Diversification has been the way of life for most firms in Industrialised Countries and the past three decades have witnessed a significant move towards greater Product Market Diversification (Shekhar Chaudri: 1982). In fact, Diversification activities are considered as panacea for many Corporate ills. If the 19th Century can be described as an era of ‘specialisation’, the 20th Century can be called as era of ‘diversification’ (Mohinder N.Kaura:1987). The ‘diversification’ activity is an important process that shapes industrial and company structures and influences the performance of both industry and enterprise (Kripa Shanker: 1989). It is rather concerned with matching the organisation to the environment in which it operates. The environment of the firm is, however, dynamic with varying degree of the pace and magnitude of change. Since the success of every business largely depends on how it satisfies the customers with its goods and services, it become important and imperative for the ‘concern’ to adopt itself for the strategic changes. The economic performance of an industrial organisation is dependent upon many factors such as the industry’s growth rate, degree of concentration, level of research and development, advertising expenditure and firm size. There is one important factor which
affects the performance of any industrial organisation, i.e., the degree of diversification.

The prevailing environmental conditions do not allow a business enterprise to adopt to any specific strategy. A variety of strategies are to be identified and analysed before any specific strategy is concentrated upon to suit to the firm's strengths and weaknesses. The strategies may differ from one industry to another and for the same industry from time to time. Chandler (1962) in his seminal work in 1960's has suggested that the successful firms first expand their operations geographically, then integrate vertically and finally, diversify their product offerings. Hence, it became the onerous task to the management to predict the emerging environment and identify the needs of different segments of the market. A quick look at the market gives an impression that the large companies prefer diversification strategy.

1.1. **CONCEPT OF DIVERSIFICATION**

Firms are considered diversified when they are regularly concentrating on more than one business. Diversification strategy could be described by the extent of participation in different businesses and the underlying pattern of relationships among various business firms (Nayyar, 1992). The diversification should result in the manufacture of product or service entering into the new markets requiring newer skills, processes and knowledge.
Diversification should be viewed as a concept centered around the idea of product market diversification. Thus, diversification involves introduction of new product or entry into a new market or both. Rumelt (1974) viewed that diversification should require a change in the technical and managerial competence. He has defined diversification as a strategy to make an entry into newer business activity that requires an appreciable change in the available managerial and technical competence of the firm.

Being an important strategic decision, diversification is expected to improve the long-term financial performance of a company. A diversified business has two or more discrete business segments, which may be related or unrelated to the traditional business. Some relationship may exist between the discrete businesses of a diversified firm. The relatedness among the businesses of a firm would arise, when they share the markets, channels of distribution, technologies and manufacturing service. Thus diversification strategy of a company may be 'related' or 'unrelated' to its primary business. The concept of 'related diversification' was first developed by Ansoff (1965). According to him, companies which diversify based on their core skills (technological, marketing, financial and organisational) are Related Diversifiers and companies which are diversified into areas of unrelated to past activities are 'unrelated diversifiers'. Hence, related diversification calls for synergy by utilising the existing core skills. Unrelated diversification, on the other hand, implies that a company to engage in two or more businesses, each of which requiring different technologies, markets.
utilising different resources Wrigley (1970) had classified the companies on the basis of core skills as diversified with related or unrelated businesses.

Diversification could be achieved through acquisition (S Salter and Weinhold 1978) Vertical integration is another strategy for diversification of business (Robert D Buzell 1985) Vertical integration is included under the category of related diversification as it does not require acquiring of new marketing skills to improve the economies of operations (George Paul 1985) Vertical integration could be backward or forward It is a functional corporate strategy in the fields of strategic management and organisational economics (Joseph T Mahoney 1992)

Corporate diversification could also be pursued through merger activities which can be classified into horizontal, vertical and conglomerative categories The horizontal merger may be dealing with a related product line or geographic expansions A vertical merger occurs between a firm operating at a different stage for a linked production chain Conglomerate merger takes place where firms in unrelated businesses merge

Diversification leads to improved economic performance arising out of benefits such as great market power (Mark Ham 1973), higher economies of scale and scope (Berstom 1980), (Scher, Teece 1980), synergies from the sharing of complementary skills (Salter and Weinhold 1979) and risk reduction (Leontiades: 1986)
1.2. DIVERSIFICATION AS A BUSINESS STRATEGY

A strategy is a means to an end. Corporates are concerned with the basic long term goals and objectives of the enterprises and the adoption of difficult courses of action and the allocation of resources necessary for carrying out these goals (Chandler: A.D. 1962).

'Strategy' refers to the firm's requirement for the uncertain future in a dynamic environment. Strategic alternatives include all kinds of major strategic choices that need for the attainment of objectives. The process of strategic management has gained momentum and assumed importance during recent years due to dramatic changes in the external and internal environment of Business, (Ramanujam S., et al.:1989). A Strategy consists of a set of management guidelines which specify the firm's product-market position, the directions in which the firm seeks to grow and change (Ansoof: 1969). For Biggadike and others (1977) strategy is the pattern of objectives, purposes or goals and major policies and plans for achieving these goals, stated in such a way as to define the business that the company is in and or is to be in and the kind of company it is trying to become. The nature and number of the broad alternative patterns of strategy available to a firm are reduction, maintenance, expansion, diversification along with its related lines, innovation and differential combination of the above elements (Rastogi: 1987). The strategies represent the options for
the pace or level of effort in the current business definition or for changing the business definition. For example, a firm may decide to change its business definition by diversifying its production and business activities into related or unrelated lines. It can even maintain its definition, by changing its strategy by modifying its pace of effort within the business definition to become more efficient and effective. Besides, expansion or combination of options in varying degrees may be directed towards growth and profit.

The diversification strategy is one where the firm is said to pursue when it serves the public in additional products or services or adds markets or functions to its definition or increase the pace or activity along the lines 'related' to its existing production and business activities or along the new and unrelated lines. Diversification is thus defined as a 'strategy in which the growth objective is sought to be achieved by adding new product or service to the existing product or service lines' (Ghosh: 1986).

Various studies have revealed that diversification has been increasingly used as a strategy for adapting to the changes in the business environment. It changes the product market profile of the diversifying firm substantially. Therefore, diversification needs a break with the past pattern and decisions, skills and attitudes.

Diversification strategy involves an appreciable change in available managerial and technical competence and new administrative systems for ensuring the
efficient use of the diverse resources. Besides these complexities, it is becoming an increasingly general feature of large firms all over the World.

1.3. **WHY FIRMS DIVERSIFY**

The companies diversify for 'survival' in a business or to superseed others in its competitive environment. The process of diversification is adopted usually by a firm when there is a decline in its existing range of products or when markets have not grown fast enough. It is also closely related to the programme of growth and maintenance of the viability of a firm. Diversification 'reduces the risk' by stabilising profits and spreading the investment over several business. It is a method of exploiting an organisation's strengths. However, the Indian firms are going for diversification largely to minimize the effort of overnment 'regulations' in its current line of activity (Chandler et-al., 1972). Salter and Weinhold (1979), Ansoff et-al., (1971) have observed that the primary reasons for adopting diversification strategy by a corporate enterprise in USA and UK were related to prestige, power, profits, growth and risk reduction and compensation motives of the corporate management.

1.4. **THE FOLLOWING ARE SOME OF THE REASONS ADVOCATED FOR FIRM DIVERSIFICATION**

1. to counter the ill effects of decrease in sales and earnings in the existing line of activity, particularly during the maturity phase of the business life cycle,
to overcome the competitive pressures,

to reduce risk business as well as financial risks,

to capitalise on distinctive technological expertise in production

to build a balanced portfolio of businesses,

to develop new products in order to use the existing distribution channel, to exploit fruitful R & D efforts with new product and photo types,

to exploit fruitful efforts with new product and prototypes,

to avoid takeovers by growing 'big' and retain control,

to reduce dependence on a few suppliers or a few customers,

to attract and maintain efficient management staff as well as to provide career opportunities for them,

to achieve sufficient size so as to have efficient access to capital markets,

to adjust to the tastes of customers and their life styles and

to satisfy power and prestige motives through economic power and control over human resources

1.5. TYPES OF DIVERSIFICATION

The diversification strategy is ultimately concerned with achieving larger market share from greater range of products in order to achieve maximum profits. From the risk point of view, it translates the policy of “not putting all of one’s eggs in the same basket” into action. The following is the strategic classifications of Wrigley (1970). By considering the ‘Specialisation Ratio’ (SR)
and Related Ratio (RR) Wrigley has classified the diversification strategies as follows. While Specialisation ratio refers to the ratio of firm's sales in its major activity as a proportion to its total sales, Related ratio is a proportion of firm's total sales which are related to one another.

<table>
<thead>
<tr>
<th>Single business</th>
<th>Specialisation Ratio (SR) &gt; 95 Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dominant business</td>
<td>95 Percent &gt; SR 70 Percent</td>
</tr>
<tr>
<td>Related business</td>
<td>SR &lt; 70 Percent, RR &gt; 70 Percent</td>
</tr>
<tr>
<td>Unrelated business</td>
<td>SR &lt; 70 Percent, RR &lt; 70 Percent</td>
</tr>
</tbody>
</table>

Rumelt (1974) classified the firms as given below:

<table>
<thead>
<tr>
<th>Single Business Firm</th>
<th>SR &gt; 95 Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dominant Vertical Related</td>
<td>&gt; 70 Percent</td>
</tr>
<tr>
<td>Dominant Constraint</td>
<td>95 Percent &lt; SR 70 Percent</td>
</tr>
<tr>
<td>Dominant Linked</td>
<td>95 Percent &lt; SR 70 Percent</td>
</tr>
<tr>
<td>Dominant Unrelated</td>
<td>95 Percent &lt; SR 70 Percent</td>
</tr>
<tr>
<td>Related Constrained</td>
<td>70 Percent SR</td>
</tr>
<tr>
<td>Related Linked</td>
<td>SR &lt; 70 Percent, RR &gt; 70 Percent</td>
</tr>
<tr>
<td>Unrelated business</td>
<td>SR &lt; 70 Percent, RR &lt; 70 Percent</td>
</tr>
</tbody>
</table>
The diversification choices can broadly be classified into:

1. Related Diversification,
2. Unrelated Diversification,
3. Acquisitions,
4. Joint Ventures,
5. Merges,
6. Amalgamations

Diversification involve high degree of risk as it amounts to manufacturing of newer products, or entering into newer markers, unfamiliar to the organisation. The diversification strategies that firms adopt could be explained as follows:

a). Related Diversification

New products, service or markets that are added if "related" and if they confirm to and are very similar to the current business definitions, such diversification is called 'Related Diversification'. The addition of related products, services or markets is termed as concentration of strength, the ability to add more quickly (than firms with unrelated expansion) for exploitation of market niche and the development synergy.

b). Unrelated Diversification

Unrelated approaches imply diversification into areas that do not confirm to the current business. The unrelated approach is usually termed as 'Congolomarate' diversification. The unrelated dimension is often associated with expansion. While Acquisition refers to the purchase of a company by another,
the Merger is the formation of a new company wherein old company loses its identity to form new. Sometimes, it is profitable to diversify through mergers. The process of merger gives the advantage of not having to start from scratch. Amalgamations enable the companies to have the advantage of fast changing technologies and to enable the reduction of administrative costs.

Joint Venture is another alternative which can meet a number of objectives such as rate of growth desired by the firm, maintaining the risk within reasonable limits and overcoming constraints of resources. Thus a firm having constraints of product capacity can have a Joint Venture with a firm having surplus productive capacity.

1.6. GLOBAL SCENARIO

Diversification as 'strategy' to adopt to the changes in corporate and economic environments has become a common feature of many large corporations all over the World. In 1970 only 6.2 per cent of U.S firms that appeared in Fortune 500 lists were carrying on single business, while 65 per cent of the large firms had diversified into newer related or unrelated fields [Rumelt 1970]. Channon (1973) found that the firms in the European countries also showed a trend towards increasing diversification. 53 per cent of the large firms in U.K and 45 per cent in West Germany, had diversified (Channon:1973). While 38 per cent in France and 35 per cent of the firms in Italy have diversified into others areas.
In India, the process of diversification has assumed greater importance, in recent years, due to the dynamic changes in the internal and external environment. Entering into the new products and markets due to diversification having far-reaching implications on the organization structure, systems, and performance (George Pual 1986) of a company. The corporate sector in India has shown desire and ability for diversification particularly during the last two decades.

Shekhar Chaudhri (1982) has observed that both private and public sector units have diversified, with differences in the degree and nature of diversification between them. In 1975, about 86 per cent of the private sector firms and 55 per cent of the public sector firms had diversified in India. While only 36.7 per cent of the firms remained undiversified, 63.3 per cent of the firms are found adopting diversification as a strategy. Out of 157 diversified units, 93 (59.2 per cent) were found engaged in unrelated fields.

The diversification strategy profile of the Indian Industry was studied by Koura (1987). It was evident that mostly the large units of the private sector have adopted diversification as a corporate strategy. It was confirmed that most large units had resorted to unrelated diversification as a corporate strategy.
The public sector firms diversified into related businesses because of the governmental pressure, in the form of public policy, for achieving the self-sufficiency and import substitution. Thus, diversification in Indian industry seems to have influenced strongly by governmental regulations and public policy (Shekhar Chaudhuri et al., 1982). The private and public sector enterprises seem diversifying rapidly almost at equal rates but in quite different directions. The corporate sector, in India has shown the desire and ability for diversification, particularly during the last decade. ITC, Birla Jute, Raymonds, Larsen and Toubro, Reliance Textiles, BHEL, HMT are typical examples of diversification in India.

**Few Indian Examples**

<table>
<thead>
<tr>
<th>Type of Diversification</th>
<th>Example</th>
</tr>
</thead>
<tbody>
<tr>
<td>Related Diversification</td>
<td>Gwalior Rayon</td>
</tr>
<tr>
<td>Unrelated Diversification</td>
<td>TVS Group known for Automobiles have started manufacturing and making Computer Peripherals</td>
</tr>
<tr>
<td>Forward Integration</td>
<td>Delhi Cloth Mill (DCM), Mafatlal, National Textile Cooperations have setup their own selling outlets</td>
</tr>
<tr>
<td>Backward Integration</td>
<td>Amajin Agro Exports Ltd integrated backwardly by cultivating the required raw-materials namely sugar cane leaves.</td>
</tr>
<tr>
<td>Horizontal Diversification</td>
<td>Ram Co. has set up a Spinning Mill. Raymond Wollen Textiles</td>
</tr>
</tbody>
</table>
now started to produce Cement and Engineering files

Acquisition
Associate Cement Company (ACC) decided to acquire Damodhar Cement and Slag Ltd. Which is one of the ailing subsidiary of Cement Corporation of India (CCI)

Mergers
Absorption of the Steel Corporation of Bengal by Indian Iron & Steel Co. Formation of Cement Corporation by merging 11 Cement Companies in 1937

Takeovers
Hidustan Lever has taken over Hot Melt Adhesives near Pune

Amalgamations
Mahindra Nissan Allwyn (MNAL) and Mahindra Ltd (MM) were amalgamated

Joint Venture
Contract between Thungabatra Industries Ltd of India & Yamaha Motors Co Ltd of Japan

1.8. REVIEW OF LITERATURE

Shekar Chaudhri and others (1982) have examined the pattern of diversification of seventy-two large private and public limited companies in India during the period of 1960-75. In their pioneering work, they observed that “reaching out” into the newer areas requiring the development of new skills, which has been regarded as the essence of diversification. The companies were divided into single business, vertical integrated, related business and unrelated business
The three quantitative measures of Rumelt (1974) for categorising the firms are Specialisation Ratio, Related Ratio, and Vertical Ratio. During 1970, it was observed that about 86 per cent of the private and 55 per cent of the public sector firms in the study sample have diversified. It was also found that most of the companies showed a rapid rate of diversification. Further, it was observed that the private companies leaned more towards unrelated diversification, while the public limited companies adopted the related diversification. The pattern of diversification has been influenced strongly by the regulations of the government and public policy.

Mohinder N Koura (1987) has brought out a study on the diversification profile of 251 private sector firms considering the definition of Stenior (1969), Rumelt (1974), Ansoff (1965), Wrigley (1970), and Pits and Hopkins (1982). The diversification profile of Indian Industries were examined to find out whether (i) the Related diversification is evenly followed than Unrelated diversification, strategy (ii) the diversification strategy was most popular among Multi-National Corporations and (iii) which type of industries adopt unrelated diversification.

An analysis was made to determine whether the company's product range is physically different, requiring separate resources, technology and financial base for manufacture and requiring a separate distribution channel to sell. On the basis of this analysis the companies were classified as undiversified, related diversified, and unrelated diversified.
The study revealed that most of the large companies followed diversification strategy. The degree of diversity varied from industry to industry and the same was more among the subsidiaries of Multi-National Corporations (MNCs). It was observed that the Indian industries showed more interest towards unrelated diversification. Private sector firms diversified subsequently.

The extent (spread) and magnitude (depth) of product diversification and the growth on the profitability of the diversified units, have been studied by Kirpa Shankar (1989) on a sample of 1694 companies during 1975-81 in order to find out issues like,

(i) which group of industries generally adopt a diversification strategy? (ii) What type of product diversification is followed by the private industries? (iii) What is the primary industry characteristics which under take diversification? (iv) whether the diversification is undertaken relatively more by large sized companies. (v) What is the difference in the magnitude diversification between companies of different sizes, different ages and different type of industries? (vi) What is the trend of the long run growth and profitability performance of the diversified companies? that 86 per cent of the private sector firms have diversified. The study also revealed that Private companies adopted unrelated diversification while the Public limited companies followed the related diversification strategy.

Paulette Dubofsy and others (1987) scrutinized whether the firms that diversify into related lines of businesses give positive results than that of unrelated
lines of business. By carrying out a longitudinal analysis of change in performance over time, on a sample of fifty one firms selected from Fortune 250 list during the period 1975-81, the study revealed that the firms diversity into unrelated areas were showing significant performance than related diversifiers.

Allen Michael and others (1984) brought out a study for examining the relationship between the extent of diversification of a firm and its financial performance. It is revealed that firms with unrelated diversification performed better than the related diversificated units.

George Paul (1985) studied on what type of a diversification strategy produced better financial performance in the long run on a sample of twenty eight Monopoly Restrictive Trade Practice Companies. The companies with many unrelated businesses showed the poorest performance. The performance of unrelated diversifiers was worse than undiversified ones.

Stephen A. Rhodes (1973) has evaluated the effect of diversification on profit performance of 241 manufacturing industries in 1963. The industry price cost margins and diversification strategies have been examined. Using multivariate regression analysis the study reveals a tentative support for the proposition that diversification has systematic influence on price-cost margins which may be attributable to entry barriers in a given industry. It also revealed the existence of a relationship between diversification and price-cost.
margins. Thus the results support the general proposition that diversification may be viewed as structural variable.

Stuti Lall (1979) examined the impact of diversification on financial performance of Indian Jute Industry during the period 1959-60 and 1969-70, with a sample of twenty eight Jute companies. The study revealed that diversification had a positive effect on financial performance. The financial performance of most moderately diversified companies was significantly higher than the performance of undiversified ones. It was observed that profitability was a 'cause' for diversification rather than an 'effect'.

The findings of the study are to be useful as it had excluded those firms which have diversified totally into unrelated fields from the scope of the study. The study used a simple variance index to measure diversification. The study observes that diversification had a positive effect on financial performance. The financial performance of moderately diversified companies was significantly higher than the performance of negligently diversified companies. The period of analysis was divided into pre-diversification, and post diversification periods. But an examination of causes and effects showed that the units with higher levels of profitability induce them to pursue diversification as they had resources for diversification. It was also observed that profitability was the cause for diversification rather than its effect.
Robert Grant and others (1986) have examined the relationship between diversification strategy and firm characteristics and the financial performance of 304 large British firms over the period 1972-1984. The firms were classified into different categories on the basis of Rumelt's (1974) method. The firms with different characteristics might be expected to adopt different strategies and different strategies might lead to the development of different characteristics. Return on Asset, Return on Equity, Return on Investment, Size, Capital intensity, Debt / Equity ratio have been calculated from the collected data. The findings that emerged were that diversification strategies were significantly related to profitability and firm characteristics like its size, capital intensity and leverage. Industry effect could not be seen as some specific strategies were associated with certain industries than with others. Diversified related businesses and unrelated businesses were more profitable when compared to specialised single business and dominant business. There was no evidence to show that the related diversification was much more profitable than unrelated diversification.

Grant, Jamine and Thomas (1984) have analysed the relationship between diversification strategy and economic performance with the sample of 305 British manufacturing companies during the period 1968-1984. An improvement was made over their earlier work (1966) by adopting additional measures of diversification and extending the period of the study. The following diversification measures were used:

(i). Wrigley's (1970) classification method,
(ii) Rumelt's (1974) classification method,

(iii) An index of product diversity based on the share of a firm's sales in each industry group and

(iv) A measure of geographical diversification measured by the proportion of a firm's revenues derived from non-UK operations

These measures were calculated for every year during the study period. The analysis revealed that the first two measures of diversification explain only a small proportion of inter-firm variability of returns. Over time, there was a weak tendency for more diversified firms to perform better in terms of return on assets than the more specialised categories. Related diversifiers improved their relative performance. Diversity could explain only a small fraction of inter-firm profitability differences which were smaller than that of industry, when a firm and industry effects are sought to be excluded. Generally, diversified firms were more profitable than specialised firms. This was also confirmed in the case of diversification of Multi-National Companies.

There was a consistent evidence of a quadratic relationship between diversity and profitability. Besides the study also investigated the issue of causation and consequence by examining the changes in the variables over time. The principal finding was that multinational diversification generated increased profitability. There was a two way relationship between multinational diversification and profitability. When the diversification increased the returns on assets, the current cash flows induced the diversification. The impact of multinational diversification was stronger on sales growth than on profitability. In
case of product diversification, profitability was only a cause for diversification rather than consequence.

George Paul (1985) examined the diversification strategy and performance of thirty-six Indian companies managed privately and belonging to five different industry groups of cotton, synthetic, woolen textiles, jute, paper and cement. The diversity of companies was determined on the basis of product-wise sales information. The percentage of sales of various products was determined by using data for at least two years during the period of 1974-75 and 1980-81. In most of the cases, a middle year data were used in determining the average sales. On the basis of the guidelines of Security Exchange Commission (SEC) USA, ten percent of total sales or assets should be used as the criteria to determine whether a particular line of business of a diversified company for corporate reporting purposes was significant or not. The companies were classified, based on the methodologies of Ansoff (1969) and Wrigley (1970) as related or unrelated diversifiers, the unrelated diversifiers, restricted unrelated diversifiers and unrestricted unrelated diversifiers. The financial performance of different strategic categories of diversifiers were examined using growth-based measures such as net sales, net worth and dividend. The study has adopted a matched pair approach and compared the performance of diversified companies with that of non-diversified ones. It was found the diversified companies outperformed the non-diversified ones. But the study suggested that selective Diversification from stagnant and government regulated industries would be more effective. It was observed that significant differences in performance of companies following
different strategic modes existed. The highest performers were unrelated diversified ones. While the unrestricted unrelated diversifiers report a performance, the related diversifiers showed moderate performance.

Praveen Nayar (1992) made a study to find out whether the actual or potential relatedness determine the strategy of diversification. The potential relatedness deals with external process such as business products, markets and technologies. An examination of these external factors permits an assessment among its various businesses. The actual relatedness might reveal the externally measured potential relatedness.

Alexis P. Jacquemin and others (1970) examined the corporate concentration and diversification with a sample of 460 large US industrial corporations over the period 1960-65. Herfindal index and Entropy measures were used. The concentration ratios were also constructed. The results proved that diversification has positively influenced related to the growth rates of these selected firms.

Varadarajan and Ramanujam (1987) have examined the levels of economic performance associated with nine different categories of diversifiers. This study has examined the linkage between diversity and performance using a new method of categorising firms based on their degree and direction of diversification. While this approach overcomes the problem of subjectivity inherent in Rumelt's classification scheme and makes no demands for the
detailed business level data that is a prerequisite of Paulette's approach to identify the Diversified firms. Diversified firms have been classified as broad spectrum (BSD) and Mean Narrow Spectrum (MNSD) in addition to traditional classification of related and unrelated. Drawing sample of 223 firms from the Directory of Corporate Affiliation in America, the study has evaluated the performance in terms of ROE, ROC, growth in sales, EPS growth. The results of the study although supports the general Rumelt's (1974) original findings regarding diversity and performance. The claim of absolute advantage attributed to related diversifiers is disputed.

Raman (1991) examined the nature and extent of diversification of 67 Indian private sector companies over the period 1979 to 1989 following Rumelt's (1982) model, for the classification of diversification. The author observed that the number of single business firms has come down from 28 in 1979 to 17 in 1989. But the unrelated businesses have increased from 9 in 1979 to 12 in 1989. The study revealed that the trend towards higher diversification was gradual. The findings of the study generally supported the results of Chaudhury and others (1982) and of Kouura (1987).

Hilary and others (1992) evaluated the mergers and the financial performance after takeovers. The study covered a sample of 146 UK's top 500 Companies. In 1989 there were 1077 Mergers in UK. A take over is essentially a game of strategy involving a number of players in which the management of the company attempts to gain control over another. The impact
of mergers were assessed and measured with accounting measures of profitability and share price changes. The CAPM methodology which uses excess stock market returns to determine the effects of mergers has been used. Three measures—Return On Capital Employed, Return On Net Assets, ROS—were used for measuring profitability. The results provide some comfort for both management and shareholders.

Bond R (1974) measured the levels of diversity in the firm's activity by product count method. The population of this study was 157 large US firms, during the period 1963-67. The study had observed that there was no significant relation between diversification and profitability. The relationship was measured as the standard deviation of the rates of return on the total invested capital, after separating the effect of firm size on these variables.

Berry (1975) adopted a measure which was an improvement over the product count measure. The corporate growth was measured as the percentage growth in total assets of each corporation during the period 1960-65. His analysis of 460 corporations showed that they were positively associated with increasing diversification regardless of the level at which diversification was measured. When measures of diversification were used, at two-digit and four-digit levels, the association was positive at four-digit level although it was not significant. His findings were that successful corporations expand into the product areas related to their areas of past success and corporations with unsatisfactory performance and potential growth branched out into unrelated areas.
Carter (1977) brought out a study to analyse whether diversification gives rise to synergy and thereby superior profit performance (growth). The sample of the study constituted 374 firms and the study was carried out during the period 1962-63. The study was based on a structure performance model. The structural variables used in the model were designed to measure concentration, type of buyer, barriers to entry, growth and diversification. He found that the synergy hypothesis received the strongest support when diversification was measured by the H-index number equivalent. The synergistic effect appeared to be of at least moderate economic significance. The entropy numbers equivalent index suggested a slight modification to moderate synergistic effect.

Rachel Davis and others (1992) brought a new perspective on diversification, vertical integration and industry analysis and measures. Using a sample of 51 firms from Fortune 250 list, the study identified that vertical integration could be of two types as between stages and within stages of the value added chain. It was possible to identify whether a business was forward or backwardly integrated by identifying the upstream or downstream location of the secondary activities of the business relative to the primary business activities. The entropy measures were used to measure diversification.

Rajagopalan and Rasheed (1991) have reviewed recently about 50 studies. This paper has identified three streams of studies on diversification-performance relationship. The first stream deals with those studies which attempt to link...
the degree of diversification to performance. Second stream refers to the type of diversification strategy and performance. Third stream of studies focussed on the mode of diversification and performance. Further, this review finds the role of industry structure as an important variable on diversification-performance relationship. On the basis of different studies, this review paper identifies the set of performance variables used by many as the return, risk and other influences of being moderated by industry structure, variables like concentration, barriers to entry, capital intensity, growth, technological change, organisational structure, culture, systems and distinctive competence.

Le Craw (1984) brought out a study to explore into the issues like to what extent did the structural characteristics of base industry of a firm and the firm's own characteristics influenced the diversification strategy. The sample was classified into four groups viz as single business, vertically integrated business, related vertically integrated business, related business and unrelated businesses. The firms' return on equity has been used as the performance variable. The study observes that those firms which follow the strategy of related diversification and vertical integration are able to outperform the others. While the firms adopt appropriate strategies, they can do well if the market share in their industries in which they operate.

Betis and Hall (1982) have examined the validity of some of the Rumelt's conclusions about related and unrelated diversification strategies using accounting
measures of risk and return An attempt has been made to test four important hypothesis, viz.

H1 Firms adopting related diversification strategies outperform unrelated diversification strategies.

H2 Unrelated diversification strategies have lower levels of accounting risk than the related diversification strategies.

H3 Accounting determined return will be strongly and positively correlated with accounting risk in case of unrelated diversification.

H4 Accounting determined return will be weakly correlated to risk if firms pursue related diversification strategy. Drawing a sample of 80 firms from Fortune 500, the study observes that the firms do not enjoy superior risk-pooling characteristics. It is further observed that the superior returns attributed by Rumelt (1974 and 1977) in related diversifiers may be due to industry effects.

Lakshmi (1990) had evaluated the performance of related and unrelated diversifiers with a sample of 56 Indian companies. The following are the results of her study.

From the table it can be inferred that two groups of firms are different from each other in their performance when measured in terms of return on assets and return on equity. A comparison of the mean performance of those diversified into related business show statistically significant differences in three variables like leverage, growth in total assets and risk differentials among groups of firms.

A more recent study by Hoskisson (1987) lends support to the notion that the structural dimensions have an important influence on the diversification
Considering a sample of 62 firms in 20 industries, it is observed that diversification results in improved returns for investors better off than one which results in lower returns but also reduces the variability of returns. Risk reduction hypothesis is tested using F-test for difference between two variances after controlling for the effects of size, asset growth and percentage change in GNP. The results of this study are given in Table 1.2

From the above studies, the following observations could be made:

1. Most of the studies have used the Specialisation Ratio as suggested by Rumelt (1974) to classify the firms into different diversification categories.

2. Performance of diversified firms has been measured through profitability measures like Return On Assets, Return On Equity, Return On Investment, growth measures in terms of sales, assets and risks measures such as variability in returns.

3. Very few studies have tried to find out the performance of diversified firms as constrained by market or industry structure variables. Few others tried to measure the market performance in terms of equity of returns.

4. Out of the two types of diversifiers, the diversifiers into related area are found to out-perform the unrelated diversifiers due to superior risk pooling characteristics.

1.9 NEED FOR THE STUDY

Corporate diversification in India is not a well researched subject. The studies referred above are presenting the classification of the diversifiers into
Table I.1

RESULTS OF LAKSHMI'S STUDY

<table>
<thead>
<tr>
<th>variable</th>
<th>F-Value</th>
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<tr>
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<tr>
<td>Diversification Strategy vs ROE</td>
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<tr>
<td>Diversification Strategy vs SIZE</td>
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</tr>
<tr>
<td>Diversification Strategy vs Growth in Total Assets</td>
<td>5 7448</td>
</tr>
<tr>
<td>Diversification Strategy vs leverage</td>
<td>7 8088</td>
</tr>
<tr>
<td>Diversification Strategy vs Risk</td>
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</tr>
<tr>
<td>Diversification Strategy vs Growth in Profits</td>
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<tr>
<td>Diversification Strategy vs Beta</td>
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<td>Diversification Strategy vs leverage</td>
<td>7 4194</td>
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<td>Diversification Strategy vs Systematic Risk</td>
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<td>Diversification Strategy vs SD of ROA</td>
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<td>Diversification Strategy</td>
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<td>M-form implementation</td>
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<td>Control Variables</td>
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<td>Industry (SIC Codes)</td>
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<td>Covariates (Size / Log of sales)</td>
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<td>Anual Asset Growth Rate (Percent)</td>
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<td>Annual Percentage Change in GNP</td>
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<td>Company Trend Residuals</td>
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</tbody>
</table>

Table 1.2

HOSKISSION RESULTS OF OVERALL ANOVA FOR ROA
related and unrelated business activities and their performance without making any
indepth enquiry into the financial performance No attempt has been made to
compare the performance of diversifiers with that of the undiversified business firms
on a temporal basis Further, most studies have made no systematic attempt to
employ sophisticated research techniques to draw generalisation for wider
acceptability and appreciation Therefore, the present study is a modest
attempt with an objective to systematically classify firms based on diversification
strategies being adopted by them and examining the overall trends in operating
and financial performance of the firms and appropriately linking the relevant aspects
of performance

1.10. SCHEME OF PRESENTATION

A picture about the firm's trend in diversification strategies and their adoption
in Indian industry and elsewhere in the world and a brief review of earlier works to
evaluate the functioning of these firms and the need for the present study are given
in this Introductory Chapter

Chapter II deals with the objectives of the present study, methodology
adopted, sources of data, size of sample units, statistical and econometric tools
employed and profile of the select units
The trend in operating performance through capital-output ratios, value added, total and partial factor productivities, in capital formation, the sources which have financed these trends are analysed in chapter III.

Chapter IV has provided the trends in financial performance of select diversified companies. The results of the analysis conducted in respect of capital structure and design, capital formation and the financial performance through ratios are presented.

Different financial measures to evaluate the strategic advantages of diversification are worked out in Chapter V.

Chapter VI identifies and analyses the diversification strategy and overall performance based on accounting based measures and market based measures.

The last chapter contains the broad findings and conclusions of the present study.