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Çağlar Doğru
Ufuk University, Turkey

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Chapter 15
The Evolution of Corporate Divestment:
Towards a New Research Paradigm?

Pedro Silva
University of Aveiro, Portugal

António Carrizo Moreira
University of Aveiro, Portugal

ABSTRACT

When compared to other fields of research such as mergers and acquisitions, corporate divestment is under researched. There are at least three main reasons for this: the environment in which corporate divestment research has taken place has caused divestments to be understood as acquisition-driven rather than strategy-driven, the scope and distinct modes of divestment, and the difficulties in isolating the divestment phenomena. The objective of this chapter is to review the main theoretical approaches used in the study of divestment, to analyze their contribution to the field, and to discuss whether new approaches are needed in divestment research. Most studies of divestment are based on the concept that divestment is the outcome of poor unit performance, and the reversal of previous over-diversification and growth strategies that expanded the company size beyond optimal control. This chapter proposes four future lines of research into corporate divestment: the international business strategy, the network perspective, the stakeholders' perspective, and the institutional theory.

INTRODUCTION

In a continuously changing world, flexibility and responsiveness emerge as some of the key competitive factors for businesses. Corporate divestment is a "*firm's decision to dispose of a significant portion of its assets*" (Duhaime & Grant, 1984; p. 301). Corporate divestment is a common and growing phenomenon. Johnson (1996) found 1200 divestments worth 59.9 billion dollars in 1986 alone. Bergh & Lawless (1998) mentioned that during the 1980s and into the 1990s, almost one half of Fortune 1000 companies had engaged in divestments, acquisitions or both. More recently, Gadad, Stark, & Thomas

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(2009) observed that the scale of divestments in the United Kingdom was on average 40% of the activity in the merger market and reached levels as high as 70% in some years. Nowadays examples of corporate divestment can be found everywhere. According to UNCTAD (2016), European firms have divested from developing economies like Asia or Latin America. Caterpillar announced the shutdown of its plant on Illinois, cutting 800 jobs (Reuters, 2017). General Motors closed five of its factories in the US during 2017 (Fortune, 2017). US hard drives and data storage manufacturer Seagate closed one of its largest factories, the Suzhou China plant, in 2017, laying off 2,127 employees on what China's Ministry of Commerce classified as a "*normal business decision*" (Xinhua, 2017).

Corporate divestment is an important topic with an impact on company performance and competitive position. Dranikoff, Koller, & Schneider (2002) highlight how divestments were a keystone of General Electric strategy under the leadership of Jack Welch in the first four years of his tenure as CEO, as he divested 117 businesses accounting for 20% of General Electric's assets. Greg Summe, CEO of PerkinElmer, used divestments and acquisitions to reshape the company from a supplier with low margin services to an innovative high-tech company. A McKinsey & Company study shows that companies that actively manage their business portfolio through acquisitions and divestments deliver more value to shareholders than those that passively hold them. Dranikoff, Koller, & Schneider (2002), argue that divestment is a way to dispose of a business whilst ensuring that the remaining divisions reach their full potential and the overall company grows stronger. Thus, divestments can strengthen and rejuvenate a company and may constitute an important strategic tool for management. Nonetheless, there seems to be a bias against divestment as managers are traditionally reluctant to divest because of its association with weakness and failure (Dranikoff et al., 2002; Porter, 1976).

Regardless of its importance, corporate divestment has received scarce attention when compared to other forms of restructuring such as mergers and acquisitions (M&A) and strategic alliances (Gadad et al., 2009; Lee & Madhavan, 2010). As a result, still relatively little is known about the reasons as to why companies divest (Berry, 2013). Existing literature has examined the divestment phenomenon using a variety of theoretical approaches including the internationalization theory, imperfect market conditions and the governance issues caused by directional conflict between shareholders and managers. With the development of globalization, the traditional theories used to explain divestment have been increasingly challenged. Villalonga & Mcgahan (2005) claim that the various divestment theories, rather than being mutually exclusive, appear to be closely related and complementary.

In this chapter we review the main theories used in divestment research and their contribution to the field. Then, we develop a framework comprising the knowledge generated through the use of these approaches, discussing whether other theoretical approaches in the field are needed. Through this process, the following additional research objectives will be addressed:

- What corporate divestment is;
- How divestment research has evolved through time;
- What the main typologies of divestment are;
- What the main theories used to examine corporate divestment and their contributions to the field of research are.

The chapter is structured as follows. After this introduction, section two provides the background on the history of divestment research. Section three discusses existing typologies on divestment. Section four presents the review of the main theories used in divestment and their contributions, from which a conceptual framework is developed in section five. Section six presents the conclusions and a debate on how the theoretical approaches evolved through time and whether new paradigms in divestment research are needed.

BACKGROUND

The History of Divestment

The 1960s and 1970s were decades of continuous growth and diversification, however, the 1980s saw a strong wave of divestments for two main reasons. First, the market for corporate control became more effective, which in turn disciplined managers and decreased information advantages of diversified companies' internal capital markets (Jensen, 1993). Second, capital markets began to adopt a critical perspective towards diversified corporations and conglomerate mergers. Strong international competition increased the pressure on corporations to manage their business scope and divest non-core activities to become more competitive (Haynes, Thompson, & Wright, 2003). In other words, the motto turned into back to the core business. As a result, in the early 1980s, a large number of companies began to reverse their unsuccessful M&A activities (Markides, 1995). Porter (1987) notes that more companies divested previously acquired businesses than retained them. Because of the increase in the volume and size, research into divestment acquired greater importance during the 1980s (Haynes, Thompson, & Wright, 2000; Haynes et al., 2003).

The background against which divestment research emerged conditioned the development of the field. The fact that most divestments in the 1980s involved previously acquired businesses, created the misconception that divestments were no more than a mirror image of M&A transactions. Early on, Boudreaux (1975; p. 619) mentioned that divestments were "*similar to asset acquisitions or mergers*". However, conceptualizing divestments as reverse mergers is flawed for three reasons.

First, the concept of acquisition-driven rather than strategy-driven motives led to the notion that divestments were the outcome of failed investment decisions, establishing them as a method to correct past mistakes (Markides & Singh, 1997). This approach also ill-defines reverse mergers. A reverse merger or reverse initial public offering (IPO) is the acquisition of a public company by a private company, allowing the latter to go public via a simpler and time-efficient process. Reverse mergers allow a private company to go public without having to raise capital and go through an IPO, which considerably simplifies and shortens the process. While IPOs are more expensive, require more energy and can take several months or years, reverse mergers take only few weeks. Thus, not all divestments are indicative of a failure as some units are acquired along with other business (cherry picking) and are not necessarily meant to be integrated, getting divested shortly afterwards. Second, the divestment of previously acquired units can be motivated by the desire to pursue a new strategy or the development of a new market opportunity, which were non-existent at the time of the acquisition (Weston, 1989). Hamilton & Chow's (1993) survey on managers' main motivations to divest, showed that the desire to grow the core business and exploit growth opportunities were more relevant than the reversal of previous investment mistakes. Dranikoff et al. (2002) argue that a company must actively manage its business portfolio as even the best business may suffer a decline over time. Besides, a company must also recognize that at a certain stage of its life cycle, it may not be the best owner for that business. Third, conceiving divestments as a mirror image of M&A disregards the nature and modes of divestment; instead, it simplistically assumes that a company's divestment implies another company's acquisition. Nonetheless, spin-offs do not involve external buyers, unlike M&A transactions whose parent shareholders become shareholders of the new independent company. The concept of divestment as M&A reversal could only be applied to sell-offs as only then does a divestment constitute an acquisition to another company. Even so, contrary to a M&A, a sell-off is a voluntary decision by the management of the divesting company (Khan & Mehta, 1996). Additionally, divestments are typically associated with failure whereas M&A transactions are linked with enthusiasm (Duhaime & Schwenk, 1985).

The misconception of viewing divestment as mirror image of M&A and as a corrective means of corporate restructuring, rather than a strategic option for corporate change, restricted the interest in the field and conditioned the unique identity of divestment research (Buchholtz, Lubatkin, & O'Neill, 1999). This was aggravated on one hand, by the bundling of M&A and divestment in portfolio restructuring research, making it difficult to distinguish the antecedents and effects of corporate divestment from those of the broader and more complex portfolio restructuring and, on the other hand, by the failure to accurately define what was meant by restructuring (Markides, 1995). The use of a plethora of alternative terms from both sides such as: refocusing, de-diversification, de-conglomeration, down-scoping, exit, closure, abandonment, down-sizing, disposal, unbundling, divestiture and disinvestment (among others) increased the confusion.

Typologies of Divestment

Corporate divestment has often been understood differently by scholars and many studies fail to provide clear information on the nature, scope and modes of divestment. Several typologies for divestment have been proposed in the literature.

At its most fundamental level, divestment should be understood as involuntary or voluntary. Involuntary divestment is the seizure of foreign-owned property by actions such as nationalization, expropriation, confiscation or any other regulatory reason and in which the change of ownership is forced upon the investor. For example, in 2010, the government of Venezuela seized the control of 11 oil rigs owned by US firm Helmerich & Payne (Reuters, 2010). Some of the factors that influence involuntary divestments are social unrest and the general disruption of business activities, ineffective law enforcement, political influence of local business groups or internal rebellions and armed conflicts (Chopra, Boddewyn, & Torneden, 1978). Conversely, voluntary divestment is based on strategic considerations and is often driven by poor performance or the lack of fit for a business (Boddewyn, 1979).

Montgomery & Thomas (1988) split divestment into strategic, tactical or distressful. Strategic divestments are value-free strategic choices whose purpose reflects a broader management view of the company such as the divestment of non-core business or the reconfiguration of a company's portfolio. Tactical divestments are intended at exploring occasional opportunities such as boosting stock prices or exploiting tax benefits and can therefore be understood as a company's reaction to a market or an environment change. Distressful divestments are associated with failure or as a last resort solution such as an effort to avoid bankruptcy. Figure 1 presents the two typologies.

Besides the mentioned typologies, divestment can be partial or complete. The degree of strategic relevance is strongly related with the scope of the asset divested, in other words, divestment can range from the disposal of the whole company, to the release of smaller assets such as plants, patents or capital stakes. Figure 2 presents an overview on divestment scope.

Figure 1. Divestment types

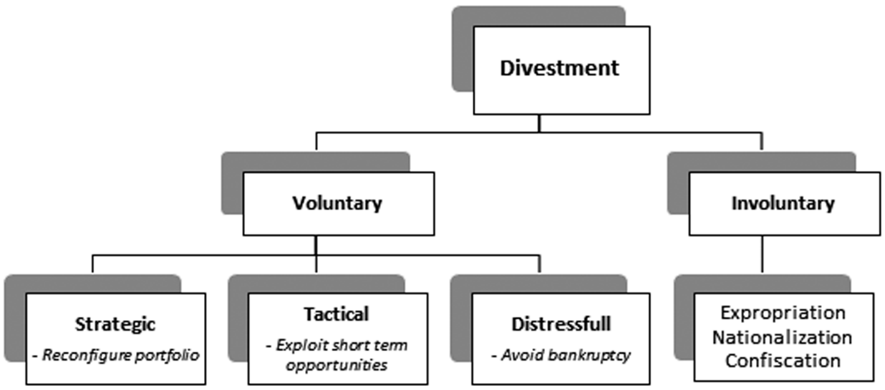
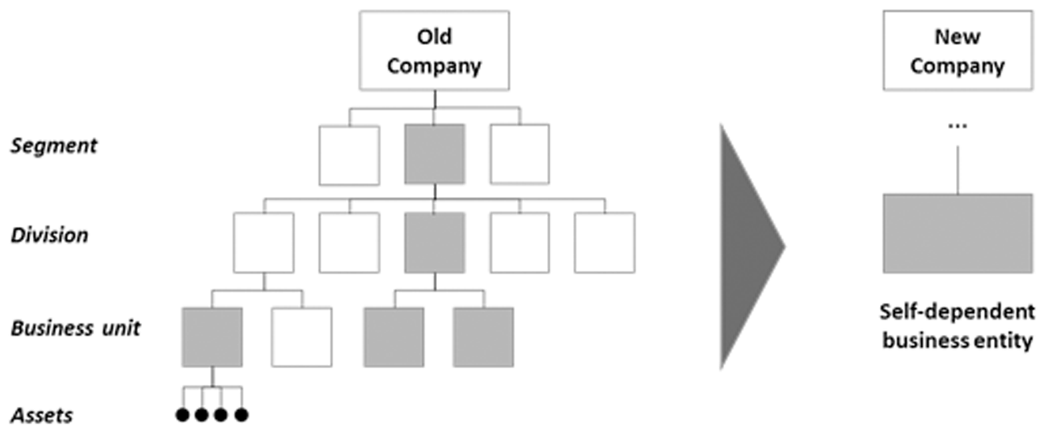
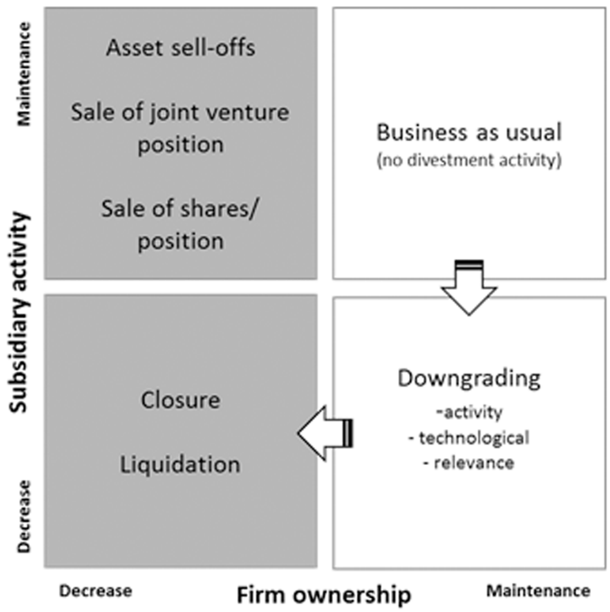


Figure 2. Divestment scope
Source: adapted from Sewing (2010)



Based on two dimensions, Simões (2002) proposed another typology for divestment: company ownership and subsidiary's activity. Company ownership is related with the parent company's decision to dispose of a portion of its assets, whereas subsidiary activity concerns the subsidiary's maintenance or decrease in activity. When company ownership and subsidiary activity is unchanged, businesses are understood to be running as usual. Closures and liquidations happen when the parent company relinquishes ownership and the subsidiary's activity is extinguished. The abandonment of business, product lines, outsourcing activities and the closure of units where the company continues to operate constitutes the most visible and delicate example of divestment (Simões, 2002). An example is Ford's decision to shut down its plant in Genk, Belgium, which besides the direct loss of workplaces, cost near 11 800 jobs in the region as suppliers to Ford had to make cuts (Reuters, 2014). Divestments also include the decrease of company ownership through the sale of assets or the share of a joint venture position, with no impact in the subsidiary activity (as the subsidiary continues to operate under a new parent company). An example is Autoeuropa, Portugal, where Ford sold its joint-venture position to Volkswagen in 1999. The plant continued to operate and the change in capital ownership had no implications for its employees, however, it constituted a divestment for Ford. Finally, divestments through downgrading lead to a decrease in a

Figure 3. Divestment activity/ownership matrix
Source: adapted from (Simões, 2002)



subsidiary's activity but not in a parent company ownership position. A downgrade in activity translates into a loss of a subsidiary's productive output with an impact on employment; technological downgrade corresponds to a scenario where the subsidiary specializes in low end products, unskilled labor activities or retains the manufacture of old products, being unable to capture new investment and product lines; a downgrade in relevance often implies a decrease of industrial activity and the shift of the subsidiary into a commercial or logistic platform (Simões, 2002). Simões (2002) claims that downgrading is often a pre-stage for a closure or liquidation. Figure 3 presents Simões' divestment typology matrix.

Besides downgrading, closure or liquidation and sell-off, divestment can be conducted through seven additional modes: spin-offs; spin-outs; carve-outs; split-offs; split-ups; leveraged buyouts; and management buyouts. Companies choose among the different divestment modes considering their strategy and future relationship with the divested unit. Table 1 presents an overview of the various divestment modes and some examples of the objectives pursued.

A Review of the Main Theories Used for Divestment

Chow and Hamilton (1993) conducted one of the first works that separate the various strands of the divestment literature. They organized the literature on divestment in three thematic strands: industrial organization, finance, and corporate strategy.

The industrial organization literature has focused on the impediments and barriers to exit, particularly, on the importance of asset specificity. The existence of specific assets that cannot be easily exploited under alternative uses or locations prevent companies from exiting a business (Caves & Porter, 1976). The financial strand of the literature is dedicated to the analysis of the capital's market reactions to divestments. Divestment is expected to increase the market value of a company because divested units are

Table 1. Overview of the multiple divestment modes

Divestment Mode	Definition	Link With Parent Company	Pursued Objective(s)
Downgrading	Decrease in the unit activity, relevance or technological investment	Yes	Pre-stage to a closure or liquidation; convert an industrial facility into a warehouse
Closure or liquidation	Shutdown of a unit	No	The business is ended; commonly associated with failures and low business returns; investors do not wish to spend time and effort to restructure their investment and the unit has poor value to the company's portfolio
Sell-off	Sale of a wholly owned company or a portion of a company's assets to a third party usually for a cash amount	No	Shedding of non-core activities; new company strategy; low unit performance; liquidity needs
Spin-off	The divested unit becomes a new company although the parent company keeps supporting this new company – the new managerial board is often from the parent company	Yes	Allow the divested unit to flourish in a new environment; release the divested unit from the parent company's ideas, historical record or image; foster innovation
Spin-out	Usually a small entrepreneurial venture founded by a leaving employee of the parent company	No	Exploit an employee's intellectual property
Equity carve-out	Disposal of a portion of a company through an IPO creating two separate legal entities – the parent company remains in control of a substantial fraction of the equity carved-out company	Yes	Temporary form of restructuring to recapitalize or raise funds in the capital market to pay shareholders or creditors; provide the carved-out unit a strong growth opportunity and avoid the negative image associated with a seasoned offered of the parent equity; allow a market value evaluation of an asset; may be used when the parent company does not believe there is a single buyer for the entire business or wants to maintain some control over the business unit
Split-off	Reorganization of a corporate structure in which the parent company shareholders receive stocks of the new company in exchange for stocks of the parent company	No	Seek for a bigger distinction between the parent company and the split-off business; method to bolster balance sheets by releasing underperforming units
Split-up	A single company is split into two separately companies with the shares of the parent company being exchanged for shares in the new company – the parent company ceases its existence	No	Taken due to strategic reasons such as when a company has completely unrelated business lines; forced by governments to end a monopoly scenario
Leveraged Buyout	Purchase of a significant amount of assets using borrowed money, bonds or loans to meet the cost of the acquisition – often through a financial sponsor	No	Allow a company to make large acquisitions without having to compromise a large amount of capital
Management Buyout	Purchase of assets, stocks or a unit of the parent company by an investor group which includes the incumbent management	Yes	Disposal of an asset which is not part of the core business

typically poor performers, and because divestment is a way to decrease diversification levels – highly diversified companies may be understood by shareholders as inefficient and encouraged to refocus (Benito, 1997). Finally, the strategic approach to divestment sees the company through the lens of the corporate life cycle or as a portfolio of assets (Chow & Hamilton, 1993).

Besides the aforementioned streams of literature, research in the field of divestment has resorted to other theoretical approaches to explain divestment. As follows, we review a group of extant theoretical approaches that has gathered scholarly consensus as being comprehensive enough to help explain divestment's fundamental reasons. We begin by following Chow & Hamilton's (1993) structure and review the exit barriers, then the agency theory, the corporate life cycle and portfolio approaches. Finally, we move onto the well accepted approaches of the Resource-Based View (RBV) of the company, the Transaction Cost Economics (TCE) and the eclectic paradigm.

Divestment From the Perspective of Exit Barriers

Divestment decisions were initially understood as rare and desperate management decisions, slowly turning into regular strategic decisions in response to unfavorable market conditions. Porter (1976; p. 29) proposed a set of barriers that worked against divestment decisions, claiming that "*the same factors that provide barriers to entry, often lead to barriers to exit, so the two are often associated in a business*." The conditions that inhibit a company from entering an industry are usually the same that later deter an exit (Harrigan, 1982). The importance of the individual exit barriers is contingent on factors such as context, life cycle phase of the industry, and the strategic value of the respective activities to the company (Harrigan, 1980, 1982).

Porter's (1976) pioneering work proposed three main barriers that made companies stay on business, even if having low return rates or rates below the cost of capital: structural or economic barriers; strategic barriers; and managerial barriers.

Structural or economic barriers are related with the characteristics of a business unit's resources such as technological factors, capital intensity, labor force, asset durability, asset specificity or asset age. Porter (1976, p. 22) mentions that "the more durable the assets are, the more specific they are to the particular industry, the particular company or the particular location, the less likely it will pay off to sell or shut down an unprofitable business, and the larger the immediate loss the company will face if it does shut down the business." Specific assets can be tangible or intangible. Tangible specifics assets such as high sunk cost in machinery (Siegfried & Evans, 1994), or intangible assets such as goodwill, advertising, research and development, company-specific human capital and the emotional attachments to the company, increase the perceived cost of abandoning a business (Caves & Porter, 1976).

Strategic exit barriers are associated with the inter-relatedness between units that act as a barrier to exit. Porter (1976) argues that the more complementary a business is to other businesses in the company, the less likely it will pay off to sell or close those businesses as even if unprofitable, they may still positively contribute to the overall company's activity – because of interrelatedness.

Managerial exit barriers are the characteristics of the company's decision-making that prevent exit decisions. Porter (1976) splits this barrier into information related and conflicting goals. Information barriers happen when a company has unsatisfactory returns in one of its business but is unaware of it – when unit's performance cannot be distinguished from aggregated financial or non-financial data. Conflicting goals report to a scenario in which manager's ambition diverges from the company's economic goals.

Porter (1976) provided empirical support for the impact of exit barriers as he found that the company's level of diversification and the existence of shared facilities with other businesses had an impact on the decision to stay on unprofitable businesses.

Divestment From the Perspective of the Agency Theory

The agency theory was born during the 1960s and early 1970s and was driven by studies examining risk sharing among individuals, in particular the problem that arises when cooperating parties have different attitudes towards risk (Eisenhardt, 1989). The agency theory extended this literature by including the problem of the agency. An agency relationship happens when one party (the principal) delegates work to another party (the agent) to perform a service on its behalf, providing decision-making authority to the agent (Ross, 1973). The fundamental concept of the agency theory is the assumption that the interests of the principal and the agent are distinct.

The agency theory aims to solve the two problems of an agency relationship. First, the agency problem that arises when the objectives of the principal and the agent diverge, and it is difficult for the principal to monitor the agent behavior. Second, the problem of risk sharing when the principal and the agent have different attitudes towards risk and consequently, exhibit different options to risk preferences (Eisenhardt, 1989). The agency theory targets efficient ways to govern the relationship between the principal and the agent taking into account personal (e.g., self-interest and risk proneness), organizational (e.g., goals conflicts between members) and information components (e.g., information can be purchased) (Eisenhardt, 1989). The principal can attenuate existing divergences with the agent by offering incentives for the agent to behave as desired or instead, by incurring in monitoring costs to limit the agent opportunistic behaviors.

The relationship between the agency theory and divestment lays in the conflict of interest between shareholders and managers – who have different goals and attitudes towards risk. While shareholders seek to maximize profit, managers may be driven by self-interest and can engage in actions to increase their personal wealth, rather than maximizing shareholders' returns. Managers driven by self-interest may follow expansionist strategies, focus on company growth, on maintaining their status quo, on refusing to admit previous mistakes and consequently, avoiding divestments. Company decisions can then be driven by a manager's own perceptions rather than by shareholders' interests. The agency issue can be aggravated by the information asymmetry in which a party, usually the agent has more and better information than the other party, the principal. The information asymmetry prevents both parties to evaluate decisions under the same conditions, leading to poor transaction business and an unreliable tracking of the agent's actions.

The agency theory suggests that managers follow over-diversification strategies as a self-service action that they take in order to increase their compensation, power, prestige or simply to reduce their personal risk by decreasing the total risk of the company. Divestments are then seen as a mean to shape back companies to their initial condition and decrease diversification levels.

Based on the agency theory, managers may also avoid divesting. Weisbach (1995) claim that managers are unwilling to divest as it may damage their reputation, and in addition, they tend to over-evaluate their management skills and acquire types of businesses they consider mastering. Ang, de Jong, & van der Poel (2014) examined the impact of familiarity with business segments on managers' divestment decisions, finding that when managers were faced with an opportunity to divest assets from different segments, they were more likely to divest assets from unfamiliar than familiar segments. Divestments are often seen as a signal of failure, preventing managers from acting in the company's best interest and divesting when necessary. Shimizu & Hitt (2005) claim that managers are not likely to divest poorly performing units because divestments are understood as an admission of an inappropriate project choice that was made initially, and adversely affect the perception of the manager's ability. Hillier, McColgan, and Werema (2009) note that managers are reluctant to dispose of poorly performing assets they previously invested in, because in doing so, they may provide a signal of low managerial quality.

The arrival of new and external managers can increase the likelihood of divestments due to the inexistence of previous attachment with past actions (Shimizu & Hitt, 2005). The existence of strong governance mechanisms may also encourage managers to behave in strategies beneficial to shareholders and divest if necessary. On the other hand, weak governance mechanisms create the conditions for poor management decisions.

Divestment From the Perspective of the Organizational Life Cycle Theory

The first studies conducted in the field of divestment used the organizational life cycle theory to explain its nature (Boddewyn & Torneden, 1973; Chopra et al., 1978). The organizational life cycle theory assumes that companies undergo various logical phases from birth to death, as opposed to a randomized set of events. This became obvious as companies underwent periods of expansion, contraction and would eventually get extinguished.

The organizational life cycle models can vary in the number of stages. Quinn & Cameron (1983) reviewed nine models of organizational life cycle proposed in the literature. They found the following four stages: (1) an entrepreneurial stage; (2) a collectivity stage; (3) a formalization and control stage; and (4) a structure elaboration and adaptation stage. Adizes's (1979) model added the decline and death that completes the life cycle. Briefly described, the entrepreneurial stage is a period in which companies attempt to keep the business active and become viable entities. The collectivity stage happens after companies have established their distinctive competences and enjoyed initial market success, seeking rapidly sales growth and further development of their capabilities and resources to capitalize their advantages on a larger scale (some organizations are unsuccessful in achieving this and fail to survive). The formalization and control stage is characterized by a stabilization in sales growth, a decline in innovation, and the establishment of a more formal hierarchy of management (the aim is to become smoother and more efficient). The structure elaboration and adaptation stage is where companies move into diversification and expansion strategies to deal with more complex and heterogeneous markets, focusing simultaneously on more sophisticated control and planning systems. The final stage or the decline is characterized by profitability drops owing to market stagnation, lack of innovation, and the individual's focus on personal objectives instead of on the organization, driving the company to its death.

Existing research on divestment conceived a company's death as a natural event based on the organizational life cycle theory. Boddewyn & Torneden (1973; p. 25) mention that "*most ventures go through a normal life cycle in which they grow, mature, and decline in purely economic terms. Although managers may prefer to think of their enterprises as eternal, a comparison of the 50 largest U.S. trusts existing at the beginning of the century with the latest Fortune 500 reveals a natural disappearance process*." Chopra et al. (1978) argue that subsidiaries are born, grow and die and the sooner companies accept the corporate life cycle perspective, the lesser the surprises and indignation caused by divestments, as they will be better planned out and accounted for. Chow & Hamilton (1993) suggest that as companies eventually die, divestments can be used as an escape route in declining or stagnated industries.

Divestment From the Perspective of the Corporate Portfolio Theory

The corporate portfolio theory is one of the most used in the field of divestment, and is well-accepted by academics in justifying divestment's major reasons (Duhaime & Baird, 1987; Duhaime & Grant, 1984). The corporate portfolio theory goes beyond the use of growth-share matrix and is at the center of corporate strategy – which includes taking key level decisions such as entering into new businesses, allocation resources to business units and liquidating subsidiaries when necessary.

To better understand the relationship of corporate portfolio theory with divestment, it is essential to go back to its roots. At the heart of the corporate portfolio theory is the company's awareness of the need to successfully manage different businesses through expansion or contraction activities. Following World War II and for three succeeding decades, strategic management thinking was molded by three main paradigms which stimulated diversification activities. Firstly, company growth was accepted as a major driver for profitability as scale productions were led by cost advantages gained through learning experience, specialization and scale economies. As a result, and because of emergent market opportunities allowing product diversification, scale growth and gaining market share through acquisition became the dominant strategy. Secondly, there was the belief that a corporate economy would be more efficient than external capital markets in terms of resource allocation and strategic businesses management – mostly because of the cost of transactions (Williamson, 1975, 1985). Thirdly, with the development of leading management schools and the universal principles of management (Drucker, 1954), there was the perception that educated managers would be capable of successfully managing multi-business companies.

Boosted by these paradigms, diversification strategies flourished between the 1950s and the 1970s with investors rewarding diversifying expansion (Shleifer & Vishny, 1991). The race for growth made companies with unrelated businesses and high earnings more attractive to stock markets, granting access to cheap capital that allowed them to keep growing through the further acquisition of new businesses. The shift towards diversification had an impact on the management field because of the need to formulate new corporate strategies to efficiently manage diversified companies through the efficient allocation of cash flows, the exploitation of synergies, the seizure of new market opportunities and the closure of underperforming units (Nippa, Pidun, & Rubner, 2011).

From a financial perspective, as the management of diversified businesses matches the one of handling a portfolio with different return rates and risks, financial concepts were soon applied to real corporations. Based on the notion that the major aim of corporate portfolio management was to balance cash-flows between businesses, several approaches were created. Perhaps the most successful one was the Boston Consulting Group (BCG) matrix that systematizes a process for evaluating different products and business units based on their cash-flow outputs.

In the 1980s, the strategic management paradigm shifted towards a more focused corporate portfolio, supported by new dominant theories that relied on the superiority of markets over corporations (e.g., core competence theories). The new belief that diversification strategies were inefficient and that financial markets outperformed managers of multi-business companies at allocating capital, stimulated companies to engage in restructuring strategies and become more focused (Nippa et al., 2011). The corporate portfolio theory saw divestment as a means for solving suboptimal internal organizational structures within diversified corporations and for reaching optimal resource allocation. High diversified companies may turn into complex and bureaucratic structures that are difficult to manage, leading to issues related to the loss of control, inefficient resource allocation, and a decrease in corporate value. Moreover, as the level of diversification is related to the number and diversity of the subsidiaries within a company, highly diversified companies are less dependent on single divisions that in turn make them more prone to be divested, particularly when experiencing poor performance. Likewise, a company's size may result in additional inefficiencies as larger companies usually have a higher complexity, making management control more difficult and eventually leading to a loss of competitiveness.

Divestment From the Perspective of Transaction Cost Economics (TCE)

TCE is a central theory in the field of strategy and divestment. TCE supports the notion that companies exist to decrease transaction costs, addressing questions on how companies set their boundaries and how they govern their operations. The unit of analysis is the individual transaction between the buyer and the seller, and the main concept is that transactions are better performed within company boundaries than in markets due to market breakdown.

Because of human cognitive limitations and the costs associated with transactions, the assumptions related with efficient markets fail to hold, making it more advantageous to structure transactions within companies. However, this was not always the economic thought. Coase (1937) first introduced the concept of transaction cost based on a gap between the theory of the company and the market organization, suggesting that relations were particularly susceptible to transaction costs. At the time, the economic theory saw companies and markets as alternative modes of coordinating production. However, Coase (1937) noticed that resources were assumed to be allocated based on price mechanisms for some purposes, and dependent upon the investor for other purposes and thus, the need to understand how the choice between alternatives was affected. The assumption that transaction costs were inexistent remained unchallenged for the following years. Later, Williamson (1975, 1985) revitalized TCE by adding a human behavioral assumption. Williamson recognized that in a transaction, some parties opportunistically take advantage of their counterparts, and identified features of a transaction (such as asset specificity, uncertainty and frequency) that make markets fail – justifying transactions being held in companies rather than in markets.

Companies must then choose the governance structure that minimizes their transaction costs. In other words, companies building a new plant must decide between buying components in the marketplace (market), manufacturing them in house (hierarchy), or engaging in some form of relationship with suppliers (hybrid). Based on TCE, companies and markets are governance alternatives that companies use to reach the point where the marginal benefit of acquiring one more business is equal to its corresponding cost. Thus, acquisitions may continue for as long as the benefits of acquiring new businesses are greater than the marginal cost of owning them. The benefits of acquiring more businesses stem from economies of scale, sharing of resources, governance reduction costs and resource allocation to higher valued operations. Regarding divestments, they increase when the costs of the administrative exchange within the company are higher than the transaction costs of the market exchange – however, strategic assets and activities should be kept within the boundaries of the company. Bergh & Lawless (1998) indicate that under environmental uncertainty, over-diversified companies have higher transaction costs and are more difficult to manage – divestments are then used to restore control and refocus. Adopting a distinct approach, Mata & Portugal (2000) relate transaction costs with the ownership structure. Transaction costs pose that joint ventures are a response to a market failure to a specific asset held by a different company. However, unlike wholly owned units, joint ventures are more difficult to manage because of shared management and because both parties share profits, having a higher incentive to free-ride that makes ventures more instable.

Divestment From the Perspective of the Resource-Based View (RBV) of the Company

The origins of the RBV date back to the early work of Penrose (1959) where the emphasis was set on the importance of a company's resources and its implication for performance. The challenge was to understand why some companies operating in the same markets outperformed others. The strategic management thus focused on a theory of how companies gain competitive advantage in their marketplace.

A company's strategy includes decisions such as which business to compete in and which mode of competition to adopt (Porter, 1980). The RBV strategy is the pattern of a company's acquisition, retention and generation of sustainable and non-replicable resources by its competitors (Barney, 1991; Penrose, 1959). The classical approach to strategy formulation begins with an assessment of organizational competences and resources, in which those that are distinctive or superior to rivals become the basis for a competitive advantage if properly matched with environmental opportunities (Andrews, 1971). A competitive advantage is created when the company's strategy is value creating and not expected to be implemented by current or future competitors. The RBV assumes that resources are heterogeneous and immobile, enabling companies to deploy different strategies to outcompete each other.

Barney (1991) indicates that a company's resource bundles and capabilities are different between companies, resulting in productive factors with different levels of efficiency, in which some are superior to others. 'Resources' are to be understood as the inputs or factors controlled by the company which help to carry out its activities, while 'capabilities' are the company's capacity to use its resources: capabilities are a non-transferable characteristic that enhances the resources possessed by the company (Makadok, 2001). Companies possessing superior resources can produce more or better satisfy their customer needs, generating rents. Resource heterogeneity allows companies with different capabilities and marginal resources to compete in the same marketplace. Besides heterogeneity, the RBV assumes that resources are not mobile and do not move between companies in the short-term, preventing companies from replicating competitors' resources and implement the same strategies. For example, intangible, knowledge-based or socially complex resources such as brand equity, corporate culture or intellectual property are company-specific. According to the RBV, companies create competitive advantage by using their resources distinctively. Owning heterogeneous and immobile resources is a critical condition for success, still, it may not be sufficient for a sustainable competitive advantage as the chain is only as strong as its weakest link. Barney (1991) argued that in order to generate a sustained competitive advantage, resources and capabilities should be valuable, rare, inimitable, and non-substitutable.

The RBV root view of the company supports the notion that divestment is the logical outcome of the process in which companies use acquisitions to reconfigure their structure of resources. Acquisitions are strategic actions that help companies reconfigure their business and modify their resources so that their new skills adapt to changes in the environment (Capron, Mitchell, & Swaminathan, 2001). Modifying resources requires the reallocation of resources from the target company to the acquirer, and often, the divestment of obsolete resources. Capron et al. (2001) note that the reallocation of resources to one business lead to divestments in the same business that receives the acquired resources: companies seek to increase the strategic similarity between acquirer and target by sharing relevant resources to seize market opportunities, and divesting those resources that do not fit. Kaul (2012) found that innovations trigger companies to reconfigure their portfolio and redistribute resources to new areas of opportunity while divesting non-core businesses. Accordingly, companies begin with an equilibrium where scarce resources are allocated to the various opportunities to maximize rents. Innovations disrupt the equilibrium as new resources developed by the company present new opportunities with better returns. Alternatively, innovations by rival companies may change the value of the existent resources creating a disequilibrium and prompting new resource allocation until a new equilibrium is reached (Kaul, 2012). The RBV contributes to explain the divestment of certain resources when compared to the non-divestment of unprofitable resources, due to their valuable, rare, inimitable and non-substitutable characteristics, as companies will hold them in order to maintain a competitive advantage.

Divestment From the Perspective of the Eclectic Paradigm

The eclectic paradigm has been traditionally used in the context of economic theories to examine the determinants of foreign direct investment (FDI) and foreign activities of multinational enterprises. Dunning's (1980, 1988) eclectic paradigm established that the degree of geographical and industrial composition of foreign production made by multinationals is the outcome of the interaction of three sets of competitive advantages: ownership, location and internalization (OLI).

The first, ownership advantages, relate to company-specific competitive advantages such as trademarks, production techniques, entrepreneurial skill and returns of scale for companies seeking to engage or increase their FDI. The second, locational advantages, are based on geo-economic factors, whereby companies seek to exploit features such as the existence of raw materials, lower wages or special taxes. The third, internalization advantages, are associated with the advantages that lead companies to favor engaging in foreign production rather than establishing third party agreements such as licensing, partnerships, joint ventures or franchises. Dunning (2000) proposes that companies engage in FDI in the following circumstances: the greater their competitive advantage relative to those of competitors in host country (O); the better the natural or created resources in the host country the company needs to use together to exploit its ownership advantages (L); and the greater the benefits of internalizing cross-border intermediate product market (I). When in the presence of the three OLI advantages, companies engage in FDI (Dunning, 1980, 1988).

Boddewyn (1983) proposed a Dunning theory of foreign divestment, or foreign divestment (FD) theory, claiming that foreign units would be closed whenever multinational companies found any of the following situations to prevail: (1) the company ceased to have an ownership advantage; (2) the company no longer found it worthwhile to internalize its advantages; and (3) the company no longer found profitable to internalize its competitive advantage in a host country. However, unlike Dunning's (1980, 1988) approach that requires all three OLI conditions to be met simultaneously for FDI, the FD theory requires just a single one of them. In other words, even if a company retains its ownership advantage, it may still divest if losing its location advantage. Benito & Welch (1997) claim that multinational companies divesting due to the loss of OLI advantages usually have the necessary room for location flexibility and the ability to adjust their resources between various countries, exploiting their advantages, markets and economic policies.

Benito (1997) notes that host countries should provide specific location advantages such as economic growth that stimulate companies to invest in those countries rather than producing domestically. Belderbos (2003) verified that plants established to circumvent payment of antidumping duties were more likely to be divested once antidumping duties were repealed due to the loss of the company's location advantage. Griffin (2003) claims that disappearance of the original investment motives is one of the reasons as to why companies divest. Benito (2005) also mention that units that are based on location factors such as cost advantages or trade barriers have higher divestment rates.

THEORETICAL FRAMEWORK

As seen in the previous sections, the decision to divest may concern to the disposal of a portion of assets of the company, such as plants, or to the complete shutdown of a business. The divestment can be conducted through different modes such as closures or sell-offs. These vary according to the companies' strategic goal, but also because of special conditions such as the availability of buyers in the market. The use of the various theoretical lenses on divestment has generated several reasons as to why companies divest. For comprehensiveness reasons, these factors can be grouped as follows: headquarters and parent company, which are related to the company's strategy; unit factors, concerning the characteristics of the divested unit candidate; and market factors, which are external to the company and include the host country environment and the characteristics of the industry itself.

Headquarters and Parent Company

Several theories focused on divestment reasons at this level, as the decision to divest is ultimately taken here. Among the most well-known accepted reasons to divest is a high level of diversification and a company size beyond optimum control, as supported by the agency, portfolio and TCE theories. Divestment is thus used as a strategic tool to decrease the levels of diversification, to increase focus on core activities and to decrease the company's complexity. Over-diversified companies are understood as having higher transaction costs and as being more difficult to manage. In addition, companies should strategically choose governance structures that minimize their internal transaction costs, deciding on which activities to keep within the company (manufacture internally and retain within the company's boundaries), which to externalize (buy in the market, subcontract) and in which to engage in some form of relationship with other partners (establish joint-ventures, licensing), using divestments to dispose of unwanted or unneeded assets.

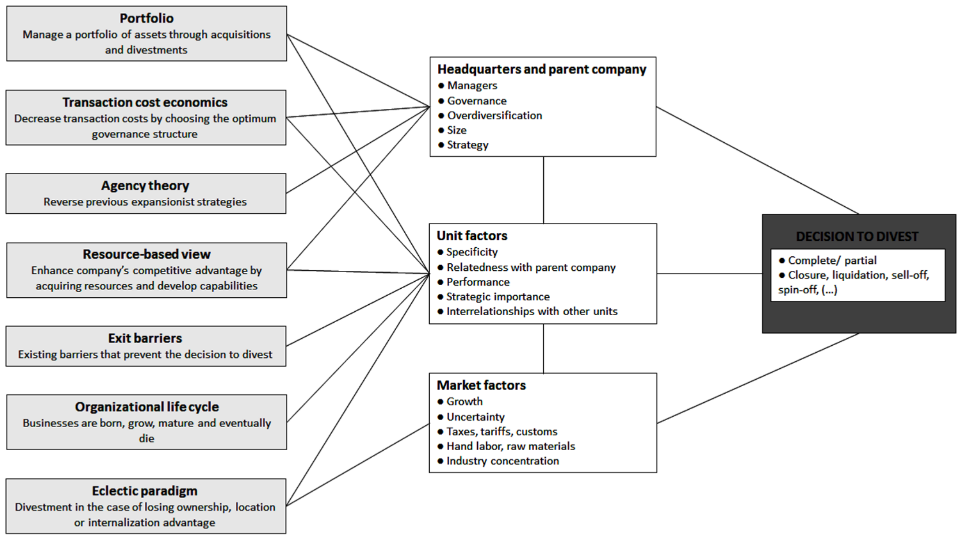
Unit Factors

The characteristics of the units influence the decision to divest. Specifically, units that are more specific, that are more related to the parent company's core activity, that exhibit a higher performance and that have a higher level of interrelationships with other units of the company are less likely to be divested. These factors found support in most of the theoretical approaches in the field, particularly the exit barriers that highlight the characteristics that make units less prone to divestment, and the RBV, that emphasizes how the unique combination of resources and capabilities generate a competitive advantage. Moreover, the stage of the life cycle of the unit or the product lines it manufactures, may also influence its divestment as some units manufacture only old or low-end products and will end up being divested when those products reach their end of life.

Market Factors

The market factors are mostly based on the eclectic paradigm. Factors such as a host country's growth, environmental uncertainty, customs, special taxes and tariffs, the existence of raw materials and labor cost increases may lead to divestment. In other words, the loss of the location advantage that constituted the competitive advantage for the company to engage in FDI oppositely works as a reason to divest. In addition, although Porter only found exit barriers at a unit level, exit barriers such as increasing industry competition and concentration ratio were found to influence divestments (Li, 1995). Divestment is thus seen as a tool to react to external environmental changes that decrease the competitiveness of the company. Figure 4 portrays the main theoretical contributions to the field of divestment.

Figure 4. Theoretical approaches and contributions to divestment



CONCLUSION AND AVENUES FOR FUTURE RESEARCH

Divestment is the decision of a company to dispose of a portion of its assets. The most recent data indicates that the number of divestments has increased over the years, and that this is a common phenomenon. However, divestment has received less attention from the literature than M&A. This is because while M&A are associated with growth and prosperity, divestments are often negatively interpreted as failures. Nonetheless, divestment is a strategic tool that can be used to improve the company's performance and reshape the business.

Clearly, existing knowledge on divestment is still scarce. This chapter addressed questions such as: what divestment is, how research on divestment has evolved over time, what the main types of divestment are and, fundamentally, what the contributions of the main theoretical approaches to divestment have been.

Research in the field of divestment is still closely tied to the 1960s and 1970s, which were decades of expansion and diversification. The study of divestment attracted researchers' attention once capital markets became more skeptical about diversified companies and corporate conglomerates. This led to increased pressure from shareholders for companies to increase their focus and divest non-nuclear activities. With an increase in the number of divestments, research in the field increased as well. The aforementioned factors contributed to the notion that divestment is the reversal of a prior acquisition or a way to correct a previous error, rather than a legitimate strategy adopted by the company.

Research in the field of divestment is also hindered by several obstacles. Among those is the difficulty to clearly isolate the phenomenon of divestment considering its various typologies and modes. Fundamentally, divestments may be forced on a company by governments; they may be the outcome of a company's voluntary decision based on a strategic option such as the reconfiguration of its portfolio of assets to take advantage of a market opportunity; or they may simply be a last resort measure to meet liquidity needs to pay creditors and avoid bankruptcy. The object of divestment varies from the company (as a whole), to a business segment, a unit or assets such as machinery. In addition, there are various legal modes through which divestments can be carried out. These modes are often associated with distinct strategic objectives and have distinct implications on the future relationship between the divesting company and the divested asset. This plurality in the divestment makes it difficult to clearly isolate the phenomenon and draw more accurate conclusions as several studies are silent on the strategic purposes of divestments, or on the legal mode used to conduct them. As a result, units sell-offs, closures or spin-offs can be analyzed from the same perspective. However, while a spin-off can be conducted to foster innovation, a sell-off can be conducted to obtain funds to start or support a new business. Likewise, whereas in a spin-off the employees may continue to operate under a new owner, in a closure, they may lose their jobs.

In this chapter we identified seven theories that have been used to examine divestment. Although others can be found in the literature, the ones reviewed in this chapter are among the most frequently used and best-accepted to explain this phenomenon.

The exit barrier is among the first theories used in the field of divestment. This theory found its application mostly in a context where it was common for companies to over-diversify and pursue growth and expansion strategies. Porter (1976) sought to explain what makes companies hold on to their assets and avoid divesting. He used his theory of barriers to entry to analyze why managers did not divest poorly performing units. He justified the decision to hold on to unprofitable assets through management-related barriers such as conflict of interest, the specificity and durability of the assets, and existing intra-unit relationships. The theory of exit barriers is one of the few approaches whose focus is on the decision not to divest (hold the assets). One of the main limitations of this approach is the fact that most of the barriers examined pertain to the company, which overlooks other potential types of barrier at an industry, market or country level.

At an early stage, divestments were seen under the theory of the organizational life cycle. The organizational life cycle posits divestments as a natural phenomenon and as an irreversible process and is perhaps among the less strategic approaches to divestment. Accordingly, divestment is seen as being beyond the company's control.

Following another approach, divestment was analyzed using the theory of FD drawn from Dunning's eclectic paradigm. Based on this approach, foreign divestment happens because of the loss of competitive advantage. As opposed to Dunning's eclectic paradigm that requires all OLI conditions to be met simultaneously for companies to engage in FDI, the theory of FD merely requires the existence of a single condition for divestment. The company is thus seen as an entity that exploits the competitive advantages of different locations. As soon as the company's competitive advantage fades, the company divests its unit or transfers production (relocates) to a new location where it can enjoy new advantages. One of the main limitations of this approach is the overemphasis of the impact of location advantage. FD theory perceives the company's decision to divest as being mostly based on the exploitation of cheaper production conditions such as lower labor or favorable import taxes, ignoring the strategic side of the business.

We may include the use of RBV, TCE, portfolio, and agency theories under the same umbrella. Like the eclectic paradigm, the RBV analyzes divestment considering the company's competitive advantage. However, the RBV takes a more internal view of the company. Accordingly, the company buys or sells assets to obtain a combination of resources and capabilities that create a competitive advantage. Divestment is seen as a tool to achieve that purpose. Nonetheless, the view of divestment based on the RBV is once again more acquisition than strategy driven, as divestments become a way to shed assets due to previous acquisitions. This is even more obvious when considering divestments under the agency, portfolio and TCE theories. Both the agency and portfolio theories explain divestments as the reversal of previous managerial decisions that had led to the over-diversification of the company, or its growth beyond the optimal level of management. This is because of the existing conflict between the manager and shareholders or simply due to managers' desire to adopt an expansionist strategy that is often more valued by shareholders. Divestment is no more than a way to return the company to its original configuration, decrease the level of diversification of the company, reverse previous acquisitions, or increase the company's focus on its core activities. Although the TCE explains acquisitions and divestments as a way of decreasing the costs of the transaction and reaching the optimum balance between manufacturing internally and buying in the market, its application also favors the aforementioned importance of company size and excessive level of diversification in the decision to divest. More diversified and larger companies have higher internal transaction costs because of their higher complexity, thus, divestments are a way to recover the operational flexibility and the ability to quickly react to external changes.

Overall, one of the main shortcomings in the field is the use of single theories, rather than the use of several of them to complement each other. Furthermore, based on existing research, the use of new theoretical approaches in the field of divestment is sorely needed. We propose four distinct approaches to deepen the analysis of the divestment phenomenon: the use of international strategies, the use of the network, the stakeholder approach and the institutional theory.

First, the use of international strategies. Existing research in the field of divestment needs to shift from the concept of the reversal of previous over-diversification. The FD theory is an approach to foreign divestment, however, the emphasis is heavily placed on locational advantages. This approach is not inclusive on the role of the international strategy on divestment. Operating internationally involves understanding the characteristics of foreign markets and the ability to deal with the uncertainty and the risks of doing business in a global marketplace. An avenue for future research is to understand how the various international, global, multi-domestic and transnational strategies influence the decision to divest. Since the various countries have unique governmental characteristics, laws, norms, taxes and cultures, operating in an international market is more complex than operating in a single domestic market only. Studying divestment in a more international setting can help understand how the economic, political, cultural, and competitive environment influence divestment decisions. Divestments have also been seen from a financial or performance-related perspective, however, companies' performance issues are often the outcome of non-financial issues. These structural problems of the company and the existing relationships among divestment reasons have remained relatively underexplored. Divestment studies have also been based on Western countries and samples. With the increasing presence of companies in emerging countries and increasingly dynamic international markets, research should be extended to emerging countries because they often adopt unique governance structures and mechanisms other than those of Western countries (e.g., family business conglomerates). These studies could also provide answers to questions such as the determinants of the various modes of divestment (e.g., sell-offs, spin-offs and carve-outs) in the context of international businesses. Besides, when considering an international environment, there are no further theoretical approaches to explain divestment other than the FD theory.

Second, the use of the network theory by adopting an intra-company and industrial network perspectives. The use of the network approach is still underexplored in the context of divestment. According to network theory, industrial markets can be understood as networks of relationships between companies. Coviello & Martin (1999) note that the network theory influences the way of entering a particular market. The position of the company in the network determines its opportunities as well as its strategy. Johanson & Mattsson (1988) describe the process of the internationalization of the company as the establishment, maintenance and development of relations with network participants on foreign markets. Just like the internationalization process, the foreign divestment process can be conditioned by the number and type of relationships the company holds with its partners. Likewise, multinational companies can be understood as a network of business units, and opportunities and threats along the company's internal network that can condition and influence the decision to divest. In the same line, units hold a position within their parent company's network. A unit's role evolves over time as a response to changes in the external environment such as market growth, labor cost changes or competition moves. Moreover, units may also acquire (or lose) capabilities because of their managers' enthusiasm or top-down decisions from headquarters. Thus, how is the decision to divest influenced by the unit's network and its strategic role within the company?

The third path for future studies entails the use of the stakeholder approach, in particular, the evaluation of the costs of divestment and on the management of the various stakeholders in the divestment process. Divestment research evaluates divestments fundamentally as an economic decision. Nonetheless, divestments have an impact on various stakeholders and the costs of exit generally go beyond the costs of closing a business unit. Besides, because divestments are usually associated with failure, managers may choose to remain in the market for too long. Both costs have been neglected by research in the field. Divestments are also an event that has an impact on a vast array of actors such as shareholders, managers, employees, suppliers, clients, banks and governments, among others. It has remained unclear how the interests of these actors are managed and what their role is in the decision to divest. Recently, Fassin, de Colle, & Freeman (2017) used the stakeholder theory and showed how intra-stakeholder alliances prevented the divestment of units in Belgium and Italy. Clearly, the stakeholders play a role in the decision to retain or divest that requires a further look.

The fourth and final potential avenue for future research is to examine divestment using the institutional theory. Research recognizes that companies are embedded in an institutional environment that directly (e.g., through regulations) and indirectly (e.g., through subsidization) influences them (Capron & Guillén, 2009; Porter, 1980). Porter (1980) argues that the analysis of companies' environments is incomplete without considering government policy. Coercive isomorphism relates to both formal and informal pressures based on legal and cultural expectations of the society in which the company operates. Changes of environmental regulations may have implications for corporate structures and divestment decisions. Mimetic isomorphism is the outcome of companies modeling themselves on other companies when there is environmental uncertainty. The uncertainty resulting from weak emerging-market institutions leads to the formation of diversified business groups across different nations (Carney, Gedajlovic, Heugens, Van Essen, & Van Oosterhout, 2011; Khanna & Palepu, 2000). It is thus likely that the institutional environment influences corporate divestment decisions through mimetic responses to uncertainty and regulation (i.e., coercive interventions).

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KEY TERMS AND DEFINITIONS

Business Diversification: Diversification is the corporate decision to enter a new business or a new market in which the company currently does not operate. Business diversification can be driven by defensive reasons such as decreasing the risk of a market contraction, or offensive ones like taking advantage of a market opportunity. Diversifying companies expect to obtain the benefits of diversification like increasing growth and profitability, but also face the risks of going into an unknown market.

Corporate Restructuring: A process that involves changing and reorganizing the structure of a company. Corporate restructuring can concern to: organizational restructuring such as the change of organizational structure, systems or practices, downsizing of workforce; financial restructuring such as management buyouts, leveraged buyouts or asset sell-offs; and portfolio restructuring such as divestments, dissolutions and mergers and acquisitions.

Corporate Strategy: The direction the company follows and how it uses its internal resources considering the external environment in which the company competes to generate value to its owners and satisfy its customers. Corporate strategy includes for example cost leadership or product differentiation strategies.

Divestment: The partial or complete disposal of a whole company, a segment, a division, a business unit or an asset. Can be conducted through various legal forms such as downgrading, closure, sell-off, spin-off, spin-out, equity carve-out, split-off, split-up, leveraged buyout, management buyout.

International Business: All activities that include the trade of goods, services, technology, capital, skills and knowledge between two countries at a global level.

Market Exit: A company's strategic decision to withdraw or abandon a certain market because of financial losses, poor profitability, low future expected returns, or to reshape its business, among others.

Merger and Acquisition: Transaction in which the ownership of a company or its units are transferred or combined. Includes mergers, in which two entities are combined in one entity; and acquisitions, in which one entity take another one stock, equity interest or asset.