MANAGEMENT SCIENCE
Vol. 31, No. 4, April 1985
Printed in U.S.A.

Note*

THE CAPITAL ASSET PRICING MODEL AND STRATEGIC PLANNING†

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We make two clarifying comments on a recent paper by Naylor and Tapon (1982). The conclusions of their paper are significantly affected by this.

The sole purpose of this note is to make two clarifying comments on a recent paper by Naylor and Tapon (NT) (1982).

1. In Naylor and Tapon (1982), it is recommended that firms should seek low covariances between the returns of different divisions (pp. 1169, 1170). According to the capital asset pricing model (CAPM), this is irrelevant. The value of a conglomerate is the sum of the values of the individual divisions and these are again only dependent on their rates of return and systematic risks, plus market factors.

2. NT further suggest that firms should buy or sell divisions based solely on their risk/return properties (pp. 1169, 1170). According to CAPM, such businesses will on the average be valued accurately by the market, such that our firm gains nothing in the trade. Instead, the stockholders can diversify individually. Firms can only do better than stockholders if there are operating synergies between the divisions such that returns or systematic risks change.

* All Notes are refereed.
† Accepted by Ambar G. Rao; received November 7, 1983.

Reference

NAYLOR, T. H. AND F. TAPON, "The Capital Asset Pricing Model: An Evaluation of Its Potential as a Strategic Planning Tool," *Management Sci.*, 28 (1982), 1166–1173.

MANAGEMENT SCIENCE
Vol. 31, No. 4, April 1985
Printed in U.S.A.

THE CAPITAL ASSET PRICING MODEL AND STRATEGIC PLANNING: RESPONSE TO WERNERFELT*

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Wernerfelt (1983) in commenting upon our paper (1982) argues that the value of a firm on the stock market is unaffected by diversification into many different product lines. This follows from the fact that at an efficient capital market equilibrium, investors have already exploited all opportunities to combine firms into portfolios and

*Accepted by Ambar G. Rao; received February 1984.

0025-1909/85/3104/0510$01.25