



**Investigating Economic Performance:
Whether International & Strategic Business Diversification
With Stakeholder Concerns Enhances Performance**

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SUMMARY OF THESIS

This research study investigated economic performance from a business and society perspective for firms in Australia. In particular tests were carried out to investigate whether firms that combined strategic business-level and international business diversification strategy (business) with a concern for stakeholders (society) enhanced economic performance. Data was gathered from a sample of 150 Australian publicly listed companies, which were made up of the top 50 companies measured by market capitalisation, for three years 1993 to 1995 inclusive.

The importance of challenging the assumption of linearity, for the business and society relationship developed, was examined. The identification of critical cut-off points for each of stakeholder and international diversification activity divided the sample into low to moderate and high levels of activity. Statistically significant and positive results of the combined effects of international and strategic business diversification with stakeholder concerns on economic performance were identified at the low-to-moderate levels of stakeholder and international diversification activity rather than at high levels. In particular it was found that the relationship between (1) multinationality and community stakeholder concerns on economic performance and (2) the interaction of multinationality with country scope and community stakeholder concerns on economic performance were both statistically significant and positive at the low-to-moderate rather than high levels of activity. These results provided evidence of a non-linear business and society relationship with economic performance.

The major implication for theory was the development of a *socioeconomic* theoretical framework using resource-based, transaction cost and instrumental stakeholder theory for investigating economic performance. Moreover a need to develop a cogent theory to explain the non-linear relationship between economic performance and stakeholder concerns was identified. The major practical implication for investigating economic performance, was the need to determine whether the individual relationships of international diversification on economic performance and stakeholder concerns on economic performance were non-linear prior to testing a combined relationship. Further research, which considers the importance of business and society aspects when investigating economic performance, should move away from the notion of treating business and society as two separate issues, as economic performance is a complex phenomenon involving more than one discipline at any one time. The major implication for future investigation, of combined business and society effects on economic performance, was to suggest the need to investigate for the possibility of non-linear relationships rather than assuming that they are linear. Further studies that identify a non-linear relationship can divide their sample into low to moderate versus high levels of activity which may reveal finer and more rewarding results as has been the case for the current study.

DECLARATIONS

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I certify that this thesis does not incorporate without acknowledgment any material previously submitted for a degree or diploma in any university; and that to the best of my knowledge and belief it does not contain any material previously published or written by any other person except where due reference is made in the text.

Nicholas Constantine Mangos

I believe that this thesis is properly presented, conforms to the specifications of thesis presentation in the university, and is *prima facie* worthy of examination.

Peter William OBrien, PhD.

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CHAPTER ONE

INTRODUCTION

1.1 Purpose of the Research

The purpose of the research study was to investigate whether a firm's combined strategic and international business diversification with stakeholder concerns enhances economic performance. This business and society study challenged the linearity of each relationship when investigating economic performance. Particular emphasis was placed on the importance of any interactive effects between business and international diversification with stakeholder management when investigation economic performance. The study considered the following variables when investigating economic performance:

- (1) business-level diversification,
- (2) international diversification,
- (3) the interaction between business-level and international diversification,
- (4) stakeholder concerns,
- (5) combined business-level and international diversification with stakeholder concerns,
- (6) combined international diversification with stakeholder concerns.

1.2 Background to the Research

Strategic management, international business management and stakeholder concerns represent three main streams of independent research which have made a contribution to investigating economic performance but they have been considered independently within unidisciplinary frameworks. Recently, consideration has been given to the interaction between the two streams of international business management and strategic management in explaining effects on economic performance, but empirical research in this area has been sparse. There was also evidence that corporations are encouraged to increase their emphasis on stakeholder accountability and that the code of conduct of a firm accommodate the interests and

needs of a variety of stakeholders (Verschoor, 1998). The idea of considering only the concerns of stockholders at the expense of other stakeholders has been criticised.

A suggestion was:

that effective corporate governance requires careful balancing the interests of customers, suppliers, the community, employees, and the general public. Consequently, a company's impact on its stakeholders is becoming an emerging hallmark of corporate performance (Verschoor, 1998: 1511).

Furthermore, Verschoor (1998) emphasised that a broader concern for social responsibility towards stakeholders was developing into a "mainstream management issue in achieving higher profitability". This view provided support for the inclusion of other stakeholders as well as stockholders in an investigation of economic performance. A combined stockholder and other stakeholder model provided additional insight when investigating economic performance.

Little, if any, research has considered the importance of the combined effects of strategic and international business diversification with stakeholders in an integrated way when investigating economic performance. The current study combines strategic management, international business management and stakeholder streams in analysing the multidimensional characteristics of economic performance. Using a dual approach has been previously suggested in prior literature where consideration was given to both the economic and organisational factors effecting economic performance (Hansen and Wernerfelt, 1989).

In the current study specific consideration was given to the strategic and international factors which include the interactive effects of business-level diversification strategy with international diversification strategy together with stakeholder effects on economic performance. Including but also extending beyond the business perspective to include a stakeholder perspective (social) when

examining organisational phenomena (such as economic performance), has been termed a “Business and Society” approach by some researchers (Gailbraith, 1952; Jones, 1983; Monsen and Downs, 1965; Wood, 1996).

Past research testing the following three linkages with economic performance abounds, but only within each perspective:

- (1) business-level diversification strategy and economic performance,
- (2) international diversification and economic performance, and
- (3) social responsibility reporting/stakeholder concerns and economic performance.

There appears to be sparse research involving the interaction between business-level and international diversification strategy and its effect on economic performance (Geringer, Beamish and da Costa, 1989; Hitt, Hoskisson and Ireland, 1997; Tallman and Li, 1996). This interaction will make up a fourth linkage to be tested:

- (4) interaction between business-level and international diversification strategy and its effect on economic performance

Furthermore, there was no evidence, from an analysis of past research, of combining both stakeholder concerns with the interaction of business level on international diversification strategy when investigating economic performance making for a fifth linkage for testing:

- (5) interaction between business level and international diversification strategy with stakeholder concerns on economic performance.

From the above mentioned five linkages it was clear that economic performance was a multidimensional phenomenon. Research has been carried out on this phenomenon in several disciplines. The current study, unlike previous studies considers the impact of all five linkages, which bring together strategic

management, international business management and stakeholder streams on economic performance.

What the three sets of explanatory factors of economic performance provided was an opportunity to analyse a broader set of stakeholders of the firm than traditionally covered in the strategic management and international business research at any one time. It could be argued that the strategic management and international business factors, which are centred on business diversification and international business diversification, are concerned in the main with the following stakeholders: management, shareholders and creditors. Whilst it could be argued that social responsibility factors are concerned with stakeholders which include: employees, environmental groups, government and community.

The combined effects of international diversification and strategic management with stakeholder management on economic performance represent a business and society approach to investigating economic performance. First from an international perspective; second from a business-level diversification strategy perspective; third from an interaction of international and business-level diversification; fourth from a social responsibility reporting perspective, and the fifth an integration of business and international diversification with stakeholder management.

Past studies have considered only a single aspect of diversification and have assumed homogeneity in other directions (Tallman and Li, 1996). To cater for the problem of homogeneity, the effect of the interaction of both business diversification and international diversification on economic performance will be further considered in the current study.

1.3 A Socioeconomic Framework: Incorporating Transaction costs, Resource based and Instrumental Stakeholder theory

In order to cater for three theories used to investigate economic performance, a socioeconomic framework was developed in the current study. The 'socio' component of the framework refers to a stakeholder perspective whilst the 'economic' component refers to a strategic and international business diversification perspective. In the process of developing this framework, detailed in Chapter Five, three extant theories from several disciplines were utilised: including transaction cost, resource-based and instrumental stakeholder theory.

From a strategic and international business diversification perspective it was argued that firms utilise core competencies/internal resources and capabilities, from business-level diversification and use that to take advantage of opportunities available on an international level. This approach was referred to as "the resource based view of the firm" (Hitt et al. 1997: 769). There was evidence that supports that as firms further diversify internationally they experience increasing transaction costs, which includes the cost of coordinating between business units between different overseas markets (Hitt et al. 1997). Recent literature argued that there will be a point where multiple transactions among international markets will cost more than the benefits derived from resource sharing, benefits of economies of scope and the advantages of additional market share opportunities (Hitt et al. 1997). Additional costs of further transacting overseas beyond a certain level have been examined in terms of transaction cost theory (Hitt et al. 1997).

The net effect of transaction costs was to create diminishing returns to international diversification which results in an inverted U-shaped curvilinear relationship between the international diversification and economic performance (Hitt et al. 1997). On further analysing, studies which have considered the potentiality of

curvilinear relationships when attention was given to international diversification strategy (Buckley, 1984; Buckley, Dunning and Pearce, 1984; Daniels and Bracker, 1989; Geringer et al. 1988; Haar, 1984; Hitt et al. 1997; Kumar, 1984; Ramaswamy, 1995) it was found that “only one (Hitt et al. 1997) articulated the beginnings of a cogent theoretical rationale behind curvilinearity and offered an empirical approach to test such a relationship” (Gomes and Ramaswamy, 1999: 179).

The second component of the socioeconomic framework referred to stakeholder concerns so reference was made to stakeholder perspective. There was evidence from stakeholder theory “that companies do explicitly manage their relationship with different stakeholders” (Bendheim, Waddock and Graves, 1998: 306). Companies are said to manage their stakeholders for instrumental or performance reasons. As the current study is concerned with the relationship between stakeholder concerns and economic performance instrumental stakeholder theory will be used (Donaldson and Preston, 1995; Freeman, 1999; Jones, 1995). Instrumental stakeholder theory was noted in the following quotation:

Stakeholder theory is also instrumental. It establishes a framework for examining the connections, if any, between the practice of stakeholder management and the achievement of various corporate performance goals. The principal focus of interest here has been the proposition that corporations practicing stakeholder management will, other things being equal, be relatively successful in conventional terms (profitability, stability, growth, etc.) (Donaldson and Preston, 1995: 67).

Instrumental stakeholder theory was used in the current research to identify connections between stakeholder concerns and economic performance. Earlier work in the field of stakeholder management outlined and developed the basic concepts of a stakeholder approach (Freeman, 1984). More recent evidence notes the usefulness of instrumental stakeholder theory in further investigation of economic performance (Freeman, 1999). The need for an instrumental stakeholder theory came from earlier studies which examined the relationship between corporate

social responsibility and economic performance (Jones, 1995). On closer examination of these earlier studies there was no “credible theory, promoting Ullmann (1985) to call them ‘data in search of a theory’ ” (Jones, 1995: 430). Regarding the relationship between economic performance and stakeholder concerns, a suggestion was that they represent “manifestations of attempts to establish trusting, cooperative firm/stakeholder relationships and should be positively linked to a company’s financial performance” (Jones, 1995: 430). An instrumental stakeholder theory was used in the current research to investigate the relationship between stakeholder concern and economic performance.

What instrumental stakeholder theory does not explain is the phenomenon that was evidenced by Bowman and Haire (1975) and at a latter date given further support by Mintzberg (1983), namely that there was an inverted U-shaped relationship between stakeholder concerns and economic performance. A critical cut off point was identified as the median level (Bowman and Haire, 1975) and Griffin and Mahon (1997) also acknowledged a cut off point in a recent study. Evidence recently suggests that much can be gained if firms are divided into low and high levels of social disclosure. More specifically, use has been made of a “Corporate financial and Social performance Matrix” in dividing corporate social performance into low and high (Griffin and Mahon, 1997: 24).

There was no theory developed to explain a cut-off point empirically observed by Bowman and Haire (1975). The inverse U-shaped relationship has been explained in two ways. In the first instance, that the stock market is willing to reward socially responsible behaviour only to a point. Another explanation for this outcome was “Don’t stand out from the crowd, do no more than is expected” or “it pays to be good but not too good” (Mintzberg, 1983: 7). In Bowman and Haire’s own terms it suggests that “the mean is really golden” (Bowman and Haire, 1975: 57).

The interesting outcome of the study by Bowman and Haire (1975) and the review of the outcomes by Mintzberg (1983) was the need for further work regarding the level or extent of stakeholder concern and whether there is a critical cut-off point statistically measured that can help in empirically examining this relationship in the current study. The issue in this discussion was that instrumental stakeholder theory together with the possibility of an inverse U-shaped relationship between stakeholder concerns and economic performance was used to test this relationship in the current study.

1.4 Research Problem and Question

Previous research which investigated economic performance identified that a broader coverage including stakeholders as well as stockholders was lacking (Verschoor, 1998). The five linkage previously described in section 1.2 considered the combined effects of strategic and international business diversification with stakeholder concerns on economic performance. These combined effects bring together stakeholder, strategic and international diversification.

The research problem underlying this study, therefore, were

Whether strategic and international business diversification with stakeholder concerns enhances economic performance?

When investigating economic performance the research question underlying the current study was

Whether the combined concerns for international and business-level diversification with stakeholder interests was positively related to economic performance?

This addressed a socioeconomic approach to investigating economic performance and suggested that successful economic performance be considered from both a stockholder and broader stakeholder perspective (Waddock and Graves, 1999).

1.5 Justification for the Study

Research which has investigated the relationship between international diversification and economic performance have provided mixed results (for instance, Geringer et al. 1989; Rugman, 1979). A possible explanation for the mixed results was that the relationship was more complex than first thought (Hitt et al. 1997). Hitt et al. (1997) suggested that many firms that are diversified on an international level are also diversified at the business-level. In particular the suggestion that firms which diversified at the business-level, gained internally from the benefits of economies of scale, scope and learning (Kogut, 1985). The aforementioned benefits allow for easier application of the relationships among business segments and international geographic areas as it allows for sharing of distinctive firm capabilities and core competencies across business segments (Porter, 1985). Thus business-level diversification can assist firms to exploit international markets based on a resource-based view of the firm (Fladmoe-Lindquist and Tallman, 1994). Firms with strong core competencies which are a result of development in their domestic country operations can apply these competencies to international markets (Bartlett and Ghoshal, 1989; Hitt et al. 1997). Furthermore, Porter (1990) argued that competitive advantages from successful domestic operations provide the confidence and willingness to apply the same competitiveness in international markets to further increase economic performance.

The positive relationship between international diversification and firm economic performance has been impressive but on closer examination it appears that the outcomes have been mixed (Ramaswamy, 1995; Tallman and Li, 1996). For instance Daniels and Braker (1989), Grant (1987), Haar (1989), Kim, Hwang and Burgers, (1993); Vernon (1971) identified a positive relationship between international diversification and economic performance. On the other hand, others

did not identify a linear relationship between international diversification and economic performance (Geringer et al. 1989, Kumar, 1984; Morck and Yeung, 1991). In particular, Geringer et al. (1989) found from their analysis that there was a non-linear inverted U-shaped relationship between international diversification and economic performance, with was further supported by Hitt et al. (1997) and more recently by Gomes and Ramaswamy (1999). The explanation for this curvilinear outcome was that low to moderate levels of international diversification provides positive benefits to a firm through economic performance. Beyond that low to moderate level however the firm experiences significant costs associated with further international diversification. Evidence suggested that, as international geographic dispersion escalates, transaction costs and managerial information processing are increased. Then diminishing returns begin which impacts progressively with a negative impact on economic performance. A few prior studies considered the increase in costs of foreign transactions by referring to geographic dispersion (Gomes and Ramaswamy, 1999; Hitt et al. 1997; Jones and Hill, 1988).

These transaction costs included coordination, distribution and management costs. Costs derive from different government regulations, trade laws and currency value fluctuations across countries, access to raw materials and employee skills requiring considerable coordination. Furthermore, these transaction costs and variations experienced across geographic region increases managerial information-processing requirements. The types of costs identified included logistical costs, trade barriers, and cultural diversity which make management of internationally diversified firms highly complex (Hitt et al. 1997).

The result of transaction costs and increasing demands of managerial information-processing demands suggest that, eventually, as an organisation progressively further internationalises, a point will be reached where the cost of international diversification will outweigh the benefits. More specifically, "the internal

governance costs exceed the benefits provided by economies achieved and thus the range of resources used and scope of governance exceeds managerial capabilities” (Hitt et al. 1997: 773).

The arguments presented suggest a non-linear inverted U-shaped relationship between international diversification and economic performance. The conflicting results evidenced from prior research of a positive, negative or no relationship between international diversification and economic performance could be explained using the argument that relationships are non-linear and that once a firm goes beyond a moderate level of international diversification then costs begin to exceed benefits and economic performance suffers.

The linkages between stakeholder management reporting and economic performance are far from clear (Ullmann, 1985; Waddock and Graves, 1997). Evidence indicates an ambiguous relationship (Alexander and Buchholz, 1978; Aupperle, Carroll and Hatfield, 1985; Shane and Spicer, 1983; Ullmann, 1985). Other findings detect a positive link but it is still unclear whether financially successful firms merely move or direct resources to social responsibility activities and so establish a higher standard, known as a "Slack Resource Theory" (Waddock and Graves, 1997: 304). Alternatively findings can suggest that better social responsibility performance results in better economic performance, known as "Good Management Theory" (Waddock and Graves, 1997: 304) also supported by McGuire, Schneeweiss and Sundgren, (1988) and Ullmann (1985).

Reports of research on the relationship between economic performance and stakeholder management have produced mixed results, however the relationship still remains important in further testing the level of managements social responsibility behaviour (e.g., Cochran and Wood, 1984). If a positive relationship between economic performance and stakeholder management can be shown to exist then

managers may be prompted to place more emphasis on the level of stakeholder involvement.

The inconsistency in findings may have been due to misspecification of the proxy variables for social responsibility. Examples of proxy variables used for social responsibility have been reputation index/ratings as well as disclosure of social responsibility in corporate annual reports. On the other hand it could have been due to the employment of differing methods of measuring economic performance. Some studies used accounting variables (Bowman, 1978; Cochran and Wood, 1984; Freedman and Jaggi, 1982; Preston, 1978), whereas others used market variables (Anderson and Frankle, 1980; Belkaoui, 1976; Ingram, 1978; McGuire et al. 1988). Cochran and Wood (1984) included small sample size and control groups and inadequate time periods as issues which contribute to these inconsistencies. Furthermore, limitations may apply to studies which assume that capital markets are efficient (e.g., Ingram, 1978) and that the Capital Asset Pricing Model applies (e.g., Anderson and Frankle, 1980).

Perhaps there was also a non-linear relationship between economic performance and stakeholder management which can explain these mixed results. Only two major studies have been identified which consider whether a non-linear relationship exists, an earlier study by Bowman and Haire (1975) where it was found that the mean level of social disclosure was 'golden' and another more recent study of Griffin and Mahon (1997) where it was found that there was justification in dividing social performance into low and high levels.

Of significance to the current study was that the inconsistencies in findings may also have been due to the significant interactive effect of international and business-level diversification strategy on economic performance. Also there is a need to consider the interactive effects of multinationality and country scope on economic

performance. Of importance was the nature of the relationship between international diversification and economic performance as well as the relationship between economic performance and stakeholder management and whether these relationships were non-linear or not. No other known study has tested the combined international, business level diversification with stakeholder concerns on economic performance.

1.6 Importance of the study

The study is important in that, unlike other studies, it investigates economic performance when consideration is given to both stockholders and stakeholders. In doing so the study specifically incorporates both an international and business-level diversification strategy from a strategic management perspective, and international business management perspective together with a corporations commitment to employees, community, customers (the product category) and environments, reflecting stakeholder concerns. The importance of combining stakeholders and stockholders is noted in the following quotation from a recent working paper:

The study, in sum, provides strong evidence that treating employees, community, environment, customers, and other groups (such as minorities and women counted in the “diversity” category) is related to successful financial performance, that is, treating owners as well.given the nature of the data, we can say that treating stakeholders--and shareholders—well seem to be strongly intertwined, creating additional evidence for what Collins and Porras called a new logic of “both/and” in thinking about stakeholders and shareholders. (Waddock and Graves, 1999: 2)

Furthermore, issues analysed recently by Collins and Porras (1995) and further developed and raised by Waddock and Graves (1999) reflect additional support for the current study:

The question remains, however, as to the extent to which these companies (visionary) also attain their extraordinary performance level by working productively and positively with other primary stakeholders (Freeman, 1984; Evan and Freeman, 1988) such as customers, employees, communities and the environment (Starick, 1995) (Waddock and Graves, 1999: 3).

Visionary companies are referred to as those that are built to last (Collins and Porras 1995). The importance of considering stakeholders, in the form of employees, customers, communities and the environment, together with international and business-level diversification strategy as they effect economic performance addresses stakeholder and stockholder effect respectively. In considering issues of international and business-level strategy with stakeholder concerns, the importance of this 'new logic' of considering stakeholders and shareholders (Waddock and Graves, 1999) when investigating economic performance can be addressed.

The study is also important in that it further considers the breadth and mode dimensions of diversification strategy, and also tests Freeman's (1984) stakeholder explanations of economic performance. The current study analyses international diversification as a strategy which has an effect on economic performance (Daniels and Bracker, 1989; Hitt et al. 1997; Kim et al. 1989). The current study provided support for the importance of international diversification strategy and to test its relationship with economic performance in an Australian context. There was evidence from US studies that the relationship between international strategy and economic performance is characterised by an inverted U-shaped relationship and the current study seeks also to test to identify whether this holds true for large firms in Australia during the mid 1990s (Kim et al. 1989). Moreover, the study, unlike others studies before it, is unique in that it also tested the stakeholder impact on economic performance, together with the previously mentioned business-level and international diversification strategy, within a "business and society" framework.

Prior studies have provided a mixed set of results concerning the relationship between diversification (either business-level or international) and economic performance. Some studies favour economic performance as the dependent variable whilst others favour it as the independent variable. This is also the case for past

research concerning the relationship between social responsibility and economic performance. Perhaps international and business-level diversification strategy has important effects (positively or negatively) on the relationship between social responsibility reporting and economic performance.

The current study is important in that it tested business and society effects on economic performance to determine the nature and direction of those relationship from an Australian perspective during the mid 1990's. It is the first Australian study which tested Australian companies using Northern American theories. In considering these relationships the importance of the linearity assumption was considered relevant, particularly in the relationship between economic performance and international diversification. More recently evidence describes this relationship as non-linear (Hitt et al. 1997; Gomes and Ramaswamy, 1999). The challenge to the assumption of linearity has been sparsely challenged in prior literature and is an important issue for further investigation. In particular in the relationship between economic performance and stakeholder management, with the notable exception of Bowman and Haire (1975) almost all other studies have not investigated for non-linearity. In a more recent study Griffin and Mahon (1996) have divided social performance into high and low levels, reflecting a range of social performance important in their study. Another important feature of the current study was that it considered this non-linear characteristic in both cases of strategic and stakeholder management, in analysing the combined effect of international and business level diversification with stakeholder management on economic performance.

1.7 Scope of the Study

The study was limited to large firms, as identified by market capitalisation, for the current study's sample selection process. Evidence suggests that for empirical examination of the relationship between business-level diversification

strategy/international strategy and economic performance, that the largest firms exhibited levels of international diversification (Bettis and Hall, 1982; Hitt et al. 1997; Kim et al. 1989; Rumelt, 1974; Simmonds, 1990; Varadarajan and Ramanujam, 1987). Furthermore, in support for the use of large publicly listed companies, it has been suggested that a sample of large companies was more likely to demonstrate examples of social responsibility than an equivalent sample of medium or small companies (Gray, Kouhy, Lavers, 1995b). In terms of trends Gray et al. (1995b) suggested that to identify innovations in social responsibility and capture more social responsibility reporting a large company sample is recommended. Companies that were selected for the study were limited to large firms and also to those that issued corporate annual reports.

The variables selected to represent strategic and international diversification were limited to business-level diversification, country scope and multinationality. Stakeholder concern variables selected were limited to social responsibility disclosures that relate to employees, consumers, environmental and community found in corporate annual reports. There were other control variables that also can have an effect on economic performance. To cater for this the current study will consider only the following control variables common to other studies which are, firm size, leverage, industry classification and mergers & acquisitions (Gomes and Ramaswamy, 1999; Herremans, Akathaporn and McInnes, 1993; Hitt et al. 1997; Mc Guire et al. 1988; Roberts, 1992; Tallman and Li, 1996; Waddock and Graves, 1997).

1.8 Research Method

A sample group of the top 50 publicly listed Australian companies for each of the years 1993, 1994, and 1995 was collected, based on market capitalisation. In total

150 companies were selected. The sample was selected as the top 50 for each year because beyond that firms were not involved in international diversification and social responsibility reporting. Use was made of the CD-Rom developed by Connect-4 Company Annual report collection of top 300 publicly listed Australian companies to collect the relevant data.

Data on the following variables economic performance, multinationality, country scope, business-level diversification, social responsibility reporting, firm size, leverage, industry classification and mergers and acquisitions are collected, measured and, analysed.

Dependent Variable: Economic Performance

For the dependent variable, the current study will measure economic performance using accounting based measures and market based measures. The authors cited favourably referred to accounting measures as most desirable for quantifying economic performance; in strategy research (Bettis and Hall, 1982; Hoskisson, Hitt, Johnson and Moesel, 1993; Robins and Wiersema, 1995); in social responsibility research (Cochran and Wood, 1984; Herremans et al. 1993; McGuire et al. 1988 and Preston, 1978). Economic performance in the current study was measured and identified using five different measures: (1) Return on Assets (ROA); (2) Return on Equity (ROE); (3) Return on Sales (ROS); (4) Earnings Per Share (EPS); (5) Dividends Per Share (DPS).

Independent Variables

The independent variables will be considered from a "business and society" approach, namely business-level and international strategy (or business) together with social responsibility (or society) in determining economic performance. First the international diversification variables will be analysed and explained followed by the business-level diversification variables. The method of accessing and

measuring social responsibility disclosure as a representative of social responsibility of a firm will then follow.

Multinationality

Several measures of international diversification have been used in previous research (Geringer et al. 1989; Grant, Jammine and Thomas, 1988; Hitt et al. 1997; Tallman and Li, 1996), and the most frequently used one has been a unidimensional measure of international sales as a percentage of total sales.

Country scope

Country scope reflected the measure of breadth and scope of international operations as a determinant of economic performance. It is this aspect of the breadth of international diversification which is of interest as it provides a measure of the geographical scope of international operations. This measure then provided a measure of the ability of a company to “arbitrage operations across countries and leverage location-based advantages” (Tallman and Li, 1996: 185).

Both these measures of international diversification can be extracted from the corporate annual reports by identifying the segment reporting section in the “notes to the accounts”. According to Australian Accounting Standards Board (AASB) 1005 “Financial Reporting by Segments” activities regarding foreign geographical and local geographical segments need to be disclosed in accordance to the guidelines pertaining to this standard in corporate annual reports. The AASB 1005 was used in assisting identification and measurement of international diversification variables in particular the level of multinationality and country scope of the firms in the data set.

Measuring Business-level Diversification Strategy: Continuous versus Categorical approaches

There was evidence of two major methods of measuring diversification strategy; a *categorical* measure as developed by Rumelt (1974) and a *continuous product count* measure built on the Standard Industry Classification (SIC) system. There has been a long debate regarding which method better reflects diversification strategy. In a study which compared the two major methods it was found that they were more similar than previously suggested (Montgomery, 1982). The SIC system represented a continuous product count and was a US federal government initiative in order to classify numerous types of economic activity in the US economy (Montgomery, 1982). As this measure does not involve managerial intention, preference was then given to the categorical measure, in this study, which does involve managerial strategic intent regarding economic performance (Hoskisson et al. 1993).

Rumelt (1974) in his extensive examination of the relationship between diversification strategy and economic performance, developed a "carefully conceptualised categorical measure of diversification" (Montgomery, 1982: 299). There was further evidence that supported the reliability and validity of the Rumelt (1974) measure as an appropriate proxy for diversification strategy (Hoskisson et al. 1993) was. The current study utilised the subjective categorical measure of diversification strategy. This measurement first classified the organisation into the various business segments in order to determine business relatedness using a specialisation ratio to determine the level of business activity in a single business or group of businesses (Hoskisson et al. 1993; Palepu, 1985; Rumelt, 1974; Simmonds, 1990 and Wrigley, 1970). To facilitate the identification and measurement of firms activities in various industries use was made of the disclosure requirements of AASB 1005 "Financial Reporting by Segments" in the corporate annual report.

Stakeholder Management

The current study applied four social responsibility themes to identify and classify each company's stakeholders. The themes are: environment related, employee related, products related and community related stakeholders. This classification is consistent with that used in former studies using social responsibility reporting (AlNajjar, 1992; Gray, 1990; Guthrie and Parker, 1989; Roberts, 1992; Trotman and Bradley, 1981).

Content analysis was the method used to determine the amount of stakeholder involvement of each firm, the content of its corporate annual report was analysed to calculate the total number of sentences in the report occupied by social responsibility disclosure. Sentences for each page in the firm's annual report devoted to each social responsibility theme was identified and recorded. The total number of sentences devoted to all themes was then calculated. Identifying the number of sentences of social responsibility disclosures, using content analysis procedure captured the firm's level of stakeholder concerns.

Control Variables

The most commonly used control variables were firm size, leverage, merger and acquisitions and industry classification. Firm size was an independent variable in the economic-strategy model and was measured by identifying and recording the number of employees from corporate annual reports. The leverage of a firm was measured using the debt to asset ratio.

Companies from the sample selected were classified according the industry to which they best fit using the "Business Classification Index", of the "Jobson's Year Book of Australian Companies". In this way the sample set can be divided into industry

type to facilitate in determining whether particular relationships tested are industry specific.

The level of international and national merger and acquisition activity was measured which reflects the mode of business-level and international diversification. Changes in economic performance could also be attributed to the act of diversifying across country borders which may be achieved through merger and or acquisition during the period of the current study. Both of these variables have shown to effect economic performance (Hitt et al. 1997). These variables were measured using the total number of mergers and acquisitions, including both foreign and local ones (Hitt et al. 1997) as disclosed in the corporate annual reports..

Data Analysis

Data was collected and entered into an SPSS spread sheet and the data will be tested for degree of association and whether there exist a cause and effect relationship. Use will be made of linear regression analysis as this is the most appropriate statistical analysis technique to test the hypotheses developed in the current study. Use was made of the statistical values of R^2 , Adjusted Multiple R^2 , Chow statistics, F tests, and multicollinearity tests to analyse the explanatory power of the components of the models. Use was also be made of Kendall's tau to test degrees of association.

1.9 Assumptions, Limitations and Definitions

Assumptions

In this study firms which, were identified as diversified at the business-level, were assumed to gain internally from the benefits of economies of scale, scope and learning (Kogut, 1985). The benefits aforementioned allowed for easier application of the relationships among business segments and international geographic areas as

it allows for sharing of distinctive firm capabilities and core competencies across business segments. It was then assumed that firms with strong core competencies, that are as a result of development in their domestic country operations, can apply these competencies to international markets (Bartlett and Ghoshal, 1989; Hitt et al. 1997).

As an organisation progressively internationalises it was assumed that there was a cut-off point where transaction costs and demands of managerial information-processing increased to a point where the cost of international diversification will outweigh the benefits. This resulted in a curvilinear or non-linear relationship between economic performance and international diversification.

It was also assumed that when consideration was given to favourable customer perceptions about the quality and nature of a firms' products, together with its environmental considerations and its community related effects, these then become a basis for competition. These positive perceptions of the corporation by various external stakeholders, were assumed to improve economic performance. Moreover, it was assumed that attention to social responsibility domains acts as a medium for stakeholder management.

Social responsibility disclosures in corporate annual reports were assumed to reflect an adequate measure and representation of firm social responsibility. The disclosure also reflected the level of stakeholder involvement.

It was assumed that the firm is "characterised by relationships with many groups and individuals (stakeholders), each with (a) the power to affect the firm's performance and/or (b) a stake in the firm's performance (Freeman, 1984). In many cases, "both conditions apply" (Jones, 1995: 407).

Other assumptions were that international sales as a percentage of total sales was an adequate measure of multinationality. That accounting measures of economic performance are adequately represented by: return on assets (ROA), return on equity (ROE) and return on sales (ROS) and market measures of economic performance are adequately represented by, earnings per share (EPS) and dividends per share (DPS).

Limitations

The current study used two independent and common measures of international diversification which included: multinationality and country scope (Hitt et al. 1997; Tallman and Li, 1996). Multinationality referred to a unidimensional measure of international sales as a percentage of total sales, whilst country scope referred to the number of geographical regions that are being serviced for each firm. In testing the relationship between economic performance and international diversification account was not taken of the idiosyncratic nature of the countries which firms export goods or services, in terms of culture and area (Hitt et al. 1994). The current study did not take into consideration any benefits or costs that may result from these country specific idiosyncrasies when firms were actively involved in international diversification (Hitt et al. 1994; Porter, 1990)

There was evidence of two major methods of measuring business diversification strategy: a categoric measure as developed by Rumelt, 1974 and a continuous product count measure built on the Standard Industry Classification (SIC) system. Business level diversification was limited to a categoric measure.

Stakeholder concerns were limited to those identified in social responsibility disclosures in corporate annual reports, which are; employees, community, product safety (customers) and environment. There were other issues such as energy,

affirmative action programs and equal opportunity issues but these did not reconcile with most commonly used stakeholder concerns from recent literature (Bendheim et al. 1998; Preston and O'Bannon, 1997; Waddock and Graves, 1997).

Stakeholder concerns were limited in measurement to social responsibility disclosures in corporate annual reports. There were other techniques for measuring stakeholder concerns such as Data Envelopment Analysis (DEA), which measures best practice companies (Bendheim et al. 1998). There were also ratings measures which can be useful in measuring stakeholder concerns such as Kinder, Lydenberg, Domini (KLD) rates. Where KLD refers to a social research firm called Kinder, Lydenberg, Domini (Bendheim et al. 1998). In Australia there are no known research firms which produce or make available ratings of best practice companies. Techniques similar to DEA and KLD were not available, so the current study was limited to sentences of social responsibility prose as the unit of analysis, found in the corporate annual reports of firms in the sample.

Since it was difficult to establish benefits from the literature on the importance of the location of the social responsibility disclosure in corporate annual reports, the data collection of social responsibility reporting ignored the location of these reports. There were reports which disclose social responsibility of a firm, other than corporate annual reports, such as special purpose reports in newspapers and other similar media, but these are not within the scope of this study and were excluded.

Other factors that have been shown to effect economic performance, representing other models have included: human resources; organisational structure; innovation; other environmental factors (Hansen and Wernerfelt, 1989; Hitt et al. 1997; Rumelt, 1974). The current study did not consider these factors but was limited to strategic business, international business diversification and stakeholder concerns which did not include innovation, organisational structure or human behavioural factors.

Definitions

There has been a suggestion that good science begins with good definitions (Bygrave and Hofer, 1991). The following definitions were used in the current study.

Business-Level Diversification strategy represented the aggregate of multiple businesses within a single organisation. It aggregated the interrelationships among businesses within an organisation (Robins and Wiersema, 1995). This fits well with a firm's diversification strategy, into related businesses, which by definition suggests that the potential for synergy exists, that they are able to share a portion of their resources and services among businesses and spread the cost, making more efficient use of the available resources" (Hall, 1995: 30).

Diversification of a firm was defined as a firm comprising a collection of businesses that compete in different industries (Bettis and Hall, 1982).

Economic performance of a firm referred to both accounting- based and market-based measures of firm performance. Returns on equity, assets and sales, which are based on data from income statements and balance sheets are most frequently employed accounting measures of economic performance (Dubofsky and Varadarajan, 1987; Freeman and Jaggi, 1988). Whilst market-based measures as developed in the finance literature are based on the firm's shares which could include dividends per share and earnings per share.

International Diversification was defined as expansion across the borders of global regions and countries into different geographic locations or markets (Hitt et al. 1997: 767). A firm's level of international diversification was divided into two quite separate measures, which are multinationality and country scope.

Multinationality was defined as the percentage of foreign sales to total sales (Hitt et al. 1997: 767). Whilst country scope referred to the number of different international markets in which a firm operated.

Primary stakeholders were defined as those individuals and groups who were most directly affected by the activities of the firm, and who make some tangible contribution to its functioning, such as employees, customers and suppliers. Clarkson (1995) also defined a primary stakeholder group as “one without whose continuing participation the corporation cannot survive as a going concern” (Clarkson, 1995: 106). In this definition of primary stakeholders the following were included: shareholders; investors; employees; customers; suppliers.

Stakeholder referred to a group or individual who can affect or is affected by the achievements of the firm’s objectives (Freeman, 1984).

Stakeholder concerns represented manager’s interests of a corporation’s broad stakeholders which are employees, product safety (customers), community relations and environment. Social responsibility disclosures in corporate annual reports measured this concern (Roberts, 1982), and is voluntary in nature in an Australian context.

Stakeholder Saliency was a term which referred to managers degree of priority to competing stakeholders (Mitchell, Agle and Wood, 1997).

Secondary stakeholders were defined as those affected by corporate actions, but do not participate in the ordinary operations of the business. Examples would include consumers as a group, women, ethnic minorities, environmental groups, the press

and competitors (Armstrong, 1977; Carroll, 1989). Clarkson (1995) also provided a similar but more refined definition to secondary as groups that are identified as those who “influence or affect, or are influenced or affected by, the corporation, but they are not engaged in transactions with the corporation and are not essential for its survival” (Clarkson 1995: 107).

1.10 Summary and Organisation of Thesis

The thesis was organised in a format similar to that suggested by Perry (1994). This chapter introduced and justified the research, detailed its purpose and discussed the theoretical framework. The research method used is described. Assumptions, limitations, scope of the study and definitions were given and the research questions that guided the study were provided.

Chapter Two presents a socioeconomic model for investigating economic performance. The model developed in this chapter integrated the dimensions of strategic, international diversification (referred to as economic) with stakeholder concerns (referred to as socio) in investigating economic performance. The chapter then discusses the need for a business and society model, referred to in the chapter and thesis as a socioeconomic model, which does not separate the economic and social. Moreover evidence of a dual perspective is analysed for investigating economic performance. An integrated socioeconomic model of economic performance is developed.

Chapter Three presents a review of the research literature on the relationship between economic performance and diversification. Four major relationships will be analysed which are: economic performance and business-level diversification; economic performance and international diversification; economic performance and the interaction of business-level with international diversification; economic

performance and the interaction of country scope with multinationality on economic performance. It also describes the importance of resource based and transaction costs views of the firm, which when applied to the above relationships, helps to understand why there is an inverse U-shaped curve for some of the outcomes (Geringer et al. 1989; Gomes and Ramaswamy, 1999; Hitt et al. 1997).

Chapter Four presents a review of the research literature on the relationship between economic performance and stakeholder concerns. It presents an argument that managers undertake social responsibility programs and the disclosure of these in corporate annual reports reflects their relationship with and concern for stakeholders. A link is established between social responsibility disclosure and stakeholder concerns. Consideration is given to the sparse amount of studies which have subdivided stakeholder concerns/social responsibility into two subgroups of, low to moderate and high concern (Bowman and Haire, 1975; Griffin and Mahon, 1997). The chapter also describes the importance of this subgrouping when applied to the above relationships, as it helps to understand why there may be an inverse U-shaped curve between economic performance and stakeholder concerns (Bowman and Haire, 1975 and Mintzberg, 1983).

Chapter Five presents the theoretical framework. It develops an integrated socioeconomic (business and society) framework for investigating economic performance and examines three theories which include resource-based theory with transactions cost theory (Gomes and Ramaswamy, 1999; Hitt et al. 1997; Tallman and Li, 1996) and instrumental stakeholder theory (Donaldson and Preston, 1995; Freeman, 1999; Jones, 1995). This chapter then develops research questions and hypotheses.

Chapter Six explains the research method used, sample selection, data collection and measurement techniques. Chapter Seven presents patterns of results and their

relevance to the research questions and hypotheses posed in this study. Chapter Eight discusses the findings of Chapter Seven within the context of the research literature, presents the conclusions and makes recommendations for further study.

CHAPTER TWO

DEVELOPING A SOCIOECONOMIC MODEL FOR INVESTIGATING ECONOMIC PERFORMANCE

2.1 Introduction

Chapter One identified the purpose of this research study as investigating whether strategic and international business diversification with stakeholder concerns enhances economic performance. It identified the need to develop a socioeconomic framework, which incorporates transactions cost, resource-based and instrumental stakeholder theory, for investigating economic performance. The chapter also reported that the research would investigate the effects of selected independent variables on economic performance. It introduced the research method, outlined definitions, assumptions and scope, and established the importance and justification of the study. Part of Chapter One introduced the socioeconomic model to further develop a socioeconomic framework underlying the research.

This chapter builds upon that introduction by developing an integrative socioeconomic model capable of improving our understanding of the effect that the combined strategic management, international business and stakeholder concerns has on economic performance. Economic performance has, been analysed, amongst other ways, from a strategic management perspective (resource-based domestic and international diversification dimension), and from a social responsibility-stakeholder perspective (stakeholder dimension). What the model in the current chapter integrated was the dimensions of strategic management in the form of business and international diversification strategy which utilised resource-based perspective, with a stakeholder dimension in the form of social responsibility reporting which utilised stakeholder thinking. The model sets the scene for a business and society approach

for investigating economic performance. The chapter introduces and develops an integrative *business and society perspective* for determining the effects of these dimensions on economic performance. In analysing performance, recognition of stakeholders has been previously identified as noted in the following quotations:

if strong performance is to continue, strategic managers must focus increasingly on the concerns of all stakeholders (Waddock and Graves, 1997: 316).

The firm is characterised by relationships with many groups and individuals ('stakeholders'), each with (a) the power to affect the firm's performance and/or (b) a stake in the firm's performance (Freeman, 1984). Many cases both conditions apply. Stakeholders include, but are not limited to, shareholders (Jones, 1995: 407).

This chapter first considered the benefits of a multidisciplinary approach to organisational complexities by analysing prior studies which utilised a dual perspective approach applying an economic perspective initially then adds on a complementary perspective. Prior literature that considered a dual perspective, used positive accounting theory to reflect the shareholder maximising effect or economic effect. The use of economic reflects a strategic management approach for developing competitive advantage and above normal profits for the benefit of managers and stockholders.

The next section considered complementary perspective's which included either an organisational, stakeholder or social orientation. Strategic management studies that have used economic perspective as their benchmark and extended this to include other perspectives were analysed. This was then followed by a brief overview of various determinants of economic performance, providing a model reflecting multidisciplinary factors, which have an effect on economic performance.

These factors originate in various research disciplines including strategic management and stakeholder thinking. Next ‘stakeholder salience’ was considered which provided an explanation of “how managers prioritize stakeholder relationships” (Mitchell et al. 1997: 853). The significance of this section was to draw attention to the possibility that managers may pay particular attention to certain classes of stakeholders be they stockholder or other stakeholders. Finally a socioeconomic model was developed for investigating economic performance which integrated strategic management and stakeholder concerns.

2.2 Combining Strategic and Stakeholder Management

Consistent with Wicks (1996) and Wood (1996), it was suggested that research in the area of “business and society” not treat social and economic perspectives as separate issues as they are as important as each other, moves away from a dichotomous way of analysing stakeholders. The current study moves away from “The Separation Thesis” (Wicks, 1996; Woods, 1996) towards an integrated *socioeconomic* approach which does not consider economics as the firms primary responsibility.

The issue of “The Separation Thesis” (Freeman, 1994) was of importance in this section of work as “The Separation Thesis” argues that economics and society be analysed as two distinctly separate categories (Wicks, 1996). The counter argument suggests that there should be no distinction between economics and society (Wicks, 1996; Wood, 1996). The implication here was that the social objective was not somehow added on to the economic objective of the firm (Wood, 1996) but viewed as an integrated part (Mangos and Lewis, 1995). Stakeholder thinking has “allowed

us to think about multiple firm objectives with respect to various stakeholder relationships” (Wood, 1996: 121,) which marries stockholders and other stakeholders of the firm. This multiple objective approach included moral obligations:

the firm’s moral responsibility to human beings and to society is argued to have primacy over any specific economic responsibility to owners. Otherwise, if the firm’s prime objective is to maximise profit, then legal and ethical obligations are dispensable (Wood, 1996: 121).

There have been numerous tests of the positive relationship between strategic diversification management (at both the business-level and international level) and economic performance. Prior tests of the positive relationship between business level diversification and economic performance include: Christensen and Montgomery, (1981); Hall, (1995); Lubatkin and Rogers, (1989); Rumelt (1974, 1982). For a positive relationship between international diversification and economic performance prior tests included: Geringer et al. (1989); Hitt et al. (1997); Kim et al. (1989); Rugman, (1979); Tallman and Li, (1996). Furthermore, research on the link between economic performance and social responsibility reporting suggested that consideration be given to managing stakeholders in order that the firm achieves the objective of maximising economic performance (Aupperle, Carroll and Hatfield, 1985; Barton, Hill and Sundaram, 1989; Cochran and Wood, 1984; Cornell and Shapiro, 1987; Donaldson and Preston, 1995; Griffin and Mahon, 1997; Kotter and Heskett, 1992; McGuire, Sundgren and Schneeweis, 1988; O’Toole, 1985; Preston, Sapienza and Miller, 1991; Preston and Sapienza, 1990; Waddock and Graves, 1997).

It was argued: “that companies manage specific stakeholder relationships as their fundamental way of engaging their responsibilities” (Bendheim et al. 1998: 301). The specific stakeholder relationships have been categorised as “public stakeholders” by Clarkson (1995: 102) and include “employees, shareholders, suppliers, customers, governments, political groups, trade associations and the community” (Donaldson and Preston, 1995: 69). From an Australian context public stakeholders could include product related, employee related, community related and environment related categorisations (Mangos and Lewis, 1995).

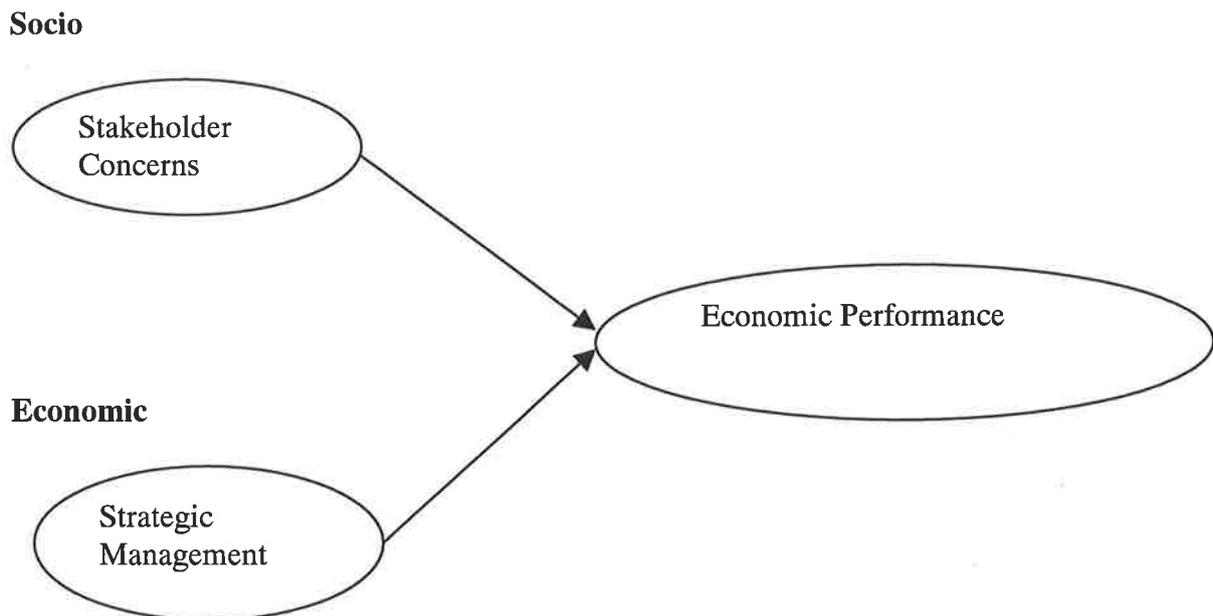
A Socioeconomic Model: Combining Strategic and Stakeholder Concerns

When combining these two sets of relationships analysed above a socioeconomic approach is developed. The two dimensions, strategic and stakeholder concerns have been empirically examined as two separate and distinct fields of research. This section of the chapter develops an integrated strategic management and stakeholder concerns model for investigating economic performance in an effort not to fall into the trap of “somehow added on” problem, as illustrated above by Wood (1996). This model was termed *socioeconomic*. More specifically this section of the chapter outlines an integrative model that combines the strategic management with stakeholder concerns. This strategy and stakeholder connection assists in achieving the purpose of the firm:

the idea that the tasks of management in a business are to manage the stakeholder relationships in a way that achieves the purpose of the business. Stakeholder management provides the tools by which we can connect strategy to social and ethical issues (Freeman and Gilbert, 1987: 397)

The model in Figure 2.1 (see also Berman, Wicks, Kotha and Jones, 1999: 493) illustrated a way of thinking about stakeholders and stockholders in a joint fashion (Collins and Porras, 1994; Waddock and Graves, 1999). The figure represented the first stage in developing a socioeconomic approach for investigating economic performance. This first stage model will be progressively developed in the current chapter.

Figure 2.1 Socioeconomic Model



As it was difficult (if not impossible) for managers to cater for all stakeholders a prioritisation of the various known stakeholders referred to as “stakeholder salience” (Mitchell et al. 1997: 854) was suggested. More specifically, stakeholder salience was referred to as “the degree to which managers give priority to competing stakeholder claims” (Mitchell et al. 1997: 854). Further consideration will be given to whether stakeholders represent primary or secondary stakeholders for the purpose of stakeholder salience.

2.3 Evidence Of Multidisciplinary Dual Perspective Studies: Combining Economic with Social or Organisational Factors

This section of the chapter analysed previous studies which have used an integrated approach using economic with organisational or social factors when examining a particular phenomenon. More specifically these studies integrated factors which use economic perspectives as their research stream together with a complementary perspective. It will be argued that researchers using a single perspective, such as the neo-classical perspective, present a partial view of the world that, although it is valid, needs to consider additional complexities of organisations (Hill and Jones, 1992; Hirsch, Michaels and Friedman, 1987). The problem of a single perspective promotes a fragmented approach which hides complexities. This problem of fragmentation was articulated eloquently in the following quotation:

research has generally proceeded under the direction of more restrictive formulations associated with a particular academic discipline or research tradition. Although beneficial, the resulting process...often encouraged a certain fragmentation that makes it difficult to discern the cumulative implications (Lenz, 1981: 131).

Eisenhardt (1989) was prepared to assert that there already existed an established body of agency-theoretic work in organisational studies and industrial sociology which thereby acknowledged the complexities of organisations. An integrated perspective constructs a cross-disciplinary bridge between, for instance, economic and social strategies on manager's decision behaviour (Etzioni, 1988). The phrase "cross-disciplinary bridge" was used by Etzioni, 1988, to mean a bridge to integrate the two disciplines of economics and of other social science disciplines into one

system. An analysis which eloquently combined economics with social argued that economics was dominated by a single paradigm, price theory and a single view of human nature (Hirsch et al. 1987). Hirsch et al. 1987 argued that integrating a number of perspectives yields a more realistic view of organisations.

There were a number of management studies which have used a dual perspective, which includes an economic perspective. These integrative approaches are reviewed in Table 2.1 below. From an analysis of the studies in Table 2.1, using a dual perspective, Singh and Harianto (1989), and Kosnik (1987) supported an economic perspective, but they also used a complementary perspective of hegemony and managerialism. Hegemony referred to ascendancy or domination of one power or of one class over another (Kosnik, 1987). In a similar vein, Eisenhardt (1988) and Conlon and Parks (1988) combined institutional and economic perspectives. The institutional emphasis on traditional complements the efficiency emphasis of positive accounting perspective and a better understanding of compensation. Another example included Anderson (1985) who coupled economic and transaction cost perspectives.

The conclusion of the studies referred in Table 2.1 was that managerial researchers have extended their empirical outlook beyond the economic perspective and extended this perspective by adding other complementary perspectives to gain a broader explanation of organisational phenomena.

This approach adds support to a socioeconomic perspective of economic performance allowing for a more inclusive strategic and stakeholder approach,

which is borne out particularly in the study of Hill and Jones (1992) where a stakeholder-positive accounting theory dual approach was operationalised.

Table 2.1
Summary of Studies using an Economic Perspective with a Companion Perspective

Author(s)	Economic Perspective	Companion Perspective	Results of Economic and Companion Perspective
Walking & Long (1984)	Positive Accounting Theory	Shareholder welfare & other controls	Support
Anderson (1985)	Positive Accounting Theory	Transaction cost	Mixed
Eisenhardt (1985)	Positive Accounting Theory	Organisational control	Support
Wolfson (1985)	Positive Accounting Theory	Tax effects	Support
Kosnik (1987)	Positive Accounting Theory	Hegemony	Mixed
Eisenhardt (1988)	Positive Accounting Theory	Institutional	Support
Barney (1988)	Positive Accounting Theory	Size & growth Controls	Support
Conlon & Parks (1988)	Positive Accounting Theory	Institutional	Support
Singh & Harianto (1989)	Positive Accounting Theory	Managerialist	Support
Hill and Jones (1992)	Positive Accounting Theory	Stakeholder	Support

Adopted from Eisenhardt (1988)

2.4 Multidisciplinary Determinants of Economic Performance: An Overview

In the strategic management literature there was a suggestion that there were two major streams of research on the determinants of economic performance, one based on an economic model and another on the organisational model (Hansen and Wernerfelt, 1989). The economic model emphasised the significance of economic factors in determining economic performance, whilst the organisational model considered behavioural and sociological factors which include social responsibility variables when investigating economic performance.

There was evidence which supported linkages to economic performance within each of the economic and organisational models, but there was scanty empirical research integrating the two, as well as little research in the evaluation of the relative effect of each on economic performance (Burke and Logsdon, 1996; Hansen and Wernerfelt, 1989). In the strategic management literature, prior research has analysed relationships between economic and strategy factors and economic performance (Grinyer, McKiernan and Yasai-Ardekani, 1988; Lenz, 1981; Miller, 1986; White 1986; White and Hammermesh, 1981). As Lenz (1981) noted:

what are the determinants of organisational performance? Answering this question required a review of empirical and case studies growing out of different research traditions and academic disciplines (Lenz, 1981: 141).

The operationalisation of a multidisciplinary framework has been recommended, in specific response to suggestions for future empirical research, by researchers such as: Bendheim et al. (1998); Burke and Logsdon (1996); Hansen and Wernerfelt (1989); Mangos and Lewis (1995).

2.4.1 Business-level Diversification Strategy Dimension and Economic Performance

The following analysis was organised around linkages used by two disciplinary approaches in investigating economic performance. First, the widely discussed strategy-economic performance linkage was examined, as an independent area, with a strategic management orientation, specifically encapsulating two major and separate areas of study, that of business level and international diversification effects on economic performance.

The relationship between diversification strategy and economic performance was not a new one as it has been tested in a number studies in the strategic management literature since the significant study of Chandler (1962). Numerous works testing this relationship have analysed diversification strategy from various dimensions of breadth and depth when explaining economic performance (Hall, 1995; Lubatkin, 1987; Robins and Wiersema, 1995; Rumelt, 1974 and 1984; Simmonds, 1990; Weston and Mansinghka, 1971). Some studies in this area have demonstrated an analytical relationship between diversification strategy and economic performance (Barton et al. 1989; Rumelt, 1974).

The issue of causality between diversification and economic performance has been researched in a loose unstructured way and there was a need to further address the causality issue in a more formal sense. This causality issue suggests that diversification leads to a higher economic performance (Grant, 1988; Hall, 1995). The most common rationale for diversification was referred to as simply, a way that a firm can become more profitable by been involved in additional businesses other

than their current one and this in turn has a positive impact on economic performance (Burgelman, 1983).

2.4.2 International Diversification Strategy Dimension and Economic Performance

Although prior research has evidenced a positive relationship between international diversification and economic performance, the outcomes from empirical studies have been mixed (for instance, Geringer et al. 1989; Rugman, 1979). A possible explanation for the mixed results was that the relationship was more complex than first thought (Gomes and Ramaswamy, 1999; Hitt et al. 1997). Hitt et al. (1997) suggested that many firms that are diversified on an international level are also diversified at the business-level. In particular what was suggested was that firms diversified at the business-level gain internally from the benefits of economies of scale, scope and learning (Kogut, 1985). The benefits allow for easier application of the relationships among business segments and international geographic areas by sharing of distinctive firm capabilities and core competencies across business segments (Porter, 1985). Thus, firms with business-level diversification enhanced their ability to exploit international markets (Fladmoe-Lindquist and Tallman, 1994). Firms with strong core competencies (which are in the main a result of development in their domestic country operations) applied these competencies to international markets (Bartlett and Ghoshal, 1989; Hitt et al. 1997). Furthermore, Porter (1990) argued that competitive advantages from successful domestic operations provide the confidence and willingness to apply the same competitiveness in international markets to further increase economic performance.

Past research which identified a positive relationship between international diversification and economic performance has been impressive but on closer examination the outcomes have been mixed (Ramaswamy, 1995; Tallman and Li, 1996). For instance, Grant (1987); Daniels and Braker (1989); Haar (1989); Kim et al. (1993); Vernon (1971) identified a positive relationship between international diversification and economic performance. On the other hand, others did not identify a linear relationship between international diversification and economic performance (Geringer et al. 1989, Kumar, 1984; Morck and Yeung, 1991). In particular, Geringer et al. (1989) found that there was a non-linear inverted U-shaped relationship between international diversification and economic performance. The explanation for this curvilinear outcome was that moderate levels of international diversification provided positive benefits to a firm via economic performance. Beyond that level, however, the firm experienced significant costs associated with further international diversification. Evidence suggested that as international geographic dispersion escalates transaction costs and managerial information processing were increased so diminishing returns commence which acted progressively with a negative impact on economic performance (Hitt et al. 1997; Jones and Hill, 1988).

Geographic dispersion increased costs which include coordination, distribution and management costs. Costs derived from different government regulations, trade laws and currency value fluctuations across countries, access to raw materials and employee skills requiring considerable coordination. Furthermore, these transactions costs and variations experienced across geographic regions increase managerial information-processing requirements. The types of costs identified

include logistical costs, trade barrier and cultural diversity which make management of internationally diversified firms highly complex (Hitt et al. 1997).

As an organisation progressively internationalises a point will be reached where the cost of international diversification will outweigh the benefits which reflects the negative effects of transaction costs and increasing demands of managerial information-processing demands. More specifically, “the internal governance costs exceed the benefits provided by economies achieved and thus the range of resources used and scope of governance exceeds managerial capabilities” (Hitt et al. 1997: 773).

The recent evidence presented suggested a non-linear inverted U-shaped relationship between international diversification and economic performance. The conflicting results evidence from prior research of a positive relationship between international diversification and economic performance could be explained using the argument that once a firm goes beyond a moderate level of international diversification then costs begin to exceed benefits and economic performance suffers.

2.4.3 Social Responsibility/Stakeholder Dimension and Economic Performance

There have been numerous studies which have tested and found a positive relationship between social responsibility reporting and economic performance (Anderson and Frankle, 1980; Belkaoui, 1976; Bowan, 1978; Chen and Metcalf, 1980; Cochran and Wood, 1984; Freedman and Jaggi, 1988; Herremans, Akathaporn and McInnes, 1993; Ingram, 1978; McGuire et al. 1988; Preston, 1978; Spicer, 1978). The relationship between social responsibility reporting and

economic performance remains important for management behaviour as to the degree of response to pressure to be socially responsible (Cochran and Wood, 1984). Since a positive relationship existed between these two variables, then managers may be prompted to place more emphasis on the level of socially responsible activity.

The way in which managers can report their social responsibility was through disclosures in corporate annual reports. The form of these social disclosures were many and varied and include the following categories: “environment, affirmative action programs, equal opportunity policies, community involvement, product safety, policies towards South Africa and energy concerns” (Roberts, 1992: 595). A popular way of measuring this type of disclosure is through content analysis where these categories are identified and areas of prose in the corporate annual report are measured by, for example page size. There are other measures which use reputational indexes and ratings to identify the level of social responsibility.

Studies which have tested the relationship between social responsibility reporting and economic performance have been located in both the accounting literature and strategic management literature indicative of the multidisciplinary nature of this area. Moreover Ullmann (1985), in reviewing prior studies, identified some of the problems with analysing the relationship between social responsibility reporting and economic performance and suggested that use should be made of a stakeholder orientation where the missing element strategy be considered. The way in which Ullmann (1985) included this element was to develop a contingency framework, in which stakeholder concept played a prominent role (Pfefer and Salancik, 1978; Thompson, 1967). The rationale for social responsibility disclosures was identified

as managers strategy to undertake social responsible programs to manage stakeholder relationships. The work of Ullmann (1985), by including strategy as a missing element, has been a useful addition when analysing the relationship between social responsibility reporting and economic performance. This stakeholder orientation then broadens the impact beyond stockholders to stakeholders which include, individuals or groups who can have an impact on or be impacted upon.

Social responsibility was linked to stakeholder concerns, as evidence suggests that social responsibility be considered as a medium for managing stakeholders (Adler and Milne, 1997). The stakeholder approach was not new in analysing the link between social responsibility reporting and economic performance (Adler and Milne, 1997; Bendheim et al. 1998; Roberts, 1992).

2.5 A Socioeconomic Model of Economic Performance: An Integrative Model

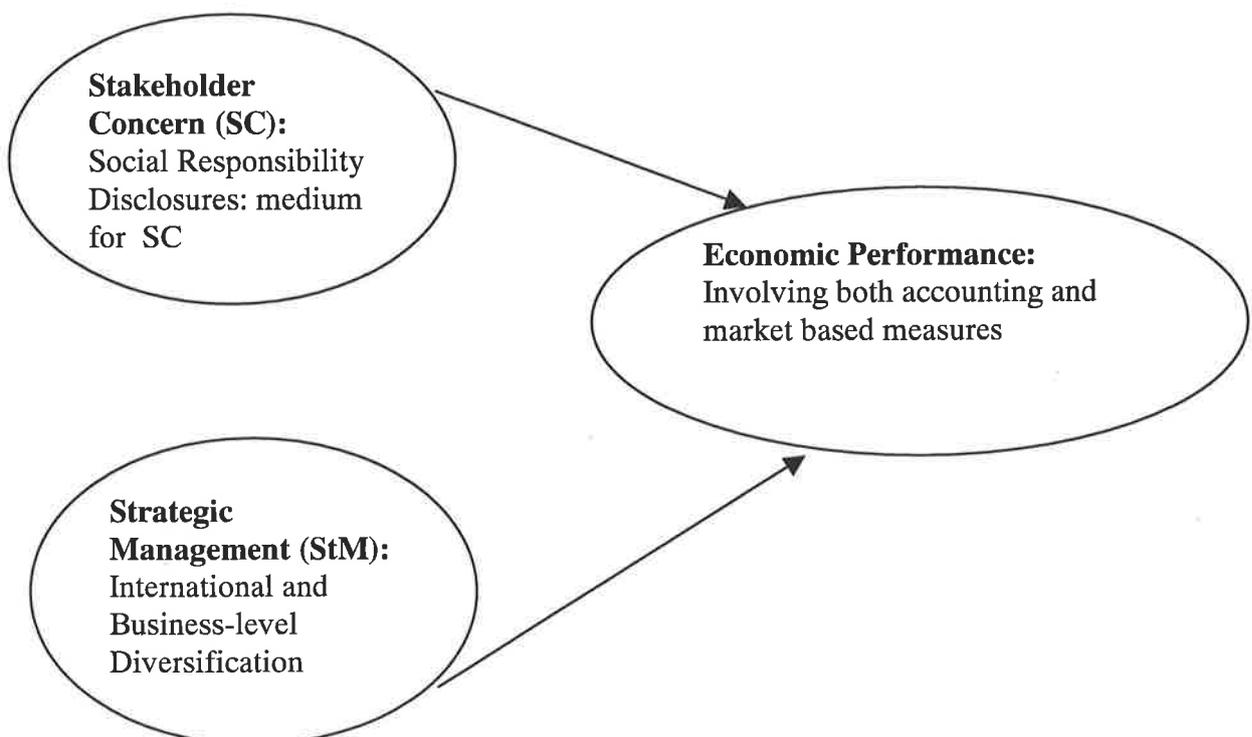
There has been a wide variety of different models of economic performance developed (Hansen and Wernerfelt, 1989). It has been suggested that "firm performance is an aggregate phenomena [sic]" (Hansen and Wernerfelt, 1989: 401). The multidimensional characteristic of economic performance was used and consideration was given to the effect of diversification as a strategic economic factor, and social responsibility as a social factor which both have evidenced an effect on economic performance and referring to it as a socioeconomic model.

This linkage between organisational climate and economic performance has been noted in previous managerial studies such as: Likert, (1961); Simmons and Mares (1983). Figure 2.2 below illustrated a socioeconomic model for investigating

economic performance which has been based on a “traditional climate model of firm performance” (Hansen and Wernerfelt 1989: 402).

The model in Figure 2.2, added specific components to stakeholder concern and strategic management in the previous Figure 2.1. There are competing models which include other factors when investigating economic performance such as: people, organisational structure, innovation, and further environmental factors (Hansen and Wernerfelt, 1989; Hitt et al. 1997; Rumelt, 1974). Given the scope of the current study consideration was given to the impact of the two factors as illustrated in the Figure 2.2 (Berman et al. 1999). Use was made of these two factors were the subject of common investigation in the fields of strategic management and stakeholder/social responsibility literature but only as separate issues.

Figure 2.2 A Socioeconomic Model for Investigating Economic Performance



Prior studies have applied two common measures of economic performance as illustrated in Figure 2.2, namely accounting-based and market-based measures, as it is a multidimensional construct (Dess and Robinson, 1984 and Keats, 1988). Using these two measures provided an opportunity to evaluate the multidimensional nature of the construct (often termed construct validity, Keats, 1989).

Integrating Social Responsibility/Stakeholder Concerns and Strategic Management

The idea of a cumulative approach using social responsibility/stakeholder concerns and strategic management was not new. Evidence suggested that a stakeholder model of strategic management was needed which also accounted for “social demands as strategic issues” Burke and Logsdon (1996: 496) (Carroll, Hoy and Hall, 1987; Freeman, 1984). The idea of jointly serving strategic business interests and the societal interests of stakeholders has been suggested by Burke and Logsdon (1996). What has been sparsely considered in this type of integrated framework is the effect of jointly serving these perspectives on economic performance and empirically testing this effect (Berman et al. 1999). What benefits, in terms of economic performance, accrue to firms when investing in both social responsibility practices (for stakeholder concern purposes) and strategic diversification practices (for strategic management purposes)?

In sum, the above section has identified a fragmented approach in prior analysis of investigating links between economic performance and three separate perspectives, namely, business level, international diversification and social responsibility. This fragmented approach has provided mixed results regarding the relationship to economic performance.

The Relevance of “The Separation Thesis” when Integrating Social Responsibility and Strategic Management

The issue of “The Separation Thesis” was initiated by Freeman in 1993, at the Society of Business Ethics annual meeting (Wicks, 1996). What this thesis embraced was the distinction between ethics and business. Conceptually this thesis divided the realms of ethics and economics into distinct components. The argument for “The Separation Thesis” has strong implications regarding any attempts to connect economic and a broader set of corporate social responsibilities (or other stakeholders). Clearly “The Separation Thesis” does not permit the meeting of the two perspectives in any meaningful way. What the thesis does propose is that what business is really about is profit maximisation and any attempts to include societal issues are naive or unintelligible.

When a firm seeks to diversify both at the business level and then at the international level it seeks to maximise its profits. This economic end in itself, whilst admirable and necessary, was not the only purpose of the business, as it may also pay to be socially responsible. In being socially responsible reference was made to the firm partaking in stakeholder concerns which involves activity beyond stockholder concerns which include customers, employees, environmental and community groups. Even though “evidence suggests that the separation thesis is a commonly held view” it was not supported by all (Wicks, 1996: 91).

In considering stakeholder and economic perspectives both as starting points positions the current research outside the realm of “The Separation Thesis”. In only studying the relationship between economic performance and stakeholder concerns provided evidence of the split between economics and society (Wicks, 1996).

However, when jointly considering strategic and stakeholder concern issues both as starting points then one would, by necessity, consider them as both important and not consider one as primary and the other as secondary. Then it can be argued that, when equal consideration is given to the firm's duties to the economic motives of the firm and of its commitments to other stakeholders, then the restrictions of the separation thesis are overcome.

Prior studies have considered the two issues of strategic management and stakeholder concerns separately, so when empirically testing the two issues one is drawn to the methods and ways in which these have been done in the past. This provides workable and proven methods of analysing these issues whilst providing a refined, and fuller more integrated approach to the problems. This more inclusive approach does not necessarily fall back into the approach described in "The Separation Thesis" but the current study combined the two issues with no preference given to one against the other.

This no preference approach of the firm has been noted: "...that obligations to other stakeholders, built as they are on 'community' membership, are as valid as the economic ones to stockholders" : (Waddock and Graves, 1997: 252). Furthermore, the current study also considered the importance management places on stakeholders to determine which stakeholders do matter whether they are employees, customers, environmental groups or the community. The importance was then placed on "stakeholder salience", to identify which stakeholders were relevant to the firm (Mitchell et al. 1997: 854). This again assists in refining the method of integrating the two issues and developing a model for analysis.

Importance of Stakeholder Salience to an Integrative Socioeconomic Model of Economic Performance

When managers concerns for stakeholders are considered, what can be considered are who and what stakeholders do matter (Agle, Mitchell and Sonnenfeld, 1999; Mitchell et al. 1997). A suggested way of attempting to identify stakeholders could be based on “their possession of power, legitimacy, and urgency in the relationship to the firm” (Mitchell et al. 1997: 871). However it was manager’s perception of stakeholders which seems to matter more to the manager’s approach to stakeholder salience. For instance there are numerous ways which managers’ approach the issue of environmental issues, also to with social regulation. What was suggested was that managers’ characteristics play an important role in the stakeholder salience issues.

The issue of stakeholder salience assists the current study in dealing with multiple stakeholders’ interests. Use was made of multiple stakeholder’s identification of particular stakeholder needs by dividing stakeholders into stockholders, customers, employees, community and environmental concerns. Emphasis was placed on identifying which stakeholders do really count when investigating economic performance using a socioeconomic model.

2.6 Summary

An integrative socioeconomic model was developed in this chapter which encapsulated, business level strategy perspective, international diversification perspective and stakeholder/social responsibility perspective. This chapter has developed a socioeconomic model capable of improving our approach to investigating economic performance. Since economic performance can be analysed from three key dimensions that of a business and international level (economic factors), with stakeholder level (social responsibility) then by cumulating these

perspectives one arrives at a socioeconomic perspective. What this socioeconomic perspective cumulated was the dimension of strategic management in the form of business and international level diversification strategy, and a stakeholder societal dimension in the form of social responsibility reporting (utilising stakeholder thinking). Consequently, the socioeconomic model takes account of the combined strategic management and stakeholder concern when investigating economic performance.

The socioeconomic model developed in Figure 2.2 was developed to help overcome the restrictions of the division between the economic and social dichotomy as articulated in “The Separation Thesis”. The inclusion of a stakeholder view of the firm provided a way of overcoming this division between social and economic. The integrated model proposed in this chapter allowed for a blending of the social and the economic by including stockholders and stakeholder considerations jointly. This model will be further developed from a theoretical perspective in Chapter Five and empirical tested in Chapter Seven. The following two chapters in Chapters Three and Four respectively, are an analysis of past literature covering individually the relationship between, in the first instance, the effect of business level diversification and/ international diversification strategy dimension on economic performance and in the second instance, the effect of stakeholder issues (using social responsibility disclosures) on economic performance.

CHAPTER THREE

ECONOMIC PERFORMANCE AND DIVERSIFICATION STRATEGY

3.1 Introduction

Chapter One identified the purpose of this research study as investigating whether strategic and international business diversification with stakeholder concerns enhances economic performance. It identified the need to develop a socioeconomic framework, which incorporates transactions cost, resource-based and instrumental stakeholder theory, for investigating economic performance. Chapter Two developed a socioeconomic model for examining the effect that strategic management, international business diversification and stakeholder concerns has on economic performance.

This chapter begins with pursuing the meaning and significance of strategy as it relates to diversification strategy and finds that the term is quite elusive. This was then followed by an analysis of diversification strategy and the identification of various business-level diversification strategies. The next section analyses the relationship between business-level diversification strategy and economic performance, identifying the mixed results from research studies. Following on from this relationship the issue of causality is reviewed which leads to the view that related diversity causes higher economic performance. The following section then considers the relationship between international diversification and economic performance. This is then followed by an analysis of the interaction of international diversification with business-level diversification on economic performance. Then an examination of the interaction of multinationality with country scope on economic performance is considered. The next section analyses past research that has evidenced a curvilinear relationship between international diversification and economic performance. The importance of transaction

costs effects on this relationship is then examined providing evidence of a curvilinear relationship between international diversification and economic performance from a sparse number of past research studies.

This chapter therefore presents empirical findings on diversification strategy, referring to strategic business-level and international diversification literature, which examined the effect of business level diversification and international business diversification strategies on economic performance. In developing the research review, multiple information channels were used. A search was performed on computerised *ABI-inform and Lexis Nexus*. A manual search of journals and periodicals concerned with strategic and international business diversification was undertaken such as: *Academy of Management Journal*; *Academy of Management Review*; *Advances in Strategic Management*; *Australian Journal of Management*; *California Management Review*; *Financial Management*; *International Marketing Review*; *Journal of Business*; *Journal of Business Research*; *Journal of International Business Studies*; *Journal of International Management*; *Journal of Management*; *Journal of Management Studies*; *Management International Review*; *Management Science*; *Strategic Management Journal*; *Organization Science*; *Rand Journal of Economics*; *Sloan Management Review*, at the University of Adelaide, the Flinders University of South Australia and, the University of New South Wales.

The various relationships investigated in this chapter are between business-level diversification strategy and economic performance and between international diversification strategy and economic performance. Recently research has examined the interactive effects of international diversification with business-level diversification on economic performance that provides a further relationship for consideration (Hitt et al. 1997 and Tallman and Li, 1996). One particular study identified two independent

measures of international diversification which included multinationality and country scope and tested the interaction of these on economic performance (Tallman and Li, 1996). This chapter reviewed the past research, which has considered the relationships mentioned above, in particular, the more recent interactive effects of international and business level diversification (Hitt et al. 1997). The interactive effects of multinationality and country scope on economic performance were also analysed (Tallman and Li, 1996). The non-linear nature of the relationship between economic performance and international diversification was also analysed and the importance of this when studying the interactive effects of diversification on economic performance.

This chapter analysed mainly American and British studies which have previously tested the relationship between international and business-level diversification on economic performance as Australian research on this relationship is scanty (if any) (Lewis and Minchev, 1998).

3.2 Strategy: An Elusive Concept

International and business-level diversification strategies were considered in investigating economic performance in Chapter Two in this section of the chapter a closer examination is given to strategy and how this is then linked to diversification in the next section. Various frameworks have been proposed to analyse strategy and its effectiveness (for instance, Dent, 1990; Hofer and Schendel, 1978; Porter, 1980, 1985; Ullmann, 1985). Strategy is an elusive concept and has been used in numerous different disciplinary studies (Pennings, 1985). It has been observed that the term strategy has been used in disciplines other than management, which include: "economics, social psychology, anthropology, sociology and political science" (Dent, 1990: 4). For earlier

uses in the management literature, strategy was considered in the main in the management literature as:

the determination of the basic long-term goals and objectives of an enterprise and the adoption of courses of action and the allocation of resources necessary for carrying out these goals" (Chandler, 1962:13).

Chandler's (1962) description of strategy was somewhat broad and included long-term goals and objectives and ways of accomplishing these. A narrower concept limits the definition to means oriented (Hofer and Schendel, 1978). A narrower concept considers strategy as "the fundamental pattern of present and planned resource deployments and environmental interactions that indicates how the organisation will achieve its objectives" (Hofer and Schendel, 1978: 25). Dent (1990) also observed a further limitation, from work by Porter (1980 and 1985), on the notion of strategy which was where "competitive strategy is the search for a favourable competitive position in an industry...(It) aims to establish a profitable and sustainable position against the forces that determine industry competition" (Porter, 1985:1). As Dent (1990) suggested the success of this depends on " the creation of unique competitive advantages" (Dent, 1990: 5) and further support for this came from Porter (1985) "strategy is the route to competitive advantage" (Porter, 1985: 25).

The definitions ranged from general to specific, but notwithstanding this range of possibilities a commonality in meaning emerges (Dent, 1990). Mainstream views of strategy often referred to a declaration of intent, or alternatively a procedure, which can be prescribed in written form in the way of a mission statement, set of objectives and a method of implementation (Dent, 1990). An analysis of the strengths and weaknesses of an organisation assisted in evaluating its internal environment and further assists in capitalising on its opportunities and reducing the likelihood of threats. In such a way an

organisation determined what it ought to be pursuing. This normative approach, stemming from an analysis of strengths, weaknesses, opportunities and threats has been and still is included in literature on strategy (e.g., Hofer & Schendel, 1978; Porter, 1980, 1985). There were other views about what strategy is and means, for instance Mintzberg (1978: 935) suggested strategy as "a pattern in a stream of decisions". Researchers from various disciplinary backgrounds have different interests in strategy (Dent, 1990).

Chandler (1962) provided a springboard from which a stream of research studies analysed linkages between diversification strategy and structure. Wrigley (1970), and later Rumelt (1974) who refined and extended Chandler's (1962) study, analysing *business diversification strategy* and economic performance. Rumelt (1982, 1974) analysed diversification strategy by first considering *product diversification* strategic patterns involving single, dominant, related and then unrelated products. Rumelt (1982, 1974) improved his analysis by then considering *business diversification* strategy as an improved measure of diversification strategy. In sum, Dent (1990) conveniently summarised various themes in strategic research into three major categories, namely; *strategy and structure, business policy and economics* and finally *strategic decision making processes*. There were differences in the approaches to strategy within these themes in the form of interpretation and approach. Briefly, some viewed strategy as "*ex ante*-as an intended process" whilst others referred to strategy as "*ex post*-via a flow of actions and decisions" (Dent, 1990: 9)

Reference was made, in particular, to the research of Rumelt (1982, 1974) where strategy was identified by considering business diversification patterns within an organisation and furthermore, to Hitt et al. (1997) where strategy was identified by considering the level of international diversification. A link is established between

strategy and diversification. The current study used diversification strategy from an international level (Hitt et al. 1997) and a business related level (Rumelt, 1974) when investigating economic performance. The next section investigates the development of diversification as a strategy.

3.3 Diversification as a Strategy

This section of the chapter in considering diversification as a strategy draws heavily on work of Rumelt (1982 and 1974) and further by the research of: Barton et al. (1989); Hall (1995); Robins and Wiersema (1995). In particular Rumelt (1974), in considering the interrelationship of diversification strategy and economic performance in large American industrial corporations, identified diversification as a strategy.

From a close examination of the literature it was apparent that there was lack of a generally accepted definition or measure of diversification (Dent, 1990; Dermer, 1990; Rumelt, 1974). This shortfall in itself identified a weakness in outcomes of prior research, however it also provides an opportunity for further research to develop the concept of diversification as a strategy. Bettis and Hall (1982) suggested that a definition of diversification includes a "collections of businesses" which "compete in different industries" (Bettis and Hall, 1982: 225).

Dermer (1990) suggested that the majority of research in the area of strategy has had a "managerial bias and has sought to offer prescriptions to make it more 'useful' to management" (Dermer, 1990: 69). One way of viewing strategy was from a teleological view, where strategy is considered to be within the control of management and prescriptive in nature (Dermer, 1990). This view proposes that, through utilising strategy, managers can effectively control the organisation and its activities. The

teleological view was suggestive of controlling a majority of issues, in the organisation, in the main in the hands of management (Dermer, 1990; Georgiou, 1973). In this sense management was viewed as:

a gatekeeper: it recognises the stimuli for change, establish priorities, initiates the search for solution, builds acceptance and then implements and administers its plans. Woven into this fabric of assumptions is the belief that it is management's rationality that guides the choice of issues for the agenda and imbues them with worth, and that managerial endorsement is the prime component of support. (Dermer, 1990: 68).

The method initially used by Rumelt (1974) to categorise strategy of a firm was to determine its level of "entry into a new product market activity" (Rumelt, 1974: 10). Diversification in this sense referred to a firm entering into new business activities which may call upon the firm to develop new core competencies or effectively use its existing core competencies (Rumelt, 1974). Rumelt (1974) based his *strategy categories* on Wrigley's survey of the 1967 *Fortune* 500 which stratified the random sample of 100 firms into four categories:

firms that were not diversified (Single Product Firms); firms primarily committed to a single business but that had diversified to a small degree (Dominant product); firms that expanded into new areas bearing either a technological or market relation to current activities (Related product); and firms that diversified without regard to such relationships (Unrelated products). (Rumelt, 1974: 3)

Rumelt (1974, 1977) in considering the relationship between diversification strategy and economic performance used a random sample of 246 firms taken from the *Fortune* 500 for the period 1949 to 1974 but limited to three points in time, 1949, 1959 and 1969. Annual observations were not used but rather data points using decade averages were identified. Major diversification strategies identified and categorised by Rumelt (1977) include the following business categorisations as opposed to his previous product categorisations: *single business, dominant business, related business* and

unrelated business. These business categorisations were an improvement to Rumelt's (1974) original product categorisation (Rumelt, 1977). In this way Rumelt was able to investigate a range of business diversification options which include: "firms that remained essentially undiversified to firms that diversified significantly into unrelated areas" (Bettis and Hall, 1982: 255). Rumelt (1974) was able to show that firms were rapidly becoming more diversified, and he was able to relate diversification strategy to performance using his categorical measure of diversification.

Rumelt (1974) recognised problems with using the narrow concept of a "product" in categorising diversification and so he developed a revised set of category titles. This revised set, as mentioned above, involved dividing the firm into discrete businesses which include: "Single Business, Dominant Business, Related Business and Unrelated Business" (Rumelt, 1974: 12). In this way the firm could then be analysed as an activity made up of a number of different businesses to assist in the process of categorising diversification strategy (Rumelt, 1974). Discrete businesses were defined as those that could be: "managed independently of the firm's other activities" (Rumelt, 1974:12). There were problems with identifying discrete businesses within the firm as interdependency was evident in firms activities. The methods used to identify discrete businesses involved:

evaluating the degree to which its basic nature and scope could be altered without meeting constraints imposed by the firm's other businesses, and without materially affecting the operation and strategic direction of other activities (Rumelt, 1974: 12).

Rumelt's categorical measure of diversification applying the discrete businesses concept was not only a better measure of diversification strategy than product categorisation, but also it was a "response to the weaknesses inherent in the Standard Industrial

Classification (SIC) system" (Montgomery, 1982: 300). The SIC system classified a firm's diversification activity using a numerical system developed by the US Federal Government for "classifying all types of economic activity within the US economy" (Montgomery, 1982: 299). The SIC system used a continuous product count measure and do not refer to the strategic intent of management (Hoskisson et al. 1993). Rumelt's classification of discreet business diversification is illustrated using Figure 3.1. It was suggested that business-level diversification strategy might best be identified using a categorical measure, such as that proposed by Rumelt (1974), which used strategic intent of management (Hoskisson et al. 1993).

Figure 3.1 Rumelts' Classification System for Diversification Strategy^{ab}

Specialisation Ratio^c

	<i>Single Business</i>	
95-100%	Firms that are basically committed to a discreet business area	single business single vertical
	<i>Dominant Business</i>	
70-94%	Firms that have diversified to some extent but still obtain the preponderance of their revenues from a discrete business area	dominant vertical dominant constrain dominant linked dominant unrelated
	<i>Related Business</i>	
> 70%	Firms that are diversified and in which more than 70% of the diversification has been accomplished by relating new activities to old	related constrained related linked
	<i>Unrelated Business</i>	
< 70%	Firms that have diversified and in which less than 70% of the diversification is related to the firm's original skills or strengths	multibusiness unrelated portfolio

Source:

^aRumelt (1974: 11-32) and (1978: 4)

^bMontgomery (1982: 301)

^cPercentage of firm's total sales in a discrete business category

The SIC relied on "establishment classifications", where each of these establishments (e.g., plants) was arranged with regard to the firms' principal activity (Montgomery, 1982). In favour of Rumelts' categorical measure of diversification there appeared opposition to the SIC approach where product classification approach was the predominant technique of classification (Montgomery (1982)).

3.4 Economic Performance and Business-level Diversification Strategy

Research examining the relationship between business-level diversification and economic performance was not new, as it has been a significant topic of strategic management since the work of Chandler (1962). Numerous studies have tested this relationship considering diversification using dimensions of breadth (related and unrelated) and mode (internal/external), and have evaluated each dimension independently in an attempt to explain economic performance variations. Studies which have considered diversification mode/breadth and economic performance include: Barton et al. (1989); Bettis (1981); Bettis and Hall (1982); Capon, Hulbert, Farley and Martin (1988); Christensen and Montgomery (1981); Lubatkin and Rogers (1989); Montgomery (1979); Palepu (1985); Rumelt (1974); Simmonds (1990). These studies suggested that related business-level diversification was far better than unrelated business-level diversification in explaining higher economic performance.

Diversification was considered as a method of growth and was said to effect economic performance and diversification was divided into breadth and mode (Simmonds 1990). Figure 3.2 illustrated the relationship between combined dimensions of breadth and mode dimensions of diversification and economic performance from a study by Simmonds (1990).

Figure 3.2 Diversification Breadth and Mode

<u>Dimensions</u>		<u>Performance</u>
Diversification Breadth	Combined Dimensions	Financial
Performance		
Related	Related-Internal	ROE
Unrelated	Related-External	ROIC
Diversification Mode		
Internal	Unrelated-Internal	ROA
External	Unrelated-External	CSG

Source:

Simmonds (1990: 401)

Where ROE, return on equity; ROIC, return on invested capital; ROA, return in assets; CSG, compound sales growth (Simmonds, 1990)

Results from empirical work carried out by Simmonds (1990) suggested further evidence that related firms performed better than unrelated firms. In fact when the two dimensions illustrated above are combined it was found that the two related dimensions were favoured over the two unrelated dimensions Simmonds (1990). This finding was previously supported by Rumelt (1974) who favoured related categories of diversification as opposed to unrelated in explaining a firm's higher economic performance.

Results of studies of a relationship between economic performance and business-level strategy have provided mixed results as reflected by a summary of such studies provided in Table 3.1. From Table 3.1, it can be concluded that corporate diversification literature has failed to reach a unanimous decision regarding the

relationship between diversification and economic performance. There was more evidence of a positive relationship but this does depend on the type of diversification measure used. There were mixed results regarding the relationship between business-level diversification strategy and economic performance, for instance some found a positive whilst some a lack of relationship. Use was made of the business-level strategy and economic performance relationship developed by Rumelt (1974, 1982). According to Rumelt (1974) strategy was determined by identifying and measuring *business-level diversification*.

The mixed results of the relationship between business-level diversification strategy and economic performance of past research was attributed to a lack of focus on causality, as prior researchers have, in the main, limited their analysis to economic performance differences between diversified firms (Grant, 1988; Hall, 1995). There was evidence that suggested that firms with related diversification strategy will lead to superior levels of economic performance whilst on the other hand unrelated diversification strategy is said to lead to inferior economic performance (Rumelt, 1974; 1982). A significant issue raised recently is a “chicken and egg” proposition, i.e. “Does diversification determine performance or does performance determine diversification” (Hall, 1995: 25).

The strength of Rumelt's (1974) arguments that the optimal strategies for firms is to engage in related diversification strategies, is supported from an analysis of the relationship between these strategies and economic performance. It was found that a positive association existed between these strategies and economic performance (Rumelt, 1974). In support of this issue further evidence suggested that related diversification are the most beneficial as they support the ideas of core competencies and competitive advantage (Tallman and Li, 1996).

**Table 3.1: Empirical Studies Testing the Relationship between Business-level
Diversification Strategy and Economic Performance**

Author	Findings from Empirical Tests	Diversification Measure	Sample selection
Lack of relationship			
Amit and Livnat (1988)	No Performance differences	SIC based	Cross sectional industries
Chang and Thomas (1989)	No Performance differences	Rumelt: Categorical	Cross sectional industries
Grant , Jammine and Thomas (1988)	Inverted U-shaped relationship	Rumelt: Categorical	Cross sectional industries
Hill, Hitt and Hoskisson (1992)	No Performance Differences	SIC based	Cross sectional industries
Montgomery and Wernerfelt (1988)	No Performance differences	SIC Based	Cross sectional industries
Positive relationship			
Bettis (1981)	Positive relationship, related diversification	Rumelt: Categorical	Cross sectional industries
Bettis and Hall (1982)	Positive relationship, related diversification	Rumelt: Categorical	Cross sectional industries
Hall (1995)	Positive relationship, related diversification	SIC- entropy measure	Cross sectional firms
Lubatkin and Rogers (1989)	Positive relationship	Rumelt: Categorical	Cross sectional industries
Michel and Shaked (1984)	Positive relationship, unrelated diversification	Rumelt: Categorical	Cross sectional industries
Palepu (1985)	Positive relationship; related diversification	SIC Based	Cross sectional industries
Robins and Wiersema (1995)	Positive relationship, related diversification	SIC based	Manufacturing firms
Rumelt (1974)	Positive relationship, related diversification	Rumelt Categorical	Cross sectional industries
Simmonds (1990)	Positive relationship, related diversification	Rumelt: Categorical	Cross sectional industries
Varadarajan and Ramanujam (1987)	Positive relationship, related	SIC Based	Cross sectional industries

Table 3.1 provides a summary of results showing on the one hand a lack of a relationship and a positive relationship. Results are mixed, with a greater number of studies providing evidence of a positive relationship. It is not surprising that other

evidence suggested that single-business or unrelated-diversified strategies outperform related diversifiers (Lubatkin, 1987; Michel and Shaked, 1984).

Rumelt (1974) was content in reporting the implication of his study referring to an *association* between these variables, rather than addressing any cause and effect relationships that may be there. In his examination of the successful relationship between strategy and economic performance he found that business activities in chartered areas were more likely to be linked to higher levels of performance.

Some, more recent, research has taken the relationship between business-level diversification strategy and economic performance a stage further, from an *association* relationship (Rumelt, 1974), to considering more closely a *causal* relationship (Hall, 1995; Robins and Wiersema, 1995).

From an analysis of the relationships between business diversification and economic performance the current study has developed the following flow diagram to illustrate the various combinations in Figure 3.3.

Figure 3.3

Relationship between Economic Performance and Business level Diversification



There are additional categories, such as single business and dominant business levels, which could have been included in the business diversification level in Figure 3.3 above, however much of the recent research has considered the differences between related and unrelated diversification (Hitt et al. 1997; Kim et al. 1989; Tallman and Li, 1996). These two business level diversification categories have taken prominence particularly when consideration is also given to the effects of international diversification on economic performance.

3.5 Business-level Diversification leads to Higher Economic Performance

Research regarding business-diversification and economic performance has “either avoided or ignored a crucial issue in causality” (Hall, 1995: 26).

The issue of causation was important as:

Prior studies have either been agnostic as to causation or have presumed performance differentials to be outcomes of the diversification strategies adopted (Grant et al. 1988: 771)

It appeared that researchers did not focus on causality but were instead happy to analyse economic performance differences between diversified firms. It was suggested that the crucial issue was whether diversification increases economic performance (Grant et al. 1988; Hall, 1995). Prior studies provide evidence of the possibility of a two way causal relationship between economic performance and diversification: (1) diversification leads to a higher economic performance; (2) higher economic performance can lead to an increase in diversification (Hall, 1995). This was commonly categorised as the chicken and egg scenario, asking the question "which came first?" (Hall, 1995: 27). Prior studies which have tested whether diversification will lead to higher levels of economic performance have been mixed such as Bettis (1981), Bettis and Hall (1982),

Christensen and Montgomery (1981), Lubatkin, (1987), Montgomery, (1985) Rumelt (1974, 1982) and Varadarajan and Ramanujam (1987).

There were various rationales for causal relationship in the literature. First, the rationale for firms diversifying can be explained as a means by which they can become more profitable by entering into businesses other than their current one(s) and hence increase their economic performance. Christensen and Montgomery (1981) provided results which supported diversification as a means to generate higher levels of economic performance. Furthermore, Grant et al. (1988) provided evidence to support the view that firms anticipating low levels of profitability in the future are more likely to move to a diversification strategy. Further support for this contention was made by Burgelman (1983), where it was suggested that when firms are not performing as well as they planned in a profitable sense then diversification may be viewed as a means of improving their economic performance. Although these studies argue that diversification leads to better economic performance, Rumelt (1974) was more specific about diversification and argued that a related diversification strategy is usually recommended as a means of improving economic performance.

The second rationale for diversification concerned the advantages of economies of scale which in turn had a negative impact on costs, thereby increasing economic performance. In particular if and when a firm diversifies into related businesses they are able to share resources and services amongst the businesses which then has the advantages of spreading the cost, which enhances the efficient use of resources (Rumelt, 1974 and 1982). The result of this activity was the higher the level of related diversification the higher the level of efficiency leading to a higher economic performance.

Overall the analysis on causation previously mentioned poses the question of “whether superior performance leads to an increase in business diversification?” or “does business-diversification lead to high levels of economic performance?” From the study by Hall (1995) findings showed that when business-level diversification was used as the independent variable a more consistent outcome resulted and the positive relationship was significant at the $p < 0.05$ level.

3.6 International Diversification Strategy and Economic Performance

Business-level diversification, reported above, provided one form of advantage contributing to a firm’s economic performance. It has been argued that international diversification offered a greater form of advantage contributing to a firm’s economic performance (Hitt, Hosskisson and Ireland, 1994). An extreme view identified that the relationship between economic performance and international diversification was positive whilst the relationship between business level diversification and economic performance was negative:

For example, Buhner’s (1987) study of West German firms found international diversification to be positively related to performance whereas domestic product diversification was negatively related to performance (Hitt et al. 1994: 302-303).

Evidence suggested that international diversification provides numerous advantages to firms which are: “economies of scale, scope and learning”(Hitt et al. 1997: 771) and also identified by Kogut (1985). There are advantages to a firm that engaged in both business and international segments (Porter, 1990). These benefits are in the form of sharing specific firm core competencies and capabilities across countries and business-levels (Hamel, 1991). Similar to the results of the relationship between economic performance and business-level diversification, the results of the relationship between

economic performance and international diversification were also mixed. This mix comprised of positive to no relationship, with a very few empirical studies suggesting a non-linear inverted U-shaped relationship (Geringer et al. 1989; Gomes and Ramaswamy, 1999; Hitt et al. 1997).

The issue of international diversification and economic performance has gained importance over the last few decades (Kim et al. 1989). As well as the product/business level diversification effect on economic performance as previously considered, there was the international business diversification dimension which also effects economic performance (Hitt et al. 1997; Rugman, 1979; Tallman and Li, 1996; Wolf, 1975). International diversification referred to the “expansion across borders of global regions and countries into different geographic locations, or markets” (Hitt et al. 1997: 767).

A firm’s level of international diversification has been reflected by the number of different international markets in which it operates, referred to as country scope, and the extent of the firms multinationality reflected by percentage of foreign sales to total sales. Numerous studies which have empirically tested international diversification and economic performance have produced mixed results as reflected by Table 3.2.

There are more positive than weak or lack of relationship outcomes in reference to Table 3.2. What does appear to be recently investigated is the non-linear relationship between international diversification and economic performance (Geringer et al. 1989; Gomes and Ramaswamy, 1999; Hitt et al. 1997).

Table 3.2: Empirical Studies Testing the Relationship between International -level Diversification Strategy and Economic Performance

Author	Measure of International Diversification	Measure of Economic Performance	Sample	Findings from Empirical Tests
Non-linear relationship				
Geringer, Beamish and da Costa (1989)	Foreign subsidiary sales to total global sales	Ratio of net annual profits to sales (ROS)	Multinational Enterprises for 1977-1981	Non-linear inverted U-shaped relationship
Gomes and Ramaswamy (1999)	Number of foreign countries; ratio of foreign sales to total sales; ratio of foreign assets to total assets	Return on Assets (ROA)	American multinational firms for 1990-1995	Support for a curvilinear relationship between multinationality and economic performance
Hitt, Hosskisson and Kim (1997)	Entropy measure: extent of diversification across foreign market areas	ROA	Manufacturing firms 1988-1990	Inverted U-shaped curvilinear relationship. There is evidence that business-level diversification moderates the relationship.
Weak Results				
Tallman and Li (1996)	Multinationality: proportion of foreign sales to total sales. Country scope: number of foreign countries of operation	Return on Sales (ROS)	Directory of the world's 450 largest industrial corporations for 1987.	Weak effect on performance of internationalising. Consideration was also given to the interaction of business and international dimensions
Positive Results				
Daniels and Bracker (1989)	Foreign sales to total sales and Foreign assets to total assets	ROA	Eighty largest industry groups in Forbes 1984 annual reports	Positive relationship
Grant (1987)	Total sales revenue of overseas subsidiaries to total firm sales	ROA	304 quoted British-owned manufacturing companies The Times 500 list for 1968 to 1984.	Positive relationship

Haar (1989)	Foreign sales to total sales	ROA	Multinational Enterprises from The World Directory of Multinational Enterprises for 1985.	Positive relationship
Kim, Hwang and Burgers (1989)	Geographic market areas: Global Market diversification; Global related diversification	ROA and Operating Profit Margin	130 multinational companies from Dun and Bradstreet for 1982 to 1985.	Positive relationship, consideration is also given to the interaction of business and international dimensions
Severn and Laurence (1974)	Foreign direct investment	ROA	Manufacturing firms in Fortune 500 for 1965	Positive relationship
Vernon (1971)	Multinational enterprises versus non MNEs	ROA and ROS	Fortune 500 corporations for 1964	Positive relationship
Wolf (1975)	Ratio of foreign operations to total operations	Return on Capital	Used Bruck and Lees (1968) data of 1965 corporations as ranked by Fortune 500	Positive relationship
Lack of a Relationship				
Kumar (1984)	Ratio of Foreign sales to total sales	ROA and ROS	672 British quoted corporations for 1972 to 1976.	Lack of a relationship
Morck and Yeung (1991)	Number of subsidiaries abroad	Market value of a firm	1978 data sample	Lack of a relationship

There has been quite a considerable amount of research on the relationship between international diversification strategy and economic performance in America and Britain but not so much in Australia (Lewis and Minchev, 1998). Evidence suggested that the studies in Australia have been limited to internationalisation in the forms of either industry-level policy or behavioural characteristics as described in the following quotation:

Although the process of firms' internationalisation is a well-researched area, studies in the Australian context are limited and focus on either industry-level policy (The Global Challenge, 1990; Yetton et al., 1992; Industry Commission

Report No 53, 1996), the behavioural characteristics of exporting firms (Barret, 1986; Welch, 1993) or the behaviour of multinationals in Australia (Bora, 1998). The overwhelming majority of research on international diversification-performance paradigm comes from the USA and Europe (Rugman, 1983; Michael and Shaked, 1986; Grant, 1987; Grant et al., 1988; Geringer et al, 1989; Olusoga, 1993; Sullivan, 1994; Tallman and Li, 1996) (Lewis and Minchev, 1998: 1).

The one Australian research study that was identified (that of Lewis and Jarvie, 1997) tested the relationship between the degree of diversification strategy and performance and found that there was no consistent relationship of the 63 Australian firms in the sample. Use was made of the categorical measure of business-level diversification of Rumelt (1974), to test against performance but no consideration was given to international diversification (Lewis and Jarvie, 1997).

3.7 An Analysis of the Interaction of Business level with International Diversification when Investigating Economic Performance.

Past research investigating the relationship between international diversification and economic performance have noted that firms which were diversified on an international level were also involved in various different business levels. This suggested that “the interaction between international and product diversification is important” (Hitt et al. 1994: 304). The benefits of the interaction between business-level (product) and international diversification have been noted:

Product diversified firms may be able to enhance performance by diversifying internationally. In doing so, they may be able to achieve some of the benefits of international diversification and capture synergies of product diversification (Hitt et al.1994: 305).

Furthermore, what was suggested was that it is not appropriate to consider global diversification without also considering product/business level dimensions. This call for the integration of both international and business level diversification dimensions

has been evidenced by prior studies which include: Geringer et al. (1989); Hitt et al. (1997); Kim et al. (1989); Pearce, (1983); Tallman and Li, (1996). Evidence suggested that firms', which diversify internationally, may also be diversified at the business level (Hitt et al. 1997) and it was these two streams that have recently been analysed:

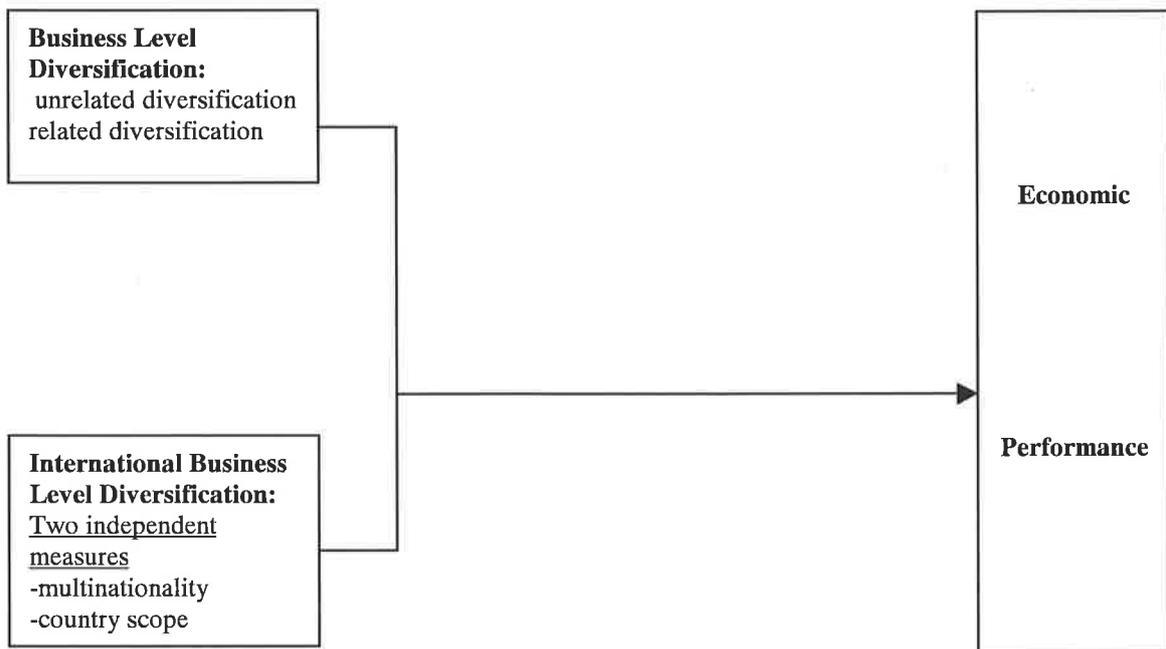
There are two major streams of research examining the profit performance impact of corporate diversification. One stream of research focuses on the product dimension (or business-level) of corporate diversification.... the other on the international market dimension (Kim et al. 1989: 45).

There was evidence, previously reported, which suggested that firms with narrow business-level diversification involving a dominant-business or related-business level diversification strategy can also diversify internationally. Firms of this nature should experience high levels of economic performance, as they may be able to capture potential synergies between their various business levels (Geringer et al. 1989; Hitt et al. 1997; Rumelt, 1974). Where firms' with these levels of interaction between business-level with international diversification, it was argued, have "increased opportunities to achieve economies of scope and scale" (Hitt et al. 1997: 775). Clearly the interaction of business-level diversification with international diversification assists firms to utilise these interdependencies across their operations to achieve productive synergies. There was a strong argument that the core competencies and capabilities, which are derived from business level diversified strategies, are useful in facilitating international diversification activities (Hitt et al. 1997). In further support of this integrative effect on performance, Kim et al. (1989) suggested that the integration of these two issues promote profit growth. The moderating effect of business-level diversification on the relationship between international diversification and economic performance has been recently supported:

many internationally diversified firms are also product diversified. Given the substantial research on product diversification and its assumed effects on firm outcomes (Hoskisson and Hitt, 1990) we expect it to moderate the relationship between international diversification and performance (Hitt et al. 1997: 788).

The resource-based view of the firm accounted for benefits in the form of synergies and economies of firms which share resources. These shared resources included, synergies and economies of scope and scale which a firm with an already existing business-level diversification are also internationally diversified. The benefits of these shared resources from a resource-based view of the firm provided further support for the integration of business-level and international diversification when considering effects on economic performance of a firm. From the above argument utilising a resource-based perspective, one arrives at the assumption that firms which are diversified at the business-level and also diversified at the international level should perform better than firms which are diversified at the international level but not at the business-level as illustrated in Figure 3.4.

Figure 3.4
The Moderating effects of Business-level Diversification on the Relationship between Economic Performance and International Diversification.



Furthermore, it was suggested that “firms able to capture the synergies and economies from product and international diversification strategies can better implement integrated business-level strategies (offering differentiated products at lower prices than competitors)” (Hitt et al. 1997: 776). The most recent research which suggested the need to consider the interaction between business level and international diversification when considering effects of diversification on economic performance included Hitt et al. (1997) and Tallman and Li (1996). There has been sparse research which has included this interactive effect of diversification on performance. This sparsity of research has been noted; “A small number of existing studies examine the combined effects of product and geographical diversification” (Tallman and Li, 1996: 181).

The relationship of the interactive effects of business level with international diversification on economic performance was illustrated in Figure 3.4.

The Interactive effects of Country Scope and Multinationality on Economic Performance

The interactive effects of the two independent measures of international diversification and economic performance was identified in one empirical study (Tallman and Li, 1996). Evidence suggested that country scope rather than multinationality had a significant relationship with economic performance and the interaction between country scope and multinationality has no effect (Tallman and Li, 1996) which is contrary to that noted by Ramaswamy (1993):

only country scope is significantly correlated with performance. Multinationality does not have a significant effect on firm performance....The coefficient of the interaction term is also nonsignificant and negative rather than showing the strong positive effect that Ramaswamy (1993) noted (Tallman and Li, 1996: 189 & 191).

These three combinations which include multinationality, country scope and the interaction of country scope with multinationality on economic performance were illustrated in Figure 3.5.

Figure 3.5
The Effects of Multinationality, Country Scope and the Interaction between Multinationality and Country Scope on Economic Performance



Sparse evidence on this interactive relationship between these two independent variables was noted from the literature analysed above suggesting a closer investigation of this relationship which may reveal interesting results. In the current study this approach could be applied to Australian firms, which diversify on an international level.

In sum, the literature previously mentioned investigated the link between business-level and international diversification and the impact of this link on economic performance (Hitt et al. 1997). Evidence also suggested that business-level diversification strategy enhances international diversification (Hitt et al. 1997). Furthermore, using a resource-based view of the firm it was suggested that there is an inverse U-shaped curvilinear relationship between economic performance and international diversification, reflecting the transaction cost effect of further global interaction. What was argued, in the situation where an inverted U-shaped relationship exists, was that economic performance could be improved as international diversification increased but only up to a particular critical cut-off point. Beyond that critical cut-off point performance did not

improve but became negative (Geringer et al. 1989; Gomes and Ramaswamy, 1999; Hitt et al. 1997).

3.8 Evidence of a Non-linear Relationship between International Diversification and Economic Performance

The following section considered past research which has identified a curvilinear relationship between international diversification and economic performance (refer to Table 3.2). The previous section analysed the results of combining the business level diversification with international diversity when investigating economic performance as evidence suggested that the resultant economic performance would improve (Tallman and Li, 1996). What was also identified in this interaction was the effect of transaction costs. It was suggested that as the firm moves towards higher levels of international diversification transaction costs increase to such a level that the costs outweigh the benefits of further international diversification (Geringer et al. 1989; Gomes and Ramaswamy, 1999; Hitt et al. 1997; Tallman and Li, 1996). This implied that the progressively higher joint levels of business level and international diversity the lower the economic performance. What was suggested here is that costs of further diversification are higher than the benefits gained in terms of performance (Hitt et al. 1997; Jones and Hill, 1988; Tallman and Li, 1996). It has been shown that: “ A firm that tries to apply a broad product portfolio on an integrated global basis may well stretch its management resources excessively” (Tallman and Li, 1996: 186).

Transaction costs are referred to as the coordination, distribution and management costs that accompany international operations (Hitt et al. 1994). These costs are: foreign government regulations and trade laws; trade barriers; logistical costs; cultural diversity (Hitt et al. 1994). Marketing program redesign for foreign markets across borders is another additional costs of implementing an international diversification strategy which add to the cost (Hitt et al. 1994; Kogut, 1985). At the initial stages of international

diversification one would expect economic performance to be positive and this is expected to continue to be positive up to a critical international diversification level. If the firm continues beyond this critical point then the benefits of further international diversification are overcome by the higher level of transaction costs that is incurred. At this higher level of international diversification the costs outweigh the benefits, such that the relationship between international diversification and economic performance becomes negative (Hitt et al. 1994).

In combining the impact of a resource-based view of the firm and the consequential effects of transaction costs provided evidence of a non-linear relationship between international diversification and economic performance (Geringer et al. 1989; Hitt et al. 1997; Kumar, 1984; Morck and Yeung, 1991). Geringer et al. (1989), at the earlier stages of the recognition of a non-linear relationship, identified that there was a non-linear inverted U-shaped relationship between international diversification and economic performance. The interpretation of a curvilinear characteristic was that at moderate levels of international diversification a firm experienced positive benefits in the form of economic performance, but when a firm went beyond that level or critical cut-off point, additional transaction costs were incurred. What has been suggested is that as a firm escalates its international geographic dispersion so the transaction costs and managerial information processing increased. This overall increase in costs and processing from further progressive steps to diversify internationally, so diminishing returns begin to take effect to a point where the firm experiences a negative impact on economic performance (Hitt et al. 1997; Jones and Hill, 1988).

A closer consideration of transaction costs indicated that progressive geographic dispersion increases costs which include coordination, distribution and management costs. Costs of transacting internationally are many and varied and include the

following; government regulations, trade laws, currency value fluctuations across countries, access to raw materials and employee skills requiring considerable coordination. As a consequence of these transactions costs and foreign country anomalies evident across geographic regions there is a greater level of managerial information-processing which adds further to the cost of international diversification. Moreover, these information processing issues include: logistical costs, trade barrier and cultural diversity which make management of internationally diversified firms highly complex (Hitt et al. 1997).

In a recent study, Gomes and Ramaswamy (1999) considered the form of the relationship between multinationality and economic performance and their results supported a curvilinear relationship between multinationality and economic performance. They referred to eight previous studies namely: Buckley et al. (1977, 1984); Daniels and Bracker, (1989); Gerlinger et al. (1989); Haar, (1989); Hitt et al. (1997); Kumar, (1984); Ramaswamy, (1995), that provided some element of a curvilinear relationship between multinationality and performance. With the exception of Hitt et al. (1997), “a majority of the studies have not made serious effort to explore [sic] curvilinearity in theoretical terms” (Gomes and Ramaswamy, 1999: 179). Of these eight studies identified by Gomes and Ramaswamy (1999), there was no empirical evidence or support for Buckley et al. (1977; 1984), and Daniels and Bracker (1989). A further three that did provide empirical findings proved a mix of results:

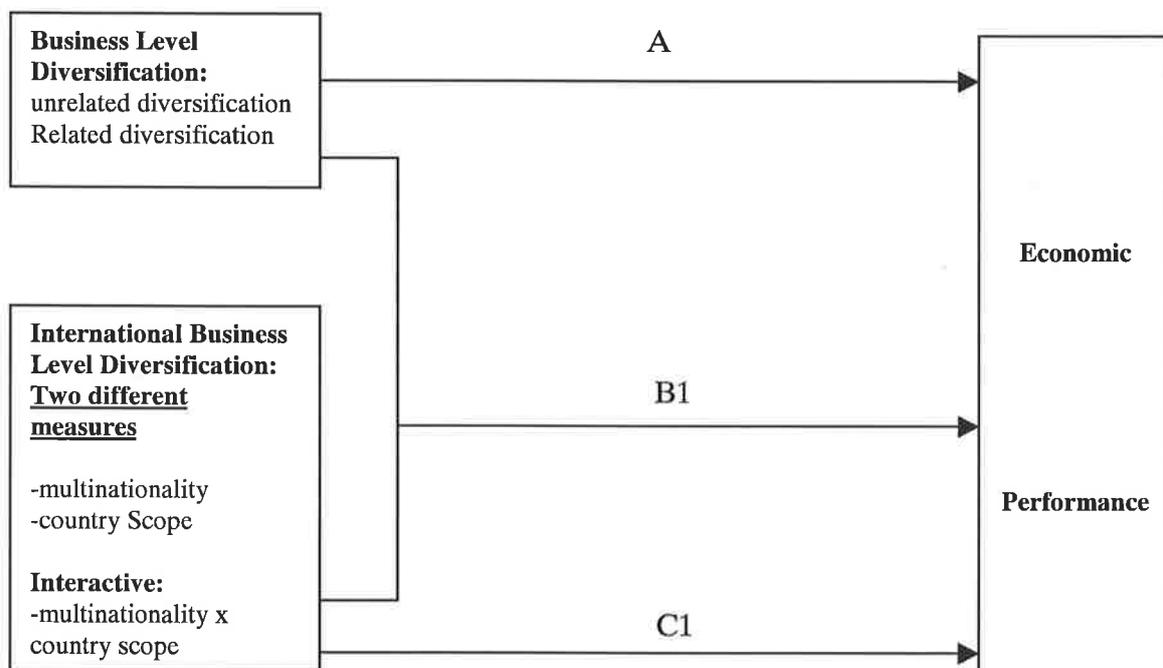
For example, while Kumar (1984) reported that multinationality had a uniform negative effect on performance, Haar (1989) and Ramaswamy (1995) reported a positive relationship (Gomes and Ramaswamy, 1999: 179).

The remaining two studies of the eight (considering a potential non-linear relationship between multinationality and economic performance), did provide some evidence of

curvilinearity. The first of these, Geringer et al. (1989) did find that economic performance did decline at some range of international diversification. They did not identify a critical cut-off point for when international diversification declines (Gomes and Ramaswamy, 1999). The second of these studies was that of Hitt et al. (1997) who identified a curvilinear relationship between international diversification and economic performance.

In conclusion, when combining the results of the literature analysed in the current chapter a summary of these relationships together with interactive relationships are illustrated for convenience in Figure 3.6 below.

Figure 3.6
Relationship between Economic performance and International Diversification:
Incorporating the moderating effects of Business level Diversification and the
Interactive effects of Country Scope with Multinationality



Where:

A refers to the relationship between business level diversification and economic performance.
-unrelated business diversification on economic performance
-related business diversification on economic performance

B1 refers to the relationship of the interaction of business level diversification (unrelated and related) and multinationality on economic performance.
-unrelated business diversification x multinationality on economic performance
-related business diversification x multinationality on economic performance
Evidence suggests non-linear or inverted U-shaped relationship may exist.

C1 refers to the relationship of
-country scope on economic performance
-multinationality on economic performance
-the interaction of multinationality and country scope on economic performance.
Evidence suggests non-linear or inverted U-shaped relationship may exist.

3.9 Summary

This chapter has reported some major works in past strategic management literature, which have tested the relationship between business level diversification strategy and economic performance. The results of these prior studies have been mixed. Furthermore, that these mixed results regarding the relationship between business-level diversification strategy and economic performance include positive, negative and a no-effect relationships. In analysing outcomes from previous strategic management studies what has been identified was a greater number of studies providing evidence of a positive relationship between related diversification strategy and economic performance.

An area of study requiring further research, identified in the literature, related to the testing of causal relationships between diversification strategy and economic performance. More specifically whether related diversification strategy will lead to superior levels of economic performance in these firms.

What has been identified in the above analysis concerning international management strategies is a need to test the integrated effects of business-level with international diversification on economic performance. The chapter has identified evidence of benefits to be gained for a firm, which integrates its business level with international diversification activities. These gains reflect the resource-based view of the firm and involve resource sharing advantages, which include, economies of scale and scope together with the benefits of synergy. After closer examination of the relationship between economic performance and international diversification only scanty evidence was identified supporting a non-linear inverted U-shaped relationship (Gomes and Ramaswamy, 1999; Hitt et al. 1997). The conflicting results from prior research of a positive relationship between international diversification and economic performance could be explained using the argument that once a firm goes beyond a particular level of international diversification, then costs begin to exceed benefits and economic performance suffers. What resulted was a non-linear inverted U-shaped curve, which better describes the relationship between economic performance and international diversification. The non-linear situation was explained by the effects of both transaction costs and additional managerial information processing. As a firm enters a larger number of geographic international areas or reaches a higher level of foreign sales to total sales so the transactions costs and managerial information processing is further complicated and so costs begin to outweigh benefits till diminishing returns set in and this creates a negative effect on economic performance.

The next Chapter investigates the relationship between stakeholder concerns on economic performance and provides evidence of a link between social responsibility of the firm and stakeholder management/concerns.

CHAPTER FOUR

ECONOMIC PERFORMANCE AND STAKEHOLDER CONCERNS

4.1 Introduction

Chapter One identified the purpose of this research study as investigating whether strategic and international business diversification with stakeholder concerns enhance economic performance. It identified the need to develop a socioeconomic framework, which incorporates transactions cost, resource-based and instrumental stakeholder theory, for investigating economic performance. Chapter Two developed a socioeconomic model examining the effect that strategic management, international business diversification and stakeholder concerns has on economic performance. Chapter Three examined the relationship between business-level diversification strategy and economic performance, the interaction of international diversification with business-level diversification on economic performance. Then an analysis of the interaction of multinationality with country scope on economic performance was considered. The importance of transaction costs effects on this relationship was then examined providing evidence of a curvilinear relationship between international diversification and economic performance from a sparse number of past research studies.

This chapter analysed the relationship between stakeholder management and economic performance. This section of work provided support for social responsibility reporting, as identified through disclosures in corporate annual reports, as a medium for stakeholder concerns. Stakeholder thinking provided an analysis of a broader set of interests of a firm of which shareholder is only one. The chapter provided evidence to support using

social responsibility disclosures themes from corporate annual reports as a way of identifying stakeholder concerns and that these concerns are positively related to economic performance. In developing the research review, multiple channels were used. A search was performed on computerised *ABI-inform and Lexis-Nexus*. A manual search of journals and periodicals concerned with social responsibility and stakeholders was undertaken such as: *Academy of Management Journal; Academy of Management Review; Accounting, Auditing and Accountability Journal; Accounting Organizations and Society; Accounting Review; Advances in Public Interest Accounting; Advances in Strategic Management; American Journal of Sociology; British Accounting Review; Business and Society Journal; California Management Review; Chartered Accountant in Australia; Cost and Management Accounting; Financial Management; Journal of Accounting Research; Journal of Behavioural Economics; Journal of Business Ethics; Journal of Business Research; Journal of Contemporary Business; Long Range Planning; Omega* at the University of Adelaide, the Flinders University of South Australia and, the University of New South Wales.

The chapter begins with a definition of social responsibility reporting then links this disclosure to themes from which stakeholder groups are identified. In this way social responsibility disclosure provided a useful way of identifying stakeholder concerns of a firm. The next section analysed past literature which has considered social disclosures in Australia as further evidence of a set of social responsibility themes. These disclosure themes were then matched with stakeholder groups from numerous stakeholder studies. The matching of themes with these groups was tabulated and analysed. In considering the relationship between social responsibility reporting and economic performance reference was made of an evaluation by Ullmann (1985) representing some earlier suggestions that the relationship between corporate social responsibility and economic performance be stakeholder oriented.

A further section recognised the stakeholder concept formalised by Freeman (1984) providing further justification for using a stakeholder orientation when examining the relationship between social responsibility reporting and economic performance. The next section analysed the interchangeability of social disclosure, reputation and rating when referring to social performance. The result of this interchangeability was that social disclosures are included in past studies particularly when reference is made to stakeholder groups. This provided justification for using social responsibility disclosures as a medium for stakeholder concerns. Recognition was also made of recent work carried out by Waddock and Graves (1997) in linking social performance to stakeholder issues. Moreover, Griffin and Mahon (1997) had positioned social disclosure, ratings and reputation under the social performance umbrella. The following section established more formally a link between social responsibility reporting and stakeholder concerns. Finally the chapter considered the nature and form of the relationship which challenged the linearity assumption of the relationship. Furthermore scanty evidence was provided of an inverted U-shaped curvilinear relationship between stakeholder concerns and economic performance

The issue of a concern for stakeholders and the effect that this concern has on economic performance was found to be significant:

statistically significant linkage between a management commitment to strong controls that emphasizesocially responsible behaviour on one hand and favourable corporate financial performance on the other.....results demonstrate the probability that a broad corporate concern for ethical conduct towards stakeholders is becoming a mainstream management issue in achieving higher profitability (Verschoor, 1998: 1515)

Use was made of past research, which has investigated the relationship between stakeholder concerns and economic performance, referring to Australian, American and British studies. An important link between social performance and forms of social responsibility measures were examined which identified social disclosure as such a measure. Further consideration was given to studies which have subdivided social responsibility behaviour into low/moderate and high levels when challenging the linearity of the relationship between economic performance and stakeholder management.

4.2 Social Responsibility Reporting: An Elusive Activity

There were a considerable variety of rationales underpinning social responsibility reporting. Advocates see it as attempting to identify the social costs of organisational activity so that organisations may be encouraged to internalise their external diseconomies. Constituents see it as an expression of the traditional stewardship concept, where the organisation was not only responsible for its pursuits of owners' interests and for monitoring their economic resources, but was also responsible for making net positive contributions to social welfare (Chen, 1975; Estes, 1972). From a management point of view, social responsibility may be undertaken as a means of justifying company activities, as a means of anticipating or avoiding pressure for change, as a means of fostering an improved public image, improved consumer response, and better profits, or simply a means of satisfying various socio-economic demands made upon business. This then preserves support or acceptance of constituents such as unions, citizen action groups, business associations and regulatory authorities (Demers and Wayland, 1982; Parker, 1976; Ullmann, 1985).

Rationales for social responsibility reporting appeared to be related to the particular perspective that the report producer adopts (Parker, 1986). A number of perspectives have been presented such as: (1) capitalist versus socialists; (2) shareholder versus other special interest groups; (3) internal report user versus external report user; (4) free marketer versus radical leftist; (5) corporate defender versus corporate critic (Parker, 1986).

A way in which corporations communicated their commitment to social responsibility activities was through narrative in corporate annual reports particularly for Australian firms. Parker (1986) was close to identifying the other constituencies which are affected by the firm and or can be affect by the firm, commonly referred to as stakeholders under the definition of Freeman (1984). Instead Parker (1986), rather preferred to consider the shareholder versus other special interest groups issue. It was the other special interest groups which go beyond the shareholders that the next section considers preferring to categorise them as stakeholders.

In sum considering social responsibility reporting as disclosed in corporate annual reports of Australian firms was a reflection of managers' concern for stakeholders as identified by Parker (1986). Parker (1986) in his description of social responsibility reporting included special interest groups as well as shareholders. This link between social responsibility and stakeholder interests was important in an Australian context.

4.3 Linking Social Responsibility Disclosures Themes to Stakeholder Groups

The Usefulness of Social Responsibility Disclosure in Identifying a Stakeholder Perspective.

Social responsibility disclosure assisted management in the provision of a corporate social policy of an organisation. Social responsibility disclosure took the form of

employee related, customer related, environment related and community related responsibility. This form of disclosure can act as an information source for stakeholders of the organisation concerned with the social performance of the organisation (Johnston, 1979). Stakeholders of an organisation were considered to take the form of individuals or groups who can have an impact on or be impacted upon by the corporate strategic mission (Freeman, 1984). It was argued by Freeman (1984) that for organisations to succeed in the present and future environment then it is advisable that managers take multiple stakeholder groups into account. Social responsibility disclosures provided a useful guide to the level of manager commitment to stakeholder management.

The stakeholder approach regarded organisations as strategically conscious of a larger society. This view indicated that there are increasing demands on managers which include wider variety of stakeholders not traditionally related to the managers' self interest. The notion of stakeholders goes beyond the immediate interest of stockholders. It viewed profit in broader terms, with a longer-term focus that encompasses a greater consideration for other groups in the firm's environment.

In as much as stakeholders approach include an indefinitely large number of groups with some interest in corporate operations, a further distinction was made between primary and secondary stakeholders. Primary stakeholders were those individuals and groups who are most directly affected by the activities of the firm, and who make some tangible contribution to its functioning, such as employees, customers and suppliers. Clarkson (1995) also defined a primary stakeholder group as "one without whose continuing participation the corporation cannot survive as a going concern" (Clarkson, 1995: 106). In this definition of primary stakeholders the following were included: shareholders; investors; employees; customers; suppliers.

Secondary stakeholders were affected by corporate actions, but do not participate in the ordinary operations of the business. Examples would include consumers as a group, women, ethnic minorities, environmental groups, the press and competitors (Armstrong, 1977; Carroll, 1989). Clarkson (1995) also provided a similar but more refined definition of secondary stakeholders:

secondary stakeholders groups are identified as those who influence or affect, or are influenced or affected by, the corporation, but they are not engaged in transactions with the corporation and are not essential for its survival (Clarkson 1995: 107).

Unlike the traditional financial information, often useful to managers and stakeholders, there appeared to be some debate as to the usefulness and use of social responsibility reporting by managers and stakeholders:

The measurement of the usefulness and use of social reporting information.... the assessment must start at the earliest stages of perception, because the process of discovering usefulness and uses is not yet as fully developed, explored and internalised by management and stakeholder groups as can be expected of more traditional information tools such as financial reporting (Dierkes and Antal, 1985: 29).

The question regarding the importance of social responsibility reporting to stakeholder groups was often determined by whether they are primary or secondary. There was an argument that stakeholders and stakeholder groups accept social responsibility reporting, which was disclosed in annual reports, as useful in their decision-making processes. The question of useable social disclosure information needed to consider whether the information was reliable, the way it was presented to stakeholders, and its impact on the decision making process (Sorg, 1979). It was noted that some managers found that social responsibility reporting was a valuable guide to predicting future policy (Bauer, 1973; Dierkes and Antal, 1985; Migros, 1978; Welbergen, 1978). Furthermore, there were

research studies that suggested that social responsibility disclosure was used to evaluate internal performance specifically when viewed from the objectives of goal accounting (Brennan, 1979; Migros, 1978, 1980; Welbergen, 1978).

As companies formally collected and published information on their social responsibility activities, whether they be environmental impacts or facilitating high quality employee conditions at work, this information can affect their decision-behaviour together with that of stakeholders decision-behaviour. This lead to the suggestion that the evidence of the processing of social responsibility reporting and publishing it in corporate annual reports (as well as other special purpose reports) thus making it available to the public makes it decision useful. In this sense, social responsibility reporting functions similarly to the traditional financial report in that its existence serves to monitor and influence managerial strategic behaviour and also to manage stakeholders of the firm.

Using Social Responsibility Disclosure in Australian Corporate Annual Reports to Identify Social Responsibility Disclosure Themes

The purpose of this section of the chapter was to identify common social responsible disclosure themes from Australian corporate annual reports. Use was made of past research that examined social responsibility in an Australian context. A summary of the most common social responsibility themes used was developed.

From an analysis of literature on social responsibility reporting which used social responsibility disclosure, three approaches to examining social responsibility were identified. First, social responsibility was assessed using expenditures on pollution control (Belkaoui, 1976; Chen and Metcalf, 1980; Freedman and Jaggi, 1982; Shane and Spicer, 1983; Spicer, 1978). A second approach to identifying social disclosures was to

assess the opinion surveys of corporate reputations. Other past studies identified social responsibility by accessing the content of corporate disclosure from corporate annual reports (Belkaoui, 1976; Cowen et al. 1987; Freedman and Jaggi, 1982; Freedman and Wasley, 1983; Fry and Hock, 1976; Guthrie and Parker 1990; Ingram, 1978; Preston, 1978). Furthermore, Cowen et al (1987) and Trotman and Bradley (1981) found that factors, such as industry and firm size also mediated the amount and content of companies social disclosure.

Australian researchers identified social responsibility themes using content analysis by analysing social disclosure and measures which included: Gul, Andrew and Teoh (1984); Guthrie (1982); Guthrie and Parker (1990); Kelly (1979); Pang (1982); Trotman (1979); Trotman and Bradley (1981). These studies reflected measures of social disclosure in an Australian context refer to Table 4.1 for a summary of these studies.

In the study carried out by Trotman (1979), a sample of the largest 100 Australian companies listed on the Sydney Stock Exchange was used. Social disclosures was found under the following headings of *environment, energy, human resources, products, community involvement and 'other'* (Mathews, 1993). In this study Trotman (1979) environment and human resources disclosures were identified as those the two which were most regularly included in the 1977 corporate annual reports. The method of measuring social disclosure in corporate annual reports included "average pages per company report". According to Mathews (1993) the significance of this study was its approach to identifying social responsibility disclosure in Australian corporate annual reports.

Table 4.1
Summary of Findings of Social Responsibility Disclosure Studies which used
Australian Corporate Annual Reports.

Study	Sample Size	Measurement method of Social Disclosure	Social responsibility disclosure themes
Gul, Andrew and Teoh (1984)	Random sample of 136 Australian listed public companies	Content Analysis of corporate annual reports: measured by percentage of pages	Social Disclosure themes were: -human resources -community development -environment
Guthrie (1982)	Top 150 Australian listed Public Companies for 1980	Content Analysis of corporate annual reports: measured by percentage of pages	Social Disclosure Themes fall into Five categories: -environment -energy -employee -product -community
Guthrie and Parker (1990)	50 largest listed companies in America, Britain and Australia covering period ending 1983	Content Analysis of Corporate annual reports: measured by written messages	Social Disclosure themes were: -human resources -community involvement -environment
Kelly (1979)	Sample of 50 corporations over a period 1960-78	Content Analysis of Corporate annual reports: average pages per company report	Social Disclosure Themes fall into Five categories: -environment -energy -human resources -product -community involvement

Table 4.1
Summary of Findings of Social Responsibility Disclosure Studies which used
Australian Corporate Annual Reports (continued).

Pang (1982)	100 Australian Companies listed on the Sydney Stock Exchange in 1980 which included 70 of the largest firms	Content Analysis of Corporate annual reports: average pages per company report	Social Disclosure themes were: -human resources -energy -community involvement -environment -product safety issues
Trotman (1979)	Largest 100 companies listed on the Sydney stock exchange	Content Analysis of Corporate annual reports: average pages per company report	Social Disclosure themes were: -human resources -energy -community involvement -environment -product safety issues -and others
Trotman and Bradley (1981)	207 companies listed on the Australian Associated Stock Exchange	Content Analysis of Corporate annual reports: average pages per company report	Social Disclosure themes were: -human resources -energy -community involvement -environment -product safety issues -and others

In another Australian study Kelly (1979), used social responsibility disclosure identified in corporate annual reports from a sample of 50 corporations covering the period 1960-78. These findings further validated Trotman's evidence of increased disclosure over a time frame. In this study Kelly (1979) identified that large sized companies were more likely to disclose environmentally oriented and product related material than smaller companies. Furthermore, Kelly (1979) found that companies in the primary and secondary

sectors were more inclined to disclose environmental and energy related material relative to companies in the tertiary sector. This represented another significant Australian study regarding the level of content of social responsibility disclosure in corporate annual reports over time.

An analysis of social disclosures in corporate annual reports by Trotman and Bradley (1981), using 207 selected Australian public companies, identified social responsibility categories which include environment, energy, human resources, products, community involvement and 'other'. A statistically significant relationship between company size and social responsibility was a valuable contribution from this Australian study. Larger corporations were more likely to engage in more social disclosures.

The Trotman and Bradley study was significant in that it gave social responsibility reporting some direction in Australia and also increased sophistication of its analysis (Mathews, 1993: 99).

Pang (1982), in her research in the area of social responsibility reporting, utilised the approach of Trotman (1979) in which she empirically examined the social responsibility disclosure of a sample of 100 Australian companies listed on the Sydney Stock Exchange in 1980. Corporate annual reports were examined according to particular social themes which include; energy, human resources, community involvement, environment and product safety issues. Pang (1982) suggested that larger companies were more likely to frequently social disclose than the smaller companies.

The social responsible themes in the research study of Pang (1982) were identified in the following locations, a separate report, a separate section of the annual report, separate headings in various reports, and coverage as part of other major topics in annual reports. There was a tendency for larger companies to supply independent reporting of social

responsibility information, on the other hand Pang (1982) noticed that smaller companies seemed more likely to disclose social information in union with other components of the corporate annual report.

In his analysis of social responsibility reporting Guthrie (1982) selected the top 150 Australian listed companies for 1980. Use was made of content analysis of corporate annual reports to identify social responsibility reporting within four major dimensions: theme; evidence; amount and location. First, theme contained five categories such as environment related, energy related, employee related (human resources), product related, community related and others. Furthermore, Guthrie (1982) analysed the form which the social disclosure took and for convenience identified the form in terms of monetary, non-monetary, and declarative (qualitative). Next, the amount was representative of the percentage of pages dedicated to social responsibility disclosure. Finally, consideration was given to the specific component of the corporate annual report that discloses social responsibility reporting together with specifically oriented and targeted publications on social responsibility.

As mentioned in Mathews (1983) a study by Guthrie (1982) on social responsibility reporting took on the following different themes and relative significance:

human resources 43%; environment 21%; community involvement 14%; energy 9%; products 5% and others 8%. With respect to *evidence*, it was established that 60% of social responsibility reporting were declarative, whilst 24% indicated some non-monetary quantification (Mathews, 1983: 100).

Following on, the most frequent locations for disclosing social responsibility was located in the director's report 50%, whilst disclosures which was not specifically located accounted for 40%, whilst only 10% of social disclosures were located in a specific place

in the corporate annual report. The significance of Guthrie's (1982) study was the way of identifying social responsibility involving content analysis.

Gul, Andrew and Teoh (1984), applied the social responsibility themes and amount as proposed by Guthrie (1982), in another Australian study. These themes comprised of 36% to human resources, whilst 32% involved community development and 10% referred to the environment. Another outcome of their Australian study provided evidence to suggest that large companies were more likely to disclose information regarding employee related social responsibility disclosures than smaller firms. Regarding location of social responsibility reporting it was found that the majority of disclosures was in the directors report. In sum it was concluded that at least 30% of companies in the sample under study contained social responsible disclosure.

In an international analysis study by Guthrie and Parker (1990), a significant finding from a content analysis of corporate annual report disclosures concerning social impacts in the United States, United Kingdom and Australia was identification of common ranking's across these three countries for human resources, community development and environmental disclosures. From a content analysis approach employed, it was assumed that the content categories identified in the written messages of annual reports had manifest meanings that could be categorised, for instance, environment and employment practices.

From a User Utility perspective, social responsibility reporting may also represent an attempt to respond to demands for social impact information from interest groups, such as, unions, investment funds, churches and environmentalists (Guthrie and Parker, 1990: 165).

In sum, the purpose of this section of the chapter was to examine the ways previous accounting and management researchers have identified and classified firm social responsibility disclosures. Themes that were most commonly used in Australian studies of listed public companies were identified to help develop social responsibility disclosure themes. These themes were then used to identify stakeholders groups. In sum, Australian studies of social responsibility (from Table 4.1) categorised social disclosures into five commonly used themes namely: employee related; environment related; product related, energy related and community related social responsibility disclosures (Gul et al. 1984; Guthrie, 1982; Guthrie and Parker, 1990; Kelly, 1979; Pang, 1982; Trotman, 1979; Trotman and Bradley, 1981). These themes are summarised in Table 4.2.

Table 4.2
Summary of Social Responsibility Disclosure Themes

Employee Related
Product Related
Community Related
Environmental Related
Energy Related

The themes in Table 4.2 are used in the next section to match social responsibility themes with stakeholder groups from other prior studies which specifically analyse stakeholder concerns.

Using Social Responsibility Disclosure Themes to Identify Stakeholder Groups

From an Australia perspective the above analysis has identified that prior studies have been restricted to social responsibility disclosures which comprised narrative messages in corporate annual reports. The reason for this was that there was no corporate reputational index or ratings scale for firms in Australia. For instance in America use was made of Kinder, Lydenberg and Domini (KLD) ratings measure (Waddock and Graves, 1997; Griffin and Mahon, 1997). KLD is a consulting firm that screens firm's social performance. Furthermore, Cochran and Wood (1984) provide an example of using Moskowitz corporate ratings. However in Australia KLD ratings measure and Moskowitz corporate ratings did not exist, so use was made of the content analysis in corporate annual reports using the themes developed in Table 4.2.

Evidence of a link between social responsibility disclosure themes and stakeholder groups was clearly visible from the identification of four most frequently used stakeholder groups in past studies. These stakeholders were community relations, employee relations, environment, customer (product category) and stockholders (Bendheim et al. 1998; Carroll, 1989; Waddock and Graves, 1997). Table 4.3 provides evidence which supports this link.

From Table 4.3 there was evidence of a linkage between stakeholder group identification and social disclosure themes. In particular the study of Waddock and Graves (1997) provides an almost identical match as between stakeholder groups and social disclosure themes providing specific evidence of the usefulness of social responsibility disclosures themes for identifying stakeholder groups.

Table 4.3
Evidence to Support Matching Social Responsibility Disclosure Themes with Stakeholder Groups

Author	Stakeholder Groups	Comments on linkages to Social Responsibility Disclosure Themes
Bendheim, Waddock, & Graves (1998).	<ul style="list-style-type: none"> -community relations -employee relations -environment -product -stockholder 	These stakeholder groups parallel the social responsibility disclosure themes in Table 4.2 and add in stockholder. Use was made of KLD corporate social performance ratings in this study.
Carroll (1989)	<u>Primary Stakeholders</u> <ul style="list-style-type: none"> -owners -employees -customers -suppliers <u>Secondary Stakeholders</u> <ul style="list-style-type: none"> -media -environmental groups -consumer groups -local community groups -society at large -special interest groups -American civil liberties union 	This categorisation of Stakeholders encapsulated the four social responsibility themes. It provided further evidence of a match between social responsibility disclosure and stakeholder groups.
Edlund (1996)	<ul style="list-style-type: none"> -owners -creditors -customers -suppliers -competitors 	Commentary in Business & Society journal. Analysed the link between social responsibility and stakeholders.



Table 4.3
Evidence to Support Matching Social Responsibility Disclosure Themes
with Stakeholder Groups (continued)

Huse & Eide (1996)	<ul style="list-style-type: none"> -local communities -governments -employees -financial institutions -stockholders -activists -unions -environmental -customers -suppliers -political groups 	The stakeholder groups in this study more than match up with themes in Table 4.2. Use was made of a single case-study of UNI Storebrand.
Preston & O'Bannon (1997)	<ul style="list-style-type: none"> -community and environmental responsibility -ability to select and retain good people 	These three stakeholder groups match three social responsibility disclosure themes. Use was made of Fortune survey data on corporate reputation.
Waddock & Graves (1997)	<ul style="list-style-type: none"> -community relations -employee relations -treatment of environment -customer relations 	These stakeholder categorisations fit almost perfectly with the social disclosure themes
Wartick & Wood (1998)	<p><u>Primary Stakeholders:</u></p> <ul style="list-style-type: none"> -owners -employees -customers -suppliers <p><u>Secondary Stakeholders</u></p> <ul style="list-style-type: none"> -media -environmental activists -consumer protection activists -competitors -financial analysts -creditors -communities non-profit organisations 	This was quite a comprehensive list of stakeholder groups that fits well with the four major themes of social responsibility disclosure. This categorisation of stakeholder into primary and secondary

In a recent working paper Smith and Waddock (1999) provided further evidence for grouping stakeholder as; customers (through product quality), employees, communities and the environment. Table 4.4 provided a summary of links between social disclosure themes with stakeholder groups and identifies energy related social disclosures as not linked clearly with any specific stakeholder group.

Table 4.4

Linking Social Disclosure Themes with Stakeholder Groups

Social Disclosure Themes	Stakeholder Groups
Employee Related	Employee relations
Product Related	Customers groups (product)
Community Related	Local community groups
Environment	Treatment of environment
Energy Related	Not clearly specified

4.4 Social Responsibility Reporting/Stakeholder Concerns and Economic Performance

There have been several studies which have tested for a relationship between social responsibility reporting and economic performance in particular whether there was a positive or negative relationship between social responsibility reporting and economic performance. This section analysed prior studies which examined the relationship between social responsibility reporting and economic performance, which are summarised in Table 4.5.

In an early study Fry and Hock (1976) tested the relationship between social responsibility reporting in annual reports and performance, and controlled for other variables such as size and industry image. In their sample they considered 135 firms from 15 industries and found that there was a positive relationship between earnings and social responsibility disclosure in corporate annual reports. Using data from Ernst and Ernst (1976), Preston (1978) tested for a relationship between the content of social responsibility reporting found in corporate annual reports and economic performance in the form of return on equity. Preston (1978) found that a weak positive association existed between economic performance and the level of social responsibility. Social responsibility was determined using content of social responsibility disclosure in annual reports and this was related to economic performance in the form of return on equity. Bowman (1978) tested for a relationship between economic performance, as measured by return on equity, and social responsibility reporting. Disclosure of social responsibility in corporate annual returns was used but restricted to prose which analysed or recorded equal employment opportunity. Use was made of content analysis to determine the percentage of the social responsibility disclosure in corporate annual reports to measure the level of social responsibility of each firm. Consideration was given to annual reports of 46 American companies for the year 1974 in the computing industry. Results of this relationship showed a positive correlation between the disclosure of equal employment opportunity information and economic performance, measured by return on equity

The above mentioned studies have highlighted some of the past research, which have provided support for a positive relationship between social responsibility reporting and economic performance. Other studies which have supported a positive relationship between social responsibility reporting and economic performance listed in Table 4.4 are Anderson and Frankle, 1980; Belkaoui, 1976; Bowman (1978); Cochran and Wood (1984); Freedman and Jaggi (1988); Griffin and Mahon (1997); Herremans et al. (1993);

Ingram (1978); McGurie et al (1988); Preston and O'Bannon (1997); Spicer (1978); Waddock and Graves (1997). The results of past studies are however mixed so there are others which provide negative or no support (refer to Table 4.5).

A study that did not find conclusive evidence of an association between social responsibility and economic performance was that of Abbott and Mosen (1979). They used the content analysis technique to measure social responsibility disclosure from corporate annual reports to reflect social responsibility together with the overall score obtained from the Ernst and Ernst studies to construct a social involvement disclosure scale. This scale was used to investigate the nature of the relationship between the social concerns and the economic performance of 450 companies. Abbott and Mosen (1979), after consideration was given to size (number of employees) of the company as a moderating variable, found that there was a no real relationship between social concerns and economic performance.

From Table 4.5 there are more positive outcomes from prior research of the relationship between economic performance and social responsibility than negative or inconclusive results. The relationship between social responsibility and economic performance was still not a clear one (Ullmann, 1985; Waddock and Graves, 1997). As argued eloquently by Waddock and Graves (1997: 304), "Results of empirical work indicate an ambiguous relationship." It still remains unclear as to whether social performance leads to greater economic performance or whether economic performance provides the resources to then perform in a social responsible way.

Table 4.5
Summary of Findings Of The Relationship Between Social
Responsibility Reputation/ Performance/Disclosure and Economic
Performance

Study	Social Respons.	Economic Performance	Control for other Variables	Sample	Results
No relationship					
Abbott and Monson (1979)	Overall disclosure score based on Ernst and Ernst	ROE 1964-1974	Size	450 of 1974 Fortune 500 firms	No Relationship
Freedman and Jaggi (1982)	Quantity and quality of pollution disclosure in annual reports of 10K	ROA, ROE, Cash flow/A, Cash flow/E, EBIT/A, EBIT/E, 1973-1974	None	109 firms of pollution intensive industries	No Relationship
Freedman and Jaggi (1988)	Pollution Disclosure index	ROA, ROE, Cash Flow/A, Cash Flow/E, EBIT/A, EBIT/E	None	1973-1974 annual statements and 10K's	No Relationship prior to adjusting for industry size
Negative relationship					
Chen and Metcalf (1980)	CEP pollution performance index	ROE, P/E ratio, total risk, beta 1968-1973, 1969-1971, 1971-1973	Size	18 firms from the paper and pulp industry included in the CEP survey	Negative
Shane and Spicer (1983)	CEP pollution performance index	Standardised abnormal mean-adjusted daily return for 6 days around release date of Council of Economic Priorities study	Cross-Sectional correlation	72 of 103 firms from CEP sample	Negative Relationship

Table 4.5
Summary of Findings Of The Relationship Between Social
Responsibility Reputation/ Performance/Disclosure and Economic
Performance (continued)

Positive relationship					
Anderson and Frankle (1980)	Overall disclosure and types of disclosure based on Ernst and Ernst	Monthly return differences 7/1972-6/1973	Beta (iso-beta portfolios)	314 of 1972 Fortune 500 firms	Positive Relationship
Belkaoui (1976)	Pollution Disclosure in Annual Reports	Monthly average residuals, 12 months prior and after disclosure	None	50 firms with and without disclosure in 1976	Positive but temporal relationship
Bowman (1978)	Percent of prose in annual reports	ROE 1972-1974	None	46 firms from electric computing industry	Positive Relationship
Cochran and Wood (1984)	Moskowitz's 1972, 1975 Reputational Scale	Operating Earnings/ sales, Operating Earnings/Assets, Excess Market Valuation 1970-1974, 1975-1979	Asset age, and Asset turnover	39 firms in 29 industries compared against industry control group	Positive Relationship
Freedman and Jaggi (1988)	Pollution Disclosure index	ROA, ROE, Cash Flow/A, Cash Flow/E, EBIT/A, EBIT/E	None	1973-1974 annual statements and 10K's	Positive Relationship after industry and size adjustment
Fry and Hock (1976)	Quantity of Disclosure in Annual reports	Earnings	Size, Industry Image	135 firms from 15 industries	Positive Relationship

Table 4.5
Summary of Findings Of The Relationship Between Social
Responsibility Reputation/ Performance/Disclosure and Economic
Performance (continued)

Griffin and Mahon (1997)	Fortune reputation survey TRLindex KLD index Corporate Philanthropy	ROA ROE ROS-5 year Asset age Total assets	None	1992 Fortune Survey	Positive relationship
Herremans and Akathaporn (1993)	Fortune 500 Corporate reputations	Operating Margin, net margin, ROA, ROE	Industry, firm size and leverage	21 Fortune 500 manufacturing firms, 1982-87	Strong Positive Relationship
Ingram (1978)	Various disclosures in annual reports	Monthly portfolio returns 9 months prior and 3 months after fiscal year end	Earnings, year, industry, beta time	287 of 1970-1976 Fortune 500 firms	Positive relationship subject to segmenting companies
McGuire, Sundgren and Schneeweis (1988)	Corporate reputation	ROA, Total Assets, sales growth, asset growth, operating income growth.	Firms size, Leverage, Alpha risk	Fortune 500 companies, 1983-1985	Positive Relationship
Preston and O'Bannon (1997)	Fortune Survey	ROA ROE ROI	None	67 companies over an 11 year period 1982-1992	Positive relationship
Preston (1978)	Quantity of Disclosure in 2 years between 1971 and 1975	ROE 1975	None	fortune 500 firms	Weak, Positive Relationship
Spicer (1978)	CEP pollution performance index	ROE, P/E ratio, total risk, beta 1968-1973, 1969-1971, 1971-1973	None	18 firms from the paper and pulp industry included in the CEP survey	Positive but size related
Waddock and Graves (1997)	KLD Index	ROA ROE ROS	Size, Risk and Industry	Standards and Poors 500.	Positive relationship when using Good Management Theory

Moreover, whether there was a simultaneous operation of the two-way action (Waddock and Graves, 1997). Waddock and Graves (1997) refer to this simultaneous and interactive impact as a “virtuous circle.” The link may run from economic performance to social performance on the one hand or/and social performance to economic performance on the other.

The inconsistency in results of the relationship between social responsibility and economic performance, noted in Table 4.5, may be also be due to misspecification of the proxy variables for social responsibility and/or the employment of differing methods in measuring economic performance. From Table 4.5 some studies have been identified as having used accounting variables for economic performance (Bowman, 1978; Cochran and Wood, 1984; Freedman and Jaggi, 1982; Preston, 1978), whereas others used market variables (Anderson and Frankle, 1980; Belkaoui, 1976; Ingram, 1978; McGuire, et al. 1988). Cochran and Wood (1984), included small sample size and control groups and inadequate time periods as reasons for inconsistencies. Furthermore, limitations may apply to studies which assumed that capital markets are efficient (e.g., Ingram, 1978) and that the Capital Asset Pricing Model applies (e.g., Anderson and Frankle, 1980).

A closer examination of the results of the foregoing empirical research studies indicated that there are various ways of identifying social responsibility which included ratings, reputations and social disclosures. When a review was made of a more recent study that considered the relationships, illustrated in Table 4.5, reference was made to corporate social performance as capturing all social responsibility activities (Griffin and Mahon, 1997).

4.5 Using Social Responsibility Disclosure When Referring to Stakeholder Concerns: A Review of Prior Research of Relationship between Economic Performance and Social Performance

On closer analysis of the relationship between economic performance and social responsibility of a corporation, the interchangeability of the terms social disclosure and social performance was identified. When Griffin and Mahon (1997: 8-9) produced their own analysis of past studies in “Table 1, Correlations Between Corporate Financial Performance and Corporate Social Performance”, they summarised these studies into positive, no effects/inconclusive and negative categories. The information contained in Table 4.5 was used to produce another Table 4.6 but separating the three social performance forms used by Griffin and Mahon (1997) which included collectively social responsibility disclosures, reputations and ratings. Only those studies used by Griffin and Mahon (1997) were used in Table 4.6 as they contain this collection of terms in a common way to reflect social performance. The importance of Table 4.6 was to illustrate the commonality of these three different forms, which Griffin and Mahon (1997) refer to collectively as social performance. The current study did not refer to social disclosure as a form of social performance but suggested social disclosure as an important measure of stakeholder concern amongst social reputation and ratings. Table 4.6 analysed the interchangeability of social disclosure, reputation and rating when referring to social performance. As a result of this interchangeability, social disclosures can be viewed as one important way of identifying stakeholder groups.

Following the conclusions derived from Table 4.6 the current study used social disclosure as a medium for stakeholder concerns. The issue of utilising social disclosures themes to identify stakeholder groups is a development of this section of the chapter and will be further considered when determining measures of stakeholder concerns in Chapter Six.

Table 4.6
Identifying a Portfolio of Social Performance Forms: Utilising Studies
of the Relationship Between Corporate Economic Performance and
Corporate Social Responsibility

Study	Social Respons.	Social Performance Form (1,2,3)			Results
		1. Social Disclosure	2. Social Reputation Index	3. Social Ratings	
Abbott and Monson (1979)	Overall disclosure score based on Ernst and Ernst	Social Disclosure measures			No Relationship
Freedman and Jaggi (1982)	Quantity and quality of pollution disclosure in annual reports of 10K	Social Disclosures in annual reports			No Relationship
Freedman and Jaggi (1988)	Pollution Disclosure index		Social Disclosure Index		No Relationship prior to adjusting for industry size
Chen and Metcalf (1980)	CEP pollution performance index		Pollution Performance Index		Negative
Shane and Spicer (1983)	CEP pollution performance index		Pollution Performance Index		Negative Relationship
Anderson and Frankle (1980)	Overall disclosure and types of disclosure based on Ernst and Ernst	Social Disclosure based on Ernst and Ernst study			Positive Relationship
Belkaoui (1976)	Pollution Disclosure in Annual Reports	Pollution category of social disclosures			Positive but temporal relationship
Bowman (1978)	Percent of prose in annual reports	Social Disclosure in Annual Reports			Positive Relationship

Table 4.6
Identifying a Portfolio of Social Performance Forms: Utilising Studies
of the Relationship Between Corporate Economic Performance and
Corporate Social Responsibility (continued)

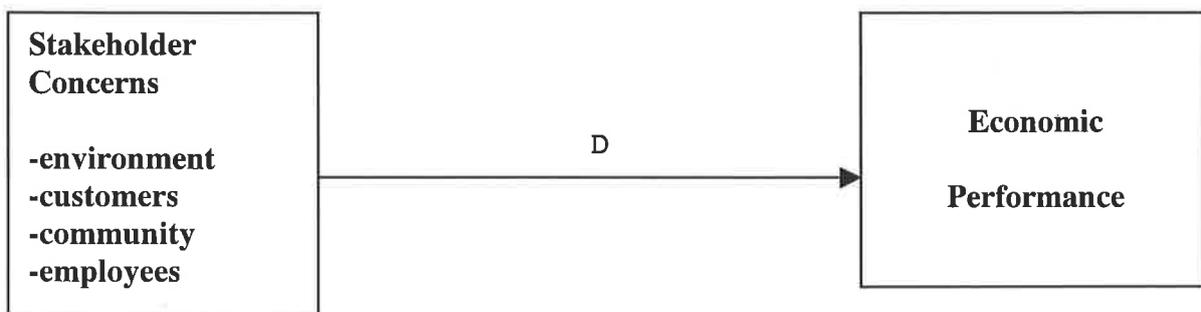
Cochran and Wood (1984)	Moskowitz's 1972, 1975 Reputational Scale		Moskowitz reputation scale		Positive Relationship
Freedman and Jaggi (1988)	Pollution Disclosure index		Pollution disclosure index		Positive Relationship after industry and size adjustment
Fry and Hock (1976)	Quantity of Disclosure in Annual reports	Social responsibility Disclosure in annual reports			Positive Relationship
Griffin and Mahon (1997)	Fortune reputation survey TRIindex KLD index Corporate Philanthropy		Fortune reputation survey TRI Index, KLD index, corporate Philanthropy		Positive relationship
Herremans and Akathaporn (1993)	Fortune 500 Corporate reputations		Reputation index		Strong Positive Relationship
Ingram (1978)	Various disclosures in annual reports	Social Disclosure in Corporate Annual reports			
McGuire, Sundgren and Schneeweis (1988)	Corporate reputation		Corporate reputation		Positive Relationship
Preston and OBannon (1997)	Fortune Survey		Fortune Survey		Positive relationship

Table 4.6
Identifying a Portfolio of Social Performance Forms: Utilising Studies
of the Relationship Between Corporate Economic Performance and
Corporate Social Responsibility (continued)

Preston (1978)	Quantity of Disclosure in 2 years between 1971 and 1975	Social Disclosures in Corporate annual reports			Weak, Positive Relationship
Spicer (1978)	CEP pollution performance index		Pollution performance index		Positive but size related
Waddock and Graves (1997)	KLD Index		KLD Index		Positive relationship when using Good Management Theory

When social responsibility disclosure is further considered in the current study use will be made of it as a form of stakeholder concern. Linking stakeholder concerns with economic performance is illustrated by the flow diagram in Figure 4.1 below.

Figure 4.1
Relationship between Economic performance and Stakeholder
Concerns



4.6 Linking Stakeholder Concerns to Social Responsibility Reporting

An earlier study which analysed previous research of the relationship between economic performance and social responsibility disclosure suggested that these relationships are indeed ambiguous and what should be analysed was the missing element of strategy (Ullmann, 1985). The inclusion of strategy referred to a concern for stakeholders (Ullmann, 1985). It was this concern for stakeholders and more particularly the way that stakeholders were managed which is of importance to this section of work. The inclusion of strategy as a variable was also suggested by Bowman and Haire (1975) who identified an inverted U shaped correlation between social reporting and economic performance indicating that managers strategy involved resource allocation. The results of Bowman and Haire's (1975) investigation were also supported subsequently by Mintzberg's (1983) study. Thompson (1967) argued that firms are selective about the stakeholders they take into consideration as well as the actions they undertake to achieve an optimal relationship with them. On the other hand Pfeffer and Salancik (1978) suggested that the stakeholders' importance derives from their power to control resources required by the company. Ullmann (1985) suggested that, as a result of wide ranging demands, different strategies can be observed. These strategies range from avoiding the stakeholders' demands to partial or total fulfilment of them. In this context social responsibility disclosure was viewed as a strategy for dealing with stakeholder concerns.

This link between social responsibility disclosure and stakeholder concerns was further considered by Roberts (1992) who utilised Ullmann's (1985) framework and stakeholder theory. Roberts (1992), amongst other relationships tested, considered the association between economic performance and social disclosure and recommended that studies of this kind be more stakeholder oriented. From the results of his study Roberts (1992) provided support for the argument that social responsibility disclosures be viewed as a

way that firms manage creditor stakeholders, government stakeholders, community service stakeholders (through philanthropic contributions) and special interest group stakeholders. Roberts (1992) found statistically significant links between social disclosure and social activity.

Furthermore, Gray et al (1995a) supported the view that concern for stakeholders were important for the continuing existence of the firm and linked social responsibility disclosures of firms with stakeholder concerns:

The more powerful the stakeholders the more the company must adapt. Social disclosure is thus seen as part of the dialogue between the company and its stakeholders and, as Roberts (1992) observes, CSR (Corporate Social Reporting) has been a relatively successful medium for negotiating these relationships (Gray et al. 1995a: 53).

Moreover, the results supported the use of social responsibility disclosures as a medium for stakeholder concerns. This outcome also matched the findings of Adler and Milne (1997) in a New Zealand study that also suggest that social responsibility disclosure acts as a medium for stakeholder management:

Corporations make social disclosures not just in their own self-interests, but because they are under pressure from employees, customers, the general public and other social activist groups to exhibit social responsibility. Such disclosures can be viewed as a medium for managing (negotiating or manipulating) stakeholders without whose support and approval the organisation would no longer exist (Adler and Milne, 1997: 4).

In a recent study Waddock and Graves (1997) developed a link between social performance and stakeholder management when analysing the relationship between social responsibility reporting and economic performance, in which they used two named theories to contrast and empirically test the relationship. These named theories were referred to as the Slack Resource Theory (SRT) and the Good Management Theory (GMT) (Waddock and Graves, 1997). The first of these, the SRT, proposed that higher

economic performance of a firm provides the available slack resources (financial or other) enabling the firm to invest in social responsibility domains, such as improving employee relations, environmental matters and community relations. Researchers in sympathy with the SRT argued that when slack resources become available then this facilitates higher levels of social responsibility as a result of allocating of those resources into social domains. The resultant relationship implied that better economic performance improves the level and extent of social responsibility activity (Waddock and Graves, 1997). On the contrary, in the second of the named theories, the GMT proposed that there is a positive relationship between good management practices and social responsibility reporting. It was argued that attention to social responsibility domains improves relationships with key stakeholders. This in turn resulted in higher economic performance. Waddock and Graves (1997) provided a useful explanation of this relationship:

good employee (including women and minorities) relations might be expected to enhance morale, productivity, and satisfaction. Excellent community relations might provide incentives for local government to provide competition-enhancing tax breaks (Waddock and Graves (1997: 307).

Waddock and Graves (1997) arrived at the opposing outcomes of the SRT and GMT termed the “virtuous circle” argument as the most preferred approach as it was a holistic approach. Tests can be done with economic performance as the dependant variable in the first instance and then with social responsibility performance as the dependent variable, hence consideration can be given to both directions then interpretations can be made of these tests. Waddock and Graves (1997: 314) referred to “meeting stakeholders expectations as becoming increasingly important” and they refer to a variety of stakeholders. In referring to stakeholders they linked this to the definition of social performance and further suggest that what should be further considered is the relationship between stakeholder relations in the link to economic performance.

4.7 Evidence of an Inverted U-Shaped relationship between Economic Performance and Stakeholder Concerns

From an analysis of literature there seemed to be sparse empirical research which considered the nature and form of various levels of social disclosure on economic performance. Studies have assumed linearity except Bowman and Haire's (1975) and recently Griffin and Mahon's (1997) study. These two studies divided social responsibility disclosure into two or more subgroups. The usefulness of dividing stakeholder management into subgroups of low/moderate and high was investigated in this section of the chapter and further reference will be made to these two studies for support.

What Bowman and Haire (1975) tested was the relationship between corporate social responsibility and profit performance. In measuring the amount of social responsibility of the firms, use was made of the proportion of lines of prose in annual reports which was devoted to social responsibility activities. The annual report was considered to be a medium to communicate socially responsible behaviour, but Bowman and Haire (1975) also considered the Moskowitz (1973) list of fourteen firms identified as showing outstanding reputations in terms of their responsibility in the public interest. By extending the method to include the Moskowitz reputational index the result was a sample of only responsible firms which were classified as the premier group. Then Bowman and Haire (1975) took, at random, a neutral control set for comparison to match with the premier groups. The outcome showed that firms which did behave in a socially responsible manner were those which disclosed it in their corporate annual reports. The Moskowitz reputation ratings were not necessarily a superior method of identifying socially responsible firms over the social disclosure method. This provided support for

the use of content analysis of prose in the corporate annual reports as an appropriate measure of socially responsibility behaviour.

Bowman and Haire (1975) identified that by dividing the data set into low, medium and high disclosure devoted to social responsibility behaviour, finer and more revealing results can be obtained. What they discovered was that a medium level of responsibility activity level was more closely associated with high profitability than was either low or high levels. This provided evidence of an inverted U-shaped curve for the relationship between social responsibility disclosure and economic performance. The issue of how much social responsibility is enough was considered, suggesting that there exists a cut off point beyond which it may not be necessarily profitable. Bowman and Haire (1975: 49) refer to “going beyond the point of doing what is required” and suggested that the mean amount of social disclosure was golden. It was interpreted from the mean position that “it pays to be good, but not too good” Mintzberg (1983: 7). It was interesting to note that the most profitable firms were the low to moderate level or least responsible and did not lie near the mean (Mintzberg, 1993).

More recently Griffin and Mahon (1997), developed a matrix to analyse the relationship between economic performance and social responsibility. In doing so they made a distinction between low and high social performance and also made a distinction between low and high financial performance. From these divisions Griffin and Mahon (1997) suggested that overall there was a positive relationship between economic performance and social performance. More specifically there was no relationship between low performance and high social performance. On the other hand firms in their study with low financial performance still managed to exhibit some level of responsibility. What Griffin and Mahon (1997) did not address ,as it was beyond the scope of their study, was the effects of low/moderate versus high levels of social responsibility on economic

performance. The issue of linearity in the relationship between stakeholder concerns and economic performance was one that could reveal important and interesting results of the relationship between stakeholder concerns and economic performance.

4.8 Summary

In conclusion, in determining stakeholder concerns, Australia has no KLD ratings, or Moskowitz reputation index to help identify stakeholders as some American studies have the privilege of using. A shortfall of accessible databases leaves Australian researchers with the only viable option of identifying stakeholder concern being the use of social disclosures in corporate annual reports. Reliance was placed on analysing of the content of social responsibility disclosures themes, in these reports, to identify the stakeholder concerns. A link between social responsibility disclosure themes and stakeholder groups was established. This permits a way of identifying stakeholder concerns from social responsibility disclosure in Australian corporate annual reports.

The chapter has provided evidence of a move to a concern for stakeholders when investigating economic performance. An analysis of past research provided support for this move, and that consideration be given to stakeholder concerns when investigating economic performance. Furthermore, when testing the relationship between economic performance and stakeholder concerns linearity should not be assumed but consideration given to the possibility of a cut off point separating low and high levels of stakeholder management. Statistical tests could be used to determine the existence of any difference between each of these levels of stakeholder concern on economic performance. Moreover, division of stakeholder management into low to moderate and high levels subgroups may also reveal an inverted U-shaped curvilinear relationship between

economic performance and stakeholder management as was the case for Bowman and Haire (1975), but in an Australian context.

CHAPTER FIVE

A SOCIOECONOMIC THEORETICAL FRAMEWORK FOR INVESTIGATING ECONOMIC PERFORMANCE

5.1 Introduction

Chapter One identified the purpose of this research study as investigating whether strategic and international business diversification with stakeholder concerns enhances economic performance. It identified the need to develop a socioeconomic framework, which incorporates transactions cost, resource-based and instrumental stakeholder theory, for investigating economic performance. Chapter Two developed a socioeconomic model examining the effect that strategic management, international business diversification and stakeholder concerns has on economic performance. Chapter Three examined the relationship between business-level diversification strategy and economic performance, the interaction of international diversification with business-level diversification on economic performance. Then an analysis of the interaction of multinationality with country scope on economic performance was considered. The importance of transaction costs effects on this relationship was then examined providing evidence of a non-linear relationship between international diversification and economic performance. Chapter Four examined the relationship between stakeholder management and economic performance. The chapter provided evidence to support using social responsibility disclosures themes from corporate annual reports as a way of identifying stakeholder concerns and that these concerns are positively related to economic performance.

This chapter developed a socioeconomic theoretical framework for investigating economic performance. The various multidisciplinary determinants of economic performance that the study investigated include business level diversification strategies,

international diversification strategies and stakeholder concerns of firms. The investigation of economic performance in the current study extended beyond the contractual arrangement between the firm and stockholders and includes the effects of a variety of stakeholders. Critical stakeholders who may have an effect on economic performance included employees, customers, communities and the environment.

The first section of this chapter analysed a multiparadigm approach to investigating economic performance. This is followed by a conceptual view of strategic management and international business management perspective's, with a focus on the interaction of business level and international diversification on economic performance, as an economic perspective. Resource based and transaction cost theory are introduced to help explain the relationship between business-level diversification and economic performance as well as the relationship between international diversification and economic performance. The effects of transaction costs theory in explaining the non-linear relationship between multinationality and economic performance are examined. The next section of the chapter specifically analysed the need for broadening the scope of economic performance investigations to also include stakeholder concerns. The stakeholder concept was then analysed and how this justified consideration of instrumental stakeholder theory when investigating the relationship between stakeholder concerns on economic performance. A section that integrated the theoretical domains, which included resource-based theory, transaction costs theory and instrumental stakeholder theory in developing a socioeconomic framework to investigate economic performance, then follows this. The final section developed the hypotheses for testing driven by the socioeconomic framework.

An investigation of this nature, which included the concern of stakeholders together with stockholder concerns has been supported in past research (Collins and Porras, 1995; Jones, 1995; Waddock and Graves, 1997, 1999). The integrative approach was useful as:

our knowledge of firm performance is greatly enhanced by our study of multiple paradigms, (Hansen and Wernerfelt, 1989: 399).

companies are responsible for a variety of stakeholders who have vested interests in the performance of the firm and whose company activities have an impact. ...a focus shifts attention away from discretionary activities ...towards a range of critical stakeholder relations ...including relationships with employees, customers, communities, and the environment as well as shareholders or owners (Waddock and Graves, 1997: 253).

In order to build a socioeconomic framework for the current study, extant theories from several disciplines were utilised. The economic perspective included international business and strategic management, together with specific theoretical domains in transaction cost theory and resource-based theory of the firm. In expanding the investigation of performance to include a range of critical stakeholders, use was made of stakeholder theory of the firm with specific consideration of instrumental stakeholder theory. This then broadened the framework to include social issues in management, thereby including a second stream, that of stakeholder concerns, when investigating economic performance (Waddock and Graves, 1997).

The idea of a socioeconomic approach came from Etzioni (1988) where it was suggested that human beings behaviour was not entirely based on a complete disregard of the well-being of others. Etzioni (1988) recommended that a call be made for a "socioeconomics" to supplement or displace the traditional neoclassical economic theory to include a wide range of human behaviour. Jones (1995) provided a partial response to the recommendations of Etzioni (1988) by introducing instrumental theory where:

The instrumental theory presented here is a partial response to Etzioni's challenge; it claims that the manifestations of certain types of ethical behaviour will result in competitive advantage (Jones, 1995: 421).

5.2 Broadening the Scope of Investigating Economic Performance: A Multiparadigm Approach

It has been recognised for some time that the scope of management research should be broadened beyond traditional positivist investigations with its technical-efficiency focus to include social and political phenomena (Cooper, 1980; Tinker, 1980). When a paradigm was limited in its empirical scope and was used to formulate theories and policies the study of our world will suffer. The current section argued that the economic paradigm (which includes strategic management theory) could be integrated with a stakeholder concept (which includes stakeholder theory of the firm) in developing a socioeconomic framework that has the potential to be more explanatory and predictive than a purely economic paradigm. This integrated framework included existing strategic management literature, existing international business literature, existing stakeholder literature and existing social responsibility literature.

Multiparadigm Approach: A problem with a single dominant view

Traditional strategic management theory approach to studying managerial behaviour to economic performance have tended to produce valuable, but nonetheless incomplete views of knowledge, mainly because they have been predicated predominantly on the tenets of one major paradigm or way of understanding organisational phenomena (Gioia and Pitre, 1990). This narrow view has been noted : "the use of any single research paradigm produces too narrow a view to reflect the multifaceted nature of organisational reality" (Gioia and Pitre (1990: 584).

In developing a socioeconomic framework the valuable contribution made of strategic and international business management theory was acknowledged, together with instrumental stakeholder theory. Given that a unique correct perspective cannot exist (Bochner, 1985) and given the multiplicity of organisational realities, a multiparadigm, which takes account of different views (for instance economic and stakeholder) becomes a necessity for achieving a comprehensive view (Gioia and Pitre, 1990). Such a multiparadigm requires that researchers consider the theories relevant to a given topic from some viewpoint beyond that of an individual paradigm.

5.3 Resource-Based and Transaction Cost Theory: Theoretical Issues for examining the Relationships of Diversification on Economic Performance:

In the current section the influence of diversification on economic performance referred to the following three relationships: (1) business-level diversification on economic performance; (2) international diversification on economic performance; (3) interaction between international and business-level diversification on economic performance. Resource based and transaction cost theory of the firm was used to examine these relationships

5.3.1 Resource-Based Theory

Business-level diversification on Economic Performance

The study of the relationship between business-level strategy of a firm and economic performance was not new (Chandler, 1962; Robins and Wiersema, 1995; Rumelt, 1974).

The theoretical issue related to these relationships have been previously considered:

The relationship between the composition of a corporation's business portfolio and the firm's economic performance has become a particularly prominent issue in strategic management theory in recent years with the development of the resource-based view of the firm. (Robins and Wiersma, 1995: 277)

The relationship between business-level diversification in a single firm and economic performance has been a part of the development of the resource-based view of the firm (Barney, 1991; Robins and Wiersema, 1995; Wernerfelt, 1984). The rationale behind resource-based strategy is that multibusiness firms benefit from the sharing of strategic capabilities between the businesses within that firm (Mahoney and Pandian, 1992; Peteraf, 1993; ; Robins and Wiersema, 1995; Teece, 1982; Teece, Pisano and Schuen, 1990). Firms gained as a result of sharing resources and gained the benefits of scope economies as a result of portfolio business composition.

The resource-based theory of the firm “argues that strategic interrelationships amongst businesses have a direct positive effect on firm performance” (Robins and Wiersema, 1995: 279). The performance effect of business-level diversification is of importance to the current study and the resource-based theory is helpful in explaining the economic performance of related diversified versus unrelated diversified firms (Mahoney and Pandian, 1992). There have been mixed results in support of related business level diversification favoured over unrelated business diversification in their relationship to economic performance. There are more studies that support the related diversification economic performance relationship than that involving unrelated diversification (Rumelt, 1974; Simmonds, 1990). Empirical studies, previously considered in Chapter Three, have provided evidence that related diversification have an advantage over unrelated diversified firms, regarding their effect on economic performance, which can be explained using resource-based theory.

International Diversification and the Interaction of Business-level and International Diversification on Economic Performance

The previous section has reported the usefulness of resource-based theory in examining the relationship between business-level diversification and economic performance. The

current section, that considered the level of international diversification of a firm and how this effected economic performance, will refer to the appropriateness of resource-based theory of the firm. International diversification provided more of an opportunity for firms to utilise the benefits of economies of scale such as greater efficiency and improved competitive advantage by utilising the opportunities coming from market imperfections in particular national resources which was explained in terms of resource-based theory (Hitt et al. 1997).

Furthermore, the interaction between business-level and international diversification on economic performance can also be examined from a resource-based view of the firm as synergies and benefits exist from business diversification to trading overseas:

Current research suggests that some firms are simultaneously pursuing both global and product diversification.....corporate strategic decisions are quite complex, and we need a better understanding of the tradeoffs between global and product diversification along with potential synergies between the two strategies” (Hoskisson and Hitt, 1990: 499).

Research analysing the relationships between diversification strategy and economic performance have been examined for a period of over forty years and have gained prominence over the last decade in the strategic management literature (Hoskisson and Hitt, 1990). According to Hoskisson and Hitt (1990) there are a total of three theoretical perspectives related to the relationship between diversification and economic performance.

The first theoretical perspective made the assumption that markets were relatively perfect, where firms within a particular industry were considered homogeneous and so had the characteristic of producing very similar or substitutable products. This was an extremely focused approach which was informed by an "economic theory that generally

assumes that firms are organized with a single product focus and have homogeneous factor markets" (Hoskisson and Hitt, 1990: 462).

The second theoretical perspective recognised that market imperfections did exist and these may create external and internal incentives to diversify. In particular it was assumed that firms exhibited idiosyncratic behaviour which triggered imperfections (Barney, 1986) in particular incentives for diversification which included "low performance and uncertainty of expected future cash flows" (Hoskisson and Hitt, 1990: 462).

The third theoretical perspective was similar to the second perspective but broadened its dimension to include managerial motivation in analysing increase in firm diversification. This perspective was informed by agency theory which assumes self interest of managers in a contractual arrangement with shareholders. The current study utilised the second theoretical perspective "diversification and performance under assumptions of market and firm imperfection" (Hoskisson and Hitt, 1990: 471).

Most recently, Hitt et al. (1997: 767) had suggested that "both international and product diversification play key roles in the strategic behaviour of large firms". Prior research in the relationship between business level diversification (sometimes called product diversification) and economic performance has been inconclusive (Hoskisson and Hitt, 1990). Similarly, examining the relationship between international diversification and economic performance has provided somewhat mixed results (Geringer et al. 1989; Hitt et al. 1997; Rugman, 1979). Hitt et al. (1997) has identified this problem and argue that the result of these mixed outcomes was due to the complexity of the issue which was not reflected by the theoretical framework and methods of research that have been previously used. From these arguments, what was identified was that several internationally oriented firms are also diversified at a business level. There was a suggestion that a firm

which is diversified at a business level moderates the relationship between international diversification and economic performance (Hitt et al. 1997). Then what follows from this moderating effect was the need to examine a more inclusive theoretical framework, which examined both these interactions. This framework included theories from both strategic management and international business which included, resource-based view of the firm and transactions costs (Hitt et al. 1997).

Firms which diversified on an international level utilised their core competencies or internal resources and capabilities to take advantage of opportunities available across global geographic scope and regions reflecting “the resource based view of the firm” (Hitt et al. 1997: 769). As international firms further diversify they experienced increasing transaction costs. These transaction costs included costs of coordinating between business units between different geographic markets. There will be a point where multiple transactions among geographical markets cost more than the benefits derived from sharing resources, exploiting market opportunities and benefits of economies of scope. The net effect of transaction costs is to create diminishing returns to international diversification which results in an inverted U-shaped curvilinear relationship (Hitt et al. 1997).

Hitt et al. (1997) suggested that business-level diversification strategy plays a moderating role in the international diversification and economic performance relationship. Initially business-level diversification positively moderates the relationship between international diversification and economic performance. This moderation effect of business-level diversification can be explained in terms of a resource-based theoretical perspective. It can be argued that corporations which have experienced business-level diversification in the past are effective, because of the issue of resourcing, and capable of expanding into international markets.

Resource-based theory of the firm reflected an organisation's ability to exploit the benefits of internalisation. Internalisation referred to performing many activities internally (Rugman, 1981). The benefits of performing internally are many and may include:

economies of scale, scope, and learning (Kogut, 1985), exploiting the relationships among business segments and geographical areas (Porter, 1985), sharing distinctive firm capabilities or core competences across business units (Hamel, 1991; Porter, 1990) and exploiting differences in factor markets (Porter, 1990) (Hitt et al. 1997: 771).

Using integrative business level and international business level diversification firms which already have proven core competencies (which have been the result of their well developed home market activity) can pass these proven competencies to their international markets (Bartlett and Ghoshal, 1989; Hitt et al. 1997). If a firm then was profitable in the home market, as a result of gains from these characteristics, then it seems reasonable to suggest that they can apply this level of confidence in competitiveness and competency into their international activities which could further improve their economic performance (Porter, 1990).

It was this primary argument regarding the benefits of capitalising on internalisation that provided the basis for a resource-based view of the firm, which was well documented in Hitt et al. (1997). In designing their conceptual framework Hitt et al. (1997) also included the effects of transactions costs when considering resource based view of the firm from an analysis of past research that tested the relationship between international diversification effects on firm performance in product diversified firms. Transactions cost theory helped to explain the additional costs associated with additional international

diversification beyond a low to moderate level. Transaction costs are further explained in the next section.

5.3.2 Transactions Cost Theory

There was evidence which suggested that firms which diversified internationally incurred significant costs associated with this level of diversification (Hitt et al. 1997). In particular, the greater the number of geographic regions the greater the “coordination, distribution and management costs” (Hitt et al. 1997: 772).

Coordination costs referred to the costs of harmoniously combining economies of scale and scope among the various geographical regions that required distribution of goods or services. In the process of distributing goods and services managers needed to deal with the government regulations and laws pertinent to that geographical region. Moreover, there were also exchange rate currency issues, which added a further cost. Hitt et al. (1997: 772) referred to numerous other transaction costs, which included “trade barriers, logistical costs, cultural diversity, and country differences in such factors as access to raw materials and employee skills”. These transaction costs required much coordination and amount to a significant number of both internal and external transactions with foreign governments, customers and in some cases suppliers (Hitt et al. 1997).

In order to coordinate these many and varied transactions managers needed an appropriate information system. The complexity of cultural diversity, trade barriers and information availability can impair the benefits of transferring competitive advantages from one geographical region to another dissimilar foreign market (Kogut, 1985). Importance was placed on the efficiency of the information system as firms enter different markets with competitors with different market strategies. It was suggested that marketing programs in dynamic global markets require redesign, which also added to the managerial cost of further developing additional international markets (Hitt et al. 1997).

It becomes increasingly costly for firms to progressively diversify internationally as they entail additional transaction costs and the demands placed on managers for more efficient information systems. There comes a point where the costs of progressively diversifying exceed the benefits, in particular economies of scope and scale, which implies a non-linear relationship could exist in the relationship between international diversification and economic performance (Hitt et al. 1997). As suggested by Hitt et al. (1997), the identification and inclusion of transaction costs in the relationship helps to explain the conflicting results of prior research.

In sum using both resource based theory of the firm together with transactions cost theory, researchers can investigate for the possibility of a non-linear relationship (Hitt et al. (1997). The theoretical contribution made by Hitt et al. (1997) which described this relationship has been recently noted:

only one (Hitt et al. 1997) articulated the beginnings of a cogent theoretical rationale behind curvilinearity and offered an empirical approach to test such a relationship (Gomes and Ramaswamy, 1999: 179).

This provided further researchers in the field with a refinement for testing the relationship between international diversification and economic performance. In particular, when investigating the relationship between international diversification and economic performance, low to moderate levels of international diversification can produce profitable results that exceed transactions costs, but beyond a critical cut-off point at a high level of international diversification the costs can exceed the benefits (Geringer et al. 1989; Hitt et al. 1997).

5.4 Stakeholder Theory of the Firm: Instrumental Stakeholder Theory for Investigating the effect of Stakeholder Concerns on Economic Performance

The idea of stakeholders introduced the notion that a firm has a further duty, which goes beyond the fiduciary one to stockholders, to serving society (Freeman and Reed, 1983). Actions taken by management must ultimately be justified by whether or not going beyond the fiduciary duty furthers the interests of the corporation and its stockholders. There has been a departure from the stockholder view to the notion of stakeholders which reflected going beyond the economic perspective (Freeman and Reed, 1983). This stakeholder notion suggested that there were other groups to whom the corporation was responsible in addition to stockholders. These other groups included customers, communities, government, special interest groups, trade associations, foreign competitors, employee rights, equal opportunity and environmental pollution.

Proposing two definitions of Stakeholder

Stakeholders have been previously defined as: “ A stakeholder is an organization is (by definition) any group or individual who can affect or is affected by the achievement of the organization’s objectives” (Freeman, 1984: 46). This section of the chapter analysed both the wide and narrow senses of stakeholders (Freeman and Reed, 1983; Mitchell et al. 1997). The wide sense of stakeholder included “any identifiable group or individual who can affect the achievement of an organisation’s objectives or who is affected by the achievement of an organisation’s objectives” (Freeman and Reed, 1983: 91) which may include, employees, communities, environment and customers. On the other hand, the *narrow sense* of stakeholder included “any identifiable group or individual on which the organisation is dependent for its continued survival” (Freeman and Reed, 1983: 91) which may include, employees, product safety, environment and communities.

It is possible that a stakeholder has more than one kind of both stake and power, especially since there are stakeholders who have multiple roles. For instance an employee may be at any one time a stockholder, customer or employee (Freeman and Reed, 1983). It can be said that shareholders and directors have formal or voting power whilst customers, suppliers and employees have economic power and governance and special interest groups have political power (Freeman and Reed, 1983). Of significance was that each organisation will have its own individual stakeholders. This suggests that managers may need to “prioritize stakeholders” or that “managers do pay certain kinds of attention to certain kinds of stakeholders” which has been previously examined and referred to as the theory of stakeholder salience (Mitchell et al. 1997: 855).

Linking Stakeholder Theory to Social Responsibility

Stakeholder management was considered as a way a firm engaged in social responsibilities: “companies manage specific stakeholder relationships as their fundamental way of engaging their social responsibilities” (Bendheim et al. 1998: 308). According to Bendheim et al. (1998), there are key stakeholder domains in community relations, employee relations, environment, customer (product category) and stock holders the first four which also fit the themes of social responsibility disclosure developed in Table 4.2 Chapter Four page 98. Within this stakeholder thinking was the suggestion that firms do “explicitly manage their relationships with different stakeholders” (Bendheim et al. 1998: 306). The themes from prior research into social responsibility are utilised to identify the stakeholders for firms which facilitates the link between stakeholder theory and social responsibility. Ideally access to reputational indexes or corporate ratings would provide a better reflection of stakeholder management, but these do not currently exist in an Australian context. Therefore the next best option of identifying stakeholder management as explained by stakeholder theory of

the firm was to utilise the social disclosures within the firms corporate annual report under the themes developed in Table 4.4. This was the explicit way in which the study links social responsibility reporting with stakeholder theory of the firm.

Stakeholder Theory and Economic Performance

In earlier evaluations of the literature, which examined the relationship between social responsibility reporting and economic performance, Ansoff (1965) was one of the first to use the term "stakeholder theory" in defining the financial objectives of the firm. According to Ansoff (1965) the major objective of the firm was to attain the ability to balance the conflicting demands of various stakeholders in the firm. Freeman (1983), categorised the stakeholder concept into a corporate planning and business policy model which included corporate social responsibility by the way of stakeholder management. Freeman (1983) analysed stakeholder effects on an organisation decisions and saw a significant role for managers in assessing the importance of meeting stakeholders demands in order to achieve strategic objectives of the firm. However, stakeholders were required to have sufficient power in order to influence managers decisions. Without power the stakeholders had no means by which managers decisions could be influenced.

Ullmann (1985) postulated a model, which sought to explain this relationship as it related to stakeholder thinking. Developing a model of social responsibility from Freeman's model, Ullmann (1985) provided a conceptual basis for studying social responsibility activities within a stakeholder framework. He suggested that a stakeholder framework provided an appropriate justification for incorporating strategic decision making into studies of social responsibility activities. In analysing the relationship between social responsibility reporting and economic performance, Ullmann (1985) concluded that the ambiguous results of prior studies suggested that the models might have been

incompletely specified. He suggested that there was a missing element in the relationship between social disclosure and economic performance, namely strategy. Ullmann proposed a contingency framework for analysing levels of social responsibility activity and economic performance based on the stakeholder framework formalised by Freeman (1984).

Instrumental Stakeholder Theory

Ullmann's (1985) approach previously discussed was important in that stakeholder status emerged once again as an issue worthy of further consideration, since Freeman's (1984) landmark publication *Strategic Management: A Stakeholder Approach* (Freeman, 1984). As a result of the evolution of stakeholder theory over the past decade or so, advances have been made of the various ways of describing and using this theory. Three types of uses were identified which include descriptive/empirical, instrumental and normative (Donaldson and Preston, 1995).

Considering the first of these types, the descriptive use of stakeholder theory has been used to describe:

(a) the nature of the firm (Brenner and Cochran, 1991), (b) the way managers think about managing (Brenner and Molander, 1977), (c) how board members think about the interests of corporate constituencies (Wang and Dewhirst, 1992) and (d) how some corporations are actually managed (Clarkson, 1991; Kreiner and Bhambri, 1991) (Donaldson and Preston, 1995: 70).

The second type of use was the normative one. This use was moral and philosophical in nature and provided the firm with suitable guidelines for their operation and management. It has been suggested that normative considerations were the core of classical stakeholder theory issues (Donaldson and Preston, 1995).

On the other hand instrumental use of stakeholder theory involved the identification of linkages between stakeholder concerns and economic performance (Donaldson and Preston, 1995). In the instrumental use of stakeholder theory stakeholders are given some relationship status with managers to achieve firm objectives in the most productive way possible (Donaldson and Preston, 1995). In this way stakeholder theory was linked instrumentally to economic performance:

generated “implications” suggesting that adherence to stakeholder principles and practices achieves conventional corporate performance objectives as well or better than rival choices (Donaldson and Preston, 1995: 71).

Moreover, Donaldson and Preston (1995) further claim that “the stakeholder model ... is seen as essential to successful organisational performance” (Donaldson and Preston, 1995: 79).

The concept of a formal instrumental theory of stakeholder management, was specifically addressed by Jones (1995). Ullmann (1985) recognised that there was no credible theory regarding the relationship between stakeholder management and economic performance. This prompted Ullmann (1985) to refer to past empirical studies testing the relationship between stakeholder concerns and economic performance as “data in search of a theory” (Jones, 1995: 430). However, since Ullmann’s (1985) early work, what has been proposed was that a useful application of instrumental stakeholder theory be considered as :

certain types of corporate social performance are manifestations of attempts to establish trusting, cooperative firm/stakeholder relationships and should be positively linked to a company’s financial performance (Jones, 1995: 430).

In their investigation Bowman and Haire (1975) identified a curvilinear relationship between social responsibility (stakeholder concerns) and economic performance, however there was no cogent theoretical explanation for this outcome. Unlike the relationship between international diversification and economic performance (Hitt et al. 1997), where a transaction cost theory was used to explain the negative slope in a curvilinear relationship, there was no theoretical explanation provided for the negative slope in the relationship between stakeholder concerns and economic performance.

5.5 Proposing a Socioeconomic Framework For Investigating Economic Performance

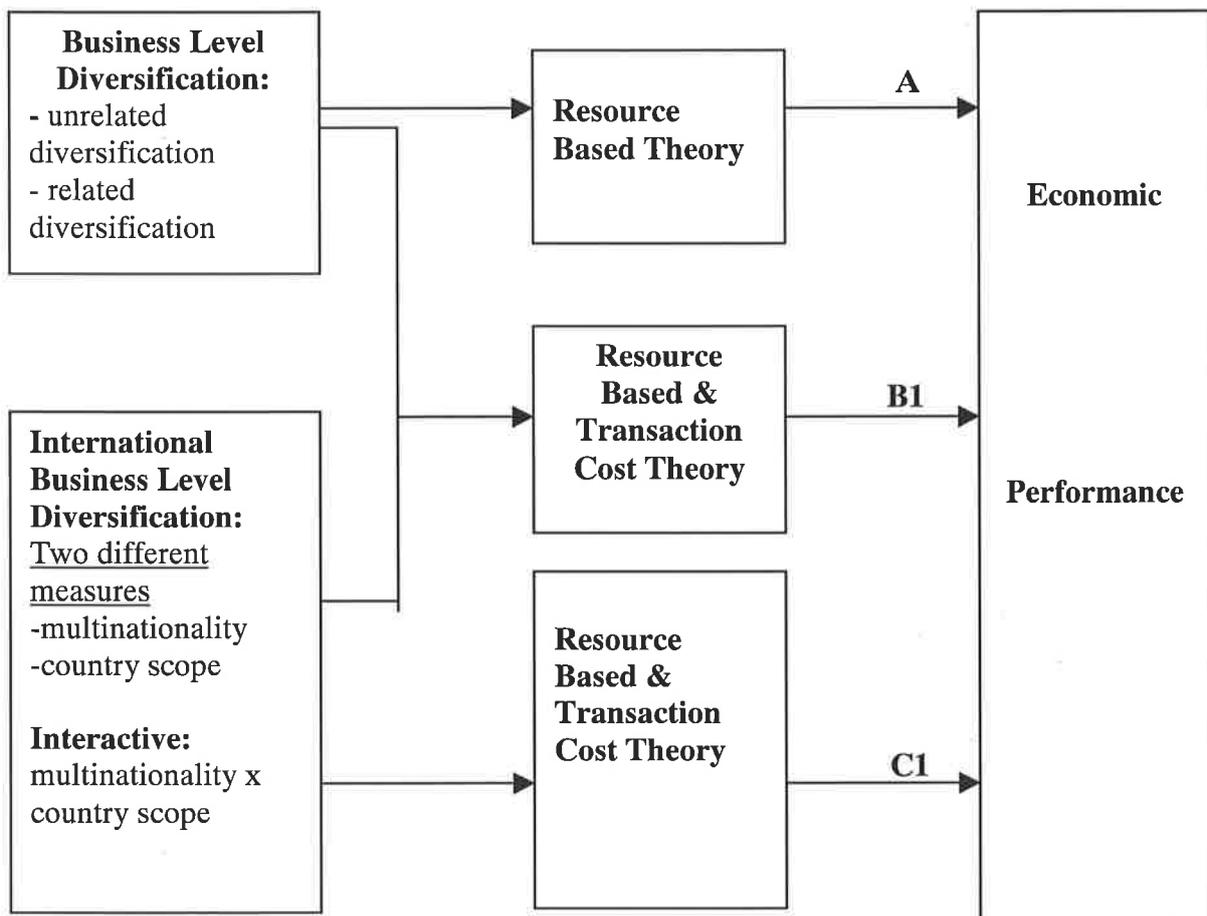
A Socioeconomic framework was developed from the socioeconomic model developed in Chapter Two and utilised extant theory from several disciplines which includes international business and strategic management, together with specific theoretical domains in transaction cost theory, resource-based theory and instrumental stakeholder theory of the firm.

Business-level and International Diversification Strategy on Economic Performance: Theoretical Issues

The first domain was business-level diversification explained in terms of resource-based theory. There was evidence of a positive relationship between economic performance and business-level diversification, refer to A in Figure 5.1 (page 138). Hitt et al. (1997) suggested that business-level diversification strategy plays a moderating role in the international diversification and economic performance relationship refers to B1 in Figure 5.1. Initially business-level diversification positively moderated the relationship between international diversification and economic performance. It was argued that this moderation effect of business-level diversification can be explained in terms of a resource-based perspective. It can be argued that corporations which have experienced

business-level diversification in the past are effective, because of the issue of resourcing and capable of expanding into international markets.

Figure 5.1: Theoretical Issues relating International Diversification to Economic performance Including the Moderating effects of Business level Diversification and the Interactive effects of Country Scope and Multinationality



There were also the interactive effects of multinationality and country scope on economic performance which were considered to be positive and significant (Tallman and Li, 1996). The enhancement of country scope on the relationship between economic performance and multinationality was also reflected by C1 in figure 5.1.

In essence, firms which diversified on an international level utilised their core competencies/ internal resources and capabilities to take advantage of opportunities available across global geographic scope and regions (the resource based view of the firm). As international firms further diversified they experience increasing transaction costs which include, costs of coordinating between business units between different geographic markets. There will be a point where multiple transactions among geographical markets cost more than the benefits derived from sharing resources, exploiting market opportunities and benefits of economies of scope. The net effect of transaction costs was to create diminishing returns to international diversification, which results in an inverted U-shaped curvilinear relationship (Hitt et al. 1997). Non-linear relationships can exist in the linkage B1 and C1 as illustrated in Figure 5.1.

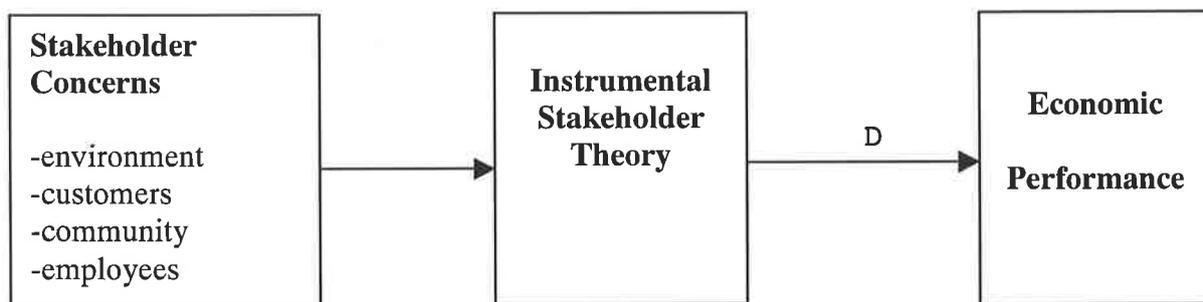
Stakeholder Concerns and Economic Performance: Theoretical Issues

In the second stream the relationship between stakeholder concerns and economic performance can be explained and understood using instrumental stakeholder theory. Figure 5.2 illustrates the link between stakeholder concerns and economic performance indicating instrumental stakeholder theory as the appropriate theoretical issue, in the linkage D.

Prahalad and Hamel (1994) suggested that favourable customer perceptions, about the quality and nature of a firms' products, together with its environmental considerations

and its community related effects become a basis for competition. These positive perceptions of the corporation by various external stakeholders, it was argued, improved economic performance (Waddock and Graves, 1997).

Figure 5.2: Relationship between Economic performance and Stakeholder Concerns: Theoretical Issues



Combining the Two Theoretical Issues

This section combines two theoretical issues first, those issues relating international diversification to economic performance including the moderating effects of business-level diversification and the interactive effects of country scope and multinationality on the one hand and second, theoretical issues relating stakeholder concerns to economic performance on the other

A socioeconomic conceptual framework was developed from these two major issues in strategic management theory and stakeholder thinking using Figures 5.1 and 5.2. From an examination of the strategic management literature there was support for utilising resource-based theory together with transaction cost theory to explain the relationships between business-level diversification and economic performance; international diversification and economic performance; the interaction between business-level

diversification and international diversification and the impact of this interaction with economic performance (Hitt et al. 1997). There was sparse evidence of a non-linear relationship between the international diversification and economic performance variables (Gomes and Ramaswamy, 1999; Hitt et al. 1997). When consideration was given to stakeholder management there may also be a non-linear relationship between economic performance and stakeholder management as has been previously identified (Bowman and Haire, 1975; Griffin and Mahon, 1997).

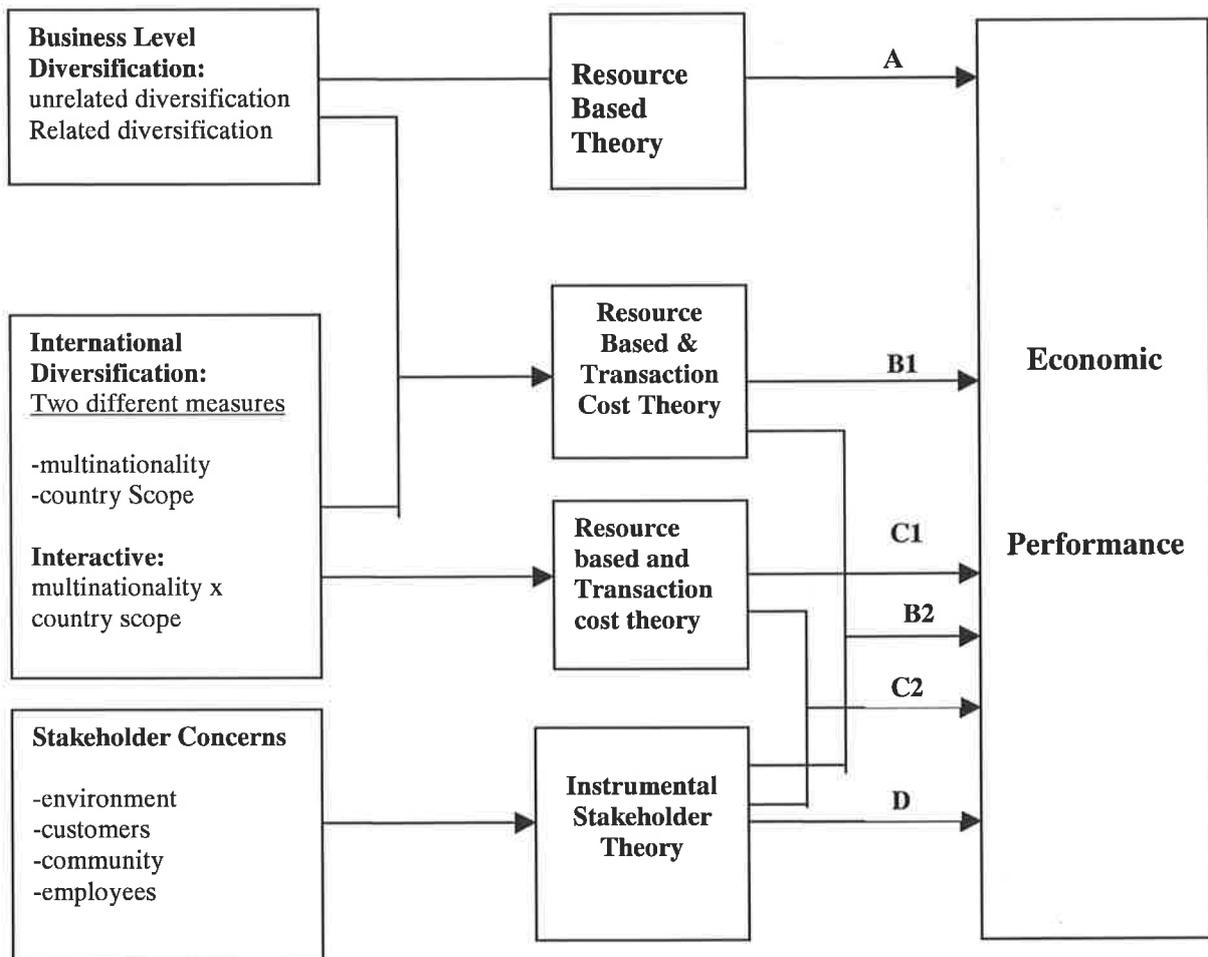
In combining the two theoretical issues mentioned above, the effect of both stakeholder concerns and international /business-level diversification on economic performance can be examined using the following conceptual socioeconomic theoretical framework illustrated in Figure 5.3 where:

- A refers to the relationship between business level diversification and economic performance.
- B1 refers to the relationship of the interaction of business level diversification (unrelated and related) and multinationality on economic performance. Evidence suggests non-linear or an inverted U-shaped relationship may exist.
- B2 refers to the effect of a combined business and international business diversification with stakeholder concerns on economic performance.
 - related diversification x multinationality + stakeholder concerns on economic performance.
 - unrelated diversification x multinationality + stakeholder concerns on economic performance.
- C1 refers to the relationship of the interaction of multinationality and country scope on economic performance. Also to the relationship between multinationality and economic performance. Evidence suggests non-linear or an inverted U-shaped relationship may exist.
- C2 refers to the effect of a combined international business diversification with Stakeholder concerns on economic performance.
 - multinationality + stakeholder concerns on economic performance.
 - country scope + stakeholder concerns on economic performance.

- multinationality x country scope + stakeholder concerns on economic performance.
- D refers to the relationship between stakeholder concerns and economic performance. Some evidence suggests non-linear / inverted U-shaped relationship may exist.

Figure 5.3: Socioeconomic Theoretical Framework

Combined effects of International/ Business-level Diversification and Stakeholder Concerns on Economic Performance:



5.6 Hypotheses Development

The following research questions and hypotheses were developed for this study. They were developed from the socioeconomic framework formulated in this chapter illustrated in Figure 5.3. Hypotheses, which follow research questions, are developed in the first instance on the following three linkages of a socioeconomic orientation on economic performance: (1) business-level diversification strategy and economic performance (2) international diversification and economic performance; and (3) stakeholder concern and economic performance. Past research, which has tested these individual linkages, is plentiful, but only within each paradigm. There was sparse research involving the combined interaction of business-level and international diversification strategy and their effect on economic performance (Geringer et al. 1989; Hitt et al. 1997; Tallman and Li, 1996). The combined interactions will comprise a fourth linkage for hypothesis development. Furthermore, there appeared no evidence in past research of effects on economic performance of a combination of both stakeholder concerns and the interaction of the combined effect of business level and international diversification strategy making for a fifth linkage for hypothesis development.

5.6.1 Business-Level Diversification Strategy and its relationship to Economic Performance

RQ 1: Do firms pursuing related diversification perform better than those firms pursuing unrelated diversification?

The effect of diversification strategy on economic performance has been a key consideration for strategic management researchers for over three decades (Chandler, 1962) (refer to Chapter Three Table 3.1). The direct link between related diversification and economic performance emerged as a key issue for research in the strategic management domain with Rumelt's (1974) pioneering study "Strategy, Structure and

Performance". One of the most influential findings of research carried out by Rumelt (1974) was that firms with related business portfolios appeared to outperform firms with unrelated business portfolios (Robins and Wiersema, 1995). This led to the development of the following hypothesis:

H: 1 Firms pursuing related diversification will perform better than those firms pursuing unrelated diversification.

5.6.2 International Diversification and its relationship to Economic Performance

A positive relationship between international diversification and firm economic performance has been impressive but on closer examination the outcomes have been mixed (Ramaswamy, 1995; Tallman and Li, 1996). For instance Grant (1987), Daniels and Braker (1989), Haar (1989) Kim et al. (1993) and Vernon (1971), identified a positive relationship between international diversification and economic performance. On the other hand, others did not identify a linear relationship between international diversification and economic performance (Geringer et al. 1989, Kumar, 1984 ; Morck and Yeung, 1991). In particular, Geringer et al. (1989) found that there was a non-linear inverted U-shaped relationship between international diversification and economic performance. The explanation for this curvilinear outcome was that moderate levels of international diversification provided positive benefits to a firm through economic performance, however beyond that level the firm experienced significant costs associated with further international diversification.

Geographic Dispersion increased costs which included coordination, distribution and management costs. Costs derived from different government regulations, trade laws and currency value fluctuations across countries, access to raw materials and employee skills

requiring considerable coordination. Furthermore, these transactions costs and variations experienced across geographic regions increases managerial information-processing requirements. The types of costs identified include logistical costs, trade barrier and cultural diversity which make management of internationally diversified firms highly complex (Hitt et al. 1997). The result of the above mentioned transaction costs and increasing demands of managerial information-processing demands suggested that eventually as an organisation progressively further internationalised a point would be reached where the cost of international diversification outweighed the benefits. More specifically, “the internal governance costs exceed the benefits provided by economies achieved and thus the range of resources used and scope of governance exceeds managerial capabilities” (Hitt et al. 1997: 773). Given the two measures of international diversification, in multinationality and country scope the following questions were developed:

RQ 2.1: Is the nature and form of the relationship between economic performance and multinationality non-linear?

RQ 2.2: Is the nature and form of the relationship between economic performance and country scope non-linear?

The arguments presented suggested a non-linear inverted U-shaped relationship between international diversification and economic performance. The conflicting results evidenced from prior research of a positive relationship between international diversification and economic performance could be explained using the argument that once a firm goes beyond a moderate level of international diversification then costs begin to exceed benefits and economic performance suffers.

One measure of international diversification was represented by the ratio of sales from overseas operations to the total sales, which the current study will refer to as multinationality, this measure was supported by Hitt et al. (1997), Geringer et al. (1989)

and Grant et al. (1988). These measures have concentrated on the strategic importance of international diversification without clearly addressing the breadth and scope of the overseas operations (Tallman and Li, 1996). The more diversified internationally the firm was the greater the opportunity it had to raise its level of economic performance. The following hypothesis is drawn from that logic (Tallman and Li, 1996):

H: 2.1 The relationship between economic performance and multinationality is non-linear, with a positive slope at low/moderate levels of international diversification but negative at the high levels of international diversification.

Country scope, was another measure of international diversification, quite separate from multinationality (Tallman and Li, 1996), referred to the number of overseas countries the corporation trades with. It was suggested that there were advantages from geographical scope which should improve the economic performance of the firm. The following hypothesis was drawn from that logic (Tallman and Li, 1996):

H: 2.2 The relationship between economic performance and country scope is non-linear, with a positive slope at low/moderate levels of international diversification but negative at the high levels of international diversification.

5.6.3 Effects of the Interaction of International Diversification and Business-level Diversification on Economic Performance

Prior research has found a positive relationship between international diversification and economic performance, however the outcomes from empirical studies have been mixed (for instance, Geringer et al. 1989; Hitt et al. 1997; Rugman, 1979). A possible explanation for the mixed results was that the relationship was more complex than first thought (Hitt et al. 1997). Hitt et al. (1997) suggested that many firms that are diversified on an international level are also diversified at the business-level. In particular what was suggested was that firms diversified at the business-level gain internally from the

benefits of economies of scale, scope and learning (Kogut, 1985). The aforementioned benefits allowed for easier application of the relationships among business segments and international geographic areas as it allowed for sharing of distinctive firm capabilities and core competencies across business segments (Porter, 1985). The following questions were developed from this logic:

RQ 3.1: Is there a positive relationship between economic performance and the interaction of multinationality with unrelated business diversification?

RQ 3.2: Is there a positive relationship between economic performance and the interaction of multinationality with related business diversification?

Firms with business-level diversification can exploit international markets, based on a resource-based view of the firm (Fladmoe-Lindquist and Tallman, 1994). Firms with strong core competencies, which were a result of development in their domestic country operations, could apply these competencies to international markets (Bartlett and Ghoshal, 1989; Hitt et al. 1997). Furthermore, Porter (1990) argued that competitive advantages from successful domestic operations provided the confidence and willingness to apply the same competitiveness in international markets. It has been argued that business level diversification, which can be related or unrelated (Rumelt, 1974; Tallman and Li, 1996), can play a moderating role in the relationship between international diversification and economic performance (Hitt et al. 1997). Furthermore, it has been suggested that related business diversification was expected to promote better economic performance than unrelated diversification strategies (Tallman and Li, 1996). International diversification with the interaction of related/ unrelated diversification was also expected to improve performance "just how can these diversity variables be expected to act together?" (Tallman and Li, 1996:185) leading to the following hypotheses:

H: 3.1 There is a positive relationship between economic performance and the interaction of multinationality with unrelated business diversification.

H: 3.2 There is a positive relationship between economic performance and the interaction of multinationality with related business diversification.

When consideration was given to the effects of resource-based and transaction cost theory which referred to the non-linear nature of relationships between international diversification and economic performance, a test could be carried out on the linearity (or lack of it) for the international interactive variables. The following questions are developed from this analysis:

RQ 4.1: Is the nature and form of the relationship between economic performance and the interaction of multinationality with unrelated business diversification non-linear?

RQ 4.2: Is the nature and form of the relationship between economic performance and the interaction of multinationality with related business diversification non-linear?

Evidence suggested that as international geographic dispersion escalates transaction costs and managerial information processing are increased so diminishing returns commence which effects negatively on economic performance (Hitt et al. 1997; Jones and Hill, 1988). The following hypotheses are developed from H_{3,1} and H_{3,2} above to test for a non-linear relationship.

H: 3.3 The relationship between economic performance and the interaction of multinationality with unrelated business diversification is non-linear, with a positive slope at low/moderate levels of international diversification but negative at the high levels of international diversification

H: 3.4 The relationship between economic performance and the interaction of multinationality with related business diversification is non-linear, with a positive slope at low/moderate levels of international diversification but negative at the high levels of international diversification

There is further evidence, which suggested that the interaction of multinationality and country scope effected economic performance. Tallman and Li (1996) suggested that multinationality and country scope were two different aspects of internationality and were independent in their effects on economic performance. The following question were developed from this understanding:

RQ5.1: Is there a positive relationship between economic performance and the interaction of multinationality with country scope?

RQ5.2: Is the nature and form of the relationship between economic performance and the interaction of multinationality with country scope non-linear?

Furthermore, there was evidence which suggested that the "scope of operations helps to moderate the scale effects of multinationality" (Tallman and Li, 1996: 185). This dual effect helped to formulate the following hypothesis:

H: 3.5 There is a positive relationship between economic performance and the interaction of multinationality with country scope

To test for the non-linear relationship that may exist between economic performance and the interaction of international diversification with country scope the following hypothesis was developed from H_{3.5} above:

H: 3.6 The relationship between economic performance and the interaction of multinationality with country scope is non-linear, with a positive slope at low/moderate levels of international diversification but negative at the high levels of international diversification

5.6.4 Stakeholder Concern and its relationship to Economic Performance

The linkages between stakeholder concern and economic performance (refer to Chapter Four, Table 4.4) are far from clear (Ullmann, 1985; Waddock and Graves, 1997). Evidence indicated an ambiguous relationship (for instance, Alexander and Buchholz, 1978; Aupperle et al. 1985; Shane and Spicer, 1983; Ullmann, 1985). Other findings detected a positive link, but it was still unclear whether financially successful firms merely direct resources to social responsibility activities and so establish a higher standard, known as a "Slack Resource Theory" (Waddock and Graves, 1997: 304). Alternatively, where better social responsibility performance (reflected in disclosures in corporate annual reports) resulted in better economic performance referred to as "Good Management Theory" (Waddock and Graves, 1997: 304). There was also scanty evidence

of a non-linear relationship by Bowman and Haire (1975) which helps to develop the following questions:

RQ 6: Is the nature and form of the relationship between economic performance and stakeholder concerns non-linear?

There is also the suggestion that stakeholders influenced the firm in their decision making processes (Freeman, 1984) so consideration was also be given to stakeholder concerns as measured by social responsibility disclosure. Moreover, there was evidence of a non-linear relationship between stakeholder management and economic performance (Bowman and Haire, 1975; Griffin and Mahon, 1997). The following hypothesis was developed from the above analysis:

H: 4.1 The relationship between economic performance and stakeholder concerns is non-linear, with a positive slope at low/moderate levels of stakeholder involvement but negative at the high levels of stakeholder involvement.

Managers' ability to meet the requirements of various stakeholders of the firm may have led to favourable economic performance (Preston and O'Bannon, 1997). What was suggested, for primary stakeholders, was that "serving the implicit claims of major stakeholders (eg., employees, customers) enhances a company's reputation in a way that has positive impact on its financial performance" versus serving secondary stakeholders (Preston and O'Bannon, 1997: 421). The following questions were developed from this thinking:

RQ 7.1: Is there a relationship between economic performance and primary stakeholders and is the nature and form of this non-linear?

RQ 7.2: Is there a relationship between economic performance and secondary stakeholders and is the nature and form of this non-linear?

The current study also categorised stakeholders into primary and secondary in which the primary referred to the employee related and customer related social responsibility disclosure themes whilst secondary stakeholders referred to community related and

environment related social responsibility disclosure themes. The following hypotheses are developed from the above analysis:

H:4.2: The relationship between economic performance and primary stakeholders is non-linear, with a positive slope at low/moderate levels of stakeholder involvement but negative at the high levels of stakeholder involvement.

H:4.3 The relationship between economic performance and secondary stakeholders is non-linear, with a positive slope at low/moderate levels of stakeholder involvement but negative at the high levels of stakeholder involvement.

Since there appeared to be sparse empirical work which has tested whether firms make trade offs among stakeholder groups, the current study tests for the trade off as between primary and secondary stakeholders of the firm when consideration was given to economic performance (Bendheim et al. 1998). The following question was thus developed from that logic:

RQ 8: When considering the relationship between economic performance and stakeholder management, are firms more concerned about primary stakeholders than secondary stakeholders?

The findings from the Bendheim et al. (1998) study make it clear that trade-offs do exist between stakeholders for American firms. Is this the case for Australian firms? The question arose as to whether in treating particular stakeholder groups well, you achieved higher economic performance outcomes. The following hypothesis was developed from this analysis:

H:4.4 When considering the relationship between economic performance and stakeholder concerns firms are more concerned about primary stakeholders than secondary stakeholders.

5.6.5 Integrative Strategic and Stakeholder Management Hypotheses

RQ 9.1: Are the combined concerns for international and business level diversification with stakeholder interests positively related to economic performance?

RQ 9.2: Are the combined concerns for international and business level diversification with stakeholder interests negatively related to economic performance?

This section developed hypotheses of the combined effect of business-level and international diversification strategies with stakeholder concerns on economic performance. Non-linear /curvilinear characteristics were found to exist in relationships between international diversification and economic performance (discussed in Chapter Three) and between stakeholder concerns and economic performance (discussed in Chapter Four). From Chapters Three and Four, there was evidence from a few previous studies of a non-linear relationship in each international management and stakeholder management fields. In the first instance, evidence suggested that the level of international diversification was divided into subgroups of low to moderate and high levels, further tests provided support for a non-linear relationship (Geringer et al. 1989; Gomes and Ramaswamy, 1999; Hitt et al. 1997). Furthermore, observed from Chapter Four, there was also very sparse evidence in past research of a split between low to moderate and high levels of stakeholder involvement and the effects of this division on economic performance (Bowman and Haire, 1975; Griffin and Mahon, 1997). When consideration was given to past research in each of these two fields of study, tests of the effects of each on economic performance has provided support for a non-linear relationship but more so in the case of the relationship between international diversification and economic performance than for stakeholder management and economic performance.

When considering the combined effect of both international diversification and stakeholder concerns on economic performance a test for the possibility of a non-linear relationship of the combined effect needed to be addressed. The cell typology in Figure 5.4 illustrates the four possible quadrants if there exists a cut-off point which divides low to moderate and high levels of activity whether they be stakeholder concerns of managers or international diversification. Since evidence suggested that it is more likely that firms perform better at low to moderate levels of stakeholder concern (Bowman and Haire, 1975) and low to moderate international diversification level than higher levels, then the hypotheses developed involve the two quadrants in Cell 1 and Cell 3. Cell 1 represents the relationship between combined international and business-level diversification with stakeholder concerns on economic performance, both at the low to moderate levels of activity.

Figure 5.4
Cell Typology Illustrating Principal Tests when Integrating International
Diversification and Stakeholder Involvement on Economic Performance: Using a
Subgroup Analysis.

High Level International Diversification	S T R A T E G I C	CELL 2	CELL 3
Low/Moderate International Diversification	M G T	CELL 1	CELL 4
		STAKEHOLDER	CONCERNS
		Low/Moderate Stakeholder Involvement	High Level Stakeholder Involvement

Cell 3 represents the relationship between combined international and business-level diversification with stakeholder concerns on economic performance both at a high levels of activity. Hypotheses are based on Cell 1 and 3 from the cell typology in Figure 5.4 as it is expected that firms perform better at the low to moderate level of activity for both stakeholder concern (Bowman and Haire, 1975) and international diversification (Geringer et al. 1989; Gomes and Ramaswamy, 1999; Hitt et al. 1997) than they would at the high levels of both stakeholder involvement (Bowman and Haire, 1975) and international diversification (Geringer, et al. 1989; Gomes and Ramaswamy, 1999; Hitt et al. 1997).

Cells 2 and 4 are a mixture of combined high and low activity and do not relate to the nature of past findings, nor do they address the issues of non-linearity of the relationships, so will not be tested in the current study. The following hypotheses were developed from cells 1 and 3:

From Cell 1 it was hypothesised that:

H:5.1 When stakeholder involvement and international diversification are both at the low to moderate level then the combined relationship of stakeholder concerns with international and business-level diversification on economic performance will be positive.

From Cell 3 it was hypothesised that:

H:5.2 When stakeholder involvement and international diversification are both at the high level then the combined relationship between stakeholder concerns with international and business-level diversification on economic performance will be negative.

5.7 Summary

This chapter identified that firm's which were involved in international diversification could also utilise their core competencies or internal resources and capabilities in order to take advantage of opportunities available across global geographic scope and regions "the resource based view of the firm" (Hitt et al. 1997: 769). This was termed the resource-based theory of the firm. As international firms further diversified they experience increasing transaction costs which include, costs of coordinating between business units between different geographic markets which was detrimental to the benefits gained from further international diversification. This was termed the transactions cost theory. There was a point where multiple transactions among geographical markets cost more than the benefits derived from sharing resources, exploiting market opportunities and benefits of economies of scope. The net effect of transaction costs was to create diminishing returns to international diversification which results in an inverted U-shaped curvilinear relationship (Hitt et al. 1997).

Business-level diversification was also explained in terms of resource-based view of the firm. Hitt et al. (1997) suggested that business-level diversification (sometimes called product diversification) strategy played a moderating role in the international diversification and economic performance relationship. Initially business-level diversification positively moderated the relationship between international diversification and economic performance. It was argued that this moderation effect of business-level diversification was explained in terms of a resource-based theoretical perspective. It was argued that corporations which experienced business-level diversification in the past are most effective from a resource perspective and displayed greater capability of expanding into international markets than those firms that do not display business-level diversification.

In this chapter a socioeconomic theoretical framework was developed (illustrated in Figure 5.3) from two major streams in strategic management theory and stakeholder theory. The relationship between stakeholder concerns and economic performance was explained using the instrumental stakeholder theory of the firm. From an analysis of the strategic management and international business literature there was support for a resource-based theory together with the use of a transaction cost theory in helping to understand and explain the following relationships: business-level diversification and economic performance; international diversification and economic performance; the interaction between business-level diversification and international diversification and the impact of this interaction with economic performance (Hitt et al. 1997).

In sum, use was made of resource-based and transaction cost theory to understand and explain the relationships between:

International diversification and economic performance

Business-level diversification and economic performance

Interaction between international diversification and business-level diversification with economic performance

Instrumental stakeholder theory was used to explain and understand the relationship between:

Stakeholder concerns and economic performance.

All three theories were used to explain and understand the combined relationship between business-level and international diversification (and their interaction) together with stakeholder concerns on economic performance. Hypotheses and related questions were developed from the socioeconomic theoretical framework in this chapter.

CHAPTER SIX

RESEARCH METHOD

6.1 Introduction

Chapter One identified the purpose of this research study as investigating whether strategic and international business diversification with stakeholder concerns enhances economic performance. It identified the need to develop a socioeconomic framework, which incorporates transactions cost, resource-based and instrumental stakeholder theory, for investigating economic performance. Chapter Two developed a socioeconomic model examining the effect that strategic management, international business diversification and stakeholder concerns has on economic performance. Chapter Three examined the relationship between business-level diversification strategy and economic performance, the interaction of international diversification with business-level diversification on economic performance. Then an analysis of the interaction of multinationality with country scope on economic performance was considered. The importance of transaction costs effects on this relationship was then examined providing evidence of a non-linear relationship between international diversification and economic performance. Chapter Four examined the relationship between stakeholder management and economic performance. The chapter provided evidence to support using social responsibility disclosures themes from corporate annual reports as a way of identifying stakeholder concerns and that these concerns are positively related to economic performance. Chapter Five developed a socioeconomic theoretical framework for investigating economic performance. The various multidisciplinary determinants of economic performance that the study investigated

include business level diversification strategies, international diversification strategies and stakeholder concerns of firms.

This chapter specifies and discusses the study's method of measuring business level, international diversification and stakeholder concerns. In identifying and evaluating the strategic, international business management and stakeholder variables the current study focused upon large listed Australian public companies. In the next section of the current chapter aspects of the research design adopted, including sample selection techniques and data collection procedures were examined. In the following section business level, international diversification strategy, stakeholder concern independent variables, and the economic performance dependent variable, are defined more precisely. Data sources and data collection methods applicable to each of the variables are then explained. This is then followed by an examination of an averaging technique used to bring together groups in common over the three year period under consideration. Furthermore, stakeholders are divided in two categories, primary and secondary, in order to determine whether firms are more likely to prefer one category over the other, and the effects of this preference on economic performance. The next section examines the Chow test as a method to test for a non-linear relationship. The Chow-test assists in dividing the averaged data into subgroups within the sample. The subgroups are twofold, first stakeholder concerns will be split between low/moderate and high levels of stakeholder concerns. Second a subgroup is identified in the international diversification strategy variable where low/moderate levels will be distinguished from high levels. In both instances the Chow statistic was described as the test to be used to determine the statistical significance of a critical cut off point for each variable. Furthermore, an F test is used as a method of determining the incremental contribution of an additional explanatory variable. Finally the method of determining the degree of multicollinearity between the explanatory variables is

detailed and correlation matrix together with variance inflation factors are suggested as recommended ways of detecting multicollinearity.

In the socioeconomic approach employed in the current study five models are constructed to measure and explain effects on economic performance of a business and society orientation. First from an international perspective, second from a business-level diversification strategy perspective, third from an integration of international and business-level diversification, fourth from a stakeholder (utilising social responsibility reporting), and the fifth an integration of the three independent paradigms.

The Socioeconomic Model can be described as:

$$\text{EP} = f(\text{International Diversification Strategy, Business-level Diversification Strategy, Stakeholder Concerns})$$

More Specifically the Five models to be tested are described:

International Diversification: $\text{EP} = \alpha + \beta_1(\text{ID}) + \varepsilon$

Business Diversification: $\text{EP} = \alpha + \beta_2(\text{BD}) + \varepsilon$

Integrated 1: $\text{EP} = \alpha + \beta_3(\text{ID}) + \beta_4(\text{BD}) + \varepsilon$

Stakeholder Concerns $\text{EP} = \alpha + \beta_5(\text{SC}) + \varepsilon$

Integrated 2: $\text{EP} = \alpha + \beta_6(\text{ID}) + \beta_7(\text{BD}) + \beta_8(\text{SC}) + \varepsilon$

Where:

EP- Economic Performance

ID- International diversification: Multinationality and country scope

BD- Business-level Diversification Strategy

SC- Stakeholder Concerns

Where *Economic Performance* refers to the profit performance of the firm relative to either assets, equity or sales using accounting based approaches or earning per share and dividends per share when using market based approaches. *International diversification* refer to two independent measures country scope and multinationality. International diversification is defined as the “expansion across borders of global regions and countries into different geographic locations, or markets” (Hitt et al. 1997: 767). Country scope refers to a firm’s level of international diversification reflected by the number of different international markets in which it operates, whilst the other measure refers to the extent of the firms multinationality reflected by the percentage of foreign sales to total sales. *Business-Level Diversification* strategy represents the aggregate of multiple businesses within a single organisation. It aggregates the interrelationships among businesses within an organisation (Robins and Wiersema, 1995). Whilst *Stakeholder Concerns* represents social responsibility disclosure in corporate annual reports of corporations as a reflection of stakeholder management, and is voluntary in nature for Australian firms. It includes the interests of a corporation’s broad stakeholders and encompasses, employee related responsibility, product safety related responsibility, community related responsibility and environmental related responsibility as described in Chapter Four.

6.2 Sample Selection

It was decided to select a sample from the top 50 Australian publicly listed companies for each year from 1993-1995 (refer to Appendix I for a list of those companies). This represents large companies covering a variety of industries contained within these 150 companies in total. Larger firms are used in this study as they are more than likely to exhibited international and social responsibility activity (Hitt et al. 1997; Gray et al. 1995a). Connect-4, a CD-ROM of the Australian Corporate Annual Report file of the top 500 companies, was utilised. Large firms, as identified by market capitalisation,

are used in the current sample selection process. Furthermore, evidence from past research identified the benefits of focusing on larger firms when examining the relationship between business-level diversification strategy/international strategy and economic performance (Bettis and Hall, 1982; Hitt et al. 1997; Kim et al. 1989; Rumelt, 1974; Simmonds, 1990; Varadarajan and Ramanujam, 1987).

Further support for the use of large publicly listed companies is based on the suggestions that a sample of large companies is more likely to demonstrate examples of social responsibility (reflecting stakeholder concerns), than an equivalent sample of medium or small companies (Gray et al. 1995a). In terms of trends, Gray et al. (1995a) suggest that to identify innovations in social responsibility and capture more social responsibility reporting, a sample of large companies was likely to provide greater evidence. As previously examined there was also evidence that larger companies were more likely to be “influential in establishing corporate trends in the social responsibility area” (Roberts, 1992: 606).

Furthermore, consideration was given to industry type as the nature of the industry can influence management of stakeholder concerns and international diversification activities. For instance it was suggested that firms in different industries need to address a different array of stakeholders, referring to a matching of particular stakeholders to a particular industry (Griffin and Mahon, 1997; Woods and Jones, 1995).

Recent American studies, which have tested the relationship between international diversification on economic performance, have deliberately chosen the manufacturing industry when selecting their sample of firms for examination (Gomes and Ramaswamy, 1999; Hitt et al. 1997; Tallman and Li, 1996). Evidence from an

Australian study however suggested that service industries as well as manufacturing should be considered when examining the relationship between international diversification and economic performance linkage (Ellis and Williams, 1995). A recent Australian study suggested that when examining such a relationship that the sample of firms not be restricted to specific industries but be cross sectional in nature thus removing the bias of past single industry studies. Furthermore, it was suggested that Australian studies select samples of firms that include both a proportion of the services and resource sectors (Lewis and Minchev, 1998).

The rationale for including both services and resource sectors when deciding on the sample for the current study, was based on evidence from a recent Australian study where:

Most of prior Australian studies on internationalisation are narrowly focused in that they examine manufacturing firms, thus excluding service and resource-based industries. Given the importance of resources and services in the Australian economy, the emphasis on manufacturing could be misleading in terms of the overall experience of internationalisation of Australian companies. (Lewis and Minchev, 1989: 8)

In both the stakeholder and international business literature the sample frame has been biased towards firms in a particular industry such as manufacturing. In order to increase the reliability of the data set and to ensure that resource and services sector firms were included in the sample the current study collected data on a cross sectional basis. The cross section included a variety of industries (which included services and resource sectors) which were in the top 50 Australian publicly listed companies for each of the three years 1993-1995 inclusive. To bias the sample by only selecting firms in a particular industry segment would be misleading (Lewis and Minchev, 1998).

6.3 Averaging the Data

The data needed to be averaged over the three-year period of the study in order to increase sample size. The results of the current study reflect the average performance of firms in the sample over the period 1993-1995. A superior statistical procedure is to pool the data, however this was not possible because of missing observations in each of the years under study. The averaging process is often used in econometrics and management studies (Cochran and Wood, 1984; Hitt et al, 1997; Mauro, 1995) particularly where missing data are an issue. Support for averaging when there is missing data has been noted:

we used a three-year average for the 1988 through 1990 period for each variable in the study (a two-year average was used for a small subsample of firms because of missing data). (Hitt et al. 1997: 778)

In the current research averaging was used to adjust for firms which appeared more than once, in the sample, for the three years period. For instance if Broken Hill Proprietary Ltd is present for all of the three years of the study an average is taken for those three years, on the other hand if say Boral Ltd appears for 2 years then the average is taken for two years and so on. This process catered for the problem of missing data in the incomplete data set. A pooled data set would have been ideal but was not appropriate in the current study due to missing data.

6.4 Method of Gathering Data on the Dependent Variable

Economic Performance is a multidimensional construct and from past research two common approaches were used to gather performance data on market and accounting based methods. Taking the first of these, the accounting based measure was defined as a “historically oriented operating performance dimension” (Keats, 1988: 151). The

accounting based measures were commonly used to gather data on economic performance by selecting historical figures such as profitability relative to assets/ sales/ equity. More specifically Return on Assets (ROA), Return on Sales (ROS) and Return on Equity (ROE) were the three accounting based measures of economic performance used in the current study. In measuring "Return" the relevant dollar amounts for profitability were measured by accessing earnings before interest and tax from financial information in the corporate annual reports. Assets for ROA were measured by calculating the net tangible assets, whilst equity for ROE was taken from the balance sheet in the corporate annual report and finally Sales for ROS were identified in the notes to the accounts as total sales revenue.

Another possible dimension of economic performance was market-based measures that were based on the price and value of shares, reflecting the market's perception of performance. Two market-based measures of economic performance used in the current study were based on a measure of the market's perception of share value, in Earnings Per Share (EPS) and Dividends Per Share (DPS). Measures for EPS and DPS were extracted from details in the corporate annual reports in the form of ratios.

Evidence has suggested that there is convergent validity between these two measures of economic performance (Keats, 1998). In essence, what has been suggested of these two measures of economic performance, was that accounting-based and market-based "constitute two separate but correlated dimensions of financial performance construct." (Keats, 1988: 152). The current study used multiple measures of economic performance, as past research reflects the implicit assumption that economic performance is a multidimensional construct (Dess and Robinson, 1984). This multiple measure of economic performance was noted by Keats (1988):

I suggest that accounting-based profitability measures and market-based measures reflect two possible dimensions of performance that are related, yet separate and distinct (Keats, 1988: 154).

The issue of whether to use market based or accounting based measures of performance, or both to satisfactorily reflect economic performance has been the subject of much debate (Hoskisson and Hitt 1990). It seems that accounting based measures have been most frequently used and defended. Keats and Hitt (1988) however, found that when using both accounting and market based measures of performance, a negative relationship was identified between diversification and accounting based economic performance and a positive relationship between diversification and market based measures of economic performance.

The current study measured economic performance using both accounting-based measures as well as market-based measures. The studies summarised in Table 6.1, suggest a strong case for using accounting based measures in studies of strategy (Bettis and Hall, 1982; Hoskisson, Hitt, Johnson and Moesel, 1993; Robins and Wiersema, 1995) and studies in social responsibility research (Cochran and Wood, 1984; Herremans et al. 1993; McGuire et al. 1988; Preston, 1978). The current study also tests whether support for using accounting-based measures holds true for the sample of Australian public companies over three consecutive years covering 1993-1995 inclusive.

There was further evidence that supported accounting-based measures as an important historical dimension of economic performance (Hitt et al. 1997; Venkatraman and Ramanujam, 1987; Woo and Willard, 1983). Results indicated that the strongest accounting based dependant variable was ROA, as the significance of the relationships tested was strongest.

Table 6.1
Various Studies Utilising Accounting Based Economic Performance Measures

Author(s)	Relationship tested	Accounting Measures of Economic Performance
Studies testing Diversification and Economic Performance Relationship		
Bettis and Hall (1982)	Diversification and Accounting Determined Return	ROA
Dubofsky and Varadarajan (1987)	Diversification and Performance	ROA
Hall (1995)	Corporate Diversification and Economic Performance	Return on Assets ROA Return on Equity ROE Return on Sales ROS
Hoskisson, Hitt, Johnson and Moesel (1993)	Diversification and Economic Performance	ROA ROE ROS
Markides (1995)	Diversification and Economic Performance	operating income before depreciation and interest as a percentage of sales
Robins and Wiersema (1995)	Portfolio Relationships and Corporate Financial Performance	ROA, considered as the most widely used measure
Simmonds (1990)	Diversification and Performance of Large Diversified Firms	ROA ROE Return on Invested Capital (ROIC) Compounded Sale Growth (CSG)
Varadarajan and Ramanujam (1987)	Diversification and Performance	ROE Return on Total Capital (ROC) Sales Growth Rate (SGR)
Wooldridge and Floyd (1990)	Strategy Process and Organisational Performance	ROA
Studies testing Social Responsibility and Economic Performance Relationship		
Aupperel, Carroll and Hatfield (1985)	Corporate Social Responsibility and Profitability	long term ROA short term ROA
Chen and Metcalf (1980)	Relationship between Pollution Control Record and Financial Indicators	ROE P/E ratio
Cochran and Wood (1984)	Corporate Social Responsibility and Financial Performance	Earning Per Share (EPS) Price Earnings Ratio (P/E)

Freedman and Jaggi (1988)	Association between Pollution Disclosures and Economic Performance	ROA-using both net income and EBIT as measures of return ROE-using both net income and EBIT as measures of return cash basis return on assets cash basis return on equity
Herremans, Akathaporn and McInnes (1993)	Corporate Social Responsibility Reputation and Economic Performance	ROA ROE Operating Margins Net Margins
Mc Guire, Sundgren and Scheeweis (1988)	Corporate Social Responsibility and Firm Financial Performance	ROA Total Assets Sales Growth Asset Growth Operating Income Growth
Preston (1978)	Corporate Social Responsibility and Economic Performance	ROE

In a more recent study the selection of ROA as the most appropriate measure of economic performance was supported by Hitt et al. (1997), who rejected ROE , as it has been shown to be “more sensitive to capital structure differences” (Hitt et al, 1997: 778). Furthermore when considering ROS as a measure, on closer examination of the independent variables, such as international diversification and the combined business level /international diversification variable, these variables are all functions of total sales. As a dependent variable, ROS which clearly contained sales might “reflect mathematical artifacts as well as true relations” (Hitt et al. 1997: 778). This problem with using ROS as a dependent variable was further recognised by Farris, Parry and Ailawadi, (1992). The outcome of these findings listed in Table 6.1 suggest that the accounting-based measure ROA was the most appropriate dependent variable.

6.5 Method of Gathering Data on the Independent Variables

This section presents the method to select data from corporate annual reports as measures of the independent variables: international diversification, business-level diversification and stakeholder concerns. The control variables measured from corporate annual reports include size, leverage, industry classification and mergers and acquisitions.

From an extensive examination of government department reports, corporate annual reports, other sources of available corporate data which included those recommended in past research, the current study was necessarily restricted to selecting all data from figures or narration contained in corporate annual reports. As previously noted (Chapter Four), there were no known social responsibility ratings or reputation studies, which ranked corporations into those which exhibited high standards of social responsibility, nor were there any known sources of data which provided a measure of international diversification. Data was extracted from the corporate annual reports and further calculations and computations were made to arrive at measures of all independent variables in, international diversification, business-level diversification and stakeholder concerns. Each of these will be considered in turn in this section

6.5.1 International Diversification Variable

More than one measure of international diversification has been used in past studies (Hitt et al. 1997; Tallman and Li, 1996). What the majority of studies considered was a unidimensional measure of international sales as a percentage of the total sales (Hitt et al. 1997). Another unidimensional measure was foreign assets as a percentage of total

assets (Geringer et al. 1989). Other studies have used an entropy approach, determined using the following criteria:

The entropy measure of international diversification is defined as

$$ID = \sum_i [P_i \times \ln(1/P_i)]$$

Where P_i is the sales attributed to global market region I and $\ln(1/P_i)$ is the weight given to each global market region (Hitt et al 1997: 780)

The entropy measure includes the number of global market regions and also the relative importance of these regions to total sales (Hitt et al. 1997). Australian accounting standards require firms to report sales data relating to exports to foreign regions in corporate annual reports. The current study did not use an entropy approach as each of the number of global regions and sales attributable to those global regions were readily available in corporate annual reports. Furthermore, it has been shown that there are positive correlations between the entropy approach used by Hitt et al. (1997) and unidimensional measures such as foreign sales to total sales (Hitt et al. 1997).

In a recent study international diversification was measured using two independent measures *multinationality* and *country scope* (Tallman and Li, 1996). Multinationality measured the sales revenue from international operations to total sales (a unidimensional measure) whilst country scope measured the number of international markets that a firm services. These measures were used in the current study.

Multinationality

Several measures of international diversification have been used in previous research and the more frequently used one was a unidimensional measure of international sales as a percentage of total sales (Geringer et al. 1989; Grant et al. 1988; Hitt et al. 1997; Tallman and Li, 1996). In most cases a measure of multinationality was extracted from

the corporate annual reports by identifying the segment reporting section in the “Notes to the Accounts”. According to Australian Accounting Standards Board 1005 (AASB 1005) “Financial Reporting by Segments”, activities regarding foreign geographical and local geographical segments need to be disclosed in accordance with the guidelines pertaining to this professional accounting standard in corporate annual reports. The AASB 1005 guideline was used to identify international diversification variables in particular the level of multinationality of the firms. Dollar amount for sales and foreign sales was identified and recorded from the segment reporting section, of the corporate annual report using AASB 1005, for all companies in the sample.

Country scope

Country scope reflects the breadth and scope of international operations as a determinant of economic performance. It is this aspect of the breadth of international diversification that is of interest, as it provides a measure of the country scope of international operations and the ability of a company to “arbitrage operations across countries and leverage location-based advantages” (Tallman and Li, 1996: 185). Further use was made of AASB 1005 “Financial Reporting by Segments”, activities regarding foreign geographical and local geographical segments need to be disclosed in accordance to the guidelines pertaining to this professional accounting standard in corporate annual reports. The AASB 1005 guideline was used to identify country segments and so determine the number of international regions that firms in the sample were exporting goods and/or services.

6.5.2 Business-Level Diversification Variable

Business-level diversification was usually measured in one of two ways. Either as a *categoric* measure developed by Rumelt (1974), and/or a *continuous product count*

measure built on the Standard Industry Classification (SIC) system. There was a long debate regarding which method better reflects business-level diversification strategy, however in a study which compared the two major methods it was found that the categoric and SIC measures were similar (Montgomery, 1982).

The SIC system represented a continuous product count and was a US federal government initiative in order to classify numerous types of economic activity in the US economy (Montgomery, 1982). As this measure does not involve managerial intention, preference was given to the categorical measure which encompasses managerial strategic intent regarding economic performance (Hoskisson et al. 1993).

The current study utilised the categorical Rumelt (1974) measure of diversification strategy. This measure first classified the organisation into the various business segments in order to determine business relatedness using a specialisation ratio to determine the level of business activity in a single business or group of businesses (Hoskisson et al. 1993; Palepu, 1985; Rumelt, 1974; Simmonds, 1990; Wrigley, 1970). Rumelt's (1982) study further refined and thereby reduced the categorisation of diversification into four main categories using a ratio analysis:

specialisation ratio (Rs) reflects "the fraction of the total revenue of the firm attributed to the largest single business unit" (Srivastava, Nargundkar and Green, 1994: 146).

It was suggested that the lower the specialisation ratio then the higher is the probability that there exists a greater level of diversity (Srivastava et al. 1994).

Following the determination of the specialisation ratio, the next step was to classify these business segments into the following four categorical classifications in line with

Rumelt (1982) *single/dominant, related constrained, related linked and unrelated businesses*. Rumelt (1982) used two distinct related ratios to differentiate between these business segments the related ratio and the related core ratio:

The *related ratio (Rr)*, represents the " fraction of the total revenue attributed to the largest group of 'somehow related business' "(Srivastava et.al. 1994: 146).

The *related core ratio (Rc)*, "is defined as the fraction of the total revenue attributed to its largest group of businesses that share the same core skill, strength or resource."(Srivastava et.al. 1994: 146).

The related linked categories referred to business segments that have a relationship with at least one other business segment. On the other hand, unrelated business segments were identified where activities relating to production are independent of other business segments. The related constrained category referred to business segments that have a one to one association with other segments of the organisation. The single/dominant business category reflects a single business segments dominated by a single business location (Srivastava et al. 1994).

Using this categorisation, with specific ratio analysis devised by Rumelt (1982), the method of identifying the four categories mentioned above was facilitated by the following four ratio specifications (Srivastava et al. 1994):

Category	Ratio Specification
Single/Dominant business	$R_s > .70$
Related Constrained	$R_s < .70, R_r > .70$ $R_c > (R_r + R_s) / 2$
Related Linked	$R_s < .70, R_r > .70$ $R_c < (R_r + R_s) / 2$
Unrelated Business	$R_s < .70, R_r < .70$

Source: Srivasatava et al. (1994: 146)

The problem with the Rumelt (1974) categoric measure of diversification strategy surround the "difficulty in calculating the ratio" (Srivastava et al. 1994: 146). The problem stems from the lack of objectivity as each researcher must make a judgement when calculating these ratios. There is also the problem with not being able to place some companies into a single category. Nevertheless preference is given to Rumelt's categorisation as it has provided a high level of explanatory power in previous work (Srivastava et al. 1994). The current study used the specialisation ratio, related ratio and related-core ratio to determine and measure business level diversification strategy from the sample.

In sum, a categorical measure for business level diversification was used in the current study and use was made of the three ratios developed by Rumelt (1974), specialisation ratio, related ratio and related core ratio. It was considered that of the three ratios related core was too subjective to identify from the corporate annual reports and so data was not collected for this ratio. The specialisation ratio was not difficult to obtain however there was some subjectivity attached to the related ratio as this ratio measures the fraction of the total revenue that relates to the largest group of somehow related businesses. AASB 1005 was used in gathering the data to calculate this ratio, as it segmented revenue into different business groups and by rule of thumb those businesses that appeared to belong to the same industry were grouped together and categorised as related businesses. There was a problem of placing some companies into a single business. Identifying discreet businesses was based in some instances on judgement, which means a degree of objectivity can be lost. In order to effectively, with a degree of objectivity, group these businesses into categories use was made of industry classification of the "Business Classification Index" of the "Jobson's Year Book of Australian Companies".

The result of the application of this ratio analysis was that data collected identified firms as either business related or unrelated. Use was also made of an approach where categorising firms that have a related ratio more than 70% as related businesses whilst those which have a related ratio less than 70% are unrelated businesses (Montgomery, 1982; Rumelt, 1974). The 70 % figure has been used by numerous other studies since its introduction by Rumelt (1974) and is applied in the current study to be consistent and comparable with other studies that preceded it. The two categories, related and unrelated diversification strategy, were used to analyse the effects of related / unrelated business diversification on economic performance.

6.5.3 Stakeholder Concerns Variable

Chapter Four argued that there was a link between social responsibility reporting and stakeholder concerns. The current study measured stakeholder reporting by calculating the content of social responsibility disclosed in the corporate annual report of firms in the sample.

Social responsibility reporting was reflected by the content of social responsibility disclosed in corporate annual reports. Chapter Four provided a link between social disclosure themes with stakeholder groups and identified four stakeholder groups which match those social disclosure themes. Effectively four stakeholder groups were matched (refer to Table 4.4) which were: employee relations; product safety (customer groups); community groups; treatment of the environment. These stakeholder concerns to management were derived, in Chapter Four and again referred to here in Table 6.2 guided by a composite of information gathered from a review of the international literature (from Australia, Britain and America). More specifically, in determining stakeholder concerns, a list was developed under each of the four related social

responsibility themes. Reference was also made to the following studies: AlNajjar (1992), Gray (1990), Mangos and Lewis (1995) and Roberts (1992) in developing the list in Table 6.2. Social responsibility reporting has been located in directors reports and other non-specific locations in corporate annual reports.

Table 6.2

Dimensions for Measuring Stakeholder Concerns

Employee

- 1 Bonuses / promotions / share option plans
- 2 Profit sharing by employees or employee property ownership
- 3 Training programs
- 4 Ensuring employment and advancement opportunities for minorities
- 5 Labour representation / unions / labour contract negotiations
- 6 Data on formal education of employees
- 7 Education and development for employees and trainees
- 8 Tuition assistance plans
- 9 Data on female managerial employees
- 10 Data on females in the total workforce
- 11 Handicapped employees
- 12 Drug and alcohol rehabilitation and educational counselling
- 13 Company health services and insurance programs
- 14 Safety and accident prevention measures
- 15 Training for safety in the workplace
- 16 Safety and fire protection research
- 17 Number of fatal accidents
- 18 Provision of child care facilities
- 19 Number of employees
- 20 Employee related costs including indirect costs
- 21 Hours worked
- 22 Employee turnover
- 23 Employee absenteeism

Product

- 1 Product quality / assurance through adequate control
- 2 Product safety and design
- 3 Formulation / packaging of products to minimise possibilities of harm or injury
- 4 Raw materials used / source of / type of / environmental impacts
- 5 Research and development activities re minimum environmental impacts

Community

- 1 Direct financial aid / scholarships / grants
- 2 Support of higher education
- 3 Support for minority students
- 4 Direct financial support to art / institutions and the performing arts
- 5 Developing and supporting a better system of health care
- 6 Help for minority businesses
- 7 Minority hiring
- 8 Minority suppliers
- 9 Philanthropic contribution
- 10 Charitable contributions
- 11 Company financed foundation rendering service to the sciences
- 12 Public or social relations department
- 13 Assistance to nation for social welfare
- 14 Publication of a public interest report
- 15 Employee volunteer activities

Environment

- 1 Pollution reduction measures / air / water
- 2 Report on environmental protection
- 3 Installation of modern pollution control equipment
- 4 Engineering new facilities for production with minimum environmental effects
- 5 Cooperating with state and local authorities in developing improved systems of environmental management
- 6 Engineering new products for minimum environmental effects
- 7 Clean up costs / Waste
- 8 Litigation
- 9 Measures to reduce risks of environmental accidents
- 10 Environmental research programs
- 11 Particular type of energy used or produced
- 12 Amounts spent of environmental protection investments
- 13 Quantified and/or qualified indication of effects of environmental investment
- 14 Recycling / Byproducts

This appendix is a composite of information gathered from Dr. Fouad K. AlNajjar of Wayne State University; Roberts, C., (1992) "Environmental Disclosures in Corporate Annual Reports in Western Europe" Chapter 7 in Owen, D., (Ed) *Green Reporting: Accountancy and the Challenge of the Nineties*, Chapman and Hall; Gray, R., (1990) *The Greening of Accountancy*, Chartered Association of Certified Accountants, June; United Nations Intergovernmental Working Group of Experts on International Standards of Accounting and Reporting, reported in Gray, 1990.

Adopted from Mangos and Lewis, (1995: 61-62)

The social responsibility disclosures reflect the level of stakeholder management which included employee related, product related, community related and environment related social responsibility by managers and reconciles with the stakeholder groups developed

in Chapter Four. Social disclosures can be identified in corporate annual reports, and quantified using content analysis. It was argued that society and other interest groups (e.g., government, environmental groups, amongst others), pay attention to the profit levels of companies. Volatility or high earnings made by companies may be interpreted as the company making 'too much' profit at society's expense. In order to counter this image managers may increase the degree of social responsibility disclosure in their corporate annual reports.

The current study recognised four social responsibility themes to classify each company's representation of stakeholder management. The themes are:

1. Environment
2. Employees
3. Products
4. Community

This classification is consistent with that used in former studies using social responsibility reporting (AlNajjar, 1992; Gray 1990; Guthrie and Parker 1987; Trotman and Bradley 1981; Roberts 1992). Moreover, it is also consistent with a recent study which considered stakeholder categorisation using social responsibility structures as "community relations, employee relations, treatment of environment and customer relations" (Waddock and Graves, 1997: 259).

Primary versus secondary stakeholders

In the current study stakeholders are further divided into primary and secondary categories (Post, Frederick, Lawrence and Weber, 1996 and Waddock and Graves,

1997). This level of categorisation distinguishes between market driven stakeholders such as suppliers, customers employees and investors as the primary ones (Post et al. 1996) and others who are considered as secondary, given they are not closely linked to the survival of the business (for instance the communities and perhaps the environment). Although it could be argued that environment be placed in the primary category (Starik, 1995; Waddock and Graves, 1997). In testing the relationship between primary stakeholders and economic performance the current study identifies primary stakeholders as employees and customer related product safety issues both measured using employee and product safety disclosures in corporate annual reports respectively. In testing the relationship between economic performance and secondary stakeholders the current study identifies secondary stakeholders as environment and community service issues both measured using environment and community service disclosures in corporate annual reports respectively.

Content Analysis

Some studies used *Fortune* reputational data or ratings level to measure social responsibility reporting or performance. Australia as yet has no equivalent to the (Kinder, Lydenberg, Domini & Co) KLD social screens as Waddock and Graves, (1997) noted:

The KLD is a registered investment advisor providing social research on US corporations to the investment community. KLD's data base consists of more than 1000 publicly listed traded corporations, each of which has been screened across a broad range of social issues. KLD screens each company annually, using a variety of sources. Each company is rated as neutral (no rating), concern or strength, or major concern or strength within each of eight screening categories. KLD rates in eight socially relevant categories using the following general criteria, with 'other' included for special considerations not encompassed within general criteria (Waddock and Graves (1997: 317).

KLD ratings with respect to stakeholder measurement was used by Waddock and Graves, (1997) in America, but these types of rating for the top 50 Australian firms were not available. This then limited the current study to measuring stakeholder concerns using content analysis of social responsibility disclosures contained in corporate annual reports.

A firm's level of stakeholder concerns was captured by identifying social responsibility disclosures using content analysis procedure. Content analysis, (see, for example, Holsti, 1969; Krippendorf, 1980) has been widely adopted in social responsibility, social performance and social research (for instance, Abbott and Monsen, 1979; Ernst and Ernst, 1978; Guthrie and Mathews, 1985; Maxwell and Mason, 1976; Zeghal and Ahmed, 1990). Content analysis was defined by Abbott and Monsen (1979: 504) as:

a technique for gathering data that consists of codifying qualitative information in anecdotal and literary form into categories in order to derive quantitative scales of varying levels of complexity.

Content analysis takes varying states of complexity. For instance the Ernst and Ernst study (1976) was effectively just "a count of the numbers of instances of a particular social responsibility disclosure" (Gray et al. 1995b: 80). However, several social responsibility studies (Abbott and Monsen, 1979; Beresford and Cowen, 1979; Bowman and Haire, 1975; Zeghal and Ahmed, 1990) and particularly, Guthrie and Mathews(1985) developed this disclosure approach providing some measure of the volume of disclosure. The usefulness of this was in the "assumption that the extent of disclosure can be taken as some indication of the importance of an issue of the reporting entity" (Gray et al. 1995b: 80).

This technique enabled discussion regarding social responsibility reporting to be quantified and summarised for subsequent statistical analysis (Guthrie and Parker, 1989). Content analysis was based upon the computed amount of social responsibility reporting within all written material of each firm's annual report. Trotman and Bradley (1981) reported that as the field has developed, social reporting has become more often incorporated into annual reports.

Location of Social Responsibility Reporting

There were two major issues regarding the location of data (Gray et al. 1995b). The first issue related to which documents were to be used in determining social responsibility reporting and the level of importance of each. The second concerned the location in a particular document (specifically a corporate annual report) at which the data resides and the significance of this.

Researchers in social responsible reporting have considered the first of these issues (Guthrie and Mathews, 1985; Guthrie and Parker, 1989; 1990; Kirkman and Hope, 1992; Roberts, 1991; Zeghal and Ahmed). It would seem from these studies that all forms of communication reaching the public domain were considered to be part of social responsibility disclosure and not restricted to corporate annual reports. Other forms of communication included advertising, housing magazines, employee and environmental reports, and press notices. These other forms are also be seen as part of social responsibility reporting (Zeghal and Ahmed, 1990). All forms of communication by an organisation could be monitored to capture all social responsible reporting by the entity. There was however a major practical problem with this all encompassing ideal (Gray et al. 1995b). It was simply impossible to determine whether all forms of communications can be effectively identified (Zeghal and Ahmed, 1990).

For the current study, this matter was resolved on grounds of pragmatism and consistency with past research in social responsibility reporting the Corporate Annual Report was used as the principal focus of reporting (Gray et al. 1995a). The corporate annual report was not only a statutory document, produced regularly, but it was one of the most important forms of communication of the corporation's construction of its own social imagery (Hines, 1998; Neimark, 1992).

The place of social responsibility reporting within a document was the second major issue of location (Gray et al. 1995b). In considering the corporate annual report various arguments have proposed that location of social responsibility reporting information was significant for the following reasons:

- it is more likely to be read (Chairman's Statement)
- it indicates the importance attached to the issues (Separate Section or Separate Booklet)
- it falls within the auditor's ambit (Statutory Sections)
- it is covered by the auditor and demonstrates the high profile of the issue and/or its integration with mainstream matters of the company (The Directors Report)
- it is fully integrated with the mainstream activities of the organisation (Review of the Year) (Gray et al. 1995a: 83)

Gray et al. (1995a) argued that whilst the above reasons were persuasive "they failed to permit a single unique choice as to why any one location should be preferred" (Gray et al. 1995b: 83). Research studies into social disclosure have yet to ascertain: (1) the value from identifying the location of disclosure; (2) an interpretation regarding the various sections social disclosure types appearing in the annual report; (3) the value of imposing *location* upon data collection and its effect on the overall results (Guthrie and Mathews, 1985; Guthrie and Parker, 1989, 1990). Since it was difficult to establish benefits from the literature on this matter, the data collection did not take into account the location in the corporate annual report of social disclosures.

Measurement of Social Responsibility Reporting

The above section dealt with the location of the data, it is also necessary to determine the methods of capturing social responsibility reporting data. An analysis of the literature suggested “one of two paths: the *number* of disclosures or the *amount* of disclosures” (Gray et al. 1995a: 83). Of these two approaches it was suggested that the latter, although time consuming, provides a richer data set and may in many instances, automatically encompass the first (Cowen, et al. 1987; Guthrie and Mathews, 1985).

The current study in using content analysis nominated for sentences as the unit of analysis using the amount of social responsibility disclosure in corporate annual reports. In past studies there has been much debate surrounding “the unit of analysis one should use in content analysis” (Gray et al. 1995a: 83). From previous studies the common unit units of analysis were written communications in the form of *words, sentences and pages* (verbal and other communications raises somewhat different problems, see, for example: Kassarian, 1977; Krippendorf, 1980; Peterson, 1991). Support for the use of various “*units of analysis*”, relied on the unit of meaning and the degree to which each unit can be used to draw suitable inferences. For instance words were preferred in content collection as they provide “more exclusive analysis (are more easily categorised)” (Gray et al. 1995a: 84). On the other hand sentences were preferred when a researcher was seeking to infer meaning. Overall, pages was the preferred measure as it reflected “the amount of total space given to a topic, and by inference, the importance of that topic” (Gray et al. 1995a: 84). Pages were also the easier unit of analysis as it provided a more reliable unit of measure (Guthrie and Parker, 1989; 1990). There was one problem with measurement of pages out of corporate annual reports and that is the use of different sizes of paper, different margins and different typefaces. It was difficult to come to any straightforward conclusion

about how important this might be. Gray et al. (1995b), examined this problem as part of their data analysis but little effect was obvious and it was far from clear that the small amount of extra information to be gained was worth the extra effort involved-or indeed, whether it makes any significant difference to the interpretation.

From recent research in New Zealand, sentences was suggested as the preferred unit of analysis as other measures, such as social responsibility disclosure as a percentage of annual report page, was problematic (Adler and Milne, 1997; Ng, 1985). Pages, as suggested by Ng (1985) are different in annual reports due to the “ different print sizes, column sizes and page sizes” (Adler and Milne, 1997: 9). Sentences were also used over words measures as evidence suggests that “measuring CSR [Corporate Social Responsibility Disclosure] amount by the number of words leaves the researcher pondering which individual word is a CSR and which is not” (Hackston and Milne, 1996: 84). This was the rationale for the current study’s preference for using sentences as the unit of analysis rather than percentage of page and word count. Use is made of the components of each stakeholder concern dimension in Table 6.2, to identify whether a sentence related to stakeholder concerns. In this way data of stakeholder concern was identified and categorised into individual themes/dimensions. Social responsibility disclosures in corporate annual reports, referred to as a “medium for managing stakeholders” (Adler and Milne, p.4, 1997) are used to gather data on stakeholder concerns for the sample of companies in the current study.

In sum, as the current study seeks to infer meaning from social disclosures, then from the above analysis sentences were the preferred unit of analysis. The current study adopted sentence counting as the unit of measure regarding data collection of social responsibility reporting to infer meaning about managements concern for stakeholders. The dimensions for measuring stakeholder concerns, illustrated in Table 6.2, were used

to code the sentences of social responsibility disclosure into their appropriate stakeholder groups (also refer to Table 4.4, Chapter Four).

6.6 Control Variables

Other variables such as *firm size, leverage, industry classification and mergers & acquisitions* have been suggested, in prior research as “other variables that are likely to effect firm performance” (Tallman and Li, 1997: 188). These other variables were used as control variables, which can affect economic performance which was consistent with other studies (Hitt et al. 1997; Tallman and Li, 1997; Ullmann, 1985; Waddock and Graves, 1997).

Firm Size

The size variable was important because there was evidence that smaller firms may not disclose as much social responsibility behaviour as do larger firms (Waddock and Graves, 1997). It has been suggested that the reason for this behaviour of larger sized firms is, “as they mature and grow, firms attract more attention from external constituents and need to respond more openly to stakeholder demands” (Waddock and Graves, 1997: 308). Firm size was a variable viewed as an indicator of scale economies and market power and there exists empirical evidence that links size to economic performance in the strategic management literature (Bettis, 1981; Grant et al. 1988; Robins and Wiersema, 1995). It was suggested that “cost advantages due to scale economies or control over pricing created by market power may enable large firms to achieve unusually high levels of profit” (Robins and Wiersema, 1995: 286).

Firm size was measured by identifying and recording number of employees from corporate annual reports in the “notes to the accounts” section of the financial

statements. In past research size has not been statistically significant when relating it to economic performance. Some coefficients in studies were found to be either zero or close to zero (Gomes and Ramaswamy, 1999; Hitt et al. 1997; Waddock and Graves, 1997). For completeness and for ease of comparison of one study to another, the current study will continue to use this variable in regression analysis in Chapter Seven.

Leverage

The leverage of a firm was measured using the debt to asset ratio. Evidence in Australian studies suggested that it would be appropriate to choose the ratio of Total Liabilities (TL) to Net Tangible Assets (NTA), referred to as TLNTA, as a proxy measure for the effects of restrictive debt covenants on economic performance (Craig, 1989; Whittred and Zimmer, 1986). It appeared that a firm burdened with large borrowing would have an incentive to increase its economic performance. By increasing current periods economic performance also improve performance over time, then breach of restrictive debt covenants is less likely.

Measures of TL and NTA were obtained from corporate annual reports, obtained from Connect-4 CDRom Corporate Annual Report Service for 1993, 1994 and 1995. Statex definitions of TL and NTA, have been adopted, namely:

NTA = Total assets less intangible assets (including future tax benefit)

less total liabilities

less preferences capital

less minority interest; and

TL = Total external liabilities, excluding ordinary and preference share capital and minority interests.

Industry Classification

Companies from the sample selected are classified according the industry to which they best fit using the “Business Classification Index”, of the “Jobson’s Year Book of Australian Companies”. In this way the sample set can be divided into industry type to determine whether particular relationships tested are industry specific.

Mergers &/Acquisitions

The level of international and national merger and acquisition activity was measured using the mode of business-level and international diversification. Changes in economic performance could also be attributed to the act of diversifying across country borders which may be achieved through mergers and or acquisitions during the period of the current study. Both of these variables have been shown to effect economic performance (Hitt et al. 1997). These variables were measured using the total number of mergers and acquisitions, including both foreign and local ones as disclosed in narrative form in the corporate annual reports (Hitt et al. 1997).

6.7 Aspects of Research Design

Correlation analysis was used to analyse the relationship between each dependent variable and each proxy independent variable in the case of the relationships with stakeholder categories and classifications, international and business level diversification strategy respectively. Linear regression statistical analysis was used to analyse the effects of interrelationships between independent international diversification strategy and stakeholder management variables and their effect on the dependent variable economic performance.

In order to test whether there was a non-linear relationship between economic performance and international diversification as well as economic performance and stakeholder concerns the sample was divided into low to moderate and high levels of international diversification and stakeholder concerns respectively. The Chow test statistic was used to divide the sample into subgroups (Gujarati, 1988; 444). Furthermore, use was made of the F test to determine whether the inclusion of additional explanatory variable(s) to the equation adds to the Estimated Sum of Squares (ESS) (Gujarati, 1988: 226). The significant statistical contribution for each additional explanatory variable was then determined. The variance inflation factor was used to test for degree of multicollinearity between the independent variables together with the correlation matrix

6.7.1 Method of Examining Non-linear relationships

The Chow test was considered as one of the most appropriate ways of testing for differences between two or more regressions (Gujarati, 1988). A Chow test was used to divide the sample into two categories or subgroups, low/moderate and high, for international diversification and for stakeholder management. This provides a test which determined whether there was a suitable cut-off point which divided each of the following variables, international diversification level and the stakeholder involvement, into two or more subgroups,

The Chow test was first used to ascertain whether structural differences existed in the relationship between economic performance and international diversification. This was then followed by application of the Chow technique to determine whether structural differences existed in the relationship between economic performance and stakeholder

management. What this test primarily did was to identify whether structural differences exist. The variables international diversification and social responsibility reporting were tested to establish whether they can take on low/moderate and high levels, and the Chow test again assisted in determining the cut off point at which low/moderate ends and high begins with this sample.

Non-linear relationship between International Diversification and Economic Performance

In order to test for the existence of a non-linear relationship between international diversification and economic performance, the current research used the Chow test to divide the sample of firms into those with low to moderate against those with high levels of international diversification. The rationale for and usefulness of dividing the sample into subgroups was identified in a study by Hitt et al. (1997). Hitt et al. (1997), in analysing their sample, identified two subgroups for international diversification using international diversification scores similar to a method used by Hitt and Middlemist (1978) described in the following quotation:

The analysis suggested two subgroups, firms with international diversification scores below .30 and those with scores of .30 and above. Subgroup 1 was composed of 107 firms with international scores below .30 and subgroup 2 was composed of 186 firms with scores of .30 and above. (Hitt et al. 1997: 784)

In using these subgroups support was provided for an inverse U-shaped curvilinear relationship between international diversification and economic performance (Hitt et al. 1997). Where subgroup 1 represented low to moderate levels of international diversification and was positively related to economic performance whilst subgroup 2 represented high levels of international diversification producing negative results.

The technique used in the current study to determine two subgroups into low to moderate and high levels of international diversification was the Chow test (Appendix II). The Chow test uses F tests to statistically divide the sample into firms with high levels of international diversification from those with low to moderate levels. To this end the Chow test was useful in determining a precise way of identifying a critical cut off point or dividing line (Gujarati, 1999).

In order to address whether there was a non-linear relationship between international diversification and economic performance the current study used a Chow test to establish a critical cut off point which enabled the subdivision of the sample of firms into two sub-groups. The current study divided the sample into two subgroups using the classification of low to moderate and high and used the Chow statistic to statistically identify the cut off point between low/moderate and high levels of international diversification (Appendix III).

Non-linear relationship between Stakeholder concern and Economic Performance

In order to test for the existence of a non-linear relationship between stakeholder concern and economic performance, the current research used the Chow test to divide the sample of firms into those with low to moderate against those with high levels of stakeholder involvement. Previously Bowman and Haire (1975) used the proportion of lines of social responsibility prose in corporate annual reports as a useful measure. This compares with the current study that used sentences of social responsibility as the unit of analysis.

In order to address whether there was a non-linear relationship between stakeholder concerns and economic performance the current study used a Chow test to establish a critical cut off point which enabled the subdivision of the sample of firms into two sub-

groups. The current study divided the sample into two subgroups using the classification of low to moderate and high and used the Chow statistic to statistically identify the cut off point between low/moderate and high levels of stakeholder concern.

6.7.2 The Incremental or Marginal Contribution of an Explanatory Variable

A further test was used to determine if an additional explanatory variable(s) introduced to a model, significantly contributes to the explanatory power (Gujarati, 1988). Contribution is defined to mean the additional explanatory variable increases the Explained Sum of Squares (ESS) and thus R^2 in a statistically significant way. This is termed the incremental or marginal contribution of an explanatory variable.

This statistical technique was used to determine the marginal contribution of adding in two interactive effects on economic performance. The two interactive effects which are pertinent to the current study are, business level with international diversification (BLID) and country scope with international diversification (CSID). The technique was used to determine the statistical significance of the incremental contribution of BLID and similarly of the incremental contribution of CSID on economic performance.

This particular test utilises the F test (recast using the R^2 values only) (Gujarati, 1988: 227). The F ratio is:

$$F = \frac{(R^2_{\text{new}} - R^2_{\text{old}})/df}{(1 - R^2_{\text{new}})/df}$$

$$= \frac{(R^2_{\text{new}} - R^2_{\text{old}})/\text{Number of new regressors}}{(1 - R^2_{\text{new}})/df (= N - \text{number of parameters in the new model})}$$

The F test will provide a value which then is compared with the F Critical, then if F is greater than F Critical the null hypothesis is rejected. The *null hypothesis* is: “that the inclusion of an additional explanatory variable does not successfully increase ESS” (Gujarati, 1988: 226).

6.7.4 Degree of Multicollinearity

Detection of multicollinearity provided information regarding the degree of linearity between the explanatory variables X_s , in a multiple regression (Gujarati, 1999: 313). Multicollinearity is a matter of degree and essentially a sample (regression) phenomenon. In essence what should be kept in mind are the following issues that relate to multicollinearity:

1. Mutlicollinearity is a question of degree and not kind. The meaningful distinction is not between the presence and absence of multicollinearity, but between its various degrees.
2. Since multicollinearity refers to the condition of the explanatory variables that are assumed to be non-stochastic, it is a feature of the sample and not the population . Therefore we do not test for multicollinearity but can, if we wish, measure its degree in any particular sample (Gujarati, 1999: 322).

There are a number of ways of detecting multicollinearity the two that were used in the current study are the correlations matrix and the Variance Inflation Factor (VIF). These are rule of thumb measures, or indicators that provided evidence about the existence of multicollinearity (Gujarati, 1999). In the first instance the correlation matrix provided numerical indicators between the X_i explanatory variables. If these figures were greater than an arbitrary number, such as 0.80, then there was a concern for the degree of multicollinearity (Studenmund, 1985: 273).

A measure of the severity of multicollinearity, that has gained popularity, was the variance inflation factor (Hitt et al 1997; Studenmund, 1985). The VIF was a method which detected the multicollinearity (refer to Appendix VI) by analysing the extent to which a given explanatory variable can be explained by all other explanatory variables in the equation.

6.8 Summary

This chapter has explained the research methods adopted, including sample selection techniques and data collection procedures. The business level and international diversification strategy together with stakeholder concern independent variables, as well as the economic performance dependent variable, were defined more precisely. Data sources and data collection methods applicable to each of the variables were also explained.

A three year continuous period covering 1993-1995 was considered which assisted in identifying consistency of these relationships over time. The Chow-test was used on the data set to determine whether there exists a cut-off point between low/moderate and high levels of international diversification. The nature and form of stakeholder concerns will be tested to determine whether a structural division between low/moderate levels of stakeholder management and high level exists. Second, for international diversification strategy, tests will be undertaken to determine whether subgroups are identified as low to moderate levels as distinct from high levels. In both instances the Chow statistic will be utilised to determine a level of statistical significance for cut off points for international diversification and stakeholder management. The Chow test provided a statistical technique to test whether there was a non-linear relationship between economic performance and international

diversification on the one hand and economic performance and stakeholder concerns on the other.

A further issue was the method of dividing stakeholders into two categorical measures, primary and secondary, which enables the current study to identify whether firms were more likely to prefer one category against the other as they effected economic performance. This reflects a form of trade-off.

Linear regression using SPSS statistical package was selected as the statistical analysis technique chosen to run the appropriate regressions, Chow tests and F tests. Use was made of the statistical values of, Chow test statistics, F-tests, Durbin Watson statistics, R^2 , Adjusted R^2 , and p values to test the explanatory power of the independent variables on economic performance.

CHAPTER SEVEN

RESEARCH FINDINGS

7.1 Introduction

Chapter One identified the purpose of this research study as investigating whether strategic and international business diversification with stakeholder concerns enhances economic performance. It identified the need to develop a socioeconomic framework, which incorporates transactions cost, resource-based and instrumental stakeholder theory, for investigating economic performance. Chapter Two developed a socioeconomic model examining the effect that strategic management, international business diversification and stakeholder concerns has on economic performance. Chapter Three examined the relationship between business-level diversification strategy and economic performance, the interaction of international diversification with business-level diversification on economic performance. Then an analysis of the interaction of multinationality with country scope on economic performance was considered. The importance of transaction costs effects on this relationship was then examined providing evidence of a non-linear relationship between international diversification and economic performance. Chapter Four examined the relationship between stakeholder management and economic performance. The chapter provided evidence to support using social responsibility disclosures themes from corporate annual reports as a way of identifying stakeholder concerns and that these concerns are positively related to economic performance. Chapter Five developed a socioeconomic theoretical framework for investigating economic performance. The various multidisciplinary determinants of economic performance that the study investigated include business level diversification strategies, international diversification strategies and stakeholder concerns of firms. Chapter Six specified and discussed the study's research. In identifying and evaluating the strategic, international business management and stakeholder variables the current study focused upon large listed Australian public companies. Also aspects of the research design adopted, including sample selection techniques and data collection

procedures will be examined. Data sources and data collection methods applicable to each of the variables are also explained.

This chapter presents the statistical findings from an analysis of the data. From the findings a case was developed for using ROA as the most appropriate dependent variable, in an Australian context. Results from hypotheses testing are provided. Furthermore, year by year analysis was also attempted but most questions could not be addressed as a result of a reduced sample size. The next section considered the effect of the combined international and business level diversification with stakeholder concern on economic performance, which included incorporation of interactive effects of particular independent variables. Furthermore, consideration was given to the non-linear characteristics of international diversification on economic performance together with those of stakeholder concerns on economic performance, when testing for the combined effect on economic performance. The final section examined two major issues (1) whether the interaction of business-level with international diversification combined with stakeholder concerns effects economic performance and (2) whether the combined effect of international diversification with stakeholder concerns effects economic performance.

7.2 Selection of the most appropriate Dependant Variable

Out of all the five measures of economic performance (ROA, ROS, ROE, DPS and EPS), from testing it was found that the accounting- based dimension, in particular, ROA was the most appropriate measure. The regressions with ROA as the dependent variable provided better statistical properties than regressions with ROS and ROE (the other accounting-based measures of performance). With regards to the market-based measures of economic performance, Earnings Per Share (EPS) and Dividends Per Share (DPS), the regression analysis for all hypotheses tested found nothing of significance to

report. The current study therefore does not support construct convergence but suggests that accounting-based measures provided the best statistical results.

7.3 Results from Hypotheses Testing

The sample was divided into *industry classification* however the resultant sample of firms within each classification was not included in the regression analysis as the sample size reduced to less than 20 firms rendering statistical analysis inappropriate. The exclusion of industry classification was further justifiable as its inclusion would have reduced the degrees of freedom to unacceptable levels. This was a limitation of the study thus all industries were considered in aggregate in the following regression analysis.

As the sample required averaging, the total number of firms was reduced from 150 to 88 as a result of the same firm appearing more than once in the three years under study. Table 7.1 reported the means, standard deviations and intercorrelations for all variables in the model. There were no major problems of multicollinearity, which is supported, in the first instance from results in the correlation matrix in Table 7.1. These results are all less than 0.80 for each intercorrelation, which provides support for the absence of severe multicollinearity (Studenmund, 1985: 273). Furthermore, use was made of the Variance Inflation Factor (VIF) to analyse the degree of multicollinearity by measuring the size of the VIF. As there is no table of formal critical VIF values, a common rule of thumb is that severe multicollinearity exists if $VIF > 5$ (Studenmund, 1985: 273). These VIF's are present in each of the regression tables that follow and include Table 7.3.

7.3.1 Testing the Effects of Business-Level Diversification on Performance

In testing the effects of business-level diversification on economic performance, evidence from Chapter Three suggested, that related business-level diversification is far better than unrelated diversification in explaining higher performance. Hypothesis H₁:

Table 7.1
Correlations, Means and Standard Deviations

Variables	2	3	4	5	6	7	8	9	10	11	12	Mean	Sd
1. ROA	.098	-.252**	-.033	-.141*	-.117#	.023	.045	.023	.053	.057	.112#	.11	.31
2. Number of Employees		.142*	.282*	.295*	.273*	-.172*	-.267*	-.019	.107#	.148*	.182*	12772	3848
3. Leverage			.118#	.171*	.174*	-.030	.029	.079	.048	-.101	-.022	.92	2.79
4. No. International Reg				.495**	.480**	-.210**	-.313**	.134*	.232**	.255**	.256**	7.45	8.08
5. International Diversif					.458**	-.281**	-.324**	.135*	.142*	.124	.218**	.22	.28
6. Mergers and Acquisit						-.311**	-.347**	.023	.076	.064	.172*	.49	.50
7. Related Diversificatio							.598**	-.039	-.048	-.033	-.142*	86	23
8. Unrelated Diversif								.068	-.100	-.158*	-.229**	74	14
9. Community related									.355**	.314**	.234**	3.9	4.88
10. Employee related										.427**	.440**	8.2	8.06
11. Environmental rel											.329**	6.9	9.1
12. Product Safety rel												2.1	2.8

Kendall's tau-b Correlations Sig. (1-tailed)

**Correlation is significant at the .01 level

*Correlation is significant at the .05 level

#Correlation is significant at the .10 level

n=88

was tested to determine whether there was support for related rather than unrelated business diversification on economic performance:

H₁: Firms pursuing related diversification will perform better than those firms pursuing unrelated diversification.

In the process of selecting the variables referred to in Table 7.2 for testing the sample size was reduced from 88 to 82 as a result of missing data. The zero coefficients for both related and unrelated diversification and the low R² value of .017 together with no levels of significance indicate that there was no support for hypothesis H₁.

Neither related nor unrelated business-level diversification was statistically significant and the R² is not high. This result does not support prior research of better results of related over unrelated business-level diversification on economic performance. This means that, in the current sample, business level diversification does not enhance economic performance.

Table 7.2

Effects of Business-Level Diversification on ROA

Independent Variables

Intercept	.075 (0.141)
Number of employees	-0.000 (0.000)
Debt/Assets	0.0004 (0.002)
Local Mergers	0.069 (0.079)
Related Diversification	0.0000 (0.002)
Unrelated Diversification	-0.0000 (.002)
R ²	.017
Adjusted R ²	-.048
F	.257
D-W	2.121

Standard errors are shown in parentheses. For n=82

DW: refers to the Durbin-Watson statistic

* p< .05

**p< .01

#p<.10

When analysing the firm size variable using number of employees as a proxy, one also obtains a zero coefficient in the regression. Removing this from the table may seem the better option, but other studies that also considered firm size variables, (alternatively measured as sales) and have also recorded a similar zero result in their table of results.

The current study has recorded the same zero result for consistency and comparison with other studies which have recorded size to performance results with near zero or zero coefficients (Hitt et al. 1997; Tallman and Li, 1996; Waddock and Graves, 1997). All regression henceforth which had zero or near zero results for the size variable are included in the appropriate tables.

The next regression to consider was the effect of international diversification on economic performance and in particular testing for evidence of a non-linear relationship that may exist as identified in Chapter Three.

7.3.2 Testing the Effects of International Diversification on Economic Performance

In testing the three years covering 1993-1995 the statistical results in the current study, reveals that there was a significant structural difference between economic performance and international diversification. A selection of international diversification measures, of the ratio of international sales to total sales measuring multinationality, were analysed using the Chow test. Of all the ratios examined the results showed that international sales to total sales at the 35% was the critical cut-off point. This result identified two subgroups, firms with international diversification less than 35% as low/moderate and those firms with greater than or equal to 35% of international sales to total sales as high level diversification. The Chow test was applied to the sample, to determine if the Chow F statistic exceeds the critical F value (refer table D.3 Gujarati, 1995: 814) and if so this result justifies rejecting the null hypothesis.

The results from that Chow test suggested rejection of the null hypothesis (for the detailed calculation refer to Appendix V). The result was that $F_{chow} 5.8 > F_{Critical} 2.56$ by a significant amount therefore the null hypothesis is rejected and the 35 % cut off point is recognised as a statistically robust measure for dividing the international diversification strategy into low/moderate and high at that level for the sample covering three years 1993-1995.

Table 7.3
Effects of International Diversification on ROA

Independent Variables	Model 1	Model 2
	Low/moderate	high level
Intercept	.0242 (0.091)	.0975 ** (0.024)
Number of employees	-0.000 (0.000) (1.005)	-0.000 (0.000) (1.145)
Debt/Assets	0.0031 (0.091) (1.010)	0.0038 ** (0.002) (1.191)
Mergers and Acquisitions international	-0.166 # (0.022) (1.466)	-0.009 (0.110) (1.262)
Country Scope	0.0214 ** (0.008) (1.623)	0.0000 (0.001) (1.383)
Multinationality	.554 * (.440) (1.642)	-.043 # (0.031) (1.098)
R ²	.241	.310
Adjusted R ²	.168	.107
F	3.295 **	1.528
D-W	2.063	3.125

Standard errors are shown in first parentheses; variance inflation factors are in the second parentheses.

For model-1, n=58; For model-2, n=23

DW: refers to the Durbin-Watson statistic

* p < .05

** p < .01

p < .10

Chow tests performed for each individual year of the study also revealed that the 35 % cut off point is the critical cut off point for dividing international diversification strategy into low/moderate and high at that level. The calculations for the Chow test for each

individual year covering 1993-1995 are detailed in Appendix VI. In sum, there is evidence using the Chow statistic to divide each individual year of the sample in to high and low/moderate levels.

This division of the sample into low/moderate and high now permits a non-linear analysis of the relationship between economic performance and international diversification as the sample can now be split into subgroups using this 35% cut off point. Table 7.3 illustrates the results of a regression of the relationship between international diversification and economic performance to determine the level of linearity that does or does not exist in this relationship.

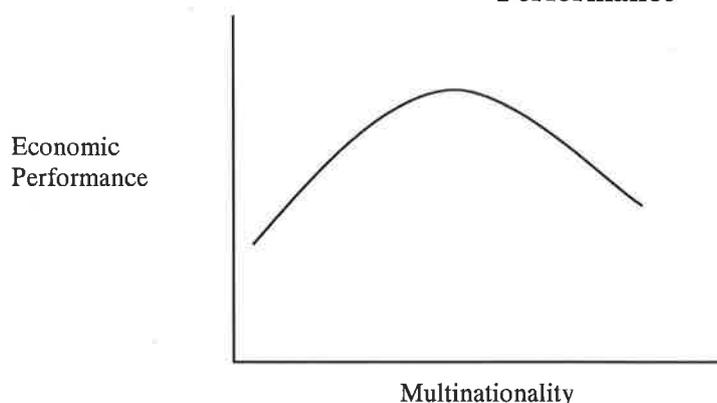
In testing the effects of international diversification on economic performance, two measures of international diversification were used, as described in Chapter Three. Multinationality was one measure which refers to the percentage of foreign sales to total sales, whilst the other independent measure, country scope refers to the number of geographic regions/markets. To examine the effect of multinationality and economic performance hypothesis $H_{2.1}$ was tested:

H_{2.1}: The relationship between economic performance and multinationality is non-linear, with a positive slope at low/moderate levels of international diversification but negative at the high levels of international diversification

Model 1, which was composed of 58 firms as a result of missing data, refers to the subgroup at the low to moderate levels of international diversification. Model 2, which was composed of 23 firms as a result of missing data, refers to the subgroup at the high level of international diversification. Results in Table 7.3 provides support for hypothesis $H_{2.1}$ as the relationship between multinationality is positive and significant at the low/moderate level of international diversification for model 1 at the $p < .05$ level. Whilst at the higher level of international diversification, in model 2 there is a negative and significant relationship between multinationality and economic performance at the $p < .10$ level. The overall significance of model 1 is quite strong reflected by the F test

significant at the $p < .01$ level, whilst the Durbin-Watson statistic does not show any major problem of autocorrelation. These results supported the hypothesised non-linear relationship between multinationality and economic performance. Moreover, this outcome provides further evidence for a curvilinear relationship between international diversification and economic performance with a positive slope at lower levels of international diversification, but negative at the higher levels of international diversification. This inverted U-shaped relationship is represented in Figure 7.1 (Gomes and Ramaswamy, 1998; Hitt et al. 1994).

Figure 7.1
The Curvilinear Model: The Effect of International Diversification on Economic Performance



The height and steepness of the curve on Figure 7.1 can vary by “firm, its ability to manage complexities, the type of diversification undertaken and country or regional location” (Hitt et al. 1994: 312).

Results from Table 7.3 provides evidence of hypothesised negative effects of transactions costs on economic performance as the firm seeks to achieve higher levels of international diversification. Further findings from the results in Table 7.3 reveal that the significance, at the $p < .01$ level, of the relationship between country scope on economic performance, in model 1, is at the low/moderate level of international diversification. The overall significance of model 1 was quite strong reflected by the F test significant at the $p < .01$ level whilst the Durbin-Watson statistic did not show any

major problem of autocorrelation. This level of significance was lost at the higher levels of international diversification, in model 2, although the sign is still positive. This suggested that there was a significant relationship between country scope and economic performance at the low/moderate levels of international diversification rather than at the higher levels.

There was no support for hypothesis H: 2.2 however there was a positive and significant relationship between economic performance and country scope at the low to moderate levels of international diversification and as the level of international diversification moves beyond the critical cut-off point the significance diminished:

H_{2.2}: The relationship between economic performance and country scope is non-linear, with a positive slope at low/moderate levels of international diversification but negative at the high levels of international diversification

The next issue for consideration was to test for the effect of the interaction between international and business level diversification on economic performance.

7.3.3 Testing the Interactive effects of International and Business-level Diversification on Economic Performance

In testing the interactive effects of international and business-level diversification on economic performance the following hypotheses H_{3.1} and H_{3.2} are tested:

H_{3.1}: There is a positive relationship between economic performance and the interaction of multinationality with unrelated business diversification.

H_{3.2}: There is a positive relationship between economic performance and the interaction of multinationality with related business diversification.

In testing the relationship reflective of hypotheses H_{3.1} and H_{3.2} consideration was given to the interactive variables; related diversification x multinationality and unrelated x multinationality in model 2, Table 7.4. The effect of this addition was R² increases from .428 to .660, measuring an improved goodness of fit, which implied that the

addition of these two interactive variables considerably improved economic performance.

Table 7.4

Interactive Effects of International & Business-Level Diversification on ROA

Independent Variables	Model 1	Model 2
Intercept	-.455 (.449)	-.082 (.400)
Number of Employees	-0.000 (0.000)	0.000 (0.000)
Debt/Assets	- .087 (.428)	.130 (.365)
Mergers and Acquisitions	(1.09) -.459 # (.326)	(1.166) -.216 (.284)
Country Scope	(1.410) .095 ** (0.023)	(1.440) .096 ** (.019)
Multinationality	(1.776) -1.45 (1.618)	(1.795) -9.394 (2.668)
Related Diversification	(1.349) -.006 (.008)	(10.416) .0017 (.013)
Unrelated Diversification	(1.817) .0139 * (.008)	(3.076) -0039 (.013)
Related Diversification x Multinationality	(2.314)	(3.289) -.009 (.059)
Unrelated Diversification x Multinationality		(18.867) .127 * (.063)
		(11.235)
R ²	.428	.660
Adjusted R ²	.348	.538
F	3.587 **	5.397 **
D-W	2.297	1.560

Standard errors are shown in parentheses ; variance inflation factors are in the second parentheses.

For both models, 1 and 2 n=81. DW: refers to the Durbin-Watson statistic

* p < .05

** p < .01

p < .10

The overall fit of the model was improved as reflected by the F test result and the Durbin-Watson statistic moved below 2 which implies that there is no problem with

autocorrelation in model 2, Table 7.4. In considering the effect of each individual interactive effect the unrelated x multinationality was statistically significant and positive whilst for related x multinationality it was negative and not statistically significant. This supported hypothesis H_{3,1} and not H_{3,2}, which suggested that unrelated business diversification enhanced the relationship between economic performance and international diversification, but does not for related diversification. Kim et al. (1989) provided evidence that an “integrated unrelated-product and international diversification strategy helped achieve profit growth” (Hitt et al. 1997: 776). Hypothesis H_{3,1} provided added support for Kim et al’s (1989) findings. An explanation for this result was that “unrelated product diversification spreads the risk across product markets, thereby reducing the probability of severe losses and increasing the probability of achieving a positive return (Hitt et al. 1997: 776).

To determine the statistical contribution of adding the interactive variables to model 2 the F test was used to statistically determine whether a set of variables adds explanatory power. The *null hypothesis* for the F test was, that the addition of two explanatory variables in related-diversification x international diversification and unrelated diversification x international diversification do not successfully increase ESS (Explained Sum of Squares). This null hypothesis was derived from Gujarati (1988) “that the inclusion of additional explanatory variables does not successfully increase ESS” (Gujarati , 1988: 226). The formula described in the previous chapter (section 6.7.2) was used to determine whether to reject or accept the null hypothesis. In applying that formula $F = 24.68$, whilst $F(2, 72) = 3.46$, (Gujarati, 1988: 682, Table D 3) which was F critical from the tables. Since F value equated to 24.68 and was greater than F critical, which equates to 5.18, the null hypothesis was rejected. The results here clearly indicated that the null hypothesis, stated above, can be rejected which provided further and refined statistical support for the significant contribution of these two additional variables in the model, using standard statistical techniques (Gujarati, 1988).

The impetus for this test was a recent study of Hitt et al. (1997), in determining whether a relationship existed between the interaction effect of business level diversification and international diversification on ROA. In particular, the statistically significant and positive effect of the interaction on ROA provided further additional statistical support for Hypothesis H_{3.1}. It was significant at the $p < .05$ and the positive sign indicates that firms with business level diversification which are unrelated show an enhanced performance as these firms diversify internationally. The next section further considers this relationship but tests for the existence of a critical cut-off point in determining whether there is a non-linear relationship.

7.3.4 Testing the Interactive Effects of International & Business-Level Diversification on Economic Performance: When Consideration is given to the Critical Cut-off Point.

In further testing the interactive effects of international and business-level diversification on economic performance, consideration was given to the effect of a critical cut-off point. In Table 7.5 the sample was divided into model 1 which represented low to moderate international diversification, comprising of 58 firms, whilst model 2 considered firms with high levels of international diversification, comprising 23 firms. This subdivision of the sample allowed for testing of hypothesis H_{3.3}.

H_{3.3}: The relationship between economic performance and the interaction of multinationality with unrelated business diversification is non-linear, with a positive slope at low/moderate levels of international diversification but negative at the high levels of international diversification

The integrated unrelated business-level diversification with international diversification showed a positive sign, at the low/moderate level, on economic performance. On the other hand for higher levels of international diversification there is a negative relationship between unrelated business-level diversification with international diversification on economic performance. This did not provide support for hypothesis H_{3.3}.

Table 7.5

**Interactive Effects of International & Business-Level Diversification on ROA:
When Consideration is given to the Critical Cut-off Point.**

Independent Variables	Model 1	Model 2
	Low/moderate	high level
Intercept	.0193 (0.093)	.102** (0.025)
Number of employees	-0.000 (0.000)	-0.000 (0.000)
Debt/Assets	0.0031 (0.091)	0.0046 ** (0.002)
Mergers and Acquisitions	-0.159 # (0.113)	-0.021 (0.026)
Country Scope	0.0217 ** (0.008)	0.0004 (0.001)
Multinationality	.420 (.768)	0.014 (0.06)
Related Diversification x Multinationality	-0.0038 (.014)	-0.0006 (0.001)
Unrelated Diversification x Multinationality	.007 (.014)	-0.00006 (0.001)
R ²	.245	.354
Adjusted R ²	.140	.052
F	2.324 **	1.172
D-W	2.040	3.131

Standard errors are shown in parentheses; variance inflation factors are in the second parentheses.

For model-1, n=58; For model-2, n=23

DW: refers to the Durbin-Watson statistic

* p < .05

**p < .01

p < .10

This further supports Hitt et al. (1997) finding that there is a non-linear relationship between international diversification and economic performance. What these current findings add was the interactive effect on economic performance using a subgroup analysis similar to that proposed by Hitt et al. (1997).

There was no support for hypothesis H:_{3,4} as related diversification x multinationality was negatively related to economic performance at both low/moderate and high levels of international diversification. Where H: _{3,4} referred to:

H: _{3,4} The relationship between economic performance and the interaction of multinationality with related business diversification is non-linear, with a positive slope at low/moderate levels of international diversification but negative at the high levels of international diversification.

Another interactive effect on economic performance identified was that between multinationality and country scope on economic performance (Tallman and Li, 1996). Where two independent measures of economic performance, multinationality and country scope are identified and the interaction of them on economic performance tested. The next section tested this interactive effect on economic performance for the three-year period under consideration in the current study for Australian firms.

7.3.5 Testing the Interactive Effects of Multinationality and Country Scope on Economic Performance

In testing the interactive effects of multinationality and country scope on economic performance the sparse evidence from past studies, considered in Chapter Three, suggested that firm's performance should vary positively with the interaction of multinationality and country scope (Tallman and Li, 1996). The implication here is that international scale economies from multinationality and geographical scope economies from country scope "address different aspects of internationality and are not identical in their performance effects" Tallman and Li, 1996: 185). What has been identified is that the interaction of multinationality and country scope on economic performance is positive (Tallman and Li, 1996). Hypotheses developed in Chapter Five reflect the two aspects of international diversification (multinationality and country scope) and the positive effect the interaction of them may have on economic performance in H:_{3,5}

H: _{3,5} There is a positive relationship between economic performance and the interaction of multinationality with country scope

In testing hypotheses H_{3.5} consideration was given to the addition of interactive variables; country scope x multinationality in model 2, Table 7.6. The effect of this addition was R² increases from .428 to .537. There was a statistically significant and positive relationship between the interaction of international diversification and country scope on economic performance. The F test indicated that there was a high level of significance at p<.01 and no problems with autocorrelation indicated by the Durbin-Watson statistics. This additional variable provided further support for a recent study of Tallman and Li (1996) and adds support to hypothesis H_{3.5}.

A further refinement in support of this finding was to statistically establish the contribution of this additional explanatory variable to the equation. The F test was used to statistically determine whether a set of variables adds explanatory power. In applying the appropriate formula as was used previously in section 7.3.3, F = 18.166 whilst F (1, 73) = 9.76, (Gujarati, 1988: 682, Table D 3) which was F critical from the tables. Since F value equated to 18.166 and is greater than F critical, which equated to 7.31, the null hypothesis is rejected. The results here clearly indicated that the null hypothesis, stated above, can be rejected which substantiates statistically the important contribution of the additional variable in this equation using standard statistical techniques (Gujarati, 1988).

The results from Table 7.6 provided further support for a positive interaction of multinationality and country scope on economic performance as was the case for Tallman and Li, (1996). The statistically significant and positive effect of this interaction on ROA in the current study provided further additional statistical support for hypothesis H_{3.5}. It was significant at the p< .01 and had a positive sign which indicated that firms with a combined country scope and multinationality exhibited enhanced performance. The next section of work takes the relationship between the interactive effects of country scope and multinationality on economic performance but further refined the analysis by also accounting for the critical cut-off point previously established.

Table 7.6

Interactive Effects of Multinationality and Country Scope on ROA.

<u>Independent Variables</u>	<u>Model 1</u>	<u>Model 2</u>
Intercept	-.445 (.449)	-.114 (.177)
Number of Employees	-0.000 (0.000) (1.017)	-0.000 (0.000) (1.017)
Debt/Assets	-.087 (.428) (1.09)	-.052 (.074) (1.150)
Mergers and Acquisitions	-.459 # (.326) (1.410)	-.213 (.092) (1.564)
Country Scope	.095 ** (0.023) (1.776)	-.013 # (.010) (4.166)
Multinationality	-1.45 (1.618) (1.349)	-1.159 (.478) (4.926)
Related Diversification	-.006 (.008) (1.879)	.0025 (.003) (1.915)
Unrelated Diversification	.0139 * (.008) (2.314)	.0008 (.002) (2.409)
Country scope x Multinationality		.178 ** (.034) (8.264)
R ²	.428	.537
Adjusted R ²	.348	.461
F	3.587 **	7.091 **
D-W	2.297	1.777

Standard errors are shown in parentheses ; variance inflation factors are in the second parentheses.

For both models, 1 and 2 n=81. DW: refers to the Durbin-Watson statistic

* p< .05

**p< .01

#p<.10

7.3.6 Testing the Interactive Effects of Multinationality & Country Scope on Economic Performance: When Consideration is given to the Critical Cut-off Point.

In further testing the interactive effects of multinationality and country scope on economic performance relationship further consideration was given to the effect of a critical cut-off point. Table 7.7 divided the sample into model 1, which represented low

to moderate levels of international diversification, whilst model 2 considered firms with high levels of international diversification. This arrangement allowed for testing of hypothesis H_{3.6}:

H_{3.6} The relationship between economic performance and the interaction of multinationality with country scope is non-linear, with a positive slope at low/moderate levels of international diversification but negative at the high levels of international diversification.

Table 7.7
Interactive Effects of International Diversification & Country Scope on ROA:
When Consideration is given to the Critical Cut-off Point

Independent Variables	Model 1	Model 2
	Low/moderate	high level
Intercept	-.114 (0.177)	.145 ** (0.053)
Number of employees	-0.000 (0.000) (1.011)	-0.000 (0.000) (1.22)
Debt/Assets	-0.052 (0.074) (1.60)	0.0044* (0.002) (1.381)
Mergers and Acquisitions	-0.02 (0.092) (1.594)	-0.009 (0.029) (2.01)
Country Scope	-0.013 # (0.010) (4.56)	-0.0013 (0.004) (10.52)
Multinationality	-1.159 ** (.478) (2.985)	-0.071 (0.084) (7.299)
Related Diversification	.0025 (.003) (2.298)	-.0003 (.001) (1.612)
Unrelated Diversification	.0008 (.002) (2.785)	-.00008 (.000) (2.380)
Country Scope x Multinationality	.178 ** (.034) (5.917)	0.0028 (0.006) (18.86)
R ²	.537	.359
Adjusted R ²	.461	-.008
F	7.091 **	.979
D-W	1.777	3.026

Standard errors are shown in parentheses; variance inflation factors are in the second parentheses.

For model-1, n=58; For model-2, n=23

DW: refers to the Durbin-Watson statistic

* p < .05

** p < .01

p < .10

The critical cut-off point created two subdivisions, which assisted in determining the signs of the coefficients and the level of significance at both the low/moderate and high levels of international diversification. The findings provided support for a positive and statistically significant relationship, at the $p < .01$ level, between economic performance and the interaction of country scope with multinationality, in model 1 at the low to moderate level of activity. There was no negative statistically significant relationship between the interaction of multinationality and country scope in model 2. Although hypothesis $H_{3,6}$ was not supported there is enhanced economic performance at the low to moderate level of international diversification over the higher level. The F test was significant in model 1 at the $p < .01$ level and showed no significance in model 2.

Furthermore, there were no autocorrelation problems in model 1, but there seemed to be problems of autocorrelation in model 2 with the Durbin-Watson statistic at 3.026. The overall result of model 1 and 2 may indicate/reflect a firm's concern for transaction costs when international diversification goes beyond a particular level as evidenced in past research (Geringer et al. 1989; Gomes and Ramaswamy, 1999; Hitt et al. 1997).

The next step in the data analysis was to test the relationship between stakeholder concerns on economic performance and also to determine whether there is evidence of a critical cut-off point in this relationship which would further suggest non-linear relationship.

7.3.7 Testing the Effects of Stakeholder Concerns on Economic Performance

Use was made of the Chow statistic to statistically identify whether such a critical cut off point exists between low/moderate and high levels of stakeholder involvement (Gujarati, 1999). It was found that from the Chow test, when using less than 15 sentences of social responsibility prose, firms were performing better than those at 15 and above. The cut-

off point of 15 sentences was then established and firms below that level were described as having concern for stakeholders at the low to moderate range. Whilst firms disclosing greater than or equal to 15 sentences of social responsibility prose were described as having a high level of concern for stakeholders. In applying the Chow test it was found that the Chow F statistic exceeds the critical F value (refer table D.3 Gujarati, 1995: 814) thus rejecting the null hypothesis (refer to Appendix VII for further calculations). The result was that $F_{\text{Chow}} > F_{\text{Critical}}$ by a significant amount therefore the null hypothesis was rejected and the “15 sentences-of-prose” cut off point is recognised as a robust measure for dividing stakeholder concerns into low/moderate and high level for the sample covering three years 1993-1995.

When consideration was also given to Chow tests for each individual year of the study the “15 sentences-of-prose” was again found to be the critical cut-off point for dividing stakeholder concerns into low/moderate and high (refer to Appendix VIII for further calculations).

In sum, results from the Chow statistic provided strong justification for dividing the sample into high and low/moderate for each of the individual years and the null hypothesis can be rejected in all cases. This result enabled consideration to be given to low to moderate and high levels of stakeholder involvement when testing the relationship between economic performance and stakeholder management. It was found that 40 firms exhibited low to moderate levels of activity whilst the remaining 42 were high levels.

The division of the sample into low to moderate levels of stakeholder concern enabled a test for a non-linear relationship between economic performance and stakeholder concerns by splitting the sample of firms into subgroups using this 15 sentences of prose cut-off point. Table 7.8 provided results of a regression of the relationship between

stakeholder concerns and economic performance for the purposes of determining the level of linearity that does or does not exist in this relationship.

Table 7.8

Effects of Stakeholder Management on ROA.

Independent Variables	Model 1	Model 2
	Low/moderate	high level
Intercept	.073 (.137)	.139 ** (.048)
Community related	.08 * (.039) (1.344)	-.005# (.002) (1.135)
Employee	.0104 (.021) (1.440)	-.0015 (0.003) (1.322)
Product safety	.058 (.066) (1.072)	-.006 (.006) (1.239)
Environment	-.019 (.024) (1.218)	0.0035* (0.002) (1.418)
Leverage	-.089 (.121) (1.104)	-.002* (.005) (1.25)
Number of employees	-.000 (0.000) (1.043)	0.0000 (0.000) (1.158)
R ²	.229	.143
Adjusted R ²	.089	-.004
F	1.632#	.975
D-W	2.282	2.023

Standard errors are shown in parentheses ; variance inflation factors are in the second parentheses.

For low/moderate n=40, for high level , n=42

DW: refers to the Durbin-Watson statistic

* p< .05

**p< .01

p <.10

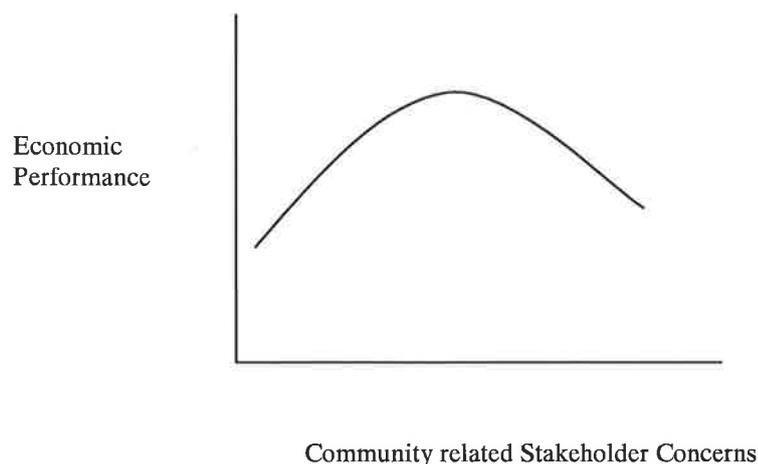
In testing the effects of stakeholder concerns on economic performance use was made of the four stakeholder groups; community, employee, product safety (customers) and environment related, as identified and developed in Chapter Four, Table 4.4. Stakeholder concerns was measured using these four groups using social responsibility disclosures in corporate annual reports as a medium for stakeholder concerns (Adler and Milne, 1997; Hackston and Milne, 1996). To test the effect of stakeholder concerns on economic

performance when consideration is given to the critical cut-off point the following hypothesis H:4.1. was tested:

H: 4.1 The relationship between economic performance and stakeholder concerns are non-linear, with a positive slope at low/moderate levels of stakeholder involvement but negative at the high levels of stakeholder involvement.

Model 1, which was composed of 40 firms, refers to the subgroup at the low to moderate levels stakeholder concerns, showed a positive and statistically significant relationship between community stakeholders and economic performance at the $p < .05$ level. Furthermore, the overall significance of model 1, was reflected in the significance of the F statistic at the $p < .10$ level. Model 2, which comprised 42 firms, referred to the subgroup at the high level of stakeholder concerns, showed a negative and significant result of the relationship between community stakeholders and economic performance at the $p < .10$ level. Table 7.8 provided support for hypothesis H:4.1 but only for the relationship between community stakeholder concerns and economic performance. What the results from Table 7.8 provided was support for the hypothesised non-linear relationship between economic performance and community stakeholder concerns. This inverted U-shaped relationship can be represented in Figure 7.2.

Figure 7.2
The Curvilinear Model: The Effect of Stakeholder Concerns on Economic Performance



At the low to moderate level of community related stakeholder involvement there was a positive and significant relationship with economic performance at the $p < .05$ level. Whilst at the high level of community related stakeholder involvement there was a negative and statistically significant relationship with economic performance at the $p < .10$ level. Moreover, this outcome provided further evidence of a non-linear relationship between stakeholder concerns (in community stakeholders) and economic performance with a positive slope at lower levels of community stakeholder concerns but negative at higher levels (Bowman and Haire, 1975).

The reason why only community related stakeholder concerns show this type of effect on economic performance is that these stakeholders may be those that managers are primarily concerned about. Chapter Three analysed the issue of identifying stakeholders in firms that count. In reference to those stakeholders that do a descriptive theory of stakeholder salience was suggested (Mitchell et al. 1997). The importance of the issue of stakeholder salience was recently provided by Mitchell et al. (1997: 853), "And to whom (or what) do managers pay attention?" From the results in the current research community stakeholder groups have a positive and stronger effect on economic performance than the other stakeholders. Consideration was given to which stakeholders concerns do count by observing which stakeholder groups show the highest statistical significance. On closer examination of the results from Table 7.8 in model 1 more emphasis was placed on community stakeholder. However in Model 2, environmental stakeholder concerns were preferred relative to the other stakeholders.

A further consideration of the relationship between stakeholder concerns and economic performance tested the possible disparate effects of primary and secondary stakeholders. The next section tested whether this categorisation of shareholders, into primary and secondary, helped to provide any further explanation of the relationship between stakeholder concerns and economic performance.

7.3.8 Testing the Effects of Primary versus Secondary Stakeholder Concerns on Economic Performance

A division was made between primary and secondary stakeholders to examine if there was any distinction between them regarding their effect on economic performance. Moreover whether firms did concern themselves with primary in preference to secondary stakeholders when concerned about economic performance. In testing the relationship between primary stakeholders and economic performance, consideration was only given to employee and product safety concerns variables as reflected in Table 7.9.

Table 7.9

Effect of Primary Stakeholder Management on ROA

Independent Variables	Model 1	Model 2
	Low/moderate	high level
Intercept	.033 (.138)	.103 ** (.040)
Employee	.023 # (.020) (1.221)	-.0002 (0.002) (1.168)
Product safety	.068 (.068) (1.201)	-.0012 (.006) (1.072)
Leverage	-.032 (.123) (1.049)	.002 (.005) (1.015)
Number of employees	-.000 (0.000) (1.011)	0.0000 (0.000) (1.111)
R ²	.116	.009
Adjusted R ²	.014	-.098
F	1.143	.085
D-W	2.079	1.807

Standard errors are shown in parentheses ; variance inflation factors are in the second parentheses.

For low/moderate n=40, for high level , n=42

DW: refers to the Durbin-Watson statistic

* p< .05

**p< .01

p <.10

The results from data in Table 7.9 provided no major statistical significant result regarding the relationship between primary stakeholder concerns and economic performance. There was a positive sign for the relationship between both primary

stakeholders and economic performance in model 1. A statistically significant relationship, at the $p < .10$ level existed between employee stakeholders and economic performance at the low to moderate level of stakeholder involvement.

This result implied that employee stakeholders influenced economic performance at the low to moderate level of stakeholder concern. For employee related stakeholder concerns at the high level of stakeholder involvement there was a negative but not a statistically significant result. One can infer from this that there is a very weak relationship between concerns for employee stakeholders and economic performance, which provides weak support for hypothesis H: 4.2 restated below:

H:4.2 The relationship between economic performance and primary stakeholders is non-linear, with a positive slope at low/moderate levels of stakeholder involvement but negative at the high levels of stakeholder involvement.

The weak support referred to the lack of statistical significance for the hypothesis regarding product safety (customer) stakeholder concerns.

When consideration was given to secondary stakeholder concerns (refer to Table 7.10) and their effects on economic performance, the two themes community service and environmental concerns were tested against performance. In testing for linearity or lack of it the sample was divided into low/moderate and high level of stakeholder concern using the critical cut-off point previously established.

From Table 7.10, results suggested that community stakeholder concerns influence economic performance at the low to moderate level and this was significant at the $p < .01$ level. As the level of stakeholder involvement of the firm increased beyond the critical cut-off point, so the relationship between community stakeholders and economic performance became negative and significant at the $p < .10$ level. This negative effect provided further evidence that “going beyond the point of doing what is required” may not necessarily be profitable (Bowman and Haire, 1975: 49). Moreover, this result may

also be explained in terms of “it pays to be good, but not too good” (Mintzberg, 1993: 7). The critical cut-off point provided the dividing line between doing what was required for stakeholders and going beyond the point of doing what was required.

Table 7.10
Effect of Secondary Stakeholder Management on ROA

Independent Variables	Model 1	Model 2
	Low/moderate	high level
Intercept	.146 (.122)	.098 ** (.036)
Community Service	.099 ** (.035)	-.0004 # (0.003)
Environment	-.015 (.023)	.002 # (.002)
Leverage	-.095 (.118)	-.0005 (.005)
Number of employees	-.000 (0.000)	0.0000 (0.000)
	(1.070)	(1.171)
	(1.026)	(1.014)
R ²	.195	.103
Adjusted R ²	.103	.006
F	2.116 *	1.063
D-W	2.274	1.872

Standard errors are shown in parentheses ; variance inflation factors are in the second parentheses.

For low/moderate n=40, for high level , n=42

DW: refers to the Durbin-Watson statistic

* p< .05

**p< .01

p <.10

There was evidence of a non-linear relationship between secondary (community related) stakeholders and economic performance as the level of stakeholder management increased beyond the low/moderate cut off point a negative and significant result was identified. This result provided support for hypothesis H_{4.3}:

H_{4.3} The relationship between economic performance and secondary stakeholders is non-linear, with a positive slope at low/moderate levels of stakeholder involvement but negative at the high levels of stakeholder involvement.

The results of data in Table 7.10 provided evidence of a statistically significant result at the $p < .01$ level between community related stakeholders and economic performance. Furthermore, the overall model 1 was significant reflected by the significant F value. This was then compared with primary stakeholders, in employee related stakeholders, from Table 7.9 and the statistical significance was higher in the case of secondary, in community related stakeholders, than for primary stakeholders. This result did not support hypothesis $H_{4.4}$ and evidence in the current study suggested that secondary stakeholders were those that really count as opposed to primary stakeholder for the years and sample in question.

H_{4.4} When considering the relationship between economic performance and stakeholder concerns firms are more concerned about primary stakeholders than secondary stakeholders.

The current research found that the community were the critical stakeholder concern of firms. When the division between primary and secondary stakeholders was considered, then the secondary stakeholders were the key ones, quite specifically community services. In providing no support for hypothesis $H_{4.4}$ suggested that there was a greater concern for secondary than there were for primary stakeholders.

The outcome of these results in both cases suggests a non-linear relationship exist for particular variables. The next step is to test the combined effect of business, international diversification with stakeholder concerns on economic performance. Consideration was also given to the non-linear relationships and the effect of these when combining business and society effect on economic performance from a socioeconomic theoretical framework developed in Chapter Five.

7.3.9 Testing the Effects of Combined International, Business-Level Diversification and Stakeholder Concerns on Economic Performance

When testing the effects of a combined international and business level diversification with stakeholder concerns on economic performance, the non-linear nature or results of

the individual relationships, previously identified in Table 7.3 (for international diversification) and Table 7.8 (for stakeholder concerns), needed to be addressed. The current study first selected firms, which had both low to moderate levels of international diversification and stakeholder concern, and tested the relationship between these firms combined effect on economic performance. The sample size then reduced from 88 as a result of the previous averaging to 29 firms which displayed both low to moderate levels of international diversification and stakeholder concerns. This 29 firm sample was used to test hypothesis H_{5.1}:

H_{5.1} When stakeholder involvement and international diversification are both at the low to moderate level then the combined relationship of stakeholder concerns with international and business-level diversification on economic performance will be positive.

Following this hypothesis the current study then selected firms, which had both high levels of international diversification and stakeholder concern, and tested the relationship between these firms combined effect on economic performance. The sample size then reduced from 88 to 13 firms, when selecting firms, which displayed both high levels of international diversification and stakeholder concerns. This 13 firm sample was used to test hypothesis H_{5.2}:

H_{5.2} When stakeholder involvement and international diversification are both at the high level then the combined relationship between stakeholder concerns with international and business-level diversification on economic performance will be negative.

In considering the importance of the combined effects of international and business level diversification with stakeholder concerns on economic performance, consideration was given to five different variations which include: unrelated diversification x multinationality, related diversification x multinationality, country scope, multinationality, and country scope x multinationality. The first two of these variations related to the integration of business level and international diversification, with

suggestions that business level strategy enhanced the relationship between international diversification and economic performance. In these two relationships business level diversification was divided into related versus unrelated diversification (Hitt et al. 1997; Kim et al. 1989; Lubatkin, 1987; Michel and Shaked, 1984; Montgomery, 1982; Rumelt, 1974; Simmonds, 1990). The remaining three variations recognised the independent variables multinationality, country scope and the interaction of multinationality and country scope (Tallman and Li, 1996).

The combined effect on economic performance can be summarised as five relationships that were subsequently tested:

Test the effect of a combined business-level and international diversification with stakeholder concerns on economic performance.

1. related diversification x multinationality + stakeholder management on economic performance.
2. unrelated diversification x multinationality + stakeholder management on economic performance.

Test the effect of combined international diversification with stakeholder concerns on economic performance.

3. multinationality + stakeholder management on economic performance.
4. country scope + stakeholder management on economic performance.
5. multinationality x country scope + stakeholder management on economic performance.

In testing these relationships consideration was given to the importance of low to moderate and high levels of involvement to identify the effect of a critical cut-off point on the combined relationship. Since evidence from the previous results above provided a clear indication of non-linear relationships summarised below;

-multinationality and economic performance (Table 7.3)

-community related stakeholders and economic performance (Table 7.8)

-employee related stakeholders and economic performance (Table 7.8)

Also evidenced from previous tests in the current study indicated that the following relationships were more significant at the low to moderate levels of involvement;

-country scope and economic performance (Table 7.3)

-country scope and multinationality and economic performance (Table 7.7)

These five tests were then considered within the critical cut-off point established for both international diversification and stakeholder concerns. The cell typology developed in Chapter Six, identified two relevant cells for testing namely cells 1 and 3.

Cell 1-Low/moderate levels of international diversification and stakeholder concerns

Cell 3-High levels of international diversification and stakeholder concerns

Figure 7.3 Cell Typology Combining Strategic and Stakeholder Management Effects on Economic Performance.

High Level International Diversification	S T R A T E G I C	CELL 2	CELL 3 N=13
		CELL 1 N = 29	CELL 4
Low/Moderate International Diversification	M G T	STAKEHOLDER <i>Low/Moderate</i> Stakeholder Involvement	MANAGEMENT <i>High</i> Stakeholder Involvement

Testing Whether the Interaction of Business-level with International Diversification Combined with Stakeholder Concerns effects Economic Performance

In testing the combined effect of international diversification and business level diversification with stakeholder concerns consideration was given to the distinction between related and unrelated diversification. Results from testing these relationships are provided in Table 7.11. For both related diversification x multinationality + stakeholder management on economic performance column A and unrelated diversification x multinationality + stakeholder management on economic performance column B there was weak support for hypothesis H_{5.1}. Furthermore, the R² was high for both interactive models and the F statistic was significant at the p < .01. There was no severe problem with multicollinearity as all variance inflation factors are less than 5. But there was no statistically significant relationship between economic performance and unrelated diversification x multinationality which provided only weak support for hypothesis H_{5.1}. There was further weak support for H_{5.1} when combining unrelated diversification x multinationality with community service on economic performance although the result was not statistically significant.

This result was not reflective of findings from prior research which claim that firms with business-level diversification which also diversify internationally should experience high levels of economic performance, as they are able to capture potential synergies between various business levels (Geringer et al. 1989; Hitt et al. 1997). This disparity may reflect the fact that prior research has been based on American data, while this study deals with (large) Australian firms.

Table 7.11

Effects of Combined International, Business-Level Diversification and Stakeholder Management on ROA

When stakeholder management and international diversification level is low to moderate

Consideration is given to unrelated diversification x multinationality(A) and related diversification x multinationality (B).

Independent Variables	A	B
Intercept	.128 (0.133)	.123 (0.131)
Number of employees	-0.000 * (0.000) (1.251)	-0.000 * (0.000) (1.203)
Debt/Assets	-0.208 * (0.100) (1.223)	-0.205 * (0.098) (1.203)
Mergers and Acquisitions	-0.298 * (0.155) (1.5841)	-0.295 * (0.162) (1.564)
Country Scope	0.04 ** (0.011) (2.298)	0.039 ** (0.011) (2.298)
Environmental related	-.086 ** (.025) (1.422)	-.086 ** (.024) (1.422)
Employee related	.015 (.022) (1.499)	.0128 (.021) (1.457)
Community Service	.182 ** (.046) (1.727)	.18 ** (.045) (1.680)
Product related	.003 (.065) (1.353)	.003 (.064) (1.329)
Unrelated Diversification x multinationality	1.682 (.008) (1.677)	
Related Diversification x multinationality		.024 (.030) (1.543)
R ²	.731	.737
Adjusted R ²	.603	.613
F	5.731 **	5.919 **
D-W	1.931	1.864

Standard errors are shown in parentheses ; variance inflation factors are in the second parentheses.

For n=29

DW: refers to the Durbin-Watson statistic

* p < .05

** p < .01

p < .10

From the current study of Australian firms, any benefits of business-level diversification did not significantly enhance the relationship between international diversification and economic performance. These two interactive effects, depicted in Table 7.11, show no statistical significant results when combined with stakeholder concerns. This however, was not the case when consideration was given to three different international diversification variables in multinationality, country scope and the interaction of multinationality and country scope, which will be tested in the following section.

Testing Whether the Combined effect of International Diversification with Stakeholder Concerns effects Economic Performance

In testing the combined effects of international diversification with stakeholder concerns on performance, use was made of the three measures of international diversification; multinationality, country scope and the interaction of country scope and multinationality. Table 7.12 provides results from testing these three variables of international diversification together with stakeholder management on economic performance.

In the first instance when testing the relationship between country scope together with stakeholder concerns consideration was given to the conditions set for Cell 1, where international diversification and stakeholder management levels were low to moderate. The results of this test was that a combined country scope with stakeholder management on economic performance was positive and statistically significant at the $p < .01$ level (refer column C, Table 7.12). In particular, community service stakeholders was also positive and statistically significant at the $p < .01$ level. Furthermore the R^2 was very high at .730 and the F statistic was significant at the $p < .01$. There was no severe problem with multicollinearity as all variance inflation factors were less than 5. This result supported hypothesis H_{5.1} in that when combining international diversification using country scope with stakeholder concerns, specifically community related stakeholders economic performance was positively related and statistically significant.

Column D in Table 7.12, which tested the combined relationship of multinationality together with stakeholder management. At this low to moderate level of international diversification and stakeholder management level the relationship, reflected by Cell 1, the combined effect of the relationship between multinationality with stakeholder management on economic performance were positive and statistically significant at the $p < .01$ level. Furthermore the R^2 was high at .668 and the F statistic was significant at the $p < .01$. There was no severe problem with multicollinearity as all variance inflation factors were less than 5. This result supported hypothesis H:5.1 when combining multinationality together with community related stakeholders on economic performance.

A test of the combined interaction of country scope x multinationality together with stakeholder management saw the best result for a combined effect, reflected in column E of Table 7.12. At this low to moderate level of international diversification and stakeholder concerns the relationship of combined country scope x multinationality with stakeholder management on economic performance was found to be positive and statistically significant at the $p < .01$ level. Furthermore the R^2 was the highest at .867 relative to those values in columns C and D and the F statistic was significant at the $p < .01$. There was no severe problem with multicollinearity as all variance inflation factors were less than 5. This result also supported hypothesis H:5.1 when combining country scope x multinationality together with community related stakeholders on economic performance.

The interaction of country scope and multinationality with stakeholder concerns did improve economic performance, but only up to a particular point referred to previously as the 'critical cut-off point'. Beyond that cut-off point, for regressions run for analysing data in Cell 3, there was predominantly negative outcomes and no statistical significant

results in any of these five relationship mentioned above as illustrated in Tables 7.13 and 7.14. The results for data in Cell 3 could be an artefact of small sample size.

Table 7.12

Effects of Combined International Diversification and Stakeholder Management on ROA:

When stakeholder management and international diversification level is low to moderate

Consideration is given to Country scope (C), Multinationality (D) and the Interaction of Country scope and Multinationality(E)

Independent Variables	C	D	E
Intercept	.131 (0.092)	.064 (0.41)	.196 * (0.092)
Number of employees	-0.000 * (0.000)	-.000 # (000)	-0.000 * (0.000)
Debt/Assets	-0.211 * (0.068)	-.198 * (0.107)	-0.173 * (0.068)
Mergers and Acquisitions	-0.293 * (0.096)	-0.214 (0.162)	-0.249 ** (0.162)
Environmental related	-.086 ** (.025)	-.05 * (.024)	-.083 ** (.025)
Employee related	.017 (.02)	.011 (.022)	.014 (.024)
Community Service	.183 ** (.044)	.198 ** (.049)	.148 ** (.032)
Product related	-.006 (.063)	.019 (.070)	-.036 (.045)
Country scope	.041 ** (.01)		
Multinationality		1.996 ** (.661)	
Country scope x multinationality			.126 ** (.031)
R ²	.730	.668	.867
Adjusted R ²	.622	.536	.814
F	6.762 **	5.041 **	16.303 **
D-W	1.964	2.494	2.208

Standard errors are shown in parentheses ; variance inflation factors are in the second parentheses. For n=29

DW: refers to the Durbin-Watson statistic

* p < .05

** p < .01

p < .10

Table 7.13
Effects of Combined International, Business-Level Diversification and Stakeholder Management on ROA
When stakeholder management and international diversification level is high
Consideration is given to unrelated diversification x multinationality(A) and related diversification x multinationality (B).

Independent Variables	A	B
Intercept	.112 (.062)	.125 (0.063)
Number of employees	.000 (.000)	0.000 (0.000)
Debt/Assets	-.0006 (.0005)	0.002 (0.005)
Mergers and Acquisitions	.041 (.067)	-0.019 (0.057)
Country Scope	-.003 (.005)	0.0005 (0.005)
Environmental related	.003 (.003)	.0022 (.002)
Employee related	.001 (.003)	-.0016 (.003)
Community Service	-.004 (.004)	-.0036 (.004)
Product related	-.011 (.013)	.0007 (.012)
Unrelated Diversification x multinationality	-.001 (.001)	
Related Diversification x multinationality		-.0009 (.001)
R ²	.790	.801
Adjusted R ²	.159	.203
F	1.252	1.339
D-W	2.006	1.778

Standard errors are shown in parentheses For n=13,

DW: refers to the Durbin-Watson statistic

* p< .05

**p< .01

p <.10

The cut-off point has provided further support for issues such as the negative effects of transactions costs for firms over involved in international diversification and ‘going beyond the point of what is required’ for stakeholder concerns.

Table 7.14

**Effects of International Diversification and Stakeholder Management on ROA:
When stakeholder management and international diversification level is high**

Consideration is given to Country scope (C), Multinationality (D) and the Interaction of Country scope and Multinationality(E)

Independent Variables	C	D	E
Intercept	.093 (0.067)	.122 (0.052)	.119 (0.057)
Number of employees	0.000 (0.000)	.000 (000)	0.000 (0.000)
Debt/Assets	0.001 (0.006)	.002 (0.003)	-0.000 (0.004)
Mergers and Acquisitions	-0.004 (0.064)	-0.01 (0.030)	0.004 (0.035)
Environmental related	.001 (.003)	.001 (.002)	.002 (.002)
Employee related	-.000 (.003)	-.002 (.022)	-.001 (.002)
Community Service	-.003 (.004)	-.002 (.003)	-.004 (.003)
Product related	-.002 (.013)	.001 (.005)	-.006 (.008)
Country scope	-.0009 (.005)		
Multinationality		-.081 (.052)	
Country scope x multinationality			-.006 (.005)
R ²	.654	.785	.750
Adjusted R ²	-.037	.355	.251
F	.947	1.825	1.502
D-W	2.156	2.262	2.504

Standard errors are shown in parentheses For n=13

DW: refers to the Durbin-Watson statistic

* p< .05

**p< .01

p <.10

The results in tables 7.13 and 7.14 provide support for hypothesis H:5.2:

H:5.2 When stakeholder management and international diversification is at the high level then the combined relationship between stakeholder management with international diversification on economic performance will be negative.

A closer examination of Tables 7.13 and 7.14 show no significance either for the overall models 1 or 2 as the F statistics was not significant. Furthermore, for the key variables in, unrelated diversification x multinationality, related diversification x multinationality, community stakeholder concerns, multinationality, country scope and multinationality x country scope, and their relationship with economic performance, no significance was identified when analysing the result from Tables 7.13 and 7.14.

In sum, the results provide support for H_{5.1}, that firms, which are low/moderately diversified at both an international and stakeholder level (Cell 1), perform better than those firms which aspire to high levels of international diversification and a high degree of concern for stakeholders (Cell 3). This situation supports H_{5.2}, that if firms go beyond a critical cut-off point for both stakeholder involvement and international diversification that they do this at the detriment of economic performance.

7.4 Summary of Findings

This chapter presented the statistical findings from an analysis of the data. Evidence supported the case for using ROA as the most appropriate dependent variable, in an Australian context. Hypotheses were tested using an averaging technique and also year by year analysis. The effect of the combining international and business level diversification with stakeholder concern on economic performance, which included incorporation of interactive effects of particular independent variables was also tested. Consideration was also given to the non-linear characteristics of international diversification on economic performance together with the non-linear relationship between stakeholder concerns on economic performance, when testing for the combined effect on economic performance. The final section tested (1) whether the interaction of business-level with international diversification combined with stakeholder concerns effects economic performance and (2) whether the combined effect of international diversification with stakeholder concerns effects economic performance.

The findings of the statistical analysis of the data on stakeholder management and international diversification on economic performance may be summarised as follows:

1. Firms with interaction of unrelated diversification x multinationality do significantly enhance economic performance
2. Firms with the interaction of country scope x multinationality do significantly enhance economic performance
3. There was a non-linear inverted relationship between multinationality and economic performance
4. There was a non linear relationship between unrelated diversification x multinationality and economic performance, however this was not statistically significant and there were high multicollinearity problems with VIF > 5.
5. There was a positive and significant relationship between economic performance and country scope only at the low/moderate level of international diversification.
6. There was a positive and significant relationship between economic performance and the interaction of multinationality with country scope at the low to moderate level of international diversification.
7. There was a non linear relationship between economic performance and community related stakeholders
8. There was a non-linear relationship between economic performance and employee related stakeholders but not statistically significant.
9. The secondary stakeholders had a greater statistical significance when related to economic performance than when primary stakeholders involvement is considered.
10. The relationship between the combined country scope with community related stakeholder management on economic performance was positive and statistically significant at the low to moderate levels of both stakeholder management and international diversification.

11. The relationship between the combined multinationality with community related stakeholder management on economic performance was positive and statistically significant at the low to moderate levels of both stakeholder management and international diversification.
12. The relationship between the combined country scope x multinationality with community related stakeholder management on economic performance was positive and statistically significant at the low to moderate levels of both stakeholder management and international diversification.
13. In the relationship between combined international diversification measures, with stakeholder concerns the key variables in; unrelated diversification x multinationality, related diversification x multinationality, community stakeholder concerns, multinationality, country scope and multinationality x country scope were found to be negative with no statistical significance, at the high levels of both stakeholder involvement and international diversification.

Chapter Eight discusses the findings of Chapter Seven within the context of the research literature, presents the conclusions and makes recommendations for further study.

CHAPTER EIGHT

CONCLUSIONS AND IMPLICATIONS

8.1 Introduction

Chapter One explained the purpose of the study, which was to investigate the importance of combining international and business diversification strategy with stakeholder management when investigating economic performance. It provided the background to the research study by examining the interaction of international business with strategic management in explaining effects on economic performance. The chapter went on further to argue that the idea of considering the concerns of international business and strategic management at the expense of stakeholders has been criticised. The chapter discussed a movement towards further concern for a broader set of stakeholders other than stockholders, which includes the interests of customers, community, employees and environment. When considering economic performance the chapter provides a number of views, which support the inclusion of stakeholders as well as stockholder interests. The chapter also identifies little, if any, research which combined international business, strategic management together with stakeholder management when investigating economic performance.

The chapter then considered the problem of assuming linearity which was evident in prior literature which has tested relationships in the areas of international business, strategic management and stakeholder management. A few recent studies were identified which accounted for the non-linear relationship between international business diversification and economic performance but little evidence was found on the non-linear relationship between stakeholder management and economic performance. The chapter then identified the research problem and the major research questions posed for this study. It also identified assumptions, limitations,

definitions, scope that applied in the current study. An introduction to the research method used in the current study was also presented

Chapter Two described an initial integrative *socioeconomic* model, which improves our understanding of the effect of both strategic management with international business and stakeholder management on economic performance. The emphasis in this chapter was the cumulation of the dimensions of, international business and strategic management utilising a resource-based perspective, with a stakeholder dimension utilising stakeholder thinking, when considering economic performance. The chapter provided an overview of studies that have considered these dimensions individually but not combined as this is a new relationship, which has not been tested. From an analysis of past studies the development of a socioeconomic model was given support. Examples of combining economic perspectives with other theories were examined and this dual perspective provided support for the argument in favour of going beyond the economic perspective to a broader more inclusive perspective which does not ignore the additional complexities of an organisation. The chapter provided support for an extension beyond the economic perspective extending to add other complementary perspectives such as hegemony, institutional factors and stakeholders

A closer examination was given to the three dimensions of strategic business diversification, international business diversification and stakeholder dimension on economic performance. These three dimensions were considered separately as they have been study, in the main, as three separate relationships. A socioeconomic model of economic performance combined these three dimensions to assist in the development of a combined framework for empirical analysis. This set the scene for the initial consideration of a perspective, or early model, which considered a firm which jointly serves these three dimensions and moves away from a fragmented or separate approach. The idea of a separate approach to analysing

effects of these dimensions on economic performance was critically analysed. Use was made of a critical appraisal of "The Separation Thesis" (Wicks, 1996). The Separation Thesis essentially advocated for a distinction between ethics and economics into separate components (Freeman, 1994). Consequently the Separation Thesis did not permit for the cumulation of these components in any inclusive and broader sense as the assumption is that business is really on about profit maximisation. This chapter, utilises Wicks (1996) criticism of the Separation Thesis, developed a model which considered stakeholder, international business and strategic management as all starting points in investigating economic performance. Furthermore, this chapter also analysed the importance of determining which stakeholder interests do matter to an organisation and that this issue provided a further refinement in the analysis of stakeholder management on economic performance. In sum, the chapter provided initial groundwork for an integrated approach to studying economic performance, which included a broader set of stakeholders beyond the strategic management and international business dimensions.

Chapter Three provided further detail of the two economic dimensions of strategic management and international business diversification when investigating economic performance. In the first instance, past studies which have tested the relationship between economic performance and business level diversification, results have been mixed. These mixed results have found positive, some negative and some no-effect. The breadth of diversification is further considered with emphasis placed on related and unrelated business-level diversification. From an analysis of prior studies, there was more evidence of a positive relationship but this was dependent on what type of diversification variable was used. From a resource based approach to this relationship when a firm diversifies into related businesses they were able to share resources and services amongst businesses which has the advantages of spreading costs so in this way enhances the efficient use of resources. The higher the level of

diversification the greater the resource efficiency which results in higher economic performance.

Chapter Three also considered the relationship between economic performance and international diversification strategy. International diversification referred to the degree of expansion across borders of global regions as multinationality and countries and also to the number of different international markets referred to as country scope (or geographic scope). The relationship between economic performance and international diversification have been mixed with some negative, no-effects and a majority positive. The chapter identified that prior research which considered a non-linear or sometimes an inverted U-shaped result were sparse. Resource based approaches together with transactions cost effects on this relationship have provided some explanation of the inverted U-shaped relationship between economic performance and international diversification. The idea of dividing international diversification into low to moderate and high was considered and the merits of this subdivision. Furthermore, the chapter considered the importance of the interaction of business-level on international diversification and how this interaction enhances economic performance.

Chapter Four analysed the relationship between economic performance and stakeholder concerns and also identifies social disclosures in corporate annual reports as a medium for stakeholder management. The issue of a concern for the interests of stakeholders by organisations and the effect of this concern on economic performance was analysed in this chapter. Mixed result of this relationship were identified from an analysis of prior studies with some negative, no-effects and a majority positive. The chapter highlighted the sparsity of test which have found a non-linear or sometimes an inverted U-shaped result in the relationship between economic performance and stakeholder management. The idea of dividing

stakeholder involvement (using social disclosure) into low to moderate and high was considered and the merits of this subdivision.

Chapter Five developed and described a *socioeconomic* theoretical framework drawn on in this study. In order to build this framework extant theories from several disciplines were utilised which include resource-based theories of strategic and international business management with transaction cost theory of the firm. For the *socio* perspective instrumental stakeholder theory of the firm was utilised together with named theories; slack management and good management theories (Donaldson and Preston, 1995; Jones, 1995; Waddock and Graves, 1997). For the *economic* perspective of the *socioeconomic* framework, resource-based theory and transaction cost theory were used. A proposed integrated socioeconomic framework in analysing economic performance was developed. The chapter described the importance of a combination of theories which helped provide a more inclusive explanation of effects on economic performance which include a strategic management, international business diversification and stakeholder dimension. This then went beyond the purely economic framework which considered stockholders and management incentives to create a competitive advantage and earn above normal profits, to a more inclusive socioeconomic framework which included other stakeholder interests in customers, environment, community and employee stakeholders. Research questions and hypotheses for the study were developed in this chapter.

Chapter Six described the research design used in this study. It explained the way in which the population was identified, justified the sample and sampling procedure used in the study and described the research instrument. The chapter justified using percentage of foreign sales to total sales as the measure of multinationality in international diversification. It also provided justification for using social responsibility disclosures in corporate annual reports as a medium for stakeholder

management. Use was made of the Chow test to determine the cut of point between low/moderate to high levels of activity for both international diversification and stakeholder involvement. Multicollinearity was primarily tested using variance inflation factor analysis for each explanatory variable in each relationship. The chapter also explained what statistical procedures were used to analyse the data.

Chapter Seven reported correlation coefficients and regression analysis for each relationship developed for testing. It then presented the patterns of results evolving from each dimension then the final five relationships considered the combined effect of socioeconomic perspectives on economic performance and analysed these in relation to the research questions and hypotheses identified for investigation in this study.

This chapter discussed the study's contribution and presents suggestions for further research. The structure of the chapter conforms to the model advocated by Perry (1994) for the concluding chapter of Australian doctoral theses.

8.2 Conclusions About the Hypotheses and Research Questions

This section summarised the findings presented in Chapter Seven for each of the research questions and hypotheses developed and investigated in Chapter Five. It discussed the findings in relation to the theoretical framework developed in Chapter Five and the review of empirical research literature on international and business level diversification in Chapter Three and stakeholder/social responsibility literature in Chapter Four.

The following hypotheses were *not supported*, on the basis of the results of statistical tests performed on the data accessed from corporate annual reports.

- H: 1 Firms pursuing related diversification will perform better than those firms pursuing unrelated diversification.*
- H:3.2 There is a positive relationship between economic performance and the interaction of multinationality with related business diversification.*
- H:3.4 The relationship between economic performance and the interaction of multinationality with related business diversification is non-linear, with a positive slope at low/moderate levels of international diversification but negative at the high levels of international diversification*
- H:4.4 When considering the relationship between economic performance and stakeholder concerns firms are more concerned about primary stakeholders than secondary stakeholders.*

The following hypotheses were supported, on the basis of the results of statistical tests performed on the data accessed from corporate annual reports. Hypotheses *H:2.2* and *H:3.6* were only supported at the low to moderate levels of international diversification. Furthermore, statistically significant support for *H:5.1* was provided by three out of five combined relationships namely: multinationality and stakeholder management; country scope and stakeholder management; interaction of country scope with multinationality and stakeholder management.

- H: 2.2 The relationship between economic performance and country scope is non-linear, with a positive slope at low/moderate levels of international diversification but negative at the high levels of international diversification.*
- H:3.1 There is a positive relationship between economic performance and the interaction of multinationality with unrelated business diversification.*
- H:3.3 The relationship between economic performance and the interaction of multinationality with unrelated business diversification is non-linear, with a positive slope at low/moderate levels of international diversification but negative at the high levels of international diversification*
- H:3.5 There is a positive relationship between economic performance and the interaction of multinationality with country scope*
- H:3.6 The relationship between economic performance and the interaction of multinationality with country scope is non-linear, with a positive slope at low/moderate levels of stakeholder involvement but negative at the high levels of stakeholder involvement.*

- H:4.1 The relationship between economic performance and stakeholder concerns is non-linear, with a positive slope at low/moderate levels of stakeholder involvement but negative at the high levels of stakeholder involvement*
- H:4.2 The relationship between economic performance and primary stakeholders is non-linear, with a positive slope at low/moderate levels of stakeholder involvement but negative at the high levels of stakeholder involvement.*
- H:4.3 The relationship between economic performance and secondary stakeholders is non-linear, with a positive slope at low/moderate levels of stakeholder involvement but negative at the high levels of stakeholder involvement.*
- H:5.1 When stakeholder management and international diversification are both at the low to moderate level then the combined relationship of stakeholder management with international diversification on economic performance will be positive.*
- H:5.2 When stakeholder involvement and international diversification are both at the high level then the combined relationship between stakeholder concerns with international and business-level diversification on economic performance will be negative.*

The following specific answers may be given for the research questions posed in this study.

RQ 1: Do firms pursuing related diversification perform better than those firms pursuing unrelated diversification?

There was a negative relation between unrelated diversification and economic performance with no level of significance whilst there is a positive but no level of significance between related diversification and economic performance. There was no strong goodness of fit as R^2 was low. Even though no high level of significance existed there appeared to be a better result for firms that have business level diversification of the related nature rather than unrelated.

RQ 2.1: Is the nature and form of the relationship between economic performance and multinationality non-linear?

There was a strong result regarding the strength of the non-linear nature of the relationship between economic performance and multinationality. Multinationality

was significant and positive at the low/moderate level but then becomes negative and significant at the high levels of international diversification. This result supported Hitt's et al. (1997) claim that there is non-linear relationship between economic performance and international diversification.

RQ 2.2 Is the nature and form of the relationship between economic performance and country scope non-linear?

This question was partially supported in that significant results were identified at the low to moderate levels of international diversification rather than at the high levels of international diversification. At the low to moderate level of international diversification, country scope was significant at the $p < .01$ level. However there was strong evidence of the loss of significance as firms further diversify. This result supported the hypothesis that there was a significant and positive relationship at the low to moderate of international diversification rather than at the higher levels. This result reflected the greater levels of transactions costs a firm can experience as it seeks to achieve higher levels of international diversification. These costs outweigh the benefits, which result in a lower level of significance on economic performance.

RQ 3.1: Is there a positive relationship between economic performance and the interaction of multinationality with unrelated business diversification?

Statistically significant results were found for the relationship between economic performance and unrelated diversification with multinationality. The addition of this variable added much to the R^2 but there were high levels of multicollinearity. Nevertheless there was a level of significance with economic performance.

RQ 3.2: Is there a positive relationship between economic performance and the interaction of multinationality with related business diversification?

There was no significant relationship between economic performance and the interaction of related diversification with multinationality. Moreover the relationship was a negative one.

RQ 4.1: Is the nature and form of the relationship between economic performance and the interaction of multinationality with unrelated business diversification non-linear?

Although there was no statistical significance identified between the variables there was evidence of a positive relationship at the low/moderate levels of international diversification whilst there was a negative result at the high levels of international diversification. This provided some support for a non-linear relationship, although lacking in statistical significance.

RQ 4.2: Is the nature and form of the relationship between economic performance and the interaction of multinationality with related business diversification non-linear?

There was no evidence of a non-linear relationship between economic performance and the interaction of multinationality with related business diversification.

RQ 5.1: Is there a positive relationship between economic performance and the interaction of multinationality and country scope?

Statistically significant and positive results were identified for the relationship between economic performance and the interaction of multinationality and country scope. This result confirmed Tallman and Li's (1996) claim that multinationality and country scope are independent variables which interact to positively effect economic performance.

RQ 5.2: Is the nature and form of the relationship between economic performance and the interaction of multinationality with country scope non-linear?

At the low to moderate level of international diversification, the relationship between economic performance and country scope x multinationality was

significant at the $p < .01$ level. There was strong evidence of the loss of significance as firms further diversify. This result supported a significant and positive relationship but at the low to moderate of international diversification rather than at the higher levels. This result reflected the greater levels of transactions and managerial processing costs a firm can experience as it seeks to achieve higher levels of international diversification. These costs outweighed the benefits, which resulted in a negative effect on economic performance at the high levels of international diversification.

RQ 6: Is the nature and form of the relationship between economic performance and stakeholder concerns non-linear?

A positive and statistically significant result was found between economic performance and community stakeholder concerns at the low to moderate levels of stakeholder involvement. Furthermore, a negative and statistically significant result was found for this relationship at the high levels of stakeholder involvement. This result provided evidence of non-linear relationship between economic performance and stakeholder management, but only specifically for community service stakeholders.

RQ 7.1: Is there a relationship between economic performance and primary stakeholders and is the nature and form of this non-linear?

Of the two primary stakeholders considered, employee and product safety (customers), employee related stakeholders were found to be related to economic performance. The relationship between employee stakeholders and economic performance was positive and significant at the low to moderate level of stakeholder involvement whilst negative and not significant at the high stakeholder involvement. This result provided evidence of a non-linear relationship between primary stakeholders and economic performance, but only specifically for employee stakeholders.

RQ 7.2: Is there a relationship between economic performance and secondary stakeholders and is the nature and form of this non-linear?

Of the two secondary stakeholders considered, that of environmental and community service stakeholders, community related stakeholders were found to be related to economic performance. The relationship between community related stakeholders and economic performance was positive and significant at the low to moderate level of stakeholder involvement whilst negative and also significant at the high level of stakeholder involvement. This result provided strong evidence of a non-linear relationship between secondary stakeholders and economic performance, but only for community related stakeholders.

RQ 8: When considering the relationship between economic performance and stakeholder concerns, are firms more concerned about primary stakeholders than secondary stakeholders?

The level of statistical significance for secondary stakeholders was higher than for primary stakeholders when consideration is given to their relationship to economic performance. This finding suggested that there was more concern for secondary than primary stakeholders, which does not support the contention that primary are more important than secondary stakeholders.

RQ 9.1: Are the combined concerns for international and strategic business level diversification with stakeholder interests positively related to economic performance?

Out of the five relationships tested there were three relationships that proved positive and statistically significant, but only when both stakeholder involvement and international diversification were at the low to moderate levels. These three combined concerns included multinationality and stakeholder management, country scope and stakeholder management, and the interaction of country scope with multinationality and stakeholder management.

RQ 9.2: Are the combined concerns for international and strategic business level diversification with stakeholder interests negatively related to economic performance?

When stakeholder involvement and international diversification were both at the high level a negative and no significant result was found for the relationship between economic performance as the dependent variable and the following independent variables: unrelated diversification x multinationality; related x diversification; community stakeholder concerns; multinationality; country scope; multinationality x country scope.

8.3 Conclusions about the Research Problem

The research problem investigated in this study was:

Whether strategic and international business diversification with stakeholder concerns enhances economic performance?

From the results, firm's that did show concerns for stakeholders and which were also involved in international and business level diversification did enhance economic performance but only at the low to moderate stakeholder and international diversification activity rather than at the high level of activity. This business and society study was also concerned with the consequences of a non-linear combined investigation of strategic and international diversification with stakeholder concerns on economic performance. Non-linear relationships were identified in the combined relationships.

A typology was developed (Figure 7.3) which illustrated the four possible quadrants out of the 2x2 matrix, in response to identifying the non-linear nature of the relationships. Of the four quadrants Cell 1 and 2 were identified as the relevant cells for testing the combined business and society effects on economic performance. In particular, the investigation challenged the linearity of the relationships between (1) strategic diversification on economic performance, (2) international diversification on economic performance, (3) interaction between multinationality and country

scope on economic performance and (4) stakeholder management and on economic performance. The non-linear nature of these four relationships was taken into account when consideration was given to the combined effect of these on economic performance, making a fifth relationship. As all four relationship showed more significance at the low to moderate levels of either international diversification or stakeholder involvement the combined model was tested at the low to moderate level of activity for both international diversification and stakeholder management.

The findings of this study suggested that the issue of economic performance was perhaps more complex than can be wholly illuminated by studies which assume linearity in their empirical analysis. The effects of a resource-based and transaction costs effect on international diversification together with determining a cut-off point divided the sample into low to moderate versus high concern. Furthermore, a cut-off point was also identified for stakeholder concerns that divided the firms into low to moderate versus high stakeholder concerns. What this helped to explain was that only up to a particular cut-off point can a firm continually engage in international diversification after which, the costs of doing so far outweigh the benefits. Furthermore, there was a point of “doing good” which involved the firms concerns for the needs of stakeholders, where additional involvement beyond that point did not enhance economic performance.

Analysing economic performance in these three domains of strategic and international business diversification with stakeholder concerns required a further investigation of the various levels of activity. Firms with these various levels of activity, low to moderate versus high, were shown to have different effects on economic performance, which need further consideration, otherwise these effects are lost if linearity was assumed. High levels of stakeholder management and international diversification are not preferred as reflected by the very low number of firms in this quadrant (refer to Figure 7.3, page 223). Firms however, that preferred

the low to moderate levels of activity were by far the largest in number and had a positive and statistically significant relationship to economic performance than did firms with a high level of activity. This preference for low to moderate versus high substantiates the importance of challenging the linear assumption in testing combined relationships of this nature.

8.4 The Importance of testing for Non-linearity when Investigating Combined International and Business Diversification with Stakeholder effects on Economic Performance

In investigating each business and society perspective a non-linear relationship was identified, in particular between international diversification and economic performance and also for the relationship between stakeholder management and economic performance. Positive and statistically significant findings were located at the low to moderate levels of international diversification, as identified in Cell 1 Figure 7.3. Furthermore, it was found that there was also a non-linear relationship between stakeholder management and economic performance. The positive and statistically significant findings were located at the low to moderate levels of stakeholder involvement.

Evidence from these findings, suggested that when investigating the combined effects of strategic and international diversification with stakeholder management, consideration needed to be given to a cut of point which divides the sample into low to moderate and high levels of activity. For each case of stakeholder management and international diversification a cut off point was identified, and a non-linear relationship recognised. The results of each case together with the consequences of non-linearity on the combined effect will be discussed further in this section.

The Importance of Identifying a Non-linear relationship between Economic Performance and International Diversification

Resource-based and transactions cost theory of the firm provided an explanation and interpretation of the non-linear relationship between economic performance and international diversification. Conceptually a firm, which diversifies internationally, utilised internal resources and capabilities to take advantage of market imperfections, which exist globally. This form of diversification was reflective of resource-based view of the firm (Hitt et al. 1997). The consequences of greater levels of international diversification were higher transaction costs. Where transaction costs referred to coordination, distribution and management costs involved in servicing these different and numerous geographical regions across global boundaries (Hitt et al. 1997). As these transaction costs increased with the level of international diversification so the costs begin to outweigh the benefits of economic of scope, scale and learning. Diminishing returns gradually set in resulting in a non-linear relationship between economic performance and international diversification.

Statistically significant results provided evidence of a non-linear relationship between economic performance and multinationality. Specifically for those firms at the low to moderate levels of international diversification, benefits were gained in terms of economic performance. As firms increased their levels of international diversification activity beyond the cut-off point, negative but statistically significant results were obtained which inferred that transaction costs were outweighing the benefits from further international diversification. This negative result supported the contention that “escalating geographic dispersion can greatly enhance transaction costs....For example, geographic dispersion increases coordination, distribution and management costs” (Hitt et al. 1997: 772).

As transaction costs increase with the level of international dispersion the costs of diversification will eventually exceed the benefits gained. The level at which costs outweigh benefits, referred to as the cut-off point, was obtained statistically using a Chow test statistic. The Chow F test was used to determine the cut-off point which enabled a subdivision of the sample into low to moderate and high levels of international diversification. As a statistically significant structural difference was identified for international diversification, at the 35% level (ratio of foreign sales to total sales), a further analysis then proceeded using the two subgroups. The first subgroup comprised of firms with less than 35% (low/moderate) and the second subgroup comprised of firms with greater than or equal to 35% (high), to test for a non-linear relationship. This provided a statistical method to appropriately divide the sample into subgroups and also a useful way of testing for the presence of a non-linear relationship. There was evidence of two different regressions as a result of performing the Chow test which allows for a sub-grouping into low to moderate and high levels of international diversification activity (Gujarati, 1988).

The conclusion that can be drawn from this investigation, in the case for Australia, for the time frame in question and the sample of firms selected, was that the relationship between economic performance and international diversification was non-linear. The non-linear relationship was characterised by a positive slope at the low to moderate levels of international diversification and negative at the high levels of international diversification.

It was evident that at the low to moderate levels of international diversification the relationship with economic performance was positive. Up till the cut-off point, international diversification can provide the benefits of economies of scope, scale and experience (Gomes and Ramaswamy, 1999, Hitt et al. 1997 and Kogut, 1985). These benefits of internationalisation do not continue infinitum but there was a suggestion that they level off and then begin to diminish. The subgroup analysis

using the Chow tests suggested the relationship becomes negative beyond the cut off point at and beyond 35%. The findings in this study, of a non-linear relationship that begins positive and then turns negative, reconciled well with the resource-based view of the firm and transaction costs theory (Hitt et al. 1997; Kogut, 1985). The results of this relationship were also consistent with the study of Geringer et al. (1989). As the firms increased their level of international diversification they then become “highly complex and difficult to manage” (Hitt et al. 1997: 789). At the cut off point of 35% and beyond, the complexity far outweighs the positive benefits to be gained from international diversification and a negative relationship with economic performance resulted.

Transaction costs played an important role in helping to explain the non-linear nature of the relationship. As Porter (1990) suggested the degree of complexity of further international involvement comes primarily from additional coordination and distribution costs which fits well with transactions cost theory. Hitt et al. (1997) suggested that there are other costs which compound coordination and distribution costs which include; “trade barriers, logistical costs, cultural diversity and other country differences” (Hitt et al. 1997: 789).

The Importance of Identifying a Non-linear relationship between Economic Performance and Stakeholder Management

The importance of this non-linear relationship was not captured in any theoretical underpinning although stakeholder theory does help to explain the relationship between economic performance and stakeholder involvement. The only study, which provided some reasonable explanation for a non-linear relationship between economic performance and stakeholder management, was that of Bowman and Haire (1975). Further support for this explanation was provided by Mintzberg (1983), where he consider “The Case for Corporate Social Responsibility”. Bowman and Haire (1975) tested whether it “pays to be good” using company

performance and social disclosures in corporate annual reports to determine whether this is the case. In their analysis Bowman and Haire (1975) found that the relationship between company performance and social responsibility was characterised by an inverse U-shape. This inverse U-shape was explained in the phrase “it pays to be good but not too good” (Mintzberg, 1983: 7). Bowman and Haire (1975) suggested that the stock market was willing to merit socially responsible behaviour but only up to a certain point. Furthermore, Bowman and Haire (1975) contended that the mean is golden. This was one explanation for dividing the sample into subgroups and yet another was “Don’t stand out from the crowd, do no more than is expected” (Mintzberg, 1983: 7). Mintzberg (1983) also recognised a cut off situation similar to that of Bowman and Haire (1975).

The current study provided statistically significant results, in support of the existence of a non-linear relationship, between economic performance and stakeholder management. In particular, statistically significant results were obtained of a non-linear relationship between community stakeholders and economic performance. Furthermore, there was a non-linear relationship between employee stakeholders and economic performance but this was not as statistically significant as the relationship with community stakeholders.

In the current study, results showed that as firms increased their levels of stakeholder involvement a positive and statistically significant result was obtained, but beyond the cut-off point a negative but statistically significant result was obtained. This non-linear result can be interpreted as firms with social disclosure below the cut-off point being rewarded and beyond that cut-off point not rewarded (Bowman and Haire, 1975; Mintzberg, 1983). The cut-off point at which firms are not rewarded for being socially responsible was obtained statistically using a Chow test statistic. The Chow F test was used to determine the cut-off point which enabled a subdivision of the sample into low to moderate and high levels of international

diversification. As a statistically significant structural difference was identified for stakeholder involvement, at the 15 sentences of prose level, an analysis then proceeded using the two subgroups. Less than 15 sentences of prose represented low to moderate activity and greater than or equal to 15 sentences of prose represented high activity. The two subgroups were used to test for a non-linear relationship. This provided a statistical method for dividing the sample into subgroups and also a useful way of testing for a non-linear relationship. There was evidence of two different regression as a result of performing the Chow test which allows for a sub-grouping into low to moderate and high levels of stakeholder involvement (Gujarati, 1988).

The conclusion that can be drawn from this investigation, in the case for the sample of Australia firms selected and for the time frame in question, was that the relationship between economic performance and stakeholder management was non-linear. The non-linear relationship was characterised by a positive slope at the low to moderate levels and negative slope at the high levels of stakeholder management.

It was evident that, at the early stages of activity at the low to moderate levels of stakeholder management, the relationship between stakeholder concerns and economic performance were positive. At this early stage, it still paid firms to be socially responsible or in another sense concerned for stakeholder interests. The results of the subgroup analysis, using the Chow tests, suggested the relationship becomes negative beyond the cut off point at and beyond 15 sentences of social responsibility prose. The findings in this study, of a non-linear relationship that begins positive and then turns negative reconciles well with the suggestions of Bowman and Haire (1975) and the assessment of Mintzberg (1983). The view of Bowman and Haire (1975) infers that the stock market is not willing to reward socially responsible behaviour however in the current study the stock market effects were not considered. The results identify negative and statistically significant

relationship between economic performance and community service stakeholders. The possible explanations for this, is that the firm may be portraying itself as “too good” and going beyond the comfort zone of stakeholders (Mintzberg, 1983). A negative and significant result was obtained at this high level of stakeholder involvement providing evidence that at the high levels the firms seem not to perform as well than at the low to moderate levels.

When Investigating the Combined Effect of Strategic and International diversification with Stakeholder Management on Economic Performance a Non-linear relationship was identified.

In considering the combined effect of strategic and international diversification with stakeholder concerns on economic performance, a non-linear relationship was identified. It was found, after statistically identifying cut off points in the data sample for both international diversification and also for stakeholder involvement, that in the combined cases that further consideration was given to what level of activity, low to moderate or high, was appropriate. It was found that the low to moderate levels of activity were statistically significant and positive when combining strategic and international diversification with stakeholder management on economic performance. Evidence of structural differences in the combined case infers that a combined analysis, of the type done in this study, needed to cater for a sub-grouping of the sample for both international diversification and stakeholder involvement. In sub-grouping, the study established the need to cater for the various levels of international diversification activity and stakeholder involvement in order to examine the combined effects on economic performance.

Past studies have assumed linearity between international diversification and economic performance. In overcoming this sparsity of research the current study divided the sample of firms into low to moderate and high levels of activity. From this division the low to moderate levels of activity and involvement showed positive results whilst the high levels proved to be negative. Much of what really happened

in these combined relationships on economic performance would be lost if linearity were assumed.

The effects of resource-based view and transaction costs on international diversification were tested together with concerns for stakeholders and the results suggested that what was preferred by the majority of firms in the sample was the low to moderate than a high involvement (refer to Cell typology Figure 7.3, Cell1 and Cell3). This suggested that firms, which were low to moderate in their stakeholder involvement and international diversification, revealed a high level of economic performance relative to high involvement. Only up to a particular point does a firm actively engage in both international diversification and stakeholder involvement after which the costs of doing so far outweigh the benefits. Furthermore there was a point of “doing good” (considering the needs of stakeholders) where additional stakeholder involvement did not enhance economic performance. This suggested that when combining international and business diversification with stakeholder concerns that at the low to moderate levels of activity the benefits outweighed the costs of further international diversification and stakeholder involvement. Statistically significant results were found, predominantly at the low to moderate rather than at the high levels of involvement.

In sum, evidence of a non-linear relationship between, in the first instance economic performance and stakeholder involvement, and then for the relationship between economic performance and international diversification, indicates that the positive results are identified at the low to moderate levels of activity rather than the high levels. Evidence from the current study found in the combined relationship that low to moderate activity was positive and more statistically significant than high levels of activity which adds support for the importance of a non-linear relationship. The results suggest that a firm’s successful economic performance can be explained from a business and society perspective, with evidence from the current study

supporting better relationships with economic performance at the low to moderate rather than high levels of activity.

8.5 Implications For Theory

The present study developed a socioeconomic theoretical framework by utilising Hitt et al's. (1997) integration of a resource-based theory of the firm and transaction costs theory together with an instrumental stakeholder theory proposed by Jones (1995) and Donaldson and Preston (1995).

The theoretical base, for the present study, integrated a resource-based view of the firm, transaction costs and instrumental stakeholder theory. The findings of a non-linear relationship between economic performance and the interaction effects of country scope and multinationality have important theoretical implications. Each of country scope and multinationality were considered as independent variables for international diversification and were shown to interact and have a positive and significant relationship with economic performance, which also supported findings by Tallman and Li (1996). Additionally, the findings of non-linear relationship between economic performance and stakeholder management, although not based on any theoretical rationale, have theoretical implications for future consideration. These results infer the importance to firms in the sample of the current study in managing both international diversification and stakeholder concerns and that these concerns can be examined using a socioeconomic theoretical framework. The socioeconomic theoretical framework developed in the current study included effects of both international and strategic management theories, with stakeholder theory of the firm.

If an investigation of economic performance is narrowly focused on the economic issues, such as competitive advantage domestically and internationally to achieve above normal profits (strategic management view) then the social/stakeholder are

excluded. This exclusion provides a partial view of the firm and does not allow for the investigation of a broader set of variables which includes stakeholder concerns which also effect economic performance. In using these three theories in an integrated way the current study contributed by providing a new path for future researchers to use a broader set of theories and provided a wider view of the bigger picture. The idea of an integrated approach was not new, but the integration of these particular theories to develop a socioeconomic framework was new. Other scholars have considered combined perspectives, for instance Hitt et al. (1997) included organisational learning perspectives with resource-based view of the firm and transaction costs and the importance of such an integrated theoretical base:

The theoretical base integrating a resource-based view of the firm, transaction costs, and organizational learning perspectives and the results of this study point scholars towards a new theory of the multinational firm (Hitt et al. 1997: 793-794).

The idea of a theory of stakeholder salience was also useful in determining which particular stakeholders matter to firms, as the current study specifically considers four major stakeholders in employees, customers, environment and community (Mitchell et al. 1997). In applying stakeholder salience the relative importance of each stakeholder concern to economic performance, can be addressed.

The major implication of the socioeconomic theoretical framework developed in the current study was to provide a new framework for examining and explaining the combined effects on economic performance and in doing so utilise resource based theory, transaction cost theory with instrumental stakeholder theory. It broadened the analysis to include stakeholder theory but not as a mere add on, but on an equal footing with the other two theories therefore moving away from the shortcomings of the "Separation Thesis" (Wicks, 1996). There was a sense that stakeholders did matter and that it does pay for a corporation to be concerned with stakeholders, thus

the inclusion of stakeholders in an investigation of economic performance provides another equally important explanatory variable when investigating economic performance.

8.6 Implications For Practice

The current study used five economic performance measures based on both market-based and accounting-based measures. There are other measures for each of these categories which could be used and further studies could continue to use both categories. The current study found ROA to be the measure of economic performance that provided the best regression results when testing the relationship for Australian firms. ROA has also been recognised by other studies, previously mentioned, as the most appropriate measure of economic performance. The other measures considered were ROE and ROS as alternative accounting measures and EPS and DPS as market based measures.

In testing the relationship between stakeholder concerns and economic performance each variable was used as the independent variable to determine the direction of the relationship. The issue of direction has been one previously analysed in the literature (Preston and O'Bannon, 1997; Waddock and Graves, 1997). The result was that economic performance provided the best regression result as the independent variable rather than stakeholder concerns in the relationship between stakeholder management and economic performance. Similarly when testing the relationship between international diversification and economic performance the result was that economic performance provided the best regression result as the independent variable rather than international diversification.

For Australian firms in the sample and years in question stakeholders were not necessarily treated equally as preference was given to community related stakeholders relative to employee, environment and customer stakeholder groups.

The current research found that firms that treat or concern themselves with community stakeholders in a low to moderate level perform better than those that are concerned at a high level.

The current study in assessing the nature and form of relationships identified a non-linear relationship between stakeholder concerns and economic performance, when considering low to moderate levels of stakeholder management versus high levels of stakeholder management. Use of a Chow test to find a precise and statistically significant cut off point dividing data into low/moderate and high levels provided the mechanism to divide the sample into these levels. The importance of this division in testing for a non-linear relationship challenged the assumption of linearity between these variables.

The result, in the current study, of a non-linear relationship between economic performance and international diversification reconciled with past evidence of a non-linear relationship between these variables (Geringer et al. 1989; Gomes and Ramaswamy, 1999; Hitt et al. 1997). Use of a Chow test to find a precise and statistically significant cut off point dividing data into low/moderate and high levels provides further researchers with another statistical technique to assist in determining a critical cut-off point. The importance of this division was that it could provide researchers with another useful statistical tool to test for a non-linear relationship between independent and dependent variable(s).

Of importance to practice was the statistical significance of the effects of interactive variables on economic performance which included the following interactive variables on economic performance: country scope x international diversification strategy on economic performance; business-level x international diversification strategy on economic performance; stakeholder management x international diversification strategy on economic performance. A closer

investigation of the possible interactive effect of independent variables, rather than testing them in isolation, may reveal additional information.

The strength of the combined results was the interactive effect of country scope with multinationality and community service stakeholder management on economic performance. Similarly with country scope variable combined with community service stakeholder management and also multinationality and community stakeholder management. The results of the current study revealed that the management of both international diversification and the degree of stakeholder concern were important when investigating economic performance, as there was a positive and statistically significant relationship between these variables on economic performance.

A significant find was that all the international diversification variables with community stakeholder variable provided support for a positive and significant effect on economic performance at the *low to moderate* level of stakeholder involvement and international diversification (refer to Table 7.12). Where the low to moderate levels of stakeholder management were measured by identifying those firms which recorded less than 15 sentences of social responsibility prose and low to moderate international diversification was measured by identifying those firms whose international sales as a percentage of total sales was less than 35%. Both these low to moderate cut off points was determined statistically using a Chow test which utilises F distributions. Structural differences between low/moderate and high levels for both models was statistically supported suggesting the assumption of linearity may explain the mixed results from past literature for each separate area.

The subgrouping of data into low to moderate and high was useful in testing for the possibility of non-linear relationships. The implication for practice was that studies need to further consider the nature and form of relationships for testing rather than

assuming linearity, in particular when considering a combined investigation like the one developed in the current study.

8.7 Limitations

Chapter One described the limitations of the research that were a deliberate part of the research design. The following section considers four limitations that became apparent during the progress of the research.

The first limitation that became apparent during the study was the reduction in the sample from 150 to 88 firms. The data analysed needed to be averaged by adjusting for the same companies appearing in the three year period. For instance if BHP Ltd was present for the three years of the study an average was taken for those three years, on the other hand if say Boral Ltd covers 2 years then the average was taken for two years and so on. In this way firms appear only once and so you end up with 88 different firms. This averaging method then limited the study to testing 88 firms over the three year period covering 1993-1995 inclusive.

The second limitation regarding the dependant variable became apparent in the data analysis phase of the research, which to some extent was anticipated from the results of Hitt et al. (1997). As noted in Chapter One, the dependent variable economic performance could be measured and tested using either accounting based-measures or market-based measures. The accounting-based measures were Return on Assets (ROA), Return on Equity (ROE), Return on Sales (ROS), whilst the market-based measures were Earnings Per Share (EPS) and Dividends Per Shares (DPS). The current study was limited to ROA as it displayed the most appropriate characteristics for use as this dependent variable, in an Australian context, which was consistent with the most recent work of Hitt et al. (1997). The data analysis stage found that there was no statistical significant results from regression analysis

for any of the two market-based economic performance measures, in Earnings Per Share (EPS) and Dividends Per Share (DPS), so no further consideration was given to these measures. Following this outcome the three accounting based measures were then considered as possible indicators of economic performance namely; Return on Assets (ROA), Return on Equity (ROE) and Return on Sales (ROS). The result was to limit the measure of economic performance to ROA, as the significance of the relationships tested was the strongest. Limiting the measure of economic performance to ROA was also consistent with Hitt et al. (1997). Similar to the rationale of Hitt et al. (1997), where they did not adopt ROE, as it has been shown to be “more sensitive to capital structure differences” (Hitt et al. 1997: 778) the current study found no statistically significant relationship using this measure. Furthermore, in considering ROS as a measure of economic performance, on closer examination of international diversification as a pervading independent variables and the combined business level /international diversification variable they were all functions of total sales which meant that as a dependent variable ROS might “reflect mathematical artifacts as well as true relations” (Hitt et al. 1997: 778). The result was to limit the tests to ROA as the most appropriate measure of economic performance.

The third limitation arose from the inability to generate a meaningful test of the industry specific influences on the relationships tested. Consideration was given initially to industry specific factors but the resultant small sample size, from splitting the database into different industries, did not provide large enough sample to statistically make any meaningful dialogue of the regression analysis. This limited the current research to a cross sectional longitudinal study.

The fourth limitation on the study was the difficulty of considering a year by year comparative analysis. All issues/questions in the current research could not be

addressed as a result of a reduced sample size. This again limited the current research to an aggregate sample covering three consecutive years.

8.8 Implications For Further Research

Evidence from prior research has emphasised the importance of applying industry specific approaches as different industries face a different configuration of stakeholders (Griffith and Mahon, 1997). Future research of Australian firms could include industry classification, as in Australia internationalisation exists in three specific industry sectors in manufacturing, services and resources (Lewis and Minchev, 1998). In selecting particular industry categories care needs to be taken to include firms that are active in both international diversification and stakeholder concerns. The current study did initially consider industry sectors in the data collection and analysis stages but the sample size of each industry classification was not large enough to examine industry specific factors in any meaningful way. As the top 50 Australian listed public companies, for each year in the current study, which represent the largest firms for examination, are more likely to contain social responsibility disclosures together with an appropriate level of international diversification activity, a longer period of time may be a productive option. Moreover, what could be further considered is a larger sample but covering a longer time frame and dividing the sample into three industry sectors advanced by Lewis and Minchev (1998) that include manufacturing, services and resources.

The research used social responsibility reporting as disclosed in corporate annual reports to identify firms stakeholder concerns. Four themes were used to measure social responsibility reporting in the current study, but further studies could expand beyond these four and include energy, affirmative action programs and equal opportunity issues. This expansion could provide additional explanations when investigation the relationship between stakeholder concerns and economic

performance and hence enrich the results of an investigation of a combined business and society effect.

Researchers in Australia have no access to a ratings based social performance measure, nor a reputational index to measure stakeholder concerns, that have been used by researchers in other countries such as Britain and America. Furthermore, Australia as yet has no equivalent to the KLD (Kinder, Lydenberg, Domini & Co) social screen method of identifying stakeholder concerns. Given this lack of ratings and social screens data further studies that can identify an alternative measure of stakeholder concerns similar to that of a ratings based approach may better assess managers concern for stakeholders. This would overcome the need to rely on content analysis, requiring the measuring of sentences of prose as the unit of analysis, from social responsibility disclosures in corporate annual reports. Social responsibility disclosure whilst a tested and established method of measuring stakeholder concerns may not adequately account for the concerns of firms towards stakeholders. A more precise measure of firms concerns for stakeholder does not exist in Australia and would be a valuable contribution in further research studies of this nature.

In analysing international diversification the current study considered both multinationality and country scope. Further studies could also take into account the idiosyncratic nature of the foreign countries which firms export goods and services that would involve the type of culture and area. These additional issues would be used in further assessing the level and nature of international diversification and its relationship to economic performance.

Further business and society research that challenges the linear assumption of relationships may provide more revealing results. In the first instance testing for the non-linear relationship between economic performance with both business and

international level diversification and in the second instance economic performance with stakeholder management may provide useful results. Similarly future studies that are involved in a combined relationship of international and business diversification with stakeholder concerns on economic performance, should test for a non-linear relationship as further insight can be gained of enhanced effects on economic performance. In this way the nature of the relationships are further investigated without restricting the study to assumptions that may not be characteristic of the relationship under examination.

Structural differences if identified in future studies, using say the Chow F test, can then enable researchers to divide their sample into two subgroups low to moderate versus high. If subgroups are identified in similar future business and society studies, then researchers can divide their combined analysis into a cell typology like that developed in Chapter Five, Figure 5.4 and finer more rewarding results can be obtained. Further tests of this nature could also reinforce the effects of resource-based and transaction costs theory of the firm on the relationship between international diversification strategy and economic performance. Moreover, from an instrumental stakeholder view, consideration could also be given to the relationship between stakeholder concerns and economic performance and the nature and form of that relationship. Further researchers could investigate whether a theoretical explanation can be given for the non-linear relationship between stakeholder concerns and economic performance, evidenced in the current study, as no cogent theory exists to explain this outcome. This business and society study can help provide a foundation that further researchers can use to examine the combined impact of stakeholder concerns and international diversification strategy on economic performance, useful for empirical researchers, theorists and managers alike.

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APPENDIX I

LIST OF TOP 50 AUSTRALIAN PUBLICLY LISTED COMPANIES FOR EACH OF THE THREE YEARS OF THE STUDY 1993-1995.

Top 50 Companies for 1993

1. Broken Hill Proprietary Co. Ltd
2. Coles Myer Ltd
3. The Adelaide Steamship Company Ltd
4. David Jones Limited
5. The News Corporation Limited
6. Woolworths Limited
7. National Australia Bank Limited
8. Foster's Brewing Group Limited
9. Australian and New Zealand Banking Group Limited
10. Commonwealth Bank of Australia
11. Fletcher Challenge Limited
12. Westpac Banking Corporation
13. Pacific Dunlop Limited
14. BTR Nylex Limited
15. TNT Limited
16. Pioneer International Limited
17. Amcor Limited
18. Goodman Fielder Limited
19. CSR
20. Boral Limited
21. Caltex Australia Limited
22. ICI Australia Limited
23. Mayne Nickless Limited
24. Burns Philp & Company Limited
25. Brambles Industries Limited
26. Southcorp Holdings Limited
27. Gestetner Holdings P/C
28. Coca Cola Amatil Limited
29. Foodland Associated Limited
30. Comalco Limited
31. GIO Australia Holdings Limited
32. Brierly Investments Limited
33. Carter Holt Harvey Ltd
34. Lion Nathan Limited
35. Westfarmers Limited
36. James Hardie Industries Limited
37. Leighton Holdings Limited
38. Rothmans Holdings Limited
39. Lend Lease Corporation Limited

40. Email Limited
41. St. George Bank Limited
42. QBE Insurance Group Limited
43. Australian National Industries Limited
44. Tubemakers of Australia Limited
45. F.H. Fauldings & Co. Limited
46. FAI Insurances Limited
47. Spicers Paper Limited
48. George Weston Foods Limited
49. Metal Manufacturers Limited
50. WD & HO Wills Limited

Top 50 Companies for 1994

1. The News Corporation Limited
2. Broken Hill Proprietary Co. Ltd Coles Myer Ltd
3. National Australia Bank Limited The Adelaide Steamship Company Ltd
4. CRA Limited
5. Fletcher Challenge Limited
6. Commonwealth Bank of Australia
7. Coles Myer limited
8. Westpac Banking Corporation
9. Telecom Limited
10. BTR Nylex Limited
11. Australian and New Zealand Banking Group Limited
12. CSR
13. Amcor Limited
14. Pacific Dunlop Limited
15. Brierly Investments Limited
16. Carter Holt Harvey Ltd
17. Lend Lease Corporation Limited
18. Woolworths Limited
19. QBE Insurance Group Limited
20. Santos Holdings Limited
21. GIO Australia Holdings Limited
22. Nothern Broken Hill Limited
23. John Fairfax Holdings Limited
24. Pioneer International Limited
25. ICI Australia Limited
26. Burns Philp & Company Limited
27. Westfield Holdings Limited
28. Television Media Limited
29. Southcorp Holdings Limited
30. Coca Cola Amatil
31. Goodman Fielder Limited
32. Seven Network Australia Limited
33. Place Pacific Limited
34. Coal & Allied Industries Limited
35. Australian Gas Light Company Limited
36. Western Mining Corporation Limited
37. General Property Trust
38. Nine Network Australia Limited
39. QCT Resources Limited
40. Arnotts Limited
41. Advance Bank Australia Limited
42. Schroders Property Fund Limited
43. Stockland Corporate Trust
44. St. George Bank Limited

45. Westfarmers Limited
46. Rothmans Holdings Limited
47. Comalco Limited
48. Poseidon Gold Limited
49. Lang Corporation Limited
50. Email Limited

Top 50 Companies for 1995

1. Broken Hill Proprietary Co. Ltd
2. The News Corporation Limited
3. National Australia Bank Limited
4. CRA Limited
5. Westpac Banking Corporation
6. Fletcher Challenge Limited
7. Telecom Limited
8. Commonwealth Bank of Australia
9. Western Mining Corporation Limited
10. Australian and New Zealand Banking Group Limited
11. Amcor Limited
12. Coca Cola Amatil
13. Carter Holt Harvey Ltd
14. Lend Lease Corporation Limited
15. Coles Myer limited
16. Woodside Petroleum Limited
17. Fosters Brewing Corporation Limited
18. CSR
19. Comalco Limited
20. Boral Limited
21. Woolworths Limited
22. Pacific Dunlop Limited
23. Brambles Industries Limited
24. Pioneer International Limited
25. Brierly Investments Limited
26. MIM Holdings Limited
27. ICI Australia Limited
28. Northern Flinders Mines Limited
29. Westfield Trust
30. Qantas Limited
31. John Fairfax Holdings Limited
32. Santos Holdings Limited
33. Advance Bank Australia Limited
34. Westfarmers Limited
35. Mayne Nickless Limited
36. Southcorp Holdings Limited
37. GIO Australia Holdings Limited
38. General Property Trust
39. Placer Pacific Limited
40. Lion Nathan Industries Limited
41. Goodman Fielder Limited
42. Burns Philp & Company Limited
43. Westfield Holdings Limited
44. Poseidon Gold Limited
45. St. George Bank Limited
46. TNT Limited

47. Australian Gas Light Company Limited
48. QBE Insurance Group Limited
49. Renison Goldfields Limited
50. Normandy Mining Limited

APPENDIX II

Chow Statistic for Determining Structural Differences in a Relationship

Step I. Combine all the N_1 and N_2 observations of the two periods (in the current study combine low/moderate and high levels of activity) and run a single pooled regression:

$$Y_t = \alpha + \beta X_t + u_t$$

From this regression obtain the residual sum of squares (RSS) say S_1 , with degrees of freedom (df), $df = N_1 + N_2 - k$, where k is the number of parameters estimated.

Step II. Run the two individual regressions and obtain their RSS say, S_2 and S_3 , with $df = N_1 - k$ and $N_2 - k$, respectively. Add these two Residual Sum of Squares, say $S_4 = S_2 + S_3$ with $df = N_1 + N_2 - 2k$.

Step III. Obtain $S_5 = S_1 - S_4$.

Step IV. Apply the F test as follows:

$$F = \frac{S_5/k}{S_4/(N_1 + N_2 - 2k)}$$

With $df = k$, $N_1 + N_2 - 2k$. If computed F exceeds critical F, reject the null hypothesis that the two regressions are the same.

Appendix III

Chow Test to determine Cut off Between Low/Moderate to High levels of International Diversification

The approach using the Chow test is reflected below. If there appears to be a difference, from glancing at the data set, between high and low/moderate levels of international diversification then parameters of the EP function may have changed. Let us use a 35% cut off point to make an evaluation.

i.e.,
$$EP1 = IBD (35\%) + SRD + Z \text{-----}(1)$$

N1 observations

$$EP2 = IBD (65\%) + SRD + Z \text{-----}(2)$$

N2 observations

Where:

EP1: economic performance when international diversification is selected at the proportion less than 35%

EP2: economic performance when international diversification is selected at the proportion greater than 35%

IBD: international business diversification

SRD: social responsibility disclosure

Z: other relevant variables

The number of observations between EP1 and EP2 can be the same or different.

If there is no change in the parameters then we can combine N21 and N2 and merely estimate one EP function

$$EP = IBD + SRD + Z \text{-----}(3)$$

N1 + N2 observations

Question:

How do we determine whether there is a structural change in EP relationship between high and low/moderate IBD?

Method:

Use can be made of the steps outlined in Gujararti (p.262, 1995)

Step I:

Combine N1 and N2 observations

i.e., from.... (3) $EP = IBD + SRD + Z$, call this RSS, S1

Estimate the Residual Sum of Squares (RSS) of this relationship.

Step II:

Estimate RSS

From ...(1) $EP1 = IBD (35\%) + SRD + Z$, call this RSS, S2.

From ...(2) $EP2 = IBD (65\%) + SRD + Z$, call this RSS, S3.

Then obtain RSS for EP1 and EP2

i.e. $S4 = S2 + S3$

Step III:

Obtain S5; $S5 = S1 - S4$

Step VI:

Given the assumptions of the Chow test it can be shown that

$$F = \frac{S5 / k}{S4 / (N1+N2-2k)} \text{-----(4)}$$

The Null Hypothesis is:

No difference in the N1 and N2 observations in the relationship between economic performance and IBD.

If it can be shown that F from (4) exceeds the critical F value then we can reject the null hypothesis. This means that the difference is significant and the split between N1 and N2 can be done in a robust fashion thus assisting in determining the cut off point at which low/moderate level ends and conversely high level begins.

APPENDIX IV

Step Method to determine Multicollinearity using the Variance Inflation Factor

A three Step Process for determining multicollinearity (Studenmund, 1985: 275).

For instance to determine the VIF to detect multicollinearity in an equation with k independent variables:

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \dots + \beta_k X_k + \varepsilon$$

Step I: Run an OLS regression that has a function of all the other explanatory variables in the equation. For example, if, $i=1$, then

$$X_1 = \alpha_1 + \alpha_2 X_2 + \alpha_3 X_3 + \dots + \alpha_k X_k + v$$

where v is a typical stochastic error term. Note that X_1 is not included on the right hand side of the equation, which is referred to as the auxiliary regression. Thus there are k auxiliary regressions, one for each independent variable in the original equation.

Step II: Calculate the VIF for β_i :

$$\text{VIF}(\beta_i) = \frac{1}{(1-R_i^2)}$$

where R_i^2 is the coefficient of determination (the unadjusted R^2) of the auxiliary regression in step one. Since there is a separate auxiliary for each independent variable in the equation, there is also an R_i^2 and $\text{VIF}(\beta_i)$ for each X_i .

Step III: Analyse the degree of multicollinearity by evaluating the size of the $VIF(\beta_i)$. The higher a given variable's VIF, the higher the variance of that variable's estimated coefficient. Hence, the higher the VIF, the more severe the effects of multicollinearity.

A common rule of thumb (since there is no table of Critical VIF's) is if $VIF(\beta_i) > 5$, then multicollinearity is severe.

APPENDIX V

Applying the Chow Statistic for International Diversification in the period 1993-1995

The following calculation supports this finding:

$$S1 = 28.453$$

$$df = 151 - 9 = 142$$

$$\text{where } N = N1 + N2 = 151$$

$$S2 = 20.328$$

$$df = 97 - 9 = 88$$

$$\text{where } N1 = 97$$

$$S3 = 0.109$$

$$df = 54 - 9 = 45$$

$$\text{where } N2 = 54$$

$$\text{therefore: } S4 = S2 + S3 = 20.437$$

$$\text{where } df = N1 + N2 - 2k$$

$$= 97 + 54 - 2(9)$$

$$= 133$$

Which provides for $S5 = S1 - S4$

$$= 28.453 - 20.437$$

$$= 8.016$$

The F Chow Statistic can now be calculated as

$$F = \frac{S5/k}{S4 / (N1 + N2 - 2k)}$$

$$= \frac{8.016/9}{20.437/(133)}$$

$$= \frac{8.016/9}{20.437/(133)}$$

$$= 5.8$$

Correspondingly the Critical F Value which this is compared with is derived from F table D.3 (Gujarati, p.814, 995). Using numerator of 9 and denominator 133

Critical F = 2.56

F chow 5.8 > F Critical 2.56 by a significant amount therefore the null hypothesis is rejected and the 35 % cut off point is recognised as a robust measure for dividing the international diversification strategy into low/moderate and high at that level for the sample covering three years 1993-1995.

APPENDIX VI

Chow test for International Diversification in each individual year of the study covering 1993-1995

First, when considering year 1993 and explanatory variable international diversification is split in the order of <35% as low/moderate and >=35% as high the following analysis results from applying the Chow test. If the Chow F statistic exceeds the critical F value (refer table D.3 Gujarati, p.814, 995) the null hypothesis will be rejected. This needs to be tested for the 35% level for 1993.

Using the above technique, the following calculation will test whether a structural split, with a cut off point at 35% in the year 1993, into low and high is a statistically acceptable one:

$$S1 = .550$$

$$df = 49 - 10 = 39$$

$$\text{where } N = N1 + N2 = 28 + 21 = 49$$

$$S2 = .483$$

$$df = 28 - 10 = 18$$

$$\text{where } N1 = 28$$

$$S3 = 0.0146$$

$$df = 21 - 10 = 11$$

$$\text{where } N2 = 21$$

$$\text{therefore: } S4 = S2 + S3 = .497$$

$$\text{where } df = N1 + N2 - 2k$$

$$= 28 + 21 - 2(10)$$

$$= 29$$

$$\text{Which provides for } S5 = S1 - S4$$

$$= .550 - .497$$

$$= .053$$

The F Chow Statistic can now be calculated as

$$F \text{ Chow} = 3.11$$

Correspondingly the Critical F Value which this is compared with is derived from F table D.3 (Gujarati, p.814, 995). Using numerator of 10 and denominator 29

$$F \text{ Critical} (10, 29) = 2.16$$

F chow > F Critical by a significant amount therefore the null hypothesis is rejected and the 35 % cut off point is recognised as a robust measure for dividing the international diversification strategy into low/moderate and high at that level. In this case F Chow > F Critical so we reject the null hypothesis. This method will be utilised further for the remaining two years 1994 and 1995

International Diversification Year 1994

$$F \text{ Chow} = 8.3028$$

$$F \text{ Critical} (10, 68) = 2.11$$

In this case F Chow > F Critical so we reject the null hypothesis

International Diversification Year 1995

$$F \text{ Chow} = 2.88$$

$$F \text{ Critical} (10, 63) = 2.10$$

In this case F Chow > F Critical so we reject the null hypothesis

APPENDIX VII

Chow test for Stakeholder Management in the period 1993-95

The following calculation supports this finding using the above step analysis:

$$S1 = 28.325$$

$$df = 141 - 12 = 129$$

$$\text{where } N = N1 + N2 = 141$$

$$S2 = 20.825$$

$$df = 59 - 12 = 47$$

$$\text{where } N1 = 59$$

$$S3 = 1.039$$

$$df = 82 - 12 = 70$$

$$\text{where } N2 = 82$$

$$\text{therefore: } S4 = S2 + S3 = 20.825 + 1.039 = 21.864$$

$$\text{where } df = N1 + N2 - 2k$$

$$= 59 + 82 - 2(12)$$

$$= 117$$

$$\text{Which provides for } S5 = S1 - S4$$

$$= 28.325 - 21.864$$

$$= 6.461$$

The F Chow Statistic can now be calculated as

$$F = \frac{S5/k}{S4 / (N1 + N2 - 2k)}$$

$$= \frac{6.461/12}{21.864/(117)}$$

$$= 2.88$$

Correspondingly the Critical F Value which this is compared with is derived from F table D.3 (Gujarati, p.814, 995). Using numerator of 9 and denominator 133

$$F \text{ Critical} = 1.60$$

The result is that $F_{\text{Chow}} > F_{\text{Critical}}$ by a significant amount therefore the null hypothesis is rejected and the “15 sentences-of-prose’ cut off point is recognised as a robust measure for dividing social responsibility disclosures into low/moderate and high level stakeholder involvement

APPENDIX VIII

Chow test for Stakeholder Management in each individual year of the study covering 1993-95

First, when considering year 1993 and explanatory variable Social responsibility reporting split in the order of , <15 sentences as low/moderate and ≥ 15 sentences as high the following analysis results from a Chow test. If there appears to be a difference, from glancing at the data set, between high and low levels of social responsibility reporting then parameters of the EP function have changed.

Using the same technique above

F Chow = 4.01

F Critical (10, 29) = 2.16

In this case F Chow > F Critical so we reject the null hypothesis

Stakeholder Management Levels- Year 1994

F Chow = 3.025

F Critical (10, 33) = 2.15

In this case F Chow > F Critical so we reject the null hypothesis

Stakeholder Management Levels- Year 1995

F Chow = 2.72

F Critical (12, 37) = 1.99

In this case F Chow > F Critical so we reject the null hypothesis

In sum, there is evidence that the Chow statistic provides strong justification to divide the sample in to high and low/moderate for each of the individual years and the null hypothesis can be rejected in all cases. This result enables consideration to be given to low/moderate and high levels of stakeholder involvement when testing the relationship between economic performance and stakeholder management

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