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Conglomeration: An Investigation into the Incidence and Significance Amongst FTSE100 Companies Since 1993

by

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A thesis submitted in partial fulfilment of the requirements for the degree of
Doctor of Philosophy in Social Sciences

University of Warwick, Warwick Business School

April 2009

Volume 1 of 2

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Word Counts (excluding contents, acknowledgements, declaration, abstract, tables and charts):
Report 80,700
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ACKNOWLEDGEMENTS

This thesis is dedicated to my wife, Melanie, whose patience, encouragement, confidence and unequivocal support made it possible. I owe her a great deal.

My supervisor, Professor John McGee, has provided invaluable guidance and support throughout this research project bringing his considerable knowledge and experience to bear on a broad range of issues - some expected, others not. John is also thanked for assuming the role of supervisor on the untimely death of Professor Tony Steele.

DECLARATION

The author declares that some background material from this thesis – not the data from the empirical chapters - has been used in two publications. The first publication is a chapter, jointly authored with Professor John McGee, for a book produced by Templeton College, Oxford. The chapter - Corporate Strategy and Structure: The Rise and ?Fall of the Conglomerate - is in ‘Mapping the Management Journey’ edited by Sue Dopson, Michael Earl and Peter Snow and published by Oxford University Press in 2008. The second publication is an article written by the author alone for the ‘Corporate Sector Review’, a magazine for members of the Association of Chartered Certified Accountants working in the corporate sector. The article - The Rise and Fall of Conglomerates - was published in March 2008. Material for both publications was drawn principally from the literature review.

The author declares this thesis, which has not been submitted for a degree at any other university, to be all his own work.

ABSTRACT

This research created a database of financial and non-financial information extracted from DataStream, annual reports and accounts, company websites and other reputable sources to investigate the incidence of conglomeration amongst the largest, by market capitalisation, companies, both industrial/manufacturing and service, that comprised the London Stock Exchange FTSE100 index at the end of 1993, 1998 and 2003.

Categorising companies according to the 4-category Rumelt-based scheme used in previous UK research by Channon (1973, 1978) and Whittington & Mayer (2000), this research has found support for the contention, based on anecdotal evidence, that conglomeration amongst the FTSE100 has declined, especially between 1998 and 2003. Rather than confirming the evolutionary flow of companies through the Model of Corporate Development from single business to conglomerate strategies, the research shows more companies to have retreated to greater focus than advanced to wider diversification. Furthermore, the breadth of activities pursued by conglomerates fell through the research period and there was also an increase in diversified companies with a core activity generating more than 50% of their turnover.

Whilst acknowledging that several conglomerates were created by strong business personalities including Lords Hanson and White at Hanson and Sir Owen Green at BTR, no strong relationships were found between corporate governance and diversification. The enhancement of corporate governance Best Practice resulted in improvements across all companies.

Finally, this research suggests performance is not a primary driver of the trend towards focus but that financial/market and regulatory, especially competition authority, factors led to changes in diversification through a mixture of divestment, demerger, capital reduction/downsizing, acquisitions and internationalisation. The Model of Corporate Development has become multi-directional with movements influenced by generic, industry specific and company specific factors. There is also an inherent trade-off across diversification categories in the potential level of risk, growth, scale and scope benefits.

1. EXECUTIVE SUMMARY

This research was undertaken in response to the growing body of anecdotal evidence suggesting conglomeration had declined amongst the largest UK companies calling into question its continued validity as a corporate strategy. The project also sought to bring research into diversification into the 21st century adding to extant UK research that ended in 1993 for industrial/manufacturing companies and 1974 for service companies.

In a slight departure from prior research which selected the largest UK companies by turnover or its equivalent, the population used in this research are companies, both industrial/manufacturing and services, quoted on the London Stock Exchange and comprising the FTSE100 index; the companies with the highest market capitalisations. By extracting relevant financial and non-financial information from DataStream, the Financial Times, company annual reports and accounts, company websites and other reputable and reliable sources a database was created for companies that were constituents of the FTSE100 at the end of 1993, 1998 and 2003. The database comprises summary profit & loss, balance sheet and ratio information for every year available on DataStream and all other information - segmental reports, board composition and investor data (share prices, P/E ratios, yields, market capitalisations) – for 1993, 1998 and 2003. The segmental data held was used to categorise each company according to its degree of diversification in 1993, 1998 and 2003. The database was mined to produce tables summarising diversification, movements between diversification categories, breadth of activities, FT classification, corporate governance and performance

in 1993, 1998 and 2003. A set of tables was produced for the full FTSE100 and another for the 54 companies that were constituents of the FTSE100 at the end of 1993, 1998 and 2003; the FTSE100 Survivors. In addition, each of the tables was split between industrial/manufacturing and service companies.

The results of the research show that conglomeration declined and focus increased through the research period amongst the FTSE100 and FTSE100 Survivors and both the industrial/manufacturing and service sectors. In addition, notwithstanding the unobservable effects of company changes to their reporting divisions, the breadth of conglomerates' activities narrowed through the period 1993 to 2003. The greater focus may explain the increase in institutional shareholdings in conglomerates through the research period.

Although the research did not originally intend to consider performance in detail, in looking for the drivers of the move to greater focus links between performance and diversification were investigated; no clear consistent significant relationship was found. Similarly, there were no major differences between the corporate governance standards of different categories of company, although there was a general improvement in line with enhanced Best Practice. There was no link between conglomeration and FT classification.

The need to identify the drivers of strategic change led to the compilation of histories for those companies identified as conglomerates in 1993, 1998 or 2003. The histories suggest adoption, maintenance and abandonment of

conglomeration is driven by a variety of financial/market and regulatory, especially competition authority, factors and that the Model of Corporate Development needs revision to reflect these forces. The new Model shows movement to be two-way and dependent on generic, industry specific and company specific drivers.

Overall, this project has brought UK research into diversification into the 21st century. Through the creation of a new database, which contains significantly more information than has been used in this research and is capable of extension/updating, this research has found clear support for the anecdotal contention that conglomeration amongst the UK's largest, by market capitalisation, listed companies has declined substantially. Furthermore, the unpopularity of conglomerates is representative of a broader move towards greater focus. This research also identified non-performance factors - generic, industry specific and company specific - that influence movements, both forwards and backwards, through the Model of Corporate Development and an inherent trade-off across diversification categories in the potential level of risk, growth, scale and scope benefits.

2. INTRODUCTION TO CONGLOMERATION

This chapter provides an overview of the background that gave rise to this research into the incidence and significance of conglomeration amongst the largest, by market capitalisation, UK listed companies; constituents of the FTSE100 index. By definition, companies covered by this research are major contributors to the UK economy and their success or failure has significant implications for the nation's prosperity. Anecdotal evidence suggests that since 1993 fewer of these companies have chosen to either adopt or maintain conglomerate strategies although this has yet to be proven by research.

2.1 Overview

After World War II, encouraged by a number of positive - environmental, regulatory and management - factors, the US and the UK saw substantial growth in unrelated diversification (conglomeration) in place of focus. Companies were following the generally accepted evolutionary path from focus to diversification in the Model of Corporate Development (See chart 1). Research shows that, largely in response to negative changes in financial/market and regulatory factors, US conglomeration stalled in the late 1970s before reversing through to the end of the millennium. In the UK, while similar research suggests growth through to the early 1990s, there is only anecdotal evidence that the maturity and decline phases of the conglomerate life cycle were experienced thereafter.

In the US, by 1969 the single business industrial/manufacturing companies that predominated had become a minority with related and conglomerate

companies increasingly pre-eminent accounting for 45% and 19% respectively of the Fortune 500 (Rumelt, 1974). The 1980s saw the tide turn and by 1990 US companies were retreating from conglomeration seeking a return to focus - '*sticking to the knitting*' (Peters & Waterman, 1982, p292-305) - that continued through to the new millennium (Franko, 2004). Research by Williams, Paez & Sanders (1988) found that, between 1975 and 1984, there had been a reduction in the number of businesses managed by US conglomerates and that the relatedness between those businesses had increased; a clear move to greater focus.

In the UK, limited research shows similar but more restrained post-war growth in conglomerate strategies among industrial/manufacturing companies. By 1970, 6% of the largest 100 companies were conglomerates; a threefold increase from 1950 (Channon, 1973). The most recent UK research (Whittington & Mayer, 2000) suggests that through the 1980s and early 1990s, rather than decline as in the US, conglomeration had continued to grow reaching 11% by 1983 and 24% by 1993. Anecdotal evidence, including the observed retrenchment of conglomerates such as BAT Industries, Hanson, BTR and Williams, suggests that since 1993 there has been a reappraisal of UK conglomeration as a valid corporate strategy and, as a decade earlier in the US, a move toward greater focus. Research has yet to prove this to be the case.

This research aims to extend UK research into conglomeration beyond 1993 to discover what has happened to conglomeration as a corporate strategy and

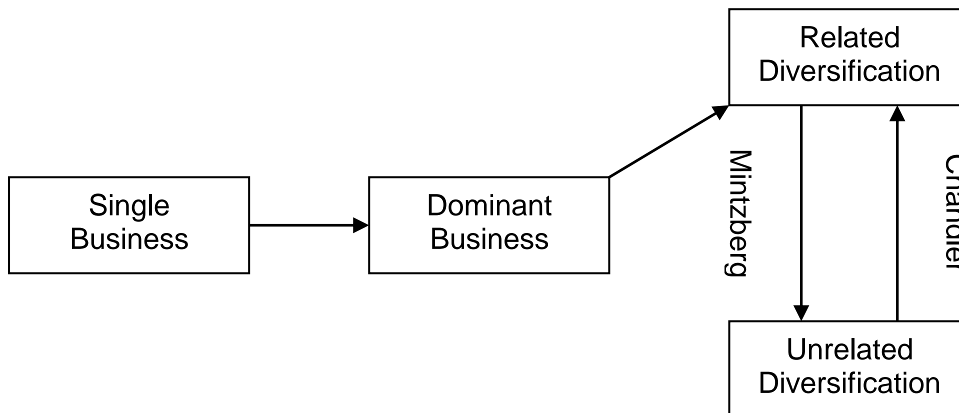
to companies that retained, adopted or abandoned the strategy through to 2003. Furthermore, recognising that services account for more than half of the UK's economic activity, this research considers not only industrial/manufacturing companies but also service companies which have been neglected in research since Channon's (1978) work.

This research addresses these issues through the creation and analysis of a new and unique database of quantitative and qualitative data on the 100 UK companies with the highest market capitalisations; constituents of the London Stock Exchange FTSE100 index in 1993, 1998 and 2003.

2.2 Corporate Evolution

The key model illustrating the evolutionary route taken by companies is shown in Chart 1 below and, while accepting that a company may stop at any stage or regress, it suggests that unrelated diversification (conglomeration) is the final destination. Although the Model does not identify drivers behind a company's evolution it does show a flow from simplicity – single business - through to complexity – conglomeration – with dominant business and related diversification as intermediate stages. Many researchers in this field have based their expectations regarding corporate evolution on this model.

Chart 1: Model of Corporate Development



Source: Whittington & Mayer (2000, p127)

The original 3-stage model (Scott, 1973) showed single business companies developing into dominant business companies before diversifying into related businesses. The fourth stage, an option for related diversifiers, unrelated diversification (conglomeration) was added by Mintzberg (1979). While this extension may be considered logical, it has certainly proved controversial given researchers' differing and conflicting views as to the sustainability of conglomeration as a corporate strategy. Critics of Mintzberg's fourth stage cite Chandler's (1962) belief that conglomeration is unsustainable with companies retreating back to related diversification, a view reinforced by Hall & St. John (1993) while supporters of Mintzberg champion the views of Channon (1973, p238) who couldn't countenance a reverse flow in the Model believing that *"once adopted, the strategy of diversification tended to become institutionalised"*. This debate highlights a major point regarding the Model which, unlike ecological and biological evolution which is based on a premise of continual development and improvement, suggests that companies are faced with a choice at each stage in their corporate evolution; they can

advance to a ‘higher’ stage, they can remain where they are or they can retreat back to a ‘lower’ stage.

Application of the Model to understand how companies have evolved over time requires each stage to be clearly defined and, to enable related and unrelated diversifiers (conglomerates) to be distinguished, a robust rationale to determine relatedness between a company’s activities; when does a related diversifier become a conglomerate? While activity turnovers can provide a basis for category definitions, assessing the relatedness between activities is more problematic. Furthermore, it is essential to recognise the inherent subjectivity in any assessment of relatedness.

While acknowledging alternative approaches to the assessment of relatedness, e.g. Prahalad & Hamel’s (1990) ‘portfolio of competences’, there appears to be broad agreement between several leading researchers in this field as to the most practical approach. Rumelt (1974), Channon (1973, 1978) and Whittington & Mayer (2000) consider relatedness between activities to be a product or service based concept centred on the question; are there key similarities between the products and/or services provided? Given the lack of sufficiently detailed publicly available information it is not possible to base assessments on commonality of processes and/or capabilities.

In categorising FTSE100 companies, this research has also adopted the product/service-based approach and looked for similarities between services and/or products in assessing relatedness.

2.3 Development and Growth of Conglomeration

As discussed below, conglomeration was initially a US phenomenon driven by several factors that may be considered to have created the ideal conditions for companies to grow through diversification.

The 1960s and 1970s saw a peak in mergers and acquisitions activity in the US as companies sought ways to grow through the re-investment of surplus cash flows generated by their increasingly profitable activities in the post World War II growth years. There was a marked reluctance by managers to return surplus cash to shareholders and investors encouraged companies to retain and invest those funds welcoming conglomeration. Investors had become convinced that conglomerates offered growth, increased profitability and, as a result, higher dividends and/or capital appreciation. The strong investor support for conglomerates is illustrated by Matsusaka (1993) who used data from the 1960s and 1970s to show that share prices of US companies making unrelated acquisitions appreciated while those of related acquirers depreciated. By 1969, 45% of the 500 largest US industrial/manufacturing companies were diversified and 19% were conglomerates (Rumelt, 1974).

The theoretical justification for growth through diversification is outlined by Penrose (1959, p113) who believed that companies with narrow product offerings – the single business and dominant business companies of the Model for Corporate Development – were constrained in their profit potential by market growth limitations and, because of their dependence on a limited

range of products/services, were vulnerable to changes in demand and competition. Furthermore, she believed that while aggressive competitive strategies, e.g. pricing, maintenance of restrictive trade practices and control of monopolistic markets, could prolong the success of non-diversified companies they did not represent viable long term strategies as competition authorities would act to restore the competitive balance in the industries and/or markets affected. Antitrust policy and regulatory regimes are seen by many as having a strong bearing on diversification. Shleifer & Vishny (1994, p405) comment that *"…it is hard to believe that diversification would have taken the enormous proportions that it did without the prevailing antitrust policy"*.

In addition to the search for growth and the enthusiastic support of investors, there were other drivers behind US conglomeration including the pursuit of earnings stability/low risk, the balance in the principal (shareholder)/agency (manager) relationship where the balance of power had shifted away from owners/shareholders to managers, stock market inefficiencies, tax incentives, changes in capital markets increasing the supply/availability of funds, increased globalisation and the leveraging of management skills with managers believing their skills were effectively generic and could successfully be applied to acquisitions regardless of business activity. In his Hubris Theory, Roll (1986) attributes much acquisition activity to managements' desire for power and the greater financial rewards associated with larger companies and notes that managers will 'take advantage' of owner (shareholder) apathy.

The post-war growth in the adoption of conglomeration cannot, therefore, be adequately explained by a single event but rather by a confluence of favourable environmental, regulatory and management circumstances and attitudes (managerial, investor and debt holder) that effectively made conglomeration appear to be a very attractive strategic option

UK conglomerate growth in the post-war years, albeit slower than in the US, was driven by similar factors to those prevailing in the US.

Table 1: UK Manufacturing Company Diversification, 1950-1993

Category	1950[1]		1960[1]		1970[1]		1983[2]		1993[2]	
	No.	%	No.	%	No.	%	No.	%	No.	%
Single	31	34	18	19	6	6	5	6	3	5
Dominant	38	41	35	36	34	34	12	16	7	10
Related	21	23	39	41	54	54	50	67	41	61
Unrelated	2	2	4	4	6	6	8	11	16	24
Totals	92	100	96	100	100	100	75	100	67	100

Source: [1]Channon (1973, p67) 100 largest UK manufacturing companies as in 1969-70, [2]Whittington & Mayer (2000, p139) UK based companies among largest 100 manufacturers as in 1983 and as in 1993.

Channon (1973), in research into diversification undertaken as part of a Harvard sponsored programme (Scott, 1973), found there had been a move toward diversification, especially related diversification. Between 1950 and 1970 related diversification increased from 23% to 54% while conglomeration increased far more slowly from 2% to 6% which was significantly below the 19% in the US in 1969. This suggests that, as in the US, UK investors saw diversified companies as the 'future' although they appeared reluctant to move into unrelated activities. Research under the Harvard programme by Pavan (1976) in Italy and Dyas & Thanheiser (1976) in France and Germany also suggests growth in UK conglomerates was similar to that in Italy but lagged behind France and especially Germany where levels were similar to the US.

There was also an increase in conglomeration amongst the largest service companies although the most recent UK research is that undertaken by Channon (1978).

Table 2: UK Service Company Diversification, 1950-1974

All Figs %	Channon					
Category	1950	1955	1960	1965	1970	1974
Single	36	31	23	17	16	16
Dominant	41	42	46	45	26	16
Related	17	19	20	26	45	49
Conglomerate	6	8	11	12	13	19
Totals	100	100	100	100	100	100
Companies	*69*	*74*	*81*	*91*	*100*	*99*

Source: Channon (1978, p31) 100 largest UK service companies as in 1973-74.

Channon (1973, p194) suggested the delay, compared to the US, in the UK's adoption of conglomeration could, in some sectors, have been a result of high levels of family ownership or control that *"might well have retarded diversification"*. This 'corporate conservatism' was overcome as institutional shareholdings increased with a consequent divorce of ownership and control leading to more professional, rather than family, management. At the same time competition, necessarily restricted in the post war years (Scott, 1973), began to gather momentum and to drive companies towards diversification, typically by acquisition, to achieve growth and stability. Channon (1973, p194) summarised the effects of new commercial environment saying that *"The onset of competition produced declining financial returns, a worsening stock market position, and increased vulnerability. Thus, these companies tried to break out from their traditional markets by acquisition"*.

It was not until the 1980s, a period that saw the creation through acquisitions of several iconic conglomerates including BTR and Hanson, the latter

becoming a household name through corporate advertisements on prime-time commercial television, that UK conglomeration began to catch up with the US. Through to the early 1990s UK investors were staunch supporters of conglomerates frequently subscribing for rights and bond issues to provide them with new funds for increasingly large acquisitions.

Research by Whittington & Mayer (2000) brought the UK data up to 1993 and showed conglomeration amongst the largest industrial companies had continued to increase reaching 11% by 1983 and 24% by 1993. This may have been the high water mark for UK conglomeration.

2.4 Re-appraisal and Decline of Conglomeration

In the US, the post-war period saw the creation of many conglomerate groups including ITT, GE, Westinghouse, Allied-Signal and Tenneco. These conglomerates experienced substantial growth through the 1970s and early 1980s becoming highly profitable companies, many with global operations, creating wealth for their supportive shareholders. However, in the mid-1980s several of the favourable conditions that had encouraged conglomerates turned neutral and some even became unfavourable. In regulation, the active US antitrust polices of the 1960s and 1970s that, by effectively limiting core activity growth, contributed to the adoption of conglomeration were replaced by the Reagan administration’s relatively benign laissez-faire policy (Shleifer & Vishny, 1991) that allowed greater horizontal acquisitions activity. In addition, considerable increases in the volume and intensity of global competition

added pressure to focus on core activities to achieve the economies of scale that would support price-based competitiveness.

Investor sentiment had also shifted adversely; conglomeration was no longer seen as the 'best' corporate strategy and the inherent complexity of conglomerates was seen as a barrier to broker/investor analysis. At a time when mastery of a core activity was increasingly regarded as a major attribute, conglomerates were criticised as being archetypical '*jacks of all trades but masters of none*' with management perceived as being incapable of effectively managing disparate activities. Invoking a juggling analogy, the more balls a company had in the air the greater the chance that one or more would be fumbled or, at worst, dropped! In a stark reversal of the position found in the 1960s and 1970s, Morck, Shleifer & Vishny (1990) showed related acquisitions yielding stock appreciation and conglomerate acquisitions stock depreciation. Institutional investors were also becoming increasingly willing, either individually or through associations such as the California Public Employees' Retirement System (CalPERS) to 'flex their muscles' and exert influence over companies in which they had substantial and growing shareholdings and they were less willing to support rights and bond issues made to fund conglomerate acquisitions.

The 1980s also saw more critical appraisal of the financial performance of conglomerates. Ravenscraft & Scherer (1987) provided evidence that conglomerates had failed to produce the financial benefits expected. Evidence was also produced questioning the success of conglomerate acquisitions

activity; Porter (1987), Ravenscraft & Scherer (1987) and Kaplan & Weisbach (1992) showed that acquirers were divesting up to 50% of their acquisitions, especially of unrelated businesses, having failed to obtain the benefits they had expected. Managers also recognised that many acquisitions made in pursuit of conglomeration had actually failed to produce the expected benefits and needed to be divested (Jensen, 1991). There was also increasing concern that conglomerates were cross-subsidising unattractive and/or underperforming activities, some of which may have been acquired in diversifying acquisitions, and that managements were failing to ensure their portfolio of diverse businesses supported the common goals and objectives of the company.

Overall, the disadvantages of conglomeration were increasingly perceived as outweighing the advantages. Shleifer & Vishny (1994) succinctly summarise this reversal in US opinion of conglomerates. Convinced that conglomeration was a fundamentally flawed concept they damningly said that *"in our opinion, both theory and evidence strongly favour the view that unrelated diversification was a mistake from the start"* (p409) and *"the fact that the market thought that conglomerates were a good idea does not mean that they were"* (p417). Moreover, they saw the 30 year US conglomeration phenomenon as *"a round trip for corporate America"* (p403), and the 1980s as bringing *"American corporations back to greater specialisation"* (p403).

Research by Franko (2004) supports the claims of Shleifer & Vishny (1994) that US companies were retreating from conglomeration. Defining a focused

company as one with 95% of turnover in one industry, Franko (2004) showed that among the largest 12 companies in a broad range of major industries the move to focus between 1980 and 2000 was greatest in the US compared to Europe and Japan.

In the UK, it was the mid-1990s rather than the mid-1980s that saw many hitherto highly successful UK conglomerates change their corporate strategies to seek greater focus often achieving change by turning from serial acquisition to serial divestment. Several shrank rapidly to a fraction of their peak size and some experienced severe financial problems. BTR, for example, declined from a position of pre-eminence amongst the top 10 FTSE100 companies in the early 1990s to acquisition by Siebe, another FTSE100 company, in 1999 with the combined group, Invensys, being ejected from the index in 2003. Similarly, beginning with the disposal of most of its US business as US Industries in 1995, Hanson split itself up by demerging its tobacco (Imperial Tobacco), energy (Energy Group) and chemicals (Millennium Chemicals) businesses becoming a focused building materials group which, after being 'exiled' for a brief period after the break-up, returned to the FTSE100 until its acquisition in 2007 by Heidelberg Cement of Germany.

The experience of the US and UK suggests the corporate strategy of conglomeration has a life cycle - development, growth, maturity and decline - similar to the generally accepted product life cycle and that the UK has followed the US into the decline phase. There are, however, suggestions that

this may not be the case and that conglomerates have been unfairly maligned.

Whittington (1999) makes a strong case for the ‘evergreen conglomerate’ suggesting that while some conglomerates may die, e.g. Hanson and BTR, others are born to replace them, e.g. Virgin Group. However, Whittington (1999) does sound a note of caution recognising the need for conglomerates to ensure their diversification is financially sound, doesn’t create excessive (unmanageable) complexity, is commensurate with the talent and ability of its managers and that the option to break-up is always recognised as a possibility. Conglomerates need to ‘manage their life span’ and, where necessary commit ‘corporate euthanasia’. There is some support for the contention that conglomerates have ‘sell-by dates’ (Said, 1999).

This view has some support, in a research report into diversified, slightly diversified and focused companies in the US, Europe and Asia, the Boston Consulting Group (2006) concluded that conglomerates do have a future and that their poor status with analysts and investors, especially in Europe where they found evidence of a conglomerate discount in valuation, is largely unfounded. BCG (2006) found that while, on average over the period 1996-2005, the relative total shareholder return (RTSR) of focused companies at 2.19% exceeded that of diversified companies at 1.34%, the average performance of focused companies was distorted by a few outstanding performers. The research suggested that conglomerates may have actually outperformed the majority of focused companies.

The lack of UK research into conglomeration since 1993 (Whittington & Mayer, 2000) means there is only anecdotal evidence that UK conglomeration declined in the mid-1990s and that conglomerates have since unbundled the portfolios of unconnected or loosely connected business activities they had accumulated over the preceding 10-20 years.

2.5 Factors Influencing Conglomeration

This research has identified a variety of factors that may influence conglomeration. Several of these factors - including risk and stability, leveraging management, the role of competition authorities, declining industries and growth opportunities, agency (manager/shareholder balance of power, management attitudes and science and opportunism/asset-stripping) - are discussed in section 3.3.2.2 of chapter 3 – Literature Review. In addition, the company histories that comprise chapter 7 – Analysing the Historical Record – seek to identify the impact of international rather than product or service diversification, the flexibility of companies to change their portfolio of business activities and/or their core activity and the changing attitudes of investors towards companies pursuing conglomeration. The impact of these factors cannot be measured although their existence and potential influence at generic, industry or company specific levels has been reflected in enhancements to the Model of Corporate Development.

There are also a number of other factors including government policy and the reduction of labour and bankruptcy risks which were identified during the research but which were felt not to have had a significant impact. Government

policy including group tax reliefs, capital allowances (depreciation charges for taxation), regional development grants and technology and/or employment-based incentives may affect corporate investment decisions. However, while government policies may provide assistance for companies to invest in their existing activities it is unlikely that they provide an incentive to diversify. This is especially true since group loss relief restrictions were introduced in the 1970s/1980s limiting the transferability of tax losses between dissimilar businesses. While the relationship between risk and diversification is considered in the literature review and subsequent analyses, the specific issues of labour risk and bankruptcy risk are not explored in depth. Notwithstanding the high levels of UK labour unrest in the 1970s, industrial relations difficulties tend to be short term and are unlikely to drive conglomeration while the avoidance of bankruptcy may encourage a company to change its focus or add related activities rather than to pursue new unrelated activities.

The research also considered factors – internal capital markets, complexity, accounting rule changes and managerial incentives - that, while potentially influential, could not be investigated. We know that internal capital markets should, if efficient, ensure returns are maximised by allocating limited capital to projects offering the highest returns which has implications for diversifying investments. Unfortunately, without details of allocation decisions made by companies it is not possible to assess whether or how far the 'efficient internal capital market' hypothesis applies, or the extent to which the allocation process plays a role in the pursuit, maintenance or abandonment of

conglomeration. Complexity is also an issue for diverse companies which, by definition, present greater management challenges than more focused businesses. Those companies diversifying by acquisition will also face a range of integration problems, including those relating to IT/IS. These problems have been mitigated by developments in management science, including increasingly sophisticated tools, models and frameworks, and greater professionalism. Acknowledging the potential influence of the complexity/diversity relationship, the lack of relevant data precludes its investigation. The effects of changes in accountancy regulations, notably in the recognition of goodwill and the creation and subsequent use of provisions relating to acquisitions, have also been identified as impacting diversification decisions although the database does not contain sufficiently detailed information to assess the effect. Finally, while the attitudes of managers to growth, especially in the context of the agency problems created by the divorce of ownership and control, were considered the research did not specifically investigate whether the granting of stock options and the setting of targets governing their exercise influenced diversification decisions. The database does include the names of chairmen, CEOs and directors – both executive and non-executive - but not their remuneration or incentive packages although this data could be added.

The research also investigated whether UK companies had moved towards less ‘pure’ conglomeration by adopting Asian diversification models where networks of companies – Keiretsu in Japan and Chaebol in Korea - may be considered quasi-conglomerates. While UK companies have recognised the

benefits of establishing closer long-term relationships backwards to their suppliers and forwards to their customers, they have stopped well short of formalising those relationships through significant cross-shareholdings or the establishment of substantial joint ventures. The cross-shareholdings of Guinness and French luxury goods company LVMH (Louis Vuitton Moet Hennessey) was an example of the formalisation of corporate co-operation although it was reversed following Guinness' acquisition of Grand Metropolitan in 1997 to create Diageo. The database, which includes details of the major (above 3%) shareholders of each FTSE100 company, reflects the insignificance of cross-shareholdings.

Finally, the influence of MBOs and MBIs, which have provided ready buyers for the unwanted peripheral activities of conglomerates, is discussed as part of the debate on corporate refocusing.

2.6 Research Questions

A review of literature covering diversification and conglomeration amongst US and UK companies since World War II suggests the number of large industrial/manufacturing companies pursuing the strategy declined significantly as the 20th century drew to a close. However, there are substantial gaps in our knowledge of conglomeration, especially regarding its apparent decline in popularity amongst the largest UK companies, a contention supported only by anecdotal evidence in the UK as the most recent academic research only covers the period to 1993. This gives rise to the central question addressed by this research: what has happened to

conglomerates, not only those carrying out industrial/manufacturing activities but also those, previously neglected in research, concentrating on services, and the strategy of conglomeration in the UK since 1993?

From this central question flow the questions specifically addressed by this research. First, is there support for the anecdotal contention that the incidence of conglomeration amongst the UK's leading companies has fallen? Second, how have companies moved – forward, backward or not at all - through the Model of Corporate Development and what implications does that have for the Model's continued validity as illustrating the accepted evolutionary path for companies? Third, has there been a general move towards greater focus amongst UK companies and has their breadth of activities narrowed? Fourth, is there a link between dominant personalities and weaknesses in corporate governance and conglomeration or was it coincidence that some of the UK's largest conglomerates broke-up after the retirements of the strong chairmen/CEOs that had created them? Fifth, if conglomeration has declined, what were the drivers, including performance, behind the abandonment of the strategy? Is the financial performance of a conglomerate related to the breadth of its activities and is there support for the *a priori* assumption that conglomerate performance is worse than that of other categories of company? Finally, sixth, do conglomerates have a future, have they a 'raison d'être' in the 21st century and, if so, what might it be?

2.7 Contribution

Through the creation of a new and unique database of financial and non-financial information on FTSE100 companies, this thesis adds to a relatively sparse, as compared to the US, UK literature and breaks new ground by bringing research into UK conglomeration into the 21st century. It goes beyond the most recent UK research which covered the period 1983 to 1993 (Whittington & Mayer, 2000) and adds to a literature that has data going back as far as 1950 (Channon, 1973 & 1978).

Rather than use turnover to determine inclusion in the population to be investigated, this research uses membership of the London Stock Exchange FTSE100 index; the 100 companies with the highest market capitalisations. Acknowledging that some FTSE100 companies, notably banks, do not have turnovers in the accepted sense, given the size of constituent companies there would be few differences with a list of UK companies with the highest turnovers. Using the FTSE100 means that comprehensive information is widely available on all companies and it is possible to gauge investor attitudes towards them. Notwithstanding small differences in populations, the research identifies trends over the 53 year period from 1950 to 2003.

Recognising the importance to the UK economy of the service sector, this research includes both industrial/manufacturing and service companies unlike the overwhelming majority of prior research which, with the exception of Channon (1978), excluded services. Conglomeration amongst services is therefore researched for the first time since the early 1970s since which time

there has been a huge increase in the scale, scope and economic importance of UK service businesses.

The research goes further than its predecessors as, using Herfindahl indices and distributions of turnover across primary activities or groups of related activities, it seeks to identify changes in the breadth of activities in corporate portfolios and, through a range of indicators, relationships between performance and diversification between 1993 and 2003. Furthermore, against a background of significant changes in corporate governance Best Practice including the LSE's Combined Code on Corporate Governance, the research seeks to identify links between corporate governance standards and the pursuit of conglomeration. Similarly, recognising the increased pro-activity of institutional investors, the research considers whether the existence and/or aggregate size of major, typically institutional, shareholdings is different for companies in different diversification categories which may signify levels of support for conglomeration. Finally, by identifying key drivers behind the adoption, retention and abandonment of conglomeration by 22 FTSE100 companies the research considers how the Model of Corporate Development may have changed since conglomeration was added in 1979.

In summarising this research, the future of conglomeration as a valid corporate strategy is discussed. The research speculates that if 'traditional' public company conglomerates are becoming an endangered species, their place may be taken by private equity companies – 'New Conglomerates' - that effectively trade in companies holding none for the long term.

2.8 Thesis Outline

This thesis is organised as follows:

Chapter 3 – Literature Review – critically examines extant literature to provide an understanding of how and why conglomeration grew in the US and the UK following World War II and stagnated and declined in the US in the 1980s. The review identifies gaps in UK research to be filled by this work and summarises its contribution to knowledge of conglomeration.

Chapter 4 – Hypotheses – distils questions raised by the literature review into a series of hypotheses which are grouped under the following broad headings: incidence, breadth of activities, performance and corporate governance (leadership, board composition and shareholder influence).

Chapter 5 – Methodology – details the approach taken to test the hypotheses. It explains the principles followed in creating a unique database of financial and non-financial information on FTSE100 companies and discusses the considerable, but not insurmountable, problems inherent in research into such a disparate collection of industrial/manufacturing and service companies as those that comprise the index. The chapter also discusses the selection of appropriate definitions and data sources for use in creating a consistent and robust database and of categorisation schemes and statistical techniques for its analysis and interrogation given the limitations of UK financial data in terms of availability and level of detail, as compared to the US. The concerns associated with using accounting data gathered over a 10

year period which has seen regulatory change are discussed as is the subjectivity inherent in assessments of the relatedness between company activities when assigning diversification categories.

Chapter 6 – Analysing the Accounting Record – shows quantitative and definitive output from interrogation of the database designed to provide answers to the questions encapsulated in the hypotheses. The chapter includes a number of tables and charts together with statistical analysis and explanatory narrative. Wherever possible/practical, specific companies are used to illustrate points/issues raised by the analyses with company histories included in chapter 7.

Chapter 7 – Analysing the Historical Record – is qualitative and discursive and uses short company histories to illustrate and examine the evolutionary path followed since 1993 by conglomerates and the external drivers behind changes, if any, in their diversification strategies.

Chapter 8 – Conclusions – pulls together key points from the analyses to answer the questions addressed by this research. Changes/trends in conglomeration since 1950 are discussed as are the drivers behind decisions to adopt, maintain or abandon conglomeration. The implications for the Model of Corporate Development are also discussed as is the outlook for conglomerates in the 21st century and the new corporate forms it may take.

3. LITERATURE REVIEW

3.1 Introduction

This chapter will outline, discuss and critically assess relevant published literature to identify gaps in our knowledge of UK conglomeration and also of the drivers behind corporate strategy decisions to adopt, maintain or abandon conglomeration. The discussion will start with the Model of Corporate Development and go on to look at how and why companies adopted conglomerate corporate strategies in the US and the UK over the second half of the 20th century. The review will consider the drivers - environmental, regulatory and management - behind the adoption of conglomerate strategies and how substantial changes in the business world in the late 20th century may have eroded many of those drivers making conglomerates an increasingly rare phenomenon.

The review will undoubtedly have a US bias as there is considerable disparity in the volume of research work undertaken and published in the US, where the topic has received significant attention, and the UK and Europe where it remains relatively under-researched although there are several key papers/books that allow trends through the second half of the 20th century to be identified. Research into conglomerates in Asia is also comparatively rare although that may be due to difficulties rooted in economic underdevelopment and the private status of most companies in that region.

The primary UK research is that of Channon (1973) covering the largest UK manufacturing/industrial companies, by turnover, through the period 1950 to

1970 and Whittington & Mayer (2000) covering a similar group of companies through the 10 years from 1983 to 1993. Together their research covers the period 1950 to 1993. This research takes up the story in 1993 and moves it forward to 2003 with the aim of bringing our understanding of the conglomerate 'phenomenon' into the 21st century.

Finally, this review will highlight the concentration, with a few notable exceptions (Channon, 1978), of extant research on manufacturing /industrial companies; service companies have effectively been ignored and little is known about their diversification strategies. In his US research into diversification and the sources of potential benefits to companies offering 'search' and/or 'experience' services, Nayyar (1993, p569) recognised the importance of the service sector which in the early 1990s, he noted, *"accounted for 75 percent of employment, 65 percent of gross national product, and nearly 90 percent of new jobs"* in the US. Similarly, over the last quarter of the 20th century services have grown to account for significantly more than 50% of UK economic activity as determined by Gross Domestic Product (GDP). The size and economic contribution of the service sector is reflected in the composition of the FTSE100 index; service companies account for over 50%, both in number and value, of the index. To restrict the research to only manufacturing companies would be to effectively ignore over half of UK economic activity. This neglect of service companies represents a significant gap in our knowledge which this research aims to fill.

3.2 Model of Corporate Development

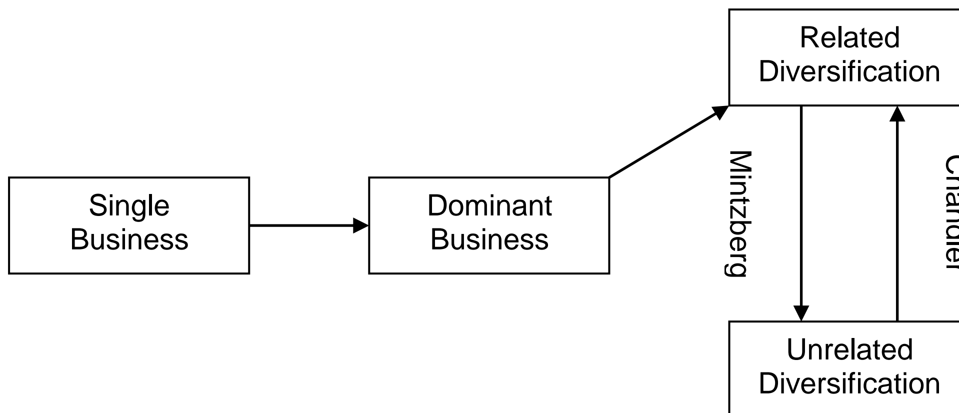
The Model of Corporate Development provides a clear framework into which companies may be placed according to their degree of diversification. The Model establishes a simple evolutionary path for companies based on changes in their degree of diversification with, at one extreme, simple single business companies and at the other, complex unrelated diversified businesses (conglomerates) with dominant business and related diversified companies representing intermediate steps. The Model is consistent with the taxonomy of diversification originally designed by Leonard Wrigley in his 1970 Harvard doctoral thesis (Divisional Autonomy and Diversification) and further developed/extended by Richard Rumelt (1974) and used in the overwhelming majority of research work into corporate diversification.

The original Model developed by Scott (1973) comprised only three stages and showed single business companies growing into dominant business companies as new, initially peripheral and usually related, activities are added with further development into an unrelated diversified company as those, and possibly further new, activities account for an increasing proportion of total activity. The original Model did not distinguish between related and unrelated (conglomerate) diversification and also showed movements in only one direction suggesting reversals were rare.

Mintzberg (1979) added a further stage to the original model - unrelated diversification (conglomeration) - believing that related diversifiers would

continue to seek profitable growth opportunities wherever they may arise and would, as a consequence, move into new unrelated activities.

Chart 1: Model of Corporate Development



Source: Whittington & Mayer (2000, p127)

While a logical extension, Mintzberg's (1979) fourth stage has not been universally accepted. Supporters cite Channon's (1973, p238) belief that diversification was effectively irreversible while opponents, including Hall & St. John (1993), reference Chandler (1962) who believed conglomeration to be unsustainable with a retreat back to related diversification almost inevitable.

Further, more recent support for Mintzberg has come from Kay (1995a) who believes conglomerates are the ultimate company form and rightly considered as the fourth and final stage in the Model. However, research has shown the dynamism of the conglomerate category with companies entering and leaving suggesting that retreat does happen. This research suggests that the Model be revised to reflect that dynamism and two-way flow.

The prevailing opinion in the 1960s and 1970s was in favour of this evolutionary path towards related diversification and is summed up by comments attributed by Grant & Thomas (1988, p68) to Caves (1980) who said of relevant 1970s Harvard Business School research that there was *"a consistent trend in corporate development in the USA and Western Europe that pointed towards the diversified divisionalised corporation as the highest evolutionary form of business enterprise"*.

While there is general acceptance that the Model reflects the path to be followed by a majority of growing companies, it is acknowledged that there are exceptions where companies either miss stages, e.g. achieving conglomerate status without having become a related diversifier, or deliberately choose not to progress beyond a particular stage, e.g. staying as related diversifier. Therefore, it is important to note that progression through all stages is not automatic or necessary. Furthermore, the Model also operates in reverse where companies, through sale, divestment or demerger, retreat towards greater focus in their activities.

In the UK, research by both Channon (1973) and Whittington & Mayer (2000) considered the stability of companies within each diversification category and also movements within categories. Channon (1973) showed relatively few companies abandoning conglomeration to return to the related diversification, dominant business or single business categories in the period up to 1970. Similarly, Whittington & Mayer (2000) showed that in the latest period covered by their research (1983 to 1993), the proportion of conglomerates amongst

the largest industrial/manufacturing companies increased steadily from 11% to 24% and very few conglomerates abandoned their strategy.

Despite finding growth in conglomeration and stability amongst conglomerates, Whittington & Mayer (2000, p58) expressed their support for those believing conglomerates were unsustainable claiming that *"….essentially the conglomerate is a freak of nature, too unprofitable to survive"*. Whittington & Mayer (2000, p127/8) summarised their views on the longevity of conglomerate strategies by endorsing Dosi et al (1992) saying that *"The orthodox resource-based view is hard on conglomerates, stigmatising them as 'hopeful monsters'. Our own view is more appreciative of the short run economic advantages available for corporate relationships, but sceptical about the longevity of the top management resources capable of exploiting them. In both these views, however, we should expect a reverse flow out of the conglomerate category, towards either greater focus or greater relatedness. Otherwise, conglomerates are likely to fail altogether"*. Whittington & Mayer did refer (p128) to comments by Kay (1995a) claiming *"robustness for the conglomerate"* and suggesting that its key advantage of reducing risk through diversification created stability and a tendency towards 'lock-in' for the conglomerate corporate strategy but still felt the strategy to be unsustainable. This suggests that investors, while welcoming the potential for earnings stability offered by conglomerates, still expect them to provide an acceptable level of return and will not support them if those stable earnings are at too low a level.

If Whittington & Mayer’s (2000) pessimistic view of the future for conglomerates is correct, the growth in conglomeration in large UK industrial/manufacturing companies experienced through to 1993 should have been followed by a period of stagnation before a fall through the final years of the 20th century and the beginning of the new millennium. However, Whittington & Mayer (2000) make no predictions as to the likely speed of any change in the incidence of conglomeration which is likely to be affected by environmental, regulatory and managerial factors. This research will show how companies have moved through the Model of Corporate Development since 1993.

3.3 History of Conglomeration

3.3.1 Overview

The growth in conglomeration may be traced back to the 1960s. Before then, companies retained focus limiting expansion – organic and/or acquisitive – to activities in the same or similar industry segments. Some became related diversifiers but very few added unrelated activities to become conglomerates. These horizontal (acquisition of businesses in the same industry) or vertical (acquisition of supplier or consumer businesses) acquisitions, frequently justified in terms of economies of scale/scope, created several large well-known groups including Ford and General Motors: the core activity of both companies remained the design and manufacture of motor vehicles although both added 'related' activities including automotive component manufacture. A prime UK example is the chemical company ICI (formerly Imperial Chemical Industries) which became a related diversifier on its creation in 1927 by the

merger of several UK chemical companies each focused on different chemical products.

The 1960s saw conglomeration gain acceptance as a valid corporate strategy. Smith & Schreiner (1969, p413) summed up the favourable opinion-of-the-day of conglomerates commenting that *"…one of the more remarkable developments within finance during the current [1960s] decade has been the rapid emergence of the conglomerate type of firm. Viewed internally, the conglomerate phenomenon has proven of great interest to academicians studying economies of scale for both human and non-human resources, while from an external focus, conglomerates represent a new type of investment opportunity"*.

The preferred route to conglomeration was by acquisition. Mueller (1969) quotes US data published in 1967 by the Antitrust Sub-committee of the Committee on the Judiciary (*Celler-Kefauver Act: Sixteen Years of Enforcement*) showing a clear trend toward conglomeration. The report showed the percentage of large company (assets over $10m) acquisitions categorised as conglomerate increased from 51% to 71% between 1950 and 1966 while horizontal mergers fell from 40% to 14% in the same period. Gaughan (1999, p30) notes that the third 20th century US merger wave - between 1965 and 1969 - is often called the conglomerate merger period: *"the FTC reported that 80% of the mergers that took place in the 10-year period between 1965 and 1975 were conglomerate mergers"* (Statistical Report on Mergers and Acquisitions, Federal Trade Commission, Washington D.C.,

1977). Gaughan (1999) uses ITT as an example of a US company that aggressively pursued a conglomerate strategy in the 1960's acquiring *"Avis Rent-a-Car, Sheraton Hotels, Continental Baking and other far-flung enterprises such as restaurant chains, consumer credit agencies, home building companies and airport parking firms"*. By 1969, in the US the single business companies that predominated had become a minority with related and unrelated (conglomerate) diversified companies increasingly pre-eminent; 19% of Fortune 500 industrial/manufacturing companies were conglomerates (Rumelt, 1974).

In the 1980s the tide turned and US companies began to refocus retreating from conglomeration back towards related diversified, dominant and single business strategies. Lee & Cooperman (1989, p45) summarise the conglomerate 'bubble' in the US as comprising 3 stages, "*1. The conglomerate wave, 1955-1968, when new conglomerates, fed by the expansion of the 1960s, naively yet feverishly acquired firms in unrelated fields, 2. A period of re-evaluation, 1969-1976, during which conglomerates began to lose profitability as a result of the recession in the mid-1970s, and 3. a third merger wave, 1977-1980s, seeing the emergence of professional managers, the entry of more conservative firms, and a corporate repositioning/restructuring of many mature conglomerates"*. The US conglomerates of the 1980s were significantly different from their 1970s predecessors. According to Lee & Cooperman (1989, p51) the 1980s conglomerate had lower gearing, was less diverse and operated in fewer industries than in the 1970s. ITT, the company singled out by Gaughan as

early adopter of conglomeration, was one of the first to reverse its strategy achieving focus by splitting itself into several independent businesses.

The UK saw similar growth in conglomerate strategies, albeit around 10 years later than in the US. By 1970 6% of manufacturing/industrial companies were conglomerates compared to only 2% in 1950 (Channon, 1973). Research by Utton (2001) showed that while the UK had seen increased levels of acquisitions activity between 1945 and 1965, it had been predominantly horizontal increasing concentration across manufacturing industry rather than creating conglomerates. The UK also lagged behind some of the major European economies in its adoption of conglomeration; in 1950 only 2% of UK's leading non-financial companies were conglomerates compared to 4% in France and 7% in Germany and in 1970 the UK's 6% compared to 10% in France and 18% in Germany (Dyas & Thanheiser, 1976). Only in Italy were the 1950 and 1970 levels of conglomeration similar to that amongst UK companies.

The most recent research (Whittington & Mayer, 2000) suggests further growth in conglomeration through to the early 1990s which contrasts to the decline seen in the US. In 1983, 11% of the UK's largest manufacturing companies, by turnover, were conglomerates (Whittington & Mayer, 2000) but by 1993 that figure had risen to 24%. Notwithstanding differences in definitions of a conglomerate, according to Whittington & Mayer (2000) growth in the UK exceeded that in Germany which increased from 25% to 32% and France which increased from 12% to 14%. In 1993, the refocusing strategies

prevailing in the US in the 1980s had yet to be adopted by UK conglomerates. However, anecdotally, refocusing in the UK has occurred in the mid to late 1990s following a critical reappraisal of conglomeration with many seeking focus through divestment and floatation of peripheral activities. Research has yet to prove this to be the case.

3.3.2 Growth

3.3.2.1 Converts to Conglomeration

The post World War II period saw unprecedented growth in conglomeration in the US where between 1949 and 1969 the percentage of conglomerates amongst the largest industrial/manufacturing companies increased from 3% to 19%. In contrast, only 6% of the same group of UK companies were conglomerates in 1970, up from 2% in 1950 (Channon, 1973). However, the percentages of companies categorised as being diversified - related and conglomerate – remained similar rising from 25% to 60% in the UK and from 30% to 64% in the US between 1949/50 and 1969/70. This suggests that, while UK and US companies had embraced diversification at a similar rate, fewer UK companies were willing to take the final step to conglomeration.

The following table draws on the work of several leading researchers to present a comparison of the strategies adopted by non-financial companies in the US and the major European economies of the UK, France, Germany and Italy in 1949/50 and 1969/70.

Table 3: Comparisons of Changes in Strategies of Leading Non-financial Companies in US and Europe, 1949/50-1969/70

Country	Year	No. of Comps[a]	% by Category[c]				Total % Divers[d]
			Single	Dominant	Related	Unrelated	
US	1949	500[b]	35	35	27	3	30
	1969	500[b]	6	29	45	19	64
UK	1950	92	34	41	23	2	25
	1970	100	6	34	54	6	60
France	1950	100	42	21	33	4	37
	1970	100	16	32	42	10	52
Germany	1950-55	99	35	26	32	7	39
	1970	100	22	22	38	18	56
Italy	1950	84	30	24	43	3	46
	1970	100	10	33	52	5	57

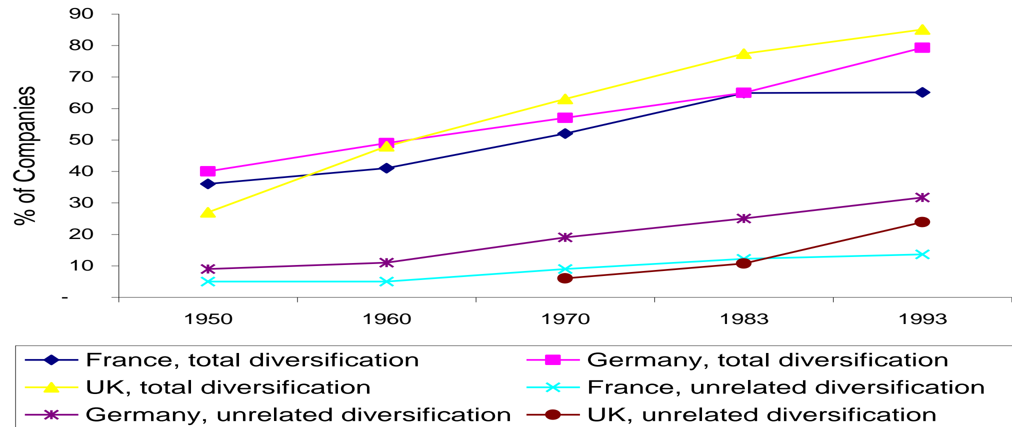
Notes:
[a] Whilst the above table shows similar percentages of diversified - related and unrelated - companies in each category, the numbers of companies surveyed varies significantly from country to country. The US analysis is based on samples drawn from the largest 500 companies while the European data is drawn from a maximum of 100 of the largest companies. It is likely that beyond the limited European sample companies, the incidence of diversification would be significantly lower than that amongst the largest 100 as represented in the table.
[b] Rumelt's procedure is based on a sample taken from the largest 500 companies for each year (1974, Appendix A).
[c] Country percentages may not total 100% due to rounding.
[d] Total diversification is the total of the related and unrelated columns.

Sources: US - Rumelt (1974, p51, Table 2.2); UK - Channon (1973, p67, Table 3-2); France – Dyas & Thanheiser (1976, p186, Table 12.1 and p191, Table 12.4); Germany – Dyas & Thanheiser (1976, p72, Table 6.4); Italy – Pavan (1976, p257, Table 4).

The table appears to show that with increases from 7% to 18% in Germany and from 4% to 10% in France, those countries led in the adoption of conglomeration in Europe between 1950 and 1970. German adoption rates were not far behind those of the US. As similar category definitions have been used by researchers in each country, pan-European and European-US comparisons are valid. However, the lower number of companies included in the European studies may raise questions regarding comparability with US research depending on the equivalence between the largest 500 US and 100

European companies. Overall, in Europe the post-war trend was away from focus and towards diversification as the following chart shows.

Chart 2: Diversification in Post-War France, Germany and the UK



Sources: Whittington & Mayer (2000, p144). Original sources - UK 1950-70, Channon (1973); France 1950-70 & Germany 1950-70, Dyas & Thanheiser (1976); All 1983-1993, Whittington & Mayer (2000).

The growth in US conglomeration continued through the 1970s. Research by Allen (1984) cited and tabulated by Scherer & Ross (1990, p157) shows clearly the continued and steady increase in conglomerate acquisitions, as compared to horizontal, vertical, product extension or market extension acquisitions, after 1970. The following table shows that between 1972 and 1979, conglomerate acquisitions accounted for 45.5%, its highest post-war level, of the total assets of manufacturing and minerals companies acquired with conglomerate transactions being defined as those where there were no complementarities between the activities of the acquiring or acquired companies. In the immediate post-war period, 1948-55, conglomerates accounted for only 10.1% of acquisition asset values compared to horizontal 39.0% and product extension 36.1% but by 1972-79 horizontal and product extension acquisitions had fallen to only 14.9% and 28.2% respectively.

Table 4: Distribution of Large Manufacturing and Minerals Company Assets Acquired, by Type of Merger, in the US, 1948-1979

Type of Merger	Percentage of Total Assets Acquired			
	1948-55	1956-63	1964-71	1972-79
Horizontal	39.0	18.7	12.0	14.9
Vertical	12.7	20.0	6.6	8.3
Product Extension	36.1	36.9	38.9	28.2
Market Extension	2.1	6.7	7.7	3.0
Pure Conglomerate	10.1	17.7	34.8	45.5

Source: Scherer & Ross (1990, p157)

While conglomeration stalled in the US in the 1980s, research suggests it continued to grow in the UK through to 1993. This time lag between the US and UK peaks in conglomeration may be due to differences in the business environment, notably competition legislation and its effective implementation and/or management and investor/market attitudes.

As the following table shows, by 1970, according to Channon (1973), 63% of the UK's largest industrial/manufacturing companies had been diversified but, according to Whittington & Mayer (2000) who used the same categorisation methodology as Channon (1973), by 1983 that had risen to 77% and by 1993 to 85%. The increase in the percentage of conglomerates was even more pronounced rising from only 6% in 1970 to 11% in 1983 and 24% by 1993. By 1993, the single business and dominant business categories had fallen to their lowest levels, 5% and 10% respectively. In 1993 at 61% the related diversified category was also above its 1950 level of 57% but below its 1983 peak of 67% suggesting more companies had moved through that category and become conglomerates rather than remain as related diversifiers. This is consistent with the increase in conglomeration.

Table 5: Diversification Trends for Domestic Top 100 Industrial Firms in the United Kingdom (Classification according to Channon)[a]

Category	1950[b]	1960[b]	1970	1983	1993
Single	24	18	6	6.7	4.5
Dominant	50	36	32	16.7	10.4
Related Diversified	27	48	57	66.7	61.2
Unrelated Diversified	-	-	6	10.7	23.9

Note:
[a] The figures for 1950, 1960 and 1970 in the above table differ slightly from those in similar tables in Channon's (1973) work. The differences are not material and do not alter trends.
[b] Related Diversified figures include Unrelated Diversified for 1950 and 1960.

Source: Whittington & Mayer (2000, p139)

The US and UK research noted above shows that conglomeration amongst UK companies did not reach the levels seen in the US in 1969 - 19% - until the early 1990s. The late adoption of conglomeration in the UK may be explained by a number of environmental, regulatory and management factors that were markedly different to those influencing the US. Caves (1980) suggested a number of reasons for the delayed adoption of diversification in Europe:

- Restriction of horizontal mergers (Channon, 1973, p90),
- Corporate 'freedom' limited by regulation and bureaucracy,
- Massive demands of post-war reconstruction which was most needed in Europe,
- Maintenance of old corporate structures; adoption of multi-divisional structures was not widespread amongst UK companies until the 1970s,
- Continuing family ownership structures.

UK Conglomeration, 1950-70 (Channon, 1973 & 1978)

Channon's (1973) initial research covered 1950 to 1970 and the UK's largest manufacturing companies, both public and private, as measured by turnover and identified using *The Times 500* list for 1969-70. Notwithstanding the difficulties inherent in categorising service companies, given the relatively small size of the service sector, excluding nationalised utilities, in the mid 20th century the concentration of research into the industrial/manufacturing sector was not surprising.

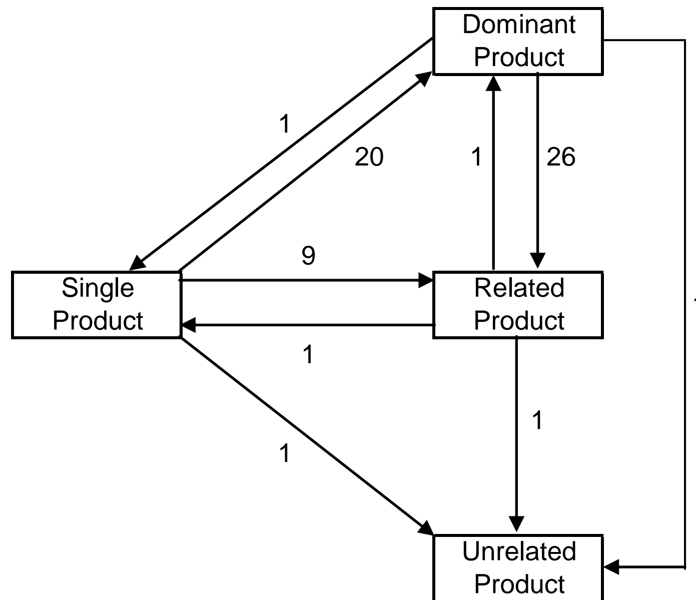
Table 6: Classifications of UK Manufacturing Companies by Strategy in 1950, 1960 & 1970

Category	1950		1960		1970	
	No.	%	No.	%	No.	%
Single Product	31	34	18	19	6	6
Dominant Product	38	41	35	36	34	34
Related Product	21	23	39	41	54	54
Unrelated Product	2	2	4	4	6	6
Totals	92	100	96	100	100	100

Source: Channon (1973, p67) 100 largest UK manufacturing companies as in 1969-70.

In addition to analysing the distribution of company strategies in 1970, Channon (1973) also analysed the same companies' strategies 10 and 20 years earlier, i.e. in 1950 and 1960. Using the Model of Corporate Development Channon tracked movements between categories over the period 1950 to 1970 as the chart on the following page shows:

Chart 3 - Number and Direction of UK Corporate Strategy Changes, 1950-70



Source: Channon (1973, p78)

The chart shows, only 3 companies took the final step to conglomeration. Although 20 companies had moved from the single to dominant business categories and 26 from the dominant business to related diversified categories only 1 company had taken the final step and become a conglomerate. A second company had made the ‘double jump’ moving from the dominant business to conglomerate category and another company had made the ‘triple jump’ from single business company to conglomerate. As only 2 companies had made double or triple jumps it appears that between 1950 and 1970 progress through the Model was evolutionary rather than revolutionary. Channon (1973) did note movements against the 'normal' flow, i.e. back toward greater focus, between 1950 and 1970, but they were very few, only 3, in number.

The chart shows the overwhelming number of movements between categories to be consistent with the logical strategic development of companies as per the Model of Corporate Development: initial growth in a single business, expansion into one or more minor, usually related, businesses with the core activity remaining dominant followed by development into an unrelated business as the non-dominant business activity becomes larger. While Channon does not list the companies categorised as conglomerates in 1950 and 1960, he does those in 1970; Rank Organisation, Reckitt & Colman, Sears Holdings, Slater Walker Securities, Standard Telephones & Cables and Thomas Tilling.

A review of the subsequent development of Channon's 6 1970 conglomerates raises questions over the strategy's durability. Slater Walker Securities, Thomas Tilling, Sears Holdings and Standard Telephones & Cables have all lost their independence. Slater Walker, an industrial conglomerate in 1970, became an investment bank and was rescued in 1975 from near collapse during the UK's secondary banking crises receiving a government loan of £70m. The company changed its name to Britannia Arrow then to Invesco and, following a merger with AIM, to Amvescap, under which name it re-entered the FTSE100 remaining a constituent until transferring its listing to the US in 2007. Thomas Tilling was acquired by BTR in 1984 and Sears Holdings, the retail group built up by Sir Charles Clore, was acquired for £549m in 1999 by JIL Ltd, an investment vehicle owned by retail entrepreneur Philip Green and financially supported by the reclusive Barclay brothers. Sears was subsequently profitably split up the major disposals being the sale of the

Freemans mail order business to Otto Versand of Germany, the sale of high street fashion retailers Wallis, Warehouse, Miss Selfridge, Richards and Outfit to Arcadia (owned by Sir Philip Green's family) and the sale of the childrenswear retailer Adams to its management. Standard Telephones & Cables was acquired in 1991 by Nortel Corporation a wholly owned subsidiary of Canada's Northern Telecom. Of the 2 surviving companies, Rank remains a conglomerate albeit one that has reduced in both size and scope and fallen out of the FTSE100 and Reckitt & Colman, which acquired A. Benckiser of the Netherlands in 1999 to become Reckitt Benckiser, is a dominant business company and an FTSE100 constituent.

Channon (1978) also researched diversification amongst the largest UK service companies as measured by turnover and identified using *The Times 1000* list for 1973-74, and found that conglomeration had increased at a much faster rate than amongst industrial/manufacturing companies although the incidence of related diversification was lower. In 1950 only 6% of service companies were conglomerates and by 1974 that had risen to 19% while the percentage of related diversifiers had increased from 17% to 49%. The incidence of both single business and dominant business companies fell over the same period from 36% to 16% and from 41% to 16% respectively.

UK Conglomeration, 1970-93 (Whittington & Mayer, 2000)

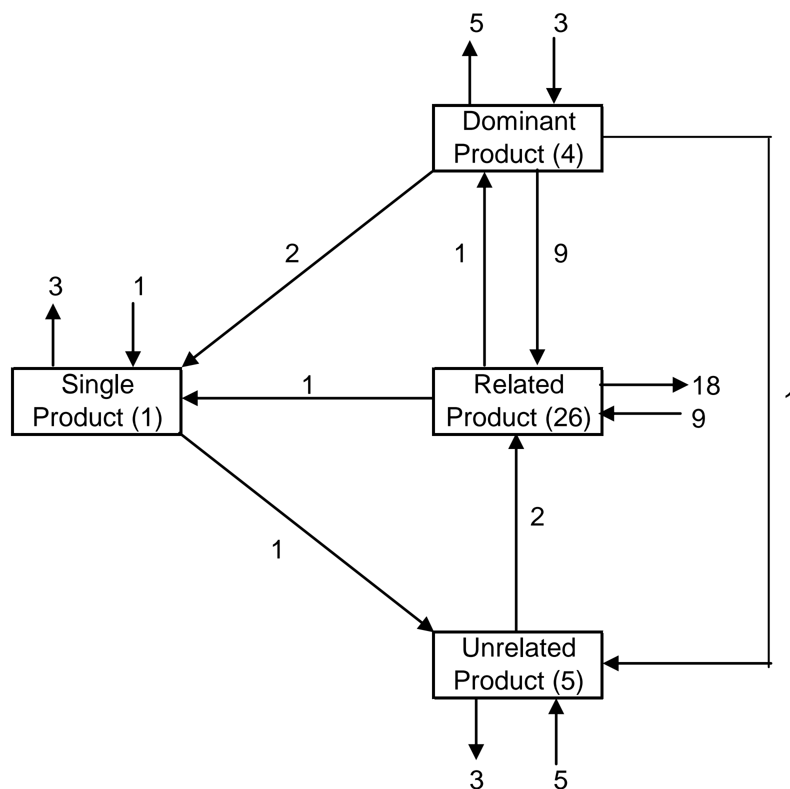
Channon's (1973) research into industrial/manufacturing companies was effectively brought up to date by Whittington & Mayer (2000) who covered the period from 1983 to 1993 and used the *Times 1000* lists to identify the largest

UK based manufacturing companies in those years. To maintain longitudinal consistency and comparability and identify trends back to 1950, they retained Channon's (1973) categorisation scheme, which in turn was based on Rumelt (1974), although, to reduce subjectivity in assessing/categorising companies, where Channon had worked alone they used 2 independent researchers and called on an expert in the field to arbitrate where there was disagreement. The expert was only needed to arbitrate in 7% of cases, the 93% level of agreement suggesting categorisation to be fairly straightforward and unambiguous. Again following Channon (1973), Whittington & Mayer (2000) used the Model of Corporate Development to track movements between categories over 2 time periods, 1970-1983 and 1983-1993. However, unlike Channon (1973) who retained the same population of companies and tracked them through from 1950 to 1970, Whittington & Mayer (2000) allowed for changes in the population, i.e. entries and exits from the population of the largest, by turnover, UK industrial/manufacturing companies.

Whittington & Mayer (2000) found the 1970s and early 1980s to have been a period of stability for related diversifiers with 26 companies, 52% of the 50 companies in the category in 1970, remaining in that category between 1970 and 1983. Given the dire economic performance of the UK through this period, which included a prolonged and deep recession, low corporate growth would have contributed to that stability. Despite this stability, the category also saw the most entries and exits (a net 9 external exits balanced by a net 9 internal entries) with the largest internal movement, 9 companies, coming from the dominant business category. However, as was the case between

1950 and 1970, related diversifiers were markedly reluctant to take the final step to conglomeration with none of them doing so between 1970 and 1983. The net increase of 2 in the conglomerate category was due to entries and exits from the population rather than changes of strategy by companies within the population in 1970; the net internal movement was 0.

Chart 4 - Number and Direction of UK Corporate Strategy Changes, 1970-83



Note: Figures in parentheses are the number of companies remaining in the category in 1970 and 1983.

Source: Whittington & Mayer (2000, p140)

The following table summarises the movements noted in the above chart; internal changes are those between categories and external changes are entries and exits from the population of the largest, by turnover, UK manufacturing companies.

Table 7: Strategy Changes of Largest UK Industrial Companies 1970-83

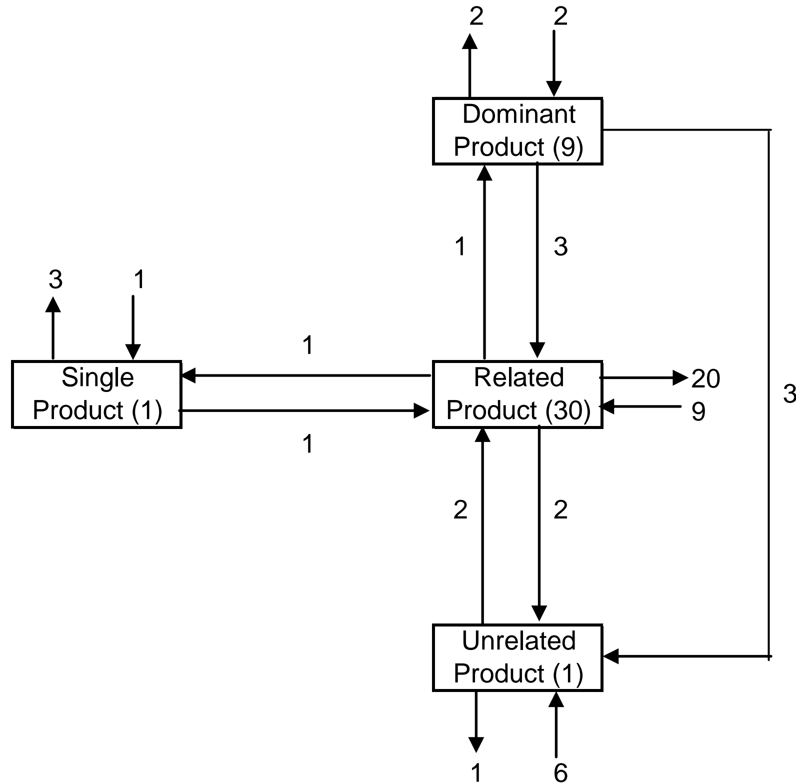
Categories	Strategies (Channon Basis)						Analysis of Chg		
	1970		1983		Change		External		Int.
	No.	%	No.	%	No.	%	In	Out	Net
Single	5	6	5	6	0	0	1	(3)	2
Dominant	25	29	12	16	(13)	(13)	3	(5)	(11)
Related	50	58	50	67	0	9	9	(18)	9
Unrelated	6	7	8	11	2	4	5	(3)	0
Totals	86	100	75	100	(11)	0	18	(29)	0

Source: Extracted from Whittington & Mayer (2000)

As with the earlier research by Channon (1973), the internal movements are almost all evolutionary, i.e. one category only. However, one company – BAT Industries – was found to have made the 'triple jump' to conglomeration from the single business category. BAT Industries' move reflected its acquisition of paper manufacturers Wiggins-Teape and Appleton and the retailer Argos in an attempt to become less reliant on the declining tobacco industry. Furthermore, British Insulated Callenders Cables (BICC) made the 'double jump' from dominant business company to conglomerate as it diversified away from engineering expanding its construction activities with the acquisition of Balfour Beatty. The net forward movement through the Model was 5 (11 advanced to greater diversification and 6 retreated to greater focus).

As with the periods 1950 to 1970 analysed by Channon (1973) and 1970 to 1983 analysed by Whittington & Mayer (2000) the changes between 1983 and 1993 shown in the following chart are again predominantly evolutionary with only 3 companies – Blue Circle Industries, Metal Box/Caradon and Trafalgar House making the 'double jump' from dominant product company to conglomeration.

Chart 5 - Number and Direction of UK Corporate Strategy Changes, 1983-93



Note: Figures in parentheses are the number of companies remaining in the category in 1983 and 1993.

Source: Whittington & Mayer (2000, p141)

Table 8: Strategy Changes of Largest UK Industrial Companies, 1983-93

Categories	Strategies (Channon Basis)						Analysis of Chg		
	1983		1993		Change		External		Int.
	No.	%	No.	%	No.	%	In	Out	Net
Single	5	6	3	5	(2)	(1)	1	(3)	0
Dominant	12	16	7	10	(5)	(6)	2	(2)	(5)
Related	50	67	41	61	(9)	(6)	9	(20)	2
Unrelated	8	11	16	24	8	13	6	(1)	3
Totals	75	100	67	100	(8)	0	18	(26)	0

Source: Extracted from Whittington & Mayer (2000)

As with 1970-1983, the change in the number of conglomerates between 1983 and 1993 was more to do with the effects of entries to and exits from the population – a net gain of 5 – than changes in strategy amongst the

companies that were in the population in 1983, a net gain of 3. Overall, the net movement was again towards greater diversification with 9 companies advancing and 4 retreating through the Model. This finding suggests that, at least amongst the largest industrial/manufacturing companies, few companies were trying to refocus.

To eliminate the effects of entries and exits from the population, Whittington & Mayer (2000) looked at the strategies of those companies that had survived between from 1970 to 1993 and found that very few remained in the same category as the following table shows:

Table 9: Strategic Stability of Domestic Top 100 Survivors, 1970-93[a]

	Period	Single	Dominant	Related	Unrelated
Numbers in 1970		5	26	50	6
% same category	1970-83	20.0	34.6	60.0	16.7
	1983-93	20.0	33.3	52.0	62.5
	1970-93	0.0	15.4	30.0	0.0

Note
[a] Survival is holding the same strategy, while remaining in the top 100 populations, at the beginning and end-points in the shorter periods, and beginning, mid- and end-points over the whole 23 years.

Source: Whittington & Mayer (2000, p147).

Of the 4 categories, related appears to be the most stable; of the 50 companies in the category in 1970, 60% remained in the category in 1983 and 30% in 1993. The single business and unrelated (conglomerate) categories were the least stable; only 16.7% of the 6 companies identified as conglomerates in 1970 were still conglomerates in 1983 and none remained in the category by 1993 and the comparative figures for the 5 single business companies were 20% and none. However, conglomerate survival did improve between 1983 and 1993 with 62.5% of 1983 conglomerates still in the

category in 1993 while there was no change in single business survival rates which remained at 20%. Dominant business company survival rates fell midway between those of single business companies and conglomerates and related diversifiers with 34.6% of the 26 companies in the category in 1970 surviving to 1983 and 15.4% to 1993 with a similar survival rate for the period from 1983 to 1993.

The continuing popularity of conglomerates through to 1993 may be illustrated by looking at some of their key statistics.

Table 10: Turnovers, Profits Before Interest and Tax, Returns on Sales and Market Capitalisations of Whittington & Mayer Unrelated Diversified Companies As At 1983 and 1993

All Figs £m except Ros % Company	1983				1993			
	Turn-over	PBIT	ROS	Mkt Cap	Turn-Over	PBIT	ROS	Mkt Cap
AMEC	524	20	3.8	113	2,338	0	0	352
BAT Industries	9,091	808	8.9	1,545	13,817	1,354	9.8	9,275
BBA Group					1,252	75	6.0	425
BICC	1,491	124	8.3	580				
Blue Circle					1,114	185	16.6	1,355
BTR	638	113	17.7	755	6,742	1,107	16.4	7,762
Charter					450	89	19.8	512
Hanson	856	83	9.7	372	7,691	2,060	26.8	10,889
Harrison & Crosfield					1,825	92	5.0	839
Metal Box / Caradon					679	130	19.1	1,406
Pearson	702	83	11.8	278	1,600	233	14.6	1,900
Rank Organisation	618	135	21.8	287				
Redland	390	55	14.1	351				
Siebe					1,481	220	14.9	871
TI Group					900	120	13.3	837
Tomkins					1,039	131	12.6	1,101
Trafalgar House					3,202	170	5.3	1,592
Unigate					1,894	109	5.8	698
Williams Holdings					1,002	183	18.3	1,687
Totals	14,310	1,421	9.9	4,281	47,026	6,258	13.3	41,501
Average	1,789	178	9.9	535	2,939	391	13.3	2,594
Survivors (5)								
Totals	11,811	1,107	9.4	3,063	32,188	4,754	14.8	30,178
Average	2,362	221	9.4	613	6,438	951	14.8	6,036
Survivors Ave v Total	+32%	+24%	(0.5)	15%	+119	+143	+1.5	+133%

Sources: Companies - Whittington & Mayer (2000), Financial Data - Times 1000 Reports (1983 & 1992-93).

The above table has been constructed to compare the size and profitability of the largest industrial/manufacturing companies categorised as conglomerates by Whittington & Mayer (2000) in 1983 and 1993. In 1983 there were 8 conglomerates (11%) in the UK's largest, by turnover, 75 manufacturing companies, the average conglomerate having turnover of £1,789m, Profit Before Interest and Tax (PBIT) of £178m, Return on Sales (ROS) of 9.9% and a market capitalisation of £535m. By 1993 the number of conglomerates in the largest, by turnover, 67 manufacturing companies had doubled to 16 (24%) and their average size was substantially greater with turnover of £2,939m (+64%), PBIT of £391m (+120%), RoS 13.3% (+3.4%) and market capitalisation £2,594m (+385%). However, 3 of the companies identified as conglomerates in 1983 were no longer in that category in 1993; BICC and Redland had retreated back to be related diversifiers while Rank Organisation was no longer large enough to be included in the Whittington & Mayer study.

As for the 5 conglomerates common to both years – AMEC, BAT Industries, BTR, Hanson and Pearson – they were, on average, larger in turnover, PBIT and market capitalisation terms than those that did not survive. The changes between 1983 and 1993 in the average financial characteristics of survivors are even more impressive with turnover increasing 173% to £6,438m, PBIT growing 330% to £951m, RoS improving 5.4% to 14.8% and market capitalisation rising 885% to £6,036m. However, several of the 1993 conglomerates have since experienced difficulties or have changed strategy and would not, either for size or strategic category reasons, be included in a list of the largest conglomerates in 2003. Therefore, anecdotally, it may be

that 1993 was a high water mark for the UK conglomerate and that a retreat to less complex and diverse strategies, as advocated by Peters & Waterman (1982) and seen in the US in the 1980s, began in the mid-1990s. This is one of the key questions addressed by this research.

3.3.2.2 Drivers

Except for recessions (defined as 2 or more quarters of negative economic growth) in the late 1970s/early 1980s and the early 1990s, the post-World War II period saw steady economic growth in the US and the major economies of Western Europe. However, economic growth and use of the financial resources that prosperity and profitability generates does not explain increases in either diversification or conglomeration. There were several factors that together created the conditions in which conglomeration was favoured and encouraged. The key drivers behind the adoption of conglomerate strategies in the 1960s, 1970s, 1980s and early 1990s illustrate the many factors that influence strategic decisions.

Attitudes to Risk and Earnings Stability

Investors, especially institutional/professional, are generally risk-adverse preferring companies that, by offering stability, are low risk. Companies try to lower their overall level of risk by *"hedging against shifts in demand"* Scherer (1980, p70) which involves creating earnings stability by building a portfolio of, ideally, countercyclical businesses, i.e. when one business is performing poorly another performs well and vice versa. Diversification and 'risk and return' are therefore closely linked.

The principles behind the creation of lower risk investment portfolios by companies through efficient diversification were first propounded by Markowitz (1952). Theoretically, by constructing a portfolio containing investments with perfectly negative correlation coefficients, cyclicality will be minimised and stability maximised. Greater earnings stability may result in lower borrowing costs as investors view the company as offering a stable and safer investment opportunity. The availability of low cost finance may provide additional funds for expansion, possibly further increasing diversification, and provide a cost advantage over competitors. Companies with diversified portfolios may also 'cross subsidise' activities with strong businesses helping investment in new potentially high growth activities or providing support to underperforming businesses, e.g. those facing difficult trading environments, reducing the need for more expensive external financing. While achieving stability through portfolio management is a theoretically sound aim, the existence, complexity and inter-connectivity of business cycles makes it impossible in practice to identify and establish a portfolio of countercyclical businesses.

There is mixed evidence as to whether conglomerates achieve greater stability in their financial performance. Amit & Livnat (1988) considered the effects of business cycles on conglomerates finding that they had lower exposure which translated into greater performance stability than was the case in more focused companies. Lewellen (1971) also found that the greater stability of conglomerate earnings meant that they were perceived a lower risk by providers of finance allowing them to borrow higher sums and at low interest rates relative to more focused companies. However, investing in

conglomerates may not be the only way for investors to reduce their risk. Smith & Weston (1977) produced research that not only found conglomerate risk-adjusted performance was no better than other categories of company but also pointed out that they provided less diversification for investors than mutual funds and similar investment vehicles.

Leveraging Management

Some business leaders believe management skills are generic and transferable. Lord Hanson at Hanson and Sir Owen Green at BTR were strong advocates of the transferability of core management skills and competencies. They believed their teams possessed the skills necessary to successfully turnaround and manage the vast range of businesses their companies acquired in industries as diverse as, at BTR in the late 1980s, ladies hosiery and heavy engineering and, at Hanson, tobacco and building products. Hanson, by describing itself as an 'industrial holding company' in its 1993 annual report and accounts suggested there was no common thread linking its activities other than ownership and management.

The acquisition-led success of Hanson and BTR suggests that replacing management teams of acquired companies with those from the acquirer will yield positive results. This view is supported by Porter (1987) who considered the management challenges arising from diversification/conglomeration, primarily achieved through acquisition, and found that, in addition to lower financing costs, shareholder value was created by the acquirer's professional management, especially expertise in areas such as taxation, business

planning and review disciplines to target areas of weakness for remedial action. BTR's renowned annual profit planning process and comprehensive monthly reporting package are prime examples of effective controls.

However, this view is not universally accepted. Matsusaka (1993) found evidence that undermines the leveraging of management skills; markets do not always view post-acquisition replacement of incumbent management positively. He found that during the 1960s markets viewed the post-acquisition retention of incumbent management positively and their replacement negatively.

It must also be remembered that, no matter how talented, knowledgeable, experienced and skilled a management team is, luck and the ability to persuade investors to provide finance also play a frequently significant part in success or failure. This view of management success or failure is exemplified by Sloan (1963, p429) who commented that *"It is not to say why one management is successful and another is not. The causes of success or failure are deep and complex, and chance plays a part"*.

Given the inherent complexity of conglomerates, their need for an effective and appropriate management structure to facilitate leveraging management skills is apparent and the importance of structure has been well researched since Chandler's (1962) pronouncement that '*structure should follow strategy*'. Williamson & Bhargava (1986) illustrated the choice of structures including Unitary (U-form), Holding Company (H-form), Multidivisional (M-form),

Transitional Multidivisional (M'-form), Corrupted Multidivisional (M-form) and Mixed (X-form). Research has highlighted the widespread adoption of the multidivisional, M-Form, structure by conglomerates. The primary advantage of multidivisional structures is that they attempt to group similar businesses together in often largely autonomous divisions, e.g. automotive, chemical, retail, etc. with each being overseen by a management team with appropriate skills and knowledge.

Williamson (1970, 1975) also provided support for the idea that management could bring greater efficiency to a range of companies operating under its control and for the effectiveness of M-Form structures. His economic rationale for the multi-business firm is based on Transaction Cost Economics (TCE) theory and takes the view that managers could allocate capital and resources more efficiently than the market and, by doing so, can create shareholder value. Williamson (1975) felt that some of this was also due to the rise of the M-Form structure which allowed managers to extend and exploit efficient multi-divisional structures by adding new businesses; the limitation of the old functional structures had been removed. In many ways *'the M-Form begat the monster of the conglomerate'* (Shleifer & Vishny, 1991).

Similarly, Kay (1997) and Angwin (2000) highlight divisionalisation as providing a means of minimising a potential disadvantage of conglomerates; that of cross-contamination. Kay (1997, p60) sees divisionalisation as minimising the risk of a poor performing activity infecting/contaminating others while Angwin (2000) sees it as allowing problem activities, depending on their

need for strategic direction from the corporate centre or resource transfer from other activities, to be isolated or kept at ‘arms length’ until they are fit to play a full roll in the business.

According to Whittington & Mayer (2000), 7 of the 8 companies identified as conglomerates in 1983 had divisional structures; the corresponding figures for 1993 were 15 of 16. The non-divisional companies – Rank Organisation in 1983 and Metal Box/Caradon in 1993 – had both adopted holding company structures. Given the overwhelming majority of conglomerates adopt the multidivisional model, it is not a variable that warranted further investigation in this research project. Moreover, without access to the education, skills or career histories of directors of FTSE100 companies, this research project could not consider whether these characteristics influence conglomeration although possible weaknesses in corporate governance that may allow chairmen and/or chief executives to overly influence strategic direction were investigated.

Role of Competition Authorities

Some businesses, typically in monopolistic or oligopolistic markets, are effectively forced to diversify as their size and dominant position would, should they attempt further focused growth, invite the attention of competition authorities who may limit such growth to ensure a reasonable level of competition is maintained.

The US was the first country to enact legislation relating to monopolies or, as they are known in the US, trusts; the Sherman Act 1890. Further legislation followed including the Clayton Antitrust Act 1914, the Celler-Kefauver Act 1950 and the Hart-Scott-Rodino Act 1976 which together effectively outlawed monopolies and required proposed acquisitions to be reviewed by the government before consummation.

In 1965 the UK became the first European country to enact acquisitions control legislation when, through the Monopolies & Mergers Act, it created the Monopolies & Mergers Commission (MMC) giving it a mandate to review all proposed transactions to see if they were against the public interest a broad indication of which was a market share of a least 33% (later 25%). Political expediency effectively sidelined the MMC until the early 1970s with the Industrial Reorganisation Corporation (IRC) established with a remit to create world beating UK companies, e.g. the merger of British Motor Holdings and Leyland to create British Leyland and the merger of English Electric with GEC were two deals brokers by the IRC. The Fair Trading Act 1973 re-established the role of the MMC.

Following the Competition Act 1988, the Competition Commission (CC) replaced the MMC and the Enterprise Act 2002 changed its role to one focused on competition issues giving it additional powers to make companies take remedial action to improve competition where problems had been identified. The CC continues to investigate not only proposed mergers and industries where competition issues have been identified, e.g. banking,

supermarkets, brewing, but, following privatisation of utilities, also problems in regulated industries where disputes have arisen between the regulator and the regulated.

In Europe, Germany introduced legislation in 1973 to prevent acquisitions that would create or strengthen market dominance and in 1977 France established a Commission on Competition to review domestic acquisitions where the resulting market share would exceed 40%. In more recent years the European Commission added another pan-European level of competition regulation with the establishment of its Competition Commission which is mandated to review acquisitions with combined turnover of €5 billion.

Given the existence of these authorities, companies contemplating further focused growth must be mindful of the potential for competition authority investigation and the remedies they may impose to restore competition. This problem was illustrated by the intervention of the CC in the battle for control of UK supermarket company Safeway (Competition Commission, 2003). In 2003, the leading UK supermarket chains - Tesco, Sainsbury, Asda and Morrison – were each told by the CC that, should they bid for, and subsequently win, control of Safeway, which had effectively been put up for sale, they would have to dispose of a number of stores in areas where they were deemed to have too great a market share thereby reducing customer choice. Morrison 'won' what effectively became a 'one-horse race' as the costs, in terms of required store disposals, placed on the other potential

supermarket bidders were too onerous. Even Morrison had to commit to selling 53 stores post-acquisition.

There is clearly a political dimension to this issue as the work of the competition authorities is influenced by the government of the day and its policies. In the US, the Reagan administration in the 1980s took a more lenient view of competition issues than its predecessors: 1977-81 Carter, 1969-77 Nixon/Ford and 1961-69 Kennedy/Johnson. Recently in the UK political expediency has necessitated the setting aside of competition rules to allow Lloyds TSB to acquire HBOS with the former effectively saving the latter in a deal, effectively brokered by the government, that created a 'superbank' – Lloyds Banking Group - with substantial market shares in mortgages, savings and current accounts that, in normal circumstances, would have been deemed against the public interest, competition reducing and stopped.

Clearly, competition regimes do impact conglomeration and this research notes instances where reference to competition authorities and/or their rulings have clearly influenced strategic decisions. The conglomerate histories included in chapter 7 refer to CC investigations that influenced diversification strategy, e.g. the impact of an investigation into competition in the UK brewing industry (Competition Commission, 1989) impacted on several subsequent proposed transactions by UK based brewers, including Bass/Intercontinental Hotels, Guinness/Diageo and Whitbread, which were referred to the CC who continued to act in line with its 1989 report that effectively limited UK market shares. In its deliberations, the CC appears to err on the side of the public

almost to the point of assuming companies under review are guilty of restricting competition until proved innocent although it would be unfair to suggest the CC is intransigent when considering company submissions.

Declining Industries & Growth Opportunities

Some companies cannot see a path to growth in their existing activities and therefore look to add/migrate to new activities. In 1970 British American Tobacco was almost exclusively a tobacco business; an industry perceived as having little future given the undoubted health issues associated with smoking and the growing intensity of ‘no smoking’ lobbies. In the late 1970s and early 1980s the company, which was renamed BAT Industries, adopted a conglomerate strategy to reduce its reliance on its ‘declining’ tobacco business by acquiring paper manufacturers Wiggins-Teape and Appleton, retailer Argos and insurers Eagle Star and Allied Dunbar in the UK and Farmers in the US along with a number of other smaller unrelated activities.

However, BAT Industries did not continue with its conglomerate strategy but, in the 1990s reversed its strategy and through a series of demergers and trade sales divested its 'non-core' businesses to, once again, become a single business tobacco company. Reverting to its original name, British American Tobacco sought to achieve growth through international expansion acquiring tobacco companies across the world to increase volumes and, through greater economies of scale, profits. British American Tobacco replaced conglomeration with internationalisation. After several years outside the FTSE100 the focused British American Tobacco regained its membership of

the index in 2003 where, surprisingly given the well-known health dangers of smoking that would suggest the industry to be in decline, it was not the only tobacco company. The index also included Imperial Tobacco which was demerged from Hanson in 1996 and Gallaher which was demerged from American Brands in 1997. Gallaher has recently (2007) been acquired by Japan Tobacco who appear to be pursing a similar global growth strategy to British American Tobacco.

Agency - Manager/Shareholder Balance of Power

Sundaramurthy (1996, p378) describes agency theory as *“viewing the corporation as a nexus of contracts”* with managers acting as agents for the shareholders who are the principals. As in any agency/principal relationship problems occur when there is ambiguity and uncertainty allowing room for the objectives of interested parties to become misaligned.

Although shareholders are the owners of a company they are seldom involved in its day-to-day operations instead they receive minimal, albeit statutorily required, information infrequently, typically semi-annually. In the post-war years as capital markets developed more companies, many previously family owned or controlled, obtained stock exchange listings. Their shareholders became more diverse with a consequent reduction in their power under the ‘divide and rule’ principle. The divorcing of ownership and control, together with shareholder apathy at the few opportunities they had to exercise power, principally general meetings, meant managers held the stronger position in the relationship and were able to pursue their own objectives which may not

always have coincided with those of shareholders and other stakeholders. Galbraith (1971) saw this shift in power towards managers as the creation of an effectively autonomous management 'technostructure'. This presented managers with an opportunity to run their companies in a way that maximised their own satisfaction; the 'hubris' theory (Roll, 1986).

In order to pursue their growth ambitions, some managers proved reluctant to distribute surplus cash to shareholders either through increased dividends or capital distributions, e.g. share buy-backs, preferring, especially where corporate governance was also weak, to retain surplus cash to fund diversifying acquisitions (Mueller, 1969). In addition to pursuing diversification/conglomeration, managers could also allocate retained resources sub-optimally. Scharfstein & Stein (2000) suggest that there may be 'socialism' in the allocation of resources resulting in poor performing divisions effectively being subsidised by those performing well. In effect, a CEO may allow sub-optimal allocations to be 'fair' or to 'keep everybody happy' rather than to maximise profit. This could result in diversification and/or conglomeration strategies being pursued despite yielding poor financial results.

Another management objective is their own continued employment and, through diversification, managers believe they can effectively hedge their employment risk (Amihud & Lev, 1981). However, Miller (2004) found that there was a risk that managers would over-diversify in their desire to reduce their employment risk and Shleifer & Vishny (1991) suggest the agency

problem was exacerbated by shareholders' failure to fully understand conglomeration, its inherent complexity, advantages, disadvantages and consequences for their investments. Sundaramurthy (1996) suggests that, without strong corporate governance, managements become 'entrenched' and can gain some immunity from the Market for Corporate Control that could force a change to the strategies they pursue. While particularly true of some US companies where managers can, sometimes without the need for shareholder approval, introduce anti-takeover measures this also has some resonance in the UK where, until recently, corporate governance has been seen as weak. Corporate governance weakness in the US, including the lack of non-executive directors and the prevalence of dual (joint chair/CEO) rather than unitary (separate chair and CEO) leadership, are seen as contributing to the problem of 'entrenched management' (Sundaramurthy, 1996).

Johnson, Hoskisson & Hitt (1993) undertook research into the influence of directors on restructuring finding that the relationship is complex and may be affected by shareholding profiles (significant director share ownership/options reduces their propensity to act in their own self-interest and promotes greater alignment of manager/owner objectives) as well as the balance of power between executive and non-executive directors and between the board and senior managers. Their study used the entropy index to assess diversification and questionnaires to obtain information on the internal power dynamics of companies researched. The inherent complexity of the diversification/ownership relationship is illustrated by the conflicting findings of research by Goranova, Alessandri, Brandes & Dharwadhar (2007) who found

that while levels of managerial ownership did not influence subsequent diversification, managerial ownership was negatively related to corporate diversification.

The increased separation of ownership and control and weaknesses in corporate governance may have contributed to the significant influence of dominant personalities at several high profile FTSE100 companies, notably Lords Hanson and White at Hanson, Sir Owen Green at BTR and Greg Hutchins at Tomkins. Since the mid-1990s some degree of balance has been restored by the introduction of corporate governance Codes of Practice requiring greater transparency regarding directors' remuneration and contracts (including incentive schemes), the separation of the key positions of chairman and chief executive officer (or equivalent) and a board comprising a majority of non-executive directors following the Cadbury committee report.

This research has not used questionnaires/interviews to supplement publicly available information and therefore cannot identify changes in internal power relationships – formal and/or informal – and their effects. However, by considering the tenure of chairmen and chief executive officers (or equivalents) this research does seek to identify similarities/differences in corporate governance across and between diversification categories.

Management Attitudes/Sciences

The 20th century saw an explosion of management theories to help managers make better, essentially profit maximising, decisions. Included in these

theories were several suggesting benefits could be derived from portfolio management. Ghemawat (2002) in his review of the development of the science of management highlighted several ‘popular’ models including Porter's Five Forces, Value Chain, Boston Consulting Group's Growth-Share Matrix (Boston Box) and Ansoff's (1965) Product/Mission Matrix. Each of these and many other models, such as Portfolio Planning (Haspeslagh, 1982) aim to help mangers to develop and/or refine their corporate strategy and, taking a ‘firm as portfolio’ approach, to decide on the optimal mix of business activities.

Almost by definition, the ‘firm as portfolio’ approach necessitates consideration of diversification. With this link in mind, several researchers have developed matrices to guide managers in making decisions regarding the strategic direction of their company. Salter & Weinhold (1979), who developed their own matrix based on industry attractiveness and business position to assess whether a company should diversify, also considered diversification by looking at three other well-known models:

- **Strategy Model** - Companies should diversify where there is potential for skills/know-how/technology transfer between the businesses. This model relies on the concept that companies are a collection of resources and competences that can be used to create and maintain competitive advantage: the resource-based view. By acquiring new activities that would benefit from their resources and competences, a company could

grow. Success is dependent on correctly understanding which resources/competences are valuable and in which activities.

- **Product/Market-Portfolio Model (form of BCG market share/growth matrix)** - Companies should diversify to either build a presence in key areas of the matrix, i.e. "Question Marks" or "Cash Cows", where they can dominate markets or use excess cash to develop opportunities: *"A company with a balanced portfolio of cash cows feeding question marks and stars is in a position both to reap the current benefit of its high market share and advantageous cost position and to develop sources of future cash flow"* (Salter & Weinhold, 1979, p75).

- **Risk-Return Model (developed from CAPM theory)** - Companies 'can' use diversification to reduce unsystematic risk, i.e. the risk inherent in investing in particular industries. However, investors can diversify for themselves with similar results: *"…various studies have shown that as few as 8 to 10 unrelated investments are sufficient to eliminate over 80% of a portfolio's unsystematic risk"* (Salter & Weinhold, 1979, p128).

While each of the approaches recommended by Salter & Weinhold (1979) has its merits, it may also be argued that each is too simplistic reducing the inherent complexities and inter-relationships of corporate decision-making, especially in large conglomerates, to 2 x 2 matrices. In some ways the increase in the number of management theories encouraged managers to

explore diversification and to believe they could effectively manage it whereas before they would have continued to pursue focus.

Others

There are several other enablers or drivers that supported the adoption of conglomeration strategies.

- **Leveraging Company Attributes**

  Companies seek to maximise returns from investments in their business, e.g. distribution networks, research & development facilities, sales forces, etc., especially if those investments are perceived to be sources of sustainable competitive advantage. Work by Lemelin (1982) considered patterns in diversification and found that there are links between diversification and the desire to exploit existing investments. This is especially true *"with respect to channels of marketing and distribution"* (p647). Clearly, leveraging company attributes works better for related diversifiers where there are product/service complementarities as well as the need to share corporate competences.

  Further support for the leveraging of company attributes comes from Penrose (1959) who, in her resource-based view, believed that companies holding surplus resources would always look for ways to profitably utilise those resources, a view later supported by Teece (1982). Whittington & Mayer (2000, p56) built on this saying, *"….it is the existence of surplus resources that stimulates diversification, and it is the nature of these*

existing resources that determine the direction in which this diversification goes". However, there is no guarantee that diversification represents the most effective or profitable use of surplus resources obvious alternatives being to increase distributions to shareholders, e.g. higher dividends or return of capital, and/or reduction/elimination of debt.

- **Opportunism**

  Some companies constantly trawl the market looking for underperforming companies that they can acquire cheaply and to which they can add value. While private equity companies are now seen as leading exponents of this strategy, BTR and Hanson were skilled exponents in the 1980s acquiring underperforming companies including Thomas Tilling, Dunlop Holdings and London Brick.

- **Asset stripping or asset mining**

  There is an obvious link between opportunism and asset stripping which is perceived by many as an insidious business practice. In brief, asset stripping is the acquisition and subsequent break-up and piecemeal disposal of a company with the expectation that the proceeds of disposal will exceed the costs of acquisition. The success of any asset stripping exercise is dependent on the value of a company's component parts being worth more than the whole; the company has negative synergies and is 'worth more dead than alive'. The acquisition and break-up of undervalued companies for profit is exemplified by Hanson's acquisition of Imperial in

1987; the subsequent disposals reduced the net cost of the highly profitable tobacco business to a fraction of its true value.

- **Available financing**

  The development and growth of increasingly complex debt instruments, the greater sophistication of financial markets and the substantial rise in pension funds, has made more funds available for growth.

  Comment & Jarrell (1995, p84) refuted the claim that conglomerates could borrow more at lower cost when they looked at leverage across diversification categories finding that there were few significant differences meaning, *"….either that diversification does not increase debt capacity or that managers in diversified firms do not choose to exploit their greater debt capacity"*. Notwithstanding the availability of finance, the sophistication of markets has increased the acceptability of higher 'paper' elements in takeover bids.

- **Critical Mass**

  The concept of 'critical mass' (Salter & Weinhold, 1979, p43) is more of an issue in dominant and related diversified businesses where greater control over an activity, e.g. through vertical and horizontal diversification, may result in increased control over that business activity/market segment compared to competitors. A company that has 'critical mass' in an industry or market may be able to influence, rather than be influenced by, that

industry or market, i.e. become the leader rather than a follower. Acquiring critical mass changes the balance of power within an industry.

Summary

Overall, this section has identified a number of drivers behind conglomeration some of which have had a greater effect than others. The drivers may be split into generic - those that effect the strategic decisions of all companies – industry specific – those that effect companies operating in a particular industry – and company specific – those that influence the strategic decisions of some, but not all, companies as shown in the following table:

Table 11: Drivers of Conglomeration

Driver	Generic	Industry Specific	Company Specific
Risk & Earnings Stability	X		
Leveraging Management			X
Competition Regulation			X
Declining Industries		X	
Growth Opportunities		X	
Agency – Power Balance	X		
Management Attitudes/Science	X		

Some drivers may have influenced the entire population, e.g. the development of management skills and the search for lower risk, while others may have effected only a few companies, e.g. a declining industry would affect only companies with interests in those industries. It is certain that, in determining diversification strategy, management is influenced by more than one driver.

This research recognises that the complexity of the business environment and the inherent uniqueness of companies effectively makes it is impossible to fully explain which drivers were behind which companies' decisions to

diversify and, conversely, which changes in drivers were behind companies' decisions to refocus. However, in chapter 7 there are a number of conglomerate company histories that try to shed light on why FTSE100 companies adopted, maintained or abandoned conglomeration between 1993 and 2003.

3.3.2.3 Role of Acquisitions

Acquisitions have played an important role in the growth of conglomeration through the 20th century both in the US and the UK. Once a decision to diversify has been taken, a company must chose how to achieve that strategy; organically or by acquisition.

In the US and UK, acquisitions activity was volatile through the 20th century with 4 clearly identifiable peaks, each larger - both in volume and constant value terms - than its predecessor. The first three peaks have each been attributed to a different phenomenon (Lev, 1982, and Salter & Weinhold, 1979, p10-11):

- 1895-1900 : Consolidation
- 1920s : Utility consolidation, manufacturing vertical integration
- 1960s : Diversification*

* Diversification includes both related and unrelated.

The 1960s diversification driven peak in activity coincides with growth in diversification – related and unrelated – identified in the US and, to a lesser

extent, Europe. The 1960s peak has since been surpassed by another at the end of the 1990s, which saw global activity reach £2.5 trillion in 2000, (Acquisitions Monthly, January 2002).

This most recent peak has been attributed to acquirers' growth aspirations and rising opportunism especially amongst the increasingly active private equity houses including Blackstone, Apax, Texas Pacific, BC Partners, Cinven, Permira and KKR, that may have effectively become the 'New Conglomerates'. In the UK, by 2003 private equity firms were the largest private-sector employers with 2.9m employees (Durran, 2003). However, as private equity becomes increasingly 'popular' and, as the acquisitive conglomerates of the 1980s found in the 1990s, the pool of underperforming and undervalued targets dries up, their position as the 'New Conglomerates' may become uncertain (Riley, 2007). Furthermore, as much of the success of private equity stems from financial engineering, especially the use of debt, continued success is heavily dependent on low interest rates and the availability of funds (Jackson, 1998).

When considered in value terms, acquisitions activity in the late 20th century was undertaken by a relatively small number of highly acquisitive companies, several of which were conglomerates. Between 1983 and late 1987, Scoullar (1987) noted that only 8 companies accounted for over 50%, by value, of UK acquisitions. These companies were: Guinness, Hanson, BAT Industries, BTR, Vantona Viyella, Habitat, Burton and P&O. The deals undertaken by the 3 Whittington & Mayer (2000) conglomerates included on the list include

BTR's 1983 acquisition of Thomas Tilling for £850m, BAT Industries' 1983 acquisition of Eagle Star for £1,060m and Hanson's 1986 acquisition of Imperial for £2,564m. The largest non-conglomerate transaction was Guinness' 1986 acquisition of Distillers for £2,531m. The dominance of the conglomerate acquirers continued through into the early 1990s with Hanson's acquisition of ConsGold in 1989 for £3,300m and BTR's 1990 acquisition of Hawker Siddeley for £1,600m. However, in contrast to the 1980s and early 1990s transactions that were predominantly acquisitions by industrial/manufacturing conglomerates, transactions towards the end of the millennium were dominated by service companies including, in financial services, Royal Bank of Scotland's acquisition of National Westminster Bank for £21.6bn and, in telecommunications, Vodafone's £100bn acquisition of Germany's Mannesmann.

Companies that decided to advance through the Model of Corporate Development were faced with a decision as to how to achieve their aims - organically or by acquisition. Many large companies saw acquisition as being the most cost effective option (Lamont & Anderson, 1985) and therefore it became the primary means of diversifying (Hitt, Hoskisson & Ireland, 1990). The advantages of acquisition over organic growth include:

- **Speed** - Acquiring a ready-made business with an existing product range, experienced management and distribution network is far quicker than starting from scratch.

- **Cost** - Acquisition, despite acquisition premiums, is almost always cheaper than organic growth which often entails high capital costs for new equipment and a period of losses while the new business builds and the necessary skills, knowledge and experience are developed.

- **Intangibles** - Where success is heavily dependent on possession and exploitation of intangible assets, e.g. patents, trade marks, copyrights and distribution networks, acquisition may be the only way to acquire the necessary assets.

- **Entry barriers** - High entry barriers, typically cost or intangible asset-based, may also preclude new 'organic' entrants. However, the protection offered by high entry barriers may push up the cost of acquiring an incumbent 'protected' business.

Having chosen the acquisition route to conglomeration, companies were then faced with deciding which targets to pursue. In choosing targets that would increase the diversity of their activities, companies needed to assess potential acquisitions against three key criteria, Porter’s (1987) "Essential Tests".:

- **The attractiveness test**

  The new industry or industries must be or have the potential to be structurally attractive, i.e. a positive evaluation using Porter's "5 Forces" model. Is the industry capable of producing 'acceptable' returns?

- **The cost-of-entry test**

  Is the cost of acquisition lower than the present value (discounted at the acquirer's cost of capital) of future earnings streams, i.e. will it make a positive contribution?

- **The better-off test**

  Will the acquirer AND target both benefit from the proposed link, i.e. are there any transferable competitive advantages, e.g. synergy benefits including shared facilities/resources/know-how?

In order for an acquisition to enhance shareholder value all three of the Essential Tests have to be met. However, UK conglomerates that grew in the 1970s and 1980s made acquisitions that MAY not have met all of Porter's tests. Again taking BTR and Hanson as examples, their acquisitions frequently passed the first two tests but not always the third. Both companies targeted established businesses that were performing poorly, e.g. Thomas Tilling, Dunlop, London Brick, and consequently were undervalued and could, despite control premiums, be acquired for prices significantly below their 'true' restructured and reinvigorated values. Therefore, they passed the attractiveness and cost of entry tests. However, whether the better-off test was always passed is debatable. This failure would not have become apparent until after the acquisitions had been completed, i.e. once post-acquisition performance had been realised, and could not have influenced shareholders when they were asked to support and, if necessary, vote on the

proposed acquisitions. Shareholders had therefore to take their boards' recommendations at face value.

According to Goold & Campbell (1987) both BTR and Hanson were 'Financial Control' companies who, by closely monitoring financial performance against agreed targets, acted, in effect, as portfolio managers, i.e. they bought and sold companies although, as noted later, not as ruthlessly as they could have. This management style is consistent with their approach to acquisitions typically passing tests 1 and 2 and failing 3, i.e. the actions of short-term investors seeking to obtain 'one-off' gains from turnarounds. In 1987, Goold & Campbell held BTR and Hanson (together with Tarmac, GEC and Ferranti) as being very successful financial control style companies. But this success has proved to be unsustainable; all five financial control companies have incurred serious problems and none survived into the new millennium without substantial change. In updates to their original paper (Goold, Campbell & Luchs, 1993a, 1993b) argued that, to enjoy continued success, companies had to ensure they matched their management style to the needs of their portfolio of businesses. The implication of their review was that unsuccessful companies, not only the financial control companies, had failed to do so.

By definition, as the activities of a company become increasingly diverse connections between activities become, at best, tenuous and, at worst, non-existent, e.g. BTR's ownership of heavy engineering and hosiery businesses. Having acquired 'problem' companies, both BTR and Hanson were (or became) very adept at changing management teams, closing loss-making

activities and, especially in Hanson's case, divesting unwanted businesses. This resulted in rapid turnarounds in financial performance. The next stage, increasing profits beyond the acquired company's turnaround potential, was dependent on the acquisition meeting the third test, i.e. both acquirer and target gaining from the transaction. There is little evidence that either BTR or Hanson was able to develop businesses acquired beyond achieving a turnaround. If the third test were failed, then the potential for the acquisition to continue to grow would be severely limited. In these circumstances, it could be argued that the acquirer should sell the acquired company immediately its turnaround is realised (assuming there are buyers). Porter (1987) suggests that if revitalised acquisitions are retained, as was often the case at BTR, then without further acquisitions (turnarounds) future company profits would stagnate which is effectively what happened at BTR in the mid-1990s. This evidence suggests that conglomerates possessed turnaround skills but not the capability to further grow and develop businesses once turnaround had been achieved.

The achievement of consistent profitable performance has important implications for growth by acquisition. Strong financial performance usually translates into a high share price which, in turn, provides the opportunity to make market value enhancing acquisitions using shares as payment. The exploitation of a high price/earnings ratio is commonly referred to as the ‘P/E Puzzle’. In simple terms, the P/E puzzle is where a highly rated group, e.g. BTR or Hanson at their peak, acquires a poorly rated underperforming company, probably with a disappointing profit record, or activities in

'unfashionable' businesses. Post-acquisition, investors assume the acquirer will be able to improve profitability at its new subsidiary and optimistically apply the acquirer's high P/E ratio to the new enlarged company's profit projections to calculate the new equity value for the combined company. As a result, the acquiring company's market capitalisation will increase by more than the value of the acquisition as the future stream of earnings from the acquired company are now given a higher P/E multiple by the investment community. The fault with this approach lies in the fact that the underlying and potential profitability of the acquired company, may, in reality, be significantly below that implied by the revaluation and be restricted by fundamental limitations in the industry/business in which it operates. However, given the level of aggregation in company financial statements, as long as a company continues to make substantial acquisitions any underperformance of previous acquisitions or of the underlying business is effectively shielded if key indicators – growth and profits – show overall continuous increases. The market value of conglomerates such as BTR and Hanson, whose acquisition activities reduced the transparency of their published accounts, benefitted from this phenomenon.

Conn (1973) analysed US data for acquiring and acquired firms through the period 1954 to 1969, and showed that while the acquisition of relatively profitable firms did not enhance an acquirer's profitability the transference of a high P/E to an acquired company’s activities did enhance value and was a valid driver of acquisitions giving credence to the ‘P/E Puzzle’ phenomenon. Conversely, Matsusaka (1993) suggested that the ‘P/E Puzzle’ is not that

important a factor as investors see 'bootstrapping' for the game that it is. That may be true of 'professional' institutional investors but less so of individual private investors.

Data included in the Annual Reports of the Director General of Fair Trading, show the popularity of diversifying acquisitions through to the end of the 1980s. The following table shows that through the 1970s and 1980s between a quarter and a third of all proposed acquisitions were diversifying transactions and that in the 1990s, when conditions were less favourable, activity in this category fell dramatically, accounting for less than a tenth of proposed acquisitions.

Table 12: Percentage of Proposed Mergers Classified by Type of Integration

Year	Horizontal	Vertical	Diversifying	
1970-74	73	5	23	1970s
1975	71	5	24	
1976	70	8	22	
1977	64	11	25	
1978	53	13	34	
1979	51	7	42	
1980	65	4	31	1980s
1981	62	6	32	
1982	65	5	30	
1983	71	4	25	
1984	63	4	33	
1985	58	4	38	
1986	69	2	29	
1987	67	3	30	
1988	58	1	41	
1989	60	2	37	
1990	75	5	20	1990s
1991	88	5	7	
1992	93	1	6	
1993	90	3	7	
1994	88	5	7	
1995	91	1	8	
1996	93	2	5	

Source: Office of Fair Trading, Annual Reports of the Director General of Fair Trading

This data, albeit comprised of proposed rather than consummated transactions and without any distinction between related diversification and conglomeration, strongly supports the contention that in the UK diversification activity was strong up to 1990. Beyond 1990 horizontal transactions show a significant increase suggesting that companies were eschewing diversification in favour of focus. Unfortunately, the series was discontinued in 1997.

Similar data on US acquisitions appears to show the same profile with peaks in both broadly and narrowly defined diversifying transactions in 1975 followed by substantial reductions in 1976, 1977 and 1978.

Table 13: Large Diversifying Acquisitions by Industrial Companies: Percentage of Total Assets Acquired[a]

Year	FTC Narrow Definition[c]	FTC Broad Definition[b]
1952-1955[d]	3.6	52.0
1956-1959[d]	14.0	N/A
1961-1970[d]	30.4	78.5
1971	45.3	79.2
1972	16.8	59.2
1973	36.7	65.3
1974	38.0	68.2
1975	68.3	94.6
1976	54.8	83.6
1977[e]	44.6	77.7
1978[f]	46.7	76.0

Notes:
[a] Large acquisitions are those involving acquired assets exceeding $10million.
[b] All acquisitions extending operations beyond present product or geographic markets.
[c] Acquisitions where the two companies are functionally unrelated in marketing or production.
[d] Average for the period.
[e] 1977 figures are subject to revision.
[f] 1978 figures are preliminary.

Sources: Salter & Weinhold (1979, p15). Original sources - Bureau of Economics, FTC, Statistical Report on Mergers and Acquisitions, July, 1974, October 1975, November 1977 and December 1978; and Jesse W. Markham, Conglomerate Enterprise and Public Policy, Division of Research, Harvard Business School, 1973.

The above table shows unrelated acquisitions (FTC Narrow Definition column) comprised a 1952-55 average of only 3.6% of all transactions involving assets of at least $10m. By 1971 the figure was 45.3% and, after the recession years of 1972-74, peaked at 68.3% in 1975 before falling back to 46.7% by 1978.

The UK and US profiles appear to support the contention that the life cycle of conglomeration amongst UK companies lags behind that experienced in the US by around 10-15 years. Conglomerate acquisitions peaked in the late 1970s in the US and in the UK proposed diversifying acquisitions, including related and conglomerate transactions, peaked in late 1980s. The wave of conglomerate acquisitions appears to have begun in the US and then moved to the UK. Similarly, the decline in conglomerate acquisitions activity began earlier in the US than the UK.

The database constructed for this research does not include details of each company's acquisitions but does note acquisitions involving companies within the FTSE100, e.g. Guinness' acquisition of Grand Metropolitan to form Diageo, Siebe's acquisition of BTR to form Invensys. This information, together with the relevant company histories in chapter 7, provides insights not only into the reasons for exits but also into movements between diversification categories within the UK's leading stock exchange index.

3.3.3 Re-Appraisal and Decline

A key element that contributed to the growth and decline of conglomerates was their financial performance – real or perceived. In the growth phase,

conglomerates were seen as offering low risk and earnings stability while in the decline phase they were seen as being economically inefficient. Finding research that supports these performance perceptions is difficult as extant research is contradictory and, given that a range of categorisation schemes is used and that there are always industry effects involved, confusing.

Some of the criticism of conglomerate performance may not have been rational but driven by the inability of analysts to fully understand these complex companies. With conglomeration had come increased corporate complexity and, as a consequence, greater opacity in financial performance. When compared to ‘pure play’ focused companies, conglomerates were judged to have performed poorly. In addition, conglomerates were increasingly seen as being inefficient in their allocation of capital with cross-subsidisation of underperformers by strong businesses reducing overall returns although research by Hubbard & Palia (1999) suggests the internal capital markets of diversifying acquirers were more efficient than those of the external markets that were effectively constrained by their lack of information. Conglomerates had fallen out of favour with the investment community who, by the 1990s, were increasingly of the view that conglomerates should put into practice the advice of Whittington & Mayer (2000, p217) that *"Corporates need to know when to be practitioners of corporate euthanasia"*.

3.3.3.1 Performance

This section considers the performance of conglomerates compared to other categories of company. In analysing conglomerate performance their use of

acquisitions as a means of growth comes to the fore and, given the poor post-deal performance of many acquisitions, has a major bearing. Acquisitions may provide a quick route to conglomeration and to turnover growth but their effect on profitability is less clear.

One of the major advantages claimed for conglomerates is their superior level of profitable growth compared to other categories of company. However, a review of the, predominantly US, literature does not provide clear evidence that conglomerates consistently outperformed other categories. Dess, Gupta, Hennart & Hill (1995) reviewed the findings of 32 papers, all except that by Grant, Jammine & Thomas (1988) into US, principally Fortune 500 or 1000, companies with the majority using Rumelt's strategy-based categorisation scheme in preference to SIC/Entropy. The studies revealed no clear picture regarding the relationship between diversity and performance with a broad range of positive, negative and neutral outcomes being observed. However, Dess, Gupta, Hennart & Hill (1995, p30) are quick to point out that, as with Rumelt's (1974) original work, many of the subsequent studies failed to control for industry effects.

Some of the earliest research into diversification was that by Weston & Mansinghka (1971) who compared conglomerates and non-conglomerates. Unsurprisingly, given their predilection to diversify by acquisition, conglomerates were found to grow more rapidly than comparative focussed companies. However, they also found that although the earnings/net worth of conglomerates was higher than for non-conglomerates the difference was not

statistically significant. By the end of their study, i.e. 1968, there were *"no significant differences in earnings performance"* (p925) where earnings were linked to total assets or net worth plus long term debt. It is important to note that there was a wide variation in performance across the conglomerate category with some companies performing significantly better than others inferring an industry effect and/or that the ability of management has a very direct influence on financial performance.

Rumelt (1974) used his 4-category categorisation scheme to research the performance of US conglomerates and found marked variations in average performance across diversification categories between 1949 and 1969 as the following table shows:

Table 14: Annualized Performance of Listed NYSE Companies, 1949-1969

All Figures % Diversification	Sales Growth	Earnings Growth	EPS Growth	ROC	ROE
Single-business	7.17	4.81	3.92	10.81	13.20
Dominant-business	8.03	7.95	5.99	9.64	11.64
Related-business	9.14	9.39	7.64	11.49	13.55
Unrelated-business	14.24	13.86	7.92	9.49	11.92
Average all comps	9.01	8.72	6.57	10.52	12.64

Source: Rumelt (1974, p91)

Conglomerates did produce superior growth rates achieving the highest sales growth, 14.24% compared to the overall average of 9.01% but also the lowest return on investment, 9.49% compared to 11.49% for related diversifiers and 10.52% overall. Of the other categories, single-business and related business companies produced better than overall returns implying that companies focusing on core activities rather than pursuing conglomeration produce better results.

Salter & Weinhold (1979, p24) note that, in response to criticisms regarding failure to control for industry, Rumelt refined his analysis adjusting for industry effects by comparing each company's performance to a weighted average 'synthetic' profit calculated for each company according to the proportions of its total investment in various business segments. Rumelt also sub-divided some of his original categories with related being split into constrained and linked and unrelated split into multi-business and unrelated.

The following table compares the performance, in terms of return on capital, of each of Rumelt's extended categories against weighted 'average' expected performance. The notes explain the new categories.

Table 15: Performance Differences Among Rumelt's Strategic Categories (Weighted for Industry Affiliation), 1962-1971

All figures % Category	Actual ROC	Expected ROC[a]	Residual
Single Business	11.45	9.94	1.51*
Dominant - Constrained[b]	12.09	11.01	1.08
Related - Constrained[b]	12.28	11.67	0.61
Related Linked[b]	10.53	10.83	(0.30)
Multibusiness[c]	8.30	10.13	(1.83)*
Unrelated Portfolio[c]	8.80	10.46	(1.66)*
Average for all companies	11.00	10.89	0.11

Notes:

[a] Average return on capital over the period for all the companies in each strategic category if they were average performers in the industries in which they participated.

[b] Rumelt's "constrained" categories closely correspond to related-complementary diversification while his "linked" categories closely correspond to related-supplementary diversification.

[c] Rumelt expanded his original unrelated category into a multibusiness segment, or companies with 2-4 relatively balanced though unrelated businesses, and an unrelated portfolio segment, or companies with numerous unrelated businesses.

* Significant at the 5% level.

Sources: Salter & Weinhold (1979, p24). Original source - Richard Rumelt, “Diversity and Profitability”, University of California at Los Angeles Working Paper MGL-51, 1977.

Using average return on capital, the best performers are single business companies which produced returns 1.51% higher than the average with the worst being the multi-business and unrelated portfolio business categories, i.e. conglomerates, whose returns were 1.83% and 1.66% lower than the average respectively. These results support those of Rumelt's (1974) earlier work.

Rumelt (1982) continued to research into the profitability of the increasingly common conglomeration strategies of US companies finding further support for his earlier results that *"corporate profitability differed significantly across groups of firms following different 'strategies' of diversification"* and that *"the lowest levels were those of vertically integrated businesses and firms following strategies of diversification into unrelated businesses"* (p359).

Holzmann, Copeland & Hayya (1975) also compared the financial performance of US conglomerates and non-conglomerates starting with the premise that: *"the growth of conglomerate corporations is often justified on the grounds that conglomerate mergers are likely to lead to superior risk-return performance, the customary rationale underlying portfolio diversification"* (p74). They categorised 349 companies using definitions developed by Forbes (1965) and Weston & Mansinghka (1971) as either conglomerate or non-conglomerate and used four performance measures; two asset-based (operating income/total gross assets and operating income/book value of equity) and two equity-based (net income after tax/stockholders' equity and net income available for common equity) to assess the performance of both

groups. They did not try to link conglomerate performance to share price performance. Data covering the period 1951-1970 was analysed and, for asset-based measures, conglomerates produced lower but less variable returns. However, for equity-based measures the picture was less clear; non-conglomerates achieved higher mean returns but they also experienced greater mean variances suggesting greater volatility.

Holzmann, Copeland & Hayya (1975) noted that their findings were consistent with earlier research by Reid (1968) who asserted that conglomerates were size rather than profit maximisers and by Weston & Mansinghka (1971) who showed that conglomerates diversified defensively to reduce risk and increase stability of returns. In summary, Holzmann, Copeland & Hayya (1975, p76) said that *"….on the basis of our findings it is possible to speculate that conglomerate managers were more concerned with overall firm performance and growth than with returns to equity holders"*. Holzmann, Copeland & Hayya (1975) also referenced consistent findings from research by Berle & Means (1968), Mason (1959), Penrose (1959), Marris (1964), Galbraith (1971) and Herendeen (1974).

Research by Mason & Goudzwaard (1976) found that, compared to randomly selected portfolios, conglomerates did not produce superior returns. They questioned why conglomerates need to exist if individual investors can achieve the same or better results. Another paper along the same lines is that of Melicher & Rush (1973) who compared the financial performance (ratio based) of 45 conglomerates against 45 non-conglomerates with the

constituents of both groups having been in the same basic industry in 1960. The financial performance of both groups was found to be similar: *"the irony of our findings is that the conglomerates were shown to be no better or worse off than those firms that remained in the basic industries that the conglomerates abandoned"* (p388).

Salter & Weinhold (1979) produced data showing that, on average, conglomerates perform worse than the market in general as represented by the average of companies comprising the All Industry Composite. Their results are summarised in the following table:

Table 16: *Business Week* Survey of Business Profits[a]

	Conglomerates[b]		All Industry Composite	
Year	Average Return On Equity	Average Price-Earnings Ratio[c]	Average Return On Equity	Average Price-Earnings Ratio[c]
1973	11.3	6	14.0	11
1974	11.8	5	14.0	9
1975	11.3	8	11.8	12
1976	13.2	8	14.0	10
1977	12.9	7	14.1	9
1978	13.5	6	15.1	8

Notes:
[a] Based on Business Week's Quarterly Survey of Business Profits.
[b] The composition of Business Week's conglomerate category is Teledyne, Northwest Industries, Textron, Avco, Studebaker-Worthington, Southdown, Martin Marietta, Signal, Colt Industries, Whittaker, Bliss & Laughlin Industries, Tenneco, Chromalloy American, Gulf + Western Industries, Fuqua Industries, Kidde (Walter), City Investing, IU International, U.S. Industries, IC Industries, Litton Industries, LTV.
[c] Based on price-earnings ratio in effect on evaluation date.

Source: Salter & Weinhold (1979, p27)

In each year both the average return on equity and the average price earnings ratio of conglomerates was substantially below that of the all industry composite. Salter & Weinhold (1979) also quote statistics of relative economic

performance between 1965 and 1978 showing the S&P index of 10 conglomerates underperformed the S&P 400 index of industrial companies and the S&P index of major companies by a substantial margin. As with Rumelt's (1974) early work, Salter & Weinhold (1979) did not control for industry effects. Furthermore, their conglomerate population, the Business Week Conglomerates, comprised a small group of only 32 companies limiting the robustness of their research.

According to Bettis & Hall (1982) industry effects can have a significant bearing on conglomerate performance. Acknowledging that diversification can be into either related or unrelated activities, they noted conglomerates should have an advantage saying, *"….unrelated diversification strategies would seem to have an advantage because they permit a wider choice of industries in which to participate"* (p255). Notwithstanding the need for diverse companies to match business strategies to their activities if overall performance is to be optimised (*"high performing diversified firms may be those firms that are able to develop and pursue appropriate strategies in their constituent businesses"* (p256)) Bettis & Hall (1982) note that the success of conglomerate strategies remains heavily dependent on the business activities into which the company diversifies. Their research showed the best performers were those with businesses in pharmaceuticals, a high growth/high profit industry. A key finding from Bettis & Hall (1982, p262) is that *"…the researchers are led to conjecture that selection of industry or industries in which to participate may be more important than a related or unrelated diversification strategy....further research is needed to separate fully the effects of industry participation from*

the effects of diversification strategy and to determine whether the two interact in some manner". In effect, corporate investors are faced with the same industry choices as private investors; both can see the relative industry performance and can make choices based on that information. The inference is that the success of a conglomerate is heavily dependent on the portfolio choices made by management.

Looking at the performance issue from a value perspective, there is a substantial body of evidence supporting the view that diversified firms are consistently valued less than 'pure play' firms. Lang & Stulz (1994) researched the Tobin's *q* ratios for US firms through the 1980s finding that *"Tobin's q and firm diversification are negatively related throughout the 1980s. This negative relation holds for different diversification measures and when we control for other known determinants of q [for example, R & D]. Further, diversified firms have lower q's than comparable portfolios of pure play firms"* (p1248). This finding was consistent with that of Servaes (1996) into performance in the 1960s and 1970s.

Berger & Ofek (1995) also considered the effect on a firm's value of its diversification activities. They found that during the period 1986-1991, when compared to focused companies, diversified companies lost 13-15% of their value. Berger & Ofek (1995) recognised the potential benefits of diversification, notably the acquisition of imperfectly correlated (counter-cyclical) profit generators, better management and resource allocation. However, they also believed that loss-making companies lose more when part

of a conglomerate than they would as independent companies as they will be cross-subsidised by other profitable operations reducing pressures to improve.

The very limited UK literature on conglomerate performance should be considered in light of the foregoing US research. Grant & Jammine (1988) conclude that, overall, UK research, limited though it is, has failed to *"shed appreciable light on the relationship between diversification strategy and performance"* (p335). Their opinion is supported by the conflicting findings of Grinyer, Yasai-Ardekani & Al-Bazzaz (1980) who found in favour of dominant business firms, Hill (1983) who found volatility but little difference in mean profitability and Luffman & Reed (1982) who found conglomerates performed better than related diversifiers. However, Grant & Jammine (1988) do note that research in this area has not been consistent with differences in profitability measures having a major influence.

Finally, it should be remembered that much of the extant literature relates to the 1960s and 1970s, a period when conglomeration and conglomerates were enjoying growth rather than contraction. Haynes, Thompson & Wright (2002, p173) covered a more recent period – 1985 to 1993 – and reported a *'positive, significant and substantial'* relationship between divestment and performance suggesting the refocusing activities undertaken by conglomerates improved their financial performance. However, research by Montgomery & Wilson (1986) into the subsequent divestment of large acquisitions made by US public companies between 1967 and 1969, the

height of the diversification boom, found no significant difference between the number of related and unrelated business divested.

Reliability of Financial Data

When assessing performance it is important to recognise that the reliability of financial performance data has, over recent years, increasingly been called into question. The lack of transparency of financial information adds to a general mistrust of conglomerates. In the UK, Smith (1996) wrote a best seller in which he claimed to be *"stripping the camouflage from company accounts"* to highlight how performance may be manipulated. Whilst Smith (1996) did not confine his analyses and criticism to conglomerates, they were well represented in his book which drew attention to a number of the 'creative' accounting practices that were in widespread use and looked at how many leading public companies adopted them strongly inferring that, in doing so, they were manipulating their accounts and to some degree misleading investors as to their financial performance. Biographies of some leading businessmen, e.g. Lord Hanson at Hanson (Brummer & Cowe, 1994), have, by questioning the financial performance of the companies they ran, provided support to Smith (1996).

The practices highlighted by Smith (1996) were, at the time, all legal and within the range of accounting treatments acceptable under accounting standards. However, several have since been restricted or eliminated by new/revised standards issued by the Accounting Standards Board (ASB) and its successors the Accounting Standards Committee (ASC) and the Financial

Reporting Council (FRC). While the ASB, ACS and FRC have closed some loopholes, many still remain. Interestingly Smith (1996, p162) notes that US generally accepted accounting practices are more prescriptive than their UK equivalents reducing, but not entirely eliminating, scope for interpretation and therefore, manipulation. Where companies have dual US and UK reporting requirements, e.g. those with a US stock market listing, Smith (1996) advocates using accounts prepared under US rather than UK GAAP when undertaking analyses.

The book was first published in 1992 and in the second edition Smith (1996) defends his record noting that several of the companies he originally criticised for questionable accounting practices had, by 1996, experienced difficulties. The following table lists the criticised companies and their subsequent problems and note in parentheses the number (out of 12) of dubious practices adopted by each company:

Table 17: Companies Using the Most Dubious Accounting Practices

Company	Problems
Tiphook (4)	In talks with banks, debts soar
Queens Moat (6)	Financial reconstruction underway
Trafalgar House (8)	Auditors, chairman and chief executive depart; huge losses, two rights issues
Albert Fisher (7)	Losses, chairman departs
British Aerospace (7)	Record losses, rights issue
Ratners (7)	Founder departs, huge losses
Lonrho (6)	Huge changes in way group is run
GrandMet (9)	Shares underperform
Bass (6)	Shares underperform
Ladbroke (8)	Chairman steps down

Source: Smith (1996, p7)

While it is easy to suggest cause and effect between dubious accounting practice and subsequent problems, it must be remembered that many other

factors may have been influential, e.g. Ratners' problems were primarily due to extremely ill-advised comments by its CEO Gerald Ratner who, in a high-profile speech, described some of its products as 'total crap'!

A company singled out by Smith (1996) is the conglomerate BTR. Smith (1996) points to the 'misuse' - aggressive but not illegal - of provisions during the company's acquisition of Hawker Siddeley in 1990. According to Smith (1996), BTR acquired Hawker Siddeley, which had net assets of £748 million, for £1,513 million and then created provisions, primarily to adjust book asset values to fair values, of £445 million (£285 million in 1991 and £160 million in 1992). These 'fair value' adjustments - made under the rules of SSAP22 (revised) - represented 59.5% of the net asset value and 29.4% of the purchase consideration. Smith's (1996) point is that the judicious reversal of these provisions, and others relating to other acquisitions and activities, without the matching costs being incurred, helped BTR maintain its historically high margins in subsequent years 'confusing' markets into believing that it was continuing to trade very profitably when, in reality, it was not. BTR released provisions totalling £305m in 1992 (28.1% of the reported profit of £1,085 million) and £81 million in the first half of 1993 (13.5% of the reported profit of £602 million). With its provisions largely exhausted by mid-1993, BTR's true underlying profitability became apparent. After stagnating in 1994 and 1995, profits fell sharply in 1996 as did the share price and City confidence in the company. The second half of the 1990s saw a series of disposals as the company attempted, unsuccessfully, to restore its profitability through

focussing its operations and to raise cash to repay the substantial debts incurred in its acquisitive years.

BTR's experience suggests that the underlying profitability of other conglomerates may have been declining long before they undertook strategic reviews that led to the adoption of divestment strategies and re-focussing.

3.3.3.2 Inhibitors

A previous section discussed the conditions – environmental, regulatory and management – that effectively facilitated and encouraged conglomeration. The following section discusses the erosion of those drivers and the effect on conglomerates. However, while each of the drivers of de-conglomeration has been considered individually, none of the extant literature appears to have drawn them together to provide an explanation of their combined influence on corporate strategy formulation and strategic change.

Failure to Reduce Risk

The issue of risk reduction is central to conglomeration. The quest for stability and low risk is a major aim of companies pursuing conglomeration with managements seeking to offer investors stability by creating low risk portfolios of business activities.

Levy & Sarnat (1970, p795) acknowledged prior research had identified a *"conglomerate effect"* where *"economic activities are unrelated"* and where in the *"purely conglomerate type"* profits remain static *"but only stabilized by*

bringing together centres with zero or negative correlations". The theory is logical although in practice flawed by the difficulty of identifying businesses with the required cyclicality. Bettis and Hall (1982, p257) make the point that diversification would be expected to produce negative correlations as the investments would be, by definition, unrelated, and would reduce variations in performance. However, they are dismissive of the ability of conglomerates to stabilise earnings in practice: *"Risk reduction (as defined herein) is not a valid rationale for selecting unrelated diversification instead of related diversification. This result is supported further by the recent work of Salter & Weinhold (1979), who propose that two of the common misconceptions about diversification are that a related strategy is always safer than an unrelated strategy and that adding countercyclical businesses to a company's portfolio leads to a stabilised earning stream"* (p262). Their view is summarised in the comment that unrelated firms *"do not have superior risk pooling characteristics [to other types of firm]"* (p263).

The risk reduction benefit of conglomeration is further undermined by the increased realisation by investors, especially professional and institutional, that they can create their own portfolios and can be equally as successful as their corporate counterparts in reducing unsystematic risk (Salter & Weinhold, 1979). While they would continue to face the same systematic risk – the level of risk inherent in the economy - as companies, investors can easily construct a portfolio of investments containing the same mix of business activities as a conglomerate could acquire and could probably do it more cheaply given that they would not have to pay acquisition premia. However, this is not as true for

international diversification which requires foreign investment which is less straightforward for individuals. As Dess, Gupta, Hennart & Hill (1995, p360) noted: *"An assumption of the risk return model for international diversification must therefore be that individuals are more limited in their ability to diversify than the firm. The second best solution is for individual investors to buy shares in firms which diversify for them"*.

While the risk of investor and corporate portfolios may be similar, it 'may' still be the case that conglomerates can produce superior returns from their portfolio of businesses than investors could from the same individually held portfolio. Investors, especially individuals, are, despite recent increases in investor 'power', effectively passive, i.e. they have little or no influence on the day-to-day running or strategy of 'their' companies, whereas by bringing its superior management skills to bear, an acquirer may be able to increase the profitability of a business. Furthermore, as noted by Berg (1965, p83), conglomerates may be better placed to undertake high-risk high-return projects: their financial resources are greater and they would not be *"putting all their eggs in one basket"*. BCG (2006, p13) support this view using a gambling analogy to highlight the risks to focused companies as compared to conglomerates: *"this is the dilemma of focussing: putting all your chips on one number has the potential to generate higher rewards than spreading your bets, as conglomerates do, but the potential losses are also greater if your number doesn't come up"*.

Risk-reduction through portfolio management is a sound theoretical basis for conglomeration. However, the practicalities and costs relative to investor portfolio selection, diminishes its success and attraction. However, especially for individual rather than institutional investors, conglomeration continues to offer the only practical way to risk-reduction (Williams, 2002).

Changes in Regulation

The introduction and use of competition legislation and regulatory processes to monitor and effectively limit market shares by precluding same industry acquisitions encouraged diversification and conglomeration through the 1970s and 1980s. In the US, Shleifer & Vishny (1991) lay a portion of the blame for what they refer to as the conglomerate 'mistake' at the US government's door believing that *"….aggressive governmental policy, in the case of antitrust policy, can have large unintended effects"* (p59).

Relaxation in the application of competition regulations in the late 1980s reduced the need for growth through diversification. Scoullar (1987) cites government reluctance to refer proposed transactions that would result in increased market shares in particular industries, i.e. non-diversifying transactions, to competition authorities as helping drive acquisition activity. In addition, in some industries globalisation and international expansion increased competition and reduced market shares meaning that fewer potential acquisitions would require competition authority clearance.

Fewer Opportunities

The UK and the US stock markets are amongst the most developed and efficient in the world. Brealey & Myers (1991) attribute the definition of three levels of stock market efficiency to Harry Roberts (1967): weak where prices reflect information from past prices, semi-strong where prices reflect past prices and other publicly available information and strong where prices reflect all information not only that publicly available. On this scale, the UK and the US stock markets are seen as being semi-strong with prices reflecting all known information suggesting prices are generally fair but with some opportunities to make gains.

In addition to the efficiency of the stock market, the depth and breadth of financial analysis, especially by institutional investors, has increased significantly in line with global information technology developments. With most quoted and all FTSE100 companies covered by at least one leading broker and analysed by several institutional investors there is a greatly increased likelihood that a 'bargain' will be spotted by several potential acquirers who, should they decide to try to acquire the company, will compete for control and bid up the price reducing the scope to add-value post-acquisition. Porter (1987) argues that the potential 'value-added' by acquirers has been reduced making the concept of portfolio management redundant. In the UK the decisions of some of the largest UK conglomerates to break themselves up is, in effect, a tacit admission of their failure to add-value across the range of unrelated business activities in their portfolios.

Therefore, stock market efficiency and greater information/analysis result in increased acquisition costs making acquisitions, the preferred route to increased diversification, less favourable.

Reduced Management Effectiveness

As companies grow and encompass a greater range of unrelated activities, top management inevitably becomes increasingly generic, i.e. specialists with the necessary skills and attributes are employed to manage specific business activities while generalists manage corporately. Where this does not happen, management skill shortages may result in the specific needs of individual businesses being unsatisfied leading to sub-optimal performance at both business and corporate levels. Kay (1995) suggests that many of the large demergers of the early 1990s – including Courtauld's demerger of its textiles operations, Racal's demerger of its Vodafone mobile communications activities, BAT Industries' demergers of retailer Argos and paper manufacturer Wiggins Teape Appleton and ICI's demerger of its pharmaceuticals business as Zeneca – were driven by the inability of management to effectively manage unrelated activities.

The claim that 'diversity cannot be managed' was explored by Leontiades (1989, p77) who included it in his 'Six Deadly Management Myths' suggesting that appropriate choice of management structure could overcome problems of complexity inherent in conglomerates. He also noted that focused (single business) companies were also liable to management failures, e.g. companies misguidedly remaining focused on declining industries.

The issue of management effectiveness and diversification is more complex than that of management effectiveness and size. Penrose (1959) discussed the problems associated with growth and noted the ongoing debate as to whether a company can become 'too big' as regards its ability to adjust effectively and efficiently to both the short and long-term conditions it faces. Essentially, Penrose (1959) saw these problems as being management control issues; can management continue to operate effectively as the firm grows? Penrose (1959), took the optimistic view that companies would evolve as they grew and change their organisation and management structure appropriately. However, Penrose (1959) must be considered in light of the type of companies that existed in 1959; predominantly single and dominant business companies with few diversified companies and no real multi-business conglomerates.

Marris (1998, p67) referred to Penrose (1959) and her belief that diversification was a natural (and essential) part of growth: *"It is Edith Penrose again who appears as the leading contemporary writer to emphasize the role of continuous diversification in the normal process of growth. She points out that by this means many firms have continued to grow over very long periods, such as fifty or even seventy five years, although there is, apparently, evidence of a tendency for the rate of growth themselves to decline over time. The planning of diversification is 'par excellence' a typical function of high management. Characteristically, it has been found, these decisions are taken at higher levels within the management hierarchy than are, for example, pricing decisions. We may therefore define a distinct variable to be known as*

'the rate of diversification', intended to summarize the implication of the series of individual decisions that lead up to the marketing of new products".

Undoubtedly, the development and, amongst diversified companies, widespread adoption of divisional management structures has contributed to the ability of companies to continue to diversify beyond the limitations of traditional structures.

Re-Assertion of Shareholder Power

The Market for Corporate Control (Jensen, 1986) has had great impact on the principal (shareholder)/agent (management) relationship. The increased risk of takeover - and its negative implications for the management team of an acquired company - faced by underperforming companies has led managers to rethink their strategies and to re-align their objectives with those of the shareholders who could decide to accept an offer made to acquire their company. This change has been exacerbated by an increased willingness, especially among institutional shareholders who often have informal contact with executives, to act to bring errant management into line. Faced with the possibility of losing their jobs, managers' instinct for self-preservation cannot be underestimated!

In addition, the development of corporate governance guidelines following the Cadbury, Greenbury and Hampel committees in the 1990s has reduced the potential for management to become 'entrenched' to the point where they effectively become protected from the invisible hand of the Market for

Corporate Control. This remains more of an issue in the US where many anti-takeover provisions may be introduced by directors without recourse to shareholders.

Retirement of Dominant Personalities

The influence of some business leaders, e.g. Lords Hanson and White at Hanson and Owen Green at BTR, must not be under-estimated. By no means perfect, these business leaders were undoubtedly entrepreneurial, opportunist and a major driving force behind the largely successful conglomeration strategies pursued by their companies. The retirement of long-serving dominant personalities is frequently followed by changes in corporate culture as the company tries to adjust to a different style of leadership. Whittington & Mayer (2000, p17) describe the continuity of top management resource as being the *"Achilles heel of conglomerates"*. Most have had to grapple with succession issues, some have been successful, e.g. Hanson's break-up after the retirement of Lord Hanson, while others have not, e.g. BTR struggled after the retirement of Sir Owen Green and several other long-serving directors credited with creating the company.

Similarly, there are instances in the US where a change in CEO proved the turning point for conglomerates. Leontiades (1980, p162) noted that several US conglomerates *"….like American Standard, Boise Cascade, and Whittaker which had pursued an aggressive acquisition program in the 1960s under one chief executive"* changed strategic direction and entered a period *"….of deconglomerating in the 1970s under a new chief executive"*.

Development of New Corporate Forms

The late 1980s saw the development of new types of corporate transaction which increased the threat of takeover faced by underperforming companies, especially conglomerates, which could be broken up by their new owners (Morck, Shleifer & Vishny, 1990). Shleifer & Vishny (1991, p53) point to the rapid growth through the 1980s of these *“radical new forms of control changes”* that provided a route back towards focus and specialisation. These new forms of control included leveraged buy-outs where the acquisition vehicle is overwhelmingly financed by debt and is usually privately owned, and break-up takeovers where the aim of the acquirer is to break the acquired business up into its component parts and sell them to focused buyers exploiting situations where ‘the sum of the parts exceeds that of the whole’. These innovations in corporate forms, which were made possible principally by developments in debt markets, sit alongside more traditional approaches including management buy-outs and management buy-ins.

The new corporate forms were helped not only by the availability of finance but also by the appetite amongst focused firms for the unwanted businesses being sold post-acquisition. This demand was enhanced by the less restrictive antitrust environment prevailing in the 1980s especially in the US. Kaplan (1990) cited in Shleifer & Vishny (1991) showed that broadly 50% of assets acquired in leveraged buy-out transactions were sold off to buyers in the same industry within 3 years of the original transaction achieving greater focus for both the selling and buying companies.

Shareholder Sentiment

Whilst acknowledging the importance of market fundamentals in valuation, especially of quoted public limited companies, and the absence of randomness in their share prices, it must be remembered that valuations are a function not only of economics/financials and future expectations but also of market sentiment. The first two of these variables may be estimated with a degree of certainty and analysts will usually agree, broadly at least, on their direction, positive or negative. The third, market sentiment, is more difficult to assess objectively. Market fundamentals tell only half the story of a company's valuation.

Investors - professional and amateur alike - like to have clarity; to be able to see and understand how a company has performed. Conglomerates are an anathema to many investors: their complex management, accounting and tax structures do not help foster understanding of underlying performance. A clear and deliverable strategy is what investors want to see; a difficult task for a company with diverse business activities.

The lack of clarity is exacerbated by an increasing short-termism. The principal providers of finance - banks through loans and institutions through share and rights issues - have or have been perceived to have become increasingly short-term and conservative in their outlook (Miles, 1993; Demirag, 1995; Grinyer, Russell & Collison, 1998; Marston & Craven, 1998). They seek to maximise their short-run profitability to attract investment themselves from individuals who are able to compare their performance

through investment league tables compiled by publications such as Acquisitions Monthly and Investor's Chronicle. Short-termism amongst the investment community, in turn, drives companies to favour short-term rather than long-term capital investment opportunities to improve profits. Understandably major investors want to see strong stable performance and dividend growth. However, they want this immediately not in the uncertain future and will quickly re-direct their funds away from companies they feel are underperforming and towards those offering immediate superior returns. Furthermore, the cumulative effect of numerous studies showing very high rates of failure for acquisitions, has made the providers of finance consider proposed transactions more critically.

The adverse investor sentiment towards conglomerates in the 1990s manifested itself in share prices; conglomerates were effectively 'on trial' in the late 1990s (Economist, 1997). Just as shareholders had encouraged and supported conglomeration in the 1960s and 1970s, they also encouraged and supported the return to focus. Where the shares of diversifying and conglomerate acquirers traded at premiums in the 1960s and 1970s it was the shares of focused acquirers that enjoyed similar premiums in the 1990s. There is a strong body of literature including Wernerfelt & Montgomery (1988), Lang & Stulz (1994), Berger & Ofek (1995), Servaes (1996), Bodnar, Tang & Weintrop (2003), Denis, Denis & Yost (2002) and Lins & Servaes (1999) which considered the existence and size of what has come to be known as the conglomerate discount.

3.3.3.3 Aftermath of Acquisitions

Failure of Acquisitions

The failure of conglomerates to perform could also be explained by the fact that many were created by acquisitions and that, in common with all acquisitions, few were successful. Mueller (1969) hypothesised that conglomerate merger activity was "irrational" believing that the absence of relatedness between the businesses involved would limit scope for synergy gains and that, therefore, conglomerate acquisitions were driven by the acquirer's desire to maximise growth rather than increase profits. Mueller acknowledged that an acquiring company's managers *"expected to be able to achieve managerial economies"* but believed that in reality these economies are very seldom realised. His view is supported by Roll (1986) whose Hubris theory states that bidders get carried away and pay too much for acquisitions which, burdened by a high purchase price, fail to achieve their projected returns. Furthermore, research by Kaplan & Weisbach (1992) into divestments found that the likelihood of acquisition failure was greatest for conglomerates as *"diversifying acquisitions are four times more likely to be divested than related acquisitions"* (p107). This is consistent with Porter's (1987) research into the acquisition and diversification activity of 33 of the largest US corporations, including several conglomerates, between 1950 and 1986 which found that: *"…most of them had divested many more acquisitions than they had kept"* (p43) with 53% of acquisitions that brought the acquiring companies into new industries later divested. Porter's research is consistent with that of Ravenscraft & Scherer (1987) who found a divestment rate of 33% relating to acquisitions made in the 1960s and 1970s by US companies.

Whitley (1994, p169) offers support to Mueller (1969) noting that diversified companies are often characterised by the independent and 'isolated' nature of their operations which typically run on a stand alone basis limiting scope for synergies. He goes on to say that this does not concern some conglomerates and (p171) draws attention to the propensity of conglomerates to minimise integration and interdependence of their diverse businesses to allow them to more easily manage on a 'portfolio' basis, i.e. acquiring and divesting businesses to maintain financial performance and meet the increasingly short-term demands of providers of finance.

Shelton (1988) also finds conglomerate acquisitions to be less successful than those involving related activities. Analysing 218 mergers by randomly selected acquirers between 1962 and 1983 and assessing their success using a 'strategic fit system', she found acquisitions *"that permit expansion into new markets (related-supplementary) or within the same business (identical) create the most value"* (p284).

Finally, according to Amburgey & Dacin (1994, p1447), *“the unrelated diversification inherent in a conglomerate merger is likely to produce greater problems with assimilation than the related diversification involved in product extension mergers”*. In their research into structural change they found the impact on structure of conglomerate acquisitions with their inherent complexity to be 3 times greater than that of acquisitions of related activities.

Through the growth years, conglomeration was achieved primarily through acquisitions. Similarly, in the decline years the reversal of conglomeration was achieved through divestments including trade sales, floatations, management buy-outs/buy-ins and leveraged buy-outs. The return to greater focus was the result of several factors including:

- Concentration on a 'core' activity; focussing management and resources to maximum effect.
- Business trends; identifying growing problems within specific businesses leading to their divestment.
- Failure to achieve 'critical mass' in specific markets and/or industries.
- Poor performance, e.g. profitability, share price.
- Pressure from investors, especially institutional for leading quoted companies.
- Capital rationing; investment opportunities exceeding available funds leading to divestment to restore balance.
- Pressure from debt financiers whose reluctance to increase facilities means not all activities can be supported leading to divestments.

Research by Kaplan & Weisbach (1992) into divestments by US companies found a variety of reasons were cited by divesters as the following table shows:

Table 18: Reasons for Divestitures

Reason	No. of Divestitures
Change of focus or corporate strategy	43
Unit unprofitable or mistake	22
Sale to finance acquisition or leveraged restructuring	29
Antitrust	2
Need cash	3
To defend against takeover	1
Good price	3
Divestitures with Reasons	103

Source: Kaplan & Weisbach (1992, p114)

In reviewing Kaplan & Weisbach's (1992) findings it must be remembered that pride may unduly influence the reason for divestment given by company: nobody likes to admit they made a mistake! Therefore, at 22 (21%) the number of divestitures following mistakes may be understated. The most frequently cited reason with 43 (42%) instances was the desire to change focus or corporate strategy which is consistent with acquisitions/divestments being used to create and destroy conglomerates.

Weston (1989) provides some support for this contention finding many divestments to be of earlier acquisitions and that rather than categorise an acquisition as a mistake there is a tendency to claim circumstances had changed. 'Mistake driven divestment' was considered by Allen, Lummer, McConnell & Reed (1995) as part of research into the reasons why many spin-offs generate gains for shareholders. In their paper, Allen, Lummer, McConnell & Reed (1995) researched spin-offs that were originally acquisitions for the selling company to see if the original acquisition was, measured by return, over-priced and reduced shareholder value, i.e. was a

mistake. They found evidence supporting the contention that *"wealth gains from corporate spin-offs result from the correction of a prior mistake"* (p465).

Sudarsanam (1995) discusses the increase in divestment activity amongst UK companies in the late 1980s/early 1990s using data from Acquisitions Monthly. By extending the data series through to its discontinuation in 1998 it can be seen that divestments peaked in 1989 and 1998 at 665 and 798 transactions respectively with the intervening years averaging around 500. Similarly, acquisitions peaked in 1988 and 1998 at 1,633 and 1,480 transactions respectively having fallen to only 684 in 1992. However, by 1998 acquisitions were only 91% of their 1988 peak having, at their lowest point, been only 42% whereas divestments were 120% of their 1989 peak, their low point having been 66% of their 1989 peak. The increase, albeit gradual until 1998s large rise, provides some support for the contention that from 1991 onward more companies were divesting activities than in earlier periods.

Table 19: Acquisitions and Divestments in the UK, 1987-98

Year	Acquisitions		Divestments		Total	
	No.	£m	No.	£m	No.	£m
1987	1,469	20,488	468	7,210	1,937	27,698
1988	1,633	24,369	608	13,254	2,241	37,623
1989	1,363	35,318	665	10,206	2,028	45,524
1990	912	17,457	612	10,221	1,524	27,678
1991	747	12,180	442	6,001	1,189	18,181
1992	684	14,428	468	5,319	1,152	19,747
1993	745	8,720	503	8,640	1,248	17,360
1994	1,017	17,842	538	7,430	1,555	25,272
1995	1,124	54,336	570	13,412	1,694	67,748
1996	1,175	43,098	545	13,234	1,720	56,332
1997	1,240	51,215	561	12,862	1,801	64,077
1998	1,480	71,914	798	18,193	2,278	90,107

Note: Acquisitions include both private and public company targets.

Source: Acquisitions Monthly Annuals

The following table, compiled using data from the Office of National Statistics, shows acquisition and disposal activity of UK companies between 1983 and 2003. The data provides support for the trends through to 1998 that were apparent in the Acquisitions Monthly data and also shows that non-UK acquisitions and disposals activity has increased adding weight to the increasing international dimension to UK business.

Table 20: UK and Non-UK Acquisitions and Disposals by UK Companies, 1983-2003

	Acquisitions				Disposals				Ratio	
	UK	Non-UK		Total	UK	Non-UK		Total	Acq'n-Disposals	
Year	No.	No.	%	No.	No.	No.	%	No.	UK	Non-UK
1983	447				142					
1984	568				170					
1985	474				134					
1986	842				221					
1987	1,528	431	22.0	1,959	340	118	25.8	458	4.5	3.7
1988	1,499	648	30.2	2,147	376	112	23.0	488	4.0	5.8
1989	1,337	681	33.7	2,018	441	134	23.3	575	3.0	5.1
1990	779	586	42.9	1,365	342	134	28.2	476	2.3	4.4
1991	506	550	52.1	1,056	214	157	42.3	371	2.4	3.5
1992	432	679	61.1	1,111	200	219	52.3	419	2.2	3.1
1993	526	521	49.8	1,047	189	221	53.9	410	2.8	2.4
1994	674	422	38.5	1,096	209	149	41.6	358	3.2	2.8
1995	505	365	42.0	870	206	117	36.2	323	2.5	3.1
1996	584	442	43.1	1,026	248	178	41.8	426	2.4	2.5
1997	506	464	47.8	970	122	176	59.1	298	4.1	2.6
1998	635	569	47.3	1,204	150	218	59.2	368	4.2	2.6
1999	493	590	54.5	1,083	93	198	68.0	291	5.3	3.0
2000	587	557	48.7	1,144	121	168	58.1	289	4.9	3.3
2001	492	371	43.0	863	173	139	44.6	312	2.8	2.7
2002	430	262	37.9	692	107	128	54.5	235	4.0	2.0
2003	558	243	30.3	801	166	136	45.0	302	3.4	1.8

Source: Office of National Statistics, Various Tables.

Unfortunately, the ONS data is not broken down according to the acquirer's size, type – public or private – or diversification category and therefore the trends identified may only be considered in the broadest sense. The percentage of acquisitions of non-UK companies increased from an average of around 30% at the end of the 1980s to almost 50% through the 1990s. This suggests that UK companies were expanding geographically through the

1990s which may have been a response to regulatory limitations on UK growth. However, the table also shows that the percentage of non-UK disposals increased through the 1990s suggesting high rates of failure for cross-border acquisitions. The relative success of UK acquisitions is also implied in the ratio of acquisitions to disposals which, with a few exceptions, is consistently higher for UK than non-UK activity.

Search for Focus and Stability

Bergh & Lawless (1998) considered the effects of environmental uncertainty on portfolio restructuring and movements towards diversification or focus and found that, in addition to seeking performance improvements, some portfolio restructuring in the 1980s may have been driven by changes in the level of environmental uncertainty. They showed that diversification was related negatively to restructuring measures (companies were divesting) although the reverse was true for less diversified companies. This suggests managers of highly diversified companies cope less well with environmental uncertainty and seek focus and simplification while less diversified companies see uncertainty as offering opportunities. This finding has implications for optimal levels of diversification and possibly for control systems employed within companies.

At the optimal level of diversification, management would maximise efficiency as well as the transfer and exploitation of core competences with a positive effect on competitive advantage (Prahalad & Hamel, 1990, p81). Research by Hoskisson & Johnson (1992) into the effects of corporate restructuring on

diversification found that there was a link with restructuring being associated with a decrease in diversity, as measured by the entropy index, as companies moved toward greater focus.

The change in the median level of diversification among Fortune 500 firms between 1980 and 1990 in the following table illustrates the shift away from conglomerate strategies. Unrelated diversification, as measured by the entropy index (max value 1), fell marginally from 0.63 to 0.59 between 1980 and 1985 before falling substantially to 0.35 by 1990 providing strong evidence of a move toward focus among the largest public companies in the US.

Table 21: Median Level of Diversification among Fortune 500 Firms in 1980, 1985 & 1990

	1980	1985	1990
Total Diversification (4-digit SIC Segment)	1.00	0.90	0.67
Unrelated Diversification (2-digit SIC Segment)	0.63	0.59	0.35
No. of Firms	468	453	448

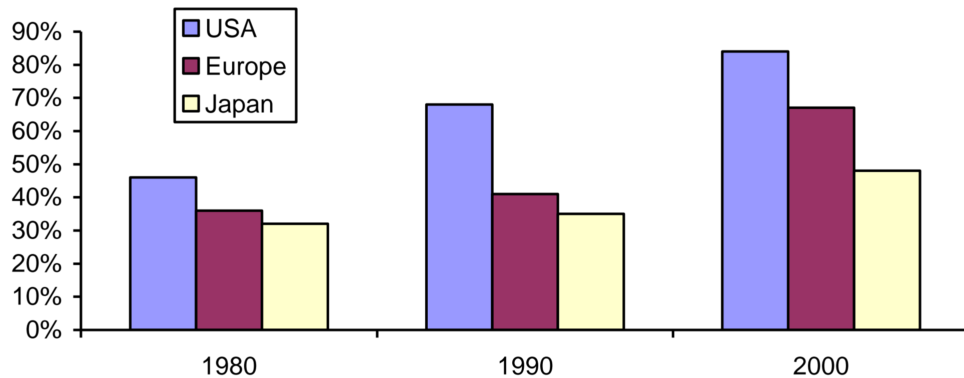
Note: Level of total diversification is calculated using the entropy measure.

Source: Davis, Diekmann & Tinsley (1994, p561)

The trend away from conglomeration in the US is also evident in the fate of Rumelt's (1974) conglomerates. According to Davis, Diekmann & Tinsley (1994, p562), *"…of the 10 firms for which data were available in 1980, three (Bangor Punto, Colt Industries and Lear Siegler) were bought out, and one (Brunswick) fended off a hostile takeover bid. Of the 7 firms still operating independently in 1990 (Brunswick, FMC, General Host, W.R. Grace, LTV, Litton Industries and Whittaker) all but one (FMC) were less diversified"*. Furthermore, research by Franko (2004) shows the rise of the focused

company to be greatest in the US between 1980 and 1990 with another increase between 1990 and 2000. As regards conglomerates, Franko (2004) showed that the percentage of conglomerates among the same group of large companies (177 companies in 15 industries in 1980 and 201 companies in 17 industries in 1990 and 2000) remained broadly constant between 1980 (34%) and 1990 (37%) but fell to only 5% by 2000.

Chart 6: The Rise of Focused Firms, 1980-2000



Source: Franko (2004)

Across a wider spectrum of US companies, the trend away from conglomeration is less clear. Starting with a 1984 sample of 2,356 US companies and tracking changes amongst survivors, i.e. not adding new entrants, Denis, Denis & Yost (2002) showed a movement towards focus amongst US firms over the period 1984 to 1997 but the changes they identified in the incidence of related diversified and conglomerate companies (26.3% to 25.6%), the average number of segments reported (3.176 to 2.759) and the increase in the average turnover-based Herfindahl index (0.486 to 0.543) were not significant. However, when the sample of companies includes new entrants, the trend toward focus is more pronounced with the changes

statistically significant. Denis, Denis & Yost (2002) also found that the increase in focus had a positive effect on the level of diversification discount reflected in market values of companies which fell from an average of 25% in 1984-1988 to 19% in 1989-1993 and to only 17% in 1994-1997 suggesting the markets welcomed the reduction in diversification and conglomeration.

Comment & Jarrell (1995, p67-68) summarised the prevailing opinion of conglomerates in the later part of the 1980s saying that, *"Conventional wisdom holds that economics of scope have been reversed in the 1980s. Managers are now advised to eschew diversification and to shrink the far flung enterprise that resulted from past diversification strategies"*. Furthermore, Comment & Jarrell (1995, p68) provide support for their contention by showing that *"55.7% of exchange-listed firms had a single business segment in 1988 compared to 38.1% in 1979"* and that *"a change of 0.1 in the absolute value of a revenue-based Herfindahl index of focus is associated with a stock return of about 4%"*.

The most recent research is that undertaken by the Boston Consulting Group (2006) into the effects of focus on conglomerates. A major finding of this research, which centred on the US, Asia and Europe (although no UK conglomerates were included) was that; *"only in Europe are conglomerates under pressure to focus. Interestingly, their fundamental performance is also significantly weaker than that of their peers in the United States and Asia, indicating that the core issue is not their degree of diversification but how they manage their business diversity"* (p11). The BCG report continues to say that

although Relative Total Shareholder Return (RTSR) of diversified companies at 1.34% is lower than that of focussed companies at 2.19% it exceeds the 0.97% achieved by 'slightly diversified' companies suggesting there is no 'halfway house' for focusing. BCG also note there were large variations in performance across the diversified companies supporting their contention that an efficiently run conglomerate performs as well as a focused company. Acknowledging a trend towards focus, BCG (2006) failed to be convinced of the benefits of divestment and refocusing finding that such strategies were often ill-conceived, poorly executed and diminished shareholder value; *"There is no evidence that diversified companies would necessarily produce higher returns if they focused on a smaller number of businesses. In some cases, notably break-ups, there is a strong probability that focussing will destroy shareholder value (p7)"*.

Divestment & Performance

Recognising that many companies had embarked on the reversal of their conglomerate strategies, Markides (1993, 1995) raised the possibility of companies having an optimal diversification level, i.e. an optimal degree of conglomeration. Markides (1993, 1995) contends that returns will increase as diversification is pursued but the law of diminishing returns will apply and once the optimal point of diversification is exceeded returns will begin to fall and at an increasing rate with each additional degree of diversification. However, Markides (1995, p173) acknowledges that each firm will have a unique optimal point and that its calculation is effectively impossible given the large number of variables involved, *"identifying a firm's exact optimal diversification*

level is an impossible task – the optimal diversification limit for a firm is really a theoretical concept, much like the utility concept in economics, and it cannot be measured precisely". Markides (1993, 1995) suggests that by refocusing, companies that had 'over-diversified' will increase management efficiency and performance.

Markides (1993, 1995) approach is consistent with that of Montgomery & Wernerfelt (1988, p631) who saw companies: "*….as having a queue of potential diversification opportunities. We argue that a firm, in electing to diversify, will begin with the most profitable opportunities and move toward the least profitable ones. Our expectation is that this process will end when marginal rents become subnormal"'*. Harper & Viguerie (2002) take a similar view suggesting that moderate diversification provides the 'best of both worlds' where a company is able to grow through diversification and avoid over-reliance on one industry but does not spread itself and its management team too thinly.

Similarly, in UK research Grant & Thomas (1988) have shown that there is a relationship between diversification and profitability that is quadratic, i.e. an inverted "U" shape that implies that beyond a certain level of diversification the costs of managing the inevitably complex organisation exceed the benefits of diversity and returns decrease. The 'Holy Grail' of companies is dynamic portfolio management that achieves and, through acquisition and divestment, maintains the optimum degree of diversification for their company in a constantly changing business environment. Harper & Viguerie (2002, p35)

believe that managers should *“continually and proactively monitor and match their current and emerging internal capabilities with external discontinuities – changes in technology, regulation, and consumer behaviour – that may create opportunities in related industries or require management skills they already have”*.

Sudarsanam (1995) believes that the desire of many divesters to get '*back to the core*' is *"a rebound from the poor performance of conglomeration which happened on a large scale in the 1960s and 1970s"* (p245). The evidence suggests that when companies break-up, the post-split value of the new companies is greater than that of the original single company. Sudarsanam suggests that one of the reasons for this is the increase in information available to the stock market; the stock market *"places a premium on corporate transparency"* (p248) and diversified companies could have "*suffered a conglomerate discount*" (p248) because of the lack of transparency. More fundamentally, Jensen (1982) questioned the rationale behind the takeover wave that led to the diversification of US companies.

Markets understand focused firms better than complex conglomerate groups and the knowledge imbalance is reflected in a conglomerate discount. Graham, Lemmon & Wolf (2002) take a different view of the diversification discount showing that a fall in value following a diversifying transaction may not be the result of an increase in diversification but the acquirer’s assumption of the discounted value of the company acquired. Graham, Lemmon & Wolf (2002) do acknowledge a key weakness of their research; that diversified

companies have a tendency to be serial acquirers and, possibly, diversifiers and therefore 'clean' periods without either acquisitions or divestments are rare making analysis difficult.

There is a growing body of evidence suggesting that by breaking up, companies gain greater analyst coverage which leads to increased value for the newly spun-off company and the former parent. Gilson, Healy, Noe & Palepu (2001) considered *"103 focus-enhancing spin-offs, equity carve-outs, and targeted stock offerings between 1990 and 1995"* and found a *"30-50% increase in analyst forecast accuracy for parent and subsidiary firms"* (p565). The same authors also report that companies show an increase in financial performance after break-ups: *"The post-break-up firms have combined median sales and net income that are higher than the pre-break-up conglomerate. Moreover, the median accounting return on equity (ROE) for the pre-break-up firm in fiscal year -1 is 10%. After the break-up, median ROEs are 12-13% for the parent firms and 10-12% for the subsidiaries. A similar pattern is observed for accounting return on assets (ROA), indicating that the ROE improvements are not due to a change in leverage for the parent and/or subsidiary firms after the break-up"* (p571-572).

But what about the financial performance of groups that reduced in size? Shleifer & Vishny (1991) found a major driver of portfolio restructuring in the 1980s was a desire to refocus to improve control, efficiency and, as a consequence, performance. Furthermore, Morck, Shleifer & Vishny (1990, p47) found evidence that, *"….in the 1980s the stock market punishes*

unrelated diversification" and *"….the source of gains in the 1980s is the reversal of the unrelated diversification of the 1960s and 1970s"*.

Kose & Ofek (1995) researched post-divestment performance and found improvements following divestments that increased focus. There are several potential explanations for this including the elimination of negative synergies, i.e. the parent suffers financially by owning the business to be divested, and better post-divestment allocation of management/financial resources. Comment & Jarrell (1995) also produced similar findings; *"greater corporate focus is consistent with shareholder wealth maximization"*. In their paper they found there was a failure of *"diversified firms to exploit financial economies of scale"* and that they were *"less likely to be subject to hostile takeover"* (p67).

Miller (1977) hypothesised that spin-offs increased shareholder wealth because there was a difference in valuation between existing shareholders and potential investors. This "Divergence of Opinion" hypothesis was tested by Kudla & McInish (1988) who researched a data set of 39 parent and spin-off cases and finding there was: *"a significant increase in the post- versus pre-spin-off dollar value of trading, which is consistent with the hypothesis that divergence of opinion concerning the value of the parent and spun-off firms is a determinant of excess returns from spin-offs, confirming the results of previous researchers"* (p28).

Bhide (1990) also considered the reversal of conglomerate acquisitions in the US. His paper argued that the key drivers for conglomerate diversification

were common ownership and internal capital markets and suggested that: *"…over time the disadvantages have come to outweigh the advantages; and thus the reported shareholder gains from "bust-ups" are not simply "paper" gains, as critics of takeovers claim, but are likely to reflect real changes in operating efficiency"* (p70). For example, in theory internal capital markets allow first mover advantage, avoid investment in marginal projects, allow problems to be solved without undue external pressure, allow managerial assistance and better cash management. However, Bhide (1990) believed there are significant disadvantages including slow reaction times, high corporate overheads, political decision-making and mis-aligned incentives including stock option schemes. Bhide (1990) also believed conglomerates were living on borrowed time with increasingly sophisticated deregulated capital markets applying greater pressure for improved performance and enhanced disclosure requirements increasing the transparency of company reporting and limiting scope for manipulation of reported results. Furthermore, investor power grew in the 1980s as the percentage of shares owned by institutions increased and investors became increasingly vocal and critical of those management teams they perceived to be failing to protect their (the owners') interests. Bhide (1990) concludes his paper by saying, unsurprisingly, that although not all conglomerates are poor performers, many really have outlived their usefulness and that while some divestments may have been 'overpriced', the process of break-up usually adds to overall value.

The relationship between the degree of corporate focus and the incidence of spin-offs also produces interesting results. Daley, Mehrotra & Sivakumar

(1997) studied 85 spin-offs between 1975 and 1991 looking at corporate focus issues by considering parent and spun off company SIC codes. They found *"a significant improvement in operating performance for cross-industry spinoffs, and none for own-industry deals"* (p257). Their summary finding was that spin-offs only create value when they result in an increase in corporate focus which, they theorised, removes unrelated businesses allowing managers to concentrate their efforts on core businesses. They saw complexity as reducing management efficiency and, as a result, performance.

As part of the control environment, managers need to assess and re-assess their strategy with the aim of profit maximisation. Faced with a dynamic business environment and conscious of the existence of the market for corporate control, managers should always be looking to ensure they cannot divest businesses and, as a result, add to shareholder wealth. According to Linn & Rozeff (1982, p594): *"a value enhancing corporate policy, therefore, calls for continual review of the assets of the firm, assessing both the internal effects of a unit's continued presence and the external market for these assets"*. An important driver in retention/divestment decisions is synergies, which can have a positive or negative value. Positive synergies occur where the post-acquisition value of a company is higher than the sum of the values of its constituents, i.e. they work better together than separately. Negative synergies occur where the reverse is true, i.e. the company is inefficient and would have a greater value if separated into two or more independent companies. Linn & Rozeff (1982) suggest managers should consider selling only if a price above the internal value and future cash flows can be achieved,

i.e. if the business is worth more to another business. In cases where profitability is poor with little likelihood of improvement, piecemeal liquidation should also be considered. Research by Hite & Owers (1983) has suggested that some companies are effectively worth more "dead than alive".

Hite & Owers (1983) considered various explanations for spin-offs concluding that those undertaken to *"facilitate mergers or to separate diverse operating units"* (p409) produced positive abnormal returns with the latter achieving the highest. Schipper & Smith (1982) concluded that there was *"a statistically significant positive average share price reaction"* (p463) for a sample of 93 voluntary spin-off announcements on the American and New York Stock Exchanges between 1963 and 1981 with gains coming primarily from reductions in complexity. Jain (1985) shows that following voluntary sell-off announcements, both sellers' and buyers' share prices react favourably, the greatest excess returns being enjoyed by the sellers' shareholders, a statistically significant 0.70% compared to the buyers' statistically significant 0.34%. Jain (1985) also noted that very few divestments were achieved through an auction process; in most instances there was only a single buyer. In the absence of an auction, is the price always right?

The questionable financial performance of conglomerates put pressure on their managements to re-assess their corporate strategies and focus their activities. Research by Levy & Sarnat (1970), Rumelt (1974) and Mason and Goudzwaard (1976) showed the financial failings of the conglomerate model while further research by Porter (1987) and Ravenscraft and Scherer (1987)

showed the high failure rate of unrelated acquisitions adding to the suggestion that conglomerates were failing. However, Porter (1987) and Ravenscraft & Scherer (1987) suggest that some of the break-up gains reflect the desire of other company managers to add to their 'empires' at prices that may not be profit maximising providing gains to the divesting company. The hubris of acquiring managers works in favour of the divesting company. Although no supporting evidence has been found, there is the possibility that a diversity reducing divestment by a conglomerate could lead to the acquiring company itself becoming a conglomerate.

There has been some recent research into the area of divestment strategy. The London office of Deloitte and Touche (2002) produced a report based on a survey they undertook on global demergers. They reviewed 1,653 demergers (spin-off and split-off) completed/declared unconditional between January 1990 and December 1999. They narrowed their sample to deals with a value above $2 billion (118 transactions). Overall D&T found that pre-announcement there is a 2-10% drop in share price with *"lack of understanding of demergers, the loss of scale and scale benefits and the fear that assets are being sold cheap"* (p3) being the major causes. They also noted that investors worry about how the divestment proceeds will be invested. However, within 1 year of demerger parents' share prices increase between 12.5% (median) to 52% (upper quartile) and divested business share prices rise more than 46% (upper quartile) but there are two distinct sub-groups; successful and others. Break-ups and spin-offs have been researched by several others - Schipper & Smith (1983), Kudla & McInish

(1988), Krishnaswami & Subramaniam (1999) – who have found that information asymmetry and voluntary actions increase shareholder returns from the transactions.

Research into the post-divestment performance of divesting companies shows performance and value improvements where the transaction has increased focus thereby providing an economic rationale for divestment. However, the source of those gains is uncertain although greater transparency and increased management and corporate efficiency are recurring themes of the literature.

Portfolio Management

Some conglomerates take a very 'enlightened' view of their portfolio of businesses, constantly reviewing the rationale supporting each activity's retention whereas others seem reluctant to 'let go' of any. Goold & Luchs (1993, p22) succinctly summarised the approach management should take in deciding on diversification, *"…diversity can only be worthwhile if corporate management adds value in some way and the test of a corporate strategy must be that the businesses in the portfolio are worth more under the management of the company in question than they would be under any other ownership"*.

Rajan, Servaes & Zingales (2000) considered the efficiency of resource allocation amongst diversified US companies between 1980 and 1993; can divestment improve resource allocation? They found that as

complexity/diversity increased the efficiency of resource allocations deteriorated; as divestment increased requests for resources rose and the efficiency of the allocation process fell. Divestment simplified the process and improved the allocation of resources and performance. Overall, this suggests managers need to review their portfolios with a degree of ruthlessness which may often be lacking.

In many ways, BTR and Hanson were different in their attitudes towards managing their portfolios. BTR very rarely divested unwanted parts of acquisitions preferring to try and make them work despite their adding to group complexity. As a consequence, BTR ended up with businesses as diverse as heavy engineering and women's hosiery. The alternative approach was typified by Hanson which was well known for selling off businesses within an acquisition that did not fit its strategy. Lublin (1989), in an article discussing Hanson's 1989 acquisition of Consolidated Gold Fields, noted that between 1973 and April 1989 *"Hanson's US arm spent more than $3.6 billion on acquisitions and recouped nearly $2.7 billion, according to analysis by London brokers Hoare Govett"*. He further noted that *"Hanson paid $930 million for SCM, Smith Corona's parent; so far, it has reaped more than $1.5 billion from SCM asset sales"*.

Porter (1987) saw Hanson as exemplifying a 'restructuring' company; an acquirer that looks for businesses with unrealised potential and, post-acquisition:

- Frequently changes management,
- Changes strategy,
- Adds new technology,
- Builds critical mass,
- Divests unneeded/unconnected parts.

The restructured unit is sold off as soon as recovery is evidenced by financial performance. Porter believes BTR could also be placed in this category but the evidence seems to suggest otherwise; BTR held on to units long after their recovery plans had been completed and their successful turnaround reflected in profitability. As Porter (1987, p52-53) says, *"companies find it very hard to dispose of business units once they are restructured and performing well. Human nature fights economic reality"*. Companies that fail to dispose of businesses after turnaround effectively become portfolio managers, a strategy found to be flawed.

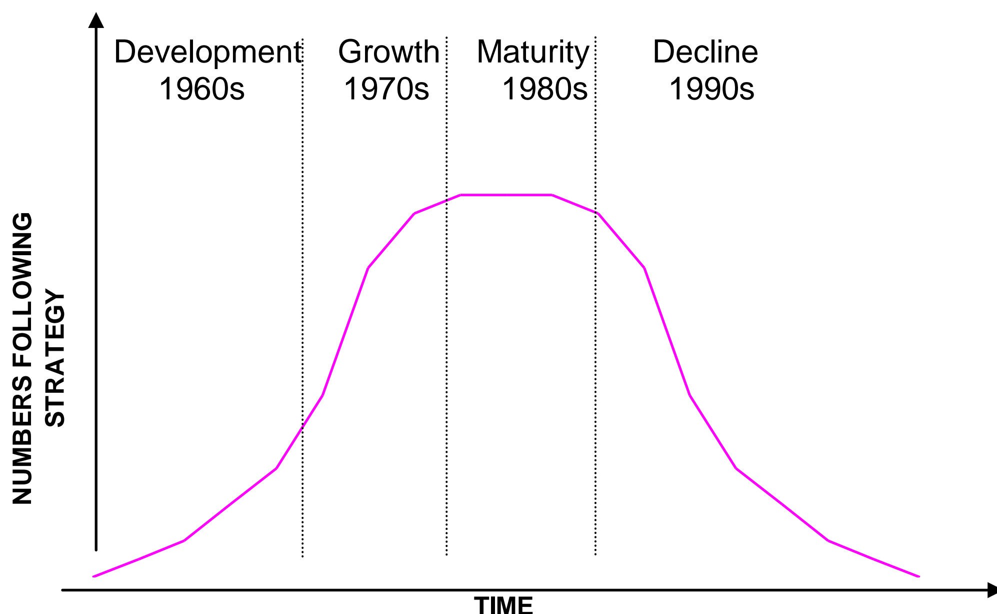
However, turnarounds are not always successful and failure is often followed by divestment. In 1988 British Aerospace, an aviation and technology company, bought Rover Group, a volume car manufacturer, from the British Government. Notwithstanding the Conservative government's desire to dispose of Rover which had been in public ownership since the mid-1970s, the acquisition was intended to give BAe a more diversified portfolio of businesses and an opportunity to use its management skills to turn a

company long seen as in terminal decline into a successful business. Unfortunately, the problems at Rover proved insurmountable for a management team skilled in ‘high-tech’ aerospace and defence businesses but with little/no experience of running high volume, low technology manufacturing operations. BAe divested Rover in 1994 to BMW of Germany, a focussed automotive group looking to broaden its product range to include lower priced vehicles and 4x4s. In 2001, BMW, despite devoting substantial financial and management resources to Rover, also admitted defeat and divested the business selling it to a consortium including former directors for only £10. Ultimately, Rover went into receivership in 2005.

Conglomerate ‘Life Cycle’

The following chart illustrates the life cycle of the strategy of conglomeration in the UK. The comparable chart for the US would shift towards the left, each phase approximately 10-15 years ahead of the UK. Other countries’ charts would be closer to that of the UK.

Chart 7: Life Cycle of Conglomerate Corporate Strategy



The chart, based broadly on extant on UK research, ascribes approximate periods for each of the generic phases; development through the 1960s, growth through the 1970s, maturity in the 1980s and decline in the 1990s. The chart outlines the life cycle of the strategy itself rather than of companies adopting it. Looking at strategic change at specific companies may reveal significant differences in the length of time conglomeration is pursued; some conglomerates, like Williams Holdings, may be short-lived ‘shooting stars’ while others, notably Bass/Intercontinental Hotels, Tomkins and Unilever, prove to be long-term adherents of the strategy.

The frequency of strategic change may prove to be considerable if the continual membership of the FTSE100 index since its introduction in 1984 is a good indicator of the extent of corporate change. As the following table shows, only 23 of the original 100 members survived the first 20 years of the index with major household names including Midland Bank, Dunlop Holdings and Distillers disappearing through acquisition.

Table 22: FTSE100 Survivors, 1984-2004

Company
Barclays
BOC Group[1]
Boots Group[2]
BP
Cadbury Schweppes
Aviva (Commercial Union Assurance)
GUS[3]
Imperial Chemical Industries[4]
Hilton Group[5]
Land Securities Group
Legal & General Group
Lloyds TSB
Marks & Spencer Group
Pearson
Prudential
Reckitt Benckiser (Reckitt & Colman)
Reed Elsevier (Reed International)
Rio Tinto (Rio Tinto-Zinc Corporation)
Royal Bank of Scotland
J Sainsbury
Shell
Tesco
Unilever

Notes
[1] BOC Group acquired by Linde AG of Germany in 2005
[2] Boots merged with AllianceUnichem in 2006 forming AllianceBoots which was taken private in 2007 by a consortium funded by KKR.
[3] In 2006 the group was split into Experian, a credit ratings agency, and Home Retail Group which comprised the Argos catalogue and Homebase DIY retail activities. Both post-split companies were in the FTSE100.
[4] Imperial Chemical Industries acquired by Akzo Nobel of Netherlands in 2007.
[5] Hilton Group (renamed Ladbroke) fell from index following the disposal of its hotel businesses in 2006.

Source: Klinger, Bolger & Waller (2004)

The rise in the adoption of conglomerate strategies through to the 1980s may be explained by several external and internal factors which created a favourable environment. Similarly, the decline in conglomeration may be explained by the reversal of several of those previously favourable factors creating an environment that was hostile to the conglomerate causing many to reverse their diversification and seek greater focus. It is difficult to explain why

the environment changed; there were no specific economic or political events or 'shocks' rather markets and investors developed and became more demanding while company managements failed to adequately control the complex organisations they had created.

While UK conglomeration entered the decline phase in the 1990s, US realisation that conglomeration was failing occurred earlier as noted by Peters & Waterman (1982, p294-296) who summarised US research into conglomerates: *"…virtually every academic study had concluded that unchannelled diversification is a losing proposition…..it seems worthwhile to illustrate rather exhaustively the almost total absence of any rigorous support for very diversified business combinations"*.

The core theory that conglomeration leads to reduced risk, greater earnings stability, improved growth and the leveraging of core competences remains valid but its practical application has been called into question. Despite the widespread introduction of M-Form structures managements have proved ill-equipped to effectively control the conglomerate groups they created largely by acquisition. This suggests that conglomeration, in the form it took in the 20th century, is a strategy that has 'had its day' and is unlikely to return to prominence or enjoy success in the future.

However, there may be a further evolutionary step beyond the traditional conglomerate that may further extend the Model of Corporate Development. Some writers have tried to link the evolutionary theories of Charles Darwin to

economic and business development and the broad Darwinian concept of the 'survival of the fittest' may be applicable, albeit simplistically, to different corporate strategies and conglomeration in particular. However, one important difference remains: Darwinian evolution in nature is determined by the environment while in business it is not only the environment but also the collective decisions of management that shapes companies. This needs to be considered in light of the changes in corporate governance seen over the last 10-15 years in the UK which has resulted in greater control over executives being exercised by non-executive directors and by more active shareholders. Clearly, companies continue to be shaped by their directors but the new corporate governance regimes restrict their largesse and ability to pursue conglomerate strategies. These issues are explored by looking for links between board composition and strategy.

3.3.4 Corporate Governance

The impact of corporate governance on conglomeration cannot be ignored. Whittington & Mayer (2000, p60) commented that *"the life-cycle of a conglomerate is effectively defined by the life-span of its original top management team"* suggesting a conglomerate was unlikely to outlive the management team that created it. Similarly, Johnson (1996) considered the period 1983-1996 finding that changes in corporate governance preceded refocusing activities.

The experiences of Hanson and BTR in the 1990s seem to bear this out as at both conglomerates changes in strategy coincided with a change in chairman

and/or chief executive; at BTR, Sir Owen Green retired as chairman in 1994 while at Hanson, Lord Hanson's retirement followed Lord White's death. This raises the question of just how powerful and influential individuals are in the pursuit and maintenance of conglomeration?

3.3.4.1 Executive & Board Composition

Since the 1990s there have been significant improvements in corporate governance at UK companies. These changes were largely in response to a series of high-profile corporate failures, including those of the Maxwell Group, BCCI and Polly Peck, and to a growing unease regarding the lack of accountability at some public companies and the size of directors' remuneration, especially bonuses and severance payments. In the US, enhancements to corporate governance and changes in incentive schemes that improve executive accountability are viewed as contributing to the trend to greater corporate focus. Citing US research by Hadlock & Lumer (1997), Whittington & Mayer (2000, p65) note that, *"[in the US] managerial selfishness and foolishness have come under control with changes in terms of corporate governance and managerial initiatives*".

The changes included requirements to increase, ideally to a majority, the number of non-executive directors, splitting the roles of chairman and chief executive officer or equivalent (a dual rather than a unitary approach), stopping the promotion of CEO to chairman, establishing various non-executive dominated committees to appoint directors, set remuneration and

deal with audit issues and, latterly, introducing independent non-executive directors.

These improved checks and balances were encapsulated in a Combined Code on Corporate Governance issued by the London Stock Exchange in June 1998. The guidelines relating to the composition of boards of directors and the positions/status of chairmen and chief executives were established by a committee which sat under the chairmanship of Lord Cadbury and reported in 1992. Subsequent committees under Lord Greenbury and Sir Richard Hampel, reported in 1995 on remuneration and in 1997 on internal controls respectively. This research has found instances of companies setting aside some guidelines. High profile examples include supermarket Morrison which, until very recently, did not have any non-executive directors, bank Barclays which allowed its retiring CEO, Matt Barrett, to become chairman and, in 2008, retailer Marks & Spencer (ironically once chaired by Lord Greenbury while also holding the position of chief executive) which, on the retirement of its chairman, made CEO Stuart Rose chairman and CEO against the wishes of several of its institutional shareholders.

Given the undoubted influence of chairmen and/or chief executive officers and the suggestion that their tenure may be linked to the continued pursuit of certain strategies, notably conglomeration, research into their length of tenure may highlight differences between categories of company. Similarly, research into changes in executive/non-executive board membership may be related to

strategy and to the level of influence wielded by the chairman and/or chief executive.

There is a limit to the depth of research into these issues that is possible without access to internal sources of information, e.g. board minutes, management operating procedures, structure charts and responsibilities, etc. Similarly, without access to personnel records, education and employment histories it is not possible to assess competence. Furthermore, even where internal information is made available, there is no way of fully understanding the true power relationships within a company without direct access to the individuals involved.

3.3.4.2 Shareholder Influence

The level of management shareholding may also have been an influence on strategy. Goranova, Alessandri, Brandes & Dharwadhar (2007) say managers/directors have historically looked to ensure the stability of their career/employment. Their research suggests there is a negative relationship between changes in management ownership, i.e. shareholdings, and diversification with executives seeking to lower risk when they have a substantial investment in the company's shares and more of their own money invested. This contrasts with the general view of managers that through diversification the company can spread risk which increases company and employment stability (Amihud & Lev, 1981; Hoskisson & Hitt, 1994). This research notes but does not look at this issue.

What influence do external shareholders have on management? Kor & Mahoney (2005) note research from Sundaramurthy (1996) showing that significant institutional shareholdings do have the potential to influence the strategic direction of a company and the decisions made by management. In cases where there is little/no concentration of shareholdings managers will have greater discretion to adopt diversification strategies that will, they hope, ensure stability and their continued employment (Amihud & Lev, 1981). Where management is not restricted by shareholder influence there is a risk of over-diversification and, as a result, poorer performance. Similarly, McConnell & Servaes (1990) found that existence of influential shareholders may have an overall positive effect on financial performance as management will feel as though their actions are under greater scrutiny and therefore need to be focused on the generation of shareholder returns.

Nickell (1995, p21) makes a clear distinction between the governance regimes in operation in the leading economies of the UK and US and Japan and Germany suggesting major shareholders to be of greatest influence in Germany and Japan. The UK and US equity markets are categorised by Nickell (1995) as being *Type I* with shareholders, institutional and individual, making essentially short-term returns-driven investments in companies but having no direct involvement in day-to-day operations/decision-making relying on non-executive directors to moderate managers' actions and with acquisitions activity relatively common. Conversely, Japan and Germany are seen as *Type II* equity markets with shareholders having long-term commitments (often nominating directors) to the companies in which they hold

substantial investments making acquisitions difficult. In the *Type I* markets of the UK and US the market for corporate control with its implicit threat of takeover exerts pressure on management while in the *Type II* markets of Germany and Japan it is long-term major shareholders that influence company management. Other countries may be aligned with these two extremes; Korea, for example, displays *Type II* characteristics while, say, Canada follows the *Type I* model.

The relationship between management, i.e. executive directors, and major shareholders is difficult to assess with any degree of objectivity. Clearly, management have a route to the market in general through their retained broker and internally or externally managed public relations activities. However, with major institutions they may hold direct meetings and make presentations to garner support, where they feel it is necessary, for key decisions which would need their support, e.g. those necessitating rights issues. In some cases, where price sensitive information is shared with the institutions, they would become ‘insiders’ and have to accept some trading restrictions in return for briefings.

Given these practices, it would seem that the existence of major shareholders will have some impact on the decision-making process and possibly on corporate strategy. But are major shareholders more prevalent in conglomerates?

3.4 Summary

This literature review clearly shows a dearth, compared to the US, of research into UK conglomerates. In addition, there is an even greater bias, in both the US and UK literature, towards industrial/manufacturing companies, which until the last quarter of the 20th century represented, in GDP terms, the largest share of economic activity. There is only one major piece of research, that undertaken by Channon (1978), into UK service companies which now account for over half of economic activity. Clearly, there is a need for further research into UK conglomerates and for that research to include service companies.

Extant research uses several different schemes to categorise companies according to their diversification with the most popular being the strategy-based approach of Wrigley/Rumelt. The research shows a confused picture of the relationship between diversity and performance; some positive, some negative and others suggesting there may be an optimal level of diversification, i.e. a point beyond which the law of diminishing returns applies.

Review of the environmental, regulatory and management factors effecting the adoption, maintenance and abandonment of conglomeration suggests that several of the factors that facilitated the growth phase – to the end of the 1970s in the US and to the early 1990s in the UK – changed and precipitated abandonment in the 1980s in the US and 1990s in the UK. The factors include issues relating to risk reduction, acquisitions activity and its success, the balance of power within the relationship between shareholders as principals

and management as their agents, corporate governance and the attitude and strength of shareholders. In the case of acquisitions, a major route to diversification, the success of such transactions has increasingly been called into question reducing the appetite for transactions without a clear rationale, i.e. those of unrelated activities.

As regards the shareholder/management relationship, the steady increase in the proportion of institutional shareholdings together with their greater willingness to exercise the power that their investments give them coupled with changes in corporate governance guidelines have changed the dynamics within boardrooms and effectively limited the power and increased the accountability of chairmen, CEOs and executive directors. Power has shifted away from directors and towards shareholders.

Finally, investors no longer see conglomeration as offering the only route to greater earnings stability and/or risk reduction as they have come to realise that they can create their own portfolios and reduce unsystematic risk as efficiently, and possibly more cheaply, as conglomerates.

The growth in the incidence of conglomeration and the comparative scarcity of single business companies served to re-enforce the path of companies through the Model of Corporate Development from focus to diversity, from constraint to growth and from high to low risk. What has yet to be seen is whether that flow has reversed and, if it has, why.

The key issues and gaps in knowledge identified are:

- Conglomeration increased in the UK to 1993 amongst industrial/manufacturing companies but while anecdotal evidence suggests a subsequent decline, there is no published formal research to support that contention.

- Regardless of the continued popularity of conglomeration, there is no research showing how stable membership of the conglomerate 'club' has been since 1993 nor the dynamics and causes (merger, acquisition, divestment, reduction in value) of entries or exits.

- While the evolutionary route implicit in the Model of Corporate Development has held up well through to 1993 with relatively few reversals of strategy, the period since may have seen a greater shift back towards focus.

- Since the 1970s no research has been undertaken into the corporate strategies adopted by UK service companies.

- Research shows no clear relationship between diversification and financial performance. However, there is a body of evidence supporting the claims of financial economists for the existence of a 'conglomerate discount' in the valuation of conglomerate companies by the markets. If conglomeration has declined what part, if any, did performance play and what were the other drivers of decisions to change strategy?

- Institutional shareholdings, especially in FTSE100 companies, have increased but no research exists to show if there are differences in holdings, and therefore potential influence, across diversification categories.

- Corporate governance guidelines have changed substantially since the early 1990s but no research exists showing how board profiles – percentage non-executives, incidence of dual and unitary leadership (chairman/CEO), tenure of chairman and CEO – differ across diversification categories or longitudinally.

This research attempts to shed light on each of these issues by framing and testing one or more hypotheses covering each issue. The hypotheses are outlined in the next chapter. The first three points noted above relate to the validity of conglomeration as a corporate strategy and whether it continues to be a realistic strategic option. Analyses of the distribution of companies across diversification categories will show the relative popularity of conglomeration and other diversification strategies between 1993 and 2003 while conglomerate company histories (see chapter 7) will shed light on the reasons, probably strategic rather than financial given the expected absence of a clear link between diversification strategy and performance, for the adoption, maintenance and abandonment of conglomeration. As regards the effect of corporate governance on diversification strategy, the exertion of undue power by executive directors, especially chairmen and chief executives, should have diminished in light of revisions to corporate

governance Best Practice but is that the case and is weaker corporate governance a contributory factor in the pursuit of conglomeration?

Clearly there are a number of issues highlighted in this literature review that will not be addressed in this research. Some of these issues cannot realistically be addressed owing to a lack of reliable and valid information/data, e.g. internal management control issues, divisional profitability, while others have been deemed to be outside of the scope of this project, e.g. managerial shareholdings. However, the flexibility, especially regards capacity to add further data, of the database created for this project will provide a starting point for further research into FTSE100 companies.

Review of the extant literature has established the context for this research into UK conglomeration. However, while much of the literature deals with the incidence of conglomeration and the drivers behind its growth it provides few insights into the factors that combined to influence strategy formulation or decisions that led to the adoption, maintenance or abandonment of conglomeration since 1993. In order to address these issues, each of the companies that was a conglomerate at all or any of the period ends – 1993, 1998 and 2003 – was investigated to identify the key drivers that had influenced their diversification strategy. The resulting conglomerate company histories form the core of chapter 7 – Analysing the Historical Record – which seeks to develop a New Model of Corporate Development.

4. HYPOTHESES

4.1 Aims of this Research

Recognising the vast majority of research into diversification and conglomeration is US centric, this research concentrates wholly on UK companies. Furthermore, as no UK research has been undertaken into UK service companies since Channon (1978), both industrial/manufacturing companies and service companies are included with analyses also carried out on the total population and sector sub-groups. The population is constituents of the LSE FTSE100 Index which comprises the largest 100, by market capitalisation, listed companies.

The research builds on extant research into the largest, by turnover, UK industrial/manufacturing companies including that of Channon (1973), Luffman & Reed (1982), Grant & Thomas (1988), Grant & Jammine (1988) and Whittington & Mayer (2000) and into the largest, by turnover, UK service companies by Channon (1978). The research covers the period from 1993, which was the end of the most recent extant research (Whittington & Mayer, 2000) to 2003.

This research seeks to answer each of the key questions concerning conglomeration in the UK that were raised at the end of the previous chapter.

4.2 Hypotheses

The database created as part of this research was designed to capture data to address the following hypotheses. The hypotheses, which were tested

against FTSE100 and the FTSE100 Survivors populations and service and industrial/manufacturing company sub-sets, for 1993, 1998 and 2003, were grouped under 4 main headings:

A. Incidence

Anecdotally, in the 1990s UK companies followed their US counterparts in abandoning conglomeration in favour of greater focus in their activities; the Model of Corporate Development appears to have been thrown into reverse.

The following hypotheses address this claim by considering the incidence of conglomeration among FTSE100 companies through the research period.

A.1 The incidence of conglomeration amongst FTSE100 companies declined between 1993 and 2003.

A.2 The incidence of conglomeration amongst FTSE100 industrial/manufacturing companies declined between 1993 and 2003.

A.3 The incidence of conglomeration amongst FTSE100 service companies declined between 1993 and 2003.

The changes identified by testing these hypotheses gave rise to supplementary questions regarding the drivers behind decisions to change diversification strategy. These drivers are explored in chapter 7 using conglomerate company histories.

B. Breadth of Activities

In addition to an anecdotal decline in conglomeration amongst the UK's largest listed companies, has there been a broader shift towards greater focus as recommended by Peters & Waterman (1982)? The following hypotheses consider the overall breadth of activities pursued by FTSE100 companies through the research period.

B.1 The breadth of activities pursued by FTSE100 companies narrowed between 1993 and 2003.

B.2 The breadth of activities pursued by FTSE100 industrial/manufacturing companies narrowed between 1993 and 2003.

B.3 The breadth of activities pursued by FTSE100 service companies narrowed between 1993 and 2003.

C. Performance

Literature strongly suggests conglomerates suffer size and complexity-related management and control problems but provides no consensus

as to the effect of diversification on performance. The following hypotheses consider performance of conglomerates through the research period.

C.1 FTSE100 conglomerates underperformed through the research period compared to other categories of company – single business, dominant business and related diversified.

C.2 FTSE100 industrial/manufacturing conglomerates underperformed through the research period compared to other categories of industrial/manufacturing company – single business, dominant business and related diversified.

C.3 FTSE100 service conglomerates underperformed through the research period compared to other categories of service company – single business, dominant business and related diversified.

C.4 FTSE100 conglomerate performance is negatively related to the breadth of activities.

C.5 FTSE100 conglomerates with a core activity generating more than 50% of turnover outperform conglomerates without a core activity.

It was expected that declining performance would be a key driver of any reduction in the incidence of conglomeration. However, as that was

not shown to be the case the existence of other drivers was investigated through the histories of those companies that were conglomerates during the research period.

D. Governance

Corporate governance Best Practice changed significantly through the research period with the express aim of increasing the accountability of executive directors by re-balancing boards in favour of non-executive directors, splitting the roles of chairman and chief executive officer (or equivalent) and making chairmen non-executive. Evidence from conglomerate company histories (see chapter 7) suggests that some companies may have pursued and maintained a conglomerate strategy because of the influence of dominant personalities such as Lord Hanson at Hanson and Sir Owen Green at BTR.

The following hypotheses consider differences between key facets of corporate governance at conglomerates over time and as compared to other categories of company. In each case the null hypothesis is that there is no difference between conglomerates over time or between conglomerates and companies pursuing other diversification strategies. Notwithstanding other influences, these hypotheses seek to identify possible links between strategy and governance especially the influence of chairmen/chief executive officers.

D.1 There was no change in the executive/non-executive split in the composition of FTSE100 conglomerate boards through the research period.

D.2 The executive/non-executive split in the composition of conglomerate boards is the same as that of other categories of FTSE100 company.

D.3 There was no change in the average tenure of chairman of FTSE100 conglomerate boards through the research period.

D.4 The average tenure of chairmen of conglomerate boards is the same as for other categories of FTSE100 company.

D.5 There was no change in the percentage of FTSE100 conglomerate company chairmen that are non-executive directors.

D.6 The percentage of conglomerate company non-executive chairmen is the same as for other categories of FTSE100 company.

D.7 There was no change in the proportion of FTSE100 conglomerates with dual chairmen/chief executive officers through the research period.

D.8 The average proportion of conglomerates with dual chairmen/chief executive officers is the same as for other categories of FTSE100 company.

D.9 There was no change in the average tenure of chief executive officers of FTSE100 conglomerates through the research period.

D.10 The average tenure of chief executive officers of conglomerates is the same as for other categories of FTSE100 company.

D.11 There was no change in the average aggregate shareholdings of investors with notifiable interests in the share capital of conglomerates through the research period.

D.12 The average aggregate shareholding of investors with notifiable interests in the share capital of conglomerates is the same as for other categories of FTSE100 companies.

D.13 There were no major differences between the corporate governance of industrial/manufacturing and service companies.

4.3 Conjectures

The preceding hypotheses are formulated to answer the key questions relating to the incidence and significance of conglomeration amongst FTSE100 companies. The hypotheses also consider whether performance is

linked to degree of diversification. However, performance, while the ‘raison d’être’ for all commercial organisations, is not the only factor driving diversification decisions.

The Model of Corporate Development offers a relatively simplistic view of the evolutionary path followed by companies seeing them move from focus through increasing levels of diversification to conglomeration. The Model does not put these movements into context or suggest which factors or groups of factors influence diversification decisions through the strategy formulation process.

Influences on corporate strategy decisions will include a number of generic, industry specific and company specific factors. Several of these factors were discussed in the literature review but their influence on strategy formulation and strategic change has not previously been considered. In determining diversification strategy, management needs to balance the scale benefits of focus against the lower risk of diversification and the potentially growth limiting regulatory influences on focused companies against unconstrained growth through diversification.

From the literature review it is expected that diversification decisions will be determined by financial/market pressures, regulatory issues and the competence of management. The effects of these drivers on conglomeration cannot be turned into hypotheses but can be the subject of additional research into the companies identified as conglomerates.

Therefore, in addition to quantitative analyses based on accounting records (Chapter 6) to address each of the hypotheses outlined in the previous section, qualitative reviews of the FTSE100 conglomerates identified in this research were undertaken (Chapter 7) to shed light on the drivers behind their strategic decisions to adopt, maintain or abandon conglomeration. Chapters 6 and 7 together comprise the results of this research. Notwithstanding the inevitable degree of subjectivity in the interpretation of each conglomerate's key events, the exercise facilitates discussion of the strategic responses of companies to drivers and the outcomes of those responses in terms of size and scope.

4.4 Contribution

This research makes valuable contributions to knowledge on several levels.

First, the database itself represents a new and unique source of data on FTSE100 companies. The database brings together financial information downloaded from DataStream (summary profit & loss accounts, balance sheets and cash flows and ratios), extracts from company annual reports and accounts (segmental revenues, profits and assets, board composition and major shareholders), Financial Times market data (capitalisation, minimum/maximum share prices, 31st December share prices, yields and P/E ratios) and miscellaneous company information (major acquisitions, demergers, listing transfers, dual listing agreements) from many other sources including FT Intelligence, the Economist and company websites. The database is in the form of an Excel workbook with separate worksheets for

each company and has capacity to accommodate considerably more additional information to facilitate further research into FTSE100 companies. The methodology (Chapter 5 and Appendices C & D) explains how the database was compiled.

Second, the literature review (Chapter 3) critically appraises what is known about conglomerates, conglomeration and its causes highlighting the dearth of UK literature that, with one notable exception, concentrates on industrial/manufacturing companies and ends in 1993 (Whittington & Mayer, 2000).

Third, by analysing the accounting record (Chapter 6) the research uses quantitative data to track the incidence of conglomeration amongst FTSE100 companies between 1993 and 2003 and movements between Channon/Whittington & Mayer diversification categories. The analysis also identifies changes in the breadth of activities, performance and corporate governance across diversification categories and over time. For the first time since Channon (1978) the research includes service companies. Given that the service sector now plays the leading role in the UK representing over 50% of the country's economic activity and that service companies comprise a majority, in both number and capitalisation, of the FTSE100 it is appropriate that they be included.

Fourth, by analysing the historical record (Chapter 7) the research uses qualitative data to identify the factors that have led FTSE100 companies to

adopt, maintain and abandon conglomeration between 1993 and 2003. The influence of these factors on the strategy formulation process are discussed as are their inclusion in a revised Model of Corporate Development which also reflects the two-way flow – forward to diversification and backward to focus - of companies.

Finally, this research provides data and analyses that will help inform the debate on the future of conglomeration amongst the largest, and arguably most economically important, UK companies.

5. METHODOLOGY

5.1 Introduction

This chapter details the methodology followed to explore the validity of the hypotheses detailed in chapter 4 of this thesis.

First section 5.2 outlines the diversification measures available/adopted, section 5.3 explains how a unique database of information on FTSE100 companies was created, section 5.4 discusses the issues/problems that were encountered and their resolution and finally section 5.5 outlines the overall design of the study and section 5.6 summarises the chapter.

The methodology recognises the limitations and inherent subjectivity in gathering and analysing financial and non-financial data on a diverse population but attempts to minimise the effects of both.

5.2 Diversification Measures

5.2.1 Definitions

Before considering the categorisation schemes available for use in research into diversification, it is important to clarify the key terms used in this area of research.

Frequently - not only in everyday speech but also in some academic papers - the terms 'diversification' and 'conglomeration' are used interchangeably to refer to companies with several different business activities which may or may not be related. The use of the word 'diversification' has become confused

(Reed & Luffman, 1986). However, there are marked differences between the terms and between diversified and conglomerate companies and, to avoid ambiguity and misunderstanding, it is essential that each is defined accurately.

Gribbin (1976) produced broad definitions of diversified and conglomerate companies that highlight the key difference between them; relatedness between activities. According to Gribbin (1976, p19-21) a diversified company is one that *"….instead of operating in one market the firm operates in a number, and each separate market is different in important ways, implying significant changes in products, production and marketing, with vertical integration being excluded"*. Similarly, he defines conglomeration as *"joining together disparate products or activities which have virtually no common characteristics"*, making a conglomerate a company that *"…is composed of a series of parts which are not horizontally or vertically related"*.

The difference between related and unrelated diversified companies lies in the relatedness of activities; both have multiple activities but those of a conglomerate are unrelated while those of a diversified company are related. This suggests that conglomerates are, in effect, a sub-division of diversified companies comprising firms with unrelated activities, i.e. diversified companies that have broadened their portfolios to include unrelated activities. Establishing a definition for diversified – related and conglomerate – companies leaves all other companies effectively defined as non-diversified, i.e. focused, companies.

This split between diversified (related/unrelated) and focused is too simplistic and fails to take account of those companies, of which there are many, that have a substantial core business activity but are also active in a number of far smaller activities. These companies are not focused in the sense of having a single activity nor are they diversified as their portfolio is dominated by one predominant activity. Recognising that the 'focused' category could, at one extreme, comprise companies with a single activity and at the other companies with one dominant and several minor activities, there is a strong argument that the non-diversified or focused category be split into single business and dominant business categories.

These definitions have therefore produced 4 categories of company; single business, dominant business, related diversified business and conglomerate. This taxonomy was originally established by Wrigley and further developed/enhanced by Rumelt (1974) who used it in their ground-breaking research into the diversification strategies of US companies. The taxonomy links to the Model of Corporate Development discussed in previous sections and has consistently been the most commonly used by researchers in this area (Dess, Gupta, Hennart & Hill, 1995) although, in some cases, with minor modifications.

Establishing robust definitions is only part of the process of determining a categorisation scheme. Another key element is a scheme's practicality, i.e. can it be consistently applied to real companies rather than theoretical constructs. Given that the categories identified above use the relatedness

between activities as a factor determining diversification category it is necessary to determine what constitutes relatedness and how related activities can be identified.

Assessing relatedness between a company's activities is, by virtue of the fact that the company will, for commercial reasons, only make publicly available a limited amount of relevant information, a subjective exercise. In UK research, this problem is further exacerbated by the absence of Standard Industrial Classification (SIC) code data which would provide a formal, structured means of assessing relatedness, e.g. at 2, 3 or 4 digit code level. Sections 5.2.2 and 5.2.3 outline a number of categorisation schemes that use SIC code data. Prahalad & Hamel's (1990) non-SIC code approach, which is based on how a company's 'portfolio of competences' is used across its activities, is unfeasible because of the lack of sufficiently detailed information. The approach followed by the leading researchers in this field – Rumelt (1974), Channon (1973, 1978) and Whittington & Mayer (2000) - relies on the identification of similarities between a company's services and/or products to determine whether or not they are related. Where there are little or no differences, say, motor vehicles and financial services, the activities are unrelated, but where there are clear similarities, say, motor vehicles and automotive components, the activities are related.

5.2.2 Categorisation

As this research attempts to isolate and analyse categories of UK companies according to their degree of diversification, it is essential that, whilst

endeavouring to minimise complexity, definitions are sufficiently detailed and unambiguous to ensure robustness and credibility and that the chance of mis-categorisation of companies is minimised.

There are two possible approaches to the categorisation of companies: positive and negative. The positive approach requires a clear definition of categories to cover the complete spectrum of diversification, i.e. including the category to be researched. The alternative, negative, approach is to design a scheme that defines categories of company other than that which is to be researched and those companies that do not fit any of the pre-determined categories will be those to be researched. The negative approach has been discounted as, to draw meaningful conclusions from this research, it is essential that the category to which any conclusions apply is clearly and positively identified which necessitates defining all categories.

Having adopted a positive approach to categorisation, there is a further choice as to which measures should be used to determine categorisation; continuous/index or discrete category based. The former comprise indices which effectively convert the distribution and relatedness of turnover, operating profit or net asset data into an index with a value between 0 and 1 where 0 denotes a company that has an infinite number of unrelated activities and 1 a single business company. Alternatively, discrete categorisation schemes consider the distribution of turnover across activities and the inter-relationships between those activities to decide into which of several pre-determined ranges, and their associated categories, a company fits.

Continuous measures are good when comparing degrees of diversification but are not descriptive; an index number does not convey any qualitative information. Discrete measures are good for grouping similar companies according to their degree of diversification. Index-based schemes are considered more objective as they typically use SIC coded turnover-by-activity data in calculating diversification indices. However, the availability of SIC coded data is a problem in countries other than the US.

Sambharya (2000) categorised the available schemes as being either business count or strategic with the former comprising continuous measures including Berry-Herfindahl, Entropy and Broad and Narrow Spectrum Diversity (BSD & MNSD) (Varadarajan & Ramanujam, 1987) and the latter primarily the discrete Wrigley/Rumelt scheme. In terms of their robustness, business count approaches which rely on SIC code data are seen as more objective than the largely subjective strategic approaches that rely on observation and non-standardised published data, e.g. segmental reports included in annual reports and accounts (Ramanujam & Varadarajan, 1989). This subjectivity reflects issues in the assessment process which generally considers inter-dependence between reported activities in terms of processes, products and technology although clearly from an ‘outsiders’ perspective. However, the simplicity of SIC code count approaches, while an advantage, is also a drawback in that is makes no allowance for the difference in the breadth of SIC codes and assumes that each is equally dissimilar.

It is important to note the limitation of diversification indices, e.g. their obvious reliance on the availability and reliability of segmental data and the possibility that they may provide conflicting assessments of degree of diversification and/or direction/quantum of change over time. The latter point is illustrated by Robins & Wiersema (2003) who question the validity of two of the most widely used continuous measures of related diversification; the related component of the entropy index and the concentric index which, they show, do not always produce consistent categorisations. Finally, in common with other measures, the entropy index fails to take account of a company's 'strategic intent', e.g. what a company intends to do. The entropy indices reflect the diversity of a company at a point in time but do not shed any light on the strategic direction of the company or on any strategic issues faced.

5.2.3 Types of Scheme

The following section reviews several of the categorisation schemes used in research into diversification with the aim of establishing which are appropriate for use in this research project. Advantages and disadvantages of each scheme are considered as are practicalities in light of the data quality and level of detail available.

5.2.3.1 Business Count (Continuous) Index Schemes

Entropy

The continuous entropy diversification index is calculated using SIC-code segmental turnover data. The index of a company's total diversification (DT) has a minimum value of 0, which equates to a single business company, and

increases with diversification. DT can be broken into two subsidiary indices to show related diversification (DR) and unrelated diversification (DU).

The measure was first developed by Jacquemin & Berry (1979) and applied to diversification by Palepu (1985) and is calculated using turnover data at 2 and 4-digit SIC-code levels as follows:

Total Diversification (DT)

$DT = \sum P_i \ln(1/P_i)$

Where, P_i is the share of the segment i and $\ln(1/P_i)$ is the weight given to each segment.

Related Diversification (DR)

$DR = \sum DR_j P^j$

and

$DRj = \sum P^j_i \ln(1/P^j_i)$

Where DR_j is the related diversification derived from the operation in several segments within an industry group j and P_j^i is defined as the share of segment i (4-digit SIC code) of group j (2-digit SIC code) in the total turnover of the group.

Unrelated Diversification (DU)

$DU = \sum P_j \ln(1/P_j)$

Which is the weighted average of all the group shares.

As noted by Palepu (1985, p244) the measure's strength lies in its reflection of three key components of product diversification: the number of product segments in which a company operates, the distribution of a company's total turnover across its product segments and the degree of relatedness between product segments.

The major advantages of the entropy measure lie in its relative simplicity and objectivity as it uses turnover data that conforms to a standardised scheme - SIC-code - which means it can be used for inter-company comparisons. Hoskisson, Hitt, Johnson & Moesel (1993) investigated the validity of the entropy measure seeking to prove it to be preferable/superior to alternative measures and found, in common with others, that strategy based measures such as Rumelt's were inherently more subjective.

Entropy does have its critics and faults. Hall & St. John (1993) believe it has a tendency to favour single and dominant business categories at the expense of the related and conglomerate categories as related businesses are only considered within 2-digit SIC codes and unrelated categories across 2-digit SIC codes. A further problem is that the determination of cut-off points to define diversification categories is arbitrary, what ranges of DT indices equate to each of the diversification categories.

The integrity of entropy indices is dependent on the accuracy of the SIC-code data used in its calculation. In the US, since its introduction in 1976 Statement of Financial Accounts Standard 14 (SFAS14) has required public companies

to publish and include in their annual 10-K filings segmental information, including SIC codes, for each activity with more than 10% of consolidated turnover, profits or assets with each segment, where relevant, sub-divided into a maximum of 4 principal products/services. In order to ensure segmental reports closely match business reality the disclosure provisions of SFAS14 were enhanced by SFAS131 (introduced in 1997) which require segments reported to be consistent with those used by management. Researchers are further helped by Standard & Poor who maintain a database – COMPUSTAT – which they do make available to some researchers and which includes segmental data, complete with SIC codes, on US companies. No such database exists in the UK.

The UK requirements introduced by the Companies Act 1965 and SSAP25 (1990) are similar but less detailed than those in the US with the two major differences being; SIC codes are not required and management can omit/consolidate segmental data where publication, in their opinion, would be commercially detrimental, e.g. show margins to competitors. While the latter may result in some reported segments comprising an odd mix of activities or being changed from one accounting period to another, the former effectively precludes the use of SIC-code based diversification measures in research. Therefore, research into US companies may be seen as more robust as it frequently uses the COMPUSTAT database allowing measures of diversity that use SIC codes, e.g. entropy, to be calculated.

Notwithstanding the other problems noted above, the UK does not have an equivalent of the US S&P COMPUSTAT database to provide the required SIC-code data. Furthermore, the lack of detail in UK company segmental reports appearing in many annual reports means SIC codes cannot, with any degree of accuracy, be assigned to the segments reported. The use of entropy in UK research is therefore effectively precluded.

Broad & Narrow Spectrum

As with entropy, calculation of broad and narrow spectrum indices relies on the availability of SIC-code turnover data. The calculations are very simple being based only on the number of segments at either a 2 or 4-digit SIC-code level, in which a company operates. The indices are calculated as follows:

Broad Spectrum Diversity

BSD = No. of 2-digit SIC codes

Narrow Spectrum Diversity

NSD = No. of 4-digit SIC Codes

In an attempt to make some, albeit very crude, assessment of relatedness between activities, a mean narrow spectrum diversity index may be calculated. In effect the MNSD shows how many, on average, 4-digit SIC-code activities are within each 2-digit SIC-code activity.

Mean Narrow Spectrum Diversity

MNSD = NSD / BSD

The advantages and disadvantages of the index are similar to those for entropy but in addition the index does not take account of the relative sizes of the segments in which the company operates and therefore provides only the most high-level assessment of diversity.

Herfindahl

This continuous index, which can be calculated using revenue, operating profit or asset data, considers the breadth or degree of concentration or focus across a company's activities (Comment & Jarrell, 1995). The index was considered by Jacquemin & Berry (1979) to be a valid alternative to entropy.

The index is most commonly used by economists to assess the degree of concentration in markets while others have used it to provide a simple but reliable measure of other types of concentration, e.g. cultural diversity. This has led to its widespread use by the UK’s Competition Commission and its foreign equivalents, as a primary means of assessing the market power that exists in industries subject to structural review, e.g. UK Brewing Industry, or that may result from the combination of two or more companies whose proposed merger has been referred for review. Other users include the government, academics and research organisations such as the National Institute for Economic and Social Research.

The index is the sum of each reported activity’s squared proportion of the company’s total activity, operating profit or assets with the extreme values of 0 representing an infinitely diverse company and 1 a single business company.

As with entropy-based measures of diversification, Herfindahl indices are best calculated using consistent level SIC-code data, e.g. at the 2, 3 or 4-digit level. However, the index's simplicity renders it amenable to being calculated using reported segmental data. Clearly, this makes the index less robust but, notwithstanding changes made to divisions and the breadth of activities within them, the index does provide a useful indication of the direction of change in diversity. The formula is:

$$H = \sum_{i=1}^{N} (P_i/\sum P_i)^2$$

Where P_i is the turnover of segment i.

The major advantages of the Herfindahl index lie in its simplicity, relative ease of calculation and inclusiveness; all reported activities are included in the calculation, none are excluded. While, notwithstanding the availability of segmental data, the index is simple and easy to calculate, it fails to take any account of any relatedness between the separately reported business activities, i.e. all reported activities are effectively deemed to be unrelated. Furthermore, in common with all continuous index measures, use of the index to categorise companies, e.g. as high, medium or low diversifiers, would require the subjective conversion of index ranges into categories which, were it practical, would not produce a scheme that distinguish related and unrelated diversifiers as relatedness between reported activities is ignored.

Therefore, Herfindahl is not valid as a primary means of categorising companies according to their degree of diversification if, as in this research,

conglomerates need to be separately identified. However, as a means of providing a simple overall measure of the breadth of activities for use in assessing whether diversity has increased or decreased over time and to compare overall levels diversity between companies whose diversification category has been determined using another more suitable scheme, e.g. Rumelt, it does have merit. Therefore, the Herfindahl index has been calculated for each FTSE100 company as at 1993, 1998 and 2003.

5.2.3.2 Strategy Schemes

Rumelt

The categorisation scheme most widely used in diversification research is that initially devised by Wrigley and further developed/enhanced by Rumelt (1974). The strategy-based scheme provides a practical, albeit inherently more subjective, and logical approach to determining a company's level of diversification; single business, dominant business, related diversified and unrelated diversified or conglomerate.

Recognising the almost universal acceptance of turnover as the only valid measure of activity, Rumelt (1974) equated value ranges of two turnover-based ratios - specialisation and related – to 4 separate diversification categories as per the following table:

Table 23: Rumelt's 4-Category Categorisation Scheme

	Description	Ratios
SB	Single Business	$R_s \geq 0.95$
DB	Dominant Business	$0.95 > R_s \geq 0.70$
RB	Related Business	$R_s < 0.70$; $R_r \geq 0.70$
UB	Unrelated Business	$R_r < 0.70$

Where;
R_s (specialisation ratio) – the proportion of total turnover accounted for by the largest single business unit,
R_r (related ratio) – the proportion of total turnover attributable to the company's largest group of somehow related business activities.

Source: Adapted from Rumelt (1974)

In addition to developing the 'basic' 4-category scheme, Rumelt (1974) also created sub-divisions to reflect different degrees of relatedness in the dominant and related categories and the passive or acquisitive nature of companies in the unrelated diversified category. Although this expanded scheme comprising 9 categories used an additional ratio - V_r (vertical ratio) - to determine the degree of vertical integration amongst dominant companies, the additional categories were heavily dependent on subjective judgements. Rumelt (1977) continued to develop the expanded scheme and by 1982 had reduced it to 7 categories - dominant sub-divided into dominant vertical, dominant constrained and dominant linked and related sub-divided into related constrained and related linked – with categorisation determined more objectively by using a further ratio – R_c (related core).

Table 24: Rumelt's 7-Category Categorisation Scheme

	Description	Ratios
SB	Single Business	$R_s \geq 0.95$
DV	Dominant Vertical	$R_v \geq 0.70$
DC	Dominant Constrained	$0.95 > R_s \geq 0.70$; $R_c > (R_r+R_s)/2$
DLU	Dominant Linked-Unrelated	$0.95 > R_s \geq 0.70$; $R_c < (R_r+R_s)/2$
RC	Related Constrained	$R_s < 0.70$; $R_r \geq 0.70$; $R_c > (R_r+R_s)/2$
RL	Related Linked	$R_s < 0.70$; $R_r \geq 0.70$; $R_c < (R_r+R_s)/2$
UB	Unrelated Business	$R_r < 0.70$

Where;

R_s (specialisation ratio) – the proportion of turnover accounted for by the largest single business unit,

R_c (related core ratio) – the proportion of turnover attributable to its largest group of businesses which share or draw on the same common core skill,

R_r (related ratio) – the proportion of a company's turnover attributable to its largest group of somehow related businesses,

R_v (vertical ratio) – the proportion of turnover attributable to the company's largest group of products, joint-products and by-products.

Source: Adapted from Rumelt (1982, p360)

The sub-division of the related category was dependent on linkages in terms of vertical integration (measured by R_v - the vertical ratio) and use of common skills (measured by R_c - the related core ratio) between dominant and other activities while sub-division of the related category was dependent on the interdependence of the related activities. While the expanded 7-category scheme is more detailed and 'richer' than the original 4-category scheme, it is inherently more subjective as it requires additional assessments of product relatedness according to the degree of vertical integration across business activities and the processes/skills used in those activities.

Notwithstanding the significantly increased level of subjectivity, the additional data requirements of the 7-category scheme make its adoption in this research difficult; it requires information/assessments regarding core skills to

calculate the related core ratio (R_c) and identification/assessments of by-products and their internal uses to calculate the vertical ratio (R_v).

The basic 4-category Rumelt scheme has been used by the overwhelming majority of researchers in this field (Dess, Gupta, Hennart & Hill, 1995). It uses turnover or its equivalent and through the calculation of 2 simple ratios and an assessment of product and/or service relatedness provides a sound basis for a categorisation that is consistent with those used in the Model of Corporate Development.

Hill & Pickering

Hill & Pickering's (1986) strategy-based scheme is one of the simplest; it has only 3 categories – low, medium and high diversification – which are determined according to the distribution of turnover between core and non-core activities. The categories are defined as follows:

- Low diversification - non-core turnover less than 5% of total turnover,
- Medium diversification - non-core turnover between 5% and 25% of total turnover,
- High diversification - non-core turnover greater than 25%.

A major strength claimed for the scheme is its simplicity. However, that simplicity is also a weakness in that it effectively ignores diversification beyond that identified between core and non-core activities. Therefore, the scheme does not reflect the underlying breadth of a company's activities nor does it make any distinction between related and conglomerate companies.

An extreme example of the scheme's weaknesses would be a company that, by reporting two activities each accounting for 50% of turnover, would be classified as highly diversified which would not be a fair reflection of its limited spread of activities. Furthermore, the low thresholds determining low and medium diversification result in a very large number of companies being categorised as highly diversified, i.e. conglomerates. A revision to the Hill & Pickering (1986) scheme that mitigates this problem is to apply the thresholds to turnover distributions across related groups rather than individual activities. A conglomerate would then be a company with more than one unrelated activity with the smallest – the non-core activity - generating at least 25% of its turnover.

This research has used the modified Hill & Pickering (1986) scheme as an alternative, primarily to support the categorisation of conglomerate or highly diversified companies.

Channon

In the 1970s Channon (1973 & 1978) produced the first research into UK diversification. His initial research (Channon, 1973) concentrated on the largest, by turnover, industrial/manufacturing companies and was part of a Harvard Business School project, administered by Scott (1973) that also included similar research in France and Germany by Dyas & Thanheiser (1976) and in Italy by Pavan (1976). Recognising the increasing importance of the service sector in the UK economy, in 1978 Channon undertook further

research concentrating on the largest, by turnover or its equivalent, UK service companies.

The categorisation scheme adopted by Channon (1973) was effectively the Rumelt (1974) 4-category scheme although the category descriptions were modified to better explain each category and the underlying concepts of relatedness. Channon's (1973) definitions are:

- Single product - At least 95% of turnover in a single product area.
- Dominant product - Single dominant product with at least 70% of total turnover with other products, which may or may not be related to the dominant product or other minor products, comprising 30% of total turnover.
- Related product - Multiple related products/markets, no single product line with 70% or more of total turnover and related products/markets account for 70% of more of total turnover.
- Unrelated product - Multiple unrelated products/markets, no single product line with more than 70% of total turnover and related products/markets account for less than 70% of total turnover.

The cut-off points used by Channon (1973) are effectively those established by Rumelt (1974) and research into the appropriateness of the category values of the specialisation ratio has found them to be robust (Reed & Sharp, 1987). They also seem reasonable, e.g. setting the cut-off for a single product company at 95% recognises that very few companies have one single product that accounts for 100% of turnover. The cut-offs used by Channon (1973) in

his UK research were also used in other European studies under the Harvard programme; Dyas & Thanheiser (1976) in Germany and France and Pavan (1976) in Italy. The consistency of the categorisation schemes used across the Harvard programme ensure that, in addition to the identification of trends, valid country comparisons may be made.

In adopting this scheme, Channon (1973) retained the simplicity of the Rumelt (1974) scheme and its link to the categories in the Model of Corporate Development, ensured that relatedness between activities was taken into consideration in determining a company's degree of diversification and distinguished between diversified and conglomerate companies. However, as with Rumelt (1974), it must be recognised that categorisations under the scheme are, inherently, subjective as they require assessments of the relatedness between activities. While not universally adopted in UK research, the Channon (1973) scheme was also used by Whittington & Mayer (2000) which meant that there are strong methodological links between the key pieces of extant UK conglomerate research.

Whittington & Mayer

Whittington & Mayer (2000), whose research is the most recent covering the 10-year period between 1983 and 1993, adopted Channon's (1973) categorisation. Their pragmatic approach not only recognised the scheme's heritage, robustness and widespread use and acceptance but also ensured consistency with prior UK research dating back to 1950 allowing meaningful trend analysis to be undertaken. In addition, Whittington & Mayer (2000) also

categorised UK companies according to Rumelt’s (1982) expanded 7-category scheme an exercise which, apart from being inherently very subjective, would have necessitated more resources, both time and information, than were available for this research.

5.2.3.3 Importance of Core Activity

One area to be researched is the incidence of related diversifiers and conglomerates that have a significant business activity within their portfolio. Clearly, such an activity could provide a ‘safety net’ of stable performance allowing greater diversification risks to be taken. The 'traditional' Channon (1973), Dyas & Thanheiser (1976) and Whittington & Mayer (2000) categorisation scheme effectively ignores the size of the largest single business activity once it falls below 70% of total turnover in its definitions of related diversifiers and conglomerates. Clearly, these categories are very broad and would include a wide range of companies with at one extreme two business companies where one activity accounts for 69.9% of turnover and, at the other, companies with several businesses none of which accounts for a significant proportion of total turnover. However, the existence of a substantial business activity in related or conglomerate companies could be a major determinant of corporate behaviour, performance and survival.

Furthermore, the underlying core business of a related diversifier or conglomerate may change and the impact on the company needs to be understood. A prime example is GEC/Marconi, categorised as a related diversifier in 1983 and 1993 by Whittington & Mayer (2000), when its

dominant core activity was electrical engineering. By 2003, GEC (then renamed Marconi) was still a related diversifier but its dominant core activity had changed to telecommunications following a strategic review and a series of high value acquisitions and divestments. However, the company had fallen out of the UK's top 100 companies by market capitalisation having narrowly avoided bankruptcy with debts exceeding £5 billion incurred funding expensive acquisitions of telecommunications businesses as it changed its core activity. Clearly, in this case the existence of a significant business activity and, more importantly, the attempt to change it, had a major and disastrous effect on the company.

Recognising the need to identify companies with a core activity, the following amended typology is proposed:

- Single Business - At least 95% of total turnover in a single product area
- Dominant Business - At least 70% of total turnover in a single product area
- Related - Multiple related products/markets, no single product line with 70% or more of total turnover and related products/markets account for 70% of more of total turnover:
    - Related – Core*
- Conglomerate - Multiple unrelated products/markets, no single product line with more than 70% of total turnover and related products/markets account for less than 70% of total turnover:
    - Conglomerate – Core*

* A core activity is one that accounts for more than 50% of total turnover.

5.2.3.4 Assessment of Relatedness

All the categorisation schemes noted earlier are similar in that they are based on segmental data. This is true of Rumelt's schemes and the variations of those schemes used by UK researchers Channon (1973) and Whittington & Mayer (2000). In each case company categorisation is determined by the distribution of turnover across business activities and an assessment of relatedness between those activities. Successful implementation of the chosen typology is dependent on the quality and accuracy of segmental data and the assessment of the relatedness between segments reported. Given the wide diversity of business activities across FTSE100 constituents and the degree of 'licence' given to directors as to how they should divide and report on their business, there are inevitably issues with segmental reporting and these are dealt with later in this chapter

While it is relatively easy to identify those companies that operate in a single business, e.g. the supermarket groups Tesco, Morrison and Sainsbury, or whose operations are overwhelmingly dominated by one principal activity, e.g. Legal & General (life assurance and general insurance), Associated British Foods (food processing and clothing retail), BAA (airports and property) it is more difficult to identify diversified companies and then to split those companies into related and unrelated (conglomerate) diversifiers. Given a key element of any categorisation scheme is assessment of the relatedness of activities, in the absence of a standard measurement of relatedness, there is always a risk of mis-categorisation due to the inherent subjectivity of assessments. This is especially true in the UK where, unlike the US,

companies are not required to report segmental data by SIC code. By gathering as much relevant data as possible/practical, subjectivity may be limited but it cannot be eliminated.

There are several approaches to determining relatedness but, as with the example that follows, many are precluded as they require information that is not publicly available. Prahalad & Hamel (1990) suggested a competence based view that views companies holding a 'portfolio of competencies' with the application of those competences determining relatedness. A company could be described as a conglomerate on a product level and as a related diversifier on a competence level. Prahalad & Hamel (1990) suggest Canon, NEC and Xerox to be competence based related diversified companies rather than conglomerates. This 'resource-based' view is supported by Whittington & Mayer (2000, p56), *"it is the existence of surplus resources that stimulates diversification"*. They go on to say that the potential breadth of resources is wide and includes management skills, specialised production facilities, trade secrets, etc. Unfortunately, without direct access to companies, it is impossible to undertake robust competence audits and to assess competence-based relatedness.

In assessing relatedness this research draws on comments made by Whittington & Mayer (2000, p247) who noted that *"vertical integration [is] explicitly considered as a related strategy"* and *"….no single core skill was required for a company to be classified as related. Rather, a domino pattern with different skills along the chain linking the different activities was*

considered sufficient". From these two comments an approach to determining the relatedness of each reported business segment was established. To be related activities (reported segments) should:

1. Use similar skills, e.g. technologies, equipment, as evidenced by the use of similar Value Chains,

Or

2. Be vertically integrated, i.e. provide inputs to or take outputs from each other.

Therefore by looking at processes, products and technology the degree of relatedness between a company's activities could be assessed. Similarities between customers or distribution channels are not considered sufficient to deem activities related as most business sell either to the public, commerce or the governments and distribution, often outsourced, represents a small part of the value chain. This research takes a holistic approach and considers the overall activity of each reported division after amalgamating geographically separate divisions comprising the same activities. The approach adopted in this research will give a view of relatedness between a company's activities but it must be remembered that it is not the only view.

Finally, using segmental reports will almost certainly understate the degree of diversification in a company as each division is typically a collection of business activities rather than a single activity.

5.2.4 Summary

This section has reviewed the most common business count (continuous) index-based schemes that use SIC-code information and strategy-based categorisation schemes which use less formal/structured turnover data with a view to identifying the scheme or schemes that are best suited to this research project. The review considered each scheme in terms of simplicity, richness, subjectivity and practicality.

The choice of scheme does have an effect on research into diversification as Hall & St. John (1993) found. They considered the relative strengths and weaknesses of different measures of diversity, including examples of both types, and concluded that scheme choice had an impact on research results, in their case the relationship between diversification and performance. While recognising the inherent benefits of categorisation based on SIC-code data, Hall & St. John (1993, p165) noted that such schemes' validity was "….*completely dependent upon the validity of SIC codes in representing strategic diversity"* which was exacerbated by inconsistencies in the width of SIC-code groupings and subjectivity in the true relatedness SIC-codes, e.g. can all 4-digit codes within a 2-digit code be considered to be related. Hall & St. John (1993) suggested that the results of research would be influenced by the diversification measure adopted and that SIC codes were not the panacea to categorisation difficulties.

The limitations of UK segmental reporting effectively preclude the use of SIC-code index schemes such as the entropy diversification index. Compared to

the US, few UK researchers have opted to the use index-based categorisation schemes primarily owing to the limitations of UK company segmental reports. However, the Herfindahl index does provide a simple, easily calculated indicator of the overall breadth of company activities although without a distinction between related diversified and conglomerate companies. Of the strategy-based schemes the most appropriate, not only on grounds of richness and robustness but also for continuity with extant UK research by Channon (1973, 1978) and Whittington & Mayer (2000), appears to be the Channon (1973) scheme which has its roots in the Rumelt (1974) categorisation scheme that has been so widely used over the last 30 years.

Having reviewed each of the commonly used categorisation schemes this research uses two primary complementary measures to determine diversification amongst FTSE100 companies; the Channon (1973)/Whittington & Mayer (2000) strategy-based scheme modified to incorporate additional sub-categories to the related diversification and conglomerate categories where a core activity accounts for more than 50% of total turnover and the continuous Herfindahl index. Hill & Pickering, modified to use turnovers of related groups rather than individual divisions, was also used as a secondary means of categorisation.

The choice of schemes to be used in this research was made in light of Ramanujam & Varadarjan's (1989) recommendation that a mix of continuous/business count and strategy measures of diversification was the most appropriate and inclusive methodological approach. Similarly, Palepu

(1985, p239) also advocated the use of both types of scheme using entropy and Rumelt schemes he claimed that the approach *"….combines the strengths of the index approach, namely simplicity, objectivity and replicability, with the essential richness of Rumelt's methodology"*.

5.3 Database

5.3.1 Population – FTSE100

Previous UK research including that by Channon (1973) and Whittington & Mayer (2000) concentrated exclusively on the largest, by turnover, UK industrial/manufacturing companies. This population included private as well as public companies but excluded financial, utility, government owned and service companies, defined as those companies for which services account for more than 50% of total turnover.

Whittington & Mayer (2000) used the annually published Times 1000 to compile their lists of UK manufacturing companies. The Times 1000 listed, in descending order of turnover, the UK's largest companies, including both public and private companies, providing additional financial information for the last two completed and reported financial years including turnover, operating profit and capital employed and non-financial information such as number of employees, sector and the names of the chairman and managing director/CEO. Unfortunately, the Times 1000 was discontinued in 1998 being replaced by the Euro 500 published by the Financial Times. The new publication is limited to public companies quoted on main European stock exchanges and lists companies in descending order of market capitalisation

rather than turnover. However, within the report there is a subsidiary table listing the UK's top 500 quoted companies by market capitalisation. Given the discontinuance of the previously used publication, it is therefore not possible to establish the same turnover-based public and private company population for study as those used in extant research.

For this research, the population is defined as constituents of the Financial Times Stock Exchange 100 Index (FTSE100) as at the close of business on the last trading day of each relevant calendar year, i.e. 1993, 1998 and 2003. The FTSE100 or 'Footsie' is the primary LSE index and comprises the 100 companies with a full stock exchange listing that are assessed by the review panel as having consistently had the largest market capitalisations at the end of each quarter. Despite comprising only 100 companies, the FTSE100 accounts for substantially more than 50% of the total market capitalisation of the LSE reflecting its importance and that of its constituents.

Using the FTSE100 companies as the research population creates discontinuity with previous UK research which used turnover to determine which companies were included, excluded service companies and included private companies. Given that relatively few private companies were of sufficient size to warrant inclusion in either Channon's (1973 & 1978) or Whittington & Mayer's (2000) research, their exclusion from this research is not seen as a problem in identifying trends since 1950. Furthermore, the inclusion of both service and non-service companies reflects the mix of the UK economy of the late 20th century and the importance and contribution of

service companies. By undertaking some separate analyses of industrial/manufacturing companies and service companies it will be possible to look for any trends in the across both sectors since 1950.

The FTSE100 does include companies with substantial non-UK activities, e.g. SABMiller and Old Mutual - but excludes companies whose primary stock exchange listing is not London, e.g. Ford (Dow Jones, US), Toyota (Nikkei, Japan). Also included are Dual Listing Companies (DLCs) which are effectively companies that have merged but which have retained a separate listing on their 'home' exchanges. While there are only a few of these companies in the FTSE100, they are substantial. DLCs in the FTSE100 are Shell (Anglo-Dutch oil company), Carnival (Anglo-US cruise line operator), BHP Billiton and RTZ (both Anglo-Australian mining companies) and Unilever (Anglo-Dutch FMCG company).

Finally, in addition to entries and exits resulting from mergers and acquisitions, floatations and transfers of listings to/from other exchanges, FTSE100 membership changes to reflect increases and decreases in market values. Therefore, the membership at the end of 1993, 1998 and 2003 is very different. To create a stable population for analysis, a sub-group of those companies that were members of the index at the end of 1993, 1998 and 2003 was created. This sub-group – FTSE100 Survivors - comprises 54 companies rather than the 23 that were identified as FTSE100 'ever presents' by the Financial Times (Dickson, 2004) as it includes companies that may have not been constituents of the index at times other than year ends.

5.3.2 Sector Definitions

By identifying FTSE100 companies as either service or industrial/manufacturing companies it will be possible to identify the characteristics of each sector as well as of the whole population and to make comparisons with relevant prior research.

The sector categorisation of a company is made by assessing each of a company's reported divisions as either being a service or industrial/manufacturing activity. The divisional assessments drive the overall categorisation of the company; where the aggregate turnover of service divisions exceeds that of industrial/manufacturing divisions the company will be categorised as a service company otherwise it will be an industrial/manufacturing company. There will be no attempt to split each division's turnover between service and industrial/manufacturing activity; a judgement is made as to which represents the majority of each division's turnover. Channon (1973, p6) took a very similar view saying that a manufacturing company is, *"….one where at least 50 percent of sales was contributed by manufacturing or processing operations"*. Channon (1973, p6) goes on to point out that this definition differs from that adopted by Fortune *"which includes mining alone and without processing as a manufacturing function"*. Whittington & Mayer (2000, p245) noted that, to identify industrial/manufacturing companies they followed Harvard *"…..in excluding utilities and construction firms, as well as firms for which trade and services accounted for more than 50% of turnover"* to eliminate service companies.

There is therefore consistency across research in the approaches to identifying service companies.

In making assessments, services are deemed to be activities that do not involve changes in the state of a product or the creation of a new product, e.g. utilities (electricity, gas, telephones, water), banks and other financial services companies fit the definition of service companies. Factoring, e.g. retailing to trade and/or the general public goods purchased in wholesale markets, are also deemed service activities. Examples include general retailers including GUS and Marks & Spencer as well as food retailers such as Sainsbury and Tesco. Similarly, Wolseley, the building and plumbing supplies company, is also a service company.

As with any definition, there are some ‘grey’ areas, e.g. catering companies that provide meals (food processors are manufacturers) and mining companies that extract ores/minerals (miners are manufacturers). FT classifications do guide categorisation although some companies do try to ‘stretch’ definitions to achieve a classification that is perceived more favourably by the investment community.

Appendix E lists constituents of the FTSE100 as at 31st December 1993, 1998 and 2003 and notes the service companies and which of those are financial services companies.

5.3.3 Incomplete Data

DataStream downloads were not available for several of the FTSE100 companies and, as a result, they have been excluded from analyses requiring financial data, i.e. performance analyses. Tables summarising financial data note the number of companies for which a complete set of data was available. Segmental data was available from annual reports and accounts for all companies in the database meaning no companies were excluded from the non-performance analyses.

Data for both of the companies in the FT classification 'Investment Companies' – 3i Group (DataStream Number 960338) and Foreign & Colonial (DS 901543) – were not available (access denied by DataStream) and they have been excluded. Review of their annual reports and accounts shows them both to be focused single business companies.

Data for Granada (DS 931524), Eastern Electricity (DS 928847), Securicor (871674) and TSB (DS 870429) were also unavailable from DataStream. Eastern Electricity was acquired in 1996 by Hanson and TSB was acquired in 1995 by Lloyds Bank and therefore they played little part in the FTSE100 over the research period. Both were focussed single business companies; Eastern in electricity generation and TSB in banking. Although in the FTSE100 in 1998, Securicor, a related diversifier, was not a member in either 1993 or 2003.

The position of Granada is more complicated. The company was a conglomerate in 1993 and 1998 with interests in media and catering/hotels and acquired Forte Hotels, then also a FTSE100 company, in 1996. Granada merged with Compass Group in 2000 to form Granada Compass before demerging the combined catering business as ‘new’ Compass in 2001 leaving Granada a media-based business. Further divestments saw Granada become a single business company by 2003. Granada was eventually acquired by Carlton Communications in 2004 to form ITV.

Finally, although still an FTSE100 company at the end of 1998, BTR did not publish an annual report and accounts for that year as by the time of publication it had been acquired by Siebe forming Invensys. Therefore, the segmental data for BTR used in the database for 1998 is that of the 12 months ended 31st December 1997.

5.3.4 Required Information/Data Inputs

All the data used in this research is secondary, i.e. drawn from publicly available sources. As a consequence, there is always a risk of bias in the way information gathered has been reported or interpreted as interrogation of the original data is not possible. However, the principal sources, especially DataStream, are all well known, respected, reputable and reliable.

A fundamental element of this research is the accurate and subjective categorisation of FTSE100 companies according to their degree of diversification in 1993, 1998 and 2003. This was undertaken using data in

segmental reports in annual reports and accounts for the most recently completed financial year of each company, i.e. 1993's reviews would use data from annual reports and accounts for financial years ending up to and including 31st December 1993. Where, in a few cases - Cadbury Schweppes, Reckitt & Colman (now Reckitt Benckiser) and United Biscuits - financial years ended in the first few days of the following January, the year end was assumed to be the preceding 31st December.

In view of the complexity of many FTSE100 companies and the wide variety of factors that could influence their diversification strategies, it was necessary to gather a substantial volume of financial and non-financial data on each company. The financial data may be divided into two sections: data required to categorise companies according to degree of diversification and assess the breadth of activities and data required to assess profitability/performance. The former need is met primarily through collection and analysis of turnover and net assets data provided in segmental reports and notes to annual reports and accounts. The latter is addressed by gathering additional financial data, e.g. summary profit & loss accounts, balance sheets and ratios from DataStream and non-financial information in the reports of chairmen and/or chief executive officers included in annual reports and accounts. The non-financial data may also be divided into two sections; data required to assess adherence to corporate governance Best Practice and data required to provide background/explanations for strategy changes. The former need is met through extracting data from annual reports and accounts and also by interrogating the FAME database of UK company information which includes

details of directors. The latter requirement is satisfied from a variety of sources including company websites, company directories and various databases including FT Intelligence and the Economist.

The annual reports and accounts of companies that provided segmental turnover data were all prepared under statute - Companies Acts - and complied with generally accepted accounting practice (GAAP) in the form of Statements of Standard Accounting Practice (SSAP) and Financial Reporting Standards (FRS). UK GAAP is considered to be amongst the best in the world although they do allow some, albeit increasingly limited, leeway in certain areas, e.g. goodwill, deferred taxation. Furthermore, in view of the sizes of the companies and their public limited liability status, all accounts have been audited and their receipt of unqualified audit reports/opinions provides comfort as to their compliance with relevant legislation and GAAP. For each set of annual accounts from which data has been extracted, the database records the name of the auditor and whether their report was unqualified.

One area researched was links between changes in corporate diversification strategy and performance. In view of the significant differences between some of the FTSE100 constituent companies, notably those involved in financial services, in their financial reporting, especially banks and insurance companies which report according to different statutory requirements, this research has not undertaken comprehensive performance reviews but has instead followed the approach adopted by Hoskisson, Hitt, Johnson & Moesel (1993) who looked at the relationships between diversification and a limited

number of accounting and stock market performance indicators. They found a negative relationship between diversification and the backward looking, i.e. historic, accounting performance indicators and a neutral relationship with forward looking, i.e. prospect based, market performance indicators.

To avoid the complexities inherent in detailed company financial analysis, this research restricted performance analysis to 5 key indicators:

- Market Capitalisation
- Share Price Volatility
- Market Value to Book Value (Excluding Intangibles)
- Return on Capital Employed
- Gearing

For all indicators simple category and population averages were calculated as weighting averages by market value would have created a bias in favour of the largest companies. Weighted averages would not have shown the performance of a 'typical' company in each category.

In addition to the above, this study also considered a number of other performance indicators including operating margin, price/earnings ratios and operating cash flows, but, calculating Pearson's Correlation Coefficients, failed to find any consistent significant relationships with diversity as measured by the Herfindahl index. A limited factor analysis was also undertaken using SPSS to look for correlations between performance and diversification but nothing significant was found.

The core summary profit & loss, balance sheet, cash flow and financial ratio data was downloaded from DataStream (Thomson Financial) and segmental data were extracted from segmental reports in copies of annual reports and accounts downloaded from Thomson Financial. All other details, e.g. market capitalisation, listing classification, etc., were taken from the first Financial Times published after the year end that contained market capitalisation information. Depending on which days of the week were bank holidays, the FT figures may have included the first day's trading of the new-year; the effect was not material.

Appendix A shows the definitions relating to the performance measures used and appendix B shows an example (Associated British Foods) database spreadsheet including the DataStream download sheet illustrating the information collected for each FTSE100 company included in the research project.

5.3.5 Research Period

The period covered by this research - 1993 to 2003 - follows directly on from research into industrial/manufacturing companies undertaken by Whittington & Mayer (2000) covering 1983 to 1993 which, in turn, built on earlier work by Channon (1973 & 1978) covering 1950 to 1970. Research into services (Channon, 1978) stopped in 1974. Despite minor differences in the populations studied, it has been possible to use the prior research to build a picture, albeit with caveats regarding its general application, of the life cycle of UK conglomeration from 1950 to 2003.

Notwithstanding the longer-term trend analysis, the 10 years covered by this research saw substantial change amongst FTSE100 conglomerates as evidenced by the changes in corporate strategy at several high profile conglomerates including BTR, Hanson and Williams. Review of companies that were conglomerates at some time during the research period provided insights into the drivers behind their adoption, maintenance or abandonment of conglomeration.

The period under review was one of steady economic growth in the UK; there were no excessive increases or decreases in gross domestic product (GDP) suggesting a stable economic environment.

5.3.6 Sources

The principal sources of information are similar to those used by Channon (1973 & 1978) and Whittington & Mayer (2000):

- Published company annual reports & accounts downloaded from company websites (largely post-2000) and the Thomson Financial database.
- DataStream financial information:
    - Profit & loss summary
    - Balance sheet summary
    - Cash flow summary
    - Key ratios
- Times 1000/FT Euro 500 reports
- Financial Times

- The Economist
- Press reports/releases extracted from databases, e.g. ProQuest, and/or company websites
- Dun & Bradstreet and similar company directories
- FAME database of company information
- FT Intelligence (FT articles)
- Times Online

The extensive use of DataStream ensures a high degree of consistency in the financial information in the research database. In creating its database of financial information, DataStream interprets annual reports and accounts of all companies in the same way adjusting profit and loss, balance sheet and cash flow figures according to consistent principles, e.g. the identification and treatment of extraordinary/exceptional items, especially reorganisation costs, and other income which varies significantly across companies and can lead to substantial differences in operating profits. DataStream is widely recognised as being a detailed and robust source of company financial information and is used extensively in both commercial and academic environments.

While all FTSE100 companies published their 1993 accounts in sterling some, notably RTZ, BP, Standard Chartered and BHP Billiton, reported in US Dollars in 1998 and/or 2003. DataStream automatically translates accounting data into sterling and the same average exchange rates have been used to translate the segmental data extracted from annual reports and accounts denominated in a foreign currency to ensure data reconcile. Similarly, some

companies have reported accounting periods longer or shorter than 12 months typically to achieve a change in accounting date (year end), e.g. Scottish & Newcastle reported an 8 month period to achieve a 31st December year end, or preceding a merger to achieve a co-terminus year end with a new partner, e.g. Carlton Communications reported a 15 month period to 31st December 2003 before acquiring Granada to form ITV in early 2004. DataStream financial information is automatically 'annualised' with figures pro rated and segmental data extracted from annual reports has been adjusted in the same way to maintain consistency.

Segmental analyses of turnover have been extracted from annual reports and accounts as that information is not captured by DataStream. To ensure downloaded DataStream information relates to the same year as the segmental data and that the underlying annual reports and accounts are the same, the segmental analyses and DataStream turnover figures have been reconciled. Wherever possible, segmental operating profits have been reconciled to the corresponding DataStream figure.

5.4 Issues

5.4.1 Subjectivity

Clearly, given the complexity of FTSE100 companies, the global business environment in which they operate and confidentiality, it is impossible for every aspect of this research to be totally objective; a degree of subjectivity is inevitable given the researcher's position as an 'an outsider'. This section recognises these problem areas and acknowledges their potential effects.

The difficulties of achieving objectivity is exemplified by the findings of Sambharya (2000) who found only 50% agreement between Rumelt scheme categorisations made the managers of the companies assessed and external researchers. This finding is similar to the 48.75% agreement found by Nayyar (1992), who also noted that external assessments were skewed towards related and away from unrelated diversification, but substantially better than the 29.5% agreement achieved by another researcher cited by Sambharya (2000). These variations may be due to errors by researchers who understandably have less information than managers but may also be due to managers' misunderstanding the categories. These findings illustrate clearly the problem of achieving objectivity.

Sambharya's (2000) contention that entropy provides the most robust and objective measure of diversification provides little comfort as the absence of SIC-code segmental data precludes the index's calculation for UK companies. An alternative would be to review and assign a single SIC-code to each division reported by companies in their segmental reports. However, it would be very difficult and extremely subjective to do this at the 2-digit let alone the 4-digit level in order to use the entropy measure of diversification. There would be a grave danger of replacing one subjective judgement with an even more subjective approach.

There will always be some degree of subjectivity in financial data. The problem is even greater when comparing profitability and profitability-based ratios across segments as the, frequently highly subjective, allocations of

central overheads to segments can distort profits. Furthermore, allocations may change across accounting periods without comment/explanation necessarily being made in notes to the accounts and could even be stopped with the corporate centre becoming a loss-making segment itself. This research does not make use of segmental profit data although it is held within the database. Segmental cash generation information would not suffer the same drawbacks as segmental profitability but, unfortunately, few companies report those figures.

5.4.2 Data Availability (Confidentiality)

The confidential nature of some company information limits its availability. The same is true of reports issued by the Competition Commission (CC) either into specific proposed transactions or the structure and dynamics of particular industries, e.g. The supply of banking services by clearing banks to small and medium-sized enterprises (CC Ref: CM5319), Supermarkets: A report on the supply of groceries from multiple stores in the United Kingdom (CC Ref. CM4842). CC reports are judiciously edited to remove information that is commercially sensitive or interesting from a researchers' point of view! Grunberg (1981, p23) noted that there are *"….few Western Governments that conduct special censuses or survey and multinational companies do not publish data on divestments, even if they collect such data. Such information is classified as confidential"*.

Therefore, it must always be remembered that this research is dependent on the quality and range of publicly available information. Unlike Whittington &

Mayer (2000), no interviews have been held with senior executives of the companies researched. Although, given the propensity of directors and senior managers to ‘spin’ information to show them/their company in the best possible light and their understandable reluctance to disclose commercially sensitive information, it is doubtful whether interviews would make a valid contribution to research in this area. An alternative may be to identify retired directors who may be more willing and/or able to discuss past events.

Effectively, this research reflects analysis of the ‘image’ a company portrays of itself through its approach to publication of data required by statute, regulation and the LSE listing agreement.

5.4.3 Changes to Segmentation

Disclosure in annual reports and accounts of mandatory segmental information provides turnover and equivalent data which may be used to categorise companies. However, there are several potential problems/pitfalls associated with segmental turnover data.

Compared to the US, segmental reporting in the UK is less developed. In the US, where Wrigley and Rumelt produced leading research in the 1970s and 1980s, Generally Accepted Accounting Principles (SFAS14 and later SFAS131) and also the FTC have required companies to produce segmental reports, including SIC codes, which have to be included in annual 10-K submissions. In addition, Standard & Poor have created and maintained a database – COMPUSTAT – which includes the submitted segmental data.

Unfortunately, this is not the case in the UK where segmental reporting, first introduced by the Companies Act 1967 and developed through several reporting standards starting with SSAP23 – Segmental Reporting, is less prescriptive. The only reporting of SIC codes by UK companies is in the Annual Returns they submit to Companies House; they are required to note the SIC codes of their activities but they do not have to provide financial data, e.g. turnover, operating profit, net assets, for each code.

Therefore, UK study in this area is inherently more difficult; research is heavily reliant on the availability of good quality segmental data and accurate assessment of relatedness between activities. The potential problems/pitfalls associated with segmental data are:

- Notwithstanding portfolio changes, companies amend reported segments and/or the composition of those segments over time, e.g. to reflect a new management structure,

- Legislation allows directors to decide which of their business activities are ‘sufficiently different’ to require separate identification in the segmental reports,

- There is no consistency across companies in the breadth of activities included within the divisions they report, i.e. one company may report each of its activities separately while another might amalgamate activities that it believes are related in some way,

- Statutes provide an 'escape clause' which effectively allows directors to amalgamate activities and, ultimately, not to provide any segmental data, where they believe that to do so would be commercially prejudicial to their company's interests, e.g. Cable & Wireless provide limited turnover analyses but no corresponding operating profit information. Where directors have relied upon this exemption in preparing segmental analyses, they are required make a disclosure to that effect,

- There are inconsistencies across companies and over time of turnover attributable to joint ventures and associated/related companies and the policies/accounting treatments followed by those companies,

- There are inconsistencies in the inclusion/exclusion of discontinued activities/businesses in the segmental reports. Where sufficient data is found, segmental data has been adjusted to exclude the discontinued activity/business, thereby providing a more accurate picture of the activities of the company at the reporting date,

- There are inconsistencies in the reporting of intra-group turnover. Some companies disclose total and external turnover figures for each of their segments while others merely show external turnover figures which, in total, agree to the headline profit and loss figure,

- Companies have reported geographic divisions that comprise the same activities, e.g. Wolseley reports its UK and US building product distribution

business separately although the activities are essentially the same. (NB Where it is clear this has occurred, the geographic divisions are amalgamated into a product-based division. Appendix D provides details of the principles followed in rationalising reported divisions),

- Companies, especially mining and building materials companies, report separate divisions for each of the ores and/or minerals mined/excavated. Given that all of the activities are essentially the same; these divisions are amalgamated into an activity-based division.

The research database reflects segmental turnover net of intra-group trading where the information is available otherwise gross figures have been used. Similarly, segmental data net of joint venture and associated/related company activity has been used reflecting the investment nature of such non-controlled activity, as compared to subsidiary company activities, and its comparative rarity amongst FTSE100 companies.

A further point is that directors may decide to change the segments they report reducing the validity of longitudinal data. Graham, Lemmon & Wolf (2002) consider the effects of such changes and found that segment changes that were not the result of changes in the business or its activities did not have any effect on market value or perceptions of the company or its activities. In their paper they do cite an unpublished paper by Piotroski (1999) arguing that segment reporting changes can actually have a positive effect on value.

5.4.4 Triangulation

Triangulating or cross-referencing data, especially non-financial data, has been undertaken wherever practical/possible having regard to the risk of bias in reporting, to ensure integrity of data and to minimise errors in categorisations and analyses. However, the inevitability of a degree of subjectivity in the process is recognised, e.g. distinguishing between related diversifiers and conglomerates is especially subjective as opinions as to the concept of relatedness will vary.

5.4.5 Risk of Mis-categorisation

Whittington & Mayer (2000) note that, unlike Channon (1973) and Dyas & Thanheiser (1976), their categorisation process used two researchers independently categorising companies with any disagreements being arbitrated by a third party. However, they note that before arbitration there was a 93.4% correlation between categorisations suggesting that, using an appropriately detailed scheme and reliable data, a single researcher would make a negligible number of mis-categorisations. This high rate of agreement is similar to that reported by Hoskisson, Hitt, Johnson & Moesel (1993) who achieved a level of agreement of 92.8% (180 out of 194 companies). The rate of agreement between this research and that of Whittington & Mayer (2000) in the categorisation of the industrial/manufacturing companies common to both studies' 1993 analyses is more than 90%. Therefore, this issue is not regarded as significant.

5.4.6 Joint Ventures & Associated/Related Companies

A further issue relates to the categorisation of those companies that have significant joint venture and/or associated/related company activities. The reporting requirements these activities have increased over the 10 years covered by this research although there remained a wide range of acceptable approaches. Very few FTSE100 companies carry out a significant proportion of their activities through joint venture or associated/related companies the major exception being Reed Elsevier, the Anglo-Dutch publishing company owned jointly (not quite equally) by UK and Dutch companies who account for their investment as a joint venture. The database includes the UK's proportion of Reed Elsevier's turnover.

Joint venture and associated/related company activities are excluded, where possible, from the turnover data used to assess diversification category. In effect, joint ventures and associated/related company activities are deemed investments yielding income rather than integral parts/activities of the company.

5.4.7 Privatisations

The possibility that privatisations distorted changes amongst the population has been considered. In the 1980s and early 1990s, the conservative government pursued a policy of returning to the private sector as many state owned industries as possible including British Telecommunications, British Gas, British Steel, British Coal (formerly the National Coal Board) and various national and regional water and electricity distribution and generation

companies. Because of their size, on privatisation many of these single business companies immediately became constituents of the FTSE100 although many, especially water and electricity companies, quickly lost their independence being acquired by other UK and, in some cases, foreign companies; a trend that has continued through into the new millennium, e.g. Thames Water acquired by RWE of Germany in 2000, BAA acquired in 2006 by the Spanish company Ferrovial and Scottish Power acquired by Iberdrola of Spain in 2006. Throughout the research period - 1993 to 2003 - there were few changes amongst utilities and, as they are all classified as service companies, they will not distort comparisons with prior research into industrial/manufacturing companies.

5.4.8 Turnover Surrogates

A further problem occurs when categorising those companies that, because of the nature of their business, do not report turnover figures that accurately reflect the spread of their activities; a surrogate for turnover must be used in determining diversification category. Channon (1978, p15) acknowledged the difficulties inherent in categorising these companies, typically financial services businesses, and suggested loans/advances, premium income and assets as alternatives to turnover. This research uses the following surrogates for turnover; premium income for insurance companies and assets for banks.

5.4.9 Accounting Regulation

Since 1960 there have been many changes in UK accounting requirements that have affected reported financial information. In addition to three major

consolidating Companies Acts in 1965, 1979 and 1985, there has also been a whole raft of GAAP. Statements of Standard Accounting Practice (SSAP) were introduced in 1970 by the Accounting Standards Board (ASB) which was itself superseded in 1990 by the Financial Reporting Council (FRC) which introduced Financial Reporting Standards (FRS) some covering new areas, other revising and replacing previously issued SSAPs. The most recent change, which will have implications for all FTSE listed companies, is the adoption of International Financial Reporting Standards (IFRS) with effect from 1st January 2007. These legal and regulatory developments have resulted in significant changes in the content and presentation of financial statements, e.g. treatment of extraordinary/exceptional items, amortisation of goodwill, calculation of earnings per share, resulting in a loss in the comparability of reported results over time. However, the changes between 1993 and 2003 are, with the exception of the treatment of extraordinary/exceptional items and goodwill, not seen as having had a significant effect on reported results.

As regards extraordinary/exceptional items and goodwill there have been significant changes since 1993. SSAP6 – Extraordinary Items and Prior Year Adjustments was superseded by FRS3 – Reporting Financial Performance which became effective in 1993 and effectively eliminated extraordinary items and tightened the definition and reporting of exceptional items in an attempt to bring greater standardisation across companies. However, the FRS3 definitions allowed directors considerable leeway in deciding what are exceptional items requiring separate disclosure and resulted in an increase

rather than a decrease in the incidence and variation in treatment of exceptional costs across companies, e.g. some companies treat reorganisation costs as exceptional while others see them as a normal business expense. The use of DataStream financial information reduces the variations across companies as adjustments are made to ensure consistent treatment of exceptional items.

In broad terms, almost without exception prior to January 1998, as allowed under SSAP22: Accounting for Goodwill, companies adopted a policy of writing off goodwill arising on acquisitions against reserves meaning that it did not appear as an intangible asset nor were subsequent years' profits reduced by amortisation charges. With the introduction of FRS10: Goodwill and Intangible Assets in 1998 this approach was effectively disallowed with companies required to capitalise and amortise goodwill arising on all acquisitions although, by undertaking annual reviews of its value, companies could avoid amortisation charges if there had been no impairment. DataStream deducts intangible assets from capital employed, although it does not adjust profits to eliminate goodwill amortisation, in its calculation of return on capital employed and from book values in calculating market value/book value ratios and therefore the effects of goodwill should be minimised.

DataStream reviews all mergers and treats them as acquisitions by one or other of the parties where the underlying substance of the transaction is an acquisition. This research has used DataStream's interpretations of transactions.

5.4.10 Generic Problems

Dess, Gupta, Hennart & Hill (1995, p370-4) raise a number of important generic methodological limitations/weaknesses regarding research into diversification each of which has been addressed:

- **General limitations of cross-sectional work**

  There is always the potential for confusion in distinguishing cause and effect and in controlling for 'unobservable factors' that may affect company performance, e.g. managerial competence. This problem has been minimised, but not eliminated, by undertaking reviews of all conglomerate companies and noting major extraneous factors that may have contributed to changes in corporate strategy/performance.

- **Differences in organisational culture**

  Management's approach to running a company will have a direct and substantial influence on its performance and behaviour and changes in that management will have an effect. Rather than ignore such influences, this research identifies the chairman and CEO (or equivalent) at each firm in 1993, 1998 and 2003 to see if changes in leadership coincide with changes in strategy.

- **Concentration on corporate level performance**

  Detail is inevitably lost in the aggregation of performance. This research does not attempt to look at performance at activity level but rather at the

corporate level. The basic unit of this research is whole companies and it is at that level that data has been gathered.

Dess, Gupta, Hennart & Hill (1995) suggest that in each of the above cases, some form of semi-structured interview or survey may help to reduce negative effects on research. As noted earlier, it was decided that this approach would not be followed. By using only published data the research will be looking at companies in the same way as their investors; the total activity of each business will be split across activities according to the directors' views as reported in segmental analyses.

5.5 Design of the Study

This research centres on the creation of a unique database of information created from three key sources of data on each company; DataStream has provided summarised profit & loss accounts and balance sheets and financial ratios, the annual reports and accounts of each company has provided segmental information and corporate governance, primarily director details, information and the Financial Times and Sunday Times have provided lists of the FTSE100 as at each calendar year end together with data, adjusted for rights issues, share splits, etc. made during the year, including share prices, price/earnings ratios and yields. The database covers constituents of the LSE FTSE100 index as at 31st December 1993, 1998 and 2003.

Each of the 160 companies in the database, which is held in an Excel spreadsheet, has its own standard format worksheet, populated with its data.

The data is used to calculate additional statistics including multiple (Channon/Whittington & Mayer, Hill & Pickering, Focus/Multiple, Core/Non-core) diversification category assessments. A summary worksheet draws together key data from each company worksheet and is used as the basis for various tables showing the incidence of conglomeration, the breadth of company activities, movements between diversification categories, performance and various corporate governance characteristics.

As there have been many changes in the composition of the FTSE100 over the 10 year research period, two sets of tables have been complied; one set shows data from the whole FTSE100 population as at 31st December 1993, 1998 and 2003 while the other shows data from the 54 companies that were FTSE100 constituents at each of the three period ends. Furthermore, each set of tables has been sub-divided into service and industrial/manufacturing companies recognising that the majority of extant research excluded service companies and therefore would be comparable only to industrial/manufacturing companies.

Recognising that the quantitative data lacks richness, a brief history of each of the FTSE100 conglomerate companies identified in the research has been compiled using a variety of sources from company websites to the FT Intelligence database. These histories provide valuable insight into the drivers - environmental, regulatory and/or management - that were behind decisions to adopt, abandon or maintain a conglomerate strategy.

Statistical analyses using Chi-squared to test for differences between category movements in different time periods and Pearson's correlation coefficients to test for performance-diversity relationships were undertaken.

5.6 Summary

In summary, the key stages of the methodology detailed in this section of the thesis are:

A. Identify the population; constituents of the FTSE100 index as at 31st December 1993, 1998 and 2003. Appendix E shows the lists with key details of each company, e.g. market capitalisation.

B. Gather financial and non-financial data on each of the companies identified in A above to create a unique database. Data for each company is drawn from annual reports and accounts downloaded from Thomson Financial database for 1993, 1998 and 2003 or until the company ceased to fulfil the criteria qualifying it for inclusion, from journal and business press databases, e.g. FT Intelligence, and DataStream.

C. Categorise the companies researched according to their degree of diversification using the same basic typology as followed by previous researchers but including sub-categories within the diversified and conglomerate categories to reflect the existence or absence of a core activity.

D. Analyse the financial performance of the companies and identify changes in corporate strategy and the drivers behind such changes and any relationship between performance and company diversification strategy.

E. Identify service companies that have become manufacturing companies or vice versa and companies that have changed their core activity and the drivers behind the changes.

F. Draw conclusions from the analyses undertaken as to the validity of the hypotheses.

This research makes contributions through the creation of a unique database of information on FTSE100 companies and its analysis to identify changes in conglomeration between 1993 and 2003 and the drivers of these changes.

Conglomeration: An Investigation into the Incidence and Significance Amongst FTSE100 Companies Since 1993

by

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A thesis submitted in partial fulfilment of the requirements for the degree of
Doctor of Philosophy in Social Sciences

University of Warwick, Warwick Business School

April 2009

Volume 2 of 2

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6. ANALYSING THE ACCOUNTING RECORD

6.1 Introduction

This chapter presents analyses of the database created using information extracted from DataStream, company annual reports and accounts and the financial press, principally the Financial Times. The database contains information on 160 companies that were members of the London Stock Exchange FTSE100 Index at the end (31st December) of any or all of the calendar years 1993, 1998 or 2003.

The data is analysed to identify trends in conglomeration between 1993, 1998 and 2003 amongst the FTSE100 as a whole at the end of each of those years (section 6.2) and amongst the 54 companies that were constituents of the FTSE100 at the end of 1993, 1998 and 2003 (section 6.3); the FTSE100 Survivors. While analysis of the FTSE100 identifies trends amongst the 100 most valuable UK listed companies regardless of changes in that population, the FTSE100 Survivors analysis identifies trends amongst a constant population and facilitates further investigative work into the drivers of change.

In addition to the incidence of conglomeration, the chapter also considers movements between diversification categories, diversification across FT classifications, the breadth of conglomerate activities, the performance of conglomerates and their corporate governance both over time and against other diversification categories. Each of these issues is reported in a separate sub-section of section 6.2 for the FTSE100 and 6.3 for the FTSE100 Survivors. The causes – loss of market value, delisting, acquisition – of 46 of

the constituents of the FTSE100 in 1993 leaving the index by the end of 2003 are provided illustrating the dynamism of the index. Finally, each of the hypotheses detailed in chapter 4 are tested against the information in the preceding analyses.

The data analyses of the FTSE100 and FTSE100 Survivor populations are also sub-divided into industrial/manufacturing companies and service companies in order that sector differences may be identified. However, it should be noted that there may be a tendency, compared to industrial/manufacturing companies, for service company categorisations to be biased toward focus. This is particularly true of banks whose segmental reports, which vary greatly in their level of detail and grouping of activities, have been standardised according to broad financial services businesses - personal & corporate banking, insurance, capital markets/investment banking and other - according to principles outlined in Appendix D. While this process improves comparability across bank segmental reports, it may show them to be less diverse than would be the case under a different set of activity definitions.

Throughout this chapter tables are used to summarise key data extracted from the database, e.g. FTSE100 By Diversification Category, and statistical analyses - Chi-squared to test for differences between population category movements in different time periods and Pearson's correlation coefficients to test for performance-diversity relationships – were undertaken. The Chi-tests found patterns of movements to be different between 1993 and 1998 and

1998 and 2003. Pearson's correlation coefficients showed no consistent significant relationships between diversity and performance although a few isolated relationships - specific indicators in specific periods - were identified.

Appendix E comprises lists of the FTSE100 as at 31st December 1993, 1998 and 2003. The market capitalisation of the FTSE100 has risen significantly through the 10 year period covered by this research increasing from £553.3 billion in 1993 to £1,067.3 billion in 1998 and £1,110.9 billion in 2003 and the membership of the index has also changed reflecting the buoyancy and, after the brief recession of the early 1990s, uninterrupted economic growth of the UK economy and its dynamism. In the five years since 2003 there has been little change in the total market capitalisation of the FTSE100 which was £1,142 billion at 31st December 2008.

Unlike the preceding 10 year period which saw publicly owned utilities - gas, electricity, water and telecommunications - returned to the public sector, the research period saw few large privatisations/floatations by the UK government (Railtrack, the provider of railway infrastructure, and British Energy, the nuclear electricity generator, were floated in 1996). However, there were a number of demutualisations including those of insurer Norwich Union (1997) and several building societies became banks including Alliance & Leicester (1997), Bradford & Bingley (2000), Halifax (1997), Northern Rock (1997) and Woolwich (1997). In addition, several companies previously quoted on foreign stock exchanges moved their primary listing to London to take advantage of the UK's status, along with New York and Tokyo, as a pre-eminent financial

centre. Companies moving to the LSE included the mining companies Anglo American (1999, ex South Africa), Xstrata (2002, ex Switzerland) and Billiton (demerged from Gencor of South Africa in 1997), the insurance company Old Mutual (demutualised and listed ex South Africa in 1999) and the brewer South African Breweries (later SABMiller) (2002, ex South Africa). As a result of these new listings several companies fell out of the FTSE100.

A key feature of the FTSE100 over the period 1993 to 2003 was the change in the percentage of service companies in the index. In 1993 only 58% of FTSE100 companies were classified as service companies where more than 50% of their turnover or, in the case of banks, assets were categorised in segmental reports as relating to service activities. By 1998 this had risen to 70% but fell back to 63% by 2003. In terms of value, service companies represented £310 billion (56%), £662 billion (62%) and £634 billion (57%) of the total market capitalisation of the FTSE100 in 1993, 1998 and 2003 respectively. Some of the increase in FTSE100 service companies would have been the result of demutualisations of banks and insurance companies where the newly floated companies entered the index immediately. These 'new' listed service companies would have been partially offset by the entry of several mining companies.

For the survivors, the percentage of service companies remained broadly constant through the research period being 64.8% in 1993 and 1998 and 63.0% in 2003 as would be expected with a stable population and the comparative rarity of companies changing sector. Only BAT/British American

Tobacco was in a different sector, industrial/manufacturing, in 2003 having been a service company in 1993. In value terms, service companies represented £242 billion (63%), £455 billion (59%) and £481 billion (55%) of the total market capitalisation of the FTSE100 survivors in 1993, 1998 and 2003 respectively.

6.2 Constituents of the FTSE100

6.2.1 Diversification

The distribution across diversification categories of FTSE100 companies has changed considerably over the 10 years covered by this research. Using definitions consistent with those of Channon/Whittington & Mayer, the following table shows a steady decline in the number (and percentage) of conglomerates within the 100 companies that comprised the index at the end of 1993, 1998 and 2003. In 1993 there were 16 conglomerates in the index but by 1998 that had fallen to 10 and by 2003 to only 7, less than half the number 10 years earlier. Similarly, the number of related diversified companies had also fallen substantially during the same period from 31 in 1993 to 27 in 1998 with an even greater fall to 18 by 2003. When conglomerates and related diversifiers are considered together – as multiple business companies – the decline is from 47 to 37 and to 25. The multiple business companies have been replaced not by dominant business companies, whose numbers have remained broadly constant through the period, but by single business companies which accounted for only 21 of the FTSE100 in 1993 but 44 in 2003.

Table 25: FTSE100 By Diversification Category

	1993		1998		2003	
	No.	%	No.	%	No.	%
Channon/W&M						
Single	21	*21.0*	34	*34.0*	44	*44.0*
Dominant	32	*32.0*	29	*29.0*	31	*31.0*
Sub-Total Focus	53	*53.0*	63	*63.0*	75	*75.0*
Related	31	*31.0*	27	*27.0*	18	*18.0*
Conglomerate	16	*16.0*	10	*10.0*	7	*7.0*
Sub-Total Multiple	47	*47.0*	37	*37.0*	25	*25.0*
Total	100	*100.0*	100	*100.0*	100	*100.0*
Related - Core	20	*20.0*	18	*18.0*	13	*13.0*
% of Related	*64.5*		*66.7*		*72.2*	
Conglomerate - Core	7	*7.0*	3	*3.0*	5	*5.0*
% of Conglomerate	*43.8*		*30.0*		*71.4*	
Hill & Pickering						
Low	68	*68.0*	75	*75.0*	77	*77.0*
Medium	14	*14.0*	12	*12.0*	15	*15.0*
High	18	*18.0*	13	*13.0*	8	*8.0*
Total	100	*100.0*	100	*100.0*	100	*100.0*

The alternative diversification measure of Hill & Pickering supports the Channon/W&M results and shows a steady fall from 18 to 8 in the number of highly diversified companies and an increase from 68 to 77 in the number of companies classified as having low diversification with medium diversification remaining broadly constant.

The table also shows the percentage of related and conglomerate companies with core activities increased, marginally in the case of related companies but significantly for conglomerates, from 64.5% in 1993 to 72.2% in 2003.

The following tables show changes in the categorisation of industrial/manufacturing and service companies the later comprising 58% of the FTSE100 in 1993, 70% in 1998 and 63% in 2003.

Table 26: FTSE100 By Diversification Category – Industrial/manufacturing

	1993		1998		2003	
	No	%	No.	%	No.	%
Channon/W&M						
Single	3	*7.1*	4	*13.3*	11	*29.7*
Dominant	7	*16.7*	7	*23.3*	14	*37.8*
Sub-Total Focus	10	*23.8*	11	*36.6*	25	*67.5*
Related	22	*52.4*	13	*43.3*	9	*24.3*
Conglomerate	10	*23.8*	6	*20.0*	3	*8.1*
Sub-Total Multiple	32	*76.2*	19	*63.3*	12	*32.4*
Total	42	*100.0*	30	*100.0*	37	*100.0*
Related - Core	13	*31.0*	9	*30.0*	7	*18.9*
% of Related	*59.1*		*69.2*		*77.8*	
Conglomerate - Core	5	*11.9*	2	*6.7*	2	*5.4*
% of Conglomerate	*50.0*		*33.3*		*66.7*	
Hill & Pickering						
Low	21	*50.0*	19	*63.3*	27	*73.0*
Medium	10	*23.8*	5	*16.7*	6	*16.2*
High	11	*26.2*	6	*20.0*	4	*10.8*
Total	42	*100.0*	30	*100.0*	37	*100.0*

Table 27: FTSE100 By Diversification Category – Services

	1993		1998		2003	
	No	%	No.	%	No.	%
Channon/W&M						
Single	18	*31.0*	30	*42.9*	33	*52.4*
Dominant	25	*43.1*	22	*31.4*	17	*27.0*
Sub-Total Focus	43	*74.1*	52	*74.3*	50	*79.4*
Related	9	*15.5*	14	*20.0*	9	*14.3*
Conglomerate	6	*10.3*	4	*5.7*	4	*6.3*
Sub-Total Multiple	15	*25.8*	18	*25.7*	13	*20.6*
Total	58	*100.0*	70	*100.0*	63	*100.0*
Related - Core	7	*12.1*	9	*12.9*	6	*9.5*
% of Related	*77.8*		*64.3*		*66.7*	
Conglomerate - Core	2	*3.4*	1	*1.4*	3	*4.8*
% of Conglomerate	*33.3*		*25.0*		*75.0*	
Hill & Pickering						
Low	47	*81.0*	56	*80.0*	50	*79.4*
Medium	4	*6.9*	7	*10.0*	9	*14.3*
High	7	*12.1*	7	*10.0*	4	*6.3*
Total	58	*100.0*	70	*100.0*	63	*100.0*

The changes appear to be more pronounced amongst the industrial/manufacturing companies where the percentage of conglomerates has fallen from 23.8% in 1993 to 20.0% in 1998 and 8.1% in 2003 by which time only 3 companies fell into that category. The corresponding figures for conglomerate service companies were 10.3%, 5.7% and 6.3% with only 4 companies in the category in 2003.

There was also a sharp reduction in related diversification amongst industrial/manufacturing companies which more than halved falling from 52.4% in 1993 to 24.3% in 2003. Again, this reduction was not matched by service companies amongst whom related diversification remained broadly constant decreasing from 15.5% in 1993 to 14.3% in 2003 notwithstanding an increase to 20.0% in 1998.

Taking the conglomerate and related diversification categories together as multiple business companies, the changes amongst industrial/manufacturing and service companies are again very different. Multiple business service companies accounted for 25.8% and 25.7% of the FTSE100 in 1993 and 1998 respectively before declining to 20.6% by 2003. By contrast the percentage of multiple business industrial/manufacturing companies fell from 76.2% in 1993 to 63.3% in 1998 before almost halving to 32.4% by 2003. The move towards greater focus was more pronounced amongst industrial/manufacturing companies.

However, changes in the incidence of focused - single and dominant business companies - differed between sectors. While both sectors saw significant increases in the incidence of single business companies - services from 31.0% to 42.9% to 52.4% and industrial/manufacturing from 7.1% to 13.3% to 29.7% - changes in dominant business companies were very different. In the industrial/manufacturing sector dominant business companies increased from 16.7% in 1993 to 23.3% in 1998 and 37.8% in 2003 while the services sector saw decreases from 43.1% in 1993 to 31.4% in 1998 and 27.0% in 2003. The Hill & Pickering based categorisations support those based on Channon/W&M with both sectors seeing reductions in high diversification and increases in low diversification with medium diversification reducing amongst industrial/manufacturing but increasing for service companies.

As these statistics refer to the FTSE100 some of the changes will be due to FTSE100 index exits and entries. However, changes in the index constituents reflect not only the LSE population from which they are drawn but also the value investors, through the market, place on those listed companies. Therefore, the move to greater focus amongst FTSE100 companies is indicative of diversification across the LSE and investor support, as evidenced by valuations that drive FTSE100 membership, of companies pursuing different diversification strategies.

6.2.2 Category Changes

By looking at movements between categories from 1993 to 2003 and in the sub-periods 1993 to 1998 and 1998 to 2003 it is possible to indentify forward

and backward movements through the Model of Corporate Development and to see how many companies maintained their strategy, i.e. remained in the same category. This section analyses the movements between categories implicit in tables 25 (all), 26 (industrial/manufacturing) and 27 (services).

Table 28: FTSE100 Diversification Changes From 1993 To 1998

		1998					
		Single	Dominant	Related	Conglom.	Exits	Totals
1993	Single	12	2	0	0	7	21
	Dominant	4	14	5	1	8	32
	Related	1	7	12	1	10	31
	Conglom	1	1	2	7	5	16
	Entries	16	5	8	1		
	Totals	34	29	27	10		100

The above table shows that, excluding exits, 45 (64%) companies remained in the same diversification category. A majority of companies in each diversification category in 1993 remained in the same category in 1998; 12 (86%) single business, 14 (58%) dominant companies, 12 (57%) related diversifiers and 7 (64%) conglomerates. The numbers of companies remaining in the same category in 1993 and 1998 are shown in each of the shaded cells in the above table as they will be in subsequent tables.

Amongst the 25 (36%) companies that changed category 9 (13%) advanced and 16 (23%) retreated in their diversification suggesting a strong trend towards greater focus. Most movements occurred amongst related diversifiers where 8 (38%) reversed (7 to dominant and 1 to single) and only 1 (5%) advanced (1 company became a conglomerate) and conglomerates where 4 (36%) companies reversed (2 to related and 1 each to dominant and single).

The ratios of entries to exits show how the index moved toward greater focus. The entries:exits ratios of the conglomerate, related and dominant categories at 1:5, 8:10 and 5:8 respectively all show more exits than entries which contrasts with the 16:7 ratio in favour of single business company entries.

The following tables show the category movements for the industrial/manufacturing and service companies.

Table 29: FTSE100 Diversification Changes From 1993 To 1998 – Industrial/Manufacturing

		1998						
		Single	Dominant	Related	Conglom.	Exits	Totals	
1993	Single	1	0	0	0	2	3	42
	Dominant	0	2	2	0	3	7	
	Related	1	4	8	1	8	22	
	Conglom	0	0	2	4	4	10	
	Entries	1	1	2	1			
	Totals	3	7	14	6			
		30						

Notes:
Table based on each company's sector in 1993
Net movement (to)/from services not included above 0
BAT Industries entered the single business category having been a service conglomerate in 1993
Scottish & Newcastle exited the related diversifier category becoming a service related diversifier in 1998

Table 30: FTSE100 Diversification Changes From 1993 To 1998 – Services

		1998						
		Single	Dominant	Related	Conglom.	Exits	Totals	
1993	Single	11	2	0	0	5	18	58
	Dominant	4	12	3	1	5	25	
	Related	0	3	4	0	2	9	
	Conglom	1	1	0	3	1	6	
	Entries	15	4	6	0			
	Totals	31	22	13	4			
		70						

Notes:
Table based on each company's sector in 1993
Net movement (to)/from industrial/manufacturing not included above 0
BAT Industries exited the conglomerate category becoming a single business industrial/manufacturing company in 1998.
Scottish & Newcastle entered the related diversifier category having been an industrial/manufacturing related diversifier in 1998.

The tables show similar levels of stability. Excluding exits, 60% of industrial/manufacturing and 67% of services companies remained in the same diversification category and in no category did the number of movements exceed stable companies. Both sectors saw more companies retreat than advance with net movements of 4 (16%) industrial/manufacturing companies (3 advances and 7 retreats) and 3 (7%) service companies (6 advances and 9 retreats). Each sector saw 1 company advance to conglomeration both as a result of an acquisition; industrial/manufacturing company Guinness acquiring Grand Metropolitan to form Diageo and service company North West Water acquiring Norweb to form United Utilities. Both sectors saw 2 companies retreat from conglomeration; industrial/manufacturing companies Williams and Siebe became related diversifiers and service companies BAT Industries/British American Tobacco and Ladbroke/Hilton retreated to the single and dominant business categories respectively.

Table 31: FTSE100 Diversification Changes From 1998 To 2003

		2003					
		Single	Dominant	Related	Conglom.	Exits	Totals
1998	Single	15	5	2	0	12	34
	Dominant	4	16	1	0	8	29
	Related	2	4	9	2	10	27
	Conglom	2	0	2	4	2	10
	Entries	21	6	4	1		
	Totals	44	31	18	7		100

The above table covering the period 1998 to 2003 tells a similar story to that of the preceding 5 years; the prevailing trend is towards focus. Ignoring entries and exits, 44 (65%) companies remained in the same diversification category although, unlike 1993 to 1998 there were significant differences between categories. While 15 (68%) single business and 16 (76%) dominant

business companies remained in the same category only 9 (53%) related diversified companies and 4 (50%) conglomerate companies did not move. Therefore, while overall stability remained broadly the same, that amongst focused categories was greater than that amongst multiple business categories.

The movements reflect a continuing shift towards greater focus with 14 (21%) companies retreating and only 10 (15%) advancing in their diversification. Again conglomerates and related diversifiers led the way back to greater focus with 4 (50%) and 6 (35%) companies respectively reversing their diversification. Of the conglomerates 2 - North West Water/United Utilities and Pearson - took a step back to related diversification while 2 - Granada and Guinness/Diageo - made the 'double jump' back to the single business company category. Only 2 companies - Whitbread and Hays - advanced to conglomeration both related diversifiers.

The ratio of entries to exits was also greatest for the conglomerate and related diversifier categories where exits exceeded entries; conglomerate 1:2 and related diversifier 4:10. This contrasts with ratios of 6:8 and 21:12 for the dominant business and single business categories respectively.

Table 32: FTSE100 Diversification Changes From 1998 To 2003 – Industrial/Manufacturing

		2003						
		Single	Dominant	Related	Conglom.	Exits	Totals	
1998	Single	1	2	0	0	1	4	30
	Dominant	0	6	0	0	1	7	
	Related	1	3	5	0	4	13	
	Conglom	1	0	1	3	1	6	
	Entries	7	3	3	0			
	Totals	10	14	9	3			
		36						

Notes:
Table based on each company's sector in 1998
Net movement (to)/from services not included above 1
Scottish & Newcastle entered the single business category having been a service related diversifier in 1998.

Table 33: FTSE100 Diversification Changes From 1998 To 2003 – Services

		2003						
		Single	Dominant	Related	Conglom.	Exits	Totals	
1998	Single	14	3	2	0	11	30	70
	Dominant	4	10	1	0	7	22	
	Related	1	1	4	2	6	14	
	Conglom	1	0	1	1	1	4	
	Entries	14	3	1	1			
	Totals	34	17	9	4			
		64						

Notes:
Table based on each company's sector in 1998
Net movement (to)/from industrial/manufacturing not included above (1)
Scottish & Newcastle exited related diversifier category becoming a single business service company in 2003.

As between 1993 and 1998, the levels of stability were again similar at 65% for industrial/manufacturing and 64% for service companies. With few exceptions, the majority of companies in each category did not change their diversification strategy. Unlike 1993-1998, there were differences between sectors in the net direction of movements. Industrial/manufacturing companies continued to focus with 6 (26%) retreating and only 2 (9%) advancing while there was a balance in service company movements with the same number of companies - 8 (18%) – retreating and advancing. No industrial/manufacturing

companies advanced to conglomeration but 2 service companies – Hays and Whitbread - advanced to conglomeration both having been related diversifiers.

Table 34: FTSE100 Diversification Changes From 1993 To 2003

		2003					
		Single	Dominant	Related	Conglom.	Exits	Totals
1993	Single	6	3	1	0	11	21
	Dominant	8	10	6	0	8	32
	Related	4	7	5	1	14	31
	Conglom	2	2	1	3	8	16
	Entries	24	9	5	3		
	Totals	44	31	18	7		100

Considering the complete 10 year research period the trend is clearly towards focus as the above table shows. Excluding entries and exits, the net movement is in favour of greater focus with 24 (41%) companies retreating and only 11 (19%) advancing through the Model of Corporate Development. The dynamism of FTSE100 companies is also well illustrated by the fact that only 24 (41%) companies remained in the same diversification category in 2003 as 1993 and only the single business company category had a majority of companies, 6 (60%), with a stable diversification strategy.

In addition to the move toward focus amongst those companies in the FTSE100 throughout the research period, the ratios of entries to exits also suggest focused companies were becoming more commonplace. The entry:exit ratio for single and dominant business categories were in favour of entries at 24:11 and 9:8 respectively while for related diversified and conglomerate categories they were in favour of exits at 5:14 and 3:8.

Table 35: FTSE100 Diversification Changes From 1993 To 2003 – Industrial/Manufacturing

		2003						
		Single	Dominant	Related	Conglom.	Exits	Totals	
1993	Single	0	1	0	0	2	3	42
	Dominant	1	3	1	0	2	7	
	Related	4	5	3	0	10	22	
	Conglom	0	1	1	2	6	10	
	Entries	5	4	4	1			
	Totals	10	14	9	3			
		36						

Notes:
Table based on each company's sector in 1993
Net movement (to)/from services not included above 1
BAT Industries entered the single business category having been a service conglomerate in 1993

Table 36: FTSE100 Diversification Changes From 1993 To 2003 – Services

		2003						
		Single	Dominant	Related	Conglom.	Exits	Totals	
1993	Single	6	2	1	0	9	18	58
	Dominant	7	7	5	0	6	25	
	Related	0	2	2	1	4	9	
	Conglom	2	1	0	1	2	6	
	Entries	19	5	1	2			
	Totals	34	17	9	4			
		64						

Notes:
Table based on each company's sector in 1993
Net movement (to)/from industrial/manufacturing not included above (1)
BAT Industries exited the conglomerate category becoming a single business service company in 2003.

Excluding exits, service companies have shown greater stability; 16 (43%) service companies remained in the same diversification category compared to only 8 (36%) industrial/manufacturing companies. In the conglomerate category 2 industrial/manufacturing companies - Tomkins and Unilever – and 1 service company – Bass/Intercontinental Hotels – were in the category in 1993 and 2003.

The prevailing trend amongst companies in both sectors was towards focus with the greatest movement in the industrial/manufacturing sector. Amongst

industrial/manufacturing companies there was a net movement of 10 (45%) towards focus with 12 (54%) retreats and only 2 (9%) advances while amongst service companies the net movement was 3 (8%) with 12 (32%) retreats and 9 (24%) advances.

The reluctance of companies to take the final step to conglomeration was similar in both sectors. While 2 industrial/manufacturing companies – Hanson and Pearson - retreated to greater focus, none advanced to conglomeration and amongst service companies 3 conglomerates – BAT/British American Tobacco, Granada and Ladbroke/Hilton - retreated and only 1 company – Whitbread - advanced to conglomeration from related diversification.

The entry:exit ratios are in favour of focus rather than multiple business categories in both sectors although industrial/manufacturing ratios are most clear cut. Again, this supports the contention that focus supplanted diversity amongst the FTSE100.

6.2.3 Diversification By FT Classification

The following tables break down tables 25 (all), 26 (industrial/manufacturing) and 27 (services) to show, by FT classification, the number of FTSE100 companies in each diversification category. These analyses seek to identify links between conglomeration and FT classification; do companies in particular classifications have a greater propensity to pursue conglomeration?

Table 37: FTSE100 Diversification Category by FT Classification 1993

FT Classification	Ind/Manu					Services					Total				
	S	D	R	C	Tot	S	D	R	C	Tot	S	D	R	C	Tot
Banks						2	5	2		9	2	5	2		9
Brewers & Distillers			4		4			1	1	2			5	1	6
Building Materials			2	2	4		1			1		1	2	2	5
Business Services							1	1		2		1	1		2
Chemicals			3		3								3		3
Conglomerates				2	2									2	2
Electricity						3	3			6	3	3			6
Electronics			1		1								1		1
Engineering - Aerospace			2		2								2		2
Engineering - General				2	2									2	2
Food Manufacturing		2	1	1	4							2	1	1	4
Food Retailing						4				4	4				4
Health & Household	2	1	3		6						2	1	3		6
Hotels & Leisure			1		1			1	3	4			2	3	5
Insurance Composite							4	1		5		4	1		5
Insurance Life							2			2		2			2
Media			1	1	2		1	1		2		1	2	1	4
Merchant Banks						2				2	2				2
Metals & Metal Forming		1			1							1			1
Mines		1			1							1			1
Miscellaneous									1	1				1	1
Oil & Gas	1	2	1		4		1			1	1	3	1		5
Other Industrials				2	2									2	2
Packaging, Paper & Print			2		2								2		2
Property						2				2	2				2
Stores						3	1	1		5	3	1	1		5
Telephone Networks						1	1	1		3	1	1	1		3
Textiles			1		1								1		1
Transport							2		1	3		2		1	3
Water						1	3			4	1	3			4
Totals	3	7	22	10	42	18	25	9	6	58	21	32	31	16	100

The distribution of FTSE100 companies by category and FT classification shows conglomerates to come from a broad range of classifications. In 1993 there was a 'conglomerates' FT classification but only 2 – Hanson and Tomkins - of the 10 conglomerates in the FTSE100 were included in the classification. It would appear that even in 1993, before the decline in the popularity of conglomerates, there was a marked reluctance for them to allow themselves to be classified as such.

The table shows basic industries, including utilities and mining companies, to be populated by dominant business companies and 'specialist' activities such as financial services to be primarily single and dominant businesses.

Table 38: FTSE100 Diversification Category by FT Classification 1998

	Ind/Manu					Services					Total				
FT Classification	S	D	R	C	Tot	S	D	R	C	Tot	S	D	R	C	Tot
Alcoholic Beverages			1	1	2								1	1	2
Banks, Retail						8	3			11	8	3			11
Breweries, Pubs & Rests						1		2	1	4	1		2	1	4
Chemicals		1	1		2							1	1		2
Electricity						2	4			6	2	4			6
Electronic & Elec. Equip.			1		1								1		1
Engineering		2	1	3	6							2	1	3	6
Engineering, Vehicles		1	1		2							1	1		2
Extractive Industries	1		1		2						1		1		2
Food Processors				1	1									1	1
Food Producers		1	1		2							1	1		2
Gas Distribution							2			2		2			2
Health Care			1		1								1		1
Household Goods & Text		1			1							1			1
Insurance							2	2		4		2	2		4
Investment Trusts						1				1	1				1
Leisure & Hotels							1		1	2		1		1	2
Life Assurance						1	2	1		4	1	2	1		4
Media	1		1	1	3	2		3		5	3		4	1	8
Oil, Integrated		1	1		2							1	1		2
Other Financial						2				2	2				2
Pharmaceuticals	1		2		3						1		2		3
Property						2				2	2				2
Retailers, Food						3	1			4	3	1			4
Retailers, General						2	2			4	2	2			4
Support Services			1		1	2		2		4	2		3		5
Telecommunications						4	1	2		7	4	1	2		7
Tobacco	1				1						1				1
Transport							3	1	1	5		3	1	1	5
Utilities									1	1				1	1
Water							1	1		2		1	1		2
Totals	4	7	13	6	30	30	22	14	4	70	34	29	27	10	100

In addition to showing the number of FTSE100 conglomerates to have fallen from 16 in 1993 to 10 in 1998, the above table shows the engineering classification to have the most conglomerates with 3 companies pursing the strategy compared to only 2 in the classification in 1993. The table also illustrates the shift toward greater focus with 13 more single business companies than in 1993 although the number of dominant business

companies decreased by 3 over the same period. The increase in financial services companies, which are predominantly single or dominant business companies, explains some of the shift.

Table 39: FTSE100 Diversification Category by FT Classification 2003

FT Classification	Ind/Manu					Services					Total				
	S	D	R	C	Tot	S	D	R	C	Tot	S	D	R	C	Tot
Aerospace & Defence		2		1	3							2		1	3
Automobiles & Parts		1			1							1			1
Banks						7	2	1		10	7	2	1		10
Beverages	2	2			4						2	2			4
Chemicals		1	2		3							1	2		3
Construction & Bldg Matls		1			1	1				1	1	1			2
Electricity						1	1			2	1	1			2
Engineering & Machinery				1	1									1	1
Food & Drug Retailers						4				4	4				4
Food Prods & Processors		1	1	1	3							1	1	1	3
General Retailers						3	3			6	3	3			6
Health	1		1		2						1		1		2
Insurance							1			1		1			1
Investment Companies						2				2	2				2
Leisure & Hotels						1	1		2	4	1	1		2	4
Life Assurance						2	1	1	1	5	2	1	1	1	5
Media & Entertainment		1	3		4	4	1			5	4	2	3		9
Mining	1	2	1		4						1	2	1		4
Oil & Gas		1	1		2			1		1		1	2		3
Personal Care & H'hold		1			1							1			1
Pharmaceuticals & Bio.	2	1			3	1				1	3	1			4
Real Estate						2		1		3	2		1		3
Software & Comp Servs	1				1						1				1
Speciality & Other Fin.						1	1	1		3	1	1	1		3
Support Services	1				1	1	1	1	1	4	2	1	1	1	5
Telecommunication Servs						2	1	1		4	2	1	1		4
Tobacco	3				3						3				3
Transport						1	2			3	1	2			3
Utilities (Ex Electricity)							2	2		4		2	2		4
Totals	11	14	9	3	37	33	17	9	4	63	44	31	18	7	100

The move towards greater focus continued from 1998; there were 10 additional single business and 2 additional dominant business companies. Since 1998 both the related diversifier and conglomerate strategies have fewer adherents, down by 9 and 3 respectively. Amongst the conglomerates, engineering accounts for only 1 compared with 3 in 1998.

6.2.4 Breadth of Activities

Having shown in tables 25 (all), 26 (industrial/manufacturing) and 27 (services) a trend towards greater focus in the diversification of FTSE100 companies – both industrial/manufacturing and service - this section considers whether the breadth of activities of companies in each diversification category increased, decreased or remained constant through the research period. Herfindahl indices and the distribution of turnover across activities/groups of related activities and the number of reported activities/groups of related activities have been used to determine the spread of each company's activities.

Table 40: FTSE100 Average Herfindahl Indices By Diversification Category

Category	1993	1998	2003
Single	0.98	0.99	0.99
Dominant	0.73	0.71	0.74
Related	0.42	0.44	0.43
Conglomerate	0.36	0.35	0.44
All	0.63	0.70	0.77

Table 41: FTSE100 Average Percentage Turnover Generated by the Largest Reported Activity and Largest Related Group of Reported Activities By Diversification Category

Category	Largest Activity			Largest Related Group		
	1993	1998	2003	1993	1998	2003
Single	98.9	99.4	99.3	99.9	99.9	99.7
Dominant	83.6	82.4	84.4	98.0	95.7	95.4
Related	53.3	54.7	56.1	93.2	95.5	95.4
Conglomerate	46.0	44.5	55.5	52.5	50.8	58.1
All	71.4	76.9	83.8	89.6	92.6	94.7

The increases in the overall Herfindahl index from 0.63 to 0.77 and in the percentages of turnover generated by the largest activity and related group of activities suggest a narrowing of the activities of FTSE100 companies. However, the averages of the single, dominant and related diversified

categories remained broadly constant throughout the research period while those of the conglomerate category all increased; Herfindahl from 0.36 to 0.44, largest activity turnover from 46.0% to 55.5% and largest related group turnover from 52.5% to 58.1%. These averages suggest that conglomerates have narrowed their activities but that companies in other categories have not. The increases in overall averages reflect the narrowing of conglomerate activities and the migration of companies to more focused categories over the research period.

Table 42: FTSE100 Average Herfindahl Indices By Diversification Category – Industrial/Manufacturing

Category	1993	1998	2003
Single	1.00	1.00	1.00
Dominant	0.66	0.69	0.72
Related	0.40	0.44	0.43
Conglomerate	0.37	0.35	0.40
All Non-Service	0.48	0.56	0.71

Table 43: FTSE100 Average Percentage Turnover Generated by the Largest Reported Activity and Largest Related Group of Reported Activities By Diversification Category – Industrial/Manufacturing

Category	Largest Activity			Largest Related Group		
	1993	1998	2003	1993	1998	2003
Single	100.0	100.0	99.9	100.0	100.0	100.0
Dominant	77.8	80.8	83.0	99.0	94.9	96.7
Related	51.1	54.7	56.8	92.6	97.9	92.7
Conglomerate	48.8	44.9	52.8	49.2	52.1	56.5
All Non-Service	58.5	64.8	79.2	83.9	88.3	93.5

The trends indentified amongst the industrial/manufacturing companies are more pronounced than those of the FTSE100 as a whole with the average Herfindahl index increasing from 0.48 to 0.71. While the conglomerate Herfindahl did increase it was only from 0.37 to 0.40, a change matched by the related diversified category. The largest change was in the dominant business category which saw its Herfindahl increase from 0.66 to 0.72. The

single business category remained constant at 1.00. Similar changes to those in Herfindahl indices were seen in the distributions of turnover across activities and, to a lesser extent, groups of related activities. Given the relatively small reductions in the breadth of dominant, related diversified and conglomerate activities, the comparatively large increases in the overall Herfindahl index were driven by the significant shift away from diversification as evidenced by the greater number of FTSE100 companies in focused categories in 2003.

Table 44: FTSE100 Average Herfindahl Indices By Diversification Category – Services

Category	1993	1998	2003
Single	0.97	0.99	0.98
Dominant	0.76	0.72	0.75
Related	0.47	0.43	0.44
Conglomerate	0.33	0.35	0.47
All Service	0.73	0.76	0.81

Table 45: FTSE100 Average Percentage Turnover Generated by the Largest Reported Activity and Largest Related Group of Reported Activities By Diversification Category – Services

Category	Largest Activity			Largest Related Group		
	1993	1998	2003	1993	1998	2003
Single	98.7	99.3	99.1	99.9	99.9	99.6
Dominant	85.2	83.0	85.5	97.7	95.9	94.4
Related	58.6	54.8	55.3	94.8	93.2	98.1
Conglomerate	41.2	43.9	57.5	57.9	48.9	59.2
All Service	80.7	82.1	86.6	93.8	94.4	95.4

In common with the preceding tables showing data for industrial/manufacturing companies, the overall average Herfindahl indices of service companies increased from 0.73 in 1993 to 0.81 in 2003. There were also increases in the turnover generated by the largest activity and group of related of activities. The conglomerate category showed the highest increases with its Herfindahl rising from 0.33 to 0.47 and the turnover generated by the largest activity increasing from 41.2% to 57.5%. While this was a driver of the

increase in overall averages, the movement towards greater focus will again have caused much of the change.

In addition to the analyses detailed above, the average number of activities and groups of related activities reported by companies was also calculated and reviewed. There has been a reduction in the average number of activities and groups of related activities reported by most categories of company. Conglomerates showed the largest falls from 4.6 activities and 3.4 related groups in 1993 to 3.3 activities and 2.4 related groups in 2003. Other falls were relatively small. This provides further support for the contention that conglomerates have narrowed the breadth of their activities.

The movements identified in this section strongly support the contention that, in addition to a shift towards focus in the categorisation of the FTSE100, conglomerates, especially in the service sector, have narrowed the breadth of their activities.

6.2.5 Performance

The following tables summarise key average performance indicators of companies within each diversification category as per tables 25 (all), 26 (industrial/manufacturing) and 27 (services). The performance reviews were undertaken to see if performance was a clear driver of changes in diversification across the FTSE100. This investigation into performance was the first stage in a process to gain an understanding of the drivers behind changes in diversification.

As DataStream financial data was not available for all companies for all relevant time periods, the number of companies in each year and category for which complete data was available is noted in the final column of each table. The maximum number is 100.

In addition to the performance indicators shown in the tables a number of others including operating margin, price/earnings ratios and operating cash flows were calculated and reviewed to see if any trends could be discerned. Tests, using Pearson's coefficients, for correlations between breadth of activities and a number of performance variables were also undertaken. While a few isolated correlations were found, there were no consistent significant relationships between performance and diversification. That is not to say no such relationships exist but rather that they could not be found using the information that was available from DataStream and the Financial Times.

Table 46: FTSE100 Average Performance By Diversification Category

	Year End		12 mnth Share Volatility (%)	Bal Sheet Date MV/Book Ex Intan.	2 Year Averages (Unweighted)		Number Of Companies Max 100
	Ave Herfindahl Index	Market Capital'n £m			ROCE (%)	Gearing (%)	
1993							
Single	0.98	4,279	70.4	2.3	16.3	31.0	18
Dominant	0.74	5,434	56.3	3.1	14.8	32.2	28
Related	0.42	5,473	47.1	9.1	16.6	37.8	31
Conglomerate	0.37	5,582	43.6	3.6	17.8	40.9	14
All	0.62	5,242	54.0	5.1	16.2	35.2	91
1998							
Single	0.98	11,747	96.8	37.6	15.3	49.5	20
Dominant	0.71	9,203	74.8	7.4	14.6	36.5	27
Related	0.44	12,900	76.5	16.1	27.0	36.0	20
Conglomerate	0.36	7,421	84.0	7.0	31.7	36.9	5
All	0.69	10,813	82.0	18.2	19.4	40.0	72
2003							
Single	0.98	9,281	71.0	5.4	1.8	43.6	30
Dominant	0.74	15,939	76.2	4.5	16.5	40.0	23
Related	0.45	23,096	46.7	3.2	12.0	40.1	12
Conglomerate	0.44	3,088	63.3	33.5	22.3	31.9	5
All	0.77	13,395	68.0	6.7	9.9	41.0	70

The average performance of FTSE100 conglomerates varies considerably through the research period but does not appear to differ markedly from that of other categories except in ROCE which is consistently higher for conglomerates. However, the standard deviation of the average ROCE also increased, especially in the conglomerate category, implying a wider range of performance. As the breadth of conglomerate activities narrowed, as reflected in a higher Herfindahl index, the average market capitalisation has fallen relative to other categories; in 1993 the average market capitalisation of conglomerates was, by a narrow margin, the highest but by 2003 it was by far the lowest.

Share price volatility, which may be an indicator of corporate stability, has risen in most categories. Conglomerates were most stable in 1993 but in 2003

only the related category had lower volatility. This is in contrast to the Market Value/Book Value Excluding Intangibles ratio which, notwithstanding distortions caused by a few extreme values in 1998 and 2003, improved across all categories, excluding related diversifiers, although 1998 figures were higher than 2003.

In terms of returns on capital employed, there was little difference between the performance of conglomerates and other categories in 1993 but by 1998 the multiple business categories – related diversifiers and conglomerates – were achieving returns significantly higher than those of focused categories and by 2003, the conglomerate category had by far the highest ROCE. The gearing of conglomerates appears similar to that of other categories. Comparison of the performance of conglomerates with and without a core activity showed neither group to consistently outperform the other.

The following tables show the average performance by diversification category of industrial/manufacturing and service companies. In broad terms, the performance of both groups mirrors that of the FTSE100 as a whole although, in terms of ROCE, service conglomerates consistently underperform their industrial/manufacturing counterparts.

Table 47: FTSE100 Average Performance By Diversification Category – Industrial/Manufacturing

	Year End		12 mnth	Bal Sheet	2 Year Averages (Unweighted)		Number
	Ave Herfindahl Index	Market Capital'n £m	Share Volatility (%)	Date MV/Book Ex Intan.	ROCE (%)	Gearing (%)	Of Companies
1993							
Single	1.00	3,954	48.4	3.6	23.5	32.8	2
Dominant	0.64	6,128	54.9	2.4	12.5	30.6	6
Related	0.40	4,495	48.4	11.9	18.2	37.9	22
Conglomerate	0.37	5,315	42.2	4.3	20.2	41.9	10
All	0.46	4,918	47.8	8.2	18.1	37.6	40
1998							
Single	1.00	8,302	77.5	553.4	18.4	72.4	1
Dominant	0.70	10,265	68.8	3.3	15.5	31.4	6
Related	0.46	14,343	74.4	16.7	28.0	34.3	9
Conglomerate	0.33	9,321	87.5	10.3	45.1	33.0	3
All	0.54	11,944	74.9	39.7	26.3	35.2	19
2003							
Single	1.00	13,825	68.0	19.6	12.9	26.7	6
Dominant	0.69	18,122	71.9	17.3	18.9	38.0	9
Related	0.43	31,651	45.2	14.0	11.6	21.6	4
Conglomerate	0.39	2,892	58.1	13.4	24.6	36.1	2
All	0.70	18,021	64.4	16.9	16.3	31.5	21

Table 48: FTSE100 Average Performance By Diversification Category – Services

	Year End		12 mnth	Bal Sheet	2 Year Averages (Unweighted)		Number
	Ave Herfindahl Index	Market Capital'n £m	Share Volatility (%)	Date MV/Book Ex Intan.	ROCE (%)	Gearing (%)	Of Companies
1993							
Single	0.98	4,320	73.1	2.1	15.4	30.8	16
Dominant	0.77	5,245	56.7	3.2	15.5	32.7	22
Related	0.47	7,864	44.1	2.5	12.6	37.5	9
Conglomerate	0.38	6,249	47.3	1.7	11.7	38.4	4
All	0.75	5,496	58.9	2.6	14.6	33.4	51
1998							
Single	0.98	11,929	97.8	10.4	15.1	48.3	19
Dominant	0.72	8,900	76.5	8.6	14.4	37.9	21
Related	0.43	11,720	78.1	15.6	26.1	37.4	11
Conglomerate	0.41	4,571	78.7	2.0	11.7	42.9	2
All	0.74	10,408	84.6	10.5	17.0	41.7	53
2003							
Single	0.98	8,145	71.7	16.4	(0.9)	47.9	24
Dominant	0.77	14,536	79.0	16.6	14.9	41.3	14
Related	0.47	18,818	47.5	12.8	12.2	49.4	8
Conglomerate	0.48	3,218	66.8	21.3	20.8	29.0	3
All	0.80	11,412	69.5	16.2	7.1	45.1	49

6.2.6 Corporate Governance

The tables on the following pages illustrate the key corporate governance characteristics of the companies that comprised the FTSE100 in 1993, 1998 and 2003. The categorisations are as per tables 25 (all), 26 (industrial/manufacturing) and 27 (services). The tables should be considered in the context of the improvements in corporate governance driven by the introduction of enhanced Best Practice. The tables show no appreciable differences between the corporate governance of industrial/manufacturing and service companies.

The average percentage of non-executive directors sitting on boards increased through the research period across all companies and sectors while the average tenure of both non-executive and executive directors remained broadly constant. While only dominant business companies had a majority of NEDs in 1993, by 1998 only conglomerates were marginally short of that mark and by 2003 all categories had around 60% NEDs.

The average percentage of chairmen that were non-executive directors increased significantly through the period with the largest increase seen between 1998 and 2003. The tenure of chairmen remained broadly constant but their length of service as a director, i.e. including service pre-chairmanship, reduced suggesting an increased willingness to appoint chairmen from outside the company.

The tenure and length of service of chief executives remained broadly constant through the period and across companies/sectors. However, consistent with the move away from executive chairmen and away from unitary leadership, the number of companies without a CEO fell through the period and across sectors. Overall, the number of companies without a CEO fell from 22 to 9 with the largest fall in the conglomerate category. In 2003 only Unilever out of 7 conglomerates was without a chief executive and that was because the company had multiple, product based, managing directors.

The average aggregate percentage of ordinary shares held by major shareholders with notifiable interests, i.e. over 3%, increased from 12.6% in 1993 to 14.5% in 1998 and 19.3% in 2003 with the largest increases being seen in companies within the related and conglomerate categories where holdings increased from 9.6% to 20.4% and 8.0% to 16.7% respectively suggesting institutional investors looked on conglomerates increasingly favourably.

The analyses suggest all categories of company have tried to improve their corporate governance in line with Best Practice and that there are no clear differences between categories. The most striking changes are in the size of major shareholdings in conglomerates.

Table 49: FTSE100 Corporate Governance by Diversification Category

All Averages	Board			Chair			CEO		No. of Companies		Major
	NED (%)	NED (yrs)	ED (yrs)	NED %	Tenure(yrs)	Director(yrs)	Tenure(yrs)	Director(yrs)	Total	No CEO	S'holds (%)
1993											
Single	46.7	8	6	33.3	4	12	4	7	21	9	22.3
Dominant	54.8	6	5	56.3	4	10	3	6	32	4	11.4
Related	49.3	5	5	35.5	4	11	3	7	31	4	9.6
Conglomerate	42.6	6	7	43.8	7	17	4	8	16	5	8.0
All	49.4	6	5	43.0	5	12	3	7	100	22	12.6
1998											
Single	58.2	5	6	55.9	5	10	3	7	34	6	19.2
Dominant	56.5	5	5	62.1	5	11	3	6	29	4	15.2
Related	53.9	4	6	59.3	6	11	4	7	27	1	9.1
Conglomerate	46.8	5	7	20.0	5	12	3	5	10	2	10.8
All	55.4	5	6	55.0	5	11	3	6	100	13	14.5
2003											
Single	60.5	4	6	72.7	6	10	4	7	44	6	21.2
Dominant	63.8	5	5	83.9	4	8	3	7	31	2	16.5
Related	62.1	5	5	77.8	3	8	4	8	18	0	20.4
Conglomerate	59.7	4	4	85.7	3	6	3	6	7	1	16.7
All	61.7	5	5	78.0	4	9	4	7	100	9	19.3

Table 50: FTSE100 Corporate Governance by Diversification Category – Industrial/Manufacturing

All Averages	Board			Chair			CEO		No. of Companies		Major
	NED (%)	NED (yrs)	ED (yrs)	NED %	Tenure(yrs)	Director(yrs)	Tenure(yrs)	Director(yrs)	Total	No CEO	S'holds (%)
1993											
Single	39.5	4	4	0.0	3	13	0	2	3	2	26.8
Dominant	51.1	9	6	28.6	5	15	1	4	7	2	16.0
Related	47.4	5	5	22.7	4	12	3	6	22	3	10.3
Conglomerate	44.3	7	7	40.0	7	15	3	5	10	3	9.2
All	46.7	6	6	26.2	5	13	2	6	42	10	12.2
1998											
Single	58.1	2	5	0.0	4	11	2	3	4	2	10.2
Dominant	55.3	7	7	28.6	7	15	1	5	7	2	16.2
Related	54.9	4	6	46.2	5	11	4	6	13	1	8.3
Conglomerate	45.7	5	7	16.7	3	12	1	2	6	1	9.5
All	53.6	5	6	30.0	5	12	2	5	30	6	10.6
2003											
Single	64.9	5	5	90.9	5	9	4	7	11	0	21.3
Dominant	68.5	5	5	92.9	3	8	2	7	14	0	21.0
Related	61.3	5	5	77.8	3	7	6	9	9	0	30.8
Conglomerate	57.4	4	5	66.7	5	10	3	3	3	1	17.0
All	64.8	5	5	86.5	4	8	4	7	37	1	23.2

Table 51: FTSE100 Corporate Governance by Diversification Category – Services

All Averages	Board			Chair			CEO		No. of Companies		Major
	NED (%)	NED (yrs)	ED (yrs)	NED %	Tenure(yrs)	Director(yrs)	Tenure(yrs)	Director(yrs)	Total	No CEO	S'holds (%)
1993											
Single	47.9	8	6	38.9	5	12	2	4	18	7	21.5
Dominant	55.9	5	4	64.0	4	8	3	5	25	2	10.2
Related	53.8	6	5	66.7	3	9	3	6	9	1	7.7
Conglomerate	39.8	5	7	50.0	7	19	3	5	6	2	6.0
All	51.4	6	5	55.2	4	10	3	5	58	12	12.9
1998											
Single	58.2	5	6	63.3	5	10	3	6	30	4	20.4
Dominant	56.9	5	5	72.7	5	9	3	5	22	2	15.0
Related	53.0	5	6	71.4	8	11	4	8	14	0	9.9
Conglomerate	48.3	5	6	25.0	7	12	4	7	4	1	12.7
All	56.2	5	6	65.7	5	10	3	6	70	7	16.2
2003											
Single	59.0	4	6	66.7	6	10	3	6	33	6	21.1
Dominant	59.9	5	5	76.5	4	8	3	6	17	2	12.8
Related	62.9	5	5	77.8	3	8	2	7	9	0	10.0
Conglomerate	61.4	3	4	100.0	2	3	3	6	4	0	16.6
All	59.9	5	5	73.0	5	9	3	6	63	8	17.0

6.2.7 Conglomerates in the FTSE100 Index

The following table lists those FTSE100 companies that were categorised as conglomerates at the end of 1993, 1998 or 2003 and notes changes and their causes. Chapter 7 provides brief histories for each of the conglomerates in the table and tries to explain the drivers behind their change of diversification strategy.

Table 52: FTSE100 Conglomerates in 1993, 1998 & 2003

1993 Company	1993-1998 Change	1998 Company	1998-2003 Change	2003 Company
Bass		Bass		Intercont. Hotels
BAT Industries	To Single			
Blue Circle	MV Exit			
BTR		BTR	Acquired	
Caradon	MV Exit			
	From Related	Diageo	To Single	
Forte	Acquired			
Granada		Granada	To Single	
Hanson	MV Exit			
			From Related	Hays
Ladbroke Grp	To Dominant			
	From Dominant	United Utilities	To Related	
			New Listing	Old Mutual
P&O		P&O	To Related	
Pearson		Pearson	To Related	
Siebe	To Related			
	MV Entry	Smiths Inds		Smiths Group
TI Group	MV Exit			
Tomkins		Tomkins		Tomkins
Unilever		Unilever		Unilever
			From Related	Whitbread
Williams Hldgs	To Related			
16	-6	10	-3	7

Of the 16 conglomerates in the FTSE100 in 1993 only 3 – Bass/Intercontinental Hotels, Tomkins and Unilever – were still pursuing the strategy at the end of 2003.

Between 1993 and 1998, the conglomerate category fell by a net 6 companies; 9 leaving and 3 joining. In addition to 1 company – Forte – being

acquired, 4 conglomerates were displaced from the FTSE100 because of falls in their market capitalisation relative to other companies and 4 others retreated to greater focus; 2 to the related diversified, 1 to the dominant company and 1 to the single business company categories. Of the 3 companies that moved into the category; Guinness/Diageo advanced from the related diversified category and North West Water/United Utilities from the dominant business category following acquisitions and Smiths was a new constituent of the FTSE100.

The movement between 1998 and 2003 was less extensive; the category fell by a net 3 companies with 3 joining and 6 leaving. In addition to 1 company leaving following a merger with another FTSE100 company, 5 companies moved to greater focus; 3 to the related and 2 to the single business categories. The period also saw 1 new listing and 2 related diversified companies broadening their activities to become conglomerates.

These movements suggest an overall trend towards greater focus and this is borne out by changes in the breadth of each conglomerates' activities as measured by the Herfindahl index. The average Herfindahl index of the conglomerate category increased between 1993, 1998 and 2003 suggesting a narrowing of the breadth of activities. This is underlined by the following table which shows the Herfindahl indices of companies categorised as conglomerates in 1993, 1998 and 2003. With the exception of Pearson, the indices of all companies that were conglomerates in more than one period

showed increases between each period suggesting a consistent narrowing of conglomerate activities.

Table 53: Herfindahl Indices of FTSE100 Conglomerates in 1993, 1998 & 2003

Company	Herfindahl Index		
	1993	1998	2003
Bass	0.21	0.29	0.58
BAT Industries	0.50		
Blue Circle	0.48		
BTR	0.21	0.52	
Caradon	0.49		
Forte	0.34		
Granada	0.24	0.30	
Guinness/Diageo		0.32	
Hanson	0.21		
Hays			0.45
Ladbroke/Hilton	0.43		
NWW/United Utilities		0.47	
Old Mutual			0.45
P&O	0.24	0.35	
Pearson	0.48	0.27	
Siebe/Invensys	0.50		
Smiths Industries		0.34	0.30
TI Group	0.35		
Tomkins	0.23	0.28	0.48
Unilever	0.35	0.38	0.41
Whitbread			0.41
Williams Hldgs	0.43		
Conglomerate Average	0.36	0.35	0.44
No. of Conglomerates	16	10	7

When reviewing these indices it should be remembered that they are calculated on data that originated in company segmental reports that may have been 'manipulated' by directors to reduce the number of reported activities to appease investors desire for greater focus and may not be a true reflection of a material change in the portfolio.

6.3 FTSE100 Survivors

Of the 100 companies in the index in 1993 only 54 remained by 2003 and of those several had changed their names to reflect portfolio changes, rebranding or, most often, following acquisitions some of which accounted for exits from the index where two FTSE100 companies were involved.

A prime example of portfolio change driving a name change is BAT Industries which reverted British American Tobacco as it divested its non-tobacco activities including insurance companies Allied Dunbar and Eagle Star. Argyll sought to rebrand itself to better reflect its Safeway supermarket operations while the privatised telephone company British Telecom changed its name to British Telecommunications and then to BT Group following restructurings.

Acquisitions have resulted in the majority of corporate name changes. When Guinness acquired Grand Metropolitan 1997 the enlarged group took the name Diageo and the pharmaceutical company Glaxo changed its name to GlaxoWellcome after acquiring its peer Wellcome in 1995 and again to GlaxoSmithKline in 2001 after merging with SmithKlineBeecham. Lloyds Bank added TSB to its name after acquiring that company in 1995, Zeneca became AstraZeneca after merging with Swedish company Astra in 1999 and Commercial Union became CGU after acquiring General Accident in 1998 and to Aviva in 2000 after adding Norwich Union which had been demutualised in 1997. BP briefly became BP Amoco after acquiring Amoco of the US in 1998 before reverting back to BP, Rentokil became Rentokil Initial after it acquired

Initial Services' parent company, BET, in 1996 and Allied Lyons became Allied Domeq after it acquired the Spanish drinks company Domeq in 1994.

Table 54 shows the 54 companies that were constituents of the FTSE100 in 1993, 1998 and 2003 with conglomerates shown in bold type and any name changes over the 10 year period noted. Chapter 7 – Analysing the Historical Record - discusses each of the FTSE100 Survivors conglomerates and their adoption, maintenance or abandonment of conglomeration over the period from 1993 to 2003.

Table 54: FTSE100 Survivors, 1993-2003 (Name Changes Noted)

1993	1998	2003
Abbey National	Abbey National	Abbey National
Allied Lyons	Allied Domeq	Allied Domeq
Argyll Group	Safeway	Safeway
Associated British Foods	Associated British Foods	Associated British Foods
BAA	BAA	BAA
Barclays Bank	Barclays Bank	Barclays Bank
Bass	**Bass**	**Intercontinental Hotels**
BAT Industries	British American Tobacco	British American Tobacco
BOC Group	BOC Group	BOC Group
Boots	Boots	Boots
BP	BP Amoco	BP
British Aerospace	British Aerospace	BAE Systems
British Airways	British Airways	British Airways
British Gas	BG	BG
British Telecom	British Telecommunications	BT Group
Cable & Wireless	Cable & Wireless	Cable & Wireless
Cadbury Schweppes	Cadbury Schweppes	Cadbury Schweppes
Commercial Union	CGU	Aviva
Glaxo	Glaxo Wellcome	Glaxo SmithKline
Granada	**Granada**	Granada
Guinness	**Diageo**	Diageo
GUS	GUS	GUS
HSBC	HSBC	HSBC
ICI	ICI	ICI
Kingfisher	Kingfisher	Kingfisher
Ladbroke Group	Ladbroke Group	Hilton
Land Securities	Land Securities	Land Securities
Legal & General	Legal & General	Legal & General
Lloyds Bank	Lloyds TSB	Lloyds TSB
Marks & Spencer	Marks & Spencer	Marks & Spencer
North West Water	**United Utilities**	United Utilities
Pearson	**Pearson**	Pearson
Prudential	Prudential	Prudential
Reckitt & Colman	Reckitt & Colman	Reckitt Benckiser
Reed International	Reed International	Reed Elsevier
Rentokil	Rentokil Initial	Rentokil Initial
Reuters	Reuters	Reuters
Rolls-Royce	Rolls-Royce	Rolls-Royce
Royal Bank of Scotland	Royal Bank of Scotland	Royal Bank of Scotland
RTZ	Rio Tinto	Rio Tinto
Sainsbury	Sainsbury	Sainsbury
Schroders	Schroders	Schroders
Scottish & Newcastle	Scottish & Newcastle	Scottish & Newcastle
Scottish Power	Scottish Power	Scottish Power
Severn Trent	Severn Trent	Severn Trent
Shell Transport & Trading	Shell Transport & Trading	Shell Transport & Trading
Standard Chartered	Standard Chartered	Standard Chartered
Sun Alliance	Royal & Sun Alliance	Royal & Sun Alliance
Tesco	Tesco	Tesco
Tomkins	**Tomkins**	**Tomkins**
Unilever	**Unilever**	**Unilever**
Vodafone Group	Vodafone Group	Vodafone Group
Whitbread	Whitbread	**Whitbread**
Zeneca Group	Zeneca Group	AstraZeneca

Note: Conglomerates are in **bold** type

6.3.1 Diversification

Analysis of the diversification categories of the 54 FTSE100 survivors is shown in the following table.

Table 55: FTSE100 Survivors By Diversification Category

	1993		1998		2003	
	No.	%	No.	%	No.	%
Channon/W&M						
Single	10	*18.5*	14	*25.9*	17	*31.5*
Dominant	21	*38.9*	19	*35.2*	20	*37.0*
Sub-Total Focus	31	*57.4*	33	*61.1*	37	*68.5*
Related	16	*29.6*	14	*25.9*	13	*24.1*
Conglomerate	7	*13.0*	7	*13.0*	4	*7.4*
Sub-Total Multiple	23	*42.6*	21	*38.9*	17	*31.5*
Total	54	*100.0*	54	*100.0*	54	*100.0*
Related - Core	12	*22.2*	11	*20.4*	9	*16.7*
% of Related	*75.0*		*78.6*		*69.2*	
Conglomerate - Core	4	*7.4*	2	*3.7*	4	*7.4*
% of Conglomerate	*57.1*		*28.6*		*100.0*	
Hill & Pickering						
Low	38	*70.4*	35	*64.8*	38	*70.4*
Medium	9	*16.7*	9	*16.7*	12	*22.2*
High	7	*13.0*	10	*18.5*	4	*7.4*
Total	54	*100.0*	54	*100.0*	54	*100.0*

The table clearly shows that using both Channon/Whittington & Mayer and Hill & Pickering categorisations, there has been a retreat back from diversification, especially, conglomeration, toward greater focus between 1993 and 2003. Using the Channon/W&M measure, the number of conglomerates fell from 7 (13%) in 1993 to only 4 (7.4%) by 2003 while the corresponding figures for single business companies increased from 10 (18.5%) to 17 (31.5%). The figures for the middle diversification categories – dominant and related – remained broadly constant with 16 (29.6%) related companies in 1993 and 13 (24.1%) in 2003 and 21 (38.9%) dominant companies in 1993 and 20 (37.0%) in 2003. When single and dominant business companies are combined into a

focus category and related diversified and conglomerate companies into a multiple business category the reduction in the multiple category is from 23 (42.6%) companies to 17 (31.5%) with a corresponding increase in focused companies from 31 (57.4%) to 37 (68.5%). The less detailed Hill & Pickering categorisations show broadly the same change with 7 companies (13.0%) classed as highly diversified in 1993 but only 4 (7.4%) in 2003.

However, there is some conflict between Channon/W&M and Hill & Pickering in 1998. Categorisation according to Channon/W&M shows conglomeration in 1998 to have remained constant at the same level as 1993 – 7 companies and 13% - while Hill & Pickering show an increase from 7 to 10 companies or 13% to 18.5%.

The table also shows a consistently high percentage of related companies, around 70%, to have a core activity that generates more than 50% of turnover. This is not surprising given the definition of related diversification, i.e. that there are links between activities. The percentage of conglomerate companies with a core activity varies greatly. In 1993, 4 (57.1%) conglomerates had a core activity but by 1998 the corresponding figure had fallen to only 2 (28.6%). However, by 2003 all four conglomerates had core activities.

The following tables show how diversification had changed through the 10 years of the research period for industrial/manufacturing and service companies.

Table 56: FTSE100 Survivors By Diversification Category – Industrial/Manufacturing

	1993		1998		2003	
	No	%	No.	%	No.	%
Channon/W&M						
Single	1	*5.3*	2	*10.5*	4	*20.0*
Dominant	4	*21.1*	6	*31.6*	9	*45.0*
Sub-Total Focus	5	*26.4*	8	*42.1*	13	*65.0*
Related	11	*57.9*	7	*36.8*	5	*25.0*
Conglomerate	3	*15.8*	4	*21.1*	2	*10.0*
Sub-Total Multiple	14	*73.7*	11	*57.9*	7	*35.0*
Total	19	*100.0*	19	*100.0*	20	*100.0*
Related - Core	7	*36.8*	6	*31.6*	4	*20.0*
% of Related	*63.6*		*85.7*		*80.0*	
Conglomerate - Core	2	*10.5*	1	*5.3*	2	*10.0*
% of Conglomerate	*66.7*		*25.0*		*100.0*	
Hill & Pickering						
Low	11	*57.9*	12	*63.2*	12	*60.0*
Medium	5	*26.3*	3	*15.8*	6	*30.0*
High	3	*15.8*	4	*21.1*	2	*10.0*
Total	19	*100.0*	19	*100.0*	20	*100.0*

Table 57: FTSE100 Survivors By Diversification Category – Services

	1993		1998		2003	
	No	%	No.	%	No.	%
Channon/W&M						
Single	9	*25.7*	12	*34.3*	13	*38.2*
Dominant	17	*48.6*	13	*37.1*	11	*32.4*
Sub-Total Focus	26	*74.3*	25	*71.4*	24	*70.6*
Related	5	*14.3*	7	*20.0*	8	*23.5*
Conglomerate	4	*11.4*	3	*8.6*	2	*5.9*
Sub-Total Multiple	9	*25.7*	10	*28.6*	10	*29.4*
Total	35	*100.0*	35	*100.0*	34	*100.0*
Related - Core	5	*14.3*	5	*14.3*	5	*14.7*
% of Related	*100.0*		*71.4*		*62.5*	
Conglomerate - Core	2	*5.7*	1	*2.9*	2	*5.9*
% of Conglomerate	*50.0*		*33.3*		*100.0*	
Hill & Pickering						
Low	27	*77.1*	23	*65.7*	26	*76.5*
Medium	4	*11.4*	6	*17.1*	6	*17.6*
High	4	*11.4*	6	*17.1*	2	*5.9*
Total	35	*100.0*	35	*100.0*	34	*100.0*

Both service and industrial/manufacturing sectors show a similar reduction in the number and percentage of conglomerate companies between 1993 and 2003 although there is an increase amongst industrial/manufacturing companies in 1998. Interestingly, while the industrial/manufacturing sector shows a consistent and substantial reduction in related diversification from 57.9% in 1993 to 36.8% in 1998 and 25.0% in 2003, the trend amongst service companies is in the opposite direction rising from 14.3% to 20% and 23.5%.

Overall, multiple business companies – conglomerate and related diversified - amongst service companies remain broadly constant at between 25.7% and 29.4% while amongst industrial/manufacturing companies they more than halve from 73.7% to only 35.0%. While this suggests the retreat toward focus is far greater amongst industrial/manufacturing companies it should be noted that the starting points in 1993 were very different, 73.7% compared to 25.7% giving the industrial/manufacturing sector more scope for focusing.

Amongst industrial/manufacturing companies the reduction in multiple business companies is offset by an increase in focused companies, especially single business companies which increased from only 5.3% in 1993 to 10.5% in 1998 and 20.0% in 2003. Amongst service companies, while the relative stability in multiple business companies is matched by that in focused business companies the number of single business companies increased from 25.7% to 38.2% while that of dominant business companies decreased from 48.6% to 32.4%.

These tables provide only 'high level' information on the categorisations of the 54 FTSE100 survivors. They do not show how dynamic companies have been or how radical their changes in diversification strategy have been.

6.3.2 Category Changes

By looking at the movements between categories from 1993 to 2003 and in the sub-periods 1993 to 1998 and 1998 to 2003 it is possible to identify forward and backward movements through the Model of Corporate Development and to see how many companies remained in the same category. This section analyses the movements between categories implicit in tables 55 (all), 56 (industrial/manufacturing) and 57 (services).

Table 58: FTSE100 Survivors Category Changes From 1993 To 1998

		1998				
		Single	Dominant	Related	Conglom.	Totals
1993	Single	9	1	0	0	10
	Dominant	4	11	5	1	21
	Related	0	6	9	1	16
	Conglom.	1	1	0	5	7
	Totals	14	19	14	7	54

The first 5 year period shows 34 (63%) companies to have remained in the same category with single business showing the highest level of stability, 90%, and dominant business companies the lowest, 52% with 71% conglomerate stability. The numbers of companies remaining in the same category in 1993 and 1998 are shown in each of the shaded cells in the above table as they will be in subsequent tables.

Considering the changes in terms of movements through the Model of Corporate Development, the table shows 8 (15%) companies to have

advanced and 12 (22%) to have retreated; a net reversal of 4 (7%) companies. The single business category had least movement with only one company advancing; Sainsbury became a dominant company with the development of its Homebase DIY business. The dominant category showed itself to be a stepping stone within the model; although 11 (52%) companies remained in the category, 4 (19%) retreated to more focus while 6 (29%) advanced to greater diversification, 5 becoming related diversifiers and 1 a conglomerate; North West Water became a conglomerate, renamed United Utilities, through its acquisition of electricity distribution company Norweb. Companies in the related diversified category proved reluctant to take the final step to conglomeration with only 1 company doing so; Guinness acquired another related diversified FTSE100 company, Grand Metropolitan, to form Diageo. In contrast to their reluctance to advance, 6 related companies decided related diversification was a step too far and retreated back to the dominant category. Finally, the conglomerate category saw 2 reversals with 1 company retreating 2 steps to the dominant business and another 3 steps to the single business categories. As neither company took the single step back to related diversification, this suggests their decision to abandon conglomeration was unequivocal.

Table 59: FTSE100 Survivors Category Changes From 1993 To 1998 - Industrial/Manufacturing & Service Sectors

		1998									
		Ind/Manu					Services				
		S	D	R	C	Tot	S	D	R	C	Tot
1993	Single	1	0	0	0	1	8	1	0	0	9
	Dominant	0	2	2	0	4	4	9	3	1	17
	Related	0	4	6	1	11	0	2	3	0	5
	Conglom.	0	0	0	3	3	1	1	0	2	4
	Totals	1	6	8	4	19	13	13	6	3	35

Notes:
Table based on each company's sector in 1993
Net movement from services to industrial/manufacturing 0
Between 1993 and 1998 BAT Industries exited the service conglomerate category becoming an industrial/manufacturing single business company and Scottish & Newcastle exited the industrial/manufacturing related diversifier category becoming a service related diversifier.

Comparing industrial/manufacturing and service sector movements shows each to have the same level of stability; 12 industrial/manufacturing and 22 service companies remained in the same diversification category representing 63% of the 19 industrial/manufacturing and 35 service companies in the 54 company FTSE100 Survivors population. Both sectors showed a shift towards greater focus although the net movements – 1 (3 advances and 4 retreats) amongst industrial/manufacturing companies and 3 (5 advances and 8 retreats) amongst service companies – were not large representing 5% and 9% of sector populations respectively. Amongst conglomerates, the industrial/manufacturing companies showed greatest stability with 3 (100%) companies remaining in the category through the period and they were joined by Guinness/Diageo which advanced from the related diversification category following an acquisition. Of the service conglomerates, 2 (50%) remained in the category and 2 (50%) left; 1 each to the single and dominant business categories. Only 1 company – North West Water/United Utilities – advanced to the conglomerate category having been a dominant business company.

Table 60: FTSE100 Survivors Category Changes From 1998 To 2003

		2003				
		Single	Dominant	Related	Conglom.	Totals
1998	Single	9	3	2	0	14
	Dominant	4	14	1	0	19
	Related	2	3	8	1	14
	Conglom.	2	0	2	3	7
	Totals	17	20	13	4	54

The period between 1998 and 2003 showed almost an identical overall movement to that of the preceding 5 years. In terms of movements through the Model of Corporate Development, the table shows 7 (13.0%) companies advanced, 13 (24.0%) retreated and 34 (63.0%) remained the in the same diversification category. Compared to the preceding 5 year period there was an acceleration in the number of companies abandoning conglomeration; between 1993 and 1998 2 companies entered and 2 left the category but between 1998 and 2003 1 entered while 4 left.

In the single, dominant and related categories the number of companies remaining in the category – 9 (64%) single, 14 (74%) dominant and 8 (57%) related – exceeded the number advancing or retreating. In the conglomerate category only 3 (43%) of the 7 companies identified as conglomerates in 1998 remained in the category in 2003 with 2 retreating to the related category – United Utilities divested a substantial proportion of its electricity activities and Pearson divested its television activities - and a further 2 to the single business category – both Granada and Guinness/Diageo divested their food/catering businesses. Of the 5 single business companies that advanced between 1998 and 2003, 3 became dominant business companies – GlaxoWellcome merged with SmithKline Beecham to form GlaxoSmithKline

with both pharmaceutical (drugs) and healthcare businesses, Schroders added other non-investment banking activities and Vodafone added fixed line telecommunications activities to its global mobile business. Two companies made the 'double jump' to related diversification; HSBC grew its investment banking/capital markets activities and Land Securities added property services to its core property rental/development business.

As in the previous 5 year period there was a reluctance among dominant companies to become related diversifiers with only 1 company – BG (formerly British Gas) adding liquefied natural gas and power generation to its core gas production and distribution business - making that move while 4 retreated to the single business category; Abbey National which reported a refocusing of activities on retail banking, Cable & Wireless which refocused on telecommunications exiting peripheral activities including cable ships and equipment, Sainsbury which sold its Homebase DIY business and Scottish Power which divested its water business. Similarly, companies in the related category were equally as reluctant to become conglomerates with only one of their number making that move - Whitbread which had divested the bulk of its traditional brewing and pubs activities in 2000 and 2001 replacing them with hotel and restaurant activities - while 5 became more focused with 3 becoming dominant business companies – Allied Domeq which had divested its retailing businesses, Reuters where information activities had grown faster than other activities and Rio Tinto where mining and metals had outgrown industrial minerals - and 2 single business companies - Scottish & Newcastle

which, by divesting its retail activities, had become a focused brewer, and AstraZeneca which had divested its agro and specialist chemicals businesses.

Table 61: FTSE100 Survivors Category Changes From 1998 To 2003 - Industrial/Manufacturing & Service Sectors

		2003									
		Ind/Manu					Services				
		S	D	R	C	Tot	S	D	R	C	Tot
1998	Single	1	1	0	0	2	8	2	2	0	12
	Dominant	0	6	0	0	6	4	8	1	0	13
	Related	1	2	4	0	7	1	1	4	1	7
	Conglom.	1	0	1	2	4	1	0	1	1	3
	Totals	3	9	5	2	19	14	11	8	2	35

Notes:
Table based on each company's sector in 1998
Net movement from services to industrial/manufacturing 1
Between 1998 and 2003 Scottish & Newcastle exited the services related diversifier category becoming an industrial/manufacturing single business company.

Comparing industrial/manufacturing and service company movements shows each group to have similar levels of stability; 13 industrial/manufacturing and 21 service companies remained in the same diversification category representing 68% of the 19 industrial/manufacturing and 60% of the 35 service companies in the 54 FTSE100 Survivors population. Both sectors showed companies to have retreated to greater focus; there was a net movement of 4 (1 advance and 5 retreats) amongst industrial/manufacturing companies and 2 (6 advances and 8 retreats) amongst service companies. Amongst conglomerates, industrial/manufacturing companies were again the most stable; 2 (50%) companies remained in the category through the period and 2 companies retreated to the related diversified and dominant business categories. Of the service conglomerates 1 (33%) remained in the category and 2 retreated 1 each to the single business and related diversified

categories. The only advance to conglomeration was made by a related diversified service company, Whitbread.

Table 62: FTSE100 Survivors Category Changes From 1993 To 2003

		2003				
		Single	Dominant	Related	Conglom.	Totals
1993	Single	6	3	1	0	10
	Dominant	6	9	6	0	21
	Related	3	7	5	1	16
	Conglom.	2	1	1	3	7
	Totals	17	20	13	4	54

The above table shows movements over the full 10 year research period. In terms of movements through the Model of Corporate Development, 11 (20%) companies advanced, 20 (37%) retreated and 23 (43%) remained in the same diversification category. The net movement towards focus was 9 (17%). This suggests there was a trend toward greater focus among the 54 companies that were members of the FTSE100 index in 1993, 1998 and 2003.

The single business company category was the most stable. In 1993 there were 10 companies in the category and by 2003 6 (60%) remained with 4 companies having advanced to greater diversification (3 to the dominant business and 1 to the related diversifier categories). Of the 21 dominant business companies in 1993 only 9 (43%) remained by 2003 with the 12 exits from the category split evenly with 6 companies advancing to related diversification and 6 retreating to the single business category. None of the single business or dominant business companies had advanced to conglomeration by 2003 although 1 of the 16 companies categorised as related diversifiers in 1993 had done so. Of the other 15 related diversifiers, 5 (31%) remained in the category while 10 (63%) retreated, 7 becoming

dominant and 3 single business companies. Finally, 3 (43%) of the 1993 conglomerates remained in that category with 4 having retreated towards greater focus, 1 becoming a related diversifier, 1 a dominant business company and 2 single business companies.

The net reduction of 3 (43%) conglomerates with only one company – Whitbread – advancing to the category through the 10 year period strongly supports the contention that, in addition to a broader trend towards focus, there was a significant move away from conglomeration. Only 1 (2%) of the 47 companies that were in the single business, dominant business or related diversified categories in 1993 managed to reach the conglomerate category by 2003 while 4 (57%) of the 1993 conglomerates abandoned the category over the same period.

When looked at in terms of focussed (single and dominant) and multiple (related and conglomerate) categories the trend to remain within the same group is even more pronounced; of the 31 companies categorised as focussed in 1993 only 7 moved into the multiple business category (all related) by 2003 while of the 23 companies in the multiple category in 1993, 13 retreated back towards greater focus. 24 (77%) of the 1993 focussed companies remained in that group in 2003 and 10 (43%) of the multiple business companies remained as such in 2003.

Table 63: FTSE100 Survivors Category Changes From 1993 To 2003 - Industrial/Manufacturing & Service Sectors

		2003									
		Ind/Manu					Services				
		S	D	R	C	Tot	S	D	R	C	Tot
1993	Single	0	1	0	0	1	6	2	1	0	9
	Dominant	0	3	1	0	4	6	6	5	0	17
	Related	3	5	3	0	11	0	2	2	1	5
	Conglom.	0	0	1	2	3	2	1	0	1	4
	Totals	3	9	5	2	19	14	11	8	2	35

Notes:
Table based on each company's sector in 1993
Net movement from services to industrial/manufacturing 1
Between 1993 and 2003 BAT Industries exited the service conglomerate category becoming an industrial/manufacturing single business company.

Over the 10 year period both sectors showed very similar levels of stability with 8 (42%) industrial/manufacturing companies and 15 (43%) service companies remaining in the same category in 1993 and 2003. While both sectors showed a trend toward greater focus, there was a net movement of 7 (37%) industrial/manufacturing companies compared to only 2 (6%) service companies. Amongst conglomerates, 2 (66%) industrial/manufacturing companies remained in the category with 1 company – Pearson - retreating to related diversification and no companies joining the category. There was more movement in the service company conglomerate category with one 1 (25%) company remaining in the category, 3 companies retreating to more focus – 2 becoming single business companies and 1 a dominant business company – and 1 related diversified company, Whitbread, advancing to the category.

6.3.3 Diversification By FT Classification

The following tables break down tables 55 (all), 56 (industrial/manufacturing) and 57 (services) to show, by FT classification, the number of FTSE100

Survivors in each diversification category. These analyses seek to identify links between conglomeration and FT classification; do companies in particular classifications have a greater propensity to pursue conglomeration?

Table 64: FTSE100 Survivors Diversification Category by FT Classification 1993

FT Classification	Ind/Manu					Services					Total				
	S	D	R	C	Tot	S	D	R	C	Tot	S	D	R	C	Tot
Banks						1	4	1		6	1	4	1		6
Brewers & Distillers			3		3			1	1	2			4	1	5
Business Services							1			1		1			1
Chemicals			2		2								2		2
Conglomerates				1	1									1	1
Electricity							1			1		1			1
Engineering - Aerospace			2		2								2		2
Food Manufacturing		1	1	1	3							1	1	1	3
Food Retailing						3				3	3				3
Health & Household	1		2		3						1		2		3
Hotels & Leisure									2	2				2	2
Insurance Composite							1	1		2		1	1		2
Insurance Life							2			2		2			2
Media			1	1	2		1			1		1	1	1	3
Merchant Banks						1				1	1				1
Mines		1			1							1			1
Miscellaneous									1	1				1	1
Oil & Gas		2			2		1			1		3			3
Property						1				1	1				1
Stores						2	1	1		4	2	1	1		4
Telephone Networks						1	1	1		3	1	1	1		3
Transport							2			2		2			2
Water							2			2		2			2
Totals	1	4	11	3	19	9	17	5	4	35	10	21	16	7	54

The above table shows conglomerates to have been in a broad range of FT classifications; only hotels and leisure had 2 conglomerates - Granada and Ladbroke Group. Companies in the utilities (water and electricity), mining (mines and oil & gas) and financial services (banks and insurances) classifications were predominantly dominant business companies. Half of the 10 single business companies were retailers; 3 food retailers (Argyll Group, Sainsbury and Tesco) and 2 stores (Boots and Kingfisher). Only one company - Tomkins – was actually quoted in the conglomerates classification.

Table 65: FTSE100 Survivors Diversification Category by FT Classification 1998

FT Classification	Ind/Manu					Services					Total				
	S	D	R	C	Tot	S	D	R	C	Tot	S	D	R	C	Tot
Alcoholic Beverages			1	1	2								1	1	2
Banks, Retail						4	2			6	4	2			6
Breweries, Pubs & Rests								2	1	3			2	1	3
Chemicals		1	1		2							1	1		2
Electricity							1			1		1			1
Engineering		2		1	3							2		1	3
Extractive Industries			1		1								1		1
Food Processors				1	1									1	1
Food Producers		1	1		2							1	1		2
Gas Distribution							1			1		1			1
Household Goods & Text		1			1							1			1
Insurance							1	1		2		1	1		2
Leisure & Hotels							1		1	2		1		1	2
Life Assurance						1	1			2	1	1			2
Media			1	1	2			1		1			2	1	3
Oil, Integrated		1	1		2							1	1		2
Other Financial						1				1	1				1
Pharmaceuticals	1		1		2						1		1		2
Property						1				1	1				1
Retailers, Food						2	1			3	2	1			3
Retailers, General						2	2			4	2	2			4
Support Services								1		1			1		1
Telecommunications						1	1	1		3	1	1	1		3
Tobacco	1				1						1				1
Transport							2			2		2			2
Utilities									1	1				1	1
Water								1		1			1		1
Totals	2	6	7	4	19	12	13	7	3	35	14	19	14	7	54

By 1998 no classification had more than one conglomerate and the separate conglomerate classification had been withdrawn. As in 1993, utility and mining companies were predominantly dominant business companies but banks had reduced their focus with 4 (HSBC, Lloyds TSB, Royal Bank of Scotland and Standard Chartered) categorised as single business companies and 2 (Abbey National and Barclays) as dominant business companies. As with 1993, retailers – food and general – accounted for 4 (Safeway (formerly Argyll), Kingfisher, Marks & Spencer and Tesco) of the single business companies.

Table 66: FTSE100 Survivors Diversification Category by FT Classification 2003

FT Classification	Ind/Manu					Services					Total				
	S	D	R	C	Tot	S	D	R	C	Tot	S	D	R	C	Tot
Aerospace & Defence		2			2							2			2
Banks						4	1	1		6	4	1	1		6
Beverages	2	1			3						2	1			3
Chemicals		1	1		2							1	1		2
Electricity						1				1	1				1
Engineering & Machinery				1	1									1	1
Food & Drug Retailers						3				3	3				3
Food Prods & Processors		1	1	1	3							1	1	1	3
General Retailers						2	2			4	2	2			4
Insurance							1			1		1			1
Leisure & Hotels							1		2	3		1		2	3
Life Assurance						1	1	1		3	1	1	1		3
Media & Entertainment			2		2	1	1			2	1	1	2		4
Mining		1			1							1			1
Oil & Gas		1	1		2			1		1		1	2		3
Personal Care & H'hold		1			1							1			1
Pharmaceuticals & Bio.	1	1			2						1	1			2
Real Estate								1		1			1		1
Speciality & Other Fin.							1			1		1			1
Support Services								1		1			1		1
Telecommunication Servs						1	1	1		3	1	1	1		3
Tobacco	1				1						1				1
Transport							2			2		2			2
Utilities (Ex Electricity)								2		2			2		2
Totals	4	9	5	2	20	13	11	8	2	34	17	20	13	4	54

The classification/categorisation table for 2003 is notable for the reduction in the number of conglomerates, down from 7 in 1993 and 1998 to only 4 of which 2 – Bass/Intercontinental Hotels and Whitbread – were in the hotels & leisure classification. The broad distribution of categories across classifications remains comparable with 1998 with banks and retailers – food and drug and general – accounting for 9 of the single business companies.

The table shows 2 single business companies - Guinness/Diageo and Scottish & Newcastle – in the beverages classification. Both of these companies had refocused between 1993 and 2003. Guinness/Diageo had been a conglomerate in 1998 after its creation by Guinness's acquisition of

Grand Metropolitan, both related diversifiers, in 1997 and Scottish & Newcastle had been a related diversifier in 1993 and 1998 before divesting its public house/retailing activities to become focused on brewing by 2003.

6.3.4 Breadth of Activities

Having shown in tables 55 (all), 56 (industrial/manufacturing) and 57 (services) a trend towards greater focus in the diversification of FTSE100 Survivors companies – both industrial/manufacturing and service - this section considers whether the breadth of activities of companies in each diversification category increased, decreased or remained constant through the research period. Herfindahl indices and the distribution of turnover across activities/related activities and the number of activities/related activities have been used to determine the spread of each company's activities.

Table 67: FTSE100 Survivors Average Herfindahl Indices By Diversification Category

Category	1993	1998	2003
Single	0.98	0.98	0.98
Dominant	0.73	0.69	0.73
Related	0.46	0.44	0.42
Conglomerate	0.35	0.33	0.47
All	0.65	0.65	0.72

Table 68: FTSE100 Survivors Average Percentage Turnover Generated by the Largest Reported Activity and Largest Related Group of Reported Activities By Category

	% Largest Activity			% Largest Related Group		
Category	1993	1998	2003	1993	1998	2003
Single	99.1	98.9	99.0	99.9	99.7	99.6
Dominant	83.8	80.8	84.0	97.0	93.4	94.7
Related	57.8	56.2	54.2	94.6	94.7	95.8
Conglomerate	45.7	41.7	61.2	53.5	49.6	62.2
All	74.0	74.0	79.8	91.2	89.7	94.1

The increase in the overall average Herfindahl index from 0.65 to 0.72 and in the percentage of turnover generated by the largest activities and related group of activities suggest a narrowing of the activities of FTSE100 Survivors. However, the averages of the single, dominant and related categories remained broadly constant throughout the research period while of the conglomerate category all increased; Herfindahl from 0.35 to 0.47, largest activity turnover from 45.7% to 61.2% and largest related group turnover from 53.5% to 62.2%. These averages suggest that conglomerates have narrowed their activities but companies in other categories have not. The increases in overall averages reflect the narrowing of conglomerate activities and the migration of companies to more focused categories over the research period.

Table 69: FTSE100 Survivors Average Herfindahl Indices By Diversification Category - Industrial/Manufacturing

Category	1993	1998	2003
Single	1.00	1.00	1.00
Dominant	0.63	0.68	0.74
Related	0.43	0.47	0.42
Conglomerate	0.35	0.31	0.45
All	0.49	0.56	0.68

Table 70: FTSE100 Survivors Average Percentage Turnover Generated by the Largest Reported Activity and Largest Related Group of Reported Activities By Category – Industrial/Manufacturing

	% Largest Activity			% Largest Related Group		
Category	1993	1998	2003	1993	1998	2003
Single	100.0	100.0	100.0	100.0	100.0	100.0
Dominant	76.2	80.3	84.4	98.3	94.1	95.0
Related	53.9	57.4	55.1	93.7	100.0	92.6
Conglomerate	48.6	40.6	60.2	49.4	51.4	60.6
All Non-Service	60.2	65.6	77.8	88.0	87.9	92.0

The trends identified amongst the manufacturing/industrial companies are similar changes to those of the total FTSE100 Survivors population with the exception that the dominant business category has shown changes similar to

those of the conglomerate category. Single business companies appear to be exactly that with an average Herfindahl index at its maximum value of 1 while the related diversified category remains broadly unchanged. The dominant company index shows an increase from 0.63 in 1993 to 0.74 by 2003 and the conglomerate category an increase from 0.35 to 0.45 suggesting companies in both categories have narrowed their activities. Similar changes to those in average Herfindahl indices were seen in the distributions of turnover across activities and groups of related activities. Given the relatively small reductions in the breadth of dominant business and conglomerate companies, the comparatively large increase from 0.49 to 0.68 in the overall Herfindahl index was also driven by the significant shift away from diversification as evidenced by the greater number of FTSE100 Survivors in focused categories in 2003.

Table 71: FTSE100 Survivors Average Herfindahl Indices By Diversification Category – Services

Category	1993	1998	2003
Single	0.98	0.97	1.00
Dominant	0.76	0.70	0.74
Related	0.53	0.42	0.42
Conglomerate	0.34	0.35	0.45
All	0.74	0.71	0.68

Table 72: FTSE100 Survivors Average Percentage Turnover Generated by the Largest Reported Activity and Largest Related Group of Reported Activities By Category – Services

	% Largest Activity			% Largest Related Group		
Category	1993	1998	2003	1993	1998	2003
Single	99.0	98.7	98.6	99.8	99.7	99.4
Dominant	85.5	81.0	83.6	96.6	93.1	94.5
Related	66.3	55.0	53.7	96.6	89.4	97.8
Conglomerate	43.6	43.2	62.1	56.6	47.2	63.9
All Service	81.5	78.6	81.0	92.9	90.7	95.4

The pattern of change amongst service companies differs from those of the manufacturing/industrial sector. As with industrial/manufacturing companies,

the breadth of conglomerate activities narrowed as evidenced by an increase from 0.34 to 0.45 in the average Herfindahl index and from 43.6% to 62.1% in turnover generated by the largest activity. However, in contrast to the industrial/manufacturing sector, the average Herfindahl of the related diversified category decreased suggesting companies in that group had increased the breadth of their activities. The single and dominant business company category averages remained broadly constant. Overall the average Herfindahl index decreased from 0.74 to 0.68 suggesting an increase in the breadth of activities. The small number of service conglomerates amongst the FTSE100 Survivors compared to related diversifiers and the less pronounced, compared to the industrial/manufacturing sector, shift to more focused diversification categories, has resulted in the decrease in overall average Herfindahl.

Finally, there has been a reduction in the average number of activities and groups of related activities reported by most categories of company. Conglomerates showed the largest falls from 4.6 activities and 3.3 related groups in 1993 to 3.3 activities and 2.5 related groups in 2003. Other falls were relatively small. This provides further support for the contention that conglomerates have narrowed the breadth of their activities.

The movements identified in this section strongly support the contention that, in addition to a shift towards focus in the categorisation of the FTSE100, conglomerates have narrowed the breadth of their activities.

6.3.5 Performance

The following table summarises the average performance statistics of companies within each diversification category as per tables 55 (all), 56 (industrial/manufacturing) and 57 (services). The performance reviews were undertaken to see if performance was a clear driver of changes in diversification across the FTSE100.

As DataStream financial data was not available for all companies for all relevant time periods, the number of companies in each year and category for which complete data was available is noted in the final column of each table. The maximum number is 54.

In addition to the performance indicators shown in the tables a number of others including operating margin, price/earnings ratios and operating cash flows were calculated and reviewed to see if any trends could be discerned. Tests, using Pearson's coefficients, for correlations between breadth of activities and a number of performance variables were also undertaken. While a few isolated correlations were found, there were no consistent significant relationships between performance and diversification. That is not to say no such relationships exist but rather that they could not be found using the information that was available from DataStream and the Financial Times.

Table 73: FTSE100 Survivors Average Performance By Diversification Category

	Year End Ave Herfindahl Index	Year End Market Capitall'n £m	12 mnth Share Volatility (%)	Bal Sheet Date MV/Book Ex Intan.	2 Year Averages (Unweighted) ROCE (%)	2 Year Averages (Unweighted) Gearing (%)	Number Of Companies Max 54
1993							
Single	0.98	5,815	70.9	2.8	21.3	25.8	8
Dominant	0.73	7,256	56.3	3.6	15.7	36.5	18
Related	0.46	6,454	50.5	12.0	14.0	36.7	16
Conglomerate	0.40	6,921	47.6	2.8	18.8	32.0	5
All	0.65	6,702	55.9	6.2	16.4	34.3	47
1998							
Single	0.98	15,597	103.8	55.4	14.6	51.2	13
Dominant	0.69	10,771	79.0	2.9	14.3	35.8	18
Related	0.45	17,882	72.0	15.0	26.1	33.4	11
Conglomerate	0.38	9,962	81.7	7.8	31.9	34.9	3
All	0.69	13,850	84.6	21.4	18.5	39.6	45
2003							
Single	0.98	16,538	52.7	17.1	15.1	48.9	14
Dominant	0.74	19,044	66.5	18.9	(32.6)	37.7	17
Related	0.41	23,167	55.5	19.2	22.2	63.7	11
Conglomerate	0.47	5,828	64.4	22.6	32.4	39.5	4
All	0.71	18,118	59.5	18.7	0.7	47.5	46

As with the performance of the FTSE100, the average performance of the FTSE100 Survivors shows a mixed picture and no clear relationship between performance and diversification; conglomerates do not appear to have performed appreciably better or worse than other categories of company. If poor performance were to have been a major driver of the search for focus, the above table should show conglomerates to have underperformed other diversification categories.

The table shows the average conglomerate to have become more focused and smaller according to the average Herfindahl index and average market capitalisation. The volatility of conglomerate share prices, similar to other categories in 2003, has increased from its low 1993 level but its Market Value/ Book Value Excluding Intangibles ratio increased from 2.8 in 1993 to 22.6,

marginally above those of other categories. The ROCE of conglomerates increased significantly between 1993 and 2003 from 18.8% to 32.4% with the category achieving the highest returns in 1998 and 2003. However, the standard deviation of the average ROCE also increased implying a wider range of performance. The average level of gearing remained broadly static for conglomerates as it did for other categories except for related diversifiers. Comparison of the performance of conglomerates with and without a core activity showed neither group to consistently outperform the other.

The following tables summarise average performance statistics by diversification category for industrial/manufacturing and service companies. Notwithstanding the low number of companies in some of the diversification categories, the relative performance of categories does not suggest that any category consistently under or over-performed. As with the 54 FTSE100 Survivors in total, the industrial/manufacturing and services sub-groups show similar movements although the ROCE of industrial/manufacturing conglomerates exceeds that of service conglomerates.

Table 74: FTSE100 Survivors Average Performance By Diversification Category – Industrial/Manufacturing

	Year End		12 mnth	Bal Sheet	2 Year Averages (Unweighted)		Number
	Ave Herfindahl Index	Market Capitall'n £m	Share Volatility (%)	Date MV/Book Ex Intan.	ROCE (%)	Gearing (%)	Of Companies
1993							
Single	0.00	0	0.0	0.0	0.0	0.0	0
Dominant	0.59	10,272	40.7	2.0	9.7	31.9	3
Related	0.43	4,618	54.1	16.4	15.1	38.6	11
Conglomerate	0.35	5,239	47.1	3.0	21.7	27.7	3
All	0.44	5,725	50.5	11.5	15.3	35.5	17
1998							
Single	1.00	8,302	77.5	553.4	18.4	72.4	1
Dominant	0.69	11,753	68.3	2.6	15.5	26.5	5
Related	0.51	20,262	62.9	12.5	27.1	31.9	5
Conglomerate	0.33	12,657	98.3	10.5	41.9	27.9	2
All	0.59	14,899	71.5	50.0	24.2	32.3	13
2003							
Single	1.00	22,017	49.1	17.8	31.6	39.3	4
Dominant	0.74	18,326	65.9	15.8	(67.3)	38.2	9
Related	0.43	29,146	82.6	27.7	25.2	47.9	4
Conglomerate	0.45	8,617	55.8	17.6	58.6	49.6	2
All	0.70	20,359	64.8	18.9	(13.7)	41.7	19

Table 75: FTSE100 Survivors Average Performance By Diversification Category – Services

	Year End		12 mnth	Bal Sheet	2 Year Averages (Unweighted)		Number
	Ave Herfindahl Index	Market Capitall'n £m	Share Volatility (%)	Date MV/Book Ex Intan.	ROCE (%)	Gearing (%)	Of Companies
1993							
Single	0.98	5,815	70.9	2.8	21.3	25.8	8
Dominant	0.76	6,653	59.4	3.9	16.9	37.4	15
Related	0.53	10,494	42.6	2.2	11.5	32.5	5
Conglomerate	0.46	9,445	48.4	2.4	14.5	38.5	2
All	0.76	7,256	58.9	3.2	17.0	33.6	30
1998							
Single	0.98	16,205	106.0	13.9	14.3	49.4	12
Dominant	0.70	10,393	83.2	3.0	13.9	39.4	13
Related	0.40	15,899	79.5	17.1	25.4	34.7	6
Conglomerate	0.47	4,573	48.6	2.4	11.9	49.0	1
All	0.74	13,423	90.0	9.7	16.1	42.6	32
2003							
Single	0.97	14,346	54.1	16.9	8.5	52.7	10
Dominant	0.73	19,852	67.1	22.4	6.4	37.1	8
Related	0.41	19,750	40.0	14.3	20.5	72.8	7
Conglomerate	0.50	3,039	73.1	27.7	6.1	29.5	2
All	0.72	16,541	55.7	18.6	10.8	51.6	27

6.3.6 Corporate Governance

The tables on the following pages illustrate the key corporate governance characteristics of the 54 companies comprising the FTSE100 Survivors. The categorisations are as per tables 55 (all), 56 (industrial/manufacturing) and 57 (services). The tables should be considered in the context of the improvements in corporate governance driven by the introduction of enhanced Best Practice. The tables show no appreciable differences between the corporate governance of industrial/manufacturing and service companies.

As with the FTSE100, the average percentage of non-executive directors sitting on boards increased through the research period across all categories and sectors. In 1993 only dominant business companies had a majority of NEDs but by 1998 the single business and related business averages had also exceeded 50%. By 2003, all categories had averages that exceeded 55%. The average tenure and length of service of both non-executive and executive directors remained broadly constant through the research period at around 5 or 6 years.

The percentage of chairmen that were NEDs increased significantly through the period rising from 38.9% in 1993 to 48.1% in 1998 and 79.6% in 2003 with all categories showing improvements. The average tenure of chairmen fell through the period from 4 years in 1993 to 3 years in 2003 with the largest reduction coming in the conglomerate category from 7 years to 3 years. The length of chairmen's service as directors, including service pre-chairmanship, almost halved from 12 years in 1993 and 1998 to only 7 years in 2003 with an

even greater fall in the length of conglomerate chairmen's service which fell from 18 years in 1993 to 11 years in 1998 and only 6 years in 2003. One of the drivers of this substantial fall is the retirement of several chairmen with extraordinarily long tenures, notably Sir Garfield Weston at Associated British Foods who was appointed chairman in 1967.

The tenure of chief executive officers remained unchanged over the research period remaining at 3 years and their total service as directors has also remained unchanged at 6 years. The number of companies with no chief executive fell from 12 (22%) in 1993 to only 3 (6%) by 2003 which is consistent with the move away from unitary leadership. Of the 12 companies without chief executives in 1993, 3 had multiple, typically, divisional, managing directors and 9 had a joint chairman and chief executive and of the 3 companies without chief executives in 2003 1 had multiple managing directors, 1 was a vacancy and only 1 had a joint chairman and chief executive.

The average percentage of ordinary shares held by major shareholders with notifiable interests, i.e. over 3%, decreased between 1993 and 1998 falling from 12.3% to 9.5% before increasing again to 16.8% by 2003. The averages for each category are higher in 2003 than they were in 1993 with the largest increase in the conglomerate category which increased from 7.7% to 14.3%. The increase in major shareholding reflects the increasing dominance of the equities market by institutions; analysis of each company's major shareholders reveals insurance companies such as Prudential, Scottish

Widows and Aviva to have substantial investments in the equity capital of many companies. The greater increase in institutional investment in conglomerates, relative to other categories, suggests they were looking more favourably on conglomerates than they had in the past. This could be due to the narrowing in the breadth of conglomerate activities or an underlying support for the economic rationale behind conglomeration.

In broad terms the corporate governance of conglomerates differs little from that of companies in other diversification categories but the levels of institutional shareholding have increased significantly.

Table 76: FTSE100 Survivors Corporate Governance By Diversification Category

All Averages	Board			Chair			CEO		No. of Companies		Major
	NED (%)	NED (yrs)	ED (yrs)	NED %	Tenure(yrs)	Director(yrs)	Tenure(yrs)	Director(yrs)	Total	No CEO	S'holds (%)
1993											
Single	41.0	7	7	20.0	5	16	5	9	10	5	15.2
Dominant	54.8	6	5	52.4	4	8	3	6	21	2	14.2
Related	48.2	5	5	25.0	2	11	2	5	16	3	9.9
Conglomerate	41.6	6	7	57.1	7	18	4	7	7	2	7.7
All	48.6	6	5	38.9	4	12	3	6	54	12	12.3
1998											
Single	52.7	5	6	42.9	3	13	3	8	14	2	11.5
Dominant	55.0	5	6	57.9	5	12	3	6	19	3	9.3
Related	55.7	4	6	57.1	4	11	4	8	14	1	8.0
Conglomerate	47.3	5	6	14.3	3	11	1	4	7	2	8.7
All	53.6	5	6	48.1	4	12	3	7	54	8	9.5
2003											
Single	60.9	4	5	70.6	3	7	2	4	17	1	21.1
Dominant	64.1	5	4	90.0	3	7	4	7	20	1	16.1
Related	61.1	5	4	76.9	3	8	3	6	13	0	12.9
Conglomerate	60.2	4	5	75.0	3	6	3	7	4	1	14.3
All	62.1	5	5	79.6	3	7	3	6	54	3	16.8

Table 77: FTSE100 Survivors Corporate Governance By Diversification Category – Industrial/Manufacturing

All Averages	Board			Chair			CEO		No. of Companies		Major
	NED (%)	NED (yrs)	ED (yrs)	NED %	Tenure(yrs)	Director(yrs)	Tenure(yrs)	Director(yrs)	Total	No CEO	S'holds (%)
1993											
Single	35.3	2	5	0.0	8	25	0	6	1	0	4.2
Dominant	48.4	11	7	25.0	7	18	1	4	4	1	21.6
Related	45.6	5	4	9.1	2	11	1	4	11	2	10.4
Conglomerate	38.6	8	9	33.3	7	14	4	6	3	1	10.2
All	44.5	6	6	15.8	4	14	2	4	19	4	12.4
1998											
Single	57.1	1	6	0.0	1	11	4	6	2	0	3.8
Dominant	52.4	7	7	16.7	7	17	1	3	6	2	16.3
Related	52.8	4	5	28.6	2	12	3	5	7	1	8.6
Conglomerate	43.3	5	7	0.0	3	13	1	2	4	1	11.5
All	51.1	5	6	15.8	4	13	2	4	19	4	11.2
2003											
Single	73.2	5	6	75.0	3	10	2	4	4	0	20.9
Dominant	66.9	5	5	88.9	1	5	3	8	9	0	17.8
Related	58.1	5	4	80.0	3	8	4	5	5	0	17.5
Conglomerate	65.3	4	5	50.0	5	10	1	1	2	1	13.1
All	65.8	5	5	80.0	2	7	3	6	20	1	17.9

Table 78: FTSE100 Survivors Corporate Governance By Diversification Category - Services

All Averages	Board			Chair			CEO		No. of Companies		Major
	NED (%)	NED (yrs)	ED (yrs)	NED %	Tenure(yrs)	Director(yrs)	Tenure(yrs)	Director(yrs)	Total	No CEO	S'holds (%)
1993											
Single	41.6	7	7	22.2	5	15	3	4	9	5	16.4
Dominant	56.3	5	4	58.8	3	6	3	6	17	1	12.5
Related	53.9	6	6	60.0	3	11	3	5	5	1	8.9
Conglomerate	43.9	4	6	75.0	8	20	2	5	4	1	5.8
All	50.8	5	5	51.4	4	11	3	5	35	8	12.2
1998											
Single	52.0	6	6	50.0	3	13	2	7	12	2	12.8
Dominant	56.2	5	5	76.9	5	10	3	6	13	1	6.1
Related	58.6	5	6	85.7	6	10	5	9	7	0	7.3
Conglomerate	52.7	4	5	33.3	4	9	1	4	3	1	5.0
All	54.9	5	6	65.7	4	11	3	7	35	4	8.5
2003											
Single	57.1	4	5	69.2	2	7	2	4	13	1	21.2
Dominant	61.8	5	4	90.9	4	8	4	6	11	1	14.7
Related	62.9	5	4	75.0	3	8	2	6	8	0	10.1
Conglomerate	55.1	3	5	100.0	2	2	4	11	2	0	15.5
All	59.9	5	4	79.4	3	7	3	5	34	2	16.1

6.3.7 Conglomerates amongst the FTSE100 Survivors

As noted in a preceding section, between 1993 and 2003 there were changes in composition of the conglomerate category although 3 of the 7 companies categorised as conglomerates in 1993 remained in that category in 2003.

Table 79: FTSE100 Survivors – Conglomerates in 1993, 1998 & 2003

1993 Company	1993-1998 Change	1998 Company	1998-2003 Change	2003 Company
Bass		Bass		Intercontinental Hotels[1]
BAT Industries	To Single			
Granada		Granada	To Single	
Ladbroke Grp	To Dominant			
Pearson		Pearson	To Related	
Tomkins		Tomkins		Tomkins
Unilever		Unilever		Unilever
	From Dominant	United Utilities[2]	To Related	
	From Related	Diageo[3]	To Single	
			From Related	Whitbread
7	+0	7	-3	4

Notes:
[1] Bass changed its name to Intercontinental Hotels reflecting its exit from brewing.
[2] North West Water changed its name to United Utilities after acquiring Norweb.
[3] Diageo was formed by Guinness' acquisition of Grand Metropolitan in 1997.

By 1998, 2 of the original 7 conglomerates – BAT Industries/British American Tobacco and Ladbroke/Hilton – had abandoned conglomeration being replaced by North West Water/United Utilities and Guinness/Diageo which, in 1993, had been dominant and related companies respectively. Between 1998 and 2003, 2 more of the original 7 left the conglomerate category with Pearson becoming a related diversifier and Granada becoming a single business company and the 2 companies that had become conglomerates between 1993 and 1998, North West Water/United Utilities and Guinness/Diageo retreated to related diversification and single business company respectively. Whitbread, previously a related diversifier, joined the

category. The ‘stories’ behind each of the conglomerates’ adoption, maintenance or abandonment of the strategy are considered in chapter 7.

The Herfindahl indices of the 3 companies that retained their conglomerate strategies throughout the 10 year period show that the breadth of activities narrowed marginally at household products company Unilever but substantially at both the brewing and hotels group Bass/Intercontinental Hotels and the engineering company Tomkins.

Table 80: FTSE100 Survivors Constant Conglomerates – Herfindahl Indices

Company	1993	1998	2003
Bass/Intercontinental Hotels	0.21	0.29	0.58
Tomkins	0.23	0.28	0.48
Unilever	0.35	0.38	0.41

6.4 Exits from the FTSE100

The list of FTSE100 survivors includes some of the best known names in UK business but a review of the companies that left the index between 1993 and 2003 reveals a number of famous companies that did not enjoy continuous membership of the index. The following table shows what happened to the 46 companies that were in the FTSE100 in 1993 but had left the index by 2003.

Table 81: FTSE100 Exits By 1998 and 2003

FTSE100 Constituents 1993	1993-1998 Reason for Exit	FTSE100 Constituents 1998	1998-2003 Reason for Exit	Other Information
Anglian Water	Value Loss/Displaced			
Arjo Wiggins Appleton	Value Loss/Displaced			A by Worms (Fr) 2000
ASDA		ASDA	A by Wal*Mart (US) 1999	
Bank of Scotland		Bank of Scotland	A by Halifax* 2001	
Blue Circle	Value Loss/Displaced			A by Lafarge (Fr) 2001
Bowater	Value Loss/Displaced			Re-entry by 2003
British Steel	Value Loss/Displaced			
BTR		BTR	A by Siebe* 1999	
Burmah Castrol	Value Loss/Displaced			A by BP* 2000
Caradon	Value Loss/Displaced			
Carlton Communications		Carlton Communications	Value Loss/Displaced	
Coats Viyella	Value Loss/Displaced			A by Guinness Peat 2003
Courtaulds	A by Akzo Nobel (Neth) 1998			
Eastern Electricity	A by Hanson* 1995			
Enterprise Oil	Value Loss/Displaced			A by Shell* 2002
Forte	A by Granada* 1996			
GEC		GEC	Liquidated 2003	
General Accident	A by Comm. Union* 1998			
Grand Metropolitan	A by Guinness* 1997			
Guardian Royal Exchange		GRE	A by Axa (Fr) 1999	
Hanson	Value Loss/Displaced			Re-entry by 2003
Inchcape	Value Loss/Displaced			
MEPC	Value Loss/Displaced			A by UK/US Consortium 2000
National Power		National Power	Value Loss/Displaced	
National Westminster Bank		Nat West	A by Royal Bank of Scot* 2000	
P&O		P&O	Value Loss/Displaced	
PowerGen		PowerGen	A by E.On (Ger) 2002	
Rank Organisation	Value Loss/Displaced			
Redland	A by Lafarge (Fr) 1997			
RMC Group	Value Loss/Displaced			
Royal Insurance	M by Sun Alliance 1996			
Scottish Hydro Electricity	Value Loss/Displaced			Re-entry by 2003
Sears Holdings	A by JIL Ltd 1999			
Siebe		Siebe	Value Loss/Displaced	
Smith & Nephew	Value Loss/Displaced			Re-entry by 2003
SmithKline Beecham		SmithKline Beecham	M with Glaxo* 2001	
Southern Electricity		Southern Electric	A by Scottish Hydro* 1999	
Thames Water		Thames Water	A by RWE (Ger) 2000	
Thorn EMI		EMI	Value Loss/Displaced	
TI Group	Value Loss/Displaced			A by Smiths Inds* 2000
TSB	A by Lloyds* 1995			
United Biscuits	Value Loss/Displaced			A by Finalrealm (US) 2000
Warburg SG	A by SBC (Sw) 1994			
Wellcome	A by Glaxo* 1995			
Williams Holdings		Williams	De-Listed 2000	
Wolseley	Value Loss/Displaced			Re-entry by 2003

Notes
All companies displaced through loss of market value remained LSE listed until merged/acquired.
Bowater (Rexam), Hanson, Scottish Hydro, Smith & Nephew and Wolseley re-entered the FTSE100 by 2003.
Merging and acquiring companies are UK unless noted.
* Denotes merging or acquiring company was a constituent of the FTSE100 at the time of the transaction.

As the table shows, in addition to displacement due to loss of market value, acquisitions activity was also a major driver of change within the FTSE100. Of the 30 companies that left the index between 1993 and 1998 and the additional 16 that exited between 1998 and 2003, value loss accounted for 19 (1998-03: 5) and acquisitions 11 (9) of which 3 (4) were by foreign acquirers, 6 (5) by fellow FTSE100 companies and 1 (0) by private equity, the acquisition

of retailer Sears by JIL Ltd, retail entrepreneur Sir Philip Green's investment vehicle. The 1999 to 2003 period also saw the de-listing of Williams and the liquidation of GEC.

Williams, which, since the 1970s under Sir Nigel Rudd, had grown from a small engineering company into an FTSE100 conglomerate by 1993, embarked on a break-up to realise shareholder value that saw its businesses which included lock-maker Chubb and security company Kidde either sold or floated with the holding company finally de-listed. Williams' successful break-up may be contrasted with GEC's decision, championed by its new chief executive Lord Simpson after the retirement of its managing director for over 30 years, Lord Weinstock, to retreat from a related diversification strategy to become a focused telecommunications company renamed Marconi and achieving the change through a series of disposals and acquisitions. The strategic change provided ill-timed given the spike in technology and telecommunication company values and GEC's famous cash resources were turned into a debt of around £5 billion which provided unserviceable leading to profit warnings, a debt for equity swap that diluted existing shareholders ownership by over 99% and eventually a break-up of the group.

Finally, 5 of the 46 1993 FTSE100 companies excluded from the list of 54 'ever present' companies had actually returned to the index by 31st December 2003. Each of the 5 companies – Bowater (Rexam), Hanson, Scottish Hydro, Smith & Nephew and Wolseley - and had fallen out of the index at the end of

1998 on ‘Value loss/Displacement’ grounds but had re-entered by the end of 2003.

6.5 Results

Analyses of the database of FTSE100 and FTSE100 Survivors populations detailed in this chapter have the following implications for acceptance/rejection of the hypotheses stated in chapter 4. The hypotheses are considered in four sections covering incidence, breadth of activities, performance and corporate governance. In each case, acceptance or rejection of the hypothesis is assessed.

6.5.1 Incidence

These hypotheses consider the incidence of conglomeration among FTSE100 companies through the research period. Based on anecdotal evidence, a decline in the incidence of conglomeration amongst FTSE100 companies was expected. In order to assess incidence, the FTSE100 and FTSE100 Survivors were categorised according to the Rumelt-based scheme of Channon/W&M which uses segmental activity data.

A.1 The incidence of conglomeration amongst FTSE100 companies declined between 1993 and 2003.

The analyses have shown a clear and continuing decline from 16% to 7% in the incidence of conglomeration amongst FTSE100 companies since 1993. There was also a wider trend towards focused business strategies

– single business and dominant business – and away from multiple business strategies – related diversification and conglomeration - through the 10 year period. In addition to the move to greater focus, the research has also shown increases in multiple business companies, especially conglomerates, with a core activity generating more than 50% of turnover.

These trends have been seen not only amongst the 100 companies constituting the FTSE100 index in 1993, 1998 and 2003, i.e. a changing population, but also in the activities of the 54 FTSE100 Survivors.

A.2 The incidence of conglomeration amongst FTSE100 industrial/manufacturing companies declined between 1993 and 2003.

The number of industrial/manufacturing conglomerates in the FTSE100 fell from 10 (23.8%) in 1993 to 6 (20.0%) in 1998 and to only 3 (8.1%) in 2003. There was a similarly dramatic fall in the number of related diversified industrial/manufacturing companies which fell from 22 (52.4%) in 1993 to 13 (43.3%) in 1998 and to only 9 (24.3%) in 2003.

Overall multiple business industrial/manufacturing companies in the FTSE100 index fell from 32 (76.2%) in 1993 to 19 (63.3%) in 1998 and 12 (32.4%) in 2003. In addition to the move to greater focus, analysis has shown increases in conglomerate and related companies with a core activity generating more than 50% of turnover.

The number of focused business companies remained steady between 1993 and 1998 increasing by 1 from 10 (23.8%) to 11 (36.6%) but rose significantly to 25 (67.5%) by 2003. In both 5 year periods there were similar increases in single business and dominant business companies.

These trends have been seen not only amongst the 100 companies constituting the FTSE100 index in 1993, 1998 and 2003, i.e. a changing population, but also in the activities of the 54 FTSE100 Survivors.

A.3 The incidence of conglomeration amongst FTSE100 service companies declined between 1993 and 2003.

The trends identified are similar to, but not as pronounced as, those discussed above which may reflect the low, compared to the industrial/manufacturing sector, level of conglomeration in 1993 when there were only 6 (10.3%) conglomerate service companies in the FTSE100. By 1998 there were only 4 (5.7%) service conglomerates and 2003 saw the same number. There was an increase from 9 (15.5%) to 14 (20.0%) in related diversification between 1993 and 1998 followed by a fall back to 9 (14.3%) by 2003. Overall, there were 15 (25.8%) multiple business companies in 1993 and 13 (20.6%) in 2003.

The reduction in multiple business companies did not produce an increase in both focused company categories. There was a decrease in dominant business companies which fell from 25 (43.1%) in 1993 to 17

(27.0%) in 2003 meaning the single business category benefitted from the move to greater focus seeing increases from 18 (31.0%) in 1993 to 30 (42.9%) in 1998 and to 33 (52.4%) in 2003. In addition to the move to greater focus, the research also showed increases in the numbers of conglomerate, but not related, companies that have a core activity, one generating more than 50% of turnover.

These trends have been seen not only amongst the 100 companies constituting the FTSE100 index in 1993, 1998 and 2003, i.e. a changing population, but also in the activities of the 54 FTSE100 Survivors.

Each of the three hypotheses relating to the decline of conglomeration amongst FTSE100 companies has been upheld; the incidence of conglomeration declined between 1993 and 2003. The decline was seen in the total population and also in the industrial/manufacturing and service sectors. More companies retreated back to greater focus than advanced to wider diversification. Chi-Tests showed the patterns of change in each period to be significantly different.

6.5.2 Breadth of Activities

These hypotheses consider the breadth of activities pursued by FTSE100 companies through the research period. Anecdotal evidence suggests that companies, even those that remained diversified, had been narrowing the scope or breadth of their activities since 1993 and this research has used Herfindahl indices and the distribution of turnover across activities and groups

of related activities to assess whether this was the case overall and for each Channon/W&M diversification category.

B.1 The breadth of activities pursued by FTSE100 companies narrowed between 1993 and 2003.

The average Herfindahl index of the total population of FTSE100 companies increased from 0.63 to 0.77 suggesting the breadth of activities had narrowed. However, there was little change in the single, dominant and related category averages; only the conglomerate category showed a significant increase from 0.36 to 0.44. Similar movements were identified in the percentage of turnover generated by the largest activity and group of related activities.

This suggests only the breadth of conglomerate activities had narrowed. The increases in overall averages reflect this and the migration of companies to more focused categories over the research period.

B.2 The breadth of activities pursued by FTSE100 industrial/manufacturing companies narrowed between 1993 and 2003.

The average Herfindahl index of FTSE100 industrial/manufacturing companies increased significantly over the research period rising from 0.48 in 1993 to 0.56 in 1998 and 0.71 in 2003 suggesting a substantial reduction in the breadth of activities. However, only the dominant

category showed a material increase in average Herfindahl index. There were similar movements in the average percentage of turnover generated by the largest activity and group of related activities.

This suggests a narrowing of dominant company activities. The increases in overall averages reflect this and the migration of companies to more focused categories over the research period.

B.3 The breadth of activities pursued by FTSE100 service companies narrowed between 1993 and 2003.

The average Herfindahl index of FTSE100 service companies increased in both of the 5 year periods; from 0.73 in 1993 to 0.76 in 1998 and to 0.81 in 2003 suggesting the breadth of activities had narrowed. However, there was little change in the single, dominant and related category averages; only the conglomerate category showed a significant increase from 0.33 to 0.47. Similar movements were identified in the percentage of turnover generated by the largest activity and group of related activities.

This suggests only the breadth of conglomerate activities had narrowed. The increases in overall averages reflect this and the migration of companies to more focused categories over the research period.

For all three hypotheses, changes in the number of reported activities and groups of reported activities supported the findings. For all three hypotheses, the FTSE100 Survivors showed similar results.

Each of the three hypotheses relating to the breadth or scope of FTSE100 company activities between 1993 and 2003 has been upheld but only consistently for conglomerate companies. With a few exceptions, the breadth of activities of other categories remained broadly unchanged. This was true of the total population and also of the industrial/manufacturing and service sectors.

6.5.3 Performance

Ignoring effects of changes in business portfolios, these hypotheses consider the overall performance of conglomerates and other diversification categories through the research period.

C.1 FTSE100 conglomerates underperformed through the research period compared to other categories of company – single business, dominant business and related diversified.

The evidence is mixed depending on year and indicator with no clear picture emerging. In each year average conglomerate performance was similar to that of other diversification categories.

C.2 FTSE100 industrial/manufacturing conglomerates underperformed through the research period compared to other categories of industrial/manufacturing company – single business, dominant business and related diversified.

The evidence is mixed depending on year and indicator with no clear picture emerging. In each year average industrial/manufacturing company conglomerate performance was similar to that of other diversification categories.

C.3 FTSE100 service company conglomerates underperformed through the research period compared to other categories of service company – single business, dominant business and related diversified.

The evidence is mixed depending on year and indicator with no clear picture emerging. In each year average service company conglomerate performance was similar to that of other service company diversification categories.

C.4 FTSE100 conglomerate performance is negatively related to the breadth of activities.

There is no significant degree of correlation between a conglomerate's breadth of activities, as measured by its Herfindahl index, and performance, as measured by its operating margin.

C.5 FTSE100 conglomerates with a core activity generating more than 50% of turnover outperform conglomerates without a core activity.

There is no significant degree of correlation between the existence of a core activity that generates more than 50% of a conglomerate's turnover and its performance relative to other conglomerate companies.

Overall the five hypotheses covering performance are inconclusive; there appears to be no strong link between performance and diversification suggesting that many of those companies that have retreated back from conglomeration through the research period were driven by other, non-performance, strategic issues. Conglomerates did not appear, on average, to have underperformed compared to other categories. The absence of a link between diversification category and performance is re-enforced by the low and statistically insignificant Pearson correlation coefficients between diversification, as measured by Herfindahl indices, and a number of performance indicators.

In light of the absence of a clear financial driver for the reduction in conglomeration, Chapter 7 looks at each of the companies that adopted, maintained and/or abandoned conglomeration between 1993 and 2003 to identify other strategic drivers behind their decisions.

6.5.4 Corporate Governance

These hypotheses consider differences between key facets of corporate governance at conglomerates over time and as compared to other categories of company. The expectation was that, notwithstanding changes resulting from enhancement to the Code of Best Practice, the characteristics of corporate governance in conglomerates would be different to those at more focused companies.

D.1 There was no change in the executive/non-executive split in the composition of FTSE100 conglomerate boards through the research period.

There have been changes in the percentage of non-executive directors sitting on the boards of conglomerates since 1993; the percentage has increased as it has across all categories. This finding is inconsistent with that expected and suggests that FTSE100 companies have adopted Best Practice which recommends that, ideally, boards should have a majority of non-executive directors.

D.2 The executive/non-executive split in the composition of conglomerate boards is the same as for other categories of FTSE100 company.

As noted in D1 above, there was a general trend towards a higher percentage of non-executive directors on boards at all FTSE100 companies.

D.3 There was no change in the average tenure of chairmen of FTSE100 conglomerate boards through the research period.

The average tenure of the chairmen of conglomerate company boards fell significantly through the research period as has their period of service as a director, i.e. including time as a director prior to their appointment as chairman. The average tenure of chairmen of FTSE100 conglomerates has fallen by half between 1993 and 2003 while average service has fallen by two-thirds in the same period. These falls were largely due to the retirements of a few long-serving chairmen.

D.4 The average tenure of chairmen of conglomerate boards is the same as for other categories of FTSE100 companies.

The average tenure of the chairmen of non-conglomerate company boards has fallen through the research period as has their period of service as a director although the reductions have not been as large as those for conglomerate chairmen. By 2003 the tenure of chairmen of conglomerates is similar to that of chairmen of other categories of company although their period of service is shorter.

D.5 There has been no change in the percentage of conglomerate company chairmen that are non-executive directors.

Notwithstanding a reduction in 1998, the percentage of conglomerate companies with non-executive chairmen doubled between 1993 and 2003. This increase suggests conglomerates have adopted the Cadbury committee recommendation that chairmen should be non-executive.

D.6 The percentage of conglomerate company non-executive chairmen is the same as for other categories of FTSE100 companies.

The percentage of non-conglomerate companies with non-executive chairmen doubled between 1993 and 2003. This increase is similar to that at conglomerates and suggests widespread adoption of the Cadbury committee recommendation that chairmen should be non-executive.

D.7 There was no change in the proportion of FTSE100 conglomerates with dual chairmen/chief executive officers through the research period.

The proportion of conglomerate companies with no separate chief executive officer fell between 1993 (31.3%) and 2003 (14.3%). This outcome was expected as the separation of the roles of chairman and chief executive officer was an element of the Cadbury committee's recommendations.

D.8 The proportion of conglomerates with dual chairmen/chief executive officers is the same as for other categories of FTSE100 companies.

The number and percentage of non-conglomerate companies with no separate chief executive officer fell through the research period although less so at single business companies. The reduction in the incidence of non conglomerate companies having a chairman/chief executive officer is broadly similar to that at conglomerates.

D.9 There was no change in the average tenure of chief executive officers of FTSE100 conglomerates through the research period.

The average tenure and length of service of chief executive officers has remained broadly unchanged at conglomerate and non-conglomerate companies throughout the research period.

D.10 The average tenure of chief executive officers of conglomerates is the same as for other categories of FTSE100 companies.

The average tenure and length of service of chief executive officers has remained broadly unchanged at conglomerate and non-conglomerate companies throughout the research period.

D.11 There was no change in the average aggregate shareholdings of investors with notifiable interests in the share capital of conglomerates through the research period.

The average aggregate shareholdings of investors with notifiable interests almost doubled for the conglomerate category between 1993 and 2003. The largest increase happened between 1998 and 2003 and for companies in the service sector.

D.12 The average aggregate shareholding of investors with notifiable interests in the share capital of conglomerates is the same as for other categories of FTSE100 companies.

The average aggregate shareholdings of investors with notifiable interests increased for almost all categories between 1993 and 2003 but the increase for conglomerates was greater than those of other categories.

D.13 There were no major differences between the corporate governance of industrial/manufacturing and service companies.

The analyses showed the same trends to be evident in corporate governance across both sectors.

For each of the hypotheses the analyses showed similar results for the FTSE100 and FTSE100 Survivors populations. Overall there are few differences between the corporate governance characteristics of conglomerates and those of other categories of FTSE100 company suggesting they are all run along similar lines. All categories of company

increased the percentage of non-executives on their boards. The major changes concerned chairmen; the percentage having non-executive status increased across all categories of company and their period of service decreased substantially especially at conglomerates. These universal improvements in corporate governance were in line with changes in Best Practice. Finally, the significant increase in the average aggregate major shareholdings in conglomerates suggests institutional investors may be more supportive of conglomerates than had been thought.

6.6 Summary

Overall, the results have clearly shown that the incidence of conglomeration amongst FTSE100 companies has declined between 1993 and 2003 and that amongst the 54 companies that were members of the index at the end of 1993, 1998 and 2003 conglomeration has also declined. In addition, the average breadth of corporate activities has narrowed amongst conglomerates where the incidence of core activities generating more than 50% of turnover has also increased as it did amongst related diversifiers. Together with increases in the percentage of turnover generated by the largest activity/group of related activities and decreases in the number of reported activities/groups of related activities, these findings strongly suggest that, in addition to eschewing conglomeration, those companies that retained the strategy narrowed the breadth of their activities. In addition, analyses of movements between diversification categories show more companies to have retreated back through the Model of Corporate Development towards greater focus than

advanced to wider diversification. These findings are broadly true for both industrial/manufacturing and service companies.

Improvement in corporate governance at conglomerates does not appear to be a major driver of their strategic change. While the key elements of corporate governance have improved at conglomerates, the same is true of companies in other diversification categories which is consistent with the contention that enhancements to Best Practice have driven the improvements. The contention that the investment community views conglomerates unfavourably is undermined by the absolute and relative (to other diversification categories) increase in the average aggregate size of major shareholdings in conglomerates which increased between 1993 and 2003. This may suggest that institutional investors still support conglomeration or that the 2003 conglomerates are perceived as better than those that existed in 1993.

While detailed financial analysis was not an intended part of this research, the high level analyses of performance have shown that, in common with extant literature, there is no apparent link between post-hoc performance and diversification category. This suggests there are other strategic drivers such as those identified as inhibitors in the literature review (section 3.3.3.2) behind corporate decisions to retreat away from conglomeration towards greater focus. Furthermore, this implies that the non-performance drivers force companies to act before any negative performance impacts of a conglomerate

strategy are realised; it is the expectation of future poor performance (ex-ante) rather than past poor performance (post-hoc) that drives strategic change.
Given there is no clear link between diversification and post-hoc performance, other factors must also drive strategic decisions. These drivers may be generic, industry specific or company specific. Generic drivers are those that affect companies regardless of sector or industry and typically include such intangible factors as tastes/fashion, social/environmental, personal/value and economic outlook/growth. Clearly, given their nature, the effects of generic factors are hard to quantify. Industry specific factors are those that affect companies in particular industries and would include technological change, market growth and competitive market structure; is the industry dominated by a few major global companies? Again, the specific effects of these drivers are difficult to quantify especially on multi-business companies. Finally, company specific drivers include those that determine the financial/market support the company receives, how the company is led/managed and how regulation affects its ability to grow and compete in its chosen businesses.

In order to get an understanding of the impact of company specific factors on corporate strategy formulation and strategic change, principally movements between diversification categories in the Model of Corporate Development, in terms of the strategic responses and outcomes, company histories were compiled and analysed. Chapter 7 – Analysing the Historical Record – considers the circumstances in which 22 FTSE100 companies adopted, maintained or abandoned conglomeration at some point between 1993 and 2003.

7. ANALYSING THE HISTORICAL RECORD

7.1 Introduction

The results detailed in the preceding chapter provide substantial support for the contention that conglomeration has declined in the UK, at least among the companies – both industrial/manufacturing and service - that comprise the FTSE100 index, and that there has been a broad movement towards greater focus. A narrowing of the breadth of conglomerate activities was also identified. The chapter also noted the lack of any apparent link between performance (post-hoc) and diversification category or between corporate governance and diversification suggesting that other issues were behind decisions to adopt, maintain or, increasingly through the research period, abandon conglomeration. While Chapter 6 did provide a quantitative assessment, based largely on accounting data, of diversification amongst FTSE100 companies, it did not try to explain why diversification, especially conglomeration, had decreased. This chapter takes a qualitative and discursive approach to look for explanations of those strategic change decisions.

The extant literature covering the US and UK history of conglomeration discussed in chapter 3 suggests a number of drivers behind diversification decisions. The key external drivers include investor/market pressure and regulation especially the prevailing attitude of competition authorities to industry structures, as evidenced by the UK CC's investigations in industries such as brewing, banking and supermarkets, and acquisitions that reduce competition. These drivers influence internal strategic decisions regarding

corporate diversification which may result in disposals, demergers, the return of capital to shareholders and/or acquisitions to either add new or build existing activities or expand internationally. In turn, these strategic responses shape the future scope of the company which could lead to greater focus or further diversification and/or the attainment, re-assertion, maintenance or elimination of a core activity.

The following section (7.2) charts the movements between 1993 and 1998, 1998 and 2003 and 1993 and 2003 of FTSE100 and FTSE100 Survivors companies through the Model of Corporate Development. The charts show the number of companies moving between each diversification category and, for the FTSE100 index, entries and exits. The names of all companies moving to/from the conglomerate category are also shown on each chart.

The next section (7.3) provides, for each company categorised as a conglomerate at any of the period ends, a brief company history which includes references to performance and other information drawn from the database, to provide high-level qualitative assessments of the circumstances in which diversification decisions were made. Appendix F includes key database details for each of the conglomerates and notes the major references used in compiling each history.

The third section (7.4) analyses the key elements of each company history summarising them into a table (table 82) which supports discussion of links

between external drivers, strategic responses/restructuring and their outcomes.

7.2 Movements To/From Conglomeration

FTSE100

Charts 8, 10 & 12 show that only 7 of the FTSE100 companies categorised as conglomerate in 1993 remained in that diversification category in 1998 and of those only 3 – Bass/Intercontinental Hotels, Tomkins and Unilever - were still conglomerates in 2003. Over the same period the number of conglomerates in the FTSE100 more than halved from 16 to 7.

Between 1993 and 2003, 3 conglomerates entered and 8 left the FTSE100 while 5 conglomerates retreated back to more focus – 1 to related diversification and 2 each to the dominant and single business categories – and only 1 company, a related diversifier, advanced to greater diversification.

The charts show a flow back to greater focus with more activity in the 5 years from 1998 to 2003 than between 1993 and 1998.

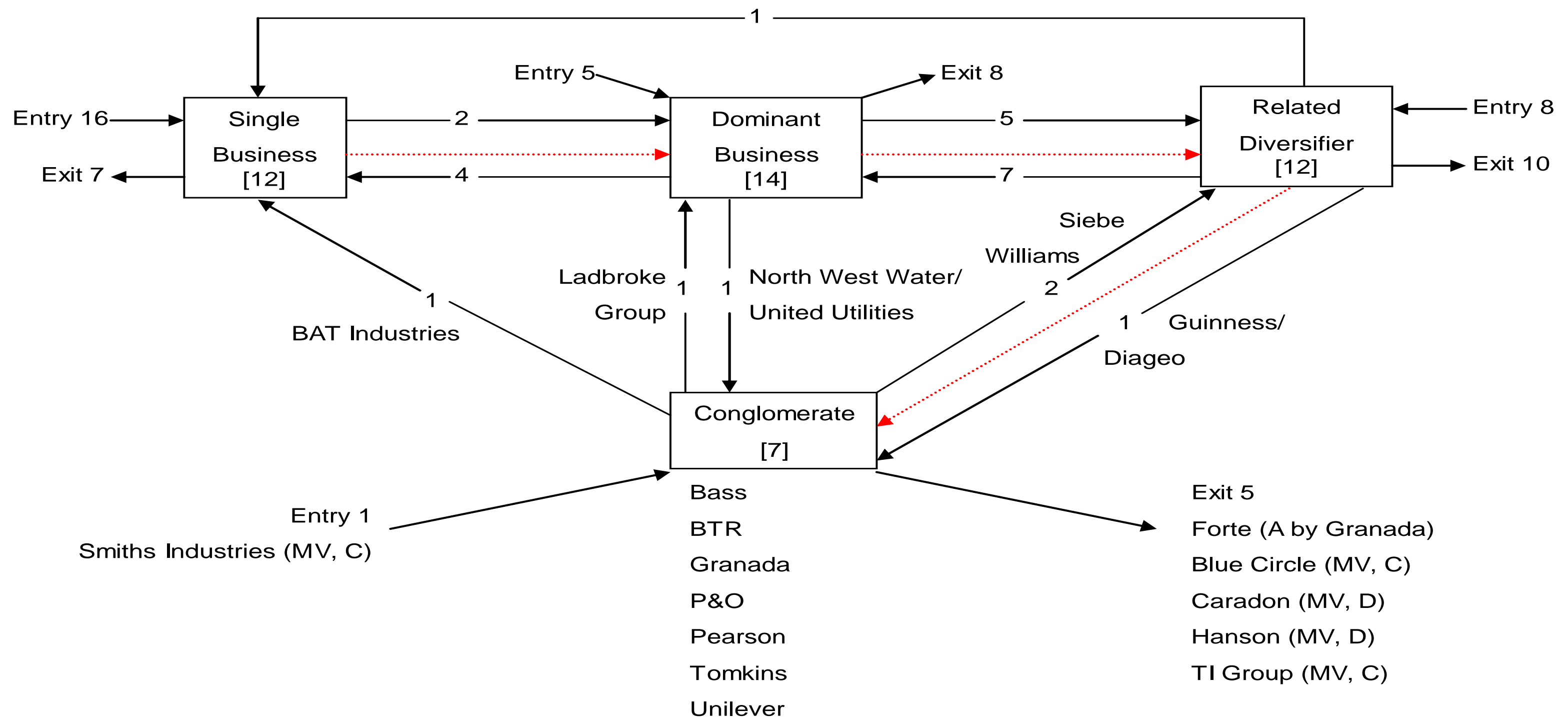
FTSE100 Survivors

Charts 9, 11 & 13 show that only 5 of the 54 FTSE100 Survivors companies categorised as conglomerate in 1993 remained in that category in 1998 and of those only 3 – Bass/Intercontinental Hotels, Tomkins and Unilever – were still conglomerates in 2003. Over the same period the number of conglomerates in the FTSE100 Survivors fell from 7 to 4.

Between 1993 and 2003 the trend was towards greater focus with 4 companies retreating to less diversified categories and only 1 company becoming a conglomerate. Of the 4 1993 conglomerates that achieved greater focus, by 1998 BAT Industries/British American Tobacco had become a single business company and Ladbroke/Hilton a dominant business company and by 2003 Granada had become a single business company and Pearson a related diversifier. The one new conglomerate was Whitbread which advanced from related diversification during the 5 years between 1998 and 2003.

As with the FTSE100, the charts show a flow back to greater focus with more activity in the 5 years from 1998 to 2003 than between 1993 and 1998.

Chart 8: FTSE100 – Movements To/From The Conglomerate Category From 1993 To 1998



Key

[1] Number of companies remaining in each category at the start and end of the period.

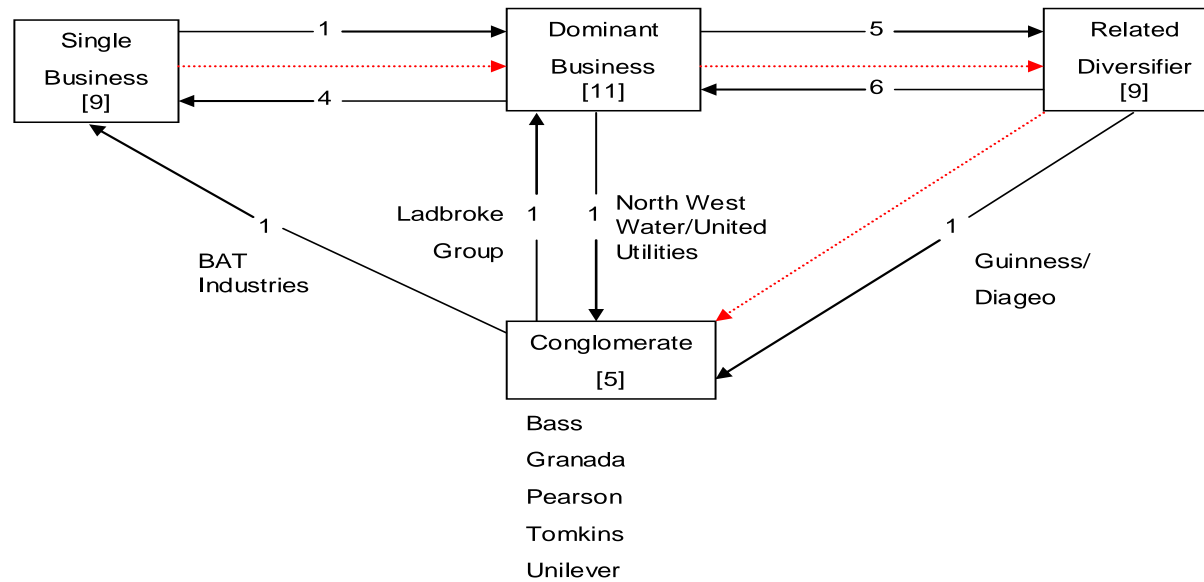
1 Number of companies moving in the direction of the arrow. Conglomerates are named.

Broken red lines denote expected movements through the Model of Corporate Development.

Solid black lines denote the actual movements to/from each diversification category during the period.

Abbreviations: MV – entry/exit due to change in market value, S, D, R, C – category pre/post FTSE100 membership if listed before/after membership, M – merged, A – acquired.

Chart 9: FTSE100 Survivors – Movements To/From the Conglomerate Category From 1993 To 1998



Key

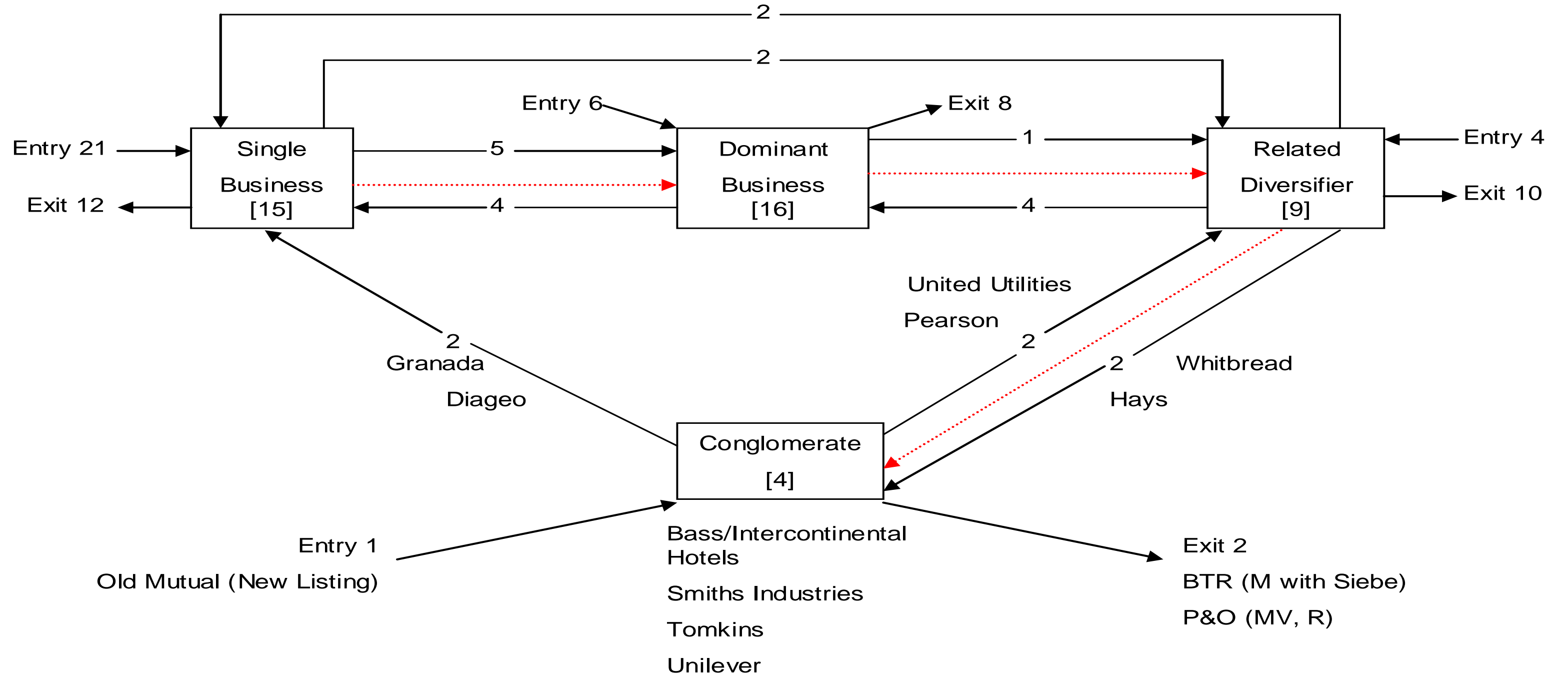
[1] Number of companies remaining in each category at the start and end of the period.

1 Number of companies moving in the direction of the arrow. Conglomerates are named.

Broken red lines denote expected movements through the Model of Corporate Development.

Solid Black lines denote the actual movements to/from each diversification category during the period.

Chart 10 FTSE100 – Movements To/From the Conglomerate Category From 1998 To 2003



Key

[1] Number of companies remaining in each category at the start and end of the period.

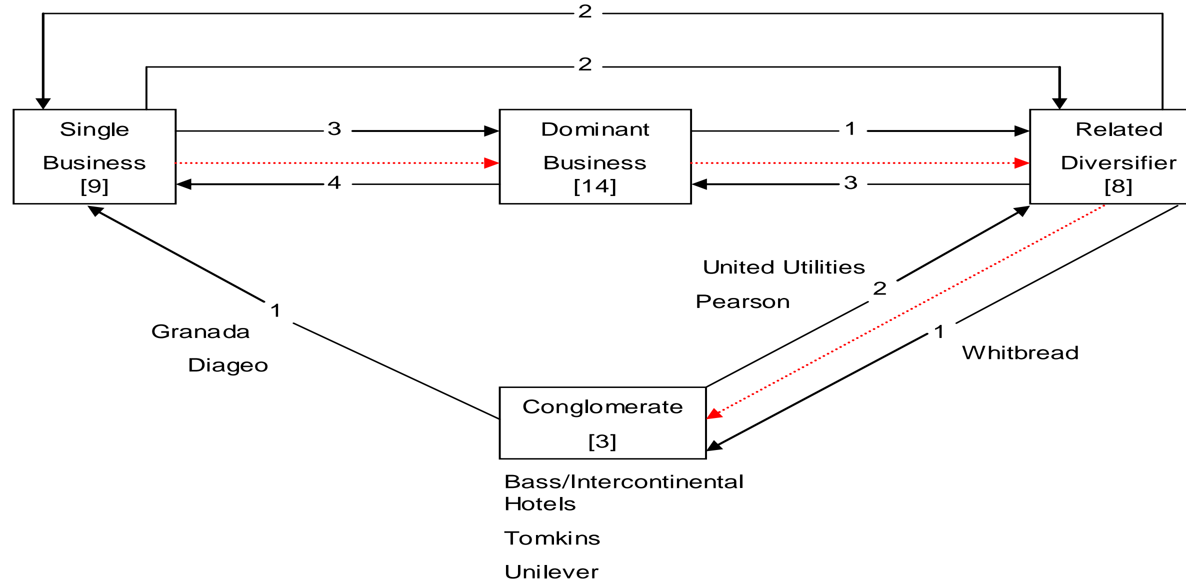
1 Number of companies moving in the direction of the arrow. Conglomerates are named.

Broken red lines denote expected movements through the Model of Corporate Development.

Solid black lines denote the actual movements to/from each diversification category during the period.

Abbreviations: MV – entry/exit due to change in market value, S, D, R, C – category pre/post FTSE100 membership if listed before/after membership, M – merged, A – acquired.

Chart 11: FTSE100 Survivors – Movements To/From the Conglomerate Category From 1998 To 2003



Key

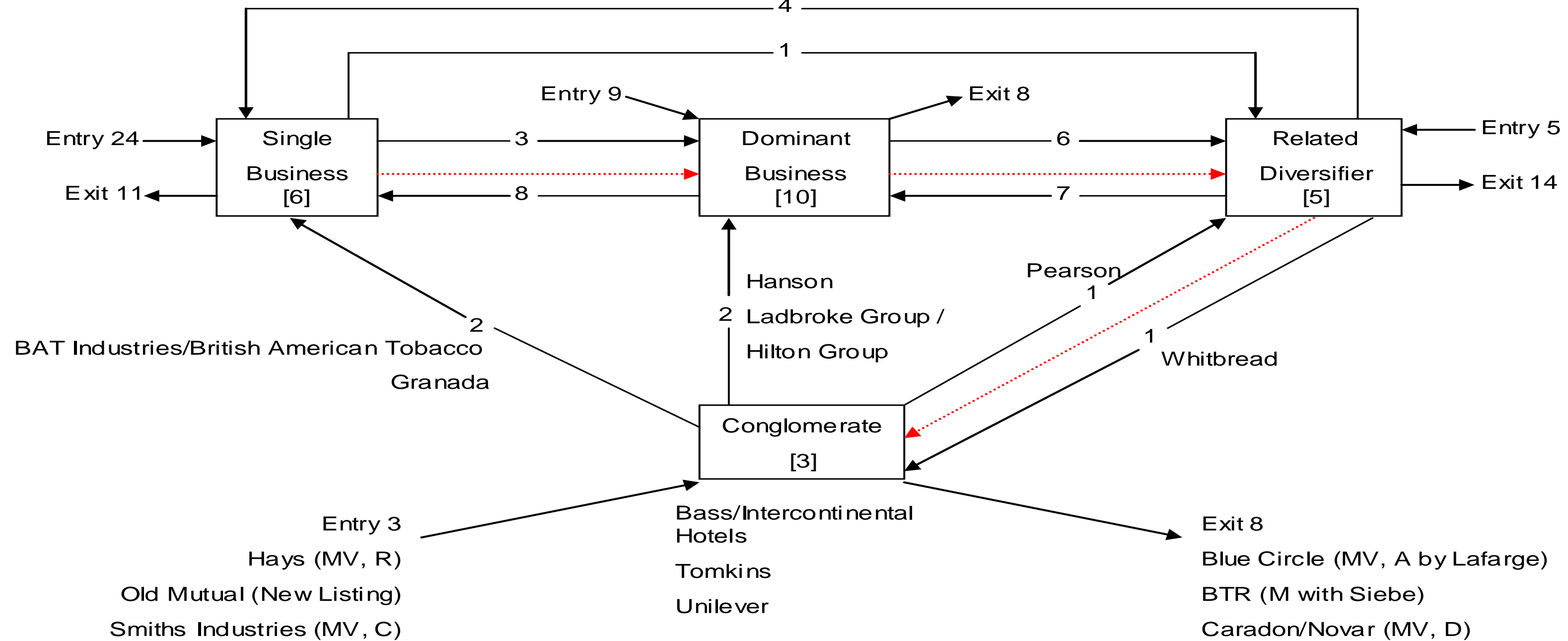
[1] Number of companies remaining in each category at the start and end of the period.

1 Number of companies moving in the direction of the arrow. Conglomerates are named.

Broken red lines denote expected movements through the Model of Corporate Development.

Solid black lines denote the actual movements to/from each diversification category during the period.

Chart 12: FTSE100 – Movements To/From the Conglomerate Category From 1993 To 2003



Key

[1] Number of companies remaining in each category at the start and end of the period.

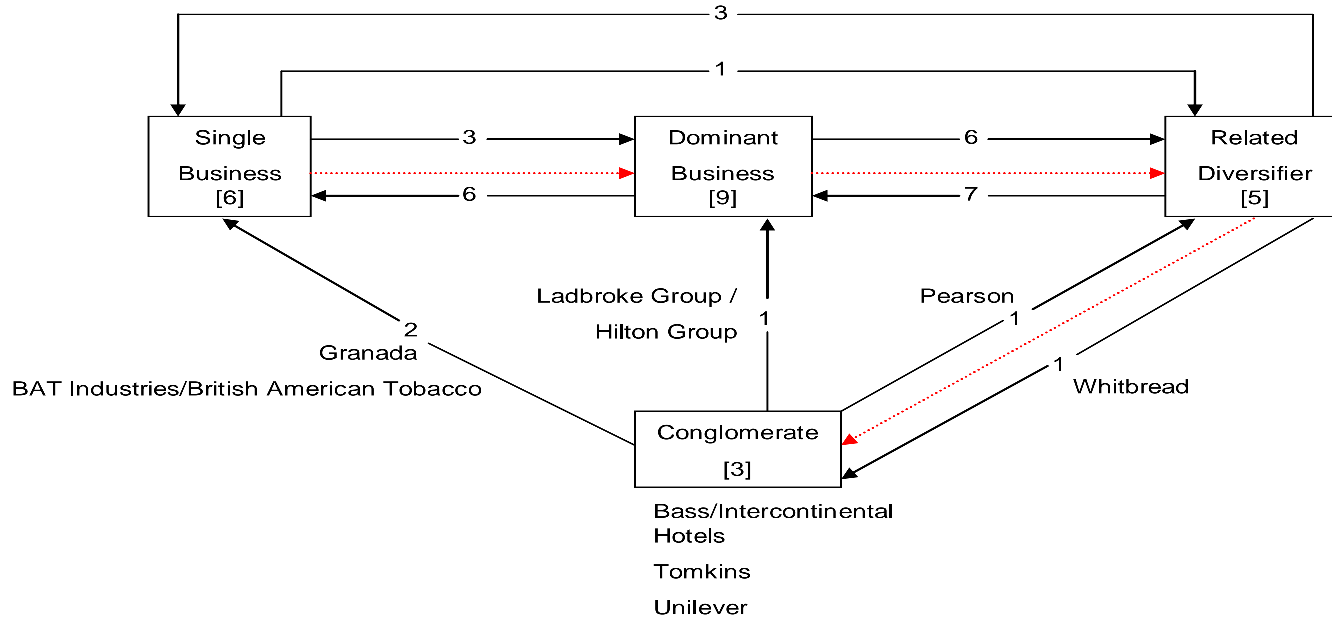
1 Number of companies moving in the direction of the arrow. Conglomerates are named.

Broken red lines denote expected movements through the Model of Corporate Development.

Solid black lines denote the actual movements to/from each diversification category during the period.

Abbreviations: MV – entry/exit due to change in market value, S, D, R, C – category pre/post FTSE100 membership if listed before/after membership, M – merged, A – acquired.

Chart 13: FTSE100 Survivors – Movements To/From the Conglomerate Category From 1993 To 2003



Key

[1] Number of companies remaining in each category at the start and end of the period.

1 Number of companies moving in the direction of the arrow. Conglomerates are named.

Broken red lines denote expected movements through the Model of Corporate Development.

Solid black lines denote the actual movements to/from each diversification category during the period.

7.3 Company Histories

The preceding charts show that there were 22 companies that were categorised as conglomerate at one or more of the period ends. For each of the 22 companies, a brief history has been compiled to look for the strategic rationale behind each decision to retain or change diversification strategy and, if a change was made, how it was achieved.

The histories are grouped under six headings:

- **Stable Conglomerates** – those that remained conglomerates in 1993, 1998 and 2003 – Bass/Intercontinental Hotels, Tomkins and Unilever,

- **Conglomerate Reversals** – those that retreated from conglomeration to become more focused - BAT Industries/British American Tobacco, Ladbroke/Hilton, Granada, Hanson, Siebe/Invensys, Williams and Pearson,

- **Advances to Conglomeration** – those that advanced to conglomeration from other categories – Hays and Whitbread,

- **Temporary Conglomerates** – those that were conglomerates only in 1998 – North West Water/United Utilities and Guinness/Diageo – having been more focused in 1993 and 2003.

- **Conglomerate Exits** – those that left the FTSE100 index – BTR, P&O, Forte, Blue Circle, Caradon/Novar and TI Group,

- **Conglomerate Entries** – those that entered the FTSE100 as conglomerates – Old Mutual and Smiths Industries.

7.3.1 Stable Conglomerates

The following 3 companies, all FTSE100 survivors, Bass/intercontinental Hotels, Tomkins and Unilever, retained their conglomerate strategies throughout the period 1993 to 2003. However, only Unilever retained the same core business activity – foods – throughout while Bass/Intercontinental Hotels moved away from its traditional base in brewing towards hotels and Tomkins divested its largest activity, the Rank Hovis McDougall bakery business. All three companies saw their Herfindahl indices rise between 1993 and 1998 and 2003 indicating greater focus.

7.3.1.1 Bass/Intercontinental Hotels

Bass enjoyed a position of pre-eminence within the UK brewing industry for many years growing through a series of focused acquisitions including those of Mitchells & Butlers in 1961 to form Bass Mitchells & Butlers and of Charrington United in 1967 to form Bass Charrington which was later renamed Bass. However, by 1970 Bass had a 25% share of the UK beer market which effectively precluded it from further non-organic UK expansion as any proposed acquisition would have been referred to, and almost certainly blocked by, the Monopolies and Mergers Commission. The competition

authorities, which in a series of investigations culminating in a report (Competition Commission, 1989) that mandated structural changes (the 'Beer Orders') had sought to introduce greater competition in the brewing industry, would influence the company's strategic decisions through the 1980s and 1990s.

Faced with regulatory restrictions, the company sought growth through international expansion - acquiring brewing businesses in Europe, notably Czechoslovakia – and diversification adding betting shops (Corals), bingo halls (Gala) and gaming machines to its activities. The largest diversification came in 1988 when, through the acquisition of Holiday Inns International, Bass added hotels to its portfolio. By 1993 brewing accounted for 27.8% of total external turnover with public house operations 24.2%, hotels 13.5% and other leisure activities 22.6%. No single activity generated more than 50% of total turnover and therefore the company did not have a core activity. ROCE was 12.9%.

Despite ongoing regulatory interest in the UK brewing sector, in 1996 Bass acquired 50% of the Anglo-Danish brewer Carlsberg-Tetley from Allied Domeq. The transaction, which gave Bass 35% of the UK market compared to Scottish Courage's 31% and Whitbread's 14%, was referred to the Competition Commission and was blocked. This decision, followed by a failed attempt in November 1997 to acquire the William Hill betting business (Nomura outbid Bass), meant Bass had to look to its other activities to generate growth (Ross, 1997).

Bass embarked on a programme to re-balance its portfolio of activities in favour of hotels which were widely seen as offering higher growth and better margins (Willman, 1998). The period from December 1997 to August 1998 saw the group dispose of non-core activities, further develop its hotel operations and return £800m to its shareholders. Divestments, which included Coral betting (sold unconditionally to gaming and hotels group Ladbroke who were subsequently forced to divest the business by the Competition Commission), Gala bingo (sold to management), BLMS (amusement machine servicing sold to private equity), Barcrest (amusement machine manufacture sold to International Game Technology), the tenanted public house estate and 300 managed public houses (sold to Punch Taverns and Enterprise Inns), yielded £1,306m while £1,765m was spent acquiring Intercontinental Hotels in March 1998. Brewing was again the largest activity generating 35.5% of the 1998 turnover with other leisure activities contributing 32.3% and hotels 20.2%. As in 1993, the company did not have a core activity. ROCE had improved to 18.9%.

The 5 years to 2003 saw the company, renamed Six Continents, make further investments in its hotel operations, which became the primary activity, and divest its brewing activities which were sold to Interbrew of Belgium for £2.3bn in 2000. Regulatory issues were again involved with the Competition Commission allowing the sale only on condition that Interbrew subsequently sell its Carling, the UK market leader, Caffrey's and Worthington brands. This requirement was an improvement on the Commission's original order that Interbrew sell all UK brewing activities (Jones, 2001).

In April 2003, the group demerged its remaining retail operations as Mitchells & Butlers and renamed itself Intercontinental Hotels to reflect its primary activity. The 2003 accounts show 69.5% of turnover to have come from hotel operations with soft drinks generating 27.5%. For the first time in the research period, the transformed group had a core activity contributing more than 50% of total turnover. In addition to the change in primary activity from brewing to hotels, Intercontinental Hotels had a narrower spread of business activities as evidenced by its Herfindahl index which had risen from 0.21 in 1993 to 0.29 in 1998 and 0.58 in 2003.

The group's corporate governance also changed through the research period. In 1993 and 1998 the group was headed by an executive chairman, Ian Prosser, who had been appointed in 1987 and had been a director since 1978. The roles of chairman and chief executive were combined and executive directors comprised 60% of the board in 1993 and 50% in 1998. Following the demerger, Ian Prosser retired and Intercontinental Hotels was led by David Webster as non-executive chairman with Richard North appointed as chief executive officer and the percentage of executive directors fell to only 44.4%. The aggregate shareholdings of major shareholders increased significantly following the demerger; having been 3.6% in 1993 and 3.8% in 1998 it rose to 10.6% in 2003.

Bass provides an excellent example of an FTSE100 company that retained its conglomerate strategy but narrowed its activities and changed its portfolio of businesses out of low growth high competition sectors where further

expansion was restricted by competition regulation and into high growth/high margin sectors. The P/E ratio of the company's shares also reflected the improved perception of the company's growth prospects. As a company primarily involved in brewing it had a P/E of only 14.5 in 1993 and 17.3 in 1998 but as a hotels and soft drinks group it had a P/E of 43.4 in 2003 although that was distorted by profit adjustments resulting from the demerger. Vindication of the demerger came in the following years which saw ROCE increase steadily from a demerger cost affected 4.2% in 2003 to 42.5% in 2007 which was substantially higher than that achieved in 1993 and 1998. In addition, the company finally embraced the corporate governance recommendations of the Cadbury committee.

7.3.1.2 Tomkins

In 1993 Tomkins was one of only a handful of companies, that also included Hanson, comprising a conglomerates classification in the FT listings but in 1985 it had only been a small manufacturer of buckles and fasteners. Tomkins' change was achieved through a series of acquisitions made under the leadership of Greg Hutchins, an ex-Hanson executive, who took a 23% stake in the company in 1983 becoming its chief executive in January 1984 (Batchelor, 2000).

The major acquisitions behind Tomkins' impressive growth included those of UK tap and valve manufacturer Pegler-Hattersley for £200m in 1985, baker Rank Hovis McDougall for £952m in 1992 (outbidding Hutchins' former employers Hanson), US gun maker Smith & Wesson for $112m in 1987, US

lawn mower and bicycle company Murray Ohio Manufacturing and diversified US group, Philips Industries.

In 1993 the largest activity generating 32.2% of turnover was bakery followed by professional, garden and leisure products including Spear & Jackson tools with 25.6% and 3 further divisions each with between 11% and 17%. No single activity generated more than 50% of total turnover. The group extolled the virtues of its diversity claiming in its 1993 Annual Report (p7) that "*From being 100% dependent on fastener businesses, we have BROADENED OUR BASE such that no one specific product market accounts for over 10% of pre tax profits*" (emphasis as per original). Furthermore, the broad base, along with earnings per share outperformance and progressive dividend growth, was one of Tomkins' three corporate objectives.

Between 1993 and 1998 the company continued to grow largely through acquisitions including those of automotive/engineering companies Gates for $1.6bn in 1996 and Stant Corporation for £381m in 1997 and 6 Spillers flour mills from Irish food group Kerry for £92m in 1998 (the acquisition, which gave Tomkins a 40% share of the flour milling market, was referred to the MMC who, in 1999, ordered the sale of 4 of the 6 mills acquired). There were also some disposals and rationalisation with the number of reported divisions falling from 5 to 4. While the RHM bakery business continued to be the largest activity in terms of turnover at 35.6% it was closely followed by Industrial & Automotive Engineering with 29.9% and Construction Components with 23.5%. Despite the clear difference between activities, the company stressed

a manufacturing link between its operations and set out its aim *"…to be a focused international manufacturing company"*. Again, no single activity generated more than 50% of total turnover. The 5 years saw significant improvements in financial performance with ROCE increasing from 18.6% in 1993 to 39.4% in 1998.

In 1999 Tomkins decided to move towards its new strategic aim of becoming more focused by demerging its baking and food activities and selling other non-core activities (Marsh, 1999) and returning capital to shareholders through buybacks. The company, whose ROCE had fallen to 34.3% in 1999, acknowledged that the decision, which would leave it focused on automotive and building products, had been made in response to market pressure; *"The stock market doesn't want Tomkins to be a conglomerate any more"* (Marsh, 1999). In addition, the low margins achieved in food businesses coupled with competition regulation restrictions on growth, as evidenced by the Spillers acquisition referral, meant the RHM business was not sufficiently dynamic for Tomkins. The refocusing of Tomkins was seen by many observers as overdue and, coming after the demise of other leading conglomerates including BTR and Hanson, signalling the end of the widely diversified UK conglomerate (Economist, 1999). RHM was sold to UK private equity group, Doughty Hanson, for £1,139m in 2000, the UK and US lawn mower business to Chinese company Summerson Investment for $221m in 2000 and Smith & Wesson to US group Saf-T-Hammer for a mere $15m in 2001 reflecting the raft of potentially costly negligence cases pending in US courts. The group

used the proceeds to reduce debt and to fund a £700m return of capital to shareholders.

By 2003 the group's restructuring was complete and chief executive Greg Hutchins had left. The 'new' Tomkins comprised only three divisions; Industrial & Automotive Engineering, Construction Components and Air Systems Components which generated 64.3%, 21.1% and 14.6% of turnover; industrial & automotive engineering had become the company's core activity. In the following years, the changes continued to bear fruit with ROCE increasing from 15.0% in 2003 to 24.6% in 2007.

The group's corporate governance changed through the research period with a different chairman and chief executive in 1993, 1998 and 2003 and the chairmanship held by a non-executive director in 1993, Michael Moore, and 2003, David Newlands. In 1998 the executive chairman was Greg Hutchins who, until his appointment, had been chief executive since 1984 having become a director the year before. The 'promotion' of a chief executive to chairman contravenes corporate governance Best Practice. However, Tomkins did maintain separation of the roles of chairman and chief executive and decreased the percentage of executive directors from 85.7% in 1993 to 62.5% in 1998 and only 25.0% in 2003. The aggregate shareholdings of major shareholders fell steadily through the research period from 16.7% in 1993 to 12.2% in 2003.

Tomkins provides another example of an FTSE100 company that retained its conglomerate strategy but changed its portfolio of businesses disposing of its primary, but not core, business activity - baking - and building other businesses, notably automotive engineering, which eventually became the core activity, and construction materials. This change is reflected in its Herfindahl index which increased marginally from 0.23 in 1993 to 0.28 in 1998 but, following divestment of RHM, reached 0.48 by 2003. There were also competition regulation influences on Tomkins' strategy. The P/E ratio of the company's shares changed little between 1993 and 2003 falling from 17.2 in 1993 to 11.8 in 1998 before improving to 13.5 in 2003 reflecting the limited growth opportunities in the traditional building and engineering activities that had become the primary businesses of Tomkins.

Finally, with the exception of Greg Hutchins' move from chief executive to chairman in 1995, the company had adopted the major tenets of the Cadbury committee recommendations regarding its corporate governance.

7.3.1.3 Unilever

Unilever, formed in 1930 by the merger of Lever Brothers and Margarine Unie, is a dual listed company (DLC) with the operating companies owned by UK and Dutch holding companies that are quoted on their national stock exchanges. Unilever is one of the world's largest consumer products companies.

The product range produced by Unilever changes constantly in line with the tastes and fashions of its consumers and also as technologies evolve. With the exception of the sale of the group's speciality chemicals activities in 1997 to ICI for £4.9bn (McCoy, 1997) which reduced the 5 divisions reported in 1993 to 4 in 1998 and 2003, the divisions reported by the group – foods, detergents, personal products (toiletries) and other - have changed little over the 10 years of the research period. Following divestment of the speciality chemicals business, the group returned £5bn to shareholders by a special dividend in 1999. Changes in the portfolio of products and brands which comprise each division are a fact of life for 'fast moving consumer goods' companies like Unilever although, given Unilever's size, none of its acquisitions between 1993 and 2003 could be considered major. In 1999 Unilever had 1,800 brands in its portfolio and, recognising that not all made acceptable contributions, intensified its increasingly aggressive approach to disposing of products and brands which were seen as underperforming that began in 1998 (Smit & Willman, 1998; Smith, 1999).

In 1993, 1998 and 2003 the foods division was the core activity of the group generating over 50% of total turnover; 1993 51.5%, 1998 52.1% and 2003 56.1%. The second largest division was the group's traditional detergents activity generating 23.4% of turnover in 1993 with personal products in third place with 14.3%. However, in 1998 the detergents business (21.8%) was overtaken by personal products (24.7%) with the gap between them widening by 2003. The consistency of the company's business portfolio and of the growth of its food turnover is reflected in a Herfindahl index that remains little

changed between 1993 and 2003. The sale of the speciality chemicals activities that contributed 8.4% of 1993 turnover was the driver behind the increase from 0.35 in 1993 to 0.38 in 1998 and changes in the relative sizes of activities is reflected in a further increase to 0.41 by 2003. Unilever has maintained a consistently high level of financial performance and, except for 1995 and 2000, has achieved continuous increases in ROCE which reached 121.1% in 2003. Similarly, investor confidence in the group has always been strong.

Unilever, primarily as a consequence of its DLC structure, has an unconventional corporate governance structure. In 1993, 1998 and 2003 the group was headed by an executive chairman supported by divisional heads rather than a single chief executive or equivalent. In line with recommended practice, Unilever has a majority of non-executive directors.

Unilever provides an example of a dynamic consumer-driven company that remained a conglomerate with a core product – foods – throughout the 10 year research period. However, Unilever did increase its focus disposing of its speciality chemicals activities.

7.3.2 Conglomerate Reversals

The following 4 companies – BAT Industries/British American Tobacco, Ladbroke/Hilton, Granada and Pearson – were conglomerates in 1993 but had retreated from that strategy by 2003, 1998, 2003 and 1998 respectively. In all four cases, the companies took deliberate actions to increase focus;

BAT Industries/British American Tobacco and Granada became single business companies focused on tobacco and television respectively, Ladbroke/Hilton became a dominant business company focused on hotels and Pearson became a related diversifier with activities in education and media including the Financial Times.

7.3.2.1 BAT Industries/British American Tobacco

In 1993 BAT Industries was a conglomerate with a core activity of financial services. By 1998 it had reversed its strategy becoming a focused tobacco business and reverting to its original name of British American Tobacco. It remained a single business company through to 2003. The change in focus and disposal of financial services activities also meant the company moved from the service to industrial/manufacturing sector.

BAT Industries became a conglomerate as a consequence of a deliberate diversification strategy which it embarked upon in the 1970s. The decision to diversify away from a reliance on tobacco products was taken against a background of increasing concerns over the health consequences of tobacco use; research into the links between smoking tobacco and lung cancer had produced increasingly robust and consistent evidence that smoking tobacco was a major cause of the disease. Faced with falling turnover in its established markets of the US and Europe, British American Tobacco decided to diversify while it could still rely on strong cash flows from its 'declining' core business activity. In a series of large acquisitions the company built up a significant presence in financial services buying the insurance companies

Allied Dunbar and Eagle Star in the UK and Farmers Group in the US. Renaming itself BAT Industries, the company also acquired UK catalogue retailer Argos and paper manufacturers Wiggins Teape and Appleton. The diversification strategy adopted by BAT Industries was similar to that pursued by another major UK tobacco company, Imperial, which had diversified into the food, drink and leisure industries. Imperial's acquisitions included food producers Golden Wonder (crisps), National Canning (Smedley's frozen & tinned foods), HP Sauce (condiments), Ross Group (frozen foods), Courage (brewing, off-licences and public houses), Pillsbury Farms (US food producer), plastics companies Creators Group and Plastic Coatings, packaging company Mardon and hotel and restaurant company Howard Johnson.

The diversification strategy was not universally welcomed by investors and in 1989 a 'break-up' bid of £13.4bn was made by Hoylake Investments a consortium headed by Sir James Goldsmith, Lord Rothschild and Kerry Packer. The bid was defeated but, in response, BAT demerged Argos and Wiggins Teape Appleton in 1990 (Kay, 1995). Despite the divestments, by 1993 tobacco accounted for a minority, 46.3%, of the total turnover.

The complexities of effectively managing a group with activities as diverse as financial services and tobacco products together with a greater degree of stability and resilience in tobacco activities and increased access to the large consumer markets of Eastern Europe, especially Russia (Brown-Humes & Oran, 1997), led the group to revise its diversification strategy. Rather than seeking to replace tobacco with financial services, the group sought to

reverse its diversification strategy to once again become a focused, single business tobacco products company.

In September 1997 the company divested its insurance businesses by merging them through a Dual Listing Agreement with those of the Zurich Insurance Company; BAT Industries' shareholders received shares in Allied Zurich plc the UK listed component of the DLC. Recognising the company's focus on tobacco, it reverted back to its original name of British American Tobacco. The company decided that it could continue to be highly profitable in a declining industry by expanding internationally especially into those countries, typically less developed countries, where smoking levels remain relatively unaffected by health concerns and, as incomes rise, may even increase in the short to medium term; globally cigarette sales were rising by 1-2% annually (Willman, 1998). International expansion, typically through the acquisition of local companies, would increase volumes and economies of scale leading to greater profits. The continued decline, albeit slow, in the historically important UK and US markets would have only a limited effect. The first major acquisition, costing £5.3bn, was that of US competitor Rothmans International which added 22 new countries including South Africa, Malaysia, Nigeria and China to British American Tobacco's international spread (Economist, 1999).

The change from conglomerate to single business company in 1997 is reflected in the increase in the group's Herfindahl index which rose from 0.50 in 1993, when turnover was split equally between financial services and

tobacco, to 1.00 in 1998 and 2003, when tobacco was the only activity. Interestingly market sentiment appears negative regarding the company's change from a conglomerate to single business strategy with the P/E ratio declining from 16.6 in 1993, when the company was a conglomerate, to 11.0 in 1998, when it was a single business company, with a marginal recovery to 13.4 by 2003. The group's ROCE best illustrates the positive effect of its return to focus. Between 1993 and 1998 ROCE averaged 20% but significant increases in the new millennium raised the average to almost 50%. The refocusing also attracted institutional investors. After having no significant shareholders in 1993 and 1998, an aggregate 35.0% of the company's ordinary share capital was held by two major shareholders in 2003.

The group's corporate governance was broadly in-line with recommended practice; there were a majority of non-executive directors in 1998 and 2003 and the roles of chairman and chief executive were split. However, when non-executive chairman Patrick Sheehy retired in 1998 when the insurance business was demerged, Mark Broughton, was promoted to chairman but retained his executive status a situation that remained unchanged in 2003.

BAT Industries/British American Tobacco is a prime example of an FTSE100 company that, to escape an industry it expected to decline sharply, diversified its activities but which, on realising there remained opportunities in the global tobacco industry that could profitably be exploited, reversed that strategy. The group, in effect, turned full circle starting and ending as a single business company with a brief period as a conglomerate in between. At the end of

2008, British American Tobacco remained a single business company and a constituent of the FTSE100 index.

7.3.2.2 Granada

Granada Group was a conglomerate without a core activity in 1993 and 1998 but by 2003 it had taken advantage of favourable regulatory changes to become a single business company focused on television.

In 1993 Granada's largest activity was its television rental business which accounted for 33.3% of total turnover with motorway services, business services including catering and workwear, television (broadcast and content and including the Granada television franchise) and computer services, principally contract maintenance, generating 25.7%, 16.1%, 15.9% and 9.0% of total turnover. The company recognised that, with the price of sets falling in real terms year-by-year, television/video rental was a dying business and by 1998 that activity generated only 9.6% of total turnover with motorway services, hotels and television the major activities accounting for 40.5%, 26.1% and 23.7% respectively. The growth in television had come from the acquisition of the London Weekend Television and Yorkshire Tyne Tees franchises following the partial relaxation of multiple ownership restrictions. Much of the growth in the hotels and motorway services activities resulted from the acquisition in 1996 of Forte Hotels Group for £3.9bn. This acquisition was followed by speculation that Granada would split into 2 focused companies; television and hotels and catering (Daneshkhu & Snoddy, 1996). Although still a conglomerate in 1998, the scope of the company's activities

had narrowed, as evidenced by an increase in the Herfindahl index from 0.24 to 0.30.

Between 1998 and 2003 Granada changed substantially; in a complex series of transactions in 2000 and 2001 the company became focused on television and media activities. In 2000 it announced a merger with the FTSE100 business services company Compass Group which would be followed by the demerger of a restructured Compass Group which would comprise all of the combined company's catering and hotels operations leaving Granada a focused television and media company (Ascarelli, 2000). While convoluted, the merger/demerger did achieve its aim of creating two focused companies that had potential to generate significant synergies from two diverse companies. By 2003 Granada television accounted for 99.7% of Granada's turnover and it had a Herfindahl index of 0.99.

Granada's corporate governance shows the company to have met the requirement for a majority of non-executive directors only in 2003 when it was being acquired by Carlton Communications. Gerry Robinson succeeded Alex Bernstein as chairman in 1996 but, unlike his predecessor, retained executive status as did his successor, Clive Allen, on appointment in 2003. Following the announcement of Carlton's acquisition of Granada creating ITV, the institutional shareholders of both companies pressed for the chairman of the new company to be non-executive in accordance with Best Practice (Burt & Malkani, 2003b).

Early in 2004 Granada was acquired by another FTSE100 company, Carlton Communications, to form ITV which effectively consolidated the previously regionalised terrestrial commercial television in the UK. The acquisition received regulatory approval as it was thought that a consolidated ITV would be better placed to compete with the increasing influence of digital and satellite broadcasters such as BSkyB and the publicly funded BBC. This decision was in complete contrast to the stance of the early 1990s when there were 15 UK commercial television companies and multiple ownership was limited (Burt & Malkani, 2003a). In 2008, ITV was still a single business company but had, because of a loss in market value, fallen out of the FTSE100.

Granada provides an example of a conglomerate faced with a declining primary activity, television/video rental, but with other activities offering potential for growth one of which, commercial television, was subject to government regulation that effectively limited growth. The turning point for Granada came when the government began to relax controls over how many commercial television franchises could be owned by a single company offering Granada the opportunity to expand its successful television operations beyond the North West of England. Notwithstanding the complex merger/demerger mechanism it adopted, Granada effectively divested its non-media activities and set about acquiring other commercial television franchises to become a major force in that industry. Given that ownership controls had been removed, acquisition by Carlton Communications to

effectively unite UK commercial television stations was the logical final step for Granada.

7.3.2.3 Hanson

Along with BTR, Hanson is probably one of the best known UK conglomerates of the 1980s and 1990s as were its two leading lights Lords Hanson and White although the latter, controversially given his influence, was never appointed a statutory director of the group. Hanson was born out of the shell of Lord Hanson's family haulage business following the post-war nationalisation of the transport industry and, through a series of seemingly ever-larger acquisitions, grew to be a major company in the FTSE100 index. Such was Hanson's size and resources that by the early 1990s few companies considered themselves safe from the possibility of a takeover bid. In 1991 Hanson bought a stake in ICI giving rise to suggestions that it may bid for the company seen by some as underperforming (Economist, 1991). Ultimately, Hanson did not make a bid for ICI but the threat of a bid is widely regarded as forcing ICI into demerging its pharmaceuticals activities as Zeneca in 1993 (Eglin, 1992).

Hanson's outstanding growth was achieved largely through the acquisition of often of poorly run, underperforming and, as a result, undervalued, companies; the 'classic' 1970s and 1980s route to conglomeration. The largest acquisitions included the diversified tobacco company Imperial (1986), US conglomerate SCM (1985), mining company Consolidated Goldfields (1989), battery company Berec (1981), US coal producer Peabody (1990) and

building products companies London Brick (1984) and Kaiser Cement (1986) (Skeel, 1991).

Unlike some other conglomerates, Hanson did not keep all of the activities of companies it acquired and often sought to reduce the price it paid for the activities it wanted to keep by selling those it did not want. Lublin (1989) noted that between 1973 and April 1989 *'Hanson's US arm spent more than $3.6bn on acquisitions and recouped nearly $2.7bn according to London brokers Hoare Govett'* with the acquisition of SCM standing out as a particularly good deal, *'Hanson paid $930m for SCM, Smith Carona's parent; so far, it has reaped more than $1.5b from SCM asset sales'*. Hanson also divested many of Imperial's non-core activities including Courage beer, Golden Wonder crisps and Ross Young's foods reducing the net cost of the highly profitable tobacco business significantly.

By 1993, Hanson had a turnover of £9,668m, an operating profit of £923m and was the 8th largest company, by market capitalisation, in the FTSE100 with activities as diverse as coal mining and tobacco reflected in a Herfindahl index of only 0.21. The company's ROCE was 10.4% and its P/E ratio of 19.9 suggested investors were confident of future growth.

In mid 1995 Hanson acquired Eastern Electricity for £2.5bn in what proved to be the group's last significant acquisition. Lord White died in August 1995 and Lord Hanson was nearing retirement and the conglomeration strategy they had pursued was no longer in favour with investors who increasingly wanted

to see companies with focus making acquisitions that would produce growth while also yielding synergies (Economist, 1995). In common with other leading UK conglomerates, Hanson took the decision to effectively abandon its conglomeration strategy to become a dominant business company.

Having, in 1995, sold most US business as US Industries, Hanson demerged its non-building materials activities into three new independent companies; Imperial Tobacco, Millennium Chemicals and the Energy Group (which included Eastern Electricity) with shareholders receiving shares in each of the new companies. Imperial Tobacco and the Energy Group were floated on the LSE in 1996 and 1997 respectively while Millennium Chemicals was floated on the New York exchange in 1996. Today, only Imperial Tobacco remains independent; the Energy Group was acquired by Texas Utilities, a US energy group, in 1998 and Millennium Chemicals by Lyondell Chemical in 2004. The demergers, which were completed shortly before Lord Hanson's retirement at the end of 1997, left Hanson a dominant business company focused on building materials. At the end of 1998 the much smaller Hanson had fallen out of the FTSE100 and had a Herfindahl index of 0.75 reflecting its greater focus. The P/E of 15.0 reflected lower growth expectation typical of building material companies where scope for innovation is limited.

Rationalisation of Hanson continued through to 2003 with the disposal of minor activities that had remained after the break-up and the acquisition of additional brick manufacturing businesses. By the end of 2003 Hanson, restored to the FTSE100, was a dominant business company although,

because of the change in relative turnovers of its aggregates and brick activities, its Herfindahl index had fallen to 0.60. In 2007 Hanson was acquired by Heidelberg Cement of Germany leaving Imperial Tobacco as the only surviving independent Hanson business.

Hanson typifies an aggressive company that identified and exploited opportunities to acquire underperforming businesses and realise value by achieving a turnaround and/or through the sale of unwanted assets. As with its peers, Hanson found fewer opportunities in the 1990s and decided to act on investors' desire for greater focus. The influence of Lords Hanson and White were major factors in the company's growth and it is no coincidence that the break-up came within a year of Lord White's death and shortly before Lord Hanson was due to retire.

7.3.2.4 Ladbroke/Hilton

Ladbroke Group was a conglomerate in 1993 with a core activity of betting, including off-track betting offices and Vernon's football pools, which generated 59.5% of its total turnover. Other activities included Hilton Hotels and Texas Homecare, a nationwide DIY chain, which accounted for 20.9% and 16.2% respectively of total turnover.

By 1998 the group had sold its retail activities to a competitor, Sainburys, and had established an alliance with Hilton Hotels Corporation reuniting the Hilton brand in the UK and US (European Report, 1997). The group had also aggressively grown its betting and gaming operations, taking advantage of the

de-regulation of betting shops in 1995, which became the company's core activity generating 79.6% of total turnover. The dominance of the betting and gaming activity would have been greater had the company been allowed to retain the 833 shop Corals business it acquired unconditionally from Bass for £383m in 1997. The acquisition was blocked by the MMC, which ordered Ladbroke to sell the shops 'en block' to restore competition in the UK off-course betting market which was dominated by Ladbroke and William Hill (Daneskhu & Wighton, 1998), in a decision that effectively placed a restriction on the group's ability to grow its UK betting activities. Coral was sold in 1999 to Morgan Grenfell Private Equity. The greater focus had a positive effect on the ROCE which increased from 7.4% in 1993 to 19.0% in 1998.

Ladbroke continued to grow its betting activities internationally and also to develop its hotel business. In early 1999 Ladbroke acquired the Stakis hotels group for £1.2bn (Brice, John & Kibazo, 1999) increasing the number of hotels operated from 54 to 92 and in 2001 it acquired Scandic Hotels which operated in Scandinavia and the Baltic States. Following the Stakis acquisition the group changed its name to Hilton Group. The group continued to be dominated by its betting and gaming activities which, by 2003, generated 81.4% of total turnover. Increased competition in its core activity limited profit growth and ROCE fell to only 10.3% in 2003.

The group's Herfindahl index reflected its transformation from conglomerate to dominant business company between 1993 and 1998 increasing from 0.43 to 0.68 after which it stabilised rising marginally to 0.70 by 2003. Market

sentiment appears to have favoured the group's change in strategy as its P/E ratio increased from 13.9 in 1993 to 15.9 in 1998 and to 18.1 in 2003. In addition, there had been no significant shareholders in the group in 1993 and 1998 but in 2003 there were 4 – Fidelity, Barclays, Scottish Widows and Legal & General – with an aggregate holding of 23.1% of the ordinary share capital.

The group's corporate governance appears to be in accordance with recommended practice with a majority of non-executive directors, separation of the roles of chairman and chief executive and chairmen, John Jackson to 2001 followed by Ian Robinson, who were both non-executive.

The Ladbroke/Hilton Group illustrates a conglomerate that sought to increase its focus by disposing of a peripheral business activity in which it believed it could not achieve critical mass. At the same time, notwithstanding the regulator's refusal to sanction the acquisition of Corals, the group took advantage of legislative changes that increased the potential of its betting and gaming activities. The group had significant market shares and very strong brand names/recognition in its two largest activities – Ladbrokes in betting and Hilton in hotels – while its Texas Homecare operation was small relative to competitors including Homebase, then owned by Sainsbury, B&Q, then owned by Kingfisher and Focus, then owned by Smiths.

Interestingly, in February 2006 the group sold its hotel activities to US company Hilton Hotels International with which it had had an alliance since 1997. The group then changed its name back to Ladbroke and was a single

business company focused on betting activities (Strauss, 2006). At the end of 2008 Ladbroke remained a single business company but, as it returned most of the proceeds of the sale of its hotel activities to its shareholders, had fallen out of the FTSE100.

7.3.2.5 Pearson

Pearson is best known for its ownership of the Financial Times although that was only one of its diverse activities that, in 1993, included the London tourist attraction Madam Tussauds and a minority interest in the Lazards merchant bank. The group was categorised as a conglomerate in 1993 and 1998 before retreating to related diversification by 2003.

In 1993 the core activity of the group was books (primarily information and entertainment but also including education) which accounted for 62.0% of total turnover with newspapers, principally the Financial Times, generating 29.1% of total turnover. In addition Madam Tussauds contributed 6.0% of total turnover and the Thames commercial television franchise another 2.9%. The company also had significant investments in several other television companies/franchises including BSkyB and Yorkshire-Tyne Tees and the Lazards merchant bank although, being related/associated companies their turnovers were not included in that reported. 1993 had seen the start of the company's refocusing with the demerger of its chinaware, Royal Doulton, and US oil services, Camco, businesses.

By 1998 Pearson had divested Madam Tussauds, a number of specialist law, tax and medical publications and a minority interest in satellite broadcaster BSkyB. The disposals were in line with the company's strategy of divesting peripheral activities and specialist publications that were not market leaders (Ford, 1998). Pearson also started to expand its portfolio of FT branded products and its education activities which were bolstered by the acquisition of Simon & Schuster for £2.9bn in 1998. Following the acquisition the education and book activities were separated recognising the size of the enlarged education business and that it included a range of products including CDs and interactive materials that made it substantially different from the entertainment books activity. In 1998 Pearson remained a conglomerate with books still its core activity generating 54.4% of turnover (education 31.2% and other 23.2%) followed by newspapers, 30.3%. The increase in ROCE from 15.8% in 1993 to 47.0% in 1998 suggests the portfolio changes were proving successful.

Between 1998 and 2003 the company continued to pursue its focus strategy divesting Thames Television and its minority investment in Lazards while making acquisitions, principally the $2.5bn purchase of school-testing firm National Computer systems Inc in 1999 and the $482m acquisition of UK publisher Dorling Kindersley, that added to its education activities (Gruner, 2001). In 2003 education was the core activity generating 60.5% of total turnover with newspapers and books each contributing around 20%. Pearson's refocusing activities had moved it from conglomeration to related diversification. The ROCE fell marginally to 13.8% in 2003.

The group's Herfindahl index decreased significantly from 0.48 to 0.27 between 1993 and 1998 reflecting the more even split of turnover across activities but by 2003 it had risen to 0.45 reflecting the increasing size of the education businesses which had become the core activity.

The P/E and significant shareholder statistics provide conflicting evidence of market sentiment towards Pearson and its future prospects. As a conglomerate in 1993 and 1998 the P/E was 33.0 and 30.5 respectively but as a related diversifier in 2003 it had fallen to only 17.9. Conversely, the percentage of ordinary share capital held by major shareholders increased from 8.9% in 1993 to 10.6% in 1998 and to 26.9% in 2003 although that may be a reflection of the share's yield which also rose over the same period from 2.5% to 3.8%.

Corporate governance at Pearson improved over the 10 year research period. Denis Stevenson succeeded Michael Blakenham as executive chairman in 1997 and had relinquished his executive status by 2003 while non-executive directors were in the majority in 1993 and 2003. The roles of chairman and chief executive were kept separate.

Pearson offers an example of a company that had a number of substantial activities; several in one broad industry that was undergoing significant technological change - Media - and others in a range of some smaller specialised businesses, e.g. Madam Tussauds. Through divestments and acquisitions the company narrowed the breadth of its activities developing an

activity – education - that had been a small part of the books division in 1993 into its core activity by 2003. However, in 2002 investors, while praising the greater focus, were becoming critical of the core activity and its low growth prospects (Reed, 2002) suggesting focus is beneficial but only when the core activity is an attractive one.

7.3.2.6 Siebe/Invensys

In 1993 Siebe was a conglomerate with several distinct divisions from controls through to safety & life support systems and property development. The company had grown, principally by acquisition, under the leadership of Barrie Stephens who joined as chief executive in 1964 later becoming chairman as well. Siebe's largest, and core, activity was controls which generated 67.9% of total turnover and overall group ROCE was 18.5%.

By 1998 the company had, through a series of divestments and acquisitions, reduced the breadth of its activities and become a related diversified company with core competences in controls – temperature and appliance - and automation which generated 39.9% and 45.9% of total turnover respectively. Controls were seen as offering slow future growth but the acquisition of APV for £327m in 1997 was believed to have added new potential markets for those products (Lex, 1997). Despite the reduction in the number of activities, the change in the relative turnovers of the remaining activities meant its Herfindahl index decreased from 0.50 to 0.39 suggesting a wider breadth of activities. Between 1993 and 1998 turnover increased from £1,619m to £3,670m, operating profits rose from £217m to £576m and ROCE improved to

38.3% although the P/E ratio fell from 20.0 to 14.7 suggesting investors' future expectations had deteriorated. Management were aware of the need to reinvigorate the business and were, according to the 1998 annual report and accounts, looking to further rationalise the remaining operations to further enhance profitability. Shortly after the March year end it further expanded its controls activity acquiring automation software company Wonderware for £225m (Edgecliffe-Johnson, 1998).

A major change occurred in early 1999 when Siebe acquired troubled FTSE100 conglomerate BTR with the combined company taking the name Invensys. In the 2 years preceding the acquisition both Siebe and, to an even greater extent, BTR had embarked upon rationalisation programmes aimed at improving efficiency, productivity and profitability. Rationalisation continued after the merger and £1bn was returned to shareholders. Further acquisitions, notably that of Dutch software company Baan for £466m in 2000, were made to develop the controls activity that was to form the core of Invensys.

Despite reorganisations and restructurings, which included the disposal of Baan, financial performance was poor leading to a fall in market capitalisation from £9.5bn on formation in 1999 to only £500m in 2003 (Jackson, 2003). At the end of 2003 Invensys, no longer an FTSE100 constituent, was still a related diversifier and, despite the significant divestment programmes, had a Herfindahl index almost unchanged from 1998 at 0.38. The poor performance and ongoing funding problems combined to push ROCE to (100.3)% in 2003.

Having had an executive chairman who was also chief executive and a majority of executive directors, corporate governance improved following the retirement of Barrie Stephens in 1998 before the acquisition of BTR in 1999. The roles of chairman and chief executive were split, the new chairman, Sir Colin Marshall, was a non-executive and the board had a majority of non-executive directors.

Siebe/Invensys exemplifies a company that successfully retreated from conglomeration to related diversification but, faced with lower growth in the activity it had chosen as its core – controls – sought growth through acquisition but chose to buy a company, BTR, beset with fundamental problems typical of the huge conglomerates built up through the 1980s and early 1990s. Lord Marshall, chairman of Siebe, acknowledged that these problems were underestimated and exacerbated by the acquisition of Baan (Marsh, 2003).

7.3.2.7 Williams

Williams Holdings epitomises the conglomerate life cycle. In 18 years it moved through each stage of the Model of Corporate Development before heeding the advice of Whittington (1999) and committing 'corporate euthanasia', by breaking itself up and delisting from the LSE.

Acquired for only £300,000 in 1982 by Sir Nigel Rudd and his business partner Brian McGowan, Williams grew from being a small Caerphilly foundry into a conglomerate with diverse manufacturing and engineering activities

through a series of often small acquisitions of poorly managed underperforming businesses many with well-known brand names including Hammerite, Cuprinol, Rawlplug and Aquilisa (Davidson, 1994). In an interview held as part of this research project, Brian McGowan, a director of Williams until 1993, stated that the success of the group's acquisition-led growth was predicated on identifying underperforming companies with widely respected brand-names that had the potential for rapid turnaround under specialist business improvement teams. The company was renowned for starting the process immediately an acquisition was complete and for implementing their carefully prepared post-acquisition plans.

Larger acquisitions were also made. In 1989 the group acquired security company Yale and fire protection company Kidde. These companies would later comprise the bulk of Williams' activities. However not all of Williams' bids were successful; in 1991 it failed to acquire Racal in a bid worth £753m although the bid did precipitate Racal's subsequent demerger of its Chubb security business. By 1993 Williams was an FTSE100 conglomerate with a core activity of building products. Turnover had grown to £1,164m, operating profits to £189m and the P/E ratio to 19.6. The company's Herfindahl index was 0.43 and its ROCE was 30.7%.

During 1993 Williams revised its corporate strategy replacing its previous opportunistic acquisition-driven strategy with one which aimed to achieve focus in three areas; fire protection, security products and building products. In 1996 the group significantly increased its focus by selling 15 of its home

products business including showers, heaters, conservatories and beds to an MBO team for £360m (Tieman, 1996) and in 1998 a further £500m was received from the sale of European filler and coating and US home improvement businesses. The disposals allowed £300m to be returned to shareholders. The focus strategy was re-enforced in early 1997 when the group acquired the security company Chubb, demerged from Racal in 1992, for £1.3bn. The Chubb acquisition was held up by Williams as offering potential fit, synergies and complementarities with existing Williams businesses (Davidson, 1997) offering further evidence that acquisitions needed to be strategically justified rather than purely opportunistic. By 1998 Williams had become a related diversified company with activities in security products, security systems and home improvement products although the group's Herfindahl index remained broadly constant at 0.43. The group's ROCE reached 65.9% in 1998 and its P/E was 18.4.

After 1998 Williams continued to perform adequately although operating profits fell 4.5% between 1998 and 1999 on turnover 14.6% higher and ROCE fell to 35.0%. The flat performance, lack of obvious growth opportunities and failed discussions with US conglomerate Tyco over a potential $6bn bid for the group (Maremont, 1999) led Williams to decide that splitting the group would enhance shareholder value. In 2000 Williams demerged its activities into two separately quoted focussed companies – Chubb (security) and Kidde (fire protection) – and de-listed from the LSE. Neither business has remained independent; United Technologies Corp. of the US acquired Chubb in 2003 and Kidde in 2005.

Williams provides an example of a company that, in less than 20 years, travelled through all of the stages of the conglomerate life cycle. The company epitomises the serial acquirers of the 1980s that fed on the ready supply of poorly managed underperforming and undervalued companies but were effectively forced to focus when that supply dried up in the 1990s. Williams also illustrates the need to maintain growth as a focused company if the support of investors is to be maintained.

7.3.3 Advances to Conglomeration

Two companies Whitbread and Hays - became conglomerates between 1998 and 2003.

7.3.3.1 Hays

After having been owned by the Kuwait Investment Office since 1980, Hays was refloated on the LSE in October 1989. The company floated was substantially different from the diverse company the KIO had acquired. The property and manufacturing activities had been sold and recruitment added, notably through the 1986 acquisition of Career Care which included the market-leading Accountancy Personnel business, to supplement the distribution and office support services activities. Hays' chief executive likened the company's three divisions to the legs of a stool in the stability they provided (Gabb, 1991).

By 1993 Hays, classified as a business services company, was a related diversifier with a Herfindahl index of 0.47. At the core of the company's

activities was distribution which generated 63.8% of total turnover of £477m. Hays' other activities were personnel (recruitment) and commercial which was primarily a mail service business related to its distribution activity. Distribution and commercial together generated 79.3% of total turnover. Hay's ROCE of 38.5% reflected its profitability and relatively small capital base, typical of service companies, and its P/E ratio of 25.1 its strong growth potential.

By 1998 Hays had entered the FTSE100 but the company still operated the same three divisions as it had in 1993; distribution remained the core activity generating 51.1% of the total turnover of £1,519m but the growing commercial/mail services activity accounted for 31.7% of total turnover up from 15.5% in 1993. Distribution and commercial now generated 82.8% of total turnover. The dominance of distribution would have been greater had the company's 1996 bid of £1.16bn for Christian Salvesen been successful. The bid was seen as a watershed for Hays as the company ruled out further bids for large distribution businesses preferring higher margin specialist over volume distributors (Dyer, 1996) and international expansion where it acquired FDS in France and van der Heijden in the Benelux countries from Australian transport group Mayne Nickless in 1997 for a total of £72m (Gresser & Robinson, 1997). The changes in relative turnovers reduced the Herfindahl index from 0.47 to 0.39 and Hays remained a related diversifier. The financial performance continued to improve with ROCE reaching 49.8% in 1998 and its shares traded on a P/E of 31.9.

Following a strategic review undertaken by the new chief executive, Bob Lawson, on taking office in 2001, the company changed its strategy with the aim of transforming *"Hays into a pure specialist recruitment and HR services business"* (Annual Report & Accounts 2003, p2). While the 2003 annual report shows the company to have the same three activities as in 1993 and 1998, no activity generated more than 50% of turnover. Personnel had become the largest division accounting for 48.3% of the total turnover of £2,294m with distribution, which was earmarked for sale, generating 46.2% and commercial only 5.6% reflecting the disposal of several of the division's businesses. This change in relative turnovers moved the company into the conglomerate category although the Herfindahl index actually rose to 0.45 suggesting greater focus. As a result of incurring substantial restructuring costs, the group made a loss in 2003 and ROCE fell to (161.9)%. Investor confidence, although still high, began to wane with the P/E ratio falling to 22.9. Interestingly, ROCE has since recovered sharply exceeding 100% in 2005 suggesting the change in direction was successful.

Although it moved from related diversification to conglomeration, Hays did not change its activities through the 10 years between 1993 and 2003. However, the company did change its strategy from seeking to maintain stability through operating in three divisions to trying, unsuccessfully, to grow the distribution division to deciding that distribution should be divested in the pursuit of greater focus. These changes in strategy highlight two aspects of diversification strategy; choice of the breadth of activities and of the activities themselves. Hays has reduced the breadth of its activities, although

divestment of distribution did not happen until after 2003, and changed its core activity.

7.3.3.2 Whitbread

The research period saw Whitbread transform itself from a related diversified company centred on brewing and public house retail activities into a conglomerate with hotel, restaurant and leisure club activities.

Whitbread, traditionally a brewer which can trace its heritage back to 1742, had, by 1993, become a related diversifier having added the related activities of public house retailing, including some pub restaurant chains such as Berni Inns and Beefeater, and public house tenancies of which it had 2,300. The 1993 accounts show that the managed public house estate was the company's core activity generating 67.3% of external turnover with brewing and leisure, including hotels, contributing 24.1% and 8.6% respectively. The Herfindahl index was 0.52. In 1993 Whitbread achieved a ROCE of 8.9% and its shares traded on a P/E of 13.9.

The pursuit of related diversification may, in part, have been a reaction to the Competition Commission investigation into the supply of beer (Competition Commission, 1989) and the 'tied house' concept where brewers were able to restrict tenants of their public houses to buying beer and other drinks from them. On grounds of increasing competition, the Commission recommended that no brewer should have a tied estate exceeding 2,000 public houses and that the product restrictions on tenants should be eased although not removed

entirely. The Commission saw its recommendations, the Beer Orders, as having an impact on the 6 national brewers one of which was Whitbread.

By 1998 Whitbread's portfolio of activities had changed significantly. In 1995 the company acquired the 16 Marriott hotels in the UK for £180m from Scott's Hospitality of Canada and also the sports and leisure centre business David Lloyd Leisure for £190m. The hotel acquisition confirmed Whitbread's commitment to the activity adding to the 66 Travel Inns and 30 'full service' hotels it had operated for several years while the leisure centre purchase signalled a move away from brewing and related activities (Buckley, 1995). This re-positioning would have been greater had the agreed £1.05bn purchase of Forte's roadside restaurants, including 430 Little Chef and Happy Eater sites and 26 Welcome Break service stations, and budget hotels - 55 branded Coty in France and 127 Travelodge in the UK - been completed (Blackwell, 1995). Granada's acquisition of Forte stopped the transaction. Whitbread further expanded its restaurants by acquiring Pelican, the operator of Café Rouge and Dome restaurants, for £133.1m in 1996. While remaining in the related diversified category, Whitbread's Herfindahl index had fallen to 0.29 reflecting the wider spread of its activities. Brewing and soft drinks had become the largest activity accounting for 42.6% of total turnover. The change in portfolio had improved performance with ROCE reaching 12.8% in 1998 although the P/E remained little changed from 1993 at 13.5.

The 5 years from 1998 to 2003 saw Whitbread continue to build the strategy initiated before 1998. The company added to its hotel and leisure activities

acquiring the Swallow chain of hotels in 2000 and Cannon's Dutch Health and Fitness activities in 2003. In 2000 the company also tried to acquire the UK retailing interests – off-licences and 3,600 public houses – of Allied Domecq. Had the acquisition been completed, Whitbread's public house estate would have risen to 7,000 and would only have been approved by the Competition Commission on condition that Whitbread's brewing activities were divested (Willman, 1999). Eventually the Allied Domecq estate was acquired by Punch Taverns.

The failure to add to its public house estate was followed by the disposal in May 2000 of the company's brewing activities to Belgium's Interbrew who also acquired the brewing activities of Bass (Beck & Carreyrou, 2000). This was followed by the sale of the public house estate to Morgan Grenfell Private Equity for £1.63bn and the return of £1.1bn to shareholders (Saigol, 2001).

By 2003 Whitbread had become a conglomerate its largest activities being restaurants and hotels which generated 54.7% and 31.9% of total revenues. The Herfindahl index had increased to 0.41. Interestingly, despite the clear differences in operating hotels, restaurants and health clubs, the company saw itself as a 'focussed leisure business' (Whitbread Annual Report & Accounts 2002/03, p2). Neither the company's ROCE, 8.1%, nor P/E ratio, 12.0, was significantly different from those of 1993 but the level of major shareholdings had risen from 4.8% in 1993 to 20.4% in 2003.

Whitbread adhered closely to the corporate governance Code of Practice. Both Sir Michael Angus, chairman in 1993 and 1998, and his successor, Sir John Banham, were non-executive and there was always a separate chief executive officer. The percentage of non-executives on the board increased from 50% in 1993 to 64.3% in 1998 before falling to 54.5% in 2003.

From the end of the 1980s Whitbread, like its fellow brewer Bass, found itself operating in an industry under significant Competition Commission restrictions, via the Beer Orders, on market shares. From 1993 both Whitbread and Bass took steps to move away from their traditional brewing activities with Whitbread finally exiting brewing in 2000 and growing its hotels, restaurants and leisure activities to become a conglomerate by 2003.

7.3.4 Temporary Conglomerates

Guinness/Diageo and North West Water/United Utilities were identified as conglomerates in 1998 only having been a related diversifier and a dominant business company respectively in 1993. By 2003 both companies had refocused their activities with North West Water/United Utilities becoming a related diversifier and Guinness/Diageo a single business company.

7.3.4.1 Guinness/Diageo

Diageo was formed in 1997 by the acquisition of Grand Metropolitan by Guinness. In 1993 Guinness and Grand Metropolitan were both related diversified companies the former having grown through acquisitions, notably that of Distillers in 1986, to become a substantial brewing and spirits

company, the latter had grown, also through acquisitions including US food group Pillsbury for $5.8bn in 1989, to have similar interests in wines and spirits together with another activity, food, including fast food, with brands such as Burger King. Although both were related diversifiers, only Guinness had a core activity, that of its traditional brewing business which included the eponymous stout. Reflecting the greater focus of Guinness, it had a Herfindahl index of 0.52 compared to the 0.38 of the more diversified Grand Metropolitan. The financial performance of the companies showed Grand Metropolitan to be generating higher returns with a ROCE of 22.0% compared to 16.0% at Guinness.

The creation of Diageo was justified on the synergies it would create - £195m by the 3rd year (Willman, 1998b) – by rationalising operations including distribution and administration and ‘managing for value’ with a view to returning cash to shareholders (Willman, 1988a). The 1998 accounts show that Diageo had no core activity although wine and spirits (43.6%) and brewing (30.8%) generated the bulk of its turnover with food (18.3%) a distant third. The new company’s ROCE was 22.9% and its Herfindahl index 0.32.

After 1998 Diageo, through a series of major divestments, underwent significant change retreating from conglomeration to become a single business company focused on premium drinks. The first divestment, the sale of two of its leading brands – Bombay Gin and Dewar’s Scotch – to Bacardi-Martini for £1.15bn, was unavoidable as it was mandated by the Competition Commission when they agreed to Guinness’ acquisition of Grand Metropolitan

(Willman, 1998b). The subsequent divestments were made with the aim of refocusing by divesting the low margin food businesses which faced severe competition as exemplified by Burger King's battle with McDonalds (Jones, 2002). Pillsbury was sold to General Mills for £4.3bn in 2001 and Berger King, after several failed attempts, to a consortium backed by private equity company Texas Pacific for £0.6bn in 2002. Diageo used some of the proceeds from the Pillsbury sale to return £1.7bn to shareholders. In addition to divestments, Diageo also made acquisitions to increase the size and international spread of its spirits activities acquiring Seagram's spirits business for £3.7bn in December 2000 as part of a joint (with Pernod Ricard) break-up acquisition from Vivendi Universal SA of Seagram for £5.62bn (Blackwell & Edgecliffe, 2000).

By 2003 Diageo had divested all but its brewing and spirits businesses which had effectively become, and were reported as, a single activity called Premium Drinks. Diageo was now a single business company with a strategy to expand globally. The group's Herfindahl index was 1.00. According to the annual report (p9), in 2003 Diageo had *'….completed the strategic transition to a focused premium drinks company'*, a process started in 2000. Given the different manufacturing processes for brewing and wines/spirits the amalgamation of the activities into one reported division could understate Diageo's degree of diversification. However, a review of the company's brands shows brewing to be a relatively small part of total activity and therefore separation of the brewing and spirits business would be unlikely to alter categorisation as a single business company.

The ROCE improved each year until 2002 when it reached 31.5% before falling to 10.6% in 2003, a year adversely affected by a £1.5bn loss on disposal of the Berger King business. ROCE recovered to 35.6% in 2004.

Corporate governance at Grand Metropolitan, Guinness and Diageo broadly met Best Practice with a majority of non-executive directors and split roles of chairman and chief executive although only by 2003 was the chairman, Lord Blyth, a non-executive. In 1998 the board was in transition following the creation of Diageo and, unusually, had joint executive chairmen – George Bull from Grand Metropolitan and Anthony Greener from Guinness – and a majority of executive directors. Major shareholdings fell from 23.9% and 3.5% at Guinness and Grand Metropolitan respectively in 1993 to 14.8% in 1998 and zero in 2003 although the unwinding of a cross-shareholding agreement with LMVH (Louis Vuitton Moet Hennessey) which was the only major Guinness shareholder in 1993 and held 10.8% of Diageo in 1998 was a major factor in the reduction.

The refocusing had little effect on investors' view of the company's future prospects. In 1993 the P/E ratios of Guinness and Grand Metropolitan were very similar at 17.8 and 18.2 respectively. A modest improvement was seen in 1998 with an increase to 20.7 following the creation of Diageo but by 2003 it had fallen back to 17.0.

Guinness/Diageo is, notwithstanding the company's amalgamation of its brewing and spirits activities, an example of industry consolidation and the

creation of a global business that divested activities to concentrate its resources in an area offering the greatest potential for growth.

7.3.4.2 North West Water/United Utilities

North West Water was floated on the LSE when the UK government privatised the regional water companies in 1989. In 1993 the company had a small number of related activities, including consultancy and the management of overseas water treatment facilities, but the provision of water and sewerage services to the north west of England remained its dominant activity. One of the drivers for diversification was the perceived need to generate income from businesses that, unlike the core water business which was under the jurisdiction of the Office of Water Regulation (Offwat), were not regulated by the government and therefore did not have price controls or efficiency targets to meet. In 1993 North West Water was a dominant business company with a Herfindahl index of 0.64. Investors saw the group, which achieved a ROCE of 12.0% in 1993, as a low risk/low growth regulated utility and its shares traded on a P/E of only 9.7.

Between 1993 and 1998, the company expanded both its regulated and unregulated activities. In 1995 it acquired Norweb, the regional electricity company covering the north west of England, for £1.8bn to become a multi-utility company and changed its name to United Utilities. However, in order to mitigate the restrictive influence of UK regulators, both Offwat and, for the newly acquired UK electricity business, Offgen, the company continued to build its infrastructure management business and also developed a number of

other non-regulated businesses (Martinson, 1996). These additional activities included a business to compete in the broader UK energy market which was deregulated in 1998, a specialist (business and government) telecommunications company and Vertex, a business process outsourcing company. These changes turned the United Utilities into a conglomerate with a core activity of electricity generation and distribution that accounted for 53.6% of turnover.

The changes pushed ROCE up to 13.6% and the increased potential for future growth in the unregulated activities explains the increase in the P/E ratio to 11.5. Reflecting its broader range of activities, United Utilities' Herfindahl index had fallen to 0.47. However, despite the improvements, investors were unimpressed by the financial performance which had failed to meet the ambitious targets set by the board and forced changes in the chief executive and chairman. In late 1997, the new leadership announced that the company would seek greater focus to restore performance (Holberton, 1997).

The breadth of United Utilities' activities had narrowed by 2003 following the sale of its US electricity business and, in 2000, of its Norweb retail power supply business for £500m to TXU, a subsidiary of Texas Utilities of the US which had also acquired Eastern Electricity in 1998 shortly after its demerger from Hanson. The period saw substantial consolidation through the UK electricity industry with several regional electricity companies being acquired, some by US and European companies. The range potential bidders for Norweb had included UK companies Scottish Power, Scottish & Southern,

National Power and British Energy, European companies Electricite de France, RWE and Viag/Veba and US company AES (Taylor, 2000). In 1999 United Utilities itself was targeted by National Power, which had already acquired Midlands Electricity, but no formal bid was tabled (Taylor, 1999). The substantial reduction of electricity activities was complemented by further growth, largely organic, through the winning of new outsourcing and management contracts, in the company's non-regulated activities.

By 2003 the company had moved back to related diversification although it reported its utility – water and energy – activities together. Had those businesses been separated it is unlikely that the company would have been re-categorised as a conglomerate as, having divested the largest parts of its energy activities with the sale of the US business and largest parts of the UK business, water represented a significant percentage of the Licenced Multi-utility Operations turnover. The refocusing did little to improve performance; ROCE fell to 8.3% and P/E to 9.2 which were close to the pre-diversification 1993 levels.

The company's corporate governance, with the exception of 1993 when Desmond Pitcher was executive chairman, met Best Practice with a majority of non-executive directors, separate chairmen and chief executives and in Clive Harding, between 1998 and 2001, and Roy Evans thereafter, non-executive chairmen. The aggregate holdings of major shareholders have not been significant being 3.5%, 11.3% and 6.4% in 1993, 1998 and 2003.

North West Water/United Utilities is the only utility company amongst the 54 survivors from the 1993 FTSE100 to have been categorised as a conglomerate at the end of 1993, 1998 or 2003. The company sought to diversify its operations to supply not only the water services that it was originally established to provide as a local and then state owned utility company but also electricity, telephone services and business outsourcing. Diversification was seen as a way of reducing reliance on regulated activities with their attendant operational and profit restrictions. However, while the non-regulated diversifications were successful, the utility diversifications were not. The company retreated back towards its original core activity, which it sees as offering growth through greater efficiency over and above that demanded by the regulator, with non-regulated activities providing further growth through increases in volumes.

7.3.5 Conglomerate Exits

Between 1993 and 1998 4 conglomerates left the FTSE100 index. Forte, the hotels group led for many years by Lord Forte and his son, Rocco, was, after an acrimonious hostile takeover battle, acquired by the significantly larger Granada, another FTSE100 conglomerate. Other exits during the 5 year period - Blue Circle, Caradon/Novar and TI Group - were due to losses in market value relative to other listed companies.

The period between 1998 and 2003 saw fewer exits with only 2 conglomerates leaving the index. P&O suffered a loss of market value following the demerger of its substantial cruise line, P&O Princess, which

subsequently entered into a Dual Listing Agreement with Carnival of the US. BTR left the index as a result of its acquisition by Siebe in 1999 by which time it had become a related diversifier.

7.3.5.1 Blue Circle

Blue Circle was, until the 1980s, a company focused on heavy construction materials, especially cement which it had been manufacturing for over 100 years. However, faced with increased competition Blue Circle sought growth through diversification acquiring businesses that manufactured heating and bathroom equipment, including brands like Potterton and Myson in boilers and Armitage Shanks and Ceramica Dolomite in bathrooms. By 1993 Blue Circle was a conglomerate with two principal activities - heavy building materials and home products - which generated 49.2% and 48.9% of total external turnover; the group's Herfindahl index was 0.48. The 1993 annual report noted the company considered both activities core and worthy of further investment creating the potential for conflicting demands for the available funds.

Between 1993 and 1998 Blue Circle's activities changed little although, in line with peers including Cemex of Mexico and Holderbank of Switzerland, it expanded internationally especially in Asia spending more than £700m in 1998 acquiring cement businesses in Malaysia, Singapore and the Philippines (John, 1999). By 1998 heavy building materials was the core activity generating 63.4% of the group's turnover compared to only 35.4% from home products and the Herfindahl index rose to 0.53 primarily reflecting changes in relative turnovers. Profits remained broadly constant through the period.

Investors appeared unconvinced of the company's strategy and its shares traded on a P/E of only 10.9 at the end of 1998 despite ROCE increasing from 10.7% to 14.7%. The fall in share price and market capitalisation caused Blue Circle to fall from the FTSE100.

Shortly after the 1998 year end, despite its reiterated commitment to both activities, Blue Circle signalled its intention to move back to greater focus with the sale of its bathrooms business to American Standard for £253m (Smy, 1999). This change in strategy was re-enforced by the sale of the heating businesses to Baxi Partnerships, a Lancashire co-operative group, for £480m in late 1999 and comment from the new chief executive, Rick Haythornthwaite, that the company intended to focus on its heavy building materials activities (Batchelor, 2000). The new strategy was given little opportunity to bear fruit as, after rejecting an initially hostile bid and returning £800m to shareholders in 2000, the Blue Circle board recommended a second friendly takeover bid in 2001 of £3.1bn from the French company Lafarge, which had acquired fellow FTSE100 building materials company Redland in 1997, thereby creating the world's largest cement manufacturer (Skapinker, 2001).

Blue Circle was another UK company that chose diversification as a means of reducing its reliance on a competitive industry. Having effectively diversified to the point where it had two broadly equal business activities, Blue Circle found itself unable to fund growth in both and therefore had to refocus. As with Forte, investors had, despite the diversification, endured several years of

stagnant growth and were happy to accept Lafarge's offer which even the board believed represented good value.

7.3.5.2 BTR

The rise to prominence of BTR (originally floated in 1934 as British Tyre and Rubber) was similar to that of Hanson in that it was led by a strong personality, Sir Owen Green. Through a series of, often hostile, acquisitions, of underperforming and undervalued businesses including Thomas Tilling (1983), Dunlop (1985) and Hawker Siddeley (1990) BTR grew into a global group with activities as diverse as branded sports goods, including Dunlop and Slazenger, and heavy engineering. However, BTR's takeover bids were not always successful; hostile bids of £1.2bn for UK based glass-maker Pilkington and $1.6bn for US-based engineer Norton were defeated in 1986 and 1990 respectively. The early 1990s saw a major change in BTR's strategy following the appointment of Alan Jackson as chief executive in 1991. After years of serial acquisition with few divestments the group began to sell businesses it felt could not become world leaders; in 1991 the Pretty Polly hosiery business was sold to US company Sara Lee for £117.5m. BTR was now seeking greater focus in those businesses that offered profitable and sustainable growth and market leadership (Economist, 1991).

In 1993 BTR was the 9th largest company, by market capitalisation, in the FTSE100 with a value of £12,976m. It had a turnover of £8,422m, operating profits of £1,292m and, reflecting its diversity, a very low Herfindahl index of 0.21. BTR did not have a core activity and its 3 largest divisions each

contributed around 24% of total external turnover. The company achieved a ROCE of 24.0% and its shares traded on a P/E ratio of 20.9 suggesting investors continued to hold it in high regard and thought it had a strong future. In 1993 BTR's executive chairman Sir Owen Green retired with Norman Ireland, a director for 24 years, replacing him.

Norman Ireland's first year at the helm proved challenging as BTR began to lose the confidence of investors. The problems started when, after years of substantial growth, in September 1994 BTR announced pre-tax profits for the first half of the year were only 12% higher than the previous year suggesting that the bubble had burst. Furthermore, it was implied that the company's historically high sales margins were under severe pressure and could fall. From late 1994 onward, except for a few brief rallies, the BTR share price lost ground relative to the FTSE100 index and the announcement of the impending retirements of Ireland and chief executive officer Alan Jackson highlighted the lack of natural successors to the top executive positions. The team that had built BTR had all retired and the company would be run by 'outsiders'. In 1996 BTR reported half year profits, excluding £622m restructuring costs, down 14% on the previous year and announced it would be divesting low-growth businesses that were generating 26%, approx. £2.3bn, of total turnover (Parker-Pope, 1996). Analysts remained sceptical of BTR's ability to restore profitability through its new strategy, which would leave its conglomerate status unchanged, of focusing on 4 global businesses; automotive, process controls, power drivers and packaging (Tieman, 1996). Despite achieving some success in realising the divestment programme,

BTR's problems did not recede in 1997 and in September a further round of divestments representing another 36% or £2.8bn of total turnover were announced. This second tranche of divestments included the packaging business seen only 12 months earlier as being a core activity (Tieman, 1997). The deterioration in the company's fortunes led to a 5th profit warning in 3 years (Edgecliffe-Johnson, 1997). The 1997 accounts, the last BTR were to publish as an independent company, show its disposal programme to have increased focus, raising the Herfindahl index to 0.52, and that engineering activities accounted for 68.4% of total turnover of £7,435m. At the end of 1998 BTR was in 72nd place in the FTSE100 with a value of £4,004m, a third of its 1993 value.

Early in 1999 BTR was acquired by Siebe, a fellow FTSE100 company, to create Invensys. The rationale behind the deal, which was presented as a merger, was the creation of a global group with a core competency and leadership in controls and automation. Invensys believed it would achieve significant synergies through the rationalisation of operations and activities restoring shareholder value that had fallen at both Siebe and BTR. Almost since its creation, Invensys has experienced serious financial problems, many legacies from BTR and Siebe, which were exacerbated by its failure to complete disposal programmes or to achieve the expected sale proceeds for some businesses. Invensys fell out of the FTSE100 although it remains in the FTSE250 and, after further financial restructurings and rights issues, has begun to recover.

BTR in its heyday was, like Hanson and Williams, described as a ‘deal-making machine’ growing by acquiring underperforming and undervalued companies; the ‘classic’ route to conglomeration. However, when the pool of suitable acquisitions began to dry up in the early 1990s and BTR’s long-standing management team began to retire, the company found it difficult to manage the widely diverse conglomerate that had been created. The strategy was changed but not soon enough and, after significant deteriorations in performance and investor confidence that saw massive reductions in market value, BTR lost its independence.

7.3.5.3 Caradon/Novar

Caradon, which later changed its name to Novar, was a conglomerate in 1993 when it was 65th in the FTSE100. Its core activity – building products – accounted for 65.5% of total turnover with two other activities – automotive and security printing – generating 13.6% and 21.0% respectively. The company’s Herfindahl index was 0.49 and, with a P/E of 33.5, investors appeared confident that it would enjoy significant future growth and maintain its high level of return – 1993 ROCE was 35.3%. The 1993 annual report and accounts notes that the year saw significant changes at the group with the disposal of an investment in CarnaudMetalbox and the acquisition of a substantial part of RTZ’s Pillar building products division.

While Caradon continued to perform well in 1995, from 1996 it began to struggle in the face of increased competition, especially price competition in window, doors and bathroom products. Caradon was also marked down by

analysts who believed it had overpaid for acquisitions including that of Pillar (Pretzlik, 1999). The company responded by embarking on a reversal of its diversification strategy; non-core activities would be divested to increase focus on the core building products activities (London, 1996). Between 1994 and early 1999 divestments reduced the number of operating businesses from 60 to 24 and allowed the return of capital to its shareholders. The falling share price together with share repurchases caused Caradon to fall out of the FTSE100. By the end of 1998 the company had retreated back from conglomeration to become a dominant business company with building products generating 83.4% of external turnover and security printing 16.6%. The company's Herfindahl index had risen to 0.72 reflecting its narrower spread of activities. The 1998 financial performance was substantially worse than 1993 with ROCE of (21.8)% and poor investor expectations were reflected in a P/E ratio of only 8.3.

Caradon continued to divest non-core activities in 1999 with the sale of its doors and windows businesses in Germany and the US and of its bathroom/heating businesses, including Mira showers and Ideal boilers, in 2000. The sale of the bathroom business (Rivlin, 2000) came only a year after the company had failed in a bid to acquire Blue Circle's heating businesses. Caradon reinvested some of the disposal proceeds in acquiring building materials businesses. Despite the extent of the strategic changes at Caradon, some shareholders thought it could and should have gone further and the UK Active Value Fund tried, though a special meeting in 2000, to force the company to return a further £130m to shareholders and dispose of two

divisions to become a single business company (Felstead, 2000); the resolutions were defeated in what was effectively a vote of confidence in the board. At the end of 2003, Caradon, renamed Novar, remained a dominant business company although its Herfindahl index had fallen to 0.63 suggesting greater diversification than in 1998. The increased focus achieved through the divestment programme saw some recovery in ROCE to (8.5)% and a P/E ratio of 13.8 suggesting either the recovery was underway or a takeover was likely.

In 2005, the company was, after an initial approach from private equity company Melrose, acquired by Honeywell who intended to break-up the business retaining only some of the building products businesses (Orr, 2004).

Caradon, with its 60 operating business in 1994, epitomised the diverse conglomerate. From 1994 onwards several of the company's key businesses faced severe competition forcing it to refocus to restore shareholder value and returns. Caradon did not have regulatory issues in any of its activities but that also suggests it did not have sufficient size or critical mass in any business hampering its ability to compete effectively on price which was a major problem for its businesses.

7.3.5.4 Forte

Starting in 1936 with a small milk bar in London's Regent Street financed with £2,000, Charles (later Lord) Forte and then his son, Sir Rocco Forte, built a hotels and restaurants group with interests ranging from Little Chef and Happy Eater roadside cafes through budget hotel chains like Posthouse and

Travelodge to exclusive hotels such as London's Claridges and Hyde Park. The company, although best known for its hotels activities, included substantial restaurant and contract catering activities that led to its categorisation as a conglomerate. At the end of 1993, Forte had a Herfindahl index of 0.34 reporting 4 divisions and 2 unrelated activities; hotels and restaurants/contract catering.

The mid 1990s saw Forte embark on a restructuring and rationalisation programme to improve the quality of its services and achieve greater focus. The company sold its Gardner Merchant contract catering business, Alpha airport food business and a number of hotels deemed 'non-core'. At the same time it expanded internationally acquiring additional overseas hotels; in 1995 it acquired the 54 hotel Meriden chain in France for £215m. In an interview in 1995, Sir Rocco Forte outlined a strategy of developing an international 5 star hotel business (Davidson, 1995) and acquisitions such as that of Meriden were consistent with that strategy.

In 1996 Forte was acquired for £3.9bn by Granada Group, another FTSE100 conglomerate, after a hostile and very acrimonious takeover battle. Granada had little interest in Forte's luxury hotels including the Meriden and Exclusive chains, which it pledged to sell in its offer documents, but wanted the high volume budget hotels and roadside restaurants. In making its bid, Granada was taking advantage of Forte's poor performance and the low level of shareholder confidence in the conglomerate. A P/E ratio of 20.5 suggests investors had a positive view of the company at the end of 1993 when it was

72nd in the FTSE100. However, the company stagnated in the following years with ROCE decreasing marginally from 7.3% to 6.6% by 1995. Forte addressed the shareholder concerns in its defence documents effectively renouncing its conglomerate strategy in favour of focus on hotels which was to be achieved through the sale of the roadside restaurants and Travelodge hotels to Whitbread for £1.05bn. Forte also pledged to return £800m to shareholders and annual dividend growth of 20% to January 1999 (Cozens, 1996).

The Granada bid was successful although the Competition Commission expressed concern regarding the number of motorway service areas controlled by the enlarged group and required the sale of all 21 of Forte's Welcome Break service areas and 4 motorway sites acquired for future development. The CC also imposed price limits on the services offered at Forte sites through the period until their sale (Daneshkhu, 1996). However, given that no more could be added, service areas were seen as offering only moderate growth as compared to the turnaround opportunities offered by the Happy Eater and Little Chef restaurant chains and therefore the CC's conditions were not considered a problem. After completing the acquisition Granada wasted no time in absorbing Forte's operations and making considerable cost savings while reinvigorating the roadside restaurants (Cassell, 1996).

Forte provides an example of a conglomerate that, realising its performance had deteriorated, embarked on a strategy to return to greater focus.

Unfortunately, the strategy fell short of what was expected by shareholders providing a predator, Granada, an opportunity to acquire the company. The Forte bid defence offered its shareholders even greater focus with the planned divestment of high volume activities to Whitbread but with no guarantee of success. The Granada bid effectively offered Forte shareholders a choice as to whether to support the incumbent Forte management in an example of Porter's Market for Corporate Control.

7.3.5.5 P&O

P&O (the Peninsular and Oriental Steam Navigation Company), formed in 1837 to fulfil a contract to transport mail to Portugal and Spain, was one of the oldest companies quoted on the LSE. Until the 1970s when *'shipbuilding prices boomed, the empire collapsed, air travel took off, and tanker rates plummeted'* (Jowit, 2000) shipping, both cargo and passenger, was its core activity. However, the decline of traditional markets necessitated significant changes including the introduction of containerised shipping, the replacement of passenger liners with cruise liners and diversification. A series of acquisitions added construction and property development, warehousing, tools, catering, security and exhibition centres transforming P&O into a conglomerate. In 1993 P&O's Herfindahl index was 0.24. The company, which was 43rd in the FTSE100, enjoyed a high investor rating with a P/E ratio of 35.1 reflecting strong future expectations and achieved a ROCE of 14.5%.

After 1993, P&O's performance, and its rating amongst investors, deteriorated as concerns grew over the effect the newly opened Channel Tunnel was

having on ferry operations and problems in construction and container shipping. In response to these issues, P&O embarked on a £1bn disposal programme, with proceeds to be reinvested in cruise ships, to refocus around the core shipping operations (Tieman, 1996). Earmarked for disposal were the Bovis construction businesses, investment properties, including Manchester's Arndale Centre, and several small ports businesses. In addition, the group also restructured several of its businesses transferring some to joint ventures although there were some competition issues. In 1996 its English Channel ferry operations were merged with those of competitor Stena Line in a 60:40 joint venture. As the enlarged ferry operator had a significant cross-channel market share, the transaction was investigated by the CC but, as it meant ferry services would be maintained and continue to provide consumer choice and competition for the loss-making Eurotunnel, allowed to proceed. In 1997 P&O put its container operations in a 50:50 joint venture with Koninklijke Nedlloyd Groep of the Netherlands creating the world's leading container shipping line and the potential for significant cost savings. The benefits of the restructuring had yet to be fully realised in 1998 - the P/E had fallen to only 15.3 in line with an ROCE that had deteriorated to only 10.2% with some analysts remaining unconvinced by the restructuring (Gresser, 1997).

The company's failure to restore investor confidence drove it to announce a further rationalisation programme in 1999 (Bernholt & Kibazo, 1999). The construction company, Bovis, was sold to Lend Lease, an Australian property group, for £285m in 1999 and several investment properties were sold generating a further £650m. The company also prepared to float its container

joint venture, P&O Nedlloyd, although that divestment was not fully completed until early 2004. Over the same period the group invested £800m in its international ports activities and, primarily to release shareholder value, floated its substantial cruise line business as P&O Princess in 2000. As a result of the demerger, the group became a related diversified company and, because of the fall in its market capitalisation – down to £1.74bn from a 1998 peak of £4.6bn - fell out of the FTSE100. The return to greater focus failed to improve the group's performance and by 2003 ROCE had fallen to only 4.7%.

P&O was acquired by Dubai Ports World for £3.9bn in 2006 (Tait, 2006) while the single business company P&O Princess, after a brief period as an FTSE100 company, merged in 2003 with Carnival Cruises of the US with the enlarged company taking a DLC structure retaining membership of the FTSE100 and S&P500 indices.

P&O is an example of a company that, faced with structural and technological change in its core businesses, saw diversification as essential. However, conglomeration failed to stabilise profitability and investor sentiment pushed the company back towards greater focus and the re-development of one of its original core activities, the cruise line, which was eventually floated partly to create two more focused companies and partly to release shareholder value.

7.3.5.6 TI Group

TI Group, formerly Tube Investments, was created in 1919 by a merger between Midlands-based tube manufacturers and distributors. By the 1980s,

TI's business portfolio was dominated not by the original tube businesses, which were still owned, but by a range of branded consumer products businesses including cookers, kettles, heaters and bicycles. The intense competition in these markets, exemplified by that in the cycle market where low cost foreign imports were gaining market share, impacted negatively on TI's profitability and necessitated significant portfolio change (Lorenz, 1996).

By 1993, through a series of acquisitions and divestments, the business portfolio of TI changed; consumer products businesses were divested and aerospace, seals and automotive components businesses acquired. The transforming deals were the sale of the Creda appliances business to GEC in 1987 and the acquisitions of US mechanical seals company John Crane Houdaille and small bore tube manufacturer Bundy Corporation in 1987 and 1988 respectively. In addition to repositioning the group as a tube and seals manufacturer, the transactions increased geographic spread reducing reliance on UK and Commonwealth markets. The final stage in the transformation was the acquisition of Dowty for £509m in 1992 which, after unwanted activities were divested to Cray Electronics, added aerospace activities to the group and moved it into the FTSE100.

The 1993 accounts show TI to be a conglomerate with a relatively balanced portfolio of engineering, polymers/seals and aerospace activities that was 88th in the FTSE100 and had a Herfindahl index of 0.35. The group's financial performance was good with a ROCE of 21.4% and a P/E ratio of 27.4 reflecting strong investor confidence in the group.

Between 1993 and 1998 TI's portfolio remained unchanged although the group did make three acquisitions; Swedish seals manufacturer Forsheda for £189m in 1996, US automotive engineering components company S&H Fabricating & Engineering for £212m in 1998 and UK engineering and aerospace company EIS for £267m also in 1998. There were also disposals of small non-core businesses. By 1998 the polymers/seals and engineering businesses had grown to generate 40.1% and 38.2% of turnover respectively and were each almost twice as large as the aerospace division which produced 21.7% of turnover. The Herfindahl index at 0.35 remained virtually unchanged. The company remained profitable with ROCE at 33.6% although lack of support amongst investors for engineering stocks meant the P/E had fallen to only 10.3 and the reduction in the group's market capitalisation had caused it to fall out of the FTSE100 in December 1997.

After 1998, TI continued to make targeted acquisitions buying US automotive components company Walbro Corporation for £393m and German polymer company Busak + Shamban for £275m in 1999 (Larsen, 1999). However, the financial performance of the company began to falter with ROCE down to 24.4% and analysts expressing concern that TI had no interest in aircraft electronics which offered substantial future growth (March & Larsen, 1999). In order restore its fortunes and boost shareholder value, TI looked for a partner entering talks with UK engineering company BBA but the discussions proved unsuccessful as insufficient synergies could be identified and BBA were unhappy at TI's level of exposure to the increasingly competitive automotive industry (Malkani, 1999). In 2000, in the aftermath of the failed talks with BBA,

TI was acquired by Smiths Industries, an FTSE100 conglomerate with significant aerospace activities, for £1.8bn and a pledge to return to shareholders up to £1.2bn of the proceeds from the planned disposal of TI's automotive businesses. Smiths wanted TI's aerospace activities and has, albeit slowly, since undertaken a disposal programme to divest it's other activities.

The changes at TI were achieved in a corporate governance environment that improved through the 1990s. The roles of chairman and chief executive were split in 1998 although there remained a majority of executive directors.

TI is an example of a company that, in response to market forces, made significant changes to its portfolio of activities but retained its conglomerate strategy with no activity generating more than 50% of total turnover.

7.3.6 Conglomerate Entries

Only 2 companies entered the FTSE100 as conglomerates; Smiths Industries between 1993 and 1998 and Old Mutual between 1998 and 2003.

7.3.6.1 Old Mutual

Old Mutual was the only conglomerate to enter the FTSE100 between 1998 and 2003. Although the majority of its business activities, which include insurance, banking and asset management, were located in South Africa, the company saw the LSE as offering better access to international capital markets and chose it for its primary listing on demutualisation, which had been

driven by the need to grow internationally, in 1999 (Ashurst, 1997). In deciding to list in London, Old Mutual was following fellow South African companies; miners Billiton and Anglo American and brewer South African Breweries (Wright, 1999). Because of its size, Old Mutual immediately became a constituent of the FTSE100.

Within a year of listing, Old mutual made a series of acquisitions that built on existing operations and reduced its reliance on its traditional South African businesses; the group aimed to derive 20% to 30% of income from outside South Africa within 3 to 5 years of floatation. This internationalisation of the group was necessary given South Africa’s high, compared to developed countries, risk of civil unrest and weak currency. The first major acquisition was that of financial services company Gerrard for £525m followed by that of US fund manager, United Asset Management (UAM), for £1.5bn plus a further $420m to gain control of a UAM associate company (Croft, 2000). The acquisitions, which did not broaden the company’s activities, reduced the percentage of income derived in South Africa from 90% to 75% (Targett, 2000). In 2001 the company added to its US operations, acquiring Fidelity and Guaranty Life Insurance for £441m and a number of smaller businesses (Bolger, 2001). In 2003 Old Mutual was a conglomerate with a Herfindahl index of 0.45 and its corporate governance was in line with Best Practice.

Old Mutual is unique amongst FTSE100 companies; a ‘foreign’ conglomerate that joined on demutualisation. The company has changed since floatation but rather than using acquisitions and divestments to achieve greater focus it has

used them to internationalise its activities and reduce reliance on its traditional South African businesses.

7.3.6.2 Smiths Industries

Smiths Industries has moved a long way from its origins as a watchmaker founded in 1851 by Samuel Smith. The company's diversification started in 1904 when motor accessories were added followed by altimeters which marked its entry into aerospace (Kay, 1992) which was its core activity in 1993 generating 54.1% of turnover alongside medical systems, 24.9%, and various industrial activities, 20.9%. The automotive activities that in 1982 generated 70% of turnover had been divested in the late 1980s. Smiths' development had been achieved through a mix of acquisitive and organic growth from successfully tendering for contracts with customers such as aircraft maker Boeing and British Aerospace. In 1993 the company, not an FTSE100 constituent, was a conglomerate with a Herfindahl of 0.40 achieving a healthy ROCE of 27.2%. The P/E ratio of 18.4 suggested investors were cautiously optimistic regarding its future prospects.

Between 1993 and 1998 on the back of strong financial performance - turnover increased from £726m in 1993 to £1,199m, operating profit rose from £106m to £240m and ROCE from 27.2% to 56.2% - Smiths gained entry to the FTSE100. Investors remained cautiously optimistic of future prospects with the P/E ratio broadly static at 17.8. The period also saw improvement in corporate governance with the splitting of the roles of chairman and chief executive in 1996 although the chairman, Sir Roger Hurn, retained his

executive status. While no major acquisitions were made, Smiths sought to reduce its reliance on the UK and US markets through expansion in Asia. The company remained a conglomerate and its Herfindahl fell to 0.34 reflecting a more even spread of activity across its three businesses – aerospace (38.6%), medical systems (28.7%) and industrial (32.6%).

Acquisitions, with the aim of expanding existing aerospace activities, were the driver of growth between 1998 and 2003. In 1999 the company acquired the aerospace business of Invensys, which was seeking to refocus its activities around controls, for £109m (Malkani, 1999) and in 2000 it acquired TI Group for £1.8bn with a further payment of up to £1.2bn dependent on the divestment of TI's automotive businesses. Undoubtedly, TI's aerospace business attracted Smiths but the acquisition, in addition to automotive components, brought seals and engineering businesses that increased diversity in the short term. Investors and analysts were not convinced of the benefits of the acquisition especially as the potential for synergies was talked down by Smiths (Wachman, 2000). In 2001 Smiths finally divested the automotive components businesses but only after a protracted and complicated process including debt-for-equity swaps, outside financing and MBOs that gave Smiths and TI's old shareholders 19.9% and 55% respectively of a new company, TI Automotive (Eaglesham, 2001). There have since been further divestments of TI businesses, notably the sale of the seals business to Swedish company Trelleborg AB for £495m in late 2003.

Notwithstanding the disposal of the automotive activities, the TI acquisition increased Smiths diversity and its Herfindahl index fell to 0.30 in 2003. However, the enlarged company's 2003 performance improved over that of 1998 with ROCE up to 31.8%. The P/E ratio of 13.2 suggested investors were uncertain of future performance.

Smiths maintained its conglomerate strategy throughout the research period and, in contrast to its peers, became steadily more diversified in terms of its Herfindahl index which was 0.40 in 1993 and 0.30 in 2003. Furthermore, while in 1993 Smiths had a core activity – aerospace generating 54.1% of total external turnover – there was no core business in 1998 and 2003 despite the acquisition of TI's aerospace business doubling its aerospace activities.

7.4 Analysis

The brief company histories of FTSE100 companies that were conglomerates at the end of 1993, 1998 and/or 2003 has provided some insight into the drivers behind their adoption, maintenance and/or abandonment of conglomeration. The histories clearly show that, despite the inherent uniqueness and complexity of the companies involved, there were similarities in the external factors they faced, their strategic responses to those catalysts for change and the effects implementation of those responses had on their levels of diversification. The following table summarises key points from each company's history to show changes in external factors (drivers), changes in corporate strategy (strategic response/restructuring) and changes in size/scope/diversity (outcomes).

Table 82: Drivers for Strategic Change in Conglomerates

Company	Category[1]			Stability/ Consistency		External Drivers[4]			Strategic Responses/Restructuring[5]					Outcomes[6]					
							Fin/	Regu	Dis-	De-	Return	Key Acq'ns		MoCD	Herfindahl		Core/Dominant Acty		
	93	98	03	Quote[2]	Strat[3]	None	Mkts	lation	posal	merger	Capital	E/N	Int'l	A/R/S	Focus	Divers	93	03	Same
Bass/Intercontinental Hotels	C	C	C	Y	Y			Y	Y	Y	Y	E	Y	S	+			Y	
BAT/British American Tobacco	C	S	S	Y			Y		Y	Y	Y	E	Y	R	+		Y	Y	
Blue Circle[7]	C	C*			Y		Y		Y		Y	E	Y	S	+			Y	
BTR[7]	C	C			Y		Y		Y		Y			S	+			Y	
Caradon/Novar	C	D*	D*	Y	Y		Y		Y		Y			R	+		Y	Y	Y
Forte[8]	C				Y		Y		Y		Y								
Granada	C	C	S	Y	Y		Y	Y	Y	Y	Y	E		R	+			Y	
Guinness/Diageo	R	C	S	Y				Y	Y		Y	E	Y	R	+		Y	Y	Y
Hanson	C	D*	D*	Y			Y		Y	Y		N		R	+			Y	
Hays	R*	R	C	Y		Y						E	Y	A		-	Y		
Ladbroke/Hilton	C	D	D	Y				Y	Y			E	Y	R	+		Y	Y	Y
NW Water/United Utilities	D	C	R	Y			Y	Y	Y			N	Y	A		-	Y	Y	Y
Old Mutual[8]			C																
P&O	C	C	R*	Y			Y	Y	Y	Y		E	Y	R	+				
Pearson	C	C	R	Y		Y			Y			E	Y	R		-	Y	Y	
Siebe/Invensys	C	R	R*	Y			Y		Y		Y	E		R		-	Y		
Smiths Industries	C*	C	C	Y	Y	Y			Y	Y		E	Y	S		-	Y		
TI[7]	C	C*			Y		Y		Y			E	Y	S	No Change				
Tomkins	C	C	C	Y	Y		Y	Y	Y		Y	E		S	+			Y	
Unilever	C	C	C	Y	Y	Y			Y		Y			S	+		Y	Y	Y
Whitbread	R	R	C	Y				Y	Y		Y	E	Y	A		-	Y	Y	
Williams[7]	C	R					Y		Y	Y	Y	E		R	No Change		Y	Y	
FTSE100 Conglomerates	**16**	**10**	**7**																
Non FTSE100 Conglomerates	1	2	0																

Notes:

1 Categories are; **S** - Single business, **D** - Dominant business, **R** - Related Diversified, **C** - Conglomerate. Asterisks indicate non-membership of FTSE100 at the year end.

2 Companies that have retained their independence are those that continued to be separately quoted on the LSE throughout the research period.

3 Companies that have a stable strategy are those that have remained in the same diversification category at each period end.

4 External drivers are categorised as being financial/market or regulatory. Regulatory includes Competition Commission and utility regulators, e.g. Offwat, Offgen.

5 Strategic Response/Restructuring indicate actions taken. Return of Capital includes special dividends and share repurchase programmes. Key acquisitions are either of **E**xisting or **N**ew activities.

6 Outcomes show the effect of the strategic responses/restructuring. Category changes (**A**dvance, **R**etreat ,**S**table) relate to the Model of Corporate Development (MoCD). Increases in herfindahl mean greater focus, decreases more diversification. Changes in core activity, including establishing a dominant activity, reflect portfolio restructuring. Changes of less than 0.025 in the herfindahl index are assumed immaterial, i.e. focus remains unchanged.

7 Changes for companies that did not remain independent - Blue Circle, BTR, TI and Williams - are for the period 1993 to 1998 (1997 for BTR as 1998 accounts not published).

8 Forte was acquired by Granada in 1996 and Old Mutual listed in 1999. Neither company was quoted for two consecutive periods and changes cannot be identified.

Only four companies - **Bass/Intercontinental Hotels, Smiths Industries, Tomkins and Unilever** - retained their independence and remained conglomerates.

The remainder of this section considers links between drivers, strategic responses and outcomes.

Stability/Consistency

There were 22 companies that were conglomerates at one or more of the period ends. Of those companies, 16 retained their independence, 7 maintained their conglomerate strategy and four companies – Bass/Intercontinental Hotels, Smiths Industries, Tomkins and Unilever retained their independence and maintained their conglomerate strategy at each period end. Of the 4 independent conglomerates only Smiths was not a constituent of the FTSE100 in 1993, 1998 and 2003 having only entered after 1993.

Environmental Stability

Only 4 companies were faced with a business environment in which there appeared to be no appreciable changes; their financial performance was good, markets were not pressing for strategic change and there were no regulatory influences. Two of those companies, Smiths Industries and Unilever, retained their conglomerate strategy while one, Hays, moved from related diversification to conglomeration and one, Pearson, retreated back from conglomeration to related diversification. There were no similarities between the companies in terms of their primary, but not necessarily core activities, which were; Hays - distribution, Pearson - publishing, Unilever – FMCG and Smiths - aerospace

Financial/Market Pressures

Over half, 12 companies, faced financial/market pressures. These pressures came either as a consequence of poor financial performance – or the expectation of poor future financial performance – or a loss of support for conglomeration. Companies, including BTR and P&O, suffered deteriorations in their financial performance in the mid-1990s, some of which may have been due to industry rather than diversification effects, which led to their decisions to refocus through a series of divestments to restore profitability and shareholder value. Other companies, including Hanson, Tomkins and Williams, appear to have been affected more by sentiment than reality as, despite stable financial performance, all three came under investor pressure to refocus. Hanson and Williams broke themselves up, primarily through demergers, while Tomkins sold several activities, including its largest, the RHM bakery business, to increase its focus although it remained a conglomerate.

Regulation

The table shows the extent of regulatory influence, primarily from the Competition Commission (Monopolies and Mergers Commission until the Competition Act 1988). Notwithstanding the change from public interest to competition issues in the CC's remit introduced by the Enterprise Act 2002, decisions of the CC regarding specific proposed acquisitions or levels of competition in specific markets, such as the UK brewing industry, had significant effects on FTSE100 companies throughout the research period. Some companies were effectively forced to grow through international

expansion while others chose to divest activities where further domestic acquisitive growth was no longer possible without counterbalancing divestments. A prime example is the CC's 1989 report into the brewing industry which had effects not only on its publication, when significant divestments were required of the largest brewers to restore acceptable levels of competition, but also when subsequent proposed acquisitions were reviewed and reported on by the CC which acted in a manner consistent with its earlier actions. Bass/Intercontinental Hotels and Whitbread both eventually divested their traditional and historic brewing activities after having been thwarted by the CC in attempts to grow them through acquisitions. Bass/Intercontinental Hotels remained a conglomerate, albeit with hotels at its core rather than brewing, while Whitbread diversified away from brewing becoming a hotels and leisure-based conglomerate.

It should also be noted that the CC has resisted attempts by companies to force its hand by completing acquisitions likely to have an adverse effect on competition before receiving its assent. The CC forced Ladbroke/Hilton to sell the 833 shop chain of Corals betting offices it acquired from Bass/Intercontinental Hotels for £383m in 1997 because the acquisition reduced competition in the off-course betting market.

A second, more recent, regulatory influence was that of utility regulators, e.g. Offwat for water companies and Offgen for electricity companies, which were established to ensure privatised utility companies that often enjoyed domestic geographic monopolies were giving their customers value for money. North

West Water/United Utilities' diversification into unregulated activities was driven by a need to generate a higher percentage of its revenues from businesses where pricing and ultimately profits were not dependent on the decisions of a regulator.

The third regulatory influence, which affected only Granada, was that of the Independent Television Commission (ITC) which implements the government legislation relating to non-BBC UK broadcasting. The ITC's relaxation of restrictions on ownership of multiple UK commercial television franchises allowed Granada to grow and focus on its television activities.

With the exception of the ITC, the influence of regulatory authorities is consistent; the CC's vigilance in pursuing competition discourages or even stops concentration and therefore encourages diversification and, similarly, utility regulators' price-setting activities also encourage regulated utility companies to diversify into non-regulated activities. Conversely, the ITC, through its removal of restrictions on multiple franchise ownership, encouraged focus. An alternative consequence of regulatory limitation of domestic growth could be an increase in non-UK acquisitions of focusing companies as they sought growth through international expansion. Statistics from the ONS (see table 19) support the contention that non-UK acquisitions have increased as a percentage of total acquisitions by UK companies through the 1990s but conversely so have disposals suggesting that either international expansion has not been successful or that the drive to greater focus has impacted on both international and domestic activities.

Strategic Responses/Restructuring

The strategic responses show all but 2 companies – Hays and TI – to have made significant divestments. TI, which was acquired by Smiths Industries in 2000, did face financial and market pressures but responded by making acquisitions and growing internationally. Hays, took the same approach although by 2003 it had announced that it was going to divest its distribution business. While both companies remained conglomerates, the portfolio of businesses changed at Hays increasing its diversification while changes in the relative sizes of TI's stable portfolio increased its focus. All other companies made significant divestments.

The almost universal incidence of divestment is consistent with the increase in focus/reduction in diversification shown in the outcomes section of the table. Although almost as many companies made significant acquisitions as made significant divestments, the broad move to greater focus suggests divestments were of unwanted activities while acquisitions were of activities already in the acquirers' portfolio producing a net reduction in diversification. Only two companies acquired new business activities; Hanson acquired Eastern Electricity and North West Water/United Utilities acquired Norweb. Hanson made its acquisition in the hope of re-invigorating an ex-public utility while North West Water/United Utilities' rationale was a desire to consolidate its activities in the North West of England and to achieve administrative synergies despite the clear differences between water and electricity businesses.

Table 82 also shows that divesters were also downsizers suggesting that while some companies chose to reinvest disposal proceeds in acquisitions that would add size and/or international scope to existing activities others chose to return capital to shareholders instead of or as well as making acquisitions. Tomkins exemplifies a company that made substantial divestments, including that of its largest activity RHM, and returned capital to shareholders. Downsizers also include two conglomerates – Hanson and Williams – that broke themselves up; Hanson divested/demerged all activities except for building materials while Williams demerged its two activities and delisted itself.

Internationalisation has been pursued by approximately half of the companies. This reflects not only the broader move towards globalisation, especially in industries such as aerospace and drinks, but also the domestic growth limitations placed on some companies by CC decisions in acquisition referral cases. Guinness/Diageo was required to sell some major spirits brands after its acquisition of Grand Metropolitan and, faced with these effective UK limits on some spirits activities, expanded internationally.

Outcomes

The charts at the start of this chapter and the tables in the previous chapter summarising movements between categories clearly show the principal outcome of the strategic responses to external drivers for change to have been a broad move towards focus; effectively a retreat back through the Model of Corporate Development. This is in contrast to predominantly forward

movement to greater diversity shown in previous research (Channon, 1973; Whittington & Mayer, 2000).

The majority of conglomerates - 14 compared to 6 - have increased their focus as reflected in movements - increases - in their Herfindahl indices between 1993 and 2003 or the date they lost their independence. Furthermore, only 3 companies – Hays, North West Water/United Utilities and Whitbread – moved forward through the Model of Corporate Development with 7 companies remaining in the same diversification category and 10 retreating back to greater focus.

In addition to the trend to focus, the companies that have either adopted or maintained conglomeration have narrowed the breadth of their activities. The average Herfindahl index of conglomerates increased from 0.36 to 0.44 between 1993 and 2003 while the average percentage of turnover generated by the largest activity rose from 46.0% to 55.5% and that of the largest related group from 52.5% to 58.1%. As the result of the narrowing of conglomerate activities and the shift of companies to more focused diversification categories, the overall FTSE100 Herfindahl index increased steadily from 0.63 in 1993 to 0.77 in 2003.

In addition to changes in diversification, strategic responses have changed the mix of activities at companies. At one company - BAT/British American Tobacco – there was a return to what had, until diversification in the 1970s and 1980s, been the company's core and only activity, tobacco. Almost all

other companies made significant changes to their business portfolios the exceptions being Guinness/Diageo which started and ended a drinks company, Ladbroke/Hilton which retained its mix of betting/gaming and hotels, TI which, until its acquisition, maintained a stable portfolio and Unilever which disposed of only a minor speciality chemicals activity.

7.5 Summary

The quantitative analyses that were undertaken in chapter 6 (Analysing the Accounting Record) clearly show that there has been a trend towards greater focus amongst FTSE100 companies since 1993. Furthermore, the analyses showed that conglomerates comprise a significantly smaller percentage of the FTSE100 and that the diversification, as measured by Herfindahl indices, number of activities and percentage of turnover attributable to the largest activity/group of related activities, of those companies that constitute the conglomerate category has also fallen. However, the quantitative analyses did not shed light on the drivers behind the move to greater focus; analyses of the average financial performance (post-hoc) of companies within different diversification categories showed no clear differences between them or over time. Therefore, company histories were compiled for all 22 companies that were, at one or more period end, conglomerates creating a new record of the activities of those companies with a view to identifying drivers for change.

The histories show that only 4 of the 22 conglomerates faced a stable external environment without either significant financial/market or regulatory pressures. Given the high profile of the conglomerates, the presence of investor pressure

was expected. However, the extent of regulatory pressure, especially from the Competition Commission, was surprising as was the far reaching effects on strategic decisions. The withdrawals of both Bass/Intercontinental Hotels and Whitbread from their traditional brewing activities are prime examples of the effect of regulation on strategic decisions.

The strategic responses illustrate the extent of refocusing activities with all but two companies making significant disposals. Furthermore, 7 companies, notably Bass/Intercontinental Hotels, Hanson, P&O and Williams, made disposals of such a size that the divestment was achieved through demerger with the demerged businesses becoming FTSE100 companies. Demergers effectively resulted in downsizing as existing shareholders were given shares in the newly independent company while other disposals yielded cash which could be reinvested and/or returned to shareholders. Several of the companies facing regulatory restrictions chose to return some/all proceeds to shareholders as their scope for growth was limited. Others turned to international expansion to avoid domestic competition issues. Despite the regulatory issues, where companies did make acquisitions, they were overwhelmingly of activities in which they already had an interest.

The outcomes clearly support the findings of chapter 6; the trend is towards focus reflecting a reversal of the normal direction of progression through the Model of Corporate Development. In addition, there was an increase in the number of companies with a core activity that generated more than 50% of

total turnover although at only 5 companies was the core activity the same in 2003 or at the time independence was lost as it had been in 1993.

The company histories do provide a picture of the key external factors that we normally take to be drivers of strategic decisions and strategic change among conglomerates. However, the histories do not and, without access to and information from the individuals who ran the companies at the time key strategic decisions were taken, cannot throw light on the existence and influence of internal factors including management attitudes. Almost all companies undertake periodic strategic reviews, typically after changes in the market/competitive environment or in the chairman/chief executive, but the detail of these reviews is, for obvious reasons, seldom made public. Therefore, the full range of drivers behind corporate strategy decisions will include not only the external factors highlighted here - financial/market and regulatory – but also a number of internal factors.

Overall, this qualitative analysis of some of the UK's largest companies has shown that while there has been a systematic move back to greater focus, the forces driving change have been inconsistent in their effects; different forces have affected different companies – there was no single universal driving force.

8. CONCLUSIONS

The aims of this research were to create a comprehensive database of financial and non-financial information on the companies that comprised the FTSE100 index – including both industrial/manufacturing and service companies – between 1993 and 2003 and to interrogate the database to test a number of hypotheses. In addition to assessing whether the incidence of conglomeration had declined, hypotheses were also established to compare conglomerates with other diversification categories – single business, dominant business and related diversified. These hypotheses covered the breadth of corporate activities, performance and corporate governance.

Initially, the research used quantitative methods to assess changes in conglomeration, the breadth of activities, performance and corporate governance across all diversification categories. However, having identified a reduction in conglomeration and a broad trend to greater focus and having failed to find any drivers of these strategic changes in performance (post-hoc) or corporate governance, there was a need to go beyond the comprehensive FTSE100 database created as part of this research. In what effectively became a second qualitative research phase, company histories of each of the 22 FTSE100 companies that were conglomerates at one or more of the period ends – 1993, 1998 and 2003 – were compiled and analysed to identify the drivers that had influenced strategy formulation and strategy change decisions. The histories led to what is effectively a New Model of Corporate Development (Chart 15) which reflects the dynamics and tensions involved in diversification decisions.

Incidence

In broad terms this research has shown that the incidence of conglomeration amongst constituents of the FTSE100 index has reduced between 1993 and 2003 and that there has been a broad trend toward greater focus. Conglomerates comprised 16% of the FTSE100 in 1993, 10% in 1998 and only 7% in 2003 with the reduction being more profound amongst industrial/manufacturing companies. The constant population provided by the 54 FTSE100 Survivors showed a similar pattern. There were also reductions in related diversification primarily amongst FTSE100 companies. The dominant category remained broadly stable with the single business category increasing significantly from 21% in 1993 to 34% in 1998 and 44% in 2003 for FTSE100 companies and from 18.5% to 25.9% to 31.5% for FTSE100 Survivors. The patterns for industrial/manufacturing and service companies were similar although there were differences in the dominant category, where industrial/manufacturing increased and services decreased, and the related category, where industrial/manufacturing fell and services were stable.

In addition, when conglomerates and related diversifiers are taken together as a multiple business category, the data clearly shows fewer companies to be in that group, especially in the industrial/manufacturing sector. When the findings of this research are added to those of prior research, it appears that there is clear evidence to support the anecdotally derived belief that conglomeration peaked in the early 1990s for both industrial/manufacturing and service companies as the following tables show.

Table 83: UK Manufacturing Company Diversification, 1950-2003

All Figs %	Channon[1]			Whittington & Mayer[2]		This Research[3]		
Category	1950	1960	1970	1983	1993	1993	1998	2003
Single	34	19	6	6	5	7	13	30
Dominant	41	36	34	16	10	16	23	38
Related	23	41	54	67	61	53	44	24
Conglomerate	2	4	6	11	24	24	20	8
Totals	100	100	100	100	100	100	100	100
Companies	*92*	*96*	*100*	*75*	*67*	*42*	*30*	*37*

Source: [1]Channon (1973, p67) 100 largest UK manufacturing companies as in 1969-70, [2]Whittington & Mayer (2000, p139) UK based companies amongst largest 100 manufacturers as in 1983 and as in 1993, [3]This research - FTSE100 industrial/manufacturing companies as in 1993, 1998 and 2003.

Table 84: UK Service Company Diversification, 1950-2003

All Figs %	Channon[1]						This Research[2]		
Category	1950	1955	1960	1965	1970	1974	1993	1998	2003
Single	36	31	23	17	16	16	31	43	53
Dominant	41	42	46	45	26	16	43	31	27
Related	17	19	20	26	45	49	16	20	14
Conglomerate	6	8	11	12	13	19	10	6	6
Totals	100	100	100	100	100	100	100	100	100
Companies	*69*	*74*	*81*	*91*	*100*	*99*	*58*	*70*	*63*

Source: [1]Channon (1978, p31) 100 largest UK service companies as in 1973-74, [2]This research – FTSE100 service companies as in 1993, 1998 and 2003.

As well as showing the decline in the incidence of conglomeration, the data also suggests that the breadth of activities of companies adopting or maintaining conglomeration narrowed. This contention is supported by increases in the average Herfindahl indices of conglomerates and in the average percentage of total turnover attributable to the largest activity or group of related activities of conglomerates. The average Herfindahl index of conglomerates increased from 0.36 to 0.44 between 1993 and 2003 while the turnover generated by the largest activity increased from 46.0% to 55.5% and that by the largest group of related activities from 52.5% to 58.1% over the same period. These increases together with the shift towards focus strategies

across the FTSE100 resulted in the overall Herfindahl and turnover distribution statistics increasing. The increases amongst the FTSE100 Survivors were similar to those of the whole index as were those for the industrial/manufacturing and service company sectors. The overall trend to greater focus was also evidenced by the reduction in the number of activities reported by FTSE100 companies, especially conglomerates, and of the number of related groups. Finally, the percentage of conglomerates having a core activity accounting for more than 50% of total turnover also rose between 1993 and 2003, from 43.8% to 71.4% for the FTSE100 and from 57.1% to 100.0% for FTSE100 Survivors.

These trends are illustrated by the 3 companies that retained membership of the FTSE100 throughout the research period and maintained their conglomerate status – Bass/Intercontinental Hotels, Tomkins and Unilever. All 3 companies showed increases in their Herfindahl indices from 1993 to 1998 and from 1998 to 2003 suggesting that even though they continued to hold a portfolio of unrelated business activities the breadth of their activities was narrowing. Furthermore, both Bass/Intercontinental Hotels – hotels - and Tomkins – industrial and automotive engineering - developed new core activities over the 10 year period while Unilever retained and marginally increased the relative size of its core of food activity.

A comparison of the old – 1993 – and new – 2003 – conglomerate shows them to have different key characteristics as the following table shows:

Table 85: Old and New FTSE100 Conglomerates

All figs Category Averages	1993		2003
Market Capitalisation (£m)	5,582		3,088
Turnover (£m)	5,287		7,433
ROCE (2-year average %)	17.8	Note	22.3
No. of Activities	4.6		3.3
No. of Related Groups	3.4		2.4
Largest Activity (% of T/O)	41.2		57.5
Largest Related Group (% T/O)	57.9		59.2
Core Activity (% of Conglomerates)	43.8		71.4
Herfindahl Index	0.36		0.44
No. of Companies	16		7
Non-executive Chairmen (%)	43.8		85.7
Non-Executive Directors (%)	42.6		59.7
Number without CEO	5		1
Aggregate Major Shareholders (%)	8.0		16.7
No. of Service Conglomerates	6		4

Note: All figures except ROCE are averages for all conglomerates. DataStream ROCE figures were only available for 14 conglomerates in 1993 and 5 in 2003.

The table clearly shows that companies categorised as conglomerate in 2003 differ significantly from their 1993 counterparts. Whilst more profitable, in terms of ROCE, the average 2003 conglomerate has a lower market capitalisation than its 1993 equivalent. The breadth of activity of the 2003 conglomerate is narrower as evidenced by a higher average Herfindahl index, the increased incidence of a core activity, a larger percentage of turnover generated by the largest activity and group of related activities and the lower number of activities. Corporate governance, in common with other categories of company, has also improved amongst conglomerates as enhanced Best Practice has been adopted. Finally, the increase in the average major shareholding from 8.0% in 1993 to 16.7% in 2003 suggests that institutional shareholders may be looking more favourably on the more focused conglomerates of 2003.

Corporate Governance

This research has failed to find any strong link between corporate governance and diversification that may explain the decline in the incidence of conglomeration and the more general trend towards greater focus. However, at several companies the renunciation of conglomeration came after the retirements of long-serving chairmen and/or chief executives, most notably Lords Hanson and White at Hanson and Sir Owen Green at BTR, who had been the driving force behind building a small company into a conglomerate. In response to changes in the corporate governance Code of Best Practice, there has been a trend towards a majority of non-executive directors on company boards, a splitting of the roles of chairman and chief executive and chairmen being non-executive. However, the trends appear to be similar across all diversification categories. Differences in the aggregate levels of substantial shareholdings, which have increased over time, are also similar across diversification categories although there has been a substantial increase in the conglomerate category. This suggests that institutional shareholders may still have confidence in conglomeration especially as conglomerates have narrowed the breadth of their activities. These similarities suggest no link between corporate governance and shareholder influence and diversification category. Again, these findings held true for the populations – FTSE100 and FTSE100 Survivors – and also for the industrial/manufacturing and service company sub-groups.

External Drivers

In common with extant literature and recognising the inherent difficulties of inter-company performance comparisons, this research has found no clear link between performance and diversification. However, as was conjectured in the hypotheses chapter, companies do not operate in a vacuum and there must be generic, industry specific and company specific factors that have an impact on them and which, in turn, drive their strategic responses which determine structure. By compiling company histories for the 22 companies that were conglomerates at the end of one or more of the three years 1993, 1998 and 2003, it has been possible to identify the company specific factors - financial/market and regulatory - that lay behind portfolio management decisions. These drivers elicited corporate strategic responses - disposals, demergers, returning capital to shareholders, acquisitions of existing or new activities and internationalisation – which determined the diversification of the company and whether it chose to establish a core activity. In making their strategic decision, management considered the pressures in light of the competing attributes of the different levels of diversification; the lower risks attaching to conglomeration, the greater scope, especially for synergies, of related diversification and the scale benefits of dominant and single business company forms.

At the majority of companies, the external drivers for change elicited strategic responses that led to refocusing but at the three companies that retained their conglomerate strategies different drivers were present and different outcomes resulted from similar strategic responses. Bass/Intercontinental Hotels was a

brewing, drinks, pubs and betting/gaming conglomerate in 1993 but by 2003 it had demerged its public house activities as Mitchells & Butlers and become a hotel company with a much reduced brewing activity. Tomkins categorised itself as a conglomerate in 1993 with activities as diverse as baking and garden products but by 2003 it had divested baking and several other peripheral activities to become an industrial and automotive engineering conglomerate. Unilever remained relatively unchanged except for the divestment of its speciality chemicals business which marginally increased its focus. Bass/Intercontinental Hotels was driven by regulatory influences in the brewing/public house industry, Tomkins was driven primarily by a need to achieve growth but also by some regulatory influences and Unilever by a recognition that speciality chemicals was a peripheral activity. All three companies used divestments and/or demergers to achieve their strategic changes and Bass/Intercontinental Hotels returned capital to shareholders as part of a downsizing exercise.

From the drivers for strategic change identified through the conglomerate company histories in chapter 7 it is possible to show how company specific factors - financial/market pressures and regulation – influenced diversification strategies and their implications for the third company specific factor – leadership or the competence to manage the complexity inherent in diverse companies. Chart 14 shows these relationships and places the conglomerates investigated in chapter 7 and that were quoted in 1993 and 2003 in each of the broad categories – increase focus, maintain focus, restructure and maintain diversity – according to changes in their diversification. Given that, at

some point, all the companies were conglomerates, none appears in the maintain focus category.

Chart 14: Influence of Company Specific Factors on Diversification

Financial/Market	Low (Management Competency)	High (Management Competency)	Regulatory Influences
High	**INCREASE FOCUS**	**RESTRUCTURE**	
High	Guinness, Granada, NWW, P&O	Tomkins	Yes
High	BAT, Caradon	Hanson, Siebe	No
Low	**MAINTAIN FOCUS**	**MAINTAIN DIVERSITY**	
Low		Bass, Whitbread, Ladbroke	Yes
Low		Hays, Smiths Inds, Pearson, Unilever	No

The chart clearly shows that companies facing low financial/market pressures are relatively stable retaining their diversity - conglomerate or related diversified – which suggests they possess the necessary management competence. Some of the companies in this group did not face any regulatory influences that would have encouraged diversification but still chose to maintain their diversity as they could manage their portfolios effectively. The companies that increased their focus were those that did have financial/market pressures. As, proportionately, companies in this group faced more regulatory issues than any other, they were, notwithstanding international expansion, limited in the level of focus they could achieve. A key reason they sought greater focus in spite of potential regulatory issues, may have been weaknesses in management competence. Finally, three companies have been categorised as restructuring as their responses to

market pressures were more extreme than others. Despite having good management teams, companies in this group chose to radically downsize. Only at Tomkins were regulatory issues, which concerned its RHM bakery activities, an influence on the change in strategy.

New Model of Corporate Development

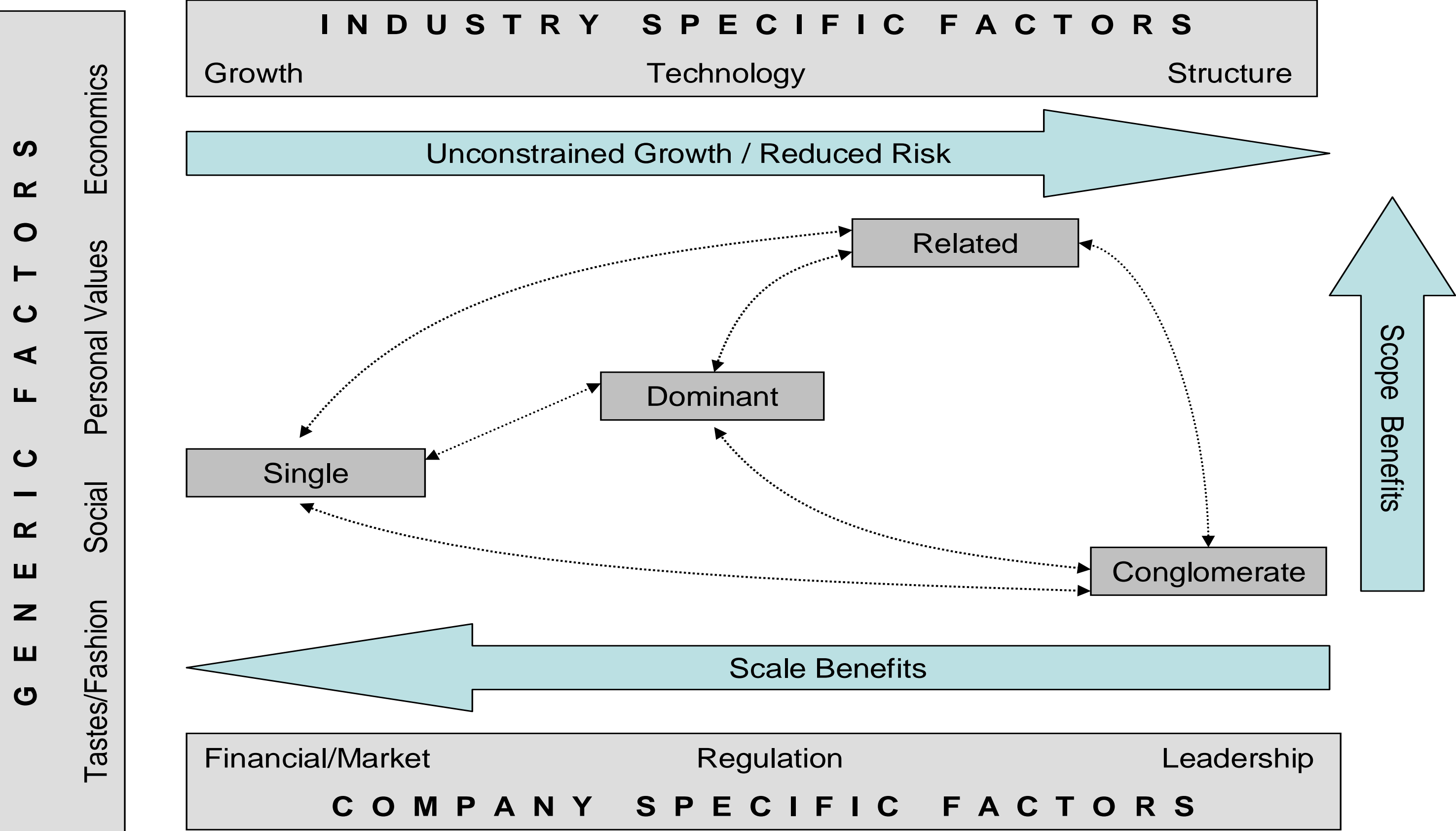
The move towards greater focus identified by this research and illustrated in the company histories in chapter 7 suggests the flow through the Model of Corporate Development has reversed. This contrasts with earlier periods when the direction – evolutionary rather than revolutionary - was predominantly forwards to greater diversification. Within the constant population of 54 FTSE100 Survivors, the 10 year period from 1993 to 2003 saw a net reversal of diversification of 9 (17%) companies; 11 (20%) advanced to greater diversification and 20 (37%) retreated back towards greater focus. Interestingly, notwithstanding movements in the intervening 10 years, 23 (42%) companies were in the same diversification category in 2003 as 1993. This net reversal contrasts with a net positive movement in the 10 year period between 1983 and 1993 when the ratio of movements was 9:4 in favour of advances. This research has found the Model of Corporate Development to continue to be a true reflection of the diversification options available to companies and the sequential path - forwards and backwards - followed by the majority of companies; few companies attempt to move by more than one category at a time even over a 5 year period. However, the Model has become multi-directional.

The increasing number of companies retreating back to focus strongly suggests that the flow through the Model of Corporate Development should be two-way rather than just forward to greater degrees of diversification. In addition, the known external and unknown internal influences that drive changes in corporate diversification should also be added to the Model.

The 'New' Model of Corporate Development - Drivers Impacting Corporate Development - on the following page clearly shows that, in addition to a range of generic, industry and company specific factors driving diversification decisions, the level of diversification pursued by a company effects its potential for growth, level of risk, opportunities for economies of scale and ability to achieve scope benefits.

As chart 15 shows, conglomerates, by virtue of having a portfolio of unrelated activities, enjoy reduced levels of risk and, by adding further activities, increased levels of growth which are unconstrained by the limitations, that may be exacerbated by restrictions imposed by competition authorities, inherent in participation in a single industry. However, conglomerates, by virtue of holding a portfolio of unrelated activities, have limited opportunities to operate at levels that enable them to achieve economies of scale or to leverage their core capabilities and competences to gain scope benefits. Furthermore, conglomerates also face greater internal organisation and management problems by virtue of the complexity inherent in their business model.

Chart 15: Drivers Impacting Corporate Development



At the other end of the spectrum of diversification, single business companies, with ‘all their eggs in one basket’ are higher risk and have limited growth opportunities while they have greater potential to achieve significant economies of scale. Single business companies may also be able to obtain limited scope benefits, e.g. through international expansion, by leveraging their core capabilities and competences and, notwithstanding their increasing globalisation, they are relatively simple in terms of their organisation and management.

Therefore, in choosing a level of diversification from single business to conglomeration managers must acknowledge the inherent trade-off in the potential level of risk, growth, scale and scope benefits. Understanding how companies achieve an acceptable balance across these benefits could be the focus of future research.

Other areas for future research include making greater use of existing database detail to further investigate links between diversification and performance, looking beyond FTSE100 constituents and investigating the role of management in diversification decisions especially how their perceptions of the relatedness of business activities impacts on those decisions.

Summary

In summary, this research has proven that the incidence of conglomeration amongst the FTSE100 has fallen markedly in the 10 years between 1993 and 2003, that there has been a trend towards greater focus and that the breadth

of activities in conglomerate portfolios has narrowed. The research failed to find evidence of a clear link between performance and diversification or between corporate governance and diversification although standards have increased across all companies in line with enhancements to Best Practice. These findings from the Analysis of the Accounting Record (Chapter 6) together with the outcomes from the Analysis of the Historical Record (Chapter 7) that included reviews of the 22 companies that were conglomerates at the end of one or more of the years 1993, 1998 and 2003, have led to a revision of the Model of Corporate Development. The 'New' Model shows movement to be two-way and dependent on generic, industry specific and company specific drivers the existence and influence of which was a conjecture made in the absence of a clear performance-based driver.

The reduced incidence of conglomeration amongst the FTSE100 does not necessarily mean that the strategy is no longer valid. The 10 years covered by this research has seen unprecedented activity by private equity companies that have, by virtue of their diverse portfolios, become the conglomerates of the 21st century. Whittington (1999) suggests conglomeration is 'evergreen' and that as old conglomerates die new conglomerates take their place and the demise of the public company conglomerate and rise of the private company conglomerate supports this view. However, the structure and management of the new conglomerates, which seek to exploit tax breaks and adopt a 'Porteresque' (acquire-turnaround-sell) approach treating companies as 'stock-in-trade', differs greatly from that of the old.

Ultimately, this research has extended our understanding of UK conglomerates and the factors – generic, industry and company specific - that influence corporate diversification decisions. It has also identified an ongoing corporate dilemma; the search for an acceptable level of trade-off between risk, growth, scale and scope which balances the benefits of higher growth and lower risk against the costs of operating on a smaller scale and with limited scope. The move towards greater focus amongst FTSE100 companies suggests prevailing management attitudes favour the achievement of scale and scope over lower risk and higher growth. Finally, given the complexities of the companies and the environments in which they operate, there will also be other drivers, including management attitudes, influencing their strategic decisions.

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APPENDICES

Appendix A – Definitions of Performance Measures

The following definitions have been used to determine the key performance measures used to assess the FTSE100 companies.

Market Capitalisation
This is the aggregate market value of a company's issued share capital. Market capitalisations are taken from the Financial Times.

Share Price Volatility
This indicator provides a measure of the stability of a company's share price during a calendar year.

The share prices are taken from the Financial Times and have been adjusted for any events, e.g. capital reorganisations, share splits, acquisitions, etc. that would have distorted share prices. Volatility is defined as the difference between the highest and lowest share price expressed as a percentage of the lowest price.

$$\frac{\text{Highest Price} - \text{Lowest Price} \times 100}{\text{Lowest Price}}$$

Volatility is a function of market, industry and company specific factors.

Market Value/Book Value Excluding Intangibles Ratio
This ratio provides an indication of how the investment community believes a company is managing its asset base; a value above 1 means the company has a value in excess of the book value of its assets.

The ratio is computed by DataStream using the value of total assets less intangible assets as per the most recent balance sheet and the market value of the issued share capital at the balance sheet date.

$$\frac{\text{Market Value}}{\text{Book Value Excluding Intangible Assets}}$$

It should be noted that the frequency of asset revaluations and their incorporation into financial statements and depreciation policies may distort this indicator.

Return on Capital Employed (ROCE)
ROCE provides a measure of how well a company is using the capital is has at its disposal.

The return is computed by DataStream using profit after tax but before interest and capital employed including short-term borrowing but excluding intangible assets.

$$\frac{\text{Pre-Tax Profit + Interest X100}}{\text{Capital Employed + Short-Term Borrowing - Intangibles}}$$

As the return uses profit after tax it will be affected by depreciation and amortisation charges.

Gearing

Gearing provides a measure of a company's indebtedness as a percentage of its overall funding, i.e. debt and equity including reserves and minority interests.

The indicator is calculated by DataStream as follows:

$$\frac{\text{Total Debt X 100}}{\text{Total Debt + Share Capital and Reserves + Minority Interest}}$$

ASSOCIATED BRITISH FOODS DS Code 900825 Check **OK**

General Data @ 31/12	1993		1998		2003	
Company Name		Associated British Foods		Associated British Foods		Associated British Foods
Changes - M&A, FTSE Entry/Exit						
Listed		Yes		Yes		Yes
FTSE100		Yes		Yes		Yes
FT Classification		**Food Manufacturing**		**Food Producers**		**Food Prods & Processors**
Market Capitalisation (Plc only)		2,527.0		5,116.0		4,661.0
Share Price (p) - Year End		563.00		568.50		584.00
- Year Low		456.00		455.00		459.00
- Year High		569.50		670.00		599.00
P/E		11.5		18.9		13.5
Yield (%)		3.4		2.1		2.5
Primary Activities		Food processing and retailing		Food processing and food & non-food retailing		Food processing and food & non-food retailing
Position in Largest 100		62		58		49
Service Company		No		No		No
Services (%)	OK	28.3	OK	7.0	OK	14.8
Financial Services		No		No		No
Financial Year Ended		18/09/1993		12/09/1998		13/09/2003
Length (Months)		12		12		12
Auditor		KPMG Peat Marwick		KPMG		KPMG
Audit Report		Clean		Clean		Clean
Significant Shareholdings (%)		63.00		53.99		54.50
DataStream - Download / Seg. Reconcil.	Yes	OK	Yes	OK	Yes	OK
Diversification Indicators						
Herfindahl (PDI = 1-Herf)	Sales	**0.594**	Sales	**0.869**	Sales	**0.748**
Herfindahl (Related Basis)	Sales	**1.000**	Sales	**0.869**	Sales	**0.748**
No. of Divisions Reported		**2**		**2**		**2**
No. of Unrelated Activities		**1**		**2**		**2**
External Sales of Largest Div. (%)		**71.7**		**93.0**		**85.2**
Ext Sales of Largest Related Grp (%)		**100.0**		**93.0**		**85.2**
Op Profit of Largest Div (%)		**87.5**		**92.7**		**78.8**
Op. Profit of Largest Rel Grp (%)		**100.0**		**92.7**		**78.8**
Assets of Largest Div (%)		**N/A**		**N/A**		**N/A**
Assets of Largest Rel Grp (%)		**N/A**		**N/A**		**N/A**
Channon/Whittington & Mayer		**Dominant**		**Dominant**		**Dominant**
Core (Related & Conglomerate only)		**N/A**		**N/A**		**N/A**
Focus Business/Multiple Business		**Focus**		**Focus**		**Focus**
Hill & Pickering		**Low**		**Medium**		**Medium**
Executive Directors (%)		**83.3**		**62.5**		**37.5**
Ave Length of Service - EDs (Years)		**15**		**20**		**6**
Ave Length of Service - NEDs (Years)		**29**		**14**		**11**
Chairman		**Weston, G.H.**		**Weston, G.H.**		**Adamson, M.G.**
Non-Executive Chairman		**No**		**No**		**Yes**
Years as a Director		**44**		**49**		**4**
Years as Chairman/Year Appointed	**26**	**1967**	**31**	**1967**	**1**	**2002**
Group Chief Executive/COO/MD		**N/A**		**N/A**		**Jackson, P.J.**
Years as a Director		**0**		**0**		**11**
Years as CEO/COO/MD/Year Appointed	**0**	**0**	**0**	**0**	**4**	**1999**
Alternative CEO		**Chair**		**Chair**		**N/A**

CATEGORISATION RATIOS

Channon/Whittington & Mayer	
Category	Ratios
Single SR ≥	**0.95**
Dominant Product SR ≥	**0.70**
Related Diversified RR ≥	**0.70**
Unrelated Diversified RR<	**0.70**
Core Activity Level	**0.50**

Hill & Pickering	
Category	Non-Core %
Low <	**5.00**
Medium ≥	**5.00**
High >	**25.00**

WHITTINGTON & MAYER*

1983	**Related**
1993	**Related**

*Categorisations as per extant W&M research

DATASTREAM DOWNLOAD - ACCOUNTS DATA

ABF **ASSOCIATED BRIT.FOODS**

TYPE	DESCRIPTION	12/09/1992	18/09/1993	17/09/1994	16/09/1995	14/09/1996	13/09/1997	12/09/1998	18/09/1999	16/09/2000	15/09/2001	14/09/2002	13/09/2003	18/09/2004	17/09/2005	16/09/2006	15/09/2007
104	TOTAL SALES	3,954,000	4,386,000	4,513,000	4,894,000	5,707,000	4,437,000	4,195,000	4,299,000	4,406,000	4,418,000	4,545,000	4,909,000	5,165,000	5,622,000	5,996,000	6,800,000
136	DEPRECIATION	122,000	138,000	148,000	154,000	172,000	156,000	151,000	147,000	212,000	160,000	167,000	184,000	185,000	239,000	218,000	293,000
696	DEPN AND OPERATING PROVISIONS	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA
993	OPERATING PROFIT	271,000	273,000	308,000	335,000	395,000	342,000	317,000	317,000	327,000	333,000	370,000	401,000	421,000	477,000	512,000	519,000
2408	NET INTEREST CHARGES	(22,000)	34,000	30,000	29,000	25,000	21,000	22,000	25,000	26,000	(35,000)	22,000	(23,000)	(36,000)	(15,000)	14,000	35,000
D011	EXTRAORD./SPECIAL ITEMS	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA
154	PRE-TAX PROFIT	297,000	338,000	382,000	375,000	430,000	401,000	392,000	300,000	240,000	350,000	413,000	450,000	483,000	469,000	409,000	498,000
623	PUBLISHED AFTER TAX PROFIT	201,000	234,000	314,000	256,000	286,000	282,000	270,000	186,000	131,000	246,000	320,000	324,000	339,000	333,000	298,000	390,000
176	MINORITY INTERESTS	5,000	6,000	6,000	6,000	8,000	8,000	2,000	1,000	(2,000)	8,000	3,000	(3,000)	6,000	7,000	7,000	31,000
625	EARNED FOR ORDINARY	195,960	227,960	308,000	250,000	278,000	274,000	265,000	184,000	138,000	243,000	322,000	332,000	342,000	333,000	301,000	369,000
193	EXTRAORD. ITEMS AFTER TAX	(30,000)	0	0	0	0	407,000	0	0	0	0	0	0	0	0	0	0
D012	ORDINARY DIVIDENDS	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA
1300	EBIT	338,000	372,000	412,000	404,000	455,000	422,000	414,000	325,000	266,000	374,000	435,000	480,000	506,000	503,000	455,000	553,000
1502	EBITDA	460,000	510,000	560,000	558,000	627,000	578,000	565,000	472,000	478,000	534,000	602,000	664,000	691,000	742,000	673,000	846,000
2260	PUBLISHED CASH EARNINGS	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA
305	EQUITY CAP. AND RESERVES	1,707,000	1,878,000	2,088,000	2,256,000	2,451,000	2,909,000	2,981,000	2,660,000	2,751,000	2,869,000	2,979,000	3,261,000	3,467,000	3,694,000	3,956,000	4,242,000
306	PREFERENCE CAPITAL	1,000	1,000	2,000	2,000	2,000	2,000	2,000	2,000	2,000	2,000	2,000	2,000	2,000	2,000	2,000	2,000
307	TOT. SHARE CAPITAL & RESERVES	1,708,000	1,879,000	2,090,000	2,258,000	2,453,000	2,911,000	2,983,000	2,662,000	2,753,000	2,871,000	2,981,000	3,263,000	3,469,000	3,696,000	3,958,000	4,244,000
315	MINORITY INTERESTS	35,000	43,000	53,000	65,000	73,000	71,000	66,000	79,000	78,000	75,000	75,000	24,000	27,000	29,000	224,000	220,000
D036	LONG TERM DEBT	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA
322	TOTAL CAPITAL EMPLOYED	1,902,000	2,086,000	2,301,000	2,482,000	2,689,000	3,139,000	3,206,000	2,898,000	2,991,000	3,103,000	3,443,000	3,669,000	3,853,000	4,252,000	4,358,000	5,062,000
339	TOT FIXED ASSETS-NET	1,319,000	1,375,000	1,444,000	1,585,000	1,650,000	1,396,000	1,439,000	1,528,000	1,459,000	1,397,000	1,421,000	1,406,000	1,459,000	2,252,000	2,525,000	2,690,000
344	TOTAL INTANGIBLES	0	0	0	0	0	0	0	108,000	151,000	179,000	383,000	510,000	593,000	1,035,000	1,542,000	1,570,000
364	TOTAL STOCK AND W.I.P.	372,000	412,000	466,000	480,000	482,000	416,000	428,000	464,000	496,000	469,000	498,000	516,000	496,000	558,000	732,000	818,000
287	TRADE DEBTORS	306,000	317,000	360,000	432,000	471,000	461,000	448,000	459,000	485,000	488,000	479,000	480,000	533,000	618,000	712,000	726,000
375	TOTAL CASH & EQUIVALENT	712,000	801,000	903,000	829,000	993,000	1,668,000	1,640,000	1,081,000	1,198,000	1,290,000	1,501,000	1,712,000	1,683,000	1,198,000	402,000	428,000
376	TOTAL CURRENT ASSETS	1,430,000	1,564,000	1,757,000	1,790,000	1,989,000	2,573,000	2,549,000	2,036,000	2,220,000	2,302,000	2,545,000	2,769,000	2,778,000	2,473,000	2,100,000	2,261,000
392	ASSETS (TOTAL)	2,754,000	2,946,000	3,206,000	3,380,000	3,647,000	3,981,000	4,000,000	3,691,000	3,857,000	3,905,000	4,377,000	4,710,000	4,913,000	5,813,000	6,410,000	6,910,000
276	TRADE CREDITORS	261,000	270,000	290,000	330,000	374,000	233,000	227,000	234,000	217,000	255,000	271,000	319,000	349,000	365,000	445,000	503,000
309	BORROWINGS REPAYABLE < 1 YEAR	144,000	136,000	90,000	69,000	33,000	51,000	44,000	53,000	57,000	82,000	64,000	92,000	68,000	447,000	531,000	125,000
389	TOTAL CURRENT LIABLITIES	826,000	841,000	897,000	849,000	908,000	773,000	726,000	733,000	792,000	753,000	800,000	891,000	897,000	1,405,000	1,673,000	1,443,000
390	NET CURRENT ASSETS	604,000	723,000	860,000	941,000	1,081,000	1,800,000	1,823,000	1,303,000	1,428,000	1,549,000	1,745,000	1,878,000	1,881,000	1,068,000	427,000	818,000
1301	TOTAL DEBT	303,000	300,000	248,000	228,000	196,000	208,000	201,000	210,000	217,000	239,000	451,000	474,000	425,000	974,000	707,000	723,000
1501	NET DEBT	(409,000)	(501,000)	(655,000)	(601,000)	(797,000)	(1,460,000)	(1,439,000)	(871,000)	(981,000)	(1,051,000)	(1,050,000)	(1,238,000)	(1,258,000)	(224,000)	305,000	295,000
1504	ENTERPRISE VALUE (EV)	1,375,681	1,789,383	1,927,414	2,658,997	2,974,698	3,254,109	3,189,160	2,536,154	1,751,107	2,602,386	3,697,875	3,023,453	3,976,253	6,377,890	7,141,476	6,794,972
MV	MV	1,748,681	2,246,383	2,527,414	3,192,997	3,696,698	4,641,109	4,560,160	3,326,154	2,652,107	3,576,386	4,670,875	4,235,453	5,205,253	6,570,890	6,610,476	6,277,972
219	TOTAL NO. OF EMPL. (UNITS)	51,724	49,968	50,241	43,665	45,173	40,371	32,712	34,186	34,372	33,989	34,957	35,416	35,584	42,375	46,703	84,636
190	DIVIDENDS PER SHARE	7.122	7.631	8.139	6.613	9.665	10.174	10.683	10.750	11.250	11.800	13.250	14.600	16.400	18.000	18.750	19.500
254	NET EPS	22.230	25.791	34.947	28.283	31.538	30.827	30.114	21.399	17.499	30.799	40.800	42.100	43.300	42.200	38.100	46.700
794	PUBLISHED CASH EPS	40.106	29.117	41.600	42.390	56.295	48.833	47.183	47.672	47.653	48.794	59.823	63.625	65.906	77.693	68.481	76.709
1308	BOOK VALUE PER SHARE	197.346	217.116	236.128	255.127	277.178	328.973	337.114	335.985	347.480	362.384	376.290	411.910	437.931	466.604	499.951	536.077
D037	MARKET TO BOOK VALUE EX. INTAN	1.020	1.200	1.210	1.420	1.510	1.600	1.530	1.300	1.020	1.330	1.800	1.540	1.810	2.470	2.740	2.350
1505	SALES PER SHARE	447.961	496.903	510.155	553.224	645.127	501.564	475.794	499.866	558.408	559.929	576.044	622.178	654.624	712.545	758.984	860.756
1015	CASH IN -OPERATING ACTIVITIES	#NA	#NA	353,000	402,000	508,000	395,000	414,000	369,000	367,000	346,000	468,000	541,000	541,000	544,000	412,000	661,000
1024	PAYMENTS: FIXED ASSETS	202,000	191,000	188,000	198,000	225,000	254,000	226,000	259,000	182,000	212,000	186,000	180,000	223,000	403,000	432,000	420,000
1040	CASH OUT-INVESTING ACTIVITIES	#NA	#NA	80,000	510,000	289,000	(364,000)	274,000	390,000	164,000	146,000	376,000	231,000	398,000	1,453,000	760,000	489,000
1045	CASH INFLOW FROM FINANCING	#NA	#NA	(304,000)	(144,000)	(118,000)	(85,000)	(134,000)	(540,000)	(88,000)	(92,000)	119,000	(111,000)	(148,000)	412,000	(221,000)	(119,000)
1048	NET CASH FLOW	#NA	#NA	(31,000)	(252,000)	101,000	674,000	6,000	(561,000)	115,000	108,000	211,000	199,000	(5,000)	(497,000)	(569,000)	53,000

DATASTREAM DOWNLOAD - RATIOS

ABF **ASSOCIATED BRIT.FOODS**

TYPE	DESCRIPTION	12/09/1992	18/09/1993	17/09/1994	16/09/1995	14/09/1996	13/09/1997	12/09/1998	18/09/1999	16/09/2000	15/09/2001	14/09/2002	13/09/2003	18/09/2004	17/09/2005	16/09/2006	15/09/2007
D013	DIVIDEND COVER - PUBLISHED	3.12	3.38	4.29	4.28	3.26	3.03	2.82	1.99	1.56	2.61	3.08	2.88	2.64	2.34	2.03	2.39
D040	PAYOUT RATIO - PUB'D	0.32	0.30	0.23	0.23	0.31	0.33	0.35	0.50	0.64	0.38	0.32	0.35	0.38	0.43	0.49	0.42
1506	RETURN ON EQUITY	9.93	12.72	15.53	11.51	11.81	25.41	9.00	6.52	5.10	8.65	11.01	10.64	10.17	9.30	7.72	9.00
D014	ROCE % - PUBLISHED	16.52	16.74	17.23	15.84	16.72	13.23	12.74	11.43	9.18	12.44	13.92	14.76	15.20	13.73	13.59	15.29
D015	OPTG PROF.MARGIN % - PUBLSHD	6.85	6.22	6.82	6.85	6.92	7.71	7.56	7.37	7.42	7.54	8.14	8.17	8.15	8.48	8.54	7.63
D016	PRETAX PROF.MARGIN % - PUB'D	7.51	7.71	8.46	7.66	7.53	9.04	9.34	6.98	5.45	7.92	9.09	9.17	9.35	8.34	6.82	7.32
D017	EARNINGS MARGIN % - PUBLISHED	4.96	5.20	6.82	5.11	4.87	6.18	6.32	4.28	3.13	5.50	7.08	6.76	6.62	5.92	5.02	5.43
722	TURNOVER/FIXED ASSETS	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA
723	TURNOVER/N. CURRENT ASSETS	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA
724	STOCK TURNOVER	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA
725	STOCK RATIO (DAYS)	47.00	45.00	50.00	48.00	42.00	51.00	51.00	53.00	58.00	57.00	54.00	53.00	50.00	50.00	57.00	59.00
731	CAPITAL GEARING %	14.81	13.50	10.37	8.94	7.20	6.52	6.18	7.12	7.12	7.50	12.86	12.60	10.84	20.73	14.46	13.94
733	BORROWING RATIO	17.75	15.97	11.88	10.11	8.00	7.15	6.74	7.89	7.89	8.33	15.14	14.54	12.26	26.37	17.87	17.04
741	WORKING CAPITAL RATIO	1.73	1.86	1.96	2.11	2.19	3.33	3.51	2.78	2.80	3.06	3.18	3.11	3.10	1.76	1.26	1.57
742	QUICK ASSETS RATIO	1.23	1.33	1.41	1.49	1.61	2.75	2.88	2.10	2.13	2.36	2.47	2.46	2.47	1.29	0.67	0.80
762	SALES PER EMPLOYEE	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA
D018	OPTG PROFIT PER EMPLOYEE	5.24	5.46	6.13	7.67	8.74	8.47	9.69	9.27	9.51	9.80	10.58	11.32	11.83	11.26	10.96	6.13
764	CAPITAL EMPLOYED /EMPLOYEE	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA
765	STOCK AND W.I.P. PER EMPLOYEE	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA	#NA
1503	RICBT	8.24	10.94	13.73	13.93	18.20	20.10	18.82	13.00	10.23	15.58	19.77	16.00	22.00	14.79	9.89	10.05
D038	MARKET VALUE TO SALES	0.44	0.51	0.56	0.65	0.65	1.05	1.09	0.77	0.60	0.81	1.03	0.86	1.01	1.17	1.10	0.92
D039	MARKET VALUE TO EBITDA	3.80	4.40	4.51	5.72	5.90	8.03	8.07	7.05	5.55	6.70	7.76	6.38	7.53	8.86	9.82	7.42

SEGMENTAL DATA EXTRACTED FROM ANNUAL REPORTS

ASSOCIATED BRITISH FOODS

	Services	1993	Services	1998	Services	2003
Sales By Division						
Manufacturing	N	3,143.0	N	3,900.0	N	4,324.0
Retail	Y	1,243.0	Y	295.0	Y	752.0
Grocery						
Primary Food & Agriculture						
Ingredients						
Spare						
Spare						
Spare						
Spare						
Spare						
Sub-Total	1,243.0	4,386.0	295.0	4,195.0	752.0	5,076.0
Duty (e.g. Excise)		0.0		0.0		0.0
Intra-Group		0.0		0.0		(185.0)
Unidentified/Rounding		0.0		0.0		0.0
External Sales		4,386.0		4,195.0		4,891.0
Discontinued		0.0		0.0		18.0
JV/Assoc. Co.		0.0		0.0		0.0
Differences		0.0		0.0		0.0
Total External Sales Per Datastream		4,386.0		4,195.0		4,909.0
Op. Profit By Division						
Manufacturing		239.0		293.0		324.0
Retail		34.0		23.0		87.0
Grocery						
Primary Food & Agriculture						
Ingredients						
Spare						
Spare						
Spare						
Spare						
Spare						
Sub-Total		273.0		316.0		411.0
Unallocated		0.0		0.0		0.0
(Profit)/Loss on Asset Disposals		0.0		0.0		0.0
Other (Income)/Costs		0.0		0.0		0.0
Discontinued		0.0		0.0		36.0
Corporate Costs		0.0		0.0		3.0
JV/Assoc. Co.		0.0		1.0		(7.0)
Exceptionals		0.0		0.0		0.0
Goodwill		0.0		0.0		(42.0)
Miscellaneous		0.0		0.0		0.0
Differences		0.0		0.0		0.0
Total Operating Profit Per Datastream		273.0		317.0		401.0
Assets (Banks Only)						
Manufacturing						
Retail						
Grocery						
Primary Food & Agriculture						
Ingredients						
Spare						
Spare						
Spare						
Spare						
Spare						
Total Continuing		0.0		0.0		0.0
Corporate		0.0		0.0		0.0
Discontinued		0.0		0.0		0.0
Miscellaneous		2,946.0		4,000.0		4,710.0
Differences		0.0		0.0		0.0
Assets Per Datastream		2,946.0		4,000.0		4,710.0
Reconciliation Datasteam to Pub Accs						
Profit After Tax & Min Ints Pub Accounts		228.0		265.0		332.0
Non-Equity Dividends		0.0		0.0		0.0
Miscellaneous		0.0		0.0		0.0
Differences		0.0		0.0		0.0
Earned For Ordinary Per Datastream		228.0		265.0		332.0

Appendix C – Database Definitions and Assumptions

This appendix provides details of the key principles, definitions and assumptions used in compiling the database.

ACCOUNTS

- **Windfall Taxes**
  The windfall tax levied by the UK government on the privatised utility companies – Gas, Electricity, Telephones & Water – in July 1997 have been excluded from tax and profit after tax figures in the database as they are exceptional charges. This treatment is consistent with DataStream.

- **Extraordinary Profits/Losses**
  Extraordinary items are excluded from the database as they are in DataStream figures. However, extraordinary items are very rare; FRS3 – Reporting Financial Performance replaced SSAP6 Extraordinary Items and Prior Year Adjustments and effectively stopped them by revising and tightening the definitions). The only significant extraordinary item in the Database is the £100m 'profit' recorded by Argyll/Safeway which represented compensation received from Guinness/Diageo following the legal case it brought relating to irregularities, principally a Guinness's illegal share support scheme, that occurred during its unsuccessful battle with Guinness to acquire Distillers.

- **Excise Duties**
  Excise duties are deducted from tobacco and brewing/spirit turnovers where possible. The accounts of Scottish & Newcastle, Allied Lyons/Allied Domeq and Guinness/Diageo show segmental turnover inclusive of excise duty which has been deducted as a single adjustment in the database to reduce total turnover to its net value. Bass/Intercontinental Hotels shows gross turnover in 1993 but net thereafter; given its withdrawal from brewing, this inconsistency is not significant. Whitbread's turnover excludes excise duty in all years.

- **Other Activities**
  Where no explanation/description provided, it is assumed that the activities relate to the major business activity. There is a reasonable assumption as, where details are given, other activities are frequently property, insurance, logistics, etc. related to the core/primary activity.

- **Mergers & Acquisitions**
  Business combinations are achieved in two ways: acquisitions where one company acquires a controlling interest, usually 100% of another and mergers where neither company is seen as acquiring the other and consideration is almost wholly in the form of shares in the enlarged company.

  A key advantage of mergers is that through the use of shares to achieve the combination of two or more companies the creation of goodwill, which

would result in amortisation charges in subsequent years, is avoided. This creates an incentive to have business combinations classified as mergers when in reality they are acquisitions. DataStream reviews mergers to establish if the underlying transaction is, in reality, an acquisition in which case it maintains the DataStream record of the company it deems to be the acquirer.

This research has categorised transactions as being acquisitions or mergers according to DataStream's interpretation of the underlying substance of each deal.

- **'Abnormal' Structures**
  Companies within the FTSE100 with 'abnormal' structures were treated as follows:
  - Dual Listing Companies (DLC)
    These companies remain separate legal entities quoted on separate exchanges but act, under a DLC agreement, as one entity with identical/balanced dividend policies and, usually, a common set of executive and non-executive directors often with the chairman of one company acting as deputy chairman of the other. DLC companies in the FTSE100 are:

    RTZ (UK and Australia) – Mining
    BHP Billiton (UK and Australia) – Mining (Billiton before DLC)
    Carnival (UK and US) – Cruises (P&O Princess before DLC)
    Shell – Oils (UK and Netherlands)
    Unilever – Food Manufacturing (UK and Netherlands)

    The consolidated accounts of DLCs are used in the database.

  - Joint Holding Companies
    These companies have no operations of their own but have a significant, usually 50%, shareholding in operating companies together with a partner. The only joint holding company in the FTSE100 is:

    Reed Elsevier (UK and Netherlands) – Publishing (Joint with Elsevier of Netherlands, UK company formerly called Reed International)

    The segmental report in the consolidated accounts of this company is used in the database with an adjustment to reduce the total turnover to zero as reported in the accounts of the LSE quoted UK holding company which records only dividend income from the operating company.

- **Service/Non-Service Split**
  Service activities are those that do not produce a tangible product. There are a few 'grey' areas which have necessitated some fine distinctions, e.g. software development (Sage Group) is non-service as it produces a

product, typically a software package, whereas computer system operation (Misys) is a service activity.

- **Categorisation Bias**
  There is an 'in-built' bias toward single business, dominant business and related diversified business categories as it is easy to aggregate reported segments that may reasonably be considered identical in terms of processes and products but it is not possible to disaggregate reported segments that, from descriptions included in the reports of chairmen and CEOs and lists of principal subsidiaries, are different.

DIRECTORS

- **Presidents**
  The position of president is deemed to be honorary without either executive or non-executive director responsibilities unless either the annual report and accounts, the remuneration report or associated notes specifically say otherwise, e.g. as at Schroders where the president is an executive director and sits on the company's board which is headed by a chairman. Examples of honorary presidents include Lord King at BA, Lord Forte at Forte and John Camden at RMC.

- **Chairmen**
  Where neither the annual report and accounts, the remuneration report nor associated notes specify the status – executive or non-executive – of the chairman, the receipt of bonus/incentive payments and/or share options is deemed to reflect executive status.

- **Length of Service**
  Where a director has left and returned to a company, an absence of less than 1 year is ignored and service is deemed continuous from the first appointment to the Board. Otherwise, the date of appointment will be that of the current period of directorship. Length of service is calculated by reference to the year of appointment rather than the exact date.

- **Mergers & Acquisitions**
  Where companies have merged, directors will be deemed to have been appointed to the Board of the combined company on the date they were appointed to the Board of either of the combining companies. However, where one company acquires another and appoints directors of the acquired company to its board the date of their appointment will be that on which they joined the acquiring company's board.

- **Additional Data Sources**
  FAME, FT Intelligence, Yearbooks and websites used to provide additional information regarding directors and their appointment dates. In a very small number of cases FAME shows default appointment dates for some directors. This only occurred in the early 1990s, the number of directors was not material and other sources were used to obtain correct dates wherever possible.

MAJOR SHAREHOLDERS

- Cross shareholdings, between Dual Listed Companies (DLCs) are ignored, e.g. BHP Billiton Pty's holding in BHP Billiton Plc and RTZ Corporation's holding in Rio Tinto plc.

- Where a substantial shareholding is noted as having more than one beneficial holder, e.g. where institutions have joint holdings, it is only included once in the list of major shareholders to avoid double counting of the holding.

- Where a trust is noted as a major shareholder, that holding will be excluded from the shareholding of any trustee should they also be noted as a major shareholder, e.g. several trusts are major shareholders in food retailer Morrisons and some of the company's directors are trustees.

APPENDIX D – Rationalisation of Reported Segments

In compiling the database some adjustments have been made to the segments reported by companies in their annual reports and accounts. Adjustments have been made to enhance consistency in reporting across companies in the same FTSE100 classifications, e.g. banks, insurance, pharmaceuticals, etc. and to eliminate geographic segmentation where the same activities are reported in separate segments according to location. These adjustments, which have been made following careful review of the descriptions of divisional activities included in reports, typically those of the chairman, chief executive and finance director, included in annual reports, seek to minimise distortion of product/service diversity by geographic diversification or by clearly identifiable differences in segmentation across companies in the same FTSE classifications. Examples of adjustments include the elimination of Wolseley's geographic – UK/US – segmentation of its Builders Merchants operations and the inconsistencies in segmental reporting by banks.

The following sections outline adjustments made to the segmental reports of companies operating in similar FTSE classifications

- **Insurance Companies**
  Insurance companies have become more complex since Channon's (1978) research into service companies; almost all insurance companies now have asset management businesses as well as insurance/assurance businesses. Published accounts (the Companies Acts make provisions for Banks and Insurance companies to submit accounts in a different format to those of other trading companies) do not provide sufficient information to identify revenues from asset management activities as they are absorbed into revenues from investments which include those on the investment of long-term and, to a lesser extent, short-term insurance premiums. Insurance companies are therefore operating in two-sided markets; one external generating premium income and, through the investment of those premiums, investment income and one internal generating revenue through investments both on behalf of customers and the company itself. As separation of customer and company investment returns is not possible from analysis of published accounts, this research effectively ignores investment revenues treating them as unallocated turnover.

  The effective under-recognition of asset management activities is accepted but it could fairly be described as an activity related to those of long-term/life and general insurance and therefore doesn't effect categorisation of insurance companies. In summary, insurance companies are treated as follows:

  - Long-term/Life Assurance Premiums – continuing and 'single' premiums less reinsurance (where insurance risk is effectively passed to third parties).

- General Premiums – all non long-term/life assurance premiums (policies include motor, household, fire, marine, etc.) less reinsurance and adjusted for unearned premiums, i.e. premiums paid in respect of periods after the financial year end.

- Differences between accounts premium incomes and DataStream revenues reflect investment returns that DataStream include in revenue. The differences are noted as 'unidentified/rounding differences'

All insurance company activities are treated as services.

- **Banks**
The nature and breadth of activities of banks has changed significantly since Channon's (1978) work on service companies. In addition to their traditional operations providing retail and business/commercial banking, they have added mortgage finance, insurance and stock broking activities and have become more international. Some of the changes followed deregulation of the City in 1986 (commonly referred to as 'Big Bang') others the demutualisation of some building societies including Northern Rock, Abbey National and Alliance & Leicester.

The increase in complexity since Channon's (1978) research into service companies is exacerbated by the lack of analysis of revenues in published accounts (the Companies Acts make provisions for Banks and Insurance companies to submit accounts in a different format to those of other trading companies) which do not provide sufficient information to identify revenues from different activities. Channon (1978) used interest income but the increased complexity of bank activities mean that this is no longer a valid proxy for turnover in the assessment of diversity. However, segmental reports do provide details of assets used by each activity. Therefore, assets have been used to determine diversification category.

Other changes in banks' operations centre on the way they manage their business; several banks now show their processing or 'manufacturing' activities as a separate activity in their segmental reports. Similarly, wholesale and treasury operations, which comprise raising finance to support other operations, are also often reported separately. Despite clear similarities between them and their operations, the banks show little consistency in their segmental reporting either across time or across the industry; HSBC, the largest UK bank, reports only two segments – commercial banking and investment banking – despite offering a full range of financial services whilst the far smaller ex-building society Abbey reports between 5 and 7 segments. Therefore, the segmental reports of banks have been rationalised into a maximum 4 'standard' activities; banking (personal and commercial), insurance (life and general), capital markets/investment banking and other which is not specified at most banks but which includes estate agency at Bradford & Bingley and private equity at Schroders. All bank activities are treated as services.

- **Property Companies**
  Primary activity is the establishment and active management of a portfolio of properties to yield income through rentals. The companies, e.g. British Land, Land Securities, MEPC, etc. do trade in properties and record profits/losses on that activity but that is considered a secondary activity ancillary to the core rental business. All property company activities are treated as services.

- **Media**
  In determining segmentation of media company activities, television broadcast and content has been amalgamated reflecting the inseparability of the two constituents of a television service. The similarities in publishing have been recognised by the amalgamation of different categories of book although, given the increased complexity of education publications which at Pearson include on-line services and CD/DVD support, they are kept separate. For similar reasons, consumer and scientific magazines are reported separately as are newspapers produced by Daily Mail and United Trust, Pearson and United News & Media. Finally, newswire services are deemed sufficiently different from the provision of financial information and transaction services at Reuters. Categorisation as industrial/manufacturing or service is dependent on whether physical products, e.g. books, are produced.

- **Mining**
  The activities of the three mining companies in the FTSE100 – BHP Billiton (formerly Billiton), RTZ and Xstrata – have been separated into high volume mining and metals activities, which, in addition to iron, bauxite and cooper extraction, include coal and some ore processing/smelting operations, and low volume/high value industrial minerals activities which include diamond mining. All mining activities are categorised as industrial/manufacturing.

- **Utilities**
  Companies providing energy and water services are classified as utilities. Reflecting the segmentation adopted by the majority of utilities companies, some of which have broadened their product range to encompass more than one type of energy, e.g. Scottish Power added water to its electricity activities, the generation and distribution of energy – gas and electricity – is treated as a single integrated activity. All utilities activities are treated as services.

- **Stores**
  Recognising the growing importance of store credit cards, where sufficient segmental information is available finance operations are treated as a separate activity. While several stores companies have both store and home/on-line shopping operations, each effectively amalgamates the two revenue streams into either a retail or home/catalogue shopping segment and makes no distinction between type of product, e.g. electrical, clothing, etc. sold. The only store to offer a pharmacy – Boots – shows this activity as a separate segment reflecting the need for specialist

professional/trained staff and legal control of stock. With the exception of Boots pharmaceutical manufacturing operations, all stores activities are services.

- **Supermarkets & Food Processing**
  A similar approach has been taken to that outlined in the above section covering stores. All food retailing activities are treated as services while food processing, primarily at Associated British Foods, is manufacturing/industrial.

- **Transport**
  Segmentation has been maintained where there are different modes of transport, e.g. bus, coach, rail and air, and substantially different operations, e.g. ferries & cruises and container & bulk shipping. All transport activities are deemed services.

- **Building Materials**
  Segmentation is maintained to reflect primary, e.g. quarrying, and processing, e.g. ready mixed concrete, activities. All distribution activities, e.g. builder's merchants, are deemed services while, consistent with the treatment of mining, quarrying is an industrial/manufacturing activity.

- **Brewers & Distillers/Hotels & Leisure**
  In classifications that cover a wide range of activities from brewing to hotels, restaurants and sports, health and fitness centres, segmentation has been maintained to reflect the differences inherent in the provision of these products/services, e.g. brewing differs from the production soft drinks. The differences inherent in the provision of hotel services compared to the operation of restaurants are reflected in those activities being kept separate. Depending on whether a physical product is produced, activities undertaken by companies within these classifications may be either industrial/manufacturing, e.g. brewing, or services, e.g. restaurants.

- **Engineering/Invensys**
  Review of the activities of companies within this classification, which includes Siebe, TI Group, British Aerospace, Rolls Royce and Smiths Industries, shows their segmentation to reflect different activities, e.g. polymer engineering, tubes and aerospace at TI Group. Except for some immaterial property development (British Aerospace) and engine leasing (Rolls Royce) activities, all operations within this classification are industrial/manufacturing.

- **Telephone Networks**
  Segmentation is maintained differentiating between fixed line and mobile telecommunications reflecting the significant differences in technology used. All operations are services.

- **Electronics**
  Information technology and computer services companies Misys and Sema are deemed to offer services while Sage, which provides software, and GEC which produces equipment which utilises a core competence in electronics, are categorised as industrial /manufacturing companies.

- **Other Classifications**
  Segmentation across companies in the oil & gas, packaging & printing, business services, chemicals and pharmaceuticals classifications has remained broadly unchanged with industrial/manufacturing categorisation dependent on the fabrication of a physical product.

APPENDIX E – FTSE100 Constituents 1993, 1998 & 2003

FTSE100 As At 31st December 1993

Company	Service	Rank	Mkt Cap	Herfindahl	W&M	Core
British Telecom	Yes	1	29,328	0.54	Related	Yes
HSBC	Yes	2	24,912	0.88	Dominant	N/A
Shell Transport & Trading	No	3	24,100	0.77	Dominant	N/A
Glaxo	No	4	22,061	1.00	Single	N/A
BP	No	5	19,650	0.56	Dominant	N/A
BAT Industries	Yes	6	17,036	0.50	Conglomerate	Yes
British Gas	Yes	7	14,776	0.66	Dominant	N/A
Hanson	No	8	13,540	0.21	Conglomerate	No
BTR	No	9	12,976	0.21	Conglomerate	No
Marks & Spencer	Yes	10	12,566	0.96	Single	N/A
Cable & Wireless	Yes	11	11,390	0.79	Dominant	N/A
SmithKline Beecham	No	12	10,316	0.41	Related	Yes
Barclays Bank	Yes	13	10,315	0.52	Related	Yes
National Westminster Bank	Yes	14	10,304	0.51	Related	Yes
Grand Metropolitan	No	15	9,852	0.38	Related	No
Unilever	No	16	9,756	0.35	Conglomerate	Yes
Guinness	No	17	9,588	0.52	Related	Yes
GEC	No	18	9,340	0.22	Related	No
RTZ	No	19	8,639	0.60	Dominant	N/A
Lloyds Bank	Yes	20	8,461	0.89	Dominant	N/A
Zeneca Group	No	21	7,942	0.34	Related	No
Sainsbury	Yes	22	7,925	0.95	Single	N/A
Reuters	Yes	23	7,433	0.57	Dominant	N/A
Prudential	Yes	24	6,826	0.86	Dominant	N/A
Abbey National	Yes	25	6,712	0.87	Dominant	N/A
GUS	Yes	26	6,528	0.65	Dominant	N/A
Boots	Yes	27	6,213	0.51	Related	Yes
National Power	Yes	28	6,185	0.98	Single	N/A
Allied Lyons	No	29	6,018	0.27	Related	No
Vodafone Group	Yes	30	5,975	1.00	Single	N/A
ICI	No	31	5,776	0.27	Related	No
Wellcome	No	32	5,704	1.00	Single	N/A
BAA	Yes	33	5,395	0.85	Dominant	N/A
Kingfisher	Yes	34	5,147	0.95	Single	N/A
Reed International	No	35	5,026	0.34	Related	No
Bass	Yes	36	4,652	0.21	Conglomerate	No
British Airways	Yes	37	4,279	0.84	Dominant	N/A
PowerGen	Yes	38	4,272	1.00	Single	N/A
Cadbury Schweppes	No	39	4,219	0.51	Related	Yes
Thorn EMI	No	40	4,207	0.25	Related	No
Tesco	Yes	41	4,191	1.00	Single	N/A
Land Securities	Yes	42	4,002	1.00	Single	N/A
P&O	Yes	43	3,856	0.24	Conglomerate	No
Scottish Power	Yes	44	3,716	0.75	Dominant	N/A
TSB	Yes	45	3,673	0.61	Dominant	N/A
Royal Bank of Scotland	Yes	46	3,620	0.97	Single	N/A
Commercial Union	Yes	47	3,597	0.57	Related	Yes
Pearson	No	48	3,344	0.48	Conglomerate	Yes
General Accident	Yes	49	3,229	0.69	Dominant	N/A
Rank Organisation	Yes	50	3,222	0.26	Related	No

FTSE100 As At 31st December 1993 (Cont.)

Company	Service	Rank	Mkt Cap	Herfindahl	W&M	Core
BOC Group	No	51	3,136	0.53	Related	Yes
Sun Alliance	Yes	52	3,123	0.63	Dominant	N/A
Argyll Group	Yes	53	3,096	1.00	Single	N/A
Redland	No	54	3,018	0.42	Related	Yes
Whitbread	Yes	55	3,016	0.52	Related	Yes
Standard Chartered	Yes	56	2,957	0.81	Dominant	N/A
Inchcape	Yes	57	2,897	0.51	Related	Yes
Scottish & Newcastle	No	58	2,835	0.43	Related	Yes
Reckitt & Colman	No	59	2,707	0.51	Related	Yes
Tomkins	No	60	2,616	0.23	Conglomerate	No
Bank of Scotland	Yes	61	2,612	1.00	Single	N/A
Associated British Foods	No	62	2,527	0.59	Dominant	N/A
British Steel	No	63	2,520	0.60	Dominant	N/A
Legal & General	Yes	64	2,459	0.88	Dominant	N/A
Caradon	No	65	2,455	0.49	Conglomerate	Yes
Siebe	No	66	2,439	0.50	Conglomerate	Yes
Granada	Yes	67	2,433	0.24	Conglomerate	No
Rentokil	Yes	68	2,349	0.65	Dominant	N/A
Blue Circle	No	69	2,332	0.48	Conglomerate	No
Bowater	No	70	2,265	0.37	Related	Yes
Thames Water	Yes	71	2,261	0.62	Dominant	N/A
Forte	Yes	72	2,249	0.34	Conglomerate	No
Wolseley	Yes	73	2,247	0.80	Dominant	N/A
MEPC	Yes	74	2,222	1.00	Single	N/A
Royal Insurance	Yes	75	2,206	0.84	Dominant	N/A
Enterprise Oil	No	76	2,204	1.00	Single	N/A
Severn Trent	Yes	77	2,193	0.69	Dominant	N/A
North West Water	Yes	78	2,185	0.64	Dominant	N/A
Warburg SG	Yes	79	2,020	1.00	Single	N/A
Guardian Royal Exchange	Yes	80	2,005	0.65	Dominant	N/A
Rolls-Royce	No	81	1,985	0.52	Related	Yes
Courtaulds	No	82	1,961	0.26	Related	No
Arjo Wiggins Appleton	No	83	1,937	0.52	Related	Yes
Sears Holdings	Yes	84	1,925	1.00	Single	N/A
Southern Electricity	Yes	85	1,918	0.89	Dominant	N/A
United Biscuits	No	86	1,895	0.73	Dominant	N/A
Carlton Communications	Yes	87	1,886	0.28	Related	No
TI Group	No	88	1,864	0.35	Conglomerate	No
Ladbroke	Yes	89	1,854	0.43	Conglomerate	Yes
RMC Group	No	90	1,836	0.45	Related	Yes
Williams Holdings	No	91	1,832	0.43	Conglomerate	Yes
Eastern Electricity	Yes	92	1,822	0.92	Single	N/A
Anglian Water	Yes	93	1,752	0.91	Single	N/A
Schroders	Yes	94	1,735	1.00	Single	N/A
Coats Viyella	No	95	1,727	0.29	Related	No
Scottish Hydro Electricity	Yes	96	1,714	0.90	Dominant	N/A
Burmah Castrol	No	97	1,628	0.43	Related	Yes
ASDA	Yes	98	1,608	0.91	Single	N/A
British Aerospace	No	99	1,561	0.50	Related	Yes
Smith & Nephew	No	100	1,535	0.73	Dominant	N/A
Totals		100	553,349	0.63	Average	

FTSE100 As At 31st December 1998

Company	Service	Rank	Mkt Cap	Herfindahl	W&M	Core
Glaxo Wellcome	No	1	74,903	1.00	Single	N/A
British Telecommunications	Yes	2	58,504	0.42	Related	Yes
BP Amoco	No	3	52,808	0.52	Related	Yes
SmithKline Beecham	No	4	46,863	0.43	Related	Yes
Lloyds TSB	Yes	5	46,460	0.96	Single	N/A
HSBC	Yes	6	41,995	0.91	Single	N/A
Shell Transport & Trading	No	7	36,718	0.63	Dominant	N/A
Vodafone Group	Yes	8	30,197	1.00	Single	N/A
Zeneca Group	No	9	24,861	0.41	Related	Yes
Diageo	No	10	24,494	0.32	Conglomerate	No
Unilever	No	11	21,979	0.38	Conglomerate	Yes
Halifax	Yes	12	20,796	1.00	Single	N/A
Nat West	Yes	13	19,668	0.64	Dominant	N/A
Barclays Bank	Yes	14	19,569	0.62	Dominant	N/A
Abbey National	Yes	15	18,198	0.81	Dominant	N/A
Cable & Wireless	Yes	16	17,773	0.85	Dominant	N/A
Prudential	Yes	17	17,678	0.95	Single	N/A
BG	Yes	18	15,010	0.59	Dominant	N/A
GEC	No	19	14,506	0.30	Related	No
Allied Zurich	Yes	20	14,084	0.57	Related	Yes
Rentokil Initial	Yes	21	12,973	0.21	Related	No
CGU	Yes	22	12,317	0.51	Related	Yes
Marks & Spencer	Yes	23	11,802	0.94	Single	N/A
Tesco	Yes	24	11,398	1.00	Single	N/A
Cadbury Schweppes	No	25	10,424	0.50	Related	Yes
Legal & General	Yes	26	9,967	0.87	Dominant	N/A
Granada	Yes	27	9,636	0.30	Conglomerate	No
Boots	Yes	28	9,354	0.56	Dominant	N/A
Sainsbury	Yes	29	9,215	0.85	Dominant	N/A
British Aerospace	No	30	8,982	0.59	Dominant	N/A
Reuters	Yes	31	8,966	0.50	Related	Yes
Bank of Scotland	Yes	32	8,869	1.00	Single	N/A
Kingfisher	Yes	33	8,846	0.98	Single	N/A
Royal Bank of Scotland	Yes	34	8,400	0.97	Single	N/A
Norwich Union	Yes	35	8,398	0.56	Related	Yes
Orange	Yes	36	8,368	1.00	Single	N/A
British American Tobacco	No	37	8,302	1.00	Single	N/A
Railtrack	Yes	38	7,965	0.75	Dominant	N/A
BSkyB	Yes	39	7,874	1.00	Single	N/A
Royal & Sun Alliance	Yes	40	7,665	0.58	Dominant	N/A
BAA	Yes	41	7,428	0.63	Dominant	N/A
Rio Tinto	No	42	7,416	0.55	Related	Yes
Scottish Power	Yes	43	7,397	0.57	Dominant	N/A
Pearson	No	44	7,265	0.27	Conglomerate	No
National Grid	Yes	45	7,071	0.86	Dominant	N/A
Bass	Yes	46	6,965	0.29	Conglomerate	No
Standard Chartered	Yes	47	6,965	1.00	Single	N/A
National Power	Yes	48	6,418	0.93	Single	N/A
GUS	Yes	49	6,373	0.60	Dominant	N/A
Allied Domeq	No	50	5,800	0.55	Related	Yes

FTSE100 As At 31st December 1998 (Cont.)

Company	Service	Rank	Mkt Cap	Herfindahl	W&M	Core
Woolwich	Yes	51	5,694	1.00	Single	N/A
GKN	No	52	5,670	0.57	Related	Yes
Reed International	No	53	5,376	0.51	Related	Yes
Centrica	Yes	54	5,370	0.83	Dominant	N/A
Colt Telecom	Yes	55	5,307	1.00	Single	N/A
Alliance & Leicester	Yes	56	5,162	1.00	Single	N/A
PowerGen	Yes	57	5,127	0.75	Dominant	N/A
Associated British Foods	No	58	5,116	0.87	Dominant	N/A
Siebe	No	59	4,991	0.39	Related	No
British Energy	Yes	60	4,950	0.99	Single	N/A
ASDA	Yes	61	4,919	1.00	Single	N/A
Compass Group	Yes	62	4,661	1.00	Single	N/A
United Utilities	Yes	63	4,573	0.47	Conglomerate	Yes
P&O	Yes	64	4,568	0.35	Conglomerate	No
Hays	Yes	65	4,525	0.39	Related	Yes
Scottish & Newcastle	Yes	66	4,327	0.48	Related	Yes
Sun Life & Provincial	Yes	67	4,286	0.77	Dominant	N/A
British Airways	Yes	68	4,267	0.84	Dominant	N/A
Land Securities	Yes	69	4,257	1.00	Single	N/A
BOC Group	No	70	4,203	0.67	Dominant	N/A
Thames Water	Yes	71	4,013	0.77	Dominant	N/A
BTR	No	72	4,004	0.52	Conglomerate	Yes
Whitbread	Yes	73	3,793	0.29	Related	No
ICI	No	74	3,787	0.27	Related	No
Rolls-Royce	No	75	3,745	0.69	Dominant	N/A
Telewest	Yes	76	3,711	1.00	Single	N/A
Severn Trent	Yes	77	3,478	0.51	Related	Yes
3i Group	Yes	78	3,451	1.00	Single	N/A
Carlton Communications	Yes	79	3,373	0.32	Related	No
Safeway	Yes	80	3,343	1.00	Single	N/A
Tomkins	No	81	3,334	0.28	Conglomerate	No
Southern Electric	Yes	82	3,275	0.79	Dominant	N/A
Reckitt & Colman	No	83	3,239	0.64	Dominant	N/A
EMI	No	84	3,159	1.00	Single	N/A
Stagecoach	Yes	85	3,146	0.42	Related	Yes
Schroders	Yes	86	3,123	1.00	Single	N/A
Amvescap	Yes	87	3,095	1.00	Single	N/A
Securicor	Yes	88	3,029	0.47	Related	No
GRE	Yes	89	2,974	0.67	Dominant	N/A
Ladbroke Group	Yes	90	2,895	0.68	Dominant	N/A
LucasVarity	No	91	2,823	0.73	Dominant	N/A
WPP	Yes	92	2,801	1.00	Single	N/A
Sema Group	Yes	93	2,724	1.00	Single	N/A
Smiths Industries	No	94	2,649	0.34	Conglomerate	No
United News & Media	Yes	95	2,635	0.35	Related	No
Nycomed Amersham	No	96	2,612	0.36	Related	No
Billiton	No	97	2,549	1.00	Single	N/A
Williams	No	98	2,487	0.43	Related	Yes
Misys	Yes	99	2,460	1.00	Single	N/A
British Land	Yes	100	2,315	1.00	Single	N/A
Totals		100	1,067,254	0.70	Average	

FTSE100 As At 31st December 2003

Company	Service	Rank	Mkt Cap	Herfindahl	W&M	Core
BP	No	1	100,589	0.47	Related	Yes
HSBC	Yes	2	97,309	0.51	Related	Yes
Vodafone Group	Yes	3	95,109	0.83	Dominant	N/A
Glaxo SmithKline	No	4	77,306	0.74	Dominant	N/A
Royal Bank of Scotland	Yes	5	48,675	0.96	Single	N/A
AstraZeneca	No	6	45,870	1.00	Single	N/A
Shell Transport & Trading	No	7	40,241	0.76	Dominant	N/A
Barclays Bank	Yes	8	32,931	0.73	Dominant	N/A
HBOS	Yes	9	27,820	0.78	Dominant	N/A
Lloyds TSB	Yes	10	25,434	0.91	Single	N/A
Diageo	No	11	22,895	1.00	Single	N/A
Tesco	Yes	12	18,810	1.00	Single	N/A
Anglo American	No	13	17,947	0.32	Related	No
Rio Tinto	No	14	16,597	0.71	Dominant	N/A
BT Group	Yes	15	16,395	0.44	Related	Yes
British American Tobacco	No	16	16,019	1.00	Single	N/A
Unilever	No	17	15,154	0.41	Conglomerate	Yes
BSkyB	Yes	18	13,729	1.00	Single	N/A
National Grid Transco	Yes	19	12,548	0.80	Dominant	N/A
BHP Billiton	No	20	12,180	0.57	Dominant	N/A
Aviva	Yes	21	11,240	0.56	Related	Yes
Standard Chartered	Yes	22	10,929	1.00	Single	N/A
BG	Yes	23	10,096	0.36	Related	No
Prudential	Yes	24	9,684	1.00	Single	N/A
Centrica	Yes	25	9,021	0.80	Dominant	N/A
Reckitt Benckiser	No	26	8,952	0.90	Dominant	N/A
Cadbury Schweppes	No	27	8,599	0.52	Related	Yes
Compass Group (New)	Yes	28	8,237	1.00	Single	N/A
Imperial Tobacco	No	29	8,094	1.00	Single	N/A
GUS	Yes	30	7,924	0.72	Dominant	N/A
Abbey National	Yes	31	7,845	0.93	Single	N/A
Kingfisher	Yes	32	7,355	0.99	Single	N/A
Scottish Power	Yes	33	6,946	1.00	Single	N/A
mmO2	Yes	34	6,892	1.00	Single	N/A
WPP	Yes	35	6,631	1.00	Single	N/A
Legal & General	Yes	36	6,616	0.88	Dominant	N/A
Marks & Spencer	Yes	37	6,540	0.92	Single	N/A
Sainsbury	Yes	38	6,103	0.96	Single	N/A
Reed Elsevier	No	39	5,936	0.41	Related	Yes
SABMiller	No	40	5,832	0.82	Dominant	N/A
Scottish & Southern Elec	Yes	41	5,814	0.85	Dominant	N/A
Boots	Yes	42	5,491	0.72	Dominant	N/A
Amersham	No	43	5,407	0.42	Related	Yes
BAA	Yes	44	5,283	0.60	Dominant	N/A
BAE Systems	No	45	5,186	0.62	Dominant	N/A
Pearson	No	46	5,039	0.45	Related	Yes
Allied Domeq	No	47	4,838	0.86	Dominant	N/A
Carnival	Yes	48	4,718	0.93	Single	N/A
Associated British Foods	No	49	4,661	0.75	Dominant	N/A
Land Securities	Yes	50	4,636	0.50	Related	Yes

FTSE100 As At 31st December 2003 (Cont.)

Company	Service	Rank	Mkt Cap	Herfindahl	W&M	Core
Wolseley	Yes	51	4,573	1.00	Single	N/A
Man	Yes	52	4,537	0.57	Related	Yes
Smith & Nephew	No	53	4,345	1.00	Single	N/A
BOC Group	No	54	4,251	0.74	Dominant	N/A
Alliance & Leicester	Yes	55	4,158	1.00	Single	N/A
Xstrata	No	56	3,987	0.99	Single	N/A
Intercontinental Hotels	Yes	57	3,940	0.58	Conglomerate	Yes
Gallaher	No	58	3,926	1.00	Single	N/A
3i Group	Yes	59	3,799	1.00	Single	N/A
Smiths	No	60	3,705	0.30	Conglomerate	No
United Utilities	Yes	61	3,697	0.48	Related	Yes
Hilton	Yes	62	3,622	0.70	Dominant	N/A
Old Mutual	Yes	63	3,577	0.45	Conglomerate	Yes
Morrison	Yes	64	3,537	0.99	Single	N/A
Rentokil Initial	Yes	65	3,489	0.23	Related	No
Reuters	Yes	66	3,456	0.58	Dominant	N/A
Granada	Yes	67	3,398	0.99	Single	N/A
Amvescap	Yes	68	3,305	1.00	Single	N/A
Scottish & Newcastle	No	69	3,282	1.00	Single	N/A
Cable & Wireless	Yes	70	3,201	1.00	Single	N/A
Next	Yes	71	3,043	0.89	Dominant	N/A
Northern Rock	Yes	72	3,043	1.00	Single	N/A
Hanson	No	73	3,006	0.60	Dominant	N/A
Safeway	Yes	74	2,987	1.00	Single	N/A
Rolls-Royce	No	75	2,903	0.60	Dominant	N/A
British Land	Yes	76	2,889	1.00	Single	N/A
Dixons Group	Yes	77	2,698	0.98	Single	N/A
Severn Trent	Yes	78	2,631	0.34	Related	No
Shire Pharmaceuticals	No	79	2,570	1.00	Single	N/A
Royal & Sun Alliance	Yes	80	2,520	0.72	Dominant	N/A
Daily Mail	No	81	2,513	0.48	Related	Yes
British Airways	Yes	82	2,485	0.85	Dominant	N/A
ICI	No	83	2,358	0.27	Related	No
Rexam	No	84	2,334	1.00	Single	N/A
Friends Provident	Yes	85	2,320	1.00	Single	N/A
Sage Group	No	86	2,264	1.00	Single	N/A
Exel	Yes	87	2,212	0.96	Single	N/A
EMAP	No	88	2,201	0.73	Dominant	N/A
Yell	Yes	89	2,156	1.00	Single	N/A
Whitbread	Yes	90	2,137	0.41	Conglomerate	Yes
Liberty International	Yes	91	2,136	0.94	Single	N/A
Hays	Yes	92	2,134	0.45	Conglomerate	No
Johnson Matthey	No	93	2,133	0.50	Related	Yes
Tomkins	No	94	2,079	0.48	Conglomerate	Yes
GKN	No	95	1,956	0.72	Dominant	N/A
Bradford & Bingley	Yes	96	1,952	1.00	Single	N/A
Bunzl	Yes	97	1,905	0.72	Dominant	N/A
Schroders	Yes	98	1,842	0.67	Dominant	N/A
Alliance Unichem	Yes	99	1,806	1.00	Single	N/A
Foreign & Colonial	Yes	100	1,788	1.00	Single	N/A
Totals		100	1,110,889	0.77	Average	

Appendix F – Data Summaries of FTSE100 Conglomerates

BASS/INTERCONTINENTAL HOTELS

	1993	1998	2003
Company Name	Bass	Bass	Intercontinental Hotels
Investor (31st Dec)			
FT Classification	Brewers & Distillers	Breweries, Pubs & Rests	Leisure & Hotels
Service	Yes	Yes	Yes
FTSE100	Yes	Yes	Yes
Market Cap. (£m)	4,652.0	6,965.0	3,940.0
Position	36	46	57
P/E Ratio	14.5	17.3	43.4
MV/Book (Excluding Intangibles)	#NA	#NA	1.6
Diversification			
Channon/W&M	Conglomerate	Conglomerate	Conglomerate
Core	No	No	Yes
Focus/Multiple Business	Multiple	Multiple	Multiple
Hill & Pickering	High	High	High
Herfindahl	0.21	0.29	0.58
No. of Divisions	6	5	2
No. of Unrelated Activities	3	3	2
Largest Activity Turnover (%)	27.8	35.5	69.5
Largest Related Group Turnover (%)	63.9	47.5	69.5
Performance			
External Turnover (£m)	3,747	4,231	2,152
Operating Profit (£m)	583	674	274
ROCE (%)	12.9	18.9	4.2
Gearing (%)	29.8	47.3	26.9
Corporate Governance			
Chairman	Prosser, I.	Prosser, I.	Webster, D.
Non-Executive	No	No	Yes
Tenure (Years)	6	11	0
CEO/COO/MD	N/A	N/A	North, R.
Tenure (Years)	0	0	1
Alt CEO/COO/MD	Chair	Chair	N/A
Major Shareholdings (%)	3.6	3.8	10.6

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Annual Reports & Accounts: 1993 Bass, 1998 Bass, 2003 Intercontinental Hotels Group.

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BAT/BRITISH AMERICAN TOBACCO

	1993	1998	2003
Company Name	BAT Industries	British American Tobacco	British American Tobacco
Investor (31st Dec)			
FT Classification	Miscellaneous	Tobacco	Tobacco
Service	Yes	No	No
FTSE100	Yes	Yes	Yes
Market Cap. (£m)	17,036.0	8,302.0	16,019.0
Position	6	37	16
P/E Ratio	16.6	11.0	13.4
MV/Book (Excluding Intangibles)	3.4	553.4	(3.5)
Diversification			
Channon/W&M	Conglomerate	Single	Single
Core	Yes	N/A	N/A
Focus/Multiple Business	Multiple	Focus	Focus
Hill & Pickering	High	Low	Low
Herfindahl	0.50	1.00	1.00
No. of Divisions	2	1	1
No. of Unrelated Activities	2	1	1
Largest Activity Turnover (%)	53.7	100.0	100.0
Largest Related Group Turnover (%)	53.7	100.0	100.0
Performance			
External Turnover (£m)	11,368	7,120	10,570
Operating Profit (£m)	1,513	1,043	2,109
ROCE (%)	21.9	19.2	44.5
Gearing (%)	37.1	91.7	62.7
Corporate Governance			
Chairman	Sheehy, P. (Sir)	Broughton, M.	Broughton, M.
Non-Executive	Yes	No	No
Tenure (Years)	11	0	5
CEO/COO/MD	Broughton, M.	Herter, U.	Adams, P.
Tenure (Years)	5	6	0
Alt CEO/COO/MD	N/A	N/A	N/A
Major Shareholdings (%)	0.0	0.0	35.0

References

Annual Reports & Accounts: 1993 BAT Industries, 1998 BAT Industries, 2003 British American Tobacco.

Brown-Humes, C. & Oram, R. (1997), *BAT Contemplates Changing Shape*, Financial Times, January 8th, 1997, p18.

Economist (1999), *Business: Got a Match?*, January 16th, Vol.350, Iss.8102, p57.

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BLUE CIRCLE

	1993	1998	2003
Company Name	Blue Circle	Blue Circle	
Investor (31st Dec)			
FT Classification	Building Materials	Building Matls & Merch	
Service	No	No	
FTSE100	Yes	No	
Market Cap. (£m)	2,332.0	2,411.0	
Position	69	0	
P/E Ratio	0.0	10.9	
MV/Book (Excluding Intangibles)	2.7	2.0	
Diversification			
Channon/W&M	Conglomerate	Conglomerate	
Core	No	Yes	
Focus/Multiple Business	Multiple	Multiple	
Hill & Pickering	High	High	
Herfindahl	0.48	0.53	
No. of Divisions	4	4	
No. of Unrelated Activities	2	2	
Largest Activity Turnover (%)	49.2	63.4	
Largest Related Group Turnover (%)	50.6	64.5	
Performance			
External Turnover (£m)	1,679	1,845	
Operating Profit (£m)	150	260	
ROCE (%)	10.7	14.7	
Gearing (%)	42.1	35.2	
Corporate Governance			
Chairman	Walters, P. (Sir)	Tugendhat, C	
Non-Executive	Yes	Yes	
Tenure (Years)	3	2	
CEO/COO/MD	Orrell-Jones, K.	Orrell-Jones, K.	
Tenure (Years)	1	6	
Alt CEO/COO/MD	N/A	N/A	
Major Shareholdings (%)	10.9	7.0	

References

Annual Reports & Accounts: 1993 Blue Circle Industries, 1998 Blue Circle Industries.

Batchelor, C. (2000), *Blue Circle to Focus on Overseas Strength*, Financial Times, February 21st, p25.

John, P. (1999), *Weighed Down by Asia*, Financial Times, March 27th, p2.

Skapinker, M. (2001), *A Cement Manufacturer With Far from Set Ideas*, Financial Times, February 23rd, p16.

Smy, L. (1999), *Blue Circle Sells Bathrooms Side*, Financial Times, February 3rd, p26.

BTR

	1993	1998	2003
Company Name	BTR	BTR	
Investor (31st Dec)			
FT Classification	Other Industrials	Engineering	
Service	No	No	
FTSE100	Yes	Yes	
Market Cap. (£m)	12,976.0	4,004.0	
Position	9	72	
P/E Ratio	20.9	16.4	
MV/Book (Excluding Intangibles)	6.2	0.0	
Diversification			
Channon/W&M	Conglomerate	Conglomerate	
Core	No	Yes	
Focus/Multiple Business	Multiple	Multiple	
Hill & Pickering	High	High	
Herfindahl	0.21	0.52	
No. of Divisions	5	4	
No. of Unrelated Activities	5	4	
Largest Activity Turnover (%)	24.6	68.4	
Largest Related Group Turnover (%)	24.6	68.4	
Performance			
External Turnover (£m)	8,422	7,435	
Operating Profit (£m)	1,292	1,126	
ROCE (%)	24.0	27.5	
Gearing (%)	46.7	57.0	
Corporate Governance			
Chairman	Ireland, N.	Bauman, R.	
Non-Executive	Yes	Yes	
Tenure (Years)	0	0	
CEO/COO/MD	Jackson, A.	Strachan, I.	
Tenure (Years)	2	2	
Alt CEO/COO/MD	N/A	N/A	
Major Shareholdings (%)	6.7	0.0	

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CARADON/NOVAR

	1993	1998	2003
Company Name	Caradon	Caradon	Novar
Investor (31st Dec)			
FT Classification	Building Materials	Building Matls & Merch	Construction & Bldg Matls
Service	No	No	No
FTSE100	Yes	No	No
Market Cap. (£m)	2,455.0	475.8	607.6
Position	65	0	0
P/E Ratio	33.5	8.3	13.8
MV/Book (Excluding Intangibles)	5.4	2.5	(5.1)
Diversification			
Channon/W&M	Conglomerate	Dominant	Dominant
Core	Yes	N/A	N/A
Focus/Multiple Business	Multiple	Focus	Focus
Hill & Pickering	High	Medium	Medium
Herfindahl	0.49	0.72	0.63
No. of Divisions	3	2	2
No. of Unrelated Activities	3	2	2
Largest Activity Turnover (%)	65.5	83.4	75.7
Largest Related Group Turnover (%)	65.5	83.4	75.7
Performance			
External Turnover (£m)	952	1,292	1,431
Operating Profit (£m)	115	124	75
ROCE (%)	35.3	(21.8)	(8.5)
Gearing (%)	20.7	39.2	50.4
Corporate Governance			
Chairman	Hichens, A.	Parker, E. (Sir)	Hearne, G. (Sir)
Non-Executive	Yes	Yes	Yes
Tenure (Years)	3	0	4
CEO/COO/MD	Jansen, P.	Hintz, J.	Hintz, J.
Tenure (Years)	4	1	6
Alt CEO/COO/MD	N/A	N/A	N/A
Major Shareholdings (%)	6.9	34.0	31.9

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FORTE

	1993	1998	2003
Company Name	Forte		
Investor (31st Dec)			
FT Classification	Hotels & Leisure		
Service	Yes		
FTSE100	Yes		
Market Cap. (£m)	2,249.0		
Position	72		
P/E Ratio	20.5		
MV/Book	0.6		
MV/EBITDA	3.9		
Diversification			
Channon/W&M	Conglomerate		
Core	No		
Focus/Multiple Business	Multiple		
Hill & Pickering	High		
Herfindahl	0.34		
No. of Divisions	4		
No. of Unrelated Activities	2		
Largest Activity Turnover (%)	43.5		
Largest Related Group Turnover (%)	53.4		
Performance			
External Turnover (£m)	1,936		
Operating Profit (£m)	169		
ROCE (%)	7.3		
Gearing (%)	32.5		
Corporate Governance			
Chairman	Forte, R.		
Non-Executive	No		
Tenure (Years)	1		
CEO/COO/MD	N/A		
Tenure (Years)	0		
Alt CEO/COO/MD	Multiple		
Major Shareholdings (%)	7.9		

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GRANADA

	1993	1998	2003
Company Name	Granada	Granada	Granada
Investor (31st Dec)			
FT Classification	Hotels & Leisure	Leisure & Hotels	Media & Entertainment
Service	Yes	Yes	Yes
FTSE100	Yes	Yes	Yes
Market Cap. (£m)	2,433.0	9,636.0	3,398.0
Position	67	27	67
P/E Ratio	21.3	18.9	26.0
MV/Book (Excluding Intangibles)	0.0	0.0	0.0
Diversification			
Channon/W&M	Conglomerate	Conglomerate	Single
Core	No	No	N/A
Focus/Multiple Business	Multiple	Multiple	Focus
Hill & Pickering	High	High	Low
Herfindahl	0.24	0.30	0.99
No. of Divisions	6	5	2
No. of Unrelated Activities	4	4	1
Largest Activity Turnover (%)	33.3	40.5	99.7
Largest Related Group Turnover (%)	49.2	40.5	100.0
Performance			
External Turnover (£m)	1,615	3,978	1,402
Operating Profit (£m)	205	967	129
ROCE (%)	0.0	0.0	0.0
Gearing (%)	0.0	0.0	0.0
Corporate Governance			
Chairman	Bernstein, A.	Robinson, G.	Allen, C.
Non-Executive	Yes	No	No
Tenure (Years)	14	2	0
CEO/COO/MD	Robinson, G.	Allen, C.	N/A
Tenure (Years)	2	2	0
Alt CEO/COO/MD	N/A	N/A	Vacant
Major Shareholdings (%)	19.8	0.0	100.0

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GUINNESS/DIAGEO

	1993	1998	2003
Company Name	Guinness	Diageo	Diageo
Investor (31st Dec)			
FT Classification	Brewers & Distillers	Alcoholic Beverages	Beverages
Service	No	No	No
FTSE100	Yes	Yes	Yes
Market Cap. (£m)	9,588.0	24,494.0	22,895.0
Position	17	10	11
P/E Ratio	17.8	20.7	17.0
MV/Book (Excluding Intangibles)	4.8	(120.8)	49.3
Diversification			
Channon/W&M	Related	Conglomerate	Single
Core	Yes	No	N/A
Focus/Multiple Business	Multiple	Multiple	Focus
Hill & Pickering	Low	High	Low
Herfindahl	0.52	0.32	1.00
No. of Divisions	2	4	1
No. of Unrelated Activities	1	3	1
Largest Activity Turnover (%)	59.5	43.6	100.0
Largest Related Group Turnover (%)	100.0	61.9	100.0
Performance			
External Turnover (£m)	3,439	9,874	6,795
Operating Profit (£m)	894	1,786	1,951
ROCE (%)	16.0	22.9	10.6
Gearing (%)	37.2	59.8	55.6
Corporate Governance			
Chairman	Greener, A. (Sir)	Greener, A. (Sir) & Bull, G. (Sir)	Blyth (Lord)
Non-Executive	No	No	Yes
Tenure (Years)	0	5	3
CEO/COO/MD	Baldock, B.	McGrath, J.	Walsh, P.
Tenure (Years)	4	1	3
Alt CEO/COO/MD	N/A	N/A	N/A
Major Shareholdings (%)	23.9	14.8	0.0

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HANSON

	1993	1998	2003
Company Name	Hanson	Hanson	Hanson
Investor (31st Dec)			
FT Classification	Conglomerates	Building Matls & Merch	Construction & Bldg Matls
Service	No	No	No
FTSE100	Yes	No	Yes
Market Cap. (£m)	13,540.0	3,109.0	3,006.0
Position	8	0	73
P/E Ratio	19.9	15.0	12.0
MV/Book (Excluding Intangibles)	3.2	2.1	1.6
Diversification			
Channon/W&M	Conglomerate	Dominant	Dominant
Core	No	N/A	N/A
Focus/Multiple Business	Multiple	Focus	Focus
Hill & Pickering	High	Low	Low
Herfindahl	0.21	0.75	0.60
No. of Divisions	8	3	2
No. of Unrelated Activities	5	2	1
Largest Activity Turnover (%)	31.8	85.7	72.1
Largest Related Group Turnover (%)	31.8	98.4	100.0
Performance			
External Turnover (£m)	9,668	1,590	3,498
Operating Profit (£m)	923	245	356
ROCE (%)	10.4	9.7	4.6
Gearing (%)	74.3	51.3	47.5
Corporate Governance			
Chairman	Hanson (Lord)	Collins, C.	Collins, C.
Non-Executive	No	Yes	Yes
Tenure (Years)	28	0	5
CEO/COO/MD	Bonham, D.	Dougal, A.	Murray, A
Tenure (Years)	1	2	1
Alt CEO/COO/MD	N/A	N/A	N/A
Major Shareholdings (%)	0.0	22.6	23.7

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HAYS

	1993	1998	2003
Company Name	Hays	Hays	Hays
Investor (31st Dec)			
FT Classification	Business Services	Support Services	Support Services
Service	Yes	Yes	Yes
FTSE100	No	Yes	Yes
Market Cap. (£m)	1,162.0	4,525.0	2,134.0
Position	0	65	92
P/E Ratio	25.1	31.9	22.9
MV/Book (Excluding Intangibles)	7.3	23.8	(14.3)
Diversification			
Channon/W&M	Related	Related	Conglomerate
Core	Yes	Yes	No
Focus/Multiple Business	Multiple	Multiple	Multiple
Hill & Pickering	Medium	Medium	High
Herfindahl	0.47	0.39	0.45
No. of Divisions	3	3	3
No. of Unrelated Activities	2	2	2
Largest Activity Turnover (%)	63.8	51.1	48.3
Largest Related Group Turnover (%)	79.3	82.8	51.8
Performance			
External Turnover (£m)	477	1,519	2,294
Operating Profit (£m)	68	208	152
ROCE (%)	38.5	49.8	(161.9)
Gearing (%)	24.9	57.2	100.7
Corporate Governance			
Chairman	Frost, R.	Frost, R.	Lawson, R.
Non-Executive	No	No	Yes
Tenure (Years)	4	9	2
CEO/COO/MD	Napier, J.	Cole, J.	Matthews, C.
Tenure (Years)	2	0	1
Alt CEO/COO/MD	N/A	N/A	N/A
Major Shareholdings (%)	25.3	7.8	12.4

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LADBROKE/HILTON

	1993	1998	2003
Company Name	Ladbroke	Ladbroke	Hilton
Investor (31st Dec)			
FT Classification	Hotels & Leisure	Leisure & Hotels	Leisure & Hotels
Service	Yes	Yes	Yes
FTSE100	Yes	Yes	Yes
Market Cap. (£m)	1,854.0	2,895.0	3,622.0
Position	89	90	62
P/E Ratio	13.9	15.9	18.1
MV/Book (Excluding Intangibles)	1.4	3.6	4.6
Diversification			
Channon/W&M	Conglomerate	Dominant	Dominant
Core	Yes	N/A	N/A
Focus/Multiple Business	Multiple	Focus	Focus
Hill & Pickering	High	Medium	Medium
Herfindahl	0.43	0.68	0.70
No. of Divisions	4	2	2
No. of Unrelated Activities	3	2	2
Largest Activity Turnover (%)	59.5	79.6	81.4
Largest Related Group Turnover (%)	59.5	79.6	81.4
Performance			
External Turnover (£m)	4,269	4,681	8,931
Operating Profit (£m)	162	325	256
ROCE (%)	7.4	19.0	10.3
Gearing (%)	38.9	41.8	41.7
Corporate Governance			
Chairman	Jackson, J.	Jackson, J.	Robinson, I. (Sir)
Non-Executive	Yes	Yes	Yes
Tenure (Years)	0	4	2
CEO/COO/MD	George, P.	George, P.	Michels, D.
Tenure (Years)	0	4	3
Alt CEO/COO/MD	N/A	N/A	N/A
Major Shareholdings (%)	0.0	0.0	23.1

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NORTH WEST WATER/UNITED UTILITIES

	1993	1998	2003
Company Name	North West Water	United Utilities	United Utilities
Investor (31st Dec)			
FT Classification	Water	Utilities	Utilities (Ex Electricity)
Service	Yes	Yes	Yes
FTSE100	Yes	Yes	Yes
Market Cap. (£m)	2,185.0	4,573.0	3,697.0
Position	78	63	61
P/E Ratio	9.7	11.5	9.2
MV/Book (Excluding Intangibles)	1.0	2.4	1.3
Diversification			
Channon/W&M	Dominant	Conglomerate	Related
Core	N/A	Yes	Yes
Focus/Multiple Business	Focus	Multiple	Multiple
Hill & Pickering	Low	High	Medium
Herfindahl	0.64	0.47	0.48
No. of Divisions	3	5	4
No. of Unrelated Activities	1	3	2
Largest Activity Turnover (%)	77.5	53.6	65.5
Largest Related Group Turnover (%)	100.0	53.6	91.4
Performance			
External Turnover (£m)	878	2,150	1,879
Operating Profit (£m)	320	597	524
ROCE (%)	12.0	13.6	8.3
Gearing (%)	28.1	52.3	58.9
Corporate Governance			
Chairman	Pitcher, D. (Sir)	Harding, C. (Sir)	Evans, R. (Sir)
Non-Executive	No	Yes	Yes
Tenure (Years)	0	0	2
CEO/COO/MD	Thian, R.	Green, D.	Roberts, J.
Tenure (Years)	1	1	4
Alt CEO/COO/MD	N/A	N/A	N/A
Major Shareholdings (%)	3.5	11.3	6.4

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OLD MUTUAL

	1993	1998	2003
Company Name			Old Mutual
Investor (31st Dec)			
FT Classification			Life Assurance
Service			Yes
FTSE100			Yes
Market Cap. (£m)			3,577.0
Position			63
P/E Ratio			8.6
MV/Book (Excluding Intangibles)			2.4
Diversification			
Channon/W&M			Conglomerate
Core			Yes
Focus/Multiple Business			Multiple
Hill & Pickering			High
Herfindahl			0.45
No. of Divisions			3
No. of Unrelated Activities			2
Largest Activity Turnover (%)			57.40
Largest Related Group Turnover (%)			57.40
Performance			
External Turnover (£m)			10,085
Operating Profit (£m)			2,446
ROCE (%)			48.4
Gearing (%)			31.6
Corporate Governance			
Chairman			Levett, M.
Non-Executive			Yes
Tenure (Years)			4
CEO/COO/MD			Sutcliffe, J.
Tenure (Years)			2
Alt CEO/COO/MD			N/A
Major Shareholdings (%)			22.8

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P&O

	1993	1998	2003
Company Name	P&O	P&O	P&O
Investor (31st Dec)			
FT Classification	Transport	Transport	Transport
Service	Yes	Yes	Yes
FTSE100	Yes	Yes	No
Market Cap. (£m)	3,856.0	4,568.0	1,740.0
Position	43	64	0
P/E Ratio	35.1	15.3	0.0
MV/Book (Excluding Intangibles)	1.5	1.6	1.7
Diversification			
Channon/W&M	Conglomerate	Conglomerate	Related
Core	No	No	No
Focus/Multiple Business	Multiple	Multiple	Multiple
Hill & Pickering	High	High	Medium
Herfindahl	0.24	0.35	0.36
No. of Divisions	5	4	4
No. of Unrelated Activities	3	2	2
Largest Activity Turnover (%)	29.4	46.1	47.2
Largest Related Group Turnover (%)	67.5	53.9	91.0
Performance			
External Turnover (£m)	5,587	5,912	2,291
Operating Profit (£m)	343	481	124
ROCE (%)	14.5	10.2	4.7
Gearing (%)	42.7	33.7	53.8
Corporate Governance			
Chairman	Sterling (Lord)	Sterling (Lord)	Sterling (Lord)
Non-Executive	No	No	No
Tenure (Years)	10	15	20
CEO/COO/MD	MacPhail, B. (Sir)	MacPhail, B. (Sir)	Woods, R.
Tenure (Years)	8	13	0
Alt CEO/COO/MD	N/A	N/A	N/A
Major Shareholdings (%)	4.9	35.6	21.9

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PEARSON

	1993	1998	2003
Company Name	Pearson	Pearson	Pearson
Investor (31st Dec)			
FT Classification	Media	Media	Media & Entertainment
Service	No	No	No
FTSE100	Yes	Yes	Yes
Market Cap. (£m)	3,344.0	7,265.0	5,039.0
Position	48	44	46
P/E Ratio	33.0	30.5	17.9
MV/Book (Excluding Intangibles)	3.4	(5.7)	(14.4)
Diversification			
Channon/W&M	Conglomerate	Conglomerate	Related
Core	Yes	No	Yes
Focus/Multiple Business	Multiple	Multiple	Multiple
Hill & Pickering	High	High	Medium
Herfindahl	0.48	0.27	0.45
No. of Divisions	4	4	3
No. of Unrelated Activities	4	3	2
Largest Activity Turnover (%)	62.0	31.2	60.5
Largest Related Group Turnover (%)	62.0	54.4	81.3
Performance			
External Turnover (£m)	1,320	2,251	4,048
Operating Profit (£m)	111	224	175
ROCE (%)	15.8	47.0	13.8
Gearing (%)	30.1	70.9	38.3
Corporate Governance			
Chairman	Blakenham, M.	Stevenson, D.	Stevenson, D.
Non-Executive	No	No	Yes
Tenure (Years)	10	1	6
CEO/COO/MD	Barlow, F.	Scardino, M.	Scardino, M.
Tenure (Years)	3	1	6
Alt CEO/COO/MD	N/A	N/A	N/A
Major Shareholdings (%)	8.9	10.6	26.9

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SIEBE/INVENSYS

	1993	1998	2003
Company Name	Siebe	Siebe	Invensys
Investor (31st Dec)			
FT Classification	Engineering - General	Engineering	Electronic & Elec Equip
Service	No	No	No
FTSE100	Yes	Yes	No
Market Cap. (£m)	2,439.0	4,991.0	647.5
Position	66	59	0
P/E Ratio	20.0	14.7	0.0
MV/Book (Excluding Intangibles)	3.1	19.5	(0.4)
Diversification			
Channon/W&M	Conglomerate	Related	Related
Core	Yes	No	No
Focus/Multiple Business	Multiple	Multiple	Multiple
Hill & Pickering	High	Medium	Low
Herfindahl	0.50	0.39	0.38
No. of Divisions	5	3	3
No. of Unrelated Activities	5	2	1
Largest Activity Turnover (%)	67.9	45.9	48.2
Largest Related Group Turnover (%)	67.9	85.8	99.9
Performance			
External Turnover (£m)	1,619	3,670	5,018
Operating Profit (£m)	217	576	208
ROCE (%)	18.5	38.3	(100.3)
Gearing (%)	46.1	49.7	95.9
Corporate Governance			
Chairman	Stephens, B.	Marshall, C. (Sir/Lord)	Marshall, C. (Sir/Lord)
Non-Executive	No	Yes	Yes
Tenure (Years)	3	0	5
CEO/COO/MD	N/A	Yurko, A.	Haythornthwaite, R.
Tenure (Years)	0	6	2
Alt CEO/COO/MD	Chair	N/A	N/A
Major Shareholdings (%)	14.0	12.0	28.9

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SMITHS INDUSTRIES

	1993	1998	2003
Company Name	Smiths Industries	Smiths Industries	Smiths
Investor (31st Dec)			
FT Classification	Engineering - Aerospace	Engineering	Aerospace & Defence
Service	No	No	No
FTSE100	No	Yes	Yes
Market Cap. (£m)	1,369.0	2,649.0	3,705.0
Position	0	94	60
P/E Ratio	18.4	17.8	13.2
MV/Book (Excluding Intangibles)	4.2	9.9	151.6
Diversification			
Channon/W&M	Conglomerate	Conglomerate	Conglomerate
Core	Yes	No	No
Focus/Multiple Business	Multiple	Multiple	Multiple
Hill & Pickering	High	High	High
Herfindahl	0.40	0.34	0.30
No. of Divisions	3	3	4
No. of Unrelated Activities	3	3	3
Largest Activity Turnover (%)	54.1	38.6	38.0
Largest Related Group Turnover (%)	54.1	38.6	48.4
Performance			
External Turnover (£m)	726	1,199	3,056
Operating Profit (£m)	106	240	380
ROCE (%)	27.2	56.2	31.8
Gearing (%)	34.7	44.3	47.8
Corporate Governance			
Chairman	Hurn, R. (Sir)	Hurn, R. (Sir)	Orrell-Jones, K.
Non-Executive	No	No	Yes
Tenure (Years)	2	7	5
CEO/COO/MD	N/A	Butler-Wheelhouse, K.	Butler-Wheelhouse, K.
Tenure (Years)	0	2	7
Alt CEO/COO/MD	Chair	N/A	N/A
Major Shareholdings (%)	12.3	10.8	24.7

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TI GROUP

	1993	1998	2003
Company Name	TI Group	TI Group	
Investor (31st Dec)			
FT Classification	Engineering - General	Engineering	
Service	No	No	
FTSE100	Yes	No	
Market Cap. (£m)	1,864.0	1,556.0	
Position	88	0	
P/E Ratio	27.4	10.3	
MV/Book (Excluding Intangibles)	6.6	21.3	
Diversification			
Channon/W&M	Conglomerate	Conglomerate	
Core	No	No	
Focus/Multiple Business	Multiple	Multiple	
Hill & Pickering	High	High	
Herfindahl	0.35	0.35	
No. of Divisions	3	3	
No. of Unrelated Activities	3	3	
Largest Activity Turnover (%)	43.2	40.1	
Largest Related Group Turnover (%)	43.2	40.1	
Performance			
External Turnover (£m)	1,323	2,079	
Operating Profit (£m)	134	239	
ROCE (%)	21.4	33.6	
Gearing (%)	59.6	53.2	
Corporate Governance			
Chairman	Lewinton, C. (Sir)	Lewinton, C. (Sir)	
Non-Executive	No	No	
Tenure (Years)	4	9	
CEO/COO/MD	N/A	Laule, W.	
Tenure (Years)	0	0	
Alt CEO/COO/MD	Chair	N/A	
Major Shareholdings (%)	14.6	16.4	

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TOMKINS

	1993	1998	2003
Company Name	Tomkins	Tomkins	Tomkins
Investor (31st Dec)			
FT Classification	Conglomerates	Engineering	Engineering & Machinery
Service	No	No	No
FTSE100	Yes	Yes	Yes
Market Cap. (£m)	2,616.0	3,334.0	2,079.0
Position	60	81	94
P/E Ratio	17.2	11.8	13.5
MV/Book (Excluding Intangibles)	3.4	13.8	10.9
Diversification			
Channon/W&M	Conglomerate	Conglomerate	Conglomerate
Core	No	No	Yes
Focus/Multiple Business	Multiple	Multiple	Multiple
Hill & Pickering	High	High	High
Herfindahl	0.23	0.28	0.48
No. of Divisions	5	4	3
No. of Unrelated Activities	5	4	3
Largest Activity Turnover (%)	32.2	35.6	64.3
Largest Related Group Turnover (%)	32.2	35.6	64.3
Performance			
External Turnover (£m)	2,060	5,048	3,150
Operating Profit (£m)	145	473	259
ROCE (%)	18.6	39.4	15.0
Gearing (%)	16.4	27.9	36.4
Corporate Governance			
Chairman	Moore, M.	Hutchins, G.	Newlands, D.
Non-Executive	Yes	No	Yes
Tenure (Years)	9	3	3
CEO/COO/MD	Hutchins, G.	Snowdon, D.	Nicol, J.
Tenure (Years)	9	2	1
Alt CEO/COO/MD	N/A	N/A	N/A
Major Shareholdings (%)	16.7	15.8	12.2

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UNILEVER

	1993	1998	2003
Company Name	Unilever	Unilever	Unilever
Investor (31st Dec)			
FT Classification	Food Manufacturing	Food Processors	Food Prods & Processors
Service	No	No	No
FTSE100	Yes	Yes	Yes
Market Cap. (£m)	9,756.0	21,979.0	15,154.0
Position	16	11	17
P/E Ratio	16.4	27.7	21.6
MV/Book (Excluding Intangibles)	2.1	7.2	(1.6)
Diversification			
Channon/W&M	Conglomerate	Conglomerate	Conglomerate
Core	Yes	Yes	Yes
Focus/Multiple Business	Multiple	Multiple	Multiple
Hill & Pickering	High	High	High
Herfindahl	0.35	0.38	0.41
No. of Divisions	5	4	4
No. of Unrelated Activities	2	2	2
Largest Activity Turnover (%)	51.5	52.1	56.1
Largest Related Group Turnover (%)	54.0	53.6	56.9
Performance			
External Turnover (£m)	27,863	27,094	29,501
Operating Profit (£m)	2,427	2,871	3,865
ROCE (%)	28.9	49.6	121.1
Gearing (%)	32.6	47.2	71.4
Corporate Governance			
Chairman	Perry, M. (Sir)	FitzGerald, N.	FitzGerald, N.
Non-Executive	No	No	No
Tenure (Years)	1	2	7
CEO/COO/MD	N/A	N/A	N/A
Tenure (Years)	0	0	0
Alt CEO/COO/MD	Multiple	Multiple	Multiple
Major Shareholdings (%)	5.0	5.0	14.0

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WHITBREAD

	1993	1998	2003
Company Name	Whitbread	Whitbread	Whitbread
Investor (31st Dec)			
FT Classification	Brewers & Distillers	Breweries, Pubs & Rests	Leisure & Hotels
Service	Yes	Yes	Yes
FTSE100	Yes	Yes	Yes
Market Cap. (£m)	3,016.0	3,793.0	2,137.0
Position	55	73	90
P/E Ratio	13.9	13.5	12.0
MV/Book (Excluding Intangibles)	1.0	2.0	0.8
Diversification			
Channon/W&M	Related	Related	Conglomerate
Core	Yes	No	Yes
Focus/Multiple Business	Multiple	Multiple	Multiple
Hill & Pickering	Low	Medium	High
Herfindahl	0.52	0.29	0.41
No. of Divisions	3	6	4
No. of Unrelated Activities	1	3	3
Largest Activity Turnover (%)	67.3	42.6	54.7
Largest Related Group Turnover (%)	100.0	91.9	58.2
Performance			
External Turnover (£m)	2,319	3,198	1,794
Operating Profit (£m)	183	384	242
ROCE (%)	8.9	12.8	8.1
Gearing (%)	20.0	26.1	33.9
Corporate Governance			
Chairman	Angus, M. (Sir)	Angus, M. (Sir)	Banham, J. (Sir)
Non-Executive	Yes	Yes	Yes
Tenure (Years)	1	6	3
CEO/COO/MD	Jarvis, P.	Thomas, D.	Thomas, D.
Tenure (Years)	8	1	6
Alt CEO/COO/MD	N/A	N/A	N/A
Major Shareholdings (%)	4.8	0.0	20.4

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WILLIAMS

	1993	1998	2003
Company Name	Williams Holdings	Williams	
Investor (31st Dec)			
FT Classification	Other Industrials	Support Services	
Service	No	No	
FTSE100	Yes	Yes	
Market Cap. (£m)	1,832.0	2,487.0	
Position	91	98	
P/E Ratio	19.6	18.4	
MV/Book (Excluding Intangibles)	7.0	(6.3)	
Diversification			
Channon/W&M	Conglomerate	Related	
Core	Yes	Yes	
Focus/Multiple Business	Multiple	Multiple	
Hill & Pickering	High	Medium	
Herfindahl	0.43	0.43	
No. of Divisions	4	3	
No. of Unrelated Activities	4	2	
Largest Activity Turnover (%)	60.2	55.0	
Largest Related Group Turnover (%)	60.2	89.1	
Performance			
External Turnover (£m)	1,164	2,320	
Operating Profit (£m)	189	313	
ROCE (%)	30.7	65.9	
Gearing (%)	45.7	96.8	
Corporate Governance			
Chairman	Rudd, N. (Sir)	Rudd, N. (Sir)	
Non-Executive	No	No	
Tenure (Years)	11	16	
CEO/COO/MD	Carr, R.	Carr, R.	
Tenure (Years)	5	10	
Alt CEO/COO/MD	N/A	N/A	
Major Shareholdings (%)	8.3	12.5	

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