Strategic Redirections
How Fortune 1000 Companies
Are Redirecting
Their Strategic Profiles

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ABSTRACT

The purpose of this paper is to define and operationalize a measure for corporate strategic change within the business portfolios of multibusiness firms. The shortcomings with the diversification typology in measuring change within multibusiness firms is addressed. Strategic redirection is coined to describe the phenomenon of strategic change occurring during the last 10 years within the multi-business firm. The concept of change in the core business is used as a measure to capture changes within the portfolios of multi-business firm. Using this measure, the extent and magnitude of such strategic change is described within a random sample of firms drawn from the F1000 manufacturing firm population.
INTRODUCTION

Many large companies have undergone a phenomenon of strategic change during the late 1970s and 1980s that differs remarkably from previous measurements of strategic change. In the past much of the attention on changes in the firm's business portfolio concentrated on the phenomenon of diversification and its increasing incidence (Chandler, 1962; Miles, 1982) as well as the different types of diversification, e.g. related vs. unrelated that were being followed (Wrigley, 1970; Rumelt, 1974). Therefore much of the empirical research on diversification concentrated on the measurement of diversification as well as analyzing economic and performance factors that could explain the diversification phenomenon (Montgomery, 1979; Biggadike, 1976; Bettis and Prahalad, 1984).

Additional research focused on the methods of investment: acquisition or internal development (Pitts, 1977); as well as the issue of divestment (Gilmour, 1973; Porter, 1976; Duhaime, 1981); and the existence of exit barriers to divestiture (Harrigan, 1980, 1981, 1982) that ultimately impact the business portfolio of the firm. These research streams address the central issues which corporate management confronts when changing the composition of the firm's portfolio.

The evidence that firms are experiencing major strategic changes is all around us. Not a week goes by without some major announcement concerning a merger, acquisition or disposition of a business. Salter and Weinhold (1979) in their research on the late 1970s merger movement found that the most significant characteristics of the recent merger movement has been the high level of acquisition activity by the so-called blue chips of american business. In addition, divestment and so called restructuring activity has gained much business popularity in recent years. There is a host of
restructuring activity within many multi-business firms that have chosen to narrow their focus by lopping off divisions (e.g. see "Splitting Up: The Other Side of Merger Mania, Business Week, July 1, 1985).

However varied the underlying causes and motivations, many firms have adopted fundamental and significant changes in their corporate strategies. These firms have radically altered their corporate strategies through changes in the mix and the relative emphasis of businesses within their portfolios. Because each firm's internal resources and the industries in which they participated differed, the courses of action varied. For some firms these strategic transformations radically alters the nature of the firm in terms of the portfolio of businesses in which it competes. Witness Gould's transformation of an industrial oriented firm to an electronics firm (see Table 1).

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<tr>
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<tbody>
<tr>
<td>Electronics</td>
<td>36%</td>
<td>46%</td>
<td>55%</td>
<td>76%</td>
</tr>
<tr>
<td>Battery</td>
<td>35</td>
<td>28</td>
<td>20</td>
<td>24</td>
</tr>
<tr>
<td>Industrial</td>
<td>29</td>
<td>26</td>
<td>25</td>
<td>-</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>100</td>
<td>100</td>
<td>100</td>
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Gould's strategic alteration is reflected by its chairman, William T. Ylvisaker: "Gould is following a strategy of applying its technological and financial strength to the development of high-margin products for selected high-growth electronics markets. Because we think electronics has by far the
greatest growth opportunities in the 1980s and 1990s, that's where we have
decided to concentrate our investment" (Gould Corporation, Annual Report,
1981). This change in strategic direction can be captured by examining the
distribution of revenues within the corporate portfolio.

For other companies, the change in strategic direction is not quite as
encompassing, but nonetheless quite dramatic. Witness Roger Smith's
transformation of the strategic posture of General Motors through the recent
acquisitions of EDS and Hughes Aircraft. The focus of these changes in
strategy at both Gould and General Motors is at the corporate level. These
activities represent managements' attempts to redirect the corporate
portfolios under their direction.

The significant corporate strategic change of the type as described here
is a new, emerging phenomenon. The re-thinking of strategy on the part of a
diversified firm involves a realignment in the number and types of business
activities for the firm. Strategic change entails moving from one portfolio
of business activities to another, but different portfolio of businesses. The
process of changing a firm's business portfolio has not been fully addressed
as a research issue. The dearth of research is due largely because
significant strategic change within predominantly multi-business firms is a
new phenomenon.

The existing ways of looking at corporate strategy have focused on the
transition of a single business to a diversified firm. However as Rumelt
confirmed in his analysis, most firms in 1974 were already diversified and
thus multi-business in nature. Further changes in the firm's portfolio are
only captured by the diversification typology when the firm experiences a
change in diversification category such as going from a related to unrelated
diversifier. Significant strategic change that does not cut across
diversification category is not captured by a measure of diversification. Because the nature of this type of strategic change is not recognized by the measures for diversification it has eluded research attention.

In addition, the literature on divestment and exit barriers addresses strategic decisions concerning one particular business. The overall change in the corporate business portfolio is a reflection of many of these decisions impacting the overall composition and importance of businesses within the portfolio. As a result this research stream while addressing specific corporate decisions regarding one particular business or industry falls short in addressing the overall corporate strategic change within the portfolio of a diversified firm.

Thus far, there exists no recognized way of measuring this phenomenon. Yet due to the predominant diversity of most large businesses, it is exactly this type of strategic change that is of research interest.

While the business press provides plenty of anecdotal evidence, very little is known as to the extent of such strategic transformations within the economy. As a result it is a unique and pressing issue for the management of these firms. It is strategic change of this level and nature that this research will address. In this paper, this type of strategic change will be called strategic redirection. The concept of strategic redirection is presented as a way of describing strategic change at the corporate level.

THE PHENOMENON OF STRATEGIC REDIRECTION

The nature of strategic change examined by this research is distinctly different from that of diversification. Before we examine the exact nature and extent of strategic redirection, it is first necessary to distinguish the
type of strategic change called diversification from the phenomenon strategic redirection. In the case of diversification, adding businesses reduces the relative size of the core business. Thus the firm has followed a strategy of reducing the importance of the core business. Similarly this type of activity could be construed as strategic redirection. What then differentiates strategic redirection from diversification?

In the case of single business firms, strategic redirection can be diversification. One of the major strategic changes these firms have open to them is to lessen their dependence on one business by adding other business activities. The variety of strategic options open to single business firms can be depicted as follows (See Figure 1).

Figure 1

Strategic Change
Within
Single Business Firms

SINGLE BUSINESS

Decrease Core Business
    /\                          /\      \
  Add New Businesses          Divest Core
(Diversification)            (Liquidation)

Expand Core Business
    /\                          /\      \
Expand Scope of Activities
The variety of strategic outcomes can be accomplished by a combination of acquisitions, divestitures, and/or internal investments. The single business firm can remain in one business and enlarge its scope of activities either through horizontal expansion and/or vertical integration. If the firm becomes a multi-business, the change in strategy is captured as diversification.

In the case of a multi-business firm, the diversification typology can only capture strategic shifts across diversification categories. A shift in diversification strategy may be due to changes in the firm's specialization ratio; related ratio; and/or the nature of the linkages between businesses. For instance a decrease in the related ratio for a multi-business firm, could mean a shift in strategy from related diversification to unrelated diversification. Similarly, a change in the way a firm's businesses are related could indicate a shift in strategy from constrained to linked diversification, or vice-a-versa.

However, a multi-business firm can undergo significant strategic shifts without changing diversification categories. A firm can remain in one diversification typology and can nonetheless use other means by which to change the character and quality of businesses within the portfolio. It can substantially alter the importance of the core business without changing diversification strategy. As can be seen, the diversification typology is limited in its ability to capture strategic shifts within a multi-business firm (See Figure 2).
Diversification does not begin to capture these types of strategic change. Since large firms are now predominantly multi-business in nature, it is this type of strategic change that is of academic interest. Strategic redirection as measured by a change in the importance of the core business is an attempt to capture these types of strategic activities.

**NATURE OF THE STUDY**

In order to fully examine the nature of strategic change, a random sample of 200 firms from the F1000 were selected and examined for the time period 1973–1981 with three specific data collection points: 1973, 1977, and 1981. For this study, a data base was constructed including both financial and managerial variables, thus allowing the analysis of both aspects in the
study of strategic redirection. Financial data on the composition of the firm's business portfolio was collected as well as data on the identification of the core business to the firm and the industry of the core business.

The purpose of the study was to operationalize a measure for changes in the business portfolio and to measure the incidence and magnitude of such changes within the sample. In addition, managerial and economic variables were examined to provide explanation as to the rationale for strategic redirection. In this specific paper, only the issue of defining and describing the incidence of strategic redirection will be addressed.

CHANGE IN CORE AS A MEASURE FOR STRATEGIC REDIRECTION

One of the major objectives of this study was to develop a measure for the concept of strategic redirection. In examining a variety of alternatives, a change in the relative size of the core business was selected to represent strategic redirection. Changes in the importance of the core business over time captures strategic activity within the whole range of businesses within the firm. The use of a measure that focuses on the core business of a firm is both logical and well supported by the previous research stream on diversification.

Change in Core as a Basis for Understanding Diversification

The diversification research and literature has developed a measure of diversification as well as different categories of diversification based on the delineation and relatedness of the discrete product-market activities within the firm. Wrigley (1970) used a "specialization ratio" to characterize the proportion of a firm's annual revenues attributable to its largest discrete product-market activity. The firm is categorized as being in one of three categories based on the relative size of their largest product-market
activity. Thus the initial measure of diversification in the policy field utilized the core business and its relative size to the firm as a demarcation of the extent of diversification.

Subsequently, Rumelt (1974) developed a "related ratio" to characterize the proportion of a firm's revenues attributable to its largest group of businesses that are related in some way to one another. Rumelt utilized his measure of relatedness to further demarcate diversification strategies. The delineation between related and unrelated diversification was based on the value of the firm's related ratio. Similarly differences between constrained and linked diversification were based on the nature of the linkages between the businesses.

The development of these diversification typologies relied on the delineation of what constituted the core business for the firm; its relative importance to the firm; and the nature of the linkages between the core business and the other activities of the firm. Shifts in the importance of the core business and its relation to the newly entered domains of the firm were used as a basis for identifying diversification strategies.

**Importance of the Core Business**

Similarly, the core business is also a good measure of significant strategic shifts in a diversified company. The core depicts the central focus of the firm. It represents the single largest business for the firm and in many cases it is also the historical base business of the firm. For a single business firm, the core business is the firm.

Even for a multi-business firm, the center of gravity is still the core business. If problems exist within the core business, the firm is hit hardest. Its preeminence as the largest business in the total portfolio means that problems in the core cannot be ignored. Difficulties within the core
business will be reflected in the bottom line for the firm. It is management's concern with the overall well being of the firm that leads to strategic focus on the activities of the core business.

Furthermore, based on the diversification literature, a firm's financial performance is linked, in part, to the manner in which its business activities are related. Firms which diversified by adding businesses unrelated to the core business, were on average poor performers (Rumelt, 1979; Montgomery, 1979). Thus from a performance standpoint, the core business is important.

**The Core Business and the Role of Top Management**

The nature of the top management task also differs according to the nature of the core business and the strategy of diversification. In an unrelated diversified firm, management is responsible for a set of businesses analogous to a stock portfolio since there is a lack of interaction or integration among the businesses within the firm. In an unrelated, diversified firm, the financial function predominates the role of top management.

In a related diversified firm, however, management must actively manage the portfolio of businesses and be aware of resource interaction and interdependencies when allocating capital among the portfolio. The role of management is more extensive when the businesses must be thought of as more than a portfolio of financial investments.

To define or delineate firm strategy in terms of what happens to the core business incorporates the significance of the relationship between the managing of the firm and its core business. Utilizing what happens to the core business as a measure of strategic change rests on this underlying logic.
A Measure for Strategic Redirection

Based on an examination of a variety of measures, a change in the importance of the core business was used to capture the overall redirection in strategy within the firm. This variable was calculated by examining the difference in the relative contribution of the core business to the firm's total revenues in 1973, 1977, and 1981. The change in the relative contribution of the core to total revenues from 1973 to 1981 was called change in the core business.

This one variable captured a variety of strategic activity within the firm. The change in the relative size of the core business could either be positive: i.e. the core's relative contribution to the firm's revenues increased; zero; i.e. the relative contribution of the core business to the firm's total revenues stayed the same; or it could be negative: i.e. the core's relative contribution to the firm's revenues decreased during the time period. In examining the possible ways that the relative importance of the core business might change, it is useful to examine the possible means by which such a transition might occur as in the following diagram (See Figure 3).
A change in the relative size of the core business over time captures strategic activity within the whole range of businesses within the firm. While the firm may not do anything specifically relating to the core business, its action with regard to the other businesses within the portfolio as well as any possible new business additions will be reflected in the change in the relative importance of the core business.

By selective investment in non-core businesses within the existing portfolio or through the addition of new businesses, the firm has chosen to lessen its dependence on the core business. Likewise the divestment or writing off of its core business will also result in a decreased dependence on the core.

Similarly the divestment or shutting down of non-core businesses within the portfolio will result in an increase in the relative size of the core business. In addition the active expansion of the core business through
internal development or acquisition at the expense of investments in the remaining mix of businesses will result in an increase in the relative size of the core business within the portfolio.

Thus changes in the business mix of the firm will be reflected through changes in the importance of the core business. Furthermore, strategic activity such as acquisitions, mergers, and divestments will also be reflected in changes in the importance of the core business. Even if a firm has no acquisition or divestment activity, unless all of its businesses grow at the same rate, a change in the business mix will occur. That is why change in the importance of the core business is a fundamental measure of strategic redirection. It captures the redirection of the firm as a result of both capital investment decisions as well as acquisition, merger, and divestment activity. Using importance of the core business as a means by which to operationalize strategic redirection, enables this study to capture a variety of means by which a firm can change strategically in one measure.

FINDINGS

Description of Strategic Redirection

Based on a large random sample study of firms drawn from the 1000 largest U.S. industrial companies, the magnitude of strategic redirection as measured by a change in the importance of the core business during the time frame (1973-1981) is widespread. The majority of firms in the sample experienced some degree of change in the relative size of the core business over time. Among the sample as a whole, 62% of the firms experienced a significant change in the importance of the core business. For these firms, the size of the core business had increased or decreased by more than 5% of total sales by 1981.
The underlying trend was a decrease in the dependence of the firm on the core business. In other words, the size of the core business as measured by the percent of total revenues has declined over time. The importance of the core business is statistically different for each point in time: 1973, 1977, 1981. The extent and size of the change in the core business for both single and multi-business firms is shown by the following (See Table 2).

Table 2

<table>
<thead>
<tr>
<th>Change in the Importance of the Core Business</th>
<th>Single Business</th>
<th>Multi-Business</th>
</tr>
</thead>
<tbody>
<tr>
<td>Size of Core Business (1973)</td>
<td>99.5%</td>
<td>55%</td>
</tr>
<tr>
<td>Size of Core Business (1981)</td>
<td>92.6</td>
<td>47</td>
</tr>
<tr>
<td>Decline</td>
<td>6.9</td>
<td>8</td>
</tr>
<tr>
<td>% Decline</td>
<td>7%</td>
<td>15%</td>
</tr>
</tbody>
</table>

The delineation of the sample between single and multi-business firms was deemed meaningful due to the significant differences in the measure of strategic redirection between these two groups of firms. Based on this categorization of the sample, single business firms on average experienced less relative change in the size of their core business than did multi-business firms.

Strategic Redirection in Single Business Firms

Since 95% or more of their sales were in one business activity in 1973, these firms were less likely to undergo major changes in the size of their core business. The reason for the lack of strategic redirection among single business firms are twofold. First, the relative size of the core business could not increase by much since it already comprised 95% or more of total sales. Similarly, very few single business firms experienced a decrease in
the importance of the core business. Due to their nondiversified nature, a decrease in the importance of the core business would involve the addition of new businesses unfamiliar to the firm. A change of this nature would require a dramatic departure in the overall strategic direction for the firm.

However, of those single business firms that did experience a change in the importance of the core business, the average change in core size was 27% of total sales. These firms decreased their dependence on the core business through sizeable investments in a broader portfolio of businesses.

**Strategic Redirection in Multi-Business Firms**

Within multi-business firms, 88% experienced a change in the importance of the core business greater than 5% of sales. Some firms experienced an increase in the size of the core business. However, the majority reduced the relative size of the core business during this time period.

**Decreased Importance of the Core Business**

For both multi-business firms and single business firms the decrease in the importance of the core business is predominantly offset by an increase in revenues attributable to the addition of new businesses to the firm. While the absolute size of the core business may not have actually changed for these firms, the relative size of the core declined within the firm's business portfolio. This can be seen by the following (See Table 3).
### Table 3

<table>
<thead>
<tr>
<th>Changes in the Business Portfolio</th>
<th>Single Business Firms</th>
<th>Multi-Business Firms</th>
</tr>
</thead>
<tbody>
<tr>
<td>Decline in Core Business as a % of Total Sales</td>
<td>6.9</td>
<td>8.0</td>
</tr>
<tr>
<td>Revenues Attributable to New Businesses as a % of Core Business Decrease</td>
<td>98%</td>
<td>64%</td>
</tr>
<tr>
<td>Revenues Attributable to a Change in Existing Mix as a % of Core Bus. Decrease</td>
<td>2%</td>
<td>36%</td>
</tr>
</tbody>
</table>

The overall decline in the relative size of the core business was offset by a change in emphasis among other businesses within the firm. For single business firms, the reduction in relative size of the core business was accounted for by an increase in revenues attributable due to the addition of new businesses. For multi-business firms, both emphasis on non-core businesses within the portfolio as well as the addition of new businesses offset the decrease in the importance of the core business.

**CONCLUSION**

One of the major contributions from this study is the identification and measurement of corporate strategic change within organizations. In the strategy field, the diversification and strategy typologies do not capture the new wave of strategic redirection many firms are experiencing. The multi-business nature of many large firms means strategic redirection can no longer be captured through diversification strategy alone. This study provides a measure of strategic redirection by which to begin to examine the nature of corporate strategic change. It is a significant first step in our ability to study the nature of current strategic redirection.
To begin with, a new concept by which to describe dramatic strategic change has been defined and measured for a large sample of firms. Strategic redirection was operationalized by using relative changes in the firm's core business as a measure of change. The use of a measure for strategic redirection relying on changes in the core business captures the essence of strategic shifts within the firm. The core business is the predominant business within the firm, thus representing the skills and competencies of the firm. In addition, due to its relative importance, much of management's strategic orientation is focused on this one business. Furthermore it is consistent with the emphasis given the core business in the diversification literature. Similarly, within the industrial organization economics literature, there has been a stream of research examining the competitive characteristics of the industry for the base or core business.

Despite the implicit reliance on the core in establishing diversification typologies, changes in the relative importance of the core business has not been used previously to track corporate strategic change. Yet as evidenced by this research, core change can be a very good surrogate for corporate strategic change. The use of changes in the core business as a measure of strategic redirection presents a new way of thinking about corporate strategy. Due to the significance of the core business to the firm, problems within the core may lead to a change in the overall strategy for the firm. Therefore using changes in the core business as a measure provides both a logical way to interpret strategic change as well as a means to investigate what may be associated with a change of this nature. The development of a quantitative measure to capture strategic redirection is a major accomplishment of the study. It provides for the first time a way of examining strategic change within large business organizations.
The utilization of the mix of business by which to measure strategic redirection is a sound basis from which to research strategic change at the corporate level. Major shifts in strategy within a multi-business firm will reflect itself in changes in the business portfolio. By examining changes in the mix and particularly those impacting the core business, this research has contributed to our understanding of the nature and extent of strategic shifts within large business firms.

The results of this study has improved our understanding of strategic redirection, but at the same time raised some interesting questions that deserve further attention. By operationalizing and providing a measure for strategic redirection, this research has shown evidence of significant strategic changes occurring among the Fortune 1000 manufacturing firms. Many firms are experiencing dramatic shifts in strategic direction. The environments of the 1970s and 1980s has obviously led to many a re-examination of corporate strategic direction. Likewise, dramatic shifts in managerial style have had their influence on corporate strategy. Additional research is called for to examine both these issues.
REFERENCES


