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Article

Financial and stock market variables as predictors of management buyouts

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Abstract

This paper investigates whether publicly held firms which change to private ownership through management buyouts (ex-public firms) possess characteristics prior to the change which differentiate them from firms which remain publicly owned. The financial characteristics of ex-public firms for the year immediately prior to going private were analyzed. A multivariate framework was developed to determine which attributes best distinguished firms going private via management buyouts from similar firms not going private. A discriminant function was developed using seven ratios: (1) concentration of ownership, (2) cash flow to net worth, (3) cash flow to total assets, (4) price/earnings ratio, (5) price/book value ratio, (6) book value of depreciable assets in relation to original costs, and (7) dividend yield. The model demonstrated a classification accuracy of 77.8 percent for the original sample and 81.4 percent in a hold-out sample validation. These findings imply that financial characteristics alone provide a means by which firms going private via management buyouts can be separated from others. Therefore one can argue that, regardless of the stated motive for going private, financial characteristics either are explicit decision variables or directly reflect non-financial reasons for management buyouts.

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