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Authors: Alex Kwaku Gyan, Rayenda Brahmana, Bakri Abdul Karim

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Diversification Strategy, Efficiency, and Firm Performance: Insight from Emerging Market

[1]Alex Kwaku Gyan, [2]Rayenda Brahmana, [3]Bakri Abdul Karim
Department of Accounting and Finance, Faculty of Economics and Business, Universiti Malaysia Sarawak, Kota Samarahan, Malaysia, 94300
[1]Kraha27@yahoo.co.uk, [2]brkhresna@unimas.my, [3]akbakri@unimas.my

Abstract

We investigate further the inconsistencies of the diversification-performance link by introducing efficiency as moderating factor. A data of 319 firms was used to conduct a panel data analysis excluding the financial sector industries and the results show three important findings. First, industrial diversification shows a significant contribution in performance improvement while international diversification shows no effect on performance. Yet, international-conglomerate shows a significant negative relationship with performance. Meanwhile, the efficiency results are contrary to our conjecture. We find that efficiency is a factor to enhance performance, but it is not the moderating variable on the diversification-performance link. This implies that the efficiency of the firm has no connection with the link between diversification and performance.

Keywords: *diversification, efficiency, firm performance, corporate strategy*

Introduction

Diversification is a strategic expansion of business into markets, sectors, industries and/or segments, mostly induced by reaction to competitiveness in the business environment (Wang, Ning & Cheng, 2013; Yang, Cao & Yang, 2017). Even though diversification is widely practiced and significantly researched, conflicting theoretical and empirical disagreements still dominate the expanse finance literature on the relationship between diversification and firm performance (Chakrabarty, 2007; Delbufalo et al., 2016; Lee et al., 2012; Sun & Govind, 2017). What worsens the situation in emerging economies bothers on the fact that, significant amount of work on this relationship has focused on data from the developed economies and consequently, findings regarding diversification and firm performance in smaller and emerging economies are sparse (Lee et al., 2012; Mathur, Singh & Gleason, 2012). In breaking the deadlock of the mixed views in the diversification-performance link, several variables playing both moderating and mediating roles have been investigated by previous research. These variables include productivity (Gyan, 2017), ownership structure (Lee at al., 2012), effect of economic environment (Charkrabarti et al., 2007), corporate governance tools (Anderson et al., 2001), degree and composition of diversification (Guo & Cao, 2012), and technology effects (Cesaroni, 2002). In all these previous analysis, diversification-performance relationship has been inconclusive. Meanwhile no research has touched on the moderating effect of efficiency to ascertain its impact in that link.

The fundamental contention holds that single focus firms are better off in terms of performance (Berger & Ofek, 1995; Lamont & Polk 2002; Lang & Stulz, 1993; Rajan, Servaes & Zingales, 2000) as compared with diversified firms. Nevertheless, proponents of