Session 10: Focus vs Diversification

Two Growth Strategies

• Focus
  – Keep a focus on present markets

• Diversification
  – Explore new markets with new products
    1. Related
    2. Unrelated

Focus Strategy

• Concentrate on one part of the market or product line.

  - Avoid strategy dilution or distraction
  - Reduce competitive pressures
  - Provide positioning strategy
  - Compete with Limited resources
  - Bypass competitor assets/competencies

Focus Strategy (cont’d)

• Although the payoff of a small niche may be less than that of a large growing market, the competition may often also be less intense.

• However, a focus strategy naturally limits the potential business. Therefore, profitable sales may be missed.

• It is crucial whether a focus strategy involves meaningful Sustainable Competitive Advantages.

Variations of Focus Strategies

• Focusing the product line in order to enhance technical superiority

• Targeting a niche

• Focusing limited geographic area

Growth Strategies under a Focus

Keep a Focus on present markets

1. With present products
   - increase market share
   - Increase product usage

2. With new products
   - add product features
   - Develop a new-generation product for the same market
Diversification

- Approach new markets with new products

- Two types
  - Related diversification
    - The new business area has meaningful commonalities with the core business.
  - Unrelated diversification
    - Unrelated diversification lacks enough commonalities.
    - The objectives are therefore mainly financial, to generate profit streams that are either larger, less uncertain, or more stable that they would be otherwise.

Motivations for Diversification

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<tr>
<th>Related Diversification</th>
<th>Unrelated Diversification</th>
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<tr>
<td>Exchange or share assets or competencies by exploiting</td>
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  - Strong brand name |
  - Strong marketing skills |
  - Strong distribution capacity |
  - Manufacturing skills |
  - R&D capability |
| Manage and allocate cash flow |
| Enter business areas with high ROI prospects |
| Refocus a firm |
| Reduce risk by operating in multiple product markets |
| Vertical integration |

Performance of Diversified Firms

- In the 1960s and early 1970s, a wave of acquisitions took place.
  - Typically, friendly mergers involving unrelated diversification.
  - The fraction of single-business companies in the Fortune 500 dropped from 23% to 15% from 1959 to 1969.
  - The percentage of conglomerates with no dominant business rose from 7.3% to 19%.

- Were they successful?

Performance of Diversified Firms (cont’d)

- From 1950 to 1980, among 2021 acquisitions made in new industries by 33 large, diversified U.S. companies, More than half were divested by 1986 (Porter, HBR, 1987)
- Among 931 unrelated diversifications, 74% were divested (Porter, HBR, 1987).
- In a sample of Fortune 500 firms, the related diversifications were highest in performance, followed by the less related diversification and finally the unrelated diversification (Rumelt, Strategic Management Journal, 1982)
- 450 related diversifications had a significantly higher ROA than 20 unrelated diversification firms (Simmonds, Strategic Management Journal 1990)

Risk of Unrelated Diversification

- Unrelated diversification, if unsuccessful, may actually damage the original core business by diverting attention and resources from it.
- Managing the new business may be difficult because it requires different assets and resources.

Issues in Diversification

- The important issue in diversification is how to achieve synergy. In unrelated diversifications, there is no possibility of synergy.
- Successful diversification requires a common core or unity represented by common markets, technology, or production processes. Without such unity, diversification is unlikely to work.