
The effect of corporate divestments on shareholder wealth: The South African experience

1. INTRODUCTION

A general observation of broad business strategy patterns indicates that the conglomerate diversification that began in the 1960s underwent a change in the 1980s. Companies began to re-evaluate the costs and benefits of their diversified status. This trend is particularly noticeable in the United States where many companies made a new commitment to reduce their operations to concentrate on core business areas (Steiner, 1997). Managers are now advised to undertake a careful analysis of the far-flung enterprises that resulted from past diversification strategies. This marks a change from the steady increase in diversification since the 1960s and from the theoretical justifications for diversifications that have been advanced, including (1) managerial economies of scale, (2) economies of scope in production and marketing, and (3) financial synergies such as earnings smoothing and the efficiencies that arise from an internal capital market.

Now where there are doubts about the benefits that flow from diversification, in their public statements, managers are apt to announce that they want to concentrate on a core business. They are likely to rationalize their growth strategies, initiate divestitures and restructuring, all reflecting a strategy of specialization. The new emphasis on specialization is consistent with Jensen (1986) who argues that corporate diversification programmes exemplify the theory that managers of firms with unused borrowing power and large cash flows are more likely to undertake low-benefit or even value-destroying investments. Similarly, Meyer, Milgrom, and Roberts (1992) argue that failing businesses can have easy access to cross-subsidies when they are part of a diversified firm.

A corporate divestiture can take one of two forms: spin-off or sell-off. In a spin-off, the assets divested forms a new independent firm with the shareholders of divesting company receiving shares in the new company. A sell-off occurs when a firm sells a part of its assets to another firm. The buying firm does not purchase the whole of the selling firm, only a part of the seller's assets or a few divisions or specific business units. Firms pursue operating, strategic or funding objectives when deciding to divest assets. Divestitures in the form of sell-offs have received very little attention in the literature, compared to corporate

mergers though in both events a transfer of the ownership and control of corporate assets occurs. In South Africa, the popularity of sell-offs is growing rapidly as part of the widely accepted restructuring of the corporate landscape. Kantor (2001) has shown that the change to a democratic dispensation in South Africa and the removal of past sanctions have encouraged the process of highly diversified companies becoming more focused by selling-off divisions that are not part of their core competency.

To date, there has been no empirical study related to divestitures in the form of sell-offs in South Africa. There is no evidence of the possible sources for the wealth effects that may be associated with a sell-off transaction. To rectify this deficiency, this study investigates sell-offs undertaken by companies listed on the JSE Securities Exchange (JSE).

Elsewhere as corporate reduction of wide diversification has increased in recent years, so too has the number of studies examining the valuation consequences of sell-offs. These studies generally find evidence that public announcements of voluntary sell-offs are associated with significantly positive abnormal returns to divesting firm's shareholders. These results lead to the overall conclusion that voluntary sell-offs increase the wealth of divesting firm shareholders.

Generally, existing studies concentrate on price movements around the date of the first public announcement of the impending divestiture. While the divestiture announcements convey information to the financial markets, it may not convey all relevant information and may actually create uncertainty. Hearth and Zaima (1986) have shown that the uncertainty could come from three sources. First, it is possible that the divestiture could be called off; second, the terms of the divestiture might change between the announcement and the resolution dates; and third, there may not be sufficient evidence that the economic benefits of the divestiture will reach fruition until after it is completed. Therefore, by not explicitly examining price movements in the divesting firm's shares during the entire divestiture process, it is possible that existing studies may have under- or over-estimated the market's reaction to divestitures. To investigate these issues this paper examines the share price movements associated with corporate divestitures from 120 days prior to 120 days following the announcement date.

This paper thus has two objectives. The first is to evaluate the wealth effects of both the selling and buying company shareholders arising from 58 sell-offs

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by JSE listed companies during the period between 1995 and 2001. The second is to examine, using cross sectional analysis, the sources of these wealth effects for the shareholders of the selling company. We find that both sellers and buyers earn significant positive excess returns around the sell-off announcements. We also find that the source of this wealth effect to selling company shareholders is the disposal of non-core assets to improve overall company performance and focusing on fewer business segments.

2. REVIEW OF LITERATURE

The two major issues examined in the literature on sell-offs are the consequences of sell-offs for shareholder wealth and the motivation behind sell-offs. Alexander, Benson, and Kampmeyer (1984), Jain (1985), and Hite, Owers, and Rogers (1987) report positive cumulative abnormal returns for both acquiring and selling firm shareholders. Alexander *et al.* and Jain find that sell-offs convey favourable information about the investment decision, which results in share price gains on the announcement date. Hirschey and Zaima (1989) find larger wealth effects for sell-offs by firms with higher insider ownership.

Hite and Vetsuypens (1989) explore the wealth effects surrounding management buyouts of divisions. This transaction, relative to a third-party sell-off, contains the possibility of managerial self-dealing at the expense of the shareholders of the parent firm. They report positive abnormal returns to shareholders during the two-day period surrounding the buyout announcement. For this reason, they conclude that the transaction is similar to a third-party sell-off. Additionally, they find a positive relation between managerial equity ownership and two-day prediction errors around the announcements of these buyouts.

The literature identifies several motives for sell-offs. They may be motivated by the desire to generate cash to reduce current or non-current debt, and thereby reduce the firm's debt to equity ratio. Lang, Poulsen, and Stulz (1995) provide evidence supporting this motive. Linn and Rozeff (1989), however, argue that this would be an expensive method compared with, for example, an equity issue. They contend that this explanation confuses the results of the sale with its cause. The real cause may be that the seller can obtain a "good" price for the assets.

A second motive for the sell-off may be that the division has poor profitability. Yet, because profitability could be improved by altering the division's marketing, production, and/or pricing, it is not obvious that an unprofitable division will necessarily be sold off. Ravenscraft and Scherer (1987) provide evidence of the importance of profitability. They follow acquisitions in the 1960s and identify which of these assets are eventually sold off during 1978 to 1981. Using regression analysis, they found both overall

performance and segment performance measures to be significantly negatively related to the sell-off decision.

A third motive for a sell-off may be that the assets are more valuable to another organization. In this case, even after optimizing production and pricing, the asset may be sold. For this to be true, greater synergies must exist for the purchasing organization, which could then be willing to bid an amount that exceeds the assets' value to the existing firm. One approach to studying the synergy argument is to use event study methodology. Hite, Owers, and Rogers (1987) investigate the sources of sell-off wealth effects and find gains generated at the announcement are lost when the transaction is unsuccessful. This supports the synergy or efficiency hypothesis over an information hypothesis. Kim and Schatzberg (1987) find, on average, total liquidations generate larger excess returns than partial sell-offs or mergers. This is consistent with moving individual assets to their most productive buyer.

Lang, Poulsen, and Stulz (1995) question the synergy argument. They find a significantly positive reaction to a sell-off when the proceeds are targeted for repaying debt, but abnormal returns are not significantly different from zero when the proceeds are retained in the firm. They conclude that the results support Jensen's free cash flow argument and cast doubt on the operating efficiency view of asset sales since the efficiency argument would predict a positive share price reaction regardless of how the proceeds are used.

The profitability, debt, and synergy arguments are appealing, but they ignore the possibility that the process may be masked by the private objectives of decision makers. Lovejoy (1971) contends the sell-off decision is often viewed by management as an admission of defeat implying that the assets could not be operated in the most efficient manner. The decision makers may have objectives inconsistent with the pure maximization of the firm's value. Therefore, it would seem that the sell-off decision may sometimes be driven by other motives. Coffee (1988) discusses how takeover threats provide stimulus for management to restructure the firm efficiently. Dann and DeAngelo (1988) look at sell-offs as a way to thwart a possible takeover by selling a key division of their firm in which a hostile party was particularly interested. They find that these types of sales generate negative, but insignificant wealth effects.

The level of firm diversification, as noted earlier, may be a significant factor influencing the sell-off decision. During the 1980s firms felt increasing pressure to refocus their operations, possibly from an increased motivation to maximize firm value due to the more active market for corporate control. Investment literature has documented the well known

phenomenon of diversified firms trading at a discount relative to stand-alone firms (Servaes, 1996). For instance, Berger and Ofek (1996: 1175) find that during 1986-1991, the share price of an average diversified firm traded at a discount of about 15% of the value its lines of business would have had if operated as stand-alone businesses. This finding may be interpreted as evidence that diversification destroys firm value.

A commonly held view is that inefficient investment policies of diversified firms are to blame for the diversification discount. Lamont and Polk (2002) find that divisional resources do not appear to be directed to segments with the most profitable investment opportunities. Dittmar and Shivdasani (2003) investigated a sample of diversified firms that altered their organizational structure by divesting one or more business segments. These firms experience a reduction in the diversification discount after the divestiture. They conclude that asset sales result in a corporate focus, which lead to an improvement in the efficiency of the remaining divisions.

Berger and Ofek (1995) find that over-investment in poorly performing segments contribute to the value loss from diversification. They show that such managerial decisions are reversible, and selling off divisions of a diversified firm to buyers who operate them as stand-alone focused businesses have generally resulted in improved performance. Doukas and Kan (2004) provide empirical evidence showing that conglomerate firms acquiring unrelated businesses experience larger cash flow decreases and valuation discounts than do bidders who buy related firms. Overall, their results suggest that a lack of investment focus result in post-acquisition cash flow declines which in turn produces the diversification discount. John and Ofek (1995) provide evidence that increase in focus is value enhancing and is a major factor in explaining seller gains from asset sales.

A final factor may be the level of management ownership. Jensen and Meckling (1976) and Stulz (1988) investigate the relationship between managerial ownership and the sell-off decision. Jensen and Meckling argue that a higher level of management ownership results in an alignment effect such that firm value increases. Applied to the sell-off decision, the implication is that sell-off rules more closely follow a value-maximizing objective as managerial ownership increases. Stulz makes arguments for the market for corporate control. He contends that at sufficiently high levels of managerial ownership firm value decreases since managers can protect themselves from the threat of a take-over through entrenchment. Applied to the sell-off decision, the sell-off rule may be dominated by managerial objectives as managers entrench themselves at higher levels of ownership.

Conversely, management decisions that support a diversified status may arise from a desire to control the level of risk managers assume. Managers commit to the firm both human and financial capital through equity purchases. These managerial investments leave the managers with an un-diversified portfolio. As a result, they may attempt to achieve diversification at the firm level. Consequently, as their equity participation increases they may increasingly resist divestments and prefer diversification. Treynor and Black (1976) argue in support of this hypothesis, and Amihud and Lev (1981) find empirical results consistent with this hypothesis. Even if the manager's equity participation does not protect management from the market for corporate control, allowing for perquisite consumption by managers in the form of firm-diversifying assets may provide for this protection or entrenchment and perpetuate the firm-diversifying agenda. Shleifer and Vishny (1989) argue that managers may entrench themselves by selecting "manager-specific" assets for which the managers are uniquely capable of operating and that are, therefore, uniquely valued by the firm and its shareholders.

The share market reaction to corporate divestiture announcements have been dominated by researchers in the US. Despite a high level of divestiture activity in the UK, the topic is under researched. Afshar, Taffler and Sudarsanam (1992); Lasfer, Sudarsanam and Taffler (1998), and Gadad and Thomas (2005) have investigated sell-offs in the UK. They find that sell-off announcements result in a positive and significant gain in shareholder wealth of approximately 1%. These results confirm US research findings that sell-off announcements are generally regarded as good news resulting in a short-term gain in shareholder wealth.

In South Africa, market reaction to voluntary sell-offs is a relatively little researched subject. There are historical antecedents for this. A key feature of the South African corporate structure is the propensity for absolute control, which is reflected by numerous pyramid companies, cross holdings, low voting shares and excessive amounts of divisions that lack a fit with core activities. The reason for the excessive amounts of divisions is largely historic. The limited size of the domestic market forced many companies to stray away from their core activities into diversifications that lacked any business logic (Gerson, 1992).

Castle and Kantor (2000) similarly note that the JSE has long being dominated by large groups of holding companies. These holding companies have held controlling shares in other companies operating in diverse sectors of the economy. This state of affairs was understandable given the limited opportunities to diversify internationally because of the strict exchange controls prevailing in the country.

The changed political dispensation in South Africa has resulted in local companies re-joining the international

business community. Several large South African companies have obtained listing on overseas stock exchanges. The holding of unfocused divisions and the lack of specialization by listed companies are disapproved overseas (Niehaus, 1998), and this provided the initial incentive for local diversified companies to sell-off assets unrelated to their core activities.

The overseas trend of unlocking shareholder value by engaging in sell-offs has also had an influence on local companies. During the past decade there has been a significant amount of sell-offs by diversified companies in South Africa. This study seeks to determine if sell-offs by South African diversified companies have, in fact, created shareholder value as predicted by investment literature.

3. SAMPLE SELECTION AND RESEARCH METHODOLOGY

3.1 Sample selection

The sample consists of all voluntary sell-offs reported by companies listed on the JSE during the period 1 January 1995 to 31 December 2001. Both the divesting company selling its assets (seller) and the corresponding purchaser (buyer) had to be listed on the JSE to be included in the investigation. To be included in the final sample, a sell-off sample had to satisfy the following criteria:

1. The sell-off had to be of a voluntary nature. Forced divestitures imposed by legislative or judicial fiat are excluded.
2. The sell-off had to be a non-financial firm.
3. The buying and selling companies had to have their daily share price data available for the full 120-day estimation period and also for the observation period.
4. The divesting firm is not engaged in another divestiture or engaged in other contemporaneous corporate restructuring activities, such as mergers.
5. The price of the transaction is disclosed with the sell-off announcement.

To avoid any potential confounding influences, the sample is limited to those divestitures in which there are no other contemporaneous corporate restructuring activities. In this context, contemporaneous refers to the window starting from three years prior to the year of the divestiture and ending three years after the year of the divestiture. Divestitures that have other restructuring events in this window are excluded to prevent those other events from contaminating the performance measures used in the study. This

exclusion device increases the confidence in attributing any performance gains to the divestiture and not to other restructuring events.

A total of 58 sell-offs met the criteria and were included in the final sample for this investigation. Table 1 shows the distribution of the completed divestitures by JSE listed companies between 1995 and 2001. The divestiture firms are almost evenly distributed across the years.

Table 1: Annual distribution of completed divestitures between 1995 and 2001

Year	Number	% of final sample
1995	7	12
1996	7	12
1997	9	16
1998	7	12
1999	10	17
2000	8	14
2001	10	17
Total	58	100

The data related to the sell-off announcements were obtained from *Reuters News*, which provides selected news service stories from *Business Day* and other financial publications. This publication was used to identify news related to sell-off announcements during the period of the investigation. The announcement dates were obtained from *Business Day* and the database of JSE SENS, which commenced providing announcements from March 1998. The data required in respect of selling and buying company share prices and the JSE All Share Index were obtained from BFA McGregor and I-NET Bridge (PTY) Ltd. All financial data required to perform the OLS regression were also obtained from these sources.

3.2 Research methodology

A review of the literature reveals that sell-off announcements are not trivial events and that they are usually accompanied by changes in the wealth of shareholders. The following hypothesis will be tested:

H₁: Sell-offs have real economic value (either positive or negative) and the divestiture announcement is significant information to the financial markets. Therefore, significant movements in the share prices of the selling and buying companies should be observed around the announcement date.

Many studies that have examined the valuation consequences of a variety of announcements (e.g., earnings, dividends, mergers etc.) as well as divestiture announcements have often relied on the one factor market model. The hypothesis is tested using the event study methodology developed by Brown and Warner (1985) based on the market model.

According to this model, each security's period return can be expressed as a linear function of the contemporaneous return on the market portfolio and a firm-specific stochastic term. Assuming that expected returns on securities conform to the market model, then the daily abnormal returns for each security j on day t is calculated as follows:

$$AR_{jt} = R_{jt} - (\alpha_j + \beta_j R_{mt}) \quad \dots (1)$$

where

AR_{jt} is the abnormal return for security j on day t , R_{jt} is the actual return of security j on day t , R_{mt} is the rate of return on the market portfolio represented by the JSE All Share Index on day t , and α_j and β_j are the market model coefficients for company j .

These coefficients were estimated for each security from day $t = -480$ to $t = -360$ relative to the sell-off announcement date. The standard reference date for each security ($t = 0$) is the day on which the divestiture announcement is made. The event period comprises of the pre-announcement period and the post-announcement period. Residuals are then calculated for the pre-announcement period ($t = -120$ to $t = 0$), and the post-announcement period ($t = 1$ to $t = 120$). The abnormal return on any day should not be significantly different from zero unless investors receive new information that affects the intrinsic value of a share. Any significant abnormal returns observed can be attributed to the information content of the sell-off.

Two methods were used to calculate the beta values for companies identified as events. The first method was the standard ordinary least square (OLS) method that is normally used to derive the value of beta. The second method employed the technique developed by Dimson (1979) and refined by Cohen, Hawawini, Maier, Schwartz and Whitcomb (1983) to overcome the problem of beta underestimation caused by serial correlation. Bradfield and Barr (1989) conducted a sensitivity study on the JSE and they showed that there is a statistical significance for two lagged terms, the contemporaneous term and one leading term. The Bradfield and Barr procedure was therefore used to calculate the beta value.

The average abnormal return (AAR) is calculated for each time period in the pre and post announcement period across the entire sample. AARs are calculated as follows:

$$AAR_t = \sum_{j=1}^N AR_{jt} / N$$

where

N is the number of sell-off announcements in the sample portfolio (58).

In addition, a cumulative abnormal return (CAR) is calculated, where:

$$CAR_t = CAR_{t-1} + AAR_t \quad \text{for } t = -120 \text{ to } +120 \quad \dots (3)$$

Statistical significance of the AARs and CARs are inferred by calculating t-statistics by means of following a procedure developed by Miles and Rosenfeld (1983). If the hypothesis to be tested is correct, then significant AARs and CARs should be observed just prior to the announcement as prices adjust to new information.

Schlingemann, Stulz and Walking (2002) has presented a model that has identified three main reasons for a divestiture: (1) company underperformance which forces managers to divest non-core assets to improve profitability- the underperformance explanation, (2) reducing the degree of diversification to make the firm more efficient- the focus explanation and (3) reducing the debt level- the financing explanation. In addition, Klein (1986) reports that the relative size of the sell-off has a positive relation to announcement day returns associated with corporate divestitures. Therefore, these four variables will be used to evaluate their effect on the wealth of shareholders of the divesting firm.

A cross sectional analysis is performed to identify the possible sources of the shareholders' wealth gains using an OLS regression. In an efficient capital market the wealth gains expected from a sell-off should be reflected in the share price of the selling company in the period immediately preceding the sell-off announcement. The CAR for the period $t = -5$ to 0 is used to capture the wealth gains to the sellers during the announcement period. The dependent variable is the CAR and four explanatory variables have been identified as being representative of the possible reasons for a divestiture. The regression equation is:

$$CAR_j = \alpha + \beta_1 R\text{-SIZE} + \beta_2 U\text{-PERF} + \beta_3 \text{FOCUS} + \beta_4 \text{FIN} + \epsilon_j \quad \dots (4)$$

where

CAR is the cumulative abnormal return for the window $t = -5$ to 0 ;

R-SIZE is the ratio of the reported value of the divestiture to the total market value of the firm in question;

U-PERF is a dummy variable taking a value of 1 if the seller reduced its operating profit margin in the year of the divestiture compared to the year before the divestiture, otherwise a value of 0;

FOCUS is a dummy variable taking a value of 1 if the seller firm focused its operations in fewer business segments in the year of the divestiture compared to the year before the divestiture, otherwise a value of 0;

FIN is a dummy variable taking a value of 1 if the seller firm reduced its debt capital in the year of the divestiture compared to the year before the divestiture, otherwise a value of 0;

ϵ_j is the error term with zero mean and constant variance.

4. EMPIRICAL RESULTS

Panel A of Table 2 presents the excess returns earned by the sellers for day -120 to day +120, where day

zero is the public announcement of the sell-off. It is observed that for day -1, -2 and -3, sellers earn significant positive excess returns. The total excess returns for these three days amount to 1,37%. The excess returns are generally negative prior to sell-off announcement and it appears that the sell-off announcement is not anticipated more than four days before day zero. The cross sectional frequency distribution also indicates that the percentage of positive excess returns is significantly larger than expected by chance. These results indicate that sell-off announcements are associated with statistically significant positive excess returns to the sellers. These findings are consistent with the results found in the UK by Afshar, Taffler and Sundarsanam (1992) and in the US by Maksimovic and Phillips (2001).

Table 2: Sellers – examination of excess returns around sell-off announcements

Panel A: Average abnormal returns (AAR) and cumulative average returns (CAR) around sell-off announcements

Day	AAR(%)	t-statistic	CAR(%)	Day	AAR(%)	t-statistic	CAR(%)
-120	0,0082	0,48	0,0082	1	0,1142	0,83	-1,3640
-110	-0,0091	0,52	0,0020	2	-0,2317	-1,51	-1,5957
-100	-0,1325	-0,98	-0,2277	3	-0,1825	-1,39	-1,7782
-90	-0,2237	-1,36	-0,6451	4	0,1137	0,79	-1,6645
-80	-0,1496	-1,12	-0,9863	5	-0,1329	1,09	-1,7974
-70	-0,3732	-2,40**	-1,4972	6	0,0511	0,78	-1,7463
-60	0,1917	1,45	-1,5018	7	-0,0000	-0,04	-1,7463
-50	0,1305	1,02	-1,4163	8	0,0073	0,43	-1,7390
-40	-0,1873	-1,33	-1,8784	9	0,1651	1,14	-1,5739
-30	-0,2241	-1,49	-2,3547	10	-0,1519	-1,20	-1,7258
-20	-0,2175	-1,37	-2,7325	20	-0,0932	-0,85	-2,1547
-10	0,0520	0,78	-2,9153	30	-0,1243	-0,97	-2,6792
-9	0,2317	1,43	-2,6836	40	0,0197	0,20	-2,7965
-8	-0,1985	-1,36	-2,8821	50	-0,2126	-1,32	-3,1219
-7	-0,1692	-1,18	-3,0513	60	0,0937	0,85	-3,2173
-6	-0,1725	-1,21	-3,2238	70	-0,0624	-0,80	-3,4493
-5	-0,0094	-0,53	-3,2332	80	0,2013	1,24	-3,3075
-4	0,1436	1,09	-3,0896	90	-0,2752	-1,84*	-3,5954
-3	0,2610	1,79*	-2,8286	100	0,0718	0,47	-3,6276
-2	0,3725	2,30**	-2,4561	110	0,1953	1,43	-3,7541
-1	0,7326	3,37***	-1,7235	120	-0,0935	-0,87	-3,9357
0	0,2453	1,61	-1,4782				

Table 2 continued

Panel B: Time series t-statistics for various intervals

Interval(days)	CAR(%)	t-statistic	Interval(days)	CAR(%)	t-statistic
-360 to -241	-3,1857	-1,59	-60 to -11	-1,4135	-0,83
-360 to -121	-6,7238	-2,73***	-10 to -6	-0,2659	-0,45
-360 to -61	-8,2225	-2,98***	-5 to 0	1,7456	2,86***
-360 to -11	-9,6192	-3,40***	1 to 5	-0,3192	-0,34
-240 to -121	-3,5381	-2,26**	6 to 10	-0,0613	-0,27
-240 to -61	-5,0769	-2,49**	11 to 60	-1,4915	-1,43
-240 to -11	-6,5036	-2,84***	61 to 120	-0,7184	-0,68
-120 to -61	-1,5100	-0,79	11 to 120	-2,2099	-1,53
-120 to -11	-2,9235	-1,82*			

* Significant at the 10% level

** Significant at the 5% level

*** Significant at the 1% level

Panel B of Table 2 presents results for a number of sub-periods. Of particular importance is the period immediately preceding the sell-off announcement (day -5 to day 0). A statistically significant excess return of 1,75% is observed during this period. In panel B of Table 2 the examination of excess returns is extended backwards to 360 days prior the sell-off announcement. The results reveal that sellers, on average, performed poorly in the pre-sell-off period. These firms on average, earned -9,62% for day -360 to day -11 (statistically significant at 1% level). The t-statistics for the most of the pre-announcement period confirm that the decline in share prices is statistically significant. The results also suggest that the sell-off announcement is preceded by the release of negative information about the firm.

The CARs after the announcement date resume their negative path but they are not statistically significant. The positive market reaction to the sell-off announcement is restricted to the period immediately preceding the event day. This evidence is consistent with the hypothesis that the market is efficient in the semi-strong form with respect to sell-off events.

Bhana (2004) investigated the performance of parent companies engaged in spin-offs on the JSE during the 1988-99 period. The performance of the selling companies engaged in sell-offs can be compared with the performance of spin-offs reported by Bhana and highlights an interesting aspect. In contrast to the negative excess returns earned by the selling firms in the pre-event period (reported here), Bhana found that firms spinning off their subsidiaries experienced significantly positive excess returns for a period of two years prior to their spin-off announcements. This suggests that, although both spin-offs and sell-offs are associated with similar contemporaneous positive share price reactions, the actions taken by management depend on the firms' performance prior to these decisions. This seems logical since firms performing poorly are more likely to face liquidity problems and therefore engage in sell-offs to overcome these problems. Spin-offs, on the other hand do not generate cash for the parent company and are, therefore, more likely to be undertaken by firms that have been performing well. This observation seems to indicate that a sell-off is a kind of action taken by the managers of poorly performing companies to improve the welfare of their shareholders.

Panel A of Table 3 presents the average excess returns earned by buyers involved in sell-off transactions. On day -1, the buyers earn a statistically significant return of 0,52%. The CARs are positive during the entire period and total 2,98% during the period covering day -120 to day + 120. Panel B of Table 3 presents the number of sub-periods during the study period. The only statistically

significant return is for days -5 to day 0 totalling 1,16%. Further, the behaviour of the share prices after the announcement date is essentially random suggesting market efficiency. In sum, sell-off announcements are also good news to the buyers, although to a lesser extent compared to the sellers.

Table 4 presents the coefficient estimates for the regression model presented in equation (4). This model identifies which of the four explanatory variables are responsible for the cumulative abnormal returns attained by selling companies in the period $t = -5$ to 0. The results indicate that a significant proportion of the market reaction to sell-offs is explained by the explanatory variables ($R^2 = 0,31$).

The coefficient of the underperformance variable (U-PERF) is positive and statistically significant at the 0,01 level. This suggests that underperformance is an important explanatory variable indicating that the desire to improve the overall performance of the company is an important consideration in the sell-off decision. The sell-off decision is a clear signal that management provide to the market of its intention to address the underperformance issue. This is consistent with the evidence provided by Steiner (1997). They investigated the motives for the sale of divisions by highly diversified companies. They showed that there was a significant correlation between divisions sold and poor overall company performance.

The coefficient of the FOCUS variable is statistically significant at the 0,05 level. Therefore, focus is also an important explanatory variable indicating that focusing on fewer business segments is an important consideration in the sell-off decision. It suggests that one possible motivation for a sell-off is to improve the focus of the seller's operations, thus improving the performance of the sellers remaining assets. The improvement in performance may be due to various reasons such as elimination of negative synergies with the divested asset or increased efficiency arising from better allocation of management time and other resources in a more focused firm.

This result supports the evidence provided by John and Ofek (1995), which shows that highly diversified companies have a propensity to sell off those divisions that do not have a strategic fit and have a detrimental effect on overall performance.

Other factors such as the size of the divested unit and the debt level of the divesting company are not significant in explaining the possible sources of shareholders' gains from divestitures undertaken by companies listed on the JSE.

Table 3: Buyers – examination of excess returns around sell-off announcements
Panel A : Average abnormal returns (AAR) and cumulative average returns (CAR) around sell-off announcements

Day	AAR(%)	t-statistic	CAR(%)	Day	AAR(%)	t-statistic	CAR(%)
-120	0,2125	1,32	0,2125	1	0,0936	0,82	2,6385
-110	0,0913	0,85	0,2642	2	-0,0934	-0,79	2,5451
-100	-0,0726	-0,82	0,2735	3	0,0863	0,84	2,6314
-90	0,0824	0,84	0,3947	4	0,0917	0,86	2,7231
-80	-0,0127	-0,71	0,4168	5	0,1144	0,96	2,8375
-70	0,0232	0,73	0,5169	6	-0,1056	-0,94	2,7319
-60	0,0018	0,69	0,5834	7	-0,3720	-2,28**	2,3599
-50	0,1937	1,45	0,9275	8	0,0060	0,37	2,3659
-40	-0,0036	-0,14	0,9983	9	-0,1997	-1,57	2,1662
-30	0,2243	1,50	1,4167	10	0,1036	0,74	2,2698
-20	-0,0417	-0,75	1,5320	20	-0,0056	-0,35	2,2754
-10	0,2352	1,43	1,9146	30	0,0000	0,03	2,2754
-9	-0,1525	-1,27	1,7621	40	0,1245	1,17	2,4175
-8	-0,0892	-0,84	1,6729	50	-0,1551	-1,27	2,3816
-7	0,0081	0,48	1,6810	60	0,3004	2,14**	2,5925
-6	-0,2912	-1,92*	1,3898	70	-0,1217	-1,15	2,4373
-5	0,1056	0,96	1,4954	80	0,3046	2,23**	2,6239
-4	0,1340	1,17	1,6294	90	0,2023	1,62	2,7510
-3	0,0997	0,92	1,7291	100	0,3011	2,27**	2,9152
-2	0,1394	1,24	1,8645	110	-0,1994	-1,56	2,8917
-1	0,5183	2,71***	2,3828	120	0,0092	0,50	2,9833
0	0,1621	1,20	2,5449				

Table 3 continued
Panel B: Time series t-statistics for various intervals

Interval(days)	CAR(%)	t-statistic
-120 to -61	0,3699	0,53
-120 to -11	1,7011	0,58
-60 to -11	1,3312	0,66
-10 to -6	-0,2896	-0,72
-5 to 0	1,1551	2,18**
1 to 5	0,2926	0,61
6 to 10	-0,5677	-1,79*
11 to 60	0,3227	0,65
61 to 120	0,3908	0,72
11 to 120	0,7135	0,63

* Significant at 10% level

** Significant at 5% level

*** Significant at 1% level

Table 4: Cross sectional analysis of the shareholders' wealth gains from sell-offs.

Variables	Estimated Coefficients				t-statistics
	β_1	β_2	β_3	β_4	
A	-0,09 (-0,14)	5,92 (1,98)*	5,18 (1,83)	3,41 (1,30)	-0,42 (-0,43)
R-SIZE	0,33 (1,21)				0,03 (0,49)
U-PERF		12,36 (3,17)***			2,93 (3,26)***
FOCUS			10,62 (2,34)**		2,41 (2,34)**
FIN				3,19 (1,20)	1,35 (1,06)
R ²	0,31	0,31	0,31	0,31	0,31

Notes :

t-statistics are adjusted for heteroscedasticity (White's correction)

* Significant at 10% level

** Significant at 5% level

*** Significant at 1% level

4.1 Discussion of the results

Sellers appear to be poor performers prior to the sell-off activities and this poor performance continues after the sell-off announcement has been made. The sell-off can be seen as action taken by the poorly performing firms to improve the welfare of their shareholders by signalling their intention to address underperformance and the need for more focus. It would appear that shareholders approve such action and the selling firm experiences an excess return in the period immediately preceding the sell-off announcement (day -5 to day 0). The results of the cross-sectional analysis reveal that poor company performance and focusing on fewer business segments are important explanatory variables for the excess returns attained by selling companies in the period $t = -5$ to 0. Therefore, selling companies should be mindful of the need to improve their performance and to become focused on their core competencies by engaging in sell-off transactions.

Buyers appear to be good performers prior to the sell-off and their superior performance continues after the sell-off announcement has been made. The excess returns earned by the buyers are smaller than those earned by sellers. This could be attributed to the fact that sellers would already derive the gains from the sell-off at the time of the sale, whereas the buyers will only benefit fully when the acquired assets become operational. Furthermore, buyers are already superior performers on the stock exchange and the sell-off announcement is not expected to generate the same level of excitement that the under-performing sellers would enjoy from the release of the favourable information.

The results show that both the buyers and sellers gain from corporate divestitures. The results support the hypothesis tested which states that significant share price movements for buyers and sellers are expected around the announcement date. The results confirm that corporate divestitures are not trivial events but produce real economic value to both buyers and sellers. Corporate divestments provide an opportunity to alter the ownership and control of corporate resources and results in the transfer of assets from poor performing companies to those providing higher value to the assets acquired. A persuasive case can be made for local companies to rationalize their activities and place greater emphasis on specialization of asset holdings.

The findings of this investigation are of particular importance to South African diversified companies that are following the international trend of restructuring their assets to become focused to their core competencies. Kantor (2001) has shown that South African diversified companies involved in restructuring have a preference to unbundling their divisions and subsidiaries despite this form of restructuring not creating shareholder value because of the cosmetic nature of the restructurings. These companies should take note of the finding of this investigation that corporate divestments provide real

economic value and on average provide a positive effect on the wealth of buying and selling company shareholders. It is suggested that South African companies should give serious consideration to sell-off transactions when making asset-restructuring decisions.

A major benefit from sell-offs is the accompanying increase in focus, which is highly rated by investors. There is an increasing trend in overseas countries for companies to increase their focus through the sale of non-core assets thereby improving the performance of the remaining assets (Kaplan and Weisbach, 1992). This trend does not appear to be meaningfully emulated by diversified companies in South Africa. Barr, Gerson and Kantor (1995) have shown that South African diversified companies have a fetish for control over assets and, until recently, were relatively immune from the sanctions of the marketplace to be disciplined for their underperformance and lack of focus. The opening up of the South African economy has created a more active market for corporate control and this competition poses a major challenge for diversified companies to refocus their operations and create shareholder value.

The need to refocus and create shareholder value was dramatically illustrated by the October 2005 announcement by Anglo American (AA) to rationalize and simplify its asset structure and focus on its core mining activities. The extensive range of AA's highly diversified investments were acquired during the period of isolation accompanying the apartheid era. Following the democratic dispensation in the country, AA listed on the London Stock Exchange in 1998 and it began a process of restructuring to create a company with a core strategy around mining activities. However, at the time of the October 2005 announcement AA was still an unfocused company having over 150 subsidiaries and associated companies in diverse activities such as steel manufacturing, paper and packaging, aluminium, sugar and building materials. AA was still penalized by the "diversification discount" and the market rating of the share price lagged those of its peer competitors such as BHP Billiton and Rio Tinto (Smith, 2005:1). The market approved the AA announcement which stated that it planned to divest its non-core manufacturing assets and focus on mining operations, and the share price increased by close to 5% on the day following the announcement.

The findings of this investigation support the large body of overseas evidence, which suggests that, in general, excessive diversification has not been beneficial for shareholders. The best course of action for South African companies is to follow the Anglo American example of reducing diversification and focus on core business. The sell-off of non-core assets will unlock shareholder value by being rewarded by the share market that is increasingly approving higher returns and efficiency over company size. In line with overseas evidence sell-offs will produce more focused firms and should lead to the reduction in the prevailing

diversification discount applicable to highly diversified companies. Managers of diversified companies impose costs on their shareholders because of the diversification penalty and these costs can be partly removed by engaging in sell-offs that increases company focus.

The *Broad-Based BEE Act No. 53 of 2003* (BEE Act) makes the empowerment of previously disadvantaged groups a social and moral imperative for South African companies. In November 2005, the Department of Trade and Industry (dti) released *The Codes Of Good Practice On Broad Based Black Economic Empowerment*. Code 101 of this publication provides that in addition to achieving ownership through the acquisition of equity shareholding by previously disadvantaged groups, an enterprise can also achieve BEE ownership recognition through the disposal of businesses and assets. This presents an opportunity for local diversified companies to dispose their non-core assets and earn valuable points towards the process of being BEE compliant. In fact, Anglo American facilitated the first BEE transaction in the mining industry in 1996 by the sale of JCI to African Mining Group and Johnnic to the National Empowerment Consortium (Mathews, 2005: 19).

5. Summary and conclusions

This study is an empirical investigation of the effects of voluntary sell-offs on the shareholder wealth of both selling and buying firms. Unlike previous studies, which concentrate mainly on the announcement period, this study investigates the price movements covering the 120-day prior and 120-day following the sell-off announcement. Fifty-eight corporate divestments by companies listed on the JSE during the period 1995 to 2001 are examined. The results show that the sell-off announcements have a positive effect on the shareholder wealth of both the sellers and buyers. However, the performance characteristics of buyers and sellers are vastly different.

For the sellers, the sell-off announcements are preceded by a period of negative excess returns, a significant -9,62% from day -360 to day -11. A highly significant excess return of 1,75% is earned from day -5 to day 0. These results suggest that the sell-off announcement is preceded by the release of negative information about the firm. The excess returns resume their negative path after the announcement date but they are not statistically significant.

For buyers, the sell-off announcements are preceded by a period of positive but not significant excess returns of 1,70% from day -120 to day -11. A highly significant excess return of 1,16% is earned from day -5 to day 0. The excess returns generally resume their positive path after the announcement date but they are not statistically significant.

The vastly different financial performance between the selling and the buying companies suggest that the

market for corporate control transfers resources from poorly performing and unfocused companies to those companies capable of providing higher value to the assets acquired. A comparative performance of South African companies engaged in spin-offs and sell-offs seems to indicate that a sell-off is a kind of action taken by the managers of poorly performing companies to improve the welfare of their shareholders. An overall conclusion is that sell-offs by South African companies have, indeed, created shareholder value as predicted by the investment literature. Diversified companies have an opportunity to sell-off those divisions that do not have a strategic fit and have a detrimental effect on overall performance.

The cross sectional analysis has revealed that addressing the prevailing company underperformance and focusing on fewer business segments are the only significant factors related to the increase in wealth of the selling company shareholders. This result could stem from the market's favourable expectation of the future benefits that are likely from companies focusing on their core competencies and improving the existing poor performance. It can be concluded that increasing focus on the core business is an important motivation for divestments undertaken by South African diversified companies.

Many local diversified companies are trading at a substantial discount to their share market value. The evidence of this investigation suggests that these diversified companies would be better served if they sold off assets that lack a strategic fit to other companies that could add substantial value to the assets so acquired. A more focused diversified company would unlock shareholder value and any discount to net asset value could be reduced or eliminated. Shareholders prefer the concept of "pure plays" and single-minded focus and reward companies that meet these criteria. Therefore, it is recommended that South African diversified companies should engage more actively in divesting their non-core assets through sell-offs. Sell-offs are preferable to the unbundling of assets, which has become the preferred method of restructuring by local diversified companies. Sell-off increase the wealth of both sellers and buyers of assets, whereas unbundling does not create shareholder wealth because of its cosmetic nature.

The recent amendment to the *Broad-Based BEE Act of 2003* also presents an opportunity for diversified companies contemplating to dispose their non-core assets to consider previously disadvantaged groups as possible buyers. This is an alternative to selling equity shares in the business and sell-offs could earn valuable points towards being BEE compliant.

This paper has not considered whether insider trading plays any role in influencing the shareholder wealth related to corporate divestitures. Hirschey and Zaima (1989) report that insider trading activity and ownership

structure of the firm are a useful context for evaluating corporate sell-off decisions. Their findings suggest that insider trading and ownership structure information are used by the market in the characterization of sell-off decisions as favourable or unfavourable for investors. It will be interesting for future researchers to investigate whether insider trading and ownership structure information plays any role in influencing shareholder reaction to sell-offs by South African companies.

This study has extended the scope of the market reaction to sell-offs beyond the traditional period immediately surrounding the sell-off announcement. However, it is possible that all the uncertainty with respect to a sell-off may not be resolved until several years following its completion. Thus, this study may still not have captured the entire market reaction to sell-offs. It is suggested that follow-up studies covering a much longer period be undertaken to fully measure the valuation consequences of sell-offs by South African companies.

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