



Faculty of Business and Law

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GSBS6481 International Business Strategy

Week 7: Diversification and Restructuring

Dr. Hao Tan



Reference & Readings

- Peng, Mike W (2021), *Global Strategy*, 5th ed. USA: Cengage Learning.
 - Chapter 9 Diversifying, Acquiring and Restructuring
 - Loredana, E 2017. 'The use of Ansoff matrix in the field of Business' (This article is in week 7 course materials)
 - Tan, H. 2022. Declining industries in emerging economies and firms' strategies. (This article is in week 7 course materials)

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Key concepts

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- Corporate-level strategy versus business-level strategy
- Product-related diversification
- Product-unrelated diversification
- Diversification premium
- Geographic diversification
- Conglomeration
- Divestiture



Outline

- Diversifying
 - Product diversification
 - Geographic diversification
 - Three perspectives on diversification
 - Evolution of the scope of the firm
- Merge & Acquisition
- Restructuring and divestiture
- Case study

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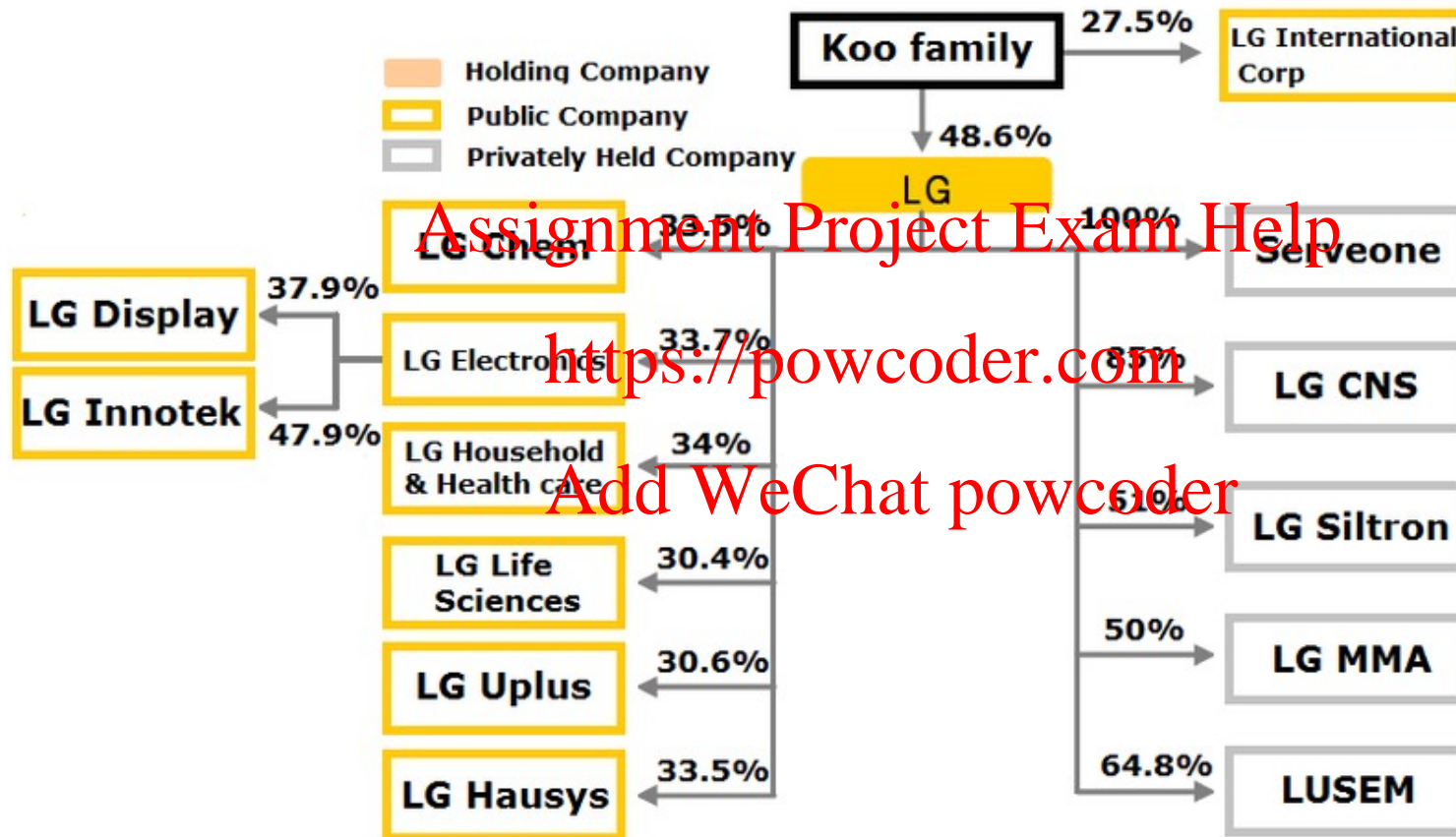


Diversification

Opening Case: How did Korean *Chaebol* emerge

- “My father and I started a cosmetic cream factory in the late 1940s. At that time, no company could supply us with plastic caps of adequate quality for cream jars, so we had to start a plastic business. Plastic caps alone were not sufficient to run the plastic molding plant, so we added combs, toothbrushes, and soap boxes. This plastics business also led us to manufacture electric fan blades and telephone cases, which in turn led us to manufacture electrical and electronic products and telecommunications equipment. The plastics business also took us into oil refining, which needed a tanker shipping company. The oil refining company alone was paying an insurance premium amounting to more than half the total revenue of the then largest insurance company in Korea. Thus, an insurance company was started.

A quote from the Chairman of LG





Product diversification

- Product-related diversification

- Enter into new product markets and / or business activities that are related to a firm's existing markets and /or activities
- Common technologies, marketing and manufacturing

- Product-unrelated diversification

- no obvious product-related connections
- those firms are also called conglomerates

Examples?



Benefits and costs of product diversification

- Benefits?
 - ..of Product-related diversification?
 - Economies of scale – derived from operational synergy
 - ..of the Product Unrelated diversification?
 - Economies of scope – derived from financial synergy
- Costs?
- Diversification premium and diversification discount

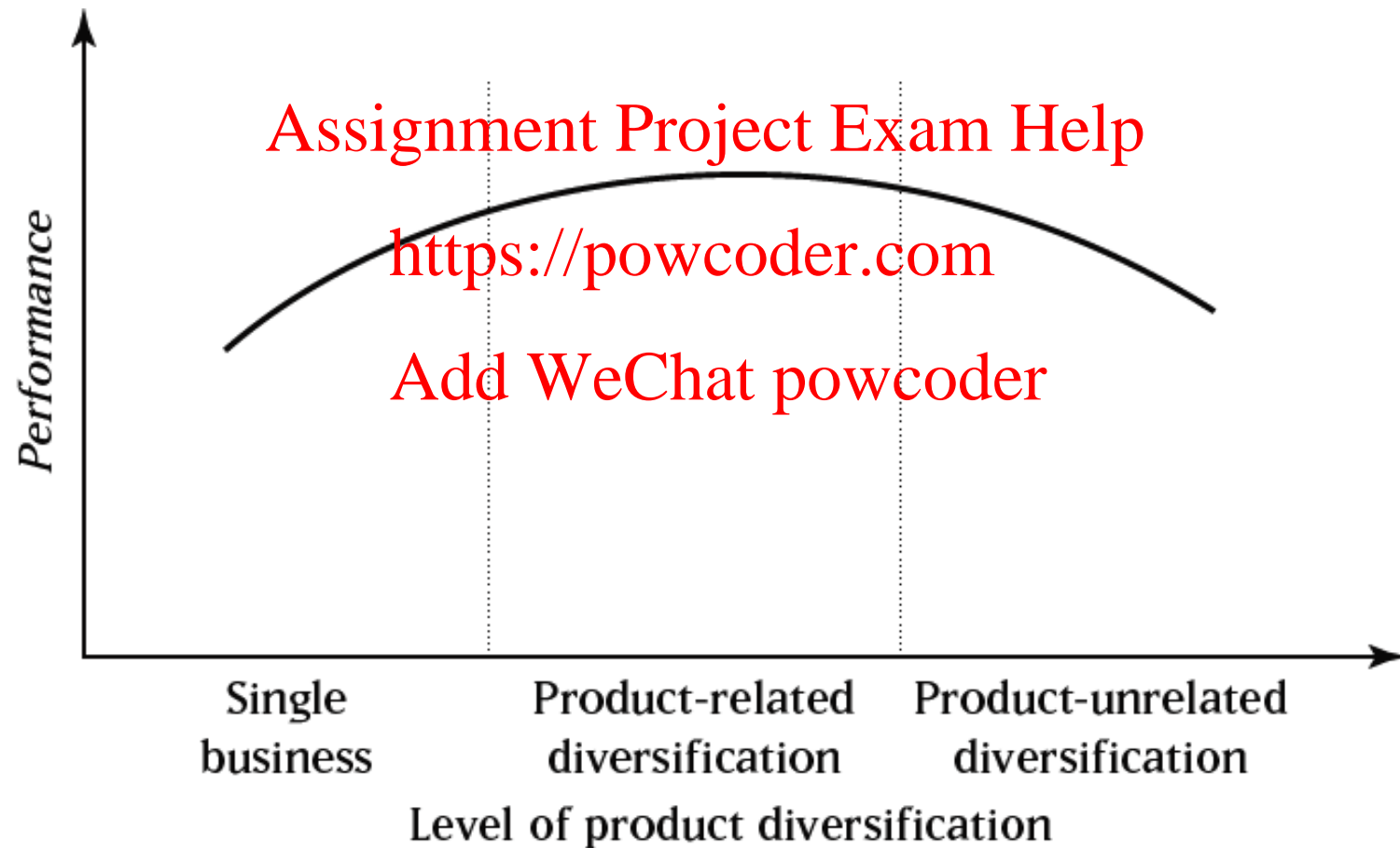
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Product diversification and firm performance





Geographic diversification

- Limited international scope
- Extensive international scope

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Geographic Diversification of the Largest Multinational Enterprises (MNEs) by Sales

	"GLOBAL" MNEs ¹		"BI-REGIONAL" MNEs ²		"HOST REGION-BASED" MNEs ³		"MOST INTERNATIONALIZED" MNEs ⁴
1	IBM	1	BP Amoco	1	DaimlerChrysler	1	ExxonMobil
2	Sony	2	Toyota	2	ING Group	2	General Motors
3	Philips	3	Nissan	3	Royal Ahold	3	BP Amoco
4	Nokia	4	Unilever	4	Honda	4	Ford
5	Intel	5	Motorola	5	Santander	5	Royal Dutch/Shell
6	Canon	6	GlaxoSmithKline	6	Delhaize 'Le Lion'	6	General Electric
7	Coca-Cola	7	EADS	7	AstraZeneca	7	Toyota
8	Flextronics	8	Bayer	8	News Corporation	8	ChevronTexaco
9	LVMH	9	Ericsson	9	Sodexo Alliance	9	TotalFinaElf
		10	Alstom	10	Manpower	10	IBM

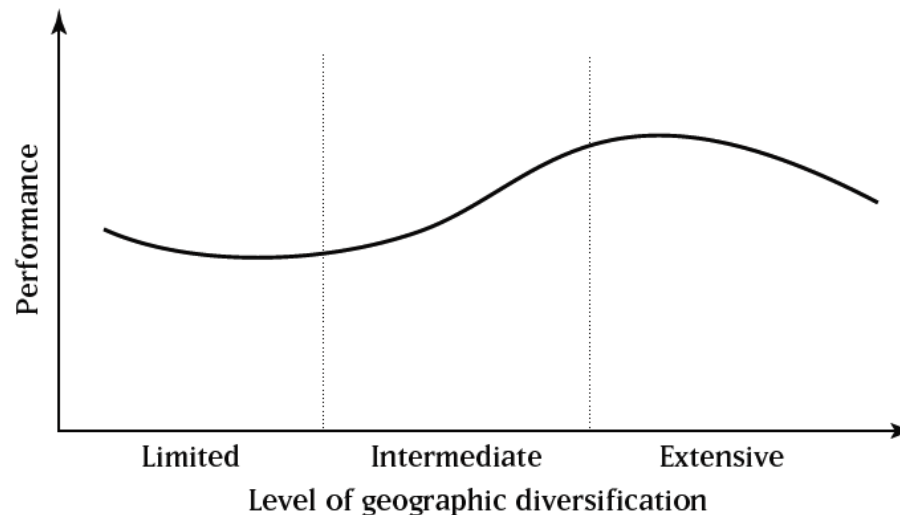
1. "Global" MNEs have at least 20 percent of sales in each of the three regions of the Triad (Asia, Europe, and North America), but less than 50 percent in any one region.
2. "Bi-regional MNEs" have at least 20 percent of sales in each of two regions of the Triad, but less than 50 percent in any one region.
3. "Host-region based" MNEs have more than 50 percent of sales in one of the Triad regions other than their home region.
4. "Most internationalized" MNEs have the highest "transnationality index," calculated by the United Nations as the average of (1) foreign/total sales, (2) foreign/total assets, and (3) foreign/total employment.

Sources: All data are from 2001. The first three columns are adapted from A. Rugman & A. Verbeke, 2004, *A perspective on regional and global strategies of multinational enterprises* (pp. 8–10), *Journal of International Business Studies*, 35: 3–18. The last column is adapted from United Nations, 2003, *World Investment Report 2003* (p. 5), New York and Geneva: United Nations.



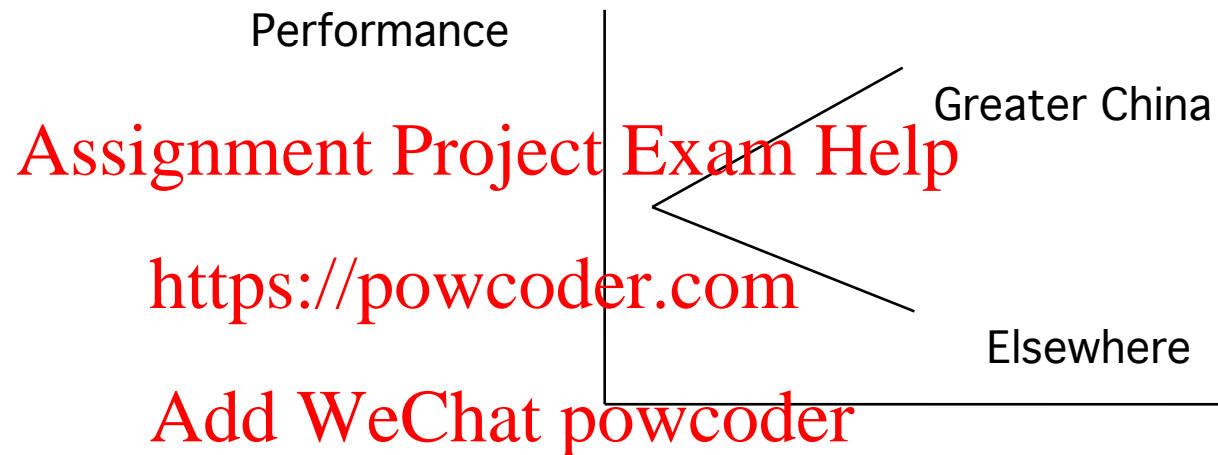
Geographic diversification and firm performance

- In this age of globalization, there are frequent calls for wider geographic diversification:
 - All firms need to go “global.”
 - Non-international firms need to start venturing abroad.
 - Firms with a little international presence should widen their geographic scope.
 - However, the evidence is not fully supportive of this popular view.





... it may also depend on where the firm internationalize to



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Chen, S. and Tan, H. (2012). Region effects in the internationalization–performance relationship in Chinese firms.

Region effects in the internationalization–performance relationship in Chinese firms

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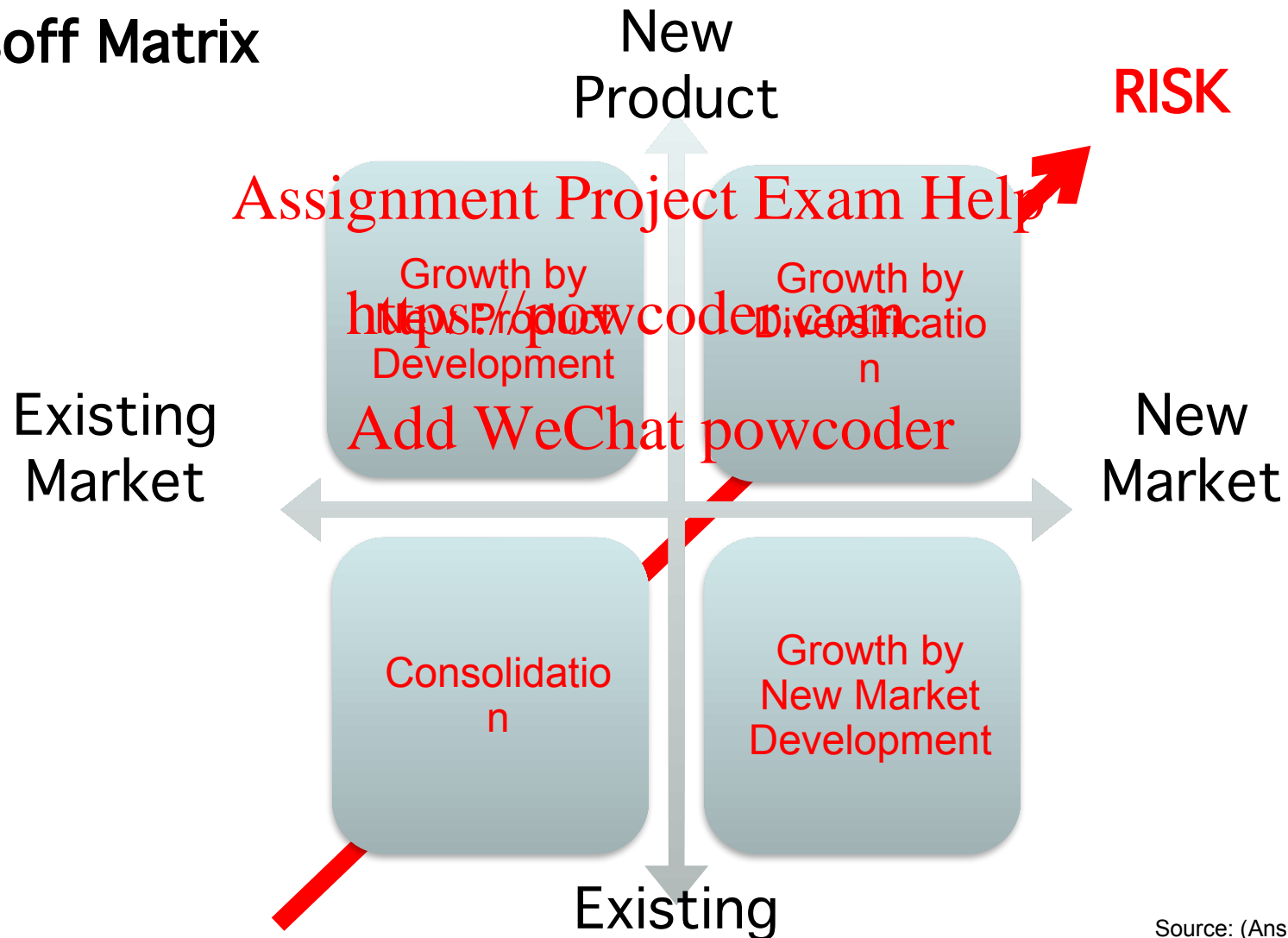
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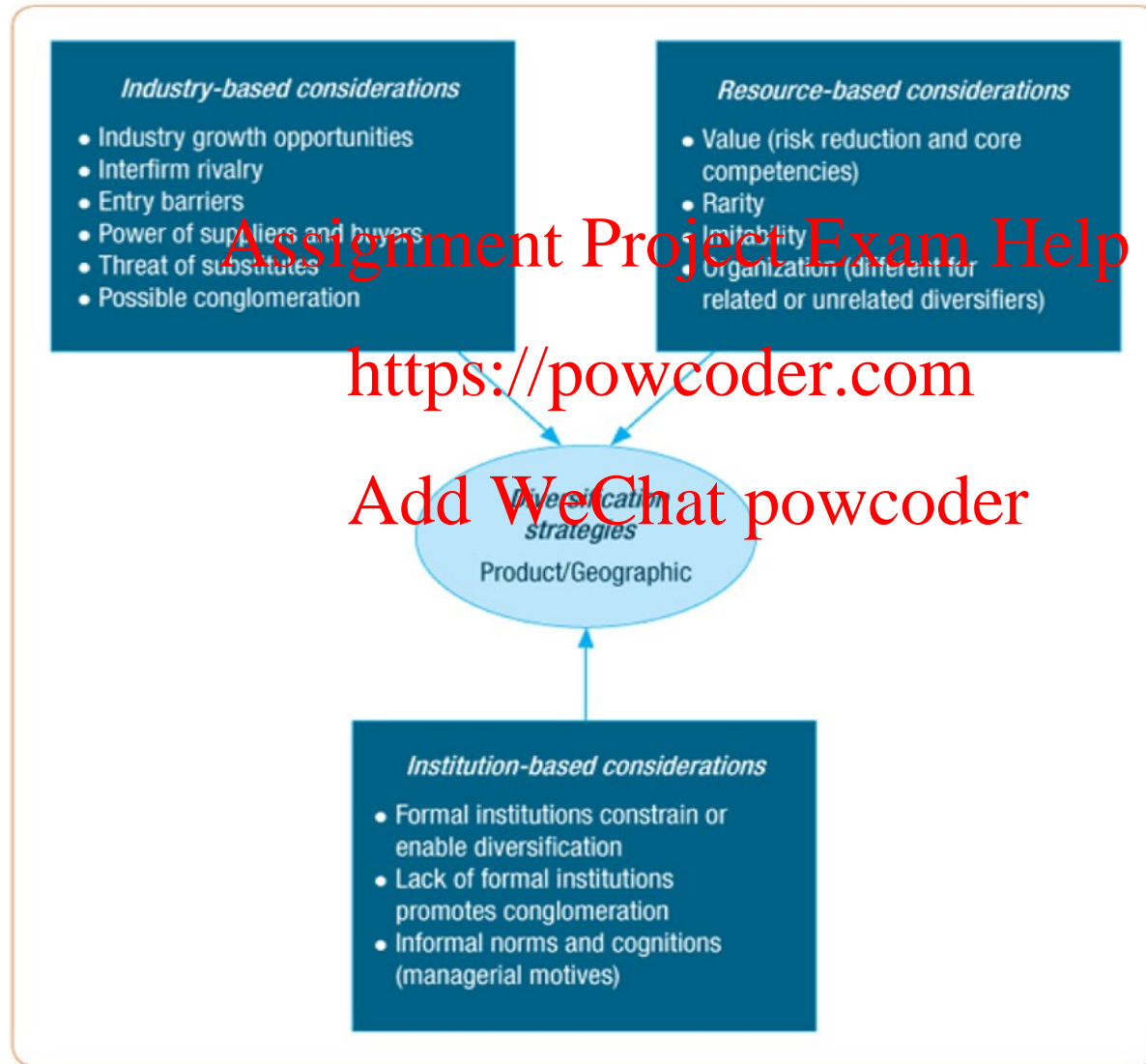
Product market growth

Ansoff Matrix





Why do firms diversify – three perspectives on diversification



Source: Peng 2017 Global Strategy 4th Edition. Cengage.



Industry-Based Considerations

- Motivations for Diversification:
 - Growth opportunities in an industry
 - Structural attractiveness
 - Five forces
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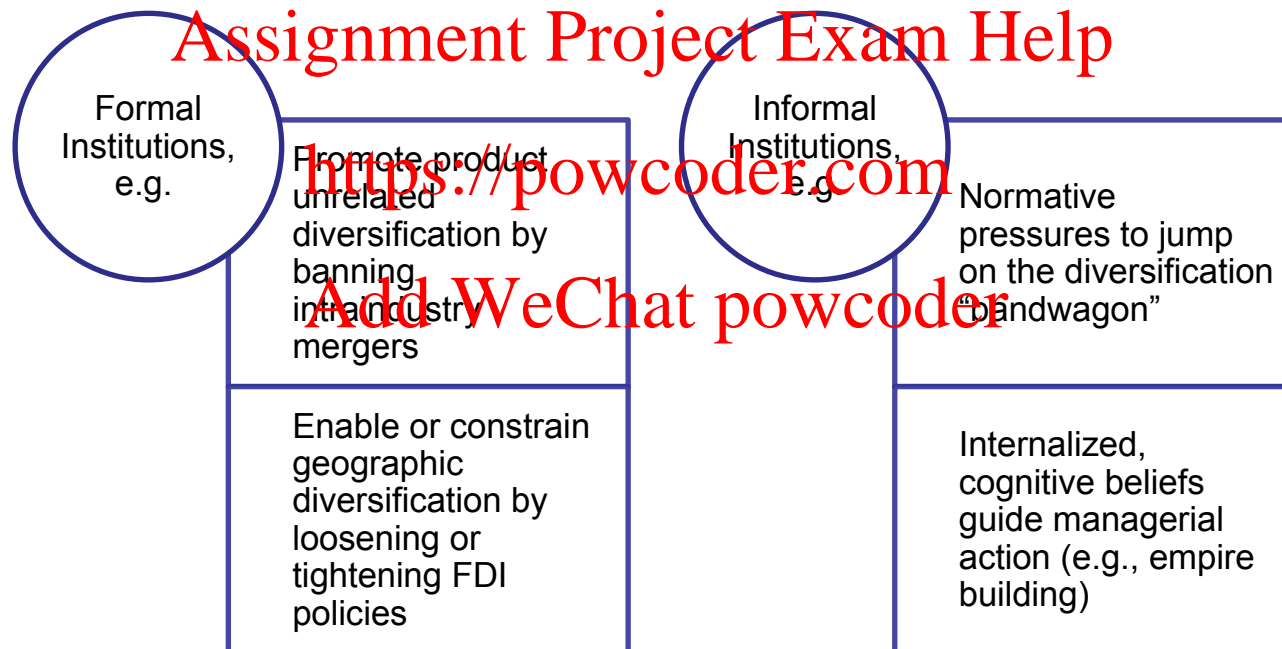


Resource-Based Considerations

- Value
 - Rarity
 - Imitability
 - Organization
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Institution-Based Considerations





The Evolution of the Scope of the Firm

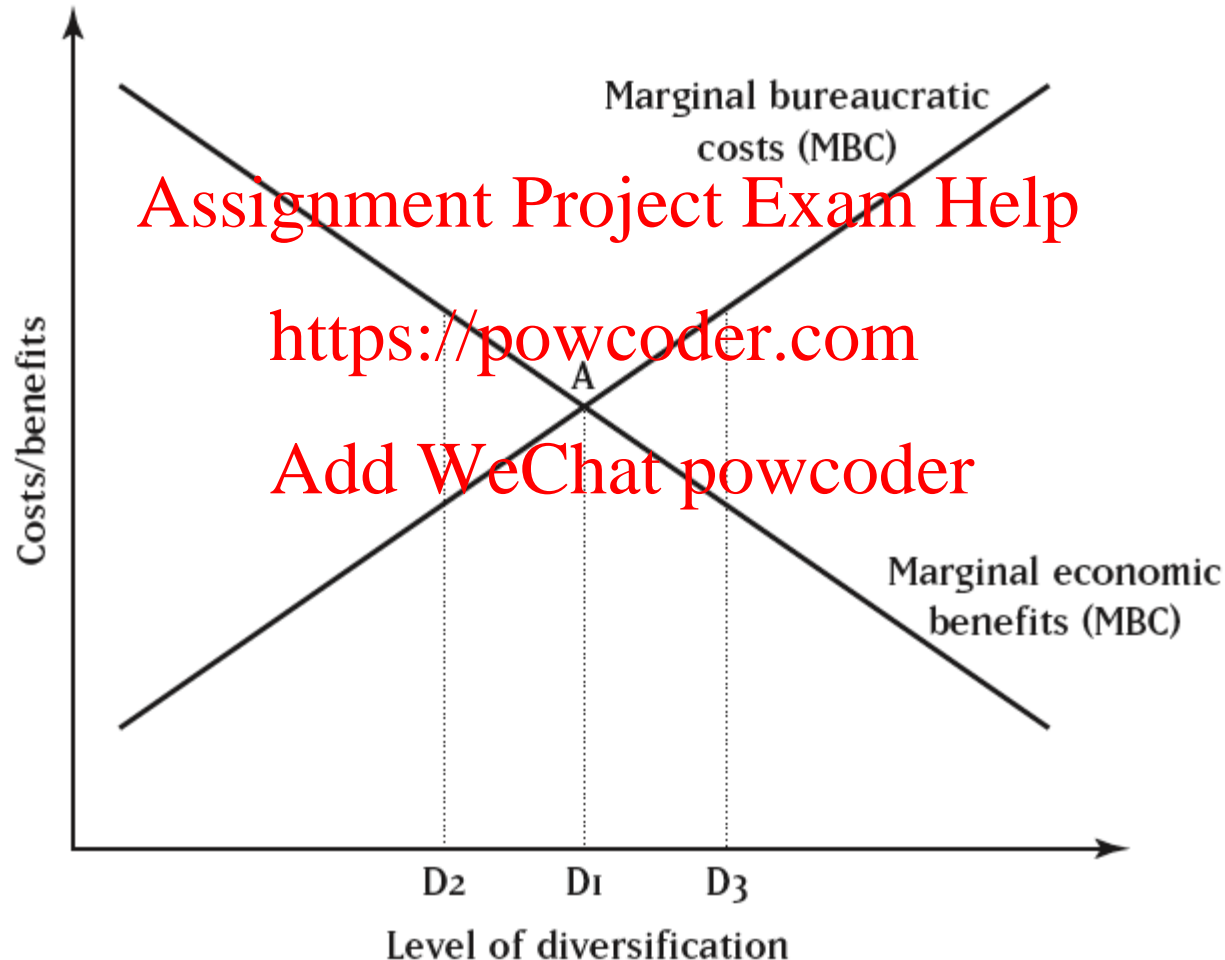
- The Scope of the Firm

- Determined by a comparison between marginal economic benefits (MEB) and the marginal bureaucratic costs (MBC).

- **MEB** are the various forms of synergy (operational or financial) gained from the last unit of growth—e.g., the last acquisition.
- **MBC** are additional costs associated with a larger, more diversified organization—e.g., more headcounts, more expensive information systems.

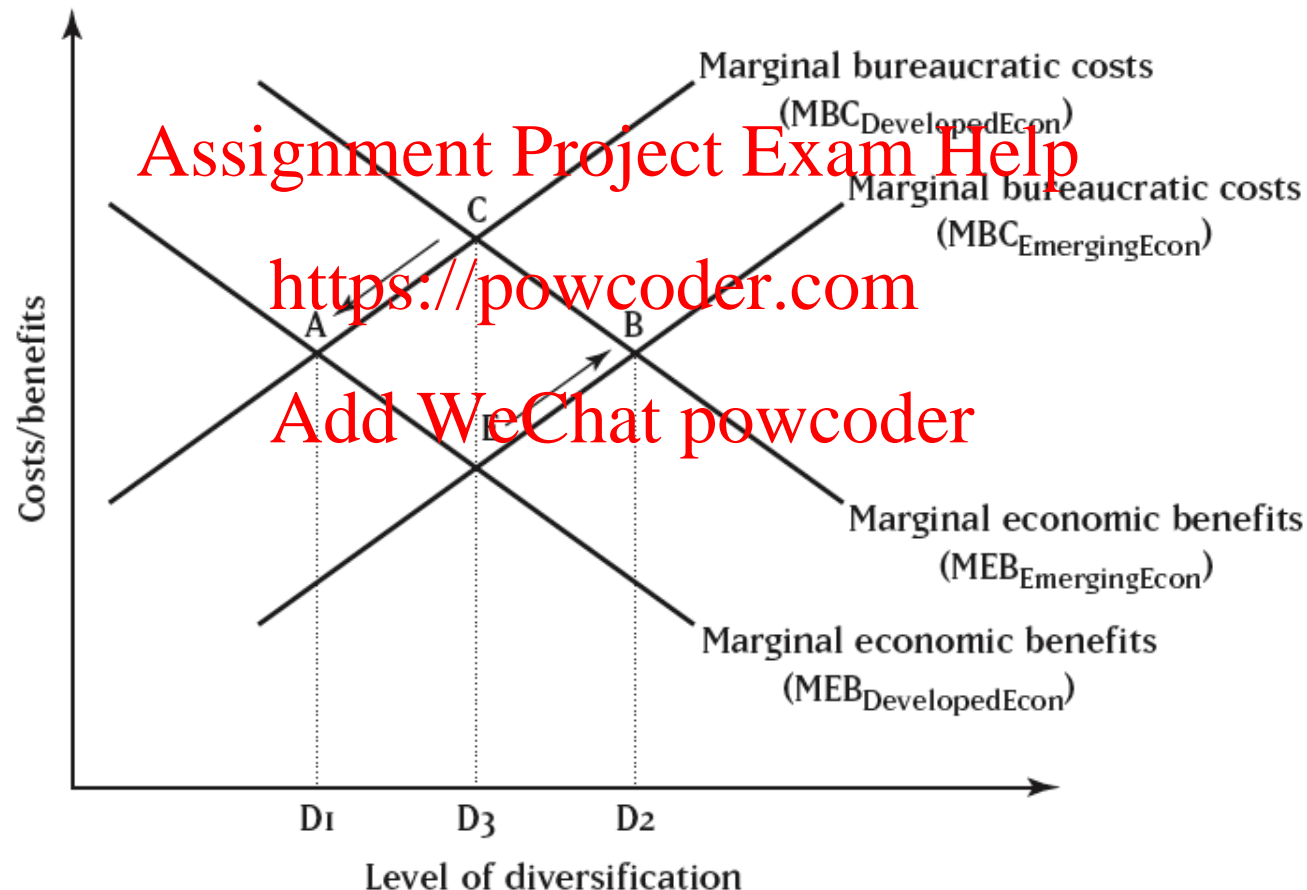


What Determines the Scope of the Firm?





The Optimal Scope of the Firm: Developed versus Emerging Economies





Mergers and Acquisitions (M&As): Types and Motives

Primary categories of M&As

- **Horizontal:** deals involving competing firms in the same industry—BP/Amoco.
- **Vertical:** deals which allow the focal firms to acquire suppliers upstream and/or buyers downstream—Sony/Columbia Pictures.
- **Conglomerate:** transactions undertaken by product unrelated diversifiers involving firms in product unrelated industries and markets—Vivendi/Universal.

Terms of M&As

- **Friendly:** the board and management of a target firm agrees to the transaction (although they may initially resist).
- **Hostile (or hostile takeovers):** undertaken against the wishes of the target firm's board and management, who reject M&A offers—SIA 9.2: Vodafone AirTouch/Mannesman

Examples

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Motives Behind Mergers and Acquisitions

	INDUSTRY-BASED ISSUES	RESOURCE-BASED ISSUES	INSTITUTION-BASED ISSUES
Synergistic motives	<ul style="list-style-type: none"> ■ Enhance and consolidate market power ■ Overcome entry barriers ■ Reduce risk ■ Scope economies 	<ul style="list-style-type: none"> ■ Leverage superior managerial capabilities ■ Access to complementary resources ■ Learning and developing new skills 	<ul style="list-style-type: none"> ■ Respond to formal institutional constraints and transitions ■ Take advantage of market opening and globalization
Hubris motives		<ul style="list-style-type: none"> ■ Managers' over-confidence in their capabilities 	<ul style="list-style-type: none"> ■ Herd behavior—following norms and chasing fads of M&As
Managerial motives			<ul style="list-style-type: none"> ■ Self-interested actions such as empire-building guided by informal norms and cognitions



Symptoms of Merger & Alliance Failures

Problems for all M & A's	Problems for Cross-border M & A's
Preacquisition: Overpayment for targets	Lack of familiarity with foreign cultures, institutions, and systems
Managers overestimate their ability to create value	Inadequate number of worthy targets
Inadequate preacquisition screening	Nationalistic concerns against foreign takeovers (political sovereignty)
Poor strategic fit and lack of trust in motives for M & A	Clashes of organisational cultures compounded by clashes of national cultures
Postacquisition: Poor organisational fit	National concerns against foreign takeovers by firm and employees
Failure to address multiple stakeholder group's concerns	

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The Performance of M&As

- As many as 70% of M&As reportedly fail
- On average, acquiring firms' performance does not improve and is often negatively affected.
- Acquisitions are the largest capital expenditures most firms ever make, yet they are often the worst planned and executed business activities of all.
- Competitors often launch aggressive attacks to take advantage of the M&A chaos.



Restructuring - reducing firm size, scope, and complexity

- Types

- Downsizing: Reducing number of employees
- Downscoping: Reducing scope of firm
- Refocusing: Narrowing scope of firm

- Motives for restructuring

- Perspectives: Industry, resource, institution

- Not widely embraced around the world



Motives for Restructuring

- Industry-based Perspective
 - Restructuring is often triggered by a rising level of competition within an industry
- Resource-based Perspective
 - While restructuring may bring benefits, there are also significant costs—organizational chaos, anxiety, frustration, and low morale
- Institution-based Perspective
 - Firms and managers in developed economies increasingly feel institutional pressures from capital markets to restructure.
 - Strong institutional pressures against restructuring around the world



Divestiture

- The action or process of selling off subsidiary business interests or investments.
- One divestiture strategy involves **the sale of the subsidiary or business line to another company.**
- By selling the business or its assets, the parent can obtain capital to use to acquire another company or assets that better fit with its current strategy.
- Example - Pepsi
- Paper discussion – “Declining industries in emerging economies and firms’ strategies”



Prepare for the next week (Week 8)

- Read Chap 10
- In the session next week, every student please prepare ONE ppt slide that shows the organization structure of one REAL multinational corporation (in the form of “organisational chart”)
 - Please present in the session an organizational chart and explain how the main businesses of the multinational company are organized internationally based on your research and group discussion
 - The company you choose could be an organization you are familiar with (e.g. your current/former employer), or one you could find information from secondary sources



Tips for searching organizational charts

- Many companies reveal their organizational charts in their annual reports
- You can also search company names (e.g. tencent + “organization chart” or “reporting structure” or “organizational structure” in Google (choose the option “image”))

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An Example

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