



Applied Economics >

Volume 36, 2004 - Issue 8

187 | 8
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Do asset sales lead to improvements in operating performance?

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Pages 865-871 | Published online: 02 Feb 2007

Cite this article <https://doi.org/10.1080/0003684042000229578>

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Abstract

The changes in operating performance associated with asset sales are investigated for a sample of UK firms. Asset sales are followed by an improvement of 11% per annum in the level of operating performance relative to the pre-sale performance level. Further, improved abnormal operating performance is found, which is measured after controlling for the performance of the industry, the pre-sale performance of the firm and the level of competition in the market for asset sales. The abnormal operating performance of the remaining assets improve by 2.4% per annum, on average, for three years after the asset sales. This study also finds that the market for asset sales is imperfectly competitive.

Acknowledgements

We would like to especially thank Jerry Coakley for comments and various helpful suggestions and Tony Arnold, Bimbola Adedeji, Richard Baker, Ephraim Clark, Jo Danbolt, Ronan Powell, Bill Rees, Richard Taffler, Andy Stark, Bob Wearing. The usual caveat applies.

Notes

¹ The total value of the transactions in the divestiture market is about £108 billion while in the merger market the total value is about £262 billion (for the period 1985–1994). Source: *Acquisitions Monthly*.

² A management buyout occurs when the incumbent management team buy all the equity shares of either a firm or a subsidiary from current shareholders. A spin-off occurs when ownership of the divested asset is transferred to a new company formed by a pro-rata distribution of equity shares in the new company to current shareholders. An equity carveout occurs when ownership of the divested assets is transferred to a new company formed by the issue of equity shares in the new company to the public.

³ The characteristics of firms that engage in asset sales and their plant level productivity changes have been examined by Maksimovic and Phillips ([2001](#)). They are unable to investigate the operating performance changes of individual firms due to the nature of their dataset.

⁴ The model used is similar in nature to that used for mergers by Healy et al. ([1992](#)).

⁵ The book value of debt is used since the debt securities of UK firms are not publicly traded. Market values of the debt securities of UK firms, therefore, cannot be directly obtained.

⁶ To test for sensitivity, the shareholders' wealth gains have also been calculated using the market model.

⁷ Median measures are computed because it is less affected by extreme observations that can skew the calculation of the mean measure.

⁸ Note that this median measure will not necessarily be that of the middle year.

⁹ For a firm with below average performance (i.e. $IAOP^{pre} < 0$), in the absence of the divestiture, $IAOP^{post}$ would further decline to values below zero, all else being equal. The interpretation of the constant term in the regression remains unaltered and as described below.

¹⁰ In the non-competitive case, $IAOP^{post}$ would not revert to zero and would be expected to persist indefinitely.

¹¹ A value less than one and greater than zero reflects an imperfectly competitive market. Further, although one can expect the competitiveness index to vary across firms it is assumed that it is the same for all firms. It is possible to estimate firm-specific values if sufficient time-series data are available for each firm. There are only three time series observations (one for each year in the pre-divestiture period) and we do not, therefore, estimate firm-specific values. In the absence of some well-specified and feasible way of allowing the index to vary across divestor firms, it seems not unreasonable to assume a common value.

¹² For example, the approach typically adopted in studies searching for improvements in operating performance following a merger is to constrain β to be equal to one (Healy et al., [1992](#) is an exception).

¹³ The Acquisitions Monthly publication defines a divestiture as a firm announcing the divestiture of either a subsidiary of the firm or a division or unit of the company (any segment of the company other than a subsidiary).

¹⁴ The outliers were identified as those observations where the pre-and post-divestiture performance measures were more than three standard deviations away from the mean.

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