal, 28(4), 789-798.

Montgomery, C. A. and Thomas, A. R. (1988). "Divestment: Motives and gains." Strategic Management Journal, 9, 93-97.

Montgomery, C. A. and Wernerfelt, B. (1988). "Diversification, Ricardian rents, and Tobin's q." RAND Journal of Economics, 19(4), 623-632.

Morck, R., Shleifer, A., and Vishny, R. W. (1990). "Do managerial objectives drive bad acquisitions?" Journal of Finance, 45, 31-48.

Paulus, J. D. and Gay, R. S. (1987). "Mergers are helping U.S. productivity." Challenge , 54-57.

Porter, M. E. (1987). "From competitive advantage to corporate strategy." Harvard Business Review, 65(3), 43-59.

Rajan, R., Servaes, H., and Zingales, L. The cost of diversity: the diversification discount and inefficient investment. National Bureau of Economic Research. 1998.

Ravenscraft, D. J. and Scherer, F. M. (1987). "Mergers, sell-offs and economic efficiency." The Brookings Institution, Washington, DC.

Robins, J. and Wiersema, M. F. (1995). "A resource-based approach to the multibusiness firm: empirical analysis of portfolio interrrelationships and corporate financial performance." Strategic Management Journal, 16(4), 277-299.

Roll, R. (1986). "The hubris hypothesis of corporate takeovers." Journal of Business, 59, 197-216.

Sadtler, D. (1997). Breakup!: How Companies Use Spin-Offs To Gain Focus And Grow Strong , Free Press.

Schmalensee, R. (1985). "Do markets differ much? " American Economic Review, 75, 341-351.

Shleifer, A. and Vishny, R. W. (1991). "Takeovers in the 60's and the 80's: evidence and implications." Strategic Management Journal, 12(Special issue), 51-60.

Stonham, P. (1997). "Demergers and the Hanson experience, Part one." European Management Journal, 15(3).

Wernerfelt, B. and Montgomery, C. A. (1988). "Tobin's q and the importance of focus in firm performance." American Economic Review, 78(1), 246-250.

---

[i] Refocusing means reducing the diversification level (and likely the size) of a multi-business company. A multi-business company is a company that operates several activities in several geographic markets and/or industries (Daems, 1980). Markides coins the term to mean the company decision to reduce the scope of its activities in order to concentrate on the "core" business (i.e., to reduce its diversification), Markides, Constantinos C. *Diversification, refocusing and economic performance*, MIT Press, 1995.

[ii] Downscoping is a term recently coined to describe programs of strategic divestiture (Hoskisson & Hitt, 1994). Such activity is thus distinguished from downsizing or strategically laying off employees during times of economic stress (Worrell, Davidson & Sharma, 1991). While downsizing can increase short-term efficiency, Hoskisson & Hitt (1994) argue that downscoping is preferable in that it enables firms to strategically refocus on their core businesses and to regain strategic control of their operations.

[iii] In a recent study on the determinants of industrial concentration, market integration and efficiency in the European Union, Veugelers et al. (2001) find that medium-large European firms (ranked 51 to 100 in a size ranking across the EU) appear to have de-diversified more substantially than the largest top 50 firms.

[iv] Diversification can bring three types of benefits, namely economic (greater market power of a large diversified firm), financial (use of an efficient internal capital market) and strategic benefits (synergy effects as well as growth benefits).

[v] Liebeskind and Opler (1993) and Hatfield (1993) find that most refocusing during the 1980s took place among more diversified firms; more focused firms continued to diversify, producing a mean-reverting pattern in diversification (see also Veugelers et al., 2001).

[vi] A bust-up is an action in which the assets of the firm are completely dismantled and/or change ownership in more than one transaction (Seth & Easterwood, 1993).

[vii] Hypercompetition is a term that points to an increased state of competition as markets become more global and innovative, R. A. D'Aveni. *Coping with Hypercompetition: Utilizing the new 7S's framework*, Academy of Management Executive, 1995, Vol. 9 No. 3 pp.45-57.

[viii] A competitive advantage is created and sustained if the rentability of the firm exceeds the cost of capital for a prolonged period of time. A firm's value is based on its ability to sustain a competitive advantage relative to its

rivals, either by producing at lower cost, or by creating more valuable (differentiated) products (Rumelt, 1984; Porter, 1985; Grant, 1989).

[ix] The original 67 industries, roughly corresponding to a 3 digit classification, have been grouped into 19 macro aggregates, roughly corresponding to a 2 digit classification.

[x] Underlying this view is the assumption that the notion of relatedness breaks down shifting from the 3-digit to the 2-digit levels. We reckon this is a fairly simplistic assumption.