Value Creation through Vertical Intervention of Corporate Centres in Single Business Units of Unrelated Diversified Portfolios - The Case of Private Equity Firms

Abstract:
This article addresses value creation by corporate centres of multi-business firms through vertical intervention in single business units. Drawing on parenting literature, agency theory, and the resource-based view, we develop a model comprising an interlinked set of hypotheses on value creation. These take into account the administrative as well as the entrepreneurial value creation function of a corporate centre. The model depicts value creation from the perspective of individual businesses in an unrelated-diversified portfolio and is tested in a unique and unconventional research setting. Regarding the necessity to add value to businesses, we consider private equity firms to have a similar role as the centre of an unrelated diversified multi-business firm, and analyse survey data on 267 portfolio companies using partial least squares structural equation modelling. The results show that corporate centres can create value through vertical intervention in single business units, by reducing agency costs through governance mechanisms as part
of their administrative function and, interestingly, by also providing businesses access to strategic resources during the course of their entrepreneurial function. In particular, the provision of intangible resources, i.e., the knowledge and networks of the corporate centre, shows to have a value creating effect on business units. Not related to the units' performance is a corporate centre's attempt to create value using horizontal synergy by fostering the cooperation of a business unit with other units.

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