

# Intra-Industry Diversification and Firm Efficiency: A Study of the U.S. Insurance Industry

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## **Abstract**

This study contributes to our understanding of the consequences of corporate diversification on firm efficiency by examining one case of intra-industry product diversification. Specifically, the study uses a sample of public and private firms that operate in the U.S. property-liability and life insurance markets. Using a version of Varian's Weak Axiom of Profit Maximization to measure firm efficiency, I compare relative performance of multi-product insurers to the performance of specialized insurers. A cross-sectional analysis of the effects of diversification across the property-liability and life insurance segments, as well as the extent of product diversification within each segment, on firm efficiency is performed. The findings of the study provide strong support for the agency-cost explanation of firms' decisions to diversify. I find that insurers that provide both property-liability and life insurance tend to be less efficient than specialized insurers. The degree of product diversification within each of the two insurance segments also negatively impacts insurer efficiency.

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