**Session 07 BUSA 7800 - Strategic Management Chapters 06 & 07**

Learning Outcomes

At the end of this session you should be able to:

* 1. Explain how firms can use unrelated diversification to achieve synergistic benefits through corporate restructuring, parenting and portfolio analysis.
  2. Compare the various means of engaging in diversification: mergers and acquisitions, strategic alliances and joint ventures and internal development.
  3. Explain how a real option can reduce the asymmetric information problem when acquiring another business.
  4. Describe several reasons for the failure of many diversification efforts.
  5. Describe several motivations for firms expanding into international markets.

**Chapter 6: Corporate-Level Strategy**

**I. Unrelated Diversification: Financial Synergies and Parenting**

What are the two sources of synergy with unrelated diversification?

1. Corporate Parenting and Restructuring
2. Portfolio Management

A. **Corporate Parenting and Restructuring**

i. Parenting

How can parent companies create value through management expertise?

* **Improve plans and budgets**
* **competent central funciton such as legal, financing**

ii. Restructuring

What types of companies are corporate offices trying to find?

* Under performing firms
* firms on the edge of big, positie change

What happens under asset restructuring?

* Selling off productive assets or business lines

How does capital restructuring work?

* Changing the debt to equity mix (adding more debt in a buy out)

What typically occurs during management restructuring?

* Can borrow at a lower interest rate
* changes to the top management team
* decrease in the number of middle management
* changes in the org. Structure becomes more flat
* changing the rewatds to the org. Reflect meeting more sshort-term goals

**B. Portfolio Management**

When is corporate portfolio analysis used?

* When a firm’s corporate strategy involves a number of businesses

What is the purpose of the Boston Consulting group (BCG) matrix?

* To identify which businesses have high potential and which are a drain on resources

How is the matrix put together?

* Expected growth rate on the Y-axis and market share on the x-axis

What are the strategic implications of each category in the BCG matrix?

1. Cash cow low expected growth and high market share. Little reinvestment send most of your cash into stars
2. Dogs
3. Question Marks high expected growth but low market share

invest to see if I can become a star

if not divest

1. Stars hobby businesses

What are a few of the major drawbacks of the portfolio model?

**C. Caveat: Is Risk Reduction a Viable Goal of Diversification?**

Compare the shareholders ability to diversify with the manager's ability to diversify.

* Fast, low transaction fees → they can instead contact a broker and stocks of other firms
* difficult and time consuming since the manager would have to enter businesses to offset the risks of their current businesses

What is the benefit of producing another product to smooth out seasonal sales fluctuation?

**II. The Means to Achieve Diversification**

* 1. **Mergers and Acquisition (M&A)**

What's the difference between a merger and an acquisition?

* Merger:Two firms of about the same size agree to form one company
* Acquisition: a larger firm buys a smaller one

i. Motivations

What are the motivations that firms have to acquire another firm?

* 1. Speed → fastest way into another businesses
  2. Gaining valuable resources → gaining IP
  3. Scale to respond to external pressures → eq your rivals are all merging together and you need to get big to compete
  4. Synergy → make better use of each other resources
  5. Entering New Markets → geographic, target

ii. Limitations

Why do buyers frequently pay premiums (overpay) to acquire a business?

* Asyn information
* who knows more about the business the buyer or seller
* seller want to sell high if they take your bid

How can a manager's ego get in the way of an acquisition?

* Buying another business is the fastest way to be a big player in the industry

How can cultural issues be a limitation to a successful M&A?

* The org culture determines how firms approach issues
* you may have a culture clash if a firm w/ an aggressive culture buys another w/ a cautions culture

**B. Strategic Alliances and Joint Ventures**

How does a strategic alliance work?

What are the pros and cons of a strategic alliance?

When are alliances likely to be longer lasting?

* When they involve collaborating w suppliers or distribution allies selling to the same end user
* new opp for

What are some of the common causes for alliances to fail?

* Diverging objectives and priorities
* inability to work well together

What is the danger of relying on alliances for essential resources and capabilities?

* Can become dependent on the other firm for essential expertise and capability
* you are in trouble if they leave the alliance

What makes a joint venture different than a typical strategic alliance?

* A type of strategic alliance where two or more firms agree to set up an independent company that they own

Why would firms set up a joint venture?

* It may be the only way to enter a foreign market
* want to tenter a market that is outside your area of expertise

What is internal development?

* Start up and develop the resources needed to enter a new business on their own

What are the pros and cons of internal development?

**III. Real Options Analysis: A Useful Tool**

How does a real option work?

* But not the obligation to enter into a business transaction

How does the real option reduce the asymmetric information problem when it comes to acquiring a business?

**IV. How Managerial Motives Can Erode Value Creation**

1. **Growth for Growth's Sake**

Why would a CEO choose to grow for growth's sake?

* More prestige, more income

**B. Egotism**

How can a healthy ego be a double-edged sword for CEOs?

**C. Anti-takeover Tactics**

How does an unfriendly or hostile takeover occur?

* A firm starts to buy up shares of a target firm in hopes of gaining full control

How does a poison pill work?

* Usually triggered when an aggressor acquires over 20% of the stock
* new shares are sold at a discount (except to the aggressor) to dilute ownership of the aggressive

How does having a staggered board slowdown the ability of an aggressor from taking over the board?

**Next Session:**

* Mid-term Exam
* Chapter 7 – International Strategy: Creating Value in Global Markets