

DIVERSIFICATION AS A MODERN GROWTH STRATEGY IN AGRICULTURE

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INTRODUCTION

The global economic crisis has had a major impact on enterprises operating in the agricultural sector in numerous countries, Ukraine among them. A significant increase in inflation and production costs, as well as a decline in production profitability and changes in tax laws, have hindered the development of enterprises and forced producers to extend the scope of their activities and seek more optimal growth strategies. Dynamic changes in the market environment prompt the need to develop marketing strategy that would most comprehensively take into account transformations of the market environment. Diversification, the subject of this paper, can be the optimal strategy in uncertain conditions. In this context, the large-scale problem of using marketing strategies for diversification in the agricultural sector, where climatic conditions pose such a risk, is particularly important. Diversification strategy creates a synergy, by which farms increase their economic efficiency and strengthen their competitive position in the market. Scientists, including Chandler [1962], Kotler [1990], Ansoff [1999], Porter [2005], Kudenko [2006] and others, have contributed significantly to the theoretical understanding of diversification strategy. Author has used their work as a fundamental basis for further research in this area. For diversification strategy in the agricultural sector, the work of Lemishko [2001], Kaninsky [2003], Kareba [2012], Malik [2012], and Pelykh [2014] stand out. These scholars' theoretical work forms the basis for practical application of diversification strategy in the farming sector. The prospects for and problems in agricultural diversification strategy is important and requires further research.

RESEARCH OBJECTIVE AND METHODOLOGY

The study examines the theoretical foundations of diversification strategy and identifying characteristics of its application in agriculture. The following research methods were used: analysis, synthesis, induction, deduction, comparison, generalisation and graphic method.

STRATEGY AND MARKETING STRATEGY

In the presence of rapid market transformation, it becomes increasingly urgent for enterprise to develop strategy. Larina has noted that “the process of developing strategy is considered to be the core of strategic management” [Larina 2008]. Given that strategy forms the direction a company will take moving forward, the claim seems justified. Chandler defines strategy as “the establishment of long-term goals and objectives of the company, elaboration of the actions plan and allocation of resources needed for these purposes” [Chandler 1962]. According to this definition, enterprise strategy is developed and implemented in order to beat competitors, capture greater market share, increase profits, receive and/or reinforce a synergetic effect and achieve other goals [Mocherny et al. 2005].

According to Kudenko, marketing strategy accounts for 80% of overall business strategy [Kudenko 2006]. After all, no enterprise can fully develop without forming and implementing marketing strategy, which is one basis for the enterprise to develop and grow.

Unfortunately, the expediency of developing and using marketing strategies in the Ukrainian farming sector, compared with the developed countries of Europe and other leading countries of the world, is not taken seriously by the heads of enterprise. The development of an effective marketing strategy that takes into account all the factors of the micro and macro environment requires appropriate knowledge, time and money. A systematic approach to its development fully justifies meeting these expenses, because scientifically grounded decisions about choosing marketing strategy will help the enterprise to survive when the external environment turns hostile. Since most agricultural groups aim not only to survive in today’s unstable market, but to ensure growth, this paper focuses in more detail on one marketing strategy for growth.

DIVERSIFICATION STRATEGY: FEATURES AND TYPES

Growing competition requires companies to constantly change the direction they’re moving in. The search for alternative areas of business to complement their main ones can be described as both a diversification and a growth strategy – ones that are often implemented when all paths to intensive growth have been exhausted. According to the definition of diversification given in the economic encyclopedic dictionary edited by Mocherny, “diversification (lat. *diversus* – different, remote, and *facere* – to do) is an expansion of the range and change of the appearance of products produced by individual enterprises, firms and companies” [Mocherny et al. 2005]. Kaminsky noted that diversification is the opposite process of production specialisation: one company combines many commodity

sectors, and sometimes even unrelated ones [Kaninsky 2003]. At the same time, however, specialisation and diversification are often parallel forces that complement each other, but nonetheless differ significantly. Excessive concentration on specialisation can greatly increase the risk of an enterprise failing. However, rash decisions or inconsistent actions in the diversification process can likewise lead to significant risks. Waterman [1988] emphasised, on the other hand, that the greatest risk to the entrepreneur is the risk of doing nothing. This would suggest that doubts and fears about a company's entrance to new areas of activity must be allayed. The Ansoff matrix gives more illustrative understanding of diversification strategy (Table 1).

TABLE 1. The Ansoff matrix

Market	Commodity	
	existing	new
Existing	strategy of deep market penetration	commodity development strategy
New	market development strategy	diversification strategy

Source: Ansoff 1999.

As Table 1 shows, a feature of diversification strategy is that it simultaneously involves both new product development and access to new markets. This in its turn is due to higher financial costs and risks compared to the other strategies presented in the matrix. Thus, diversification exists in two main forms:

- expansion of the range of products, the production of new products and the modification of that production within a given area;
- penetration into new industries and areas of the economy, through the creation of new businesses and acquisitions of others, which is the basis of the emergence of multi-business concerns [Mocherny et al. 2005]. These forms of diversification grew out of the search for additional sources of income to reduce the risk of bankruptcy in conditions of lower demand for basic products.

Diversification is accomplished mainly by one of these means: acquiring or merging with a company already working in a new field, creating a new enterprise "from scratch", or entering into a joint venture [Dican 2013]. To penetrate a new market of field, the fastest of the three is to merge with or absorb an enterprise already working in the field the company wishes to push into. The downside to this approach is that overcoming barriers to entry can be very expensive. To choose the company with which future integration ties will be built, the enterprise will need not only significant financial resources, but also to spend time. In fact, implementation of the integration process with a little known or uncompetitive enterprise does not justify the effort given and will not lead to the desired results. One outcome of diversification is the emergence of diversified conglomerates that combine enterprises from many industries and which are unrelated by a technology chain [Mocherny et al. 2005].

The most common types of diversification are concentric (vertical), horizontal and conglomerate diversification. Table 2 describes the features, advantages and disadvantages of each.

TABLE 2. The features of diversification types

Diversification types	Definition	Advantages	Disadvantages
Concentric (vertical)	Adding to the existing range of products, which from a technical and marketing point of view are similar to existing goods	<ul style="list-style-type: none"> – reduces dependence on one product or market – uninterrupted supply of material and technical resources – possibility to share risks – control over the work of all parts of the production chain 	<ul style="list-style-type: none"> – collaboration between departments, which reduces internal competition between units in the enterprise (commodity prices are not decreased) – due to interconnection between units, in the event of a one unit malfunctioning affects the whole enterprise
Horizontal	Adding to the assortment of products in no way related to those already produced but can arouse interest among existing clients	<ul style="list-style-type: none"> – growth in competitiveness in domestic and foreign markets – synergy effect – scale effect – better meet the needs of customers 	<ul style="list-style-type: none"> – sudden reduction of distribution area (prompting the need to radically change scope)
Conglomerate	Adding to the range of products which have nothing to do with the technology used by the firm or its products and markets	<ul style="list-style-type: none"> – provide full utilization of productive potential of the field in new markets and products previously gained 	<ul style="list-style-type: none"> – significant increase in costs of new technology, product development – need for skilled workers and new markets – available only to large enterprises

Source: supplemented and summarised by the author on the basis of Kotler 1990, Porter 2005.

As Table 2 shows, conglomerate diversification is both the riskiest and most expensive type because it involves the production of a new product not connected with existing ones and is offered to new customers in new markets. Such diversification is limited to large-scale enterprises with sufficient financial resources.

DIVERSIFICATION STRATEGY IN UKRAINE'S AGRICULTURAL SECTOR

Agriculture is a strategically important sector for Ukraine. It not only guarantees the country food security, but also figures prominently in its GDP (in 2015, agriculture accounted for 11.9% of GDP). Here we will consider in greater detail the place of strategy diversification in the sector. The seasonality of production and considerable dependence on climatic conditions (which are the main factors in choosing the direction of specialisation), the need to take into account environmental factors and limited areas of agricultural land all account for the peculiarity of the country's production diversification.

A leading expert on Ukraine's agricultural sector, Malik identifies the leading aspects of agricultural diversification as including "expanding the range and assortment, chang-

ing the types of products manufactured by enterprise, development of new industries to improve production efficiency, obtaining economic benefits, and prevention of bankruptcy taking into account the ecological and social needs of the population” [Malik 2012]. The formation of agricultural diversification strategy is thus used to prevent bankruptcy through moving into other areas of production and capturing new markets. Malik also describes the main factors that led to the further implementation of diversification strategies: Ukraine’s economy has transitioned from a command-administrative management system to a market economy, and technological progress changes in human psychology have both occurred. According to Lemishko, diversification of agricultural enterprises provides “integration of primary production of agricultural products with other activities, including manufacturing, trade, services, the creation of new products, services and markets” [Lemishko 2001].

Diversification trends in agriculture include [Kovalenko et al. 2008]:

- making agricultural organisations more versatile;
- increasing the share of ancillary industries and industries;
- mergers and acquisitions in the integrated structures;
- expansion of non-farm activities in rural areas to increase incomes.

The main features of diversification are the entry into new areas of production and expansion of activities. As an example, agrarian enterprises can provide services in construction and transportation, as well as in everyday life (various studios, hairdressing salons, zootechnical and other services, agrarian shops, milk collection stations, bakeries) and in the development of green tourism. Given Ukraine’s limited land resources, important types of agricultural enterprise diversification include selling and processing locally grown products, expanding sales channels for these products, and developing various subsidiary enterprises and industries [Kareba 2012]. Depending on the goal and market situation, the enterprise determines the direction of diversification on its own. The biological nature of agricultural production requires the combination of those crops which properly meet crop rotation requirements. After all, soil exhaustion in the longer term will destroy yields. Furthermore, the diversification of crops for which different weather conditions are favourable is also an effective way to reduce the risk of low-yield harvests, though this approach carries with it certain expenses.

As a result of vertical diversification in Ukraine, holding structures are formed, and the current process of transformation continues. Integrated units should also include associations, unions, cooperatives, corporations, financial-industrial groups and agricultural holdings. Agricultural structure is the highest form of vertical integration, the existence of which significantly increases the competitiveness of the agricultural sector of Ukraine, particularly with respect to export figures. The single largest agricultural holding in all of Eurasia – UkrLandFarming – operates on 654,000 ha located in 22 regions of Ukraine. This agroholding is an example of multi-production, including crop production (including seed production), dairy cows and beef cattle, eggs and egg products, sugar production, meat processing, storage and sale of grain and industrial crops, distribution of agricultural technology, parts, plant protection products, mineral and special fertilizers, seeds and technical service. Main crops include sunflowers, corn, sugar beets and wheat [WWW 1]. All of these activities and crops speak to UkrLandFarming’s versatility, a significant advantage of which is the lack of dependence on a single activity.

Diversification leads to effective interaction between agricultural enterprises and processors. It optimises existing production and introduces new lines and technologies, based on the needs of consumers. The development of an agricultural complex based on diversification of agricultural enterprises ensures the rational use of natural, industrial, financial and labour capacity and can extend production volumes [Pelykh 2014]. The figure presents the value of agricultural enterprise diversification for different categories of economic relations.

This section has shown that there are a number of benefits of implementing diversification strategy in the agricultural sector. They include: increasing the competitiveness of enterprises and their products, especially in foreign markets; strengthening enterprise market position; obtaining synergy; integration with processors, leading to the efficient use of resources; expansion of product range; and reducing risk by eliminating dependence on a single product. However, like any economic phenomenon, there are also drawbacks, which here include the fact that manufacturing processes and control are complicated; time and money must be spent to uncover and study the products and services in demand; and reduced scale effect, which is typical for highly specialised businesses.

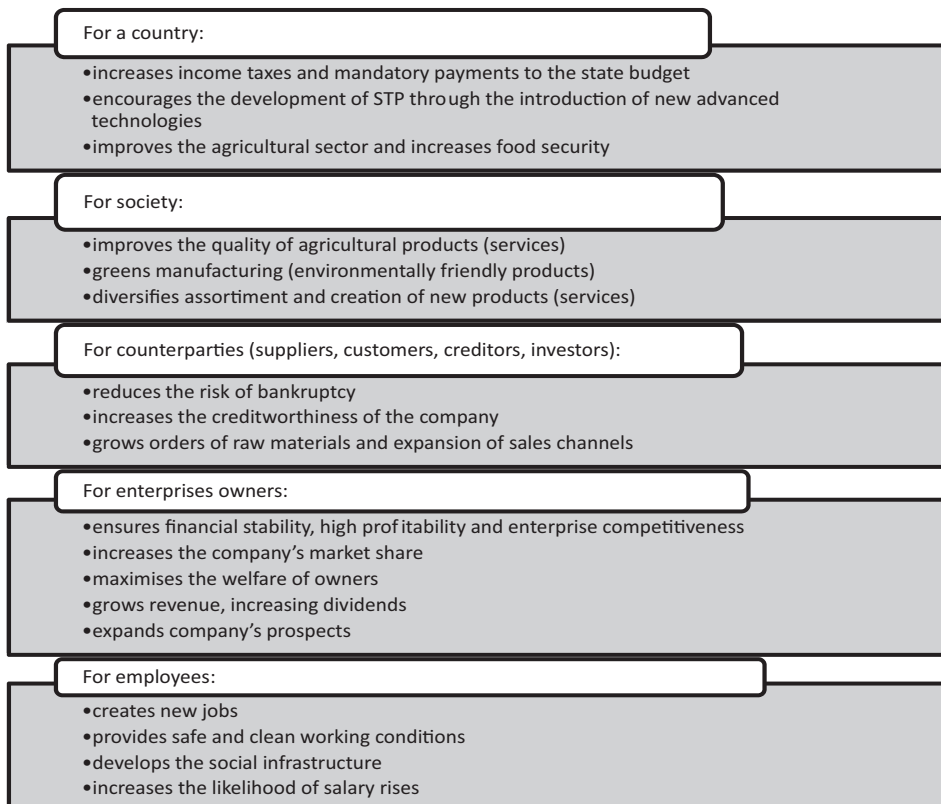


FIG. Value of agricultural enterprise diversification for different categories of economic relations
Source: the author, based on Tsalko 2008.

CONCLUSIONS

In summary, it is clear that marketing strategy forms the basis for the choice of activities for an enterprise to achieve desirable growth. In the prevailing market conditions, when demand for main products decreases, it is reasonable to use a diversification strategy, which enables the development of new goods to be sold and new spheres of activity to be entered. In turn, this allows the enterprise to establish stronger positions on the market than when it opts for highly specialised economic activity. However, diversification is expensive, and is the riskiest growth strategy. In the scientific literature, the most often discussed forms of diversification include concentric (vertical), horizontal and conglomerate diversification. The most effective and least risky is the first – vertical strategy – which involves obtaining a synergistic effect and reducing transaction costs (a single production chain from field to consumer). Agricultural holding companies are an excellent example of the effective use of vertically integrated production diversification. The agricultural industry is characterised by seasonality and operates very much at the mercy of nature and climatic conditions. Effective diversification calls for all factors to be considered – including nature and the climate, both of which are, unfortunately, difficult to estimate or predict.

The practical value of this paper is its relevance to the use of diversification strategy in today's agricultural market to move into other areas of activity. Diversification makes it possible to minimise risks and provide stable financial results even when demand for basic products fluctuates.

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Summary. The aim of the article is to examine the theoretical foundations of diversification strategy and identify the characteristics of its application in agriculture. The relevance of diversification strategy research is that its implementation allows additional income to be made, ensures financial stability for enterprise when demand for basic products fluctuates, and strengthens the competitive position in chosen markets. The importance for enterprise of implementing growth strategy is discussed, as is the economic essence of “marketing strategy”. Dynamic changes in the market force producers to review their activity and seek a more optimum development strategy. Diversification can be the optimal strategy when market conditions are uncertain. The article analyzes the essence and types of diversification along with the benefits and disadvantages of diversification strategy. As a result of the research, features of diversification strategy for the agricultural sector were analysed, the essence of which may be found in the unification of agricultural products with other kinds of activity. This is done to decrease the risk arising from receding demand for main agricultural products. The study found that the most effective and least risky strategy is vertical diversification, which involves obtaining a synergistic effect and reducing transaction costs (through the use of a single production chain from field to consumer).

Key words: strategy, marketing strategy, diversification, agrarian groups, agricultural enterprises

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