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DIVERSIFICATION BY YOUNG, SMALL FIRMS (SUMMARY)

Rui Baptista
Technical University of Lisbon, rui.baptista@ist.utl.pt

Murat Karaöz
Akdeniz University, Antalya

João Correia Leitão
University of Beira Interior

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SUMMARY

DIVERSIFICATION BY YOUNG, SMALL FIRMS

Rui Baptista, Instituto Superior Técnico, Technical University of Lisbon, Portugal
Murat Karaöz, Akdeniz University, Antalya, Turkey
João Correia Leitão, University of Beira Interior, Portugal

Principal Topic

Diversification is a relatively untapped topic among studies focusing on young, small firms. Nevertheless, a range of studies indicate that diversification has been a favored growth strategy among a small proportion of these firms. Diversifying young firms may be looking for synergies or the sharing of co-specialized innovative assets between different lines of business. They may also be forced to diversify by adverse circumstances in the market.

This paper focuses specifically on two major questions:

i. Which factors determine the timing of diversification for a start-up;

ii. How does diversification (and its timing) affect the probability of survival of young firms.

We use the Quadros de Pessoal (QP) micro-data, a longitudinal matched employer-employee data set built from mandatory information submitted annually by all Portuguese firms with at least one wage-earner to the Ministry of Labor and Social Security. We are interested in the moment of ‘first-time diversification’ i.e. the very first event of diversification by a start-up. We estimate hazard models of time to diversification and firm survival, comparing diversifiers and non-diversifiers. In both models, sets of control variables are used to account for firm-level and industry-level determinants of diversification and survival.

Results and Implications

Only a very small proportion of young, small firms diversify in their first years. The shares of managers and qualified employees of the firm both have a positive impact on the likelihood of diversification, supporting the resource-based view. Young firms that entered very concentrated industries and/or industries with high growth rate volatility are more likely to diversify early in their lifetimes, possibly to correct entry mistakes.

Results suggest that a diversification strategy which is implemented at the moment of entry represents a significant advantage for firm survival, possibly because it is based on sufficient pre-entry resources and capabilities. For firms that are not diversified at start-up, diversification in the first years significantly hinders survival, possibly because it results from the correction of an entry mistake, rather than a deliberate growth strategy.

CONTACT: Rui Baptista; rui.baptista@ist.utl.pt; (T): +351.218.417.379; (F): +351.218.496.156. IN+, Instituto Superior Técnico, Av. Rovisco Pais, 1049-001 Lisbon, Portugal.