

The Diversification of Production*

by

Boyan Jovanovic
New York University

ABSTRACT

This paper entertains the hypothesis that a firm will diversify its production so as to employ its slack managerial resources, and/or to capture R&D spillovers among its products. The paper builds a multiproduct version of Lucas's span of control model. The first version of the model shows that the historical trend towards larger and more diversified firms can in part be explained by the growth in the economy's capital-labor ratio.

The second version of the model shows that more R&D intensive firms should, on efficiency grounds, be more diversified, although the highly tentative estimate contained in this paper suggests that the size of the R&D spillovers that diversification creates may be small.

* I thank the C.V. Starr Center for Applied Economics at New York University for technical and financial help; and Martin Baily, Michael Gort, Yaw Nyarko, Steve Olley, Peter Reiss, Mike Scherer, Clifford Winston, and the discussants for useful comments, and Ray Atje and Chung Yi Tse for help with the research. Two earlier versions of this work were presented in an economic fluctuations group organized by Ricardo Caballero and Andy Caplin, and this led to considerable improvement.