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Disentangling the impacts of industrial and global diversification on firm risk

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ABSTRACT

We examine the impact of corporate diversification on firm risk exposure from 1998 to 2016. We find that both global and industrial diversification mitigate idiosyncratic and world market risk while having a negligible impact on U.S. market risk, but the effects vary before, during, and after the financial crisis of 2007–2009. Before the crisis, only global diversification mitigates idiosyncratic risk, but it increases firms' exposure to world market risk. During the crisis, industrial diversification increases idiosyncratic risk, but both types of diversification increase exposure to U.S. market risk. After the crisis, both types of diversification increase firms' exposure to U.S. market risk but have negligible impact on idiosyncratic and world market risk. Our findings remain robust after we control for the potential endogeneity of the diversification decision through various self-selection models.

JEL classifications:

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