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Corporate aging and investment decisions

Dissertation abstracts

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Paper I: Corporate aging and internal resource allocation

Abstract

Various observers argue that established firms are at a disadvantage in pursuing new growth opportunities. In this paper, we provide systematic evidence that established firms allocate fewer resources to high-growth lines of business. However, we find no evidence of inefficient resource allocation in established firms. Redirecting resources from high-growth to low-growth lines of business does not result in lower profitability. Also, resource allocation towards new growth opportunities does not increase when managers of established firms are exposed to takeover and product market threats. Rather, it seems that conservative resource allocation strategies are driven by pressures to meet investors' expectations. Our empirical evidence, thus, favors the hypothesis that established firms wisely choose to allocate fewer resources to new growth opportunities as external pressures force them to focus on efficiency rather than novelty (Holmström 1989).

Paper II: Corporate aging and asset sales

Abstract

This paper asks whether divestitures are motivated by strategic considerations about the scope of the firm's activities. Limited managerial capacity implies that exploiting core competences becomes comparatively more attractive than exploring new growth opportunities as firms mature. Divestitures help established firms free management time and increase the focus on core competences. The testable implication of this attention hypothesis is that established firms are the main sellers of assets, that their divestiture activity increases when managerial capacity is scarcer, that they sell non-core activities, and that they return the divestiture proceeds to the providers of capital instead of reinvesting them in the firm. We find strong empirical support for these predictions.

Paper III: Corporate aging and lobbying expenditures

Abstract

Creative destruction forces constantly challenge established firms, especially in competitive markets. This paper asks whether corporate lobbying is a competitive weapon of established firms to counteract the decline in rents over time. We find a statistically and economically significant positive relation between firm age and lobbying expenditures. Moreover, the documented age-effect is weaker when firms have unique products or operate in concentrated product markets. To address endogeneity, we use industry distress as an exogenous non-legislative shock to future rents and show that established firms are relatively more likely to lobby when in distress. Finally, we provide empirical evidence that corporate lobbying efforts by established firms forestall the creative destruction process. In sum, our findings suggest that corporate lobbying is a competitive weapon of established firms to retain profitability in competitive environments.