15.835: Entrepreneurial Marketing

Session 10: Focus vs Diversification

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.

Two Growth Strategies

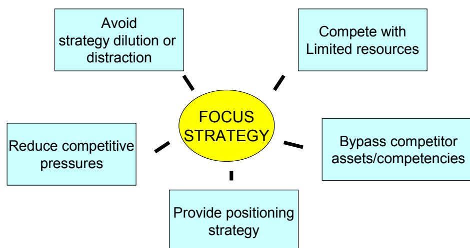
- Focus
  - Keep a focus on present markets
- Diversification
  - Explore new markets with new products
  1. Related
  2. Unrelated

Variations of Focus Strategies

- Focusing the product line in order to enhance technical superiority
- Targeting a niche
- Focusing limited geographic area

Focus Strategy

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



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.

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)

Motivations for Diversification

Related Diversification	Unrelated Diversification
•Exchange or share assets or competencies by exploiting - 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

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.

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?

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.