

Risks And Countermeasures Related to Diversification Strategy: Taking Yunnan Baiyao as An Example

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Abstract. As the cornerstone of the operation of listed companies, enterprise strategy has attracted more and more attention. Diversification strategy is a company level strategy that many companies choose to adopt. However, diversification strategy has advantages and disadvantages. How to prevent the risks from diversification strategy is worthy of our study. Therefore, this paper selects Yunnan Baiyao as a case company, specifically discusses the risks of its diversification strategy, and puts forward adjustment suggestions for its strategy, so as to provide direction for the strategic formulation and timely adjustment of relevant enterprises and industries.

Keywords: Corporate strategy, Diversification strategy, Yunnan baiyao group co., ltd., Suggestions.

1. Introduction

The most important aspect of establishing and developing a business is the formulation and execution of strategies. An effective strategy can coordinate, integrate, and allocate a company's resources, capabilities, and competitiveness to better adapt to the external environment. At the same time, the basic goal of any strategy is to achieve strategic competitiveness and excess profits. Therefore, studying the company's strategy has profound theoretical and practical significance.

Generally speaking, strategic choices include business level strategy, company level strategy, merger and acquisition strategy, internationalization strategy, and cooperation strategy. Among them, product diversification is a major form of corporate strategy, focusing on the range of markets and industries in which the company participates in competition. Although successful diversification can bring revenue from different business units to reduce the uncertainty of a company's profits, blindly adopting diversification strategies or excessively promoting diversification by management is highly likely to reduce the company's ability to create value.

Many listed companies in China and even internationally have adopted a diversification strategy. This paper selects Yunnan Baiyao as a case company to explore the current situation, existing risks, reasons, and countermeasures of its diversification strategy, in order to conduct in-depth research on this strategy, understand the importance of strategic matching and transformation for the company's development, and ultimately propose certain adjustment suggestions, providing reference for the development of Yunnan Baiyao and similar enterprises.

2. Introduction and Strategic Status of Yunnan Baiyao

2.1 Introduction to Yunnan Baiyao

Yunnan Baiyao Group Co., Ltd. (000538) was listed on the Shenzhen Stock Exchange in 1993. It is one of the first batch of national innovative enterprises and a well-known China Time-honored Brand at home and abroad.

The company completed the mixed ownership reform from 2016 to 2019, and at the same time, the company attaches great importance to brand value and does not forget to invest in research and development. Yunnan Baiyao continues to adopt a diversification strategy and steadily embarks on an internationalization journey. Therefore, Yunnan Baiyao still has sufficient momentum for enterprise development and remains at the forefront of the industry.

The business segments of Yunnan Baiyao include pharmaceuticals, health products, traditional Chinese medicine resources, tea business, industrial hemp business, etc. Each business segment has diversified products and services.

2.2 Yunnan Baiyao’s Diversification Strategy

The current company strategy of Yunnan Baiyao is to strengthen the central business and highlight the "two wings", which continuously enhances the four central business sectors of medicine, health products, traditional Chinese medicine resources, and medical logistics, and promotes the research and development of new products in the fields of orthopedics and medical aesthetics, in order to form a strategic synergy and focus on the company's long-term strategic goals.

In 2022, Yunnan Baiyao established a strategic direction of "1+4+1", completing its layout in Beijing, Shanghai, Hong Kong, Hainan, and South Korea, forming an important strategic support for gathering global resources and serving the Chinese market.

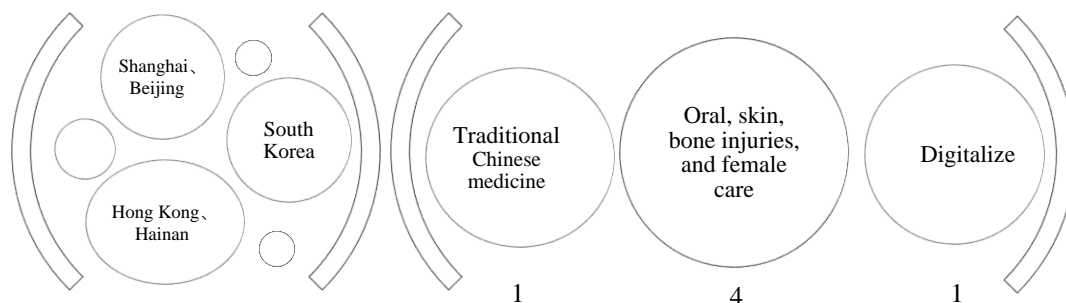


Fig. 1 "1+4+1" Strategic Layout

Yunnan Baiyao adopts a diversification strategy to improve overall performance and enhance the company's value. In fact, its financial data is also very stable, and its operating revenue is steadily increasing. The beneficial effects of the implementation of its strategy are as follows. Diversified operation is conducive to economies of scope. On the basis of Baiyao, it has joined a number of other businesses, reducing the cost of unit products. Forming synergy effects, Yunnan Baiyao's various traditional Chinese medicines, health products, etc. can share enterprise resources to create additional value. Diversified products and services can meet customer needs, enhance competitive advantages, avoid operational risks, and expand the company's control over the market.

Table 1. Financial Performance of Yunnan Baiyao

Years	2016	2017	2018	2019	2020	2021	2022
Operating margin (%)	14.8136	14.8911	14.3476	15.9886	20.8046	9.5815	9.2393
Main business profit margin (%)	29.1775	30.4894	29.8879	28.0794	27.2496	26.6203	25.7463
Proportion of non main business (%)	7.9922	7.6766	7.2212	30.7581	5.6065	29.8962	25.8786

However, Yunnan Baiyao still faces many risks in adopting a diversification strategy, facing fluctuating external environment and increasingly fierce market competition. It only maintains a weak growth rate in business performance and financial situation, and cannot enable the enterprise to break through and leverage its advantages. It urgently needs a more mature strategy to be formulated and implemented, as detailed in the following analysis.

3. Risks in Yunnan Baiyao's Diversification Strategy

3.1 Industry Entry Risks

Yunnan Baiyao actively explores new markets to seek new development opportunities, but opportunities and challenges coexist. While exploring new business sectors or industries, unknown market risks, management risks, and debt risks are closely following, and enterprises need to quickly respond to the changing environment. In terms of industry entry risk, unrelated diversification is more uncertain than related diversification, such as Yunnan Baiyao's financial business and medical beauty business. Implementing a diversification strategy is not only a buying option, but also a comprehensive result of balancing cost and benefits, conducting sufficient market research, and valuing business quality. Blindly investing in a large amount of diversified business is irrational and unpredictable, which will only pose greater risks to subsequent business development and have a negative impact on the overall enterprise.

3.2 Internal Integration Risks

Due to the different business processes, management models and market conditions of different products and services, it is not easy for enterprises to bring their diversified businesses into full play. At the same time, the management and decision-making brought about by the newly invested industries of enterprises will have a certain impact on the existing industries, which may be good or bad. As a whole, enterprises need to integrate different business segments and their management mechanisms, which is a major challenge for enterprises.

Furthermore, a company's resources are limited, and investing too much in new industries may lead to excessive dispersion of resources. Yunnan Baiyao has a number of industries. What is more necessary now is to go deep into business and seek intersections between business, abandon non-value-added service, and choose business that can create more value. If we continue to expand, the internal management of the enterprise may become chaotic, resources and capabilities cannot be effectively utilized, and the risk of internal integration gradually increases.

3.3 Main Business Weakening Risk

The main product of Yunnan Baiyao is the Baiyao series, with the main business sectors being traditional Chinese medicine, pharmaceuticals, health products, etc. In addition, there are many businesses such as tea, medical equipment, industrial hemp, etc. Based on this, the main business of the enterprise has gradually become unclear. If the diversification strategy is not improved, it may lead to the loss of market and advantage in the original dominant products or main business competition. To achieve long-term development, Yunnan Baiyao must focus on its core competitiveness and build a sustainable competitive advantage.

At the same time, the diversification process will produce development cost, supervision cost, investment cost, etc. The ideal business portfolio can balance the costs and benefits brought about by diversification, while the unbalanced or non-core business portfolio will make it difficult for enterprises to maintain capital and technical support, and ultimately lose competitiveness. Therefore, when optimizing strategic adjustments, Yunnan Baiyao urgently needs to solve the problem of insufficient core competitiveness and reduce the risk of weakening its main business.

3.4 Other Risks

In addition to the risk of industry entry, if Yunnan Baiyao opens up new business lines but the ultimate benefits are not good, a risk of industry exit will arise. At that time, the enterprise will lose a batch of manpower, material resources, and technical resources that have already been invested.

The more radical the corporate strategy is, the more serious the goodwill foam phenomenon is. If a company chooses to acquire new business in order to diversify, there may also be merger and acquisition risks.

Besides, market risk is an unpredictable and unavoidable risk, and the diversified industry of Yunnan Baiyao will face various market risks. A company needs sufficient cash flow support to combat potential risks that may occur at any time.

4. Suggestions for Strategic Adjustment of Yunnan Baiyao

In the face of the above-mentioned risks in the diversification strategy of Yunnan Baiyao, the author has analyzed and summarized the following suggestions for strategic adjustment.

4.1 Vigorously Developing Main Businesses with Core Competitiveness

Appropriate business expansion during the growth stage is beneficial for enterprises to seize more market share, but in the mature stage, it is best to selectively develop business, focusing on businesses with core competitiveness and great potential, while abandoning businesses with long investment payback periods, high capital occupation, and high market risks, to prevent the occupation of enterprise resources and capabilities. The basic point for Yunnan Baiyao to implement its diversification strategy is its core competitiveness in the "Holy Medicine of Traumatology" Baiyao series products. Only by investing sufficient resources in the main business and building a solid business foundation can we provide guarantees for the creation of corporate profits and gain sufficient market recognition. Nowadays, the industries that Yunnan Baiyao entered is diverse and very rich. It is worth noting that the development of its core business should not be ignored, as it is overshadowed by the dazzling diversification of business.

4.2 Adjusting Business Structure to Strengthen Internal Integration

When adopting diversification strategy, Yunnan Baiyao should make reasonable adjustments to its business structure, optimize the optimal allocation of resources, and enhance the synergy effect of "1+1>2". Specific adjustments can be made by reasonably dividing the business structure and processes to match certain goals, concentrating on closely related business segments, discarding unnecessary business, and specifically handling less closely related businesses. When strengthening internal integration capabilities, factors such as organizational structure, goals, resources, and culture should be taken seriously. Special attention should be paid to what is the reasonable proportion of new markets or products entered or developed in the enterprise's business, and how much resources can be allocated to them. At the same time, diversified operations have also brought great challenges to managers, achieving a linkage adjustment of "business-integration-management" to leverage the advantages of diversification strategy.

4.3 Strengthen Cash Flow Control to Reduce Financial Risks

Enterprises should pay more attention on cash flow, which is a key factor affecting the survival and development of enterprises, continuously improve the speed of capital turnover, and reasonably control the scale of cash holdings. For businesses like Yunnan Baiyao, which require mass production of commodities, cash flow management and operation are more important. Therefore, when implementing diversification, enterprises should fully consider fund management and maintain the stability of cash flow. When necessary, enterprises can establish a budget management system that relies on cash flow to prevent idle, wasted, and overly dispersed funds, in order to prevent potential financial risks. As the company's control over cash flow is in place, the risk of entering new industries and markets will not be so great.

4.4 Improvement towards Refocusing Strategy or Integration Strategy

The refocusing strategy is a development strategy that adjusts diversification strategies, requires enterprises to concentrate resources, focus on cultivating core competitiveness, and vigorously develop core businesses. The development of Yunnan Baiyao to a certain extent will lead to conflicts between business resource allocation and core capability development. Improving it into a refocusing

strategy does not mean simple specialization, but emphasizes the key position of the core business on the basis of implementing diversification.

As for the integration strategy, it is an organic combination of refocusing strategy and diversification strategy. It requires, first, shaping core business and expanding core competitive advantages. Secondly, diversify investment in a planned manner, rather than diversified operations. If Yunnan Baiyao can adopt this integration strategy, it means that it cannot be limited to a specific industry when strengthening its core capabilities, and diversified investment must rely on its core business. Therefore, Yunnan Baiyao can try to organically adjust its strategic execution by combining its business structure.

5. Summary

The strategy of an enterprise is not fixed after formulation, and it should be adjusted in a timely manner at each development stage to promote the creation of enterprise value and the enhancement of enterprise status. The development of Yunnan Baiyao has entered a mature stage, and it is not reasonable to continue to expand aggressively at this time. It is necessary to adjust the business composition and intensify processing to achieve diversification while not losing core priorities. With a general direction, specific measures such as vigorously developing core competitive main businesses, strengthening internal integration and cash flow control, approaching refocusing or integration strategies, or enhancing organizational knowledge innovation, improving corporate governance structure, and building strategic alliances can be gradually implemented to promote the steady improvement of Yunnan Baiyao and maintain competitive advantages in the industry.

The same applies to other similar enterprises that implement diversification strategies. We need to consider whether the internal and external environment for implementing diversification strategies is appropriate, and consider about every factor such as internal resource allocation, financial risk warning, competitor threats, and external policy impact. After making decisions, continuously follow up and dynamically adjust to ensure that the company's strategy aligns with the company's goals and vision.

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