Exploring interdependencies in the pre – and post-divestiture periods

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Résumé :

Dans le cadre des relations collaboratives, les rôles de l'encastrement des réseaux de partenaires et de l'asymétrie du degré de proximité de leurs activités sont reconnus comme d'importants facteurs de création de valeur. Cependant, ces éléments ont été principalement étudiés dans le cadre de la création de nouveaux liens et les connaissances relatives à la perte de liens restent limitées. En tant que transactions impliquant une rupture entre l'activité cédée et le portefeuille d'activités conservé, les désinvestissements représentent un contexte prometteur pour combler ce manque. De plus, la littérature portant sur les relations entre désinvestissement d'une part et alliances et réseaux d'autre part demeure inexplorée. Combler ce manque participera à mieux appréhender le choix de l'acquéreur et comprendre comment de nouvelles relations se créent à la suite du processus de cession. Fondés sur les concepts d'encastrement et de proximité des activités, cette étude vise à améliorer notre compréhension des relations inter-organisationnelles pré et post-cession. Premièrement, je propose que cédants et acquéreurs ayant une relation pré-cession soient plus enclins à effectuer une transaction. Deuxièmement, je propose qu'en période post-cession, l'entreprise cédante créera probablement une nouvelle relation avec l'acquéreur si les activités cédées sont particulièrement liées aux activités conservées par l'entreprise.

Mots-clés : cession d'activité, relations inter organisationnelles, encastrement, interrelation métiers

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INTRODUCTION

A role of network embeddedness of partners and an asymmetry of business relatedness of two firms has been acknowledged as an important factor for total value creation in collaborative relations (Gulati & Wang, 2003). This was mostly explored for a cases of new ties creation, but not for tie loss. Divestitures, by their turn, are corporate transactions which encompass detachment from firm's current activities. The separation from former activities and resources might have a substantial impact for divestors during post-divestiture periods (Moschieri, 2011). If extensive research has been conducted over the past decades on implementation challenges of acquisitions (Rouzies, Colman, & Angwin, 2018), various forms of partnerships and alliances, surprisingly little attention has been paid to analysing factors driving to variance in divestiture outcomes (Lee & Madhavan, 2010). On their turn, divestitures are prevalent mechanisms for management of firm's portfolios, when 84% of companies consider divestiture decisions within the next two years (EY, 2019).

This conceptual paper explores the inter-organizational relationships between divestors and buyers before and after divestiture transaction. The literature remained salient on a relationship between divestitures, alliances and networks (Brauer, 2006). Although inter-organizational relationships in pre- and post-divestiture period may lead for higher value creation (Friesl, Garreau, & Heracleous, 2018) from these deals by ensuring the best owner for the firm's formal activities and a maintained access to valuable resources while avoiding the sudden disturbance of former linkages. The presence of prior inter-organisational relationships and their formation after divestitures between involved parties might lead to the difference in divestiture performance, thus our objective is to explore the phenomenon of formation of inter-firm cooperative arrangement in divestiture process.

Given these particularities, we suggest that inter-organizational governance choices before and after divestiture require theoretical refinement and ask: *What is an impact of inter-organizational relationships between divestor and buyer in pre- and post-divestiture periods?*

Drawing on the concepts of embeddedness and business relatedness this article aims at enhancing our understanding of divestiture process. We explore the possible impact of divestor's inter-organizational and intra-organizational ties to future divestiture decisions. Firstly, we propose that prior inter-organizational relationships between divesting firm and acquirer lead to higher propensity of divestiture deal between two parties due to partner-specific knowledge during pre-divestiture period. Secondly, we examine the propensity of inter-organizational relationships' creation between parties in post-divestiture period to divested resource characteristics, and more precisely to a level of divested business relatedness to remaining operations.

1. DIVESTITURES

Corporate strategy scholars demonstrated that divestitures are important pathways for growth (Brauer, 2006; Feldman, 2020; Lee & Madhavan, 2010) . They enable to adapt firms' scope and boundaries in face of changing market conditions, and to pursue new strategic orientations with a goal of value creation. Divestitures encompass a reallocation and/or sale of assets, business units, divisions and/or segments by parent firm for value maximization or as a response to internal and external issues (Feldman & McGrath, 2016; Hurry, 1993; Villalonga & Mcgahan, 2005). These modes are used for decreasing diversification level (Moschieri & Mair, 2012), focusing on core activities by eliminating negative synergies (Bergh & Lim, 2008), raising cash for investment or liquidity concerns (Moschieri & Mair, 2012) or responding to legal or regulatory changes (Moschieri & Mair, 2008). Even though, divestitures are often applied to unrelated businesses to core activities of the selling firm (Damaraju, Barney, & Makhija, 2015; Duhaime & Grant, 1984), the legacy businesses, as those which historically be the first businesses the companies operating at the time of the creation can be also divested (Feldman, 2014). In spite of being an effective ways for value-maximization, divestitures also may encounter major difficulties during their implementation for a parent firm leading to decrease in financial performance (Bergh 1995), a subsequent lack of innovation (Hitt, Hoskisson, Johnson, & Moesel, 1996), or even a further liquidation.

In the corporate divestiture literature, only a few scholars study the process of divestitures (Karim & Capron, 2016) and there is a pressing need for developing a sound understanding of the role of distinct management processes that shape the way businesses are divested (Lee & Madhavan, 2010; Moschieri, 2011). The role of time and speed (Thywissen, 2015, 2017), post-deal access and control, experience (Bergh & Lim, 2008; Brauer, Mammen, & Luger, 2017; Kolev, 2016; Shimizu & Hitt, 2005) impact post-divestiture outcomes while the separation from valuable resources may result in disruption of existing interdependencies between remaining ones (Damaraju et al., 2015) and unique forms of collaborative relationships may be formed to support strategic change.

Divestitures include separation from parent firm's current business activities and their transmission to other parties, so by their nature they are multilateral transactions. The selection of an acquirer in pre-divestiture phase or a decision to form an inter-organizational relationship in post-divestiture period might have an impact on the divestiture outcomes. These inter-organizational arrangements were studied in research on mergers & acquisitions, but remain unexplored in divestiture literature (Brauer, 2006; Lee & Madhavan, 2010). Studies on interorganizational relationships illustrated that social embeddedness from prior interactions among firms enhance trust which further modify subsequent outcomes (Gulati & Wang, 2003; Lavie, 2012).Recently, Schilke and Jiang (2019) showed that there exists a link between premerger alliances and divestitures and found that firms creating alliance before mergers are less likely to further divest these activities (Schilke & Jiang, 2019).

Moreover, parent firms might retain links with divested businesses with acquirers to ensure that implementation of the deal is not disruptive to the remaining operations. Newly formed inter-organizational relationships enable to reduce the level of partner opportunism, facilitate the exchange of information, enhance the learning mechanisms (Gulati & Wang, 2003), but also to enable smooth disentanglement reducing the level of stress, fear and uncertainty among employees (Sewing, 2010) in reaction to restructuring. These may affect the employees' motivation; thus, the sense of continuity and legitimacy should be delivered to employees (Defren, Wirtz, & Ullrich, 2012; Moschieri, 2011; Ullrich, Wieseke, & Van Dick, 2005).

2. EMBEDDEDNESS AND RELATEDNESS AS SOURCE OF INTERDEPENDECIES

The main pillar of embeddedness concept lies in the importance of relations that enable to develop economic exchanges and efficient governance in interfirm networks (Granovetter, 1985; Uzzi, 1996) that is leading to beneficial performance outcomes (Gulati, 1999). Over time economic exchanges are becoming more integrated into social relations, which trigger the trust and reciprocity among actors situated in the network (Granovetter, 1985). This effect is multiplied in case of tie repetitions through prior dealings and homophily through similarity

(Walter, Heinrichs, & Walter, 2014). Direct ties or shared ties with the third party enable access to valuable information at less cost (Stuart, 1998).

Businesses have numerous types of interactions (Kessler 2013, p.744) and social relationships along with networks impact firm's behaviours and outcomes. Relational and structural embeddedness formed with the presence of direct and indirect ties respectively (Granovetter, 1985). The role of business interactions was largely investigated in terms of different interfirm relationships (Gulati, 1999; Gulati & Wang, 2003) but remains underexplored in terms of the shift from intra- to inter-organizational ones.

The relatedness concerns the level of existent interdependencies between firms' current divisions (Moschieri & Mair, 2008). Asset relatedness of the main businesses of the firm enable to enhance interrelationships between them and contribute to the development of the competitive advantage in the most cases (Bergh & Lim, 2008; Lee & Madhavan, 2010). The units that are less related to the parent firm activities, especially in resource profiles (Duhaime & Grant, 1984) or that are not related to the firm's core activities (Damaraju, Barney, & Makhija, 2015) are more often divested. It is consistent with Porter's view (1976) on three categories of barriers to exit from business: structural, corporate strategy and managerial barriers. More precisely, corporate strategy's exit barriers combine interrelatedness among the businesses, expressed in the relationship between department, divisions, and units. In case the level of interrelationships is high, the likelihood of divestiture is lower, as it could affect the operations of the remaining units following substantial losses (Porter, 1976).

Despite this taken-for-granted assumption, in the meta-analysis of divestiture and firm performance, Lee and Madhavan (2010) did not find any moderation relationship between the level of the relatedness and post-divestiture performance. However, even the businesses in divesting firm may belong to the same industry, they might have no coherent ties. The management can evaluate the value of these interactions, on the contrary, they cannot be perceived in the same extent from outside, thus it creates information asymmetries (Bergh, Ketchen, Orlandi, Heugens, & Boyd, 2019).

2.1. PRE-DIVESTITURE INTER-ORGANIZATIONAL RELATIONSHIPS

There exist various forms of inter-organizational relationships that may take place between companies prior to divestiture deal. Taking into consideration that firms are not autonomous but are embedded within networks of relationships (Yang, Lin, & Peng, 2011), the inter organizational relationship is the source of information and capabilities among actors. Inter-organizational relationships include executive (Feldman, 2016; Mizruchi, 1996), board interlocks (Zona, Gomez-Mejia, & Withers, 2018), and alliances. Interlocking directors are serving as communication mechanisms (Mizruchi, 1996), that transfer information and capabilities. Executive or board interlocks occur when person affiliated in the one organization sits on the board of directors or serve as an executive in another organization, by enabling to exercise the monitoring and control function, provide legitimacy and signals and act as “boundary spanner”. The board interlocks were studied through the lenses of agency, resource dependency (Pfeffer & Salancik, 1978) and managerial power theory. The context of the executive presence on several boards may impact the performance, more precisely the nature of relationships both firms have buyer/supplier, being a part of one platform ecosystem, or spin-offs, etc. For example, Feldman (2016) showed that the dual directors have a positive impact on the parent and divested firm performance, but the impact on the performance on the spin-off is rather negative if there is an ongoing sale relationship between two (Feldman, 2016).

Alliance is another form of inter-organizational relationships. Alliance in the past brings information, trust in the dyadic level and leads to more likelihood of both alliances and acquisitions between firms, but not vice versa: the acquisition between two firms in the past is not leading to an alliance between them in the future. Therefore, taking into consideration that the sustained links enable divested activity to access the social networks (Hernandez, 2016; Wiedner & Mantere, 2018) and the ability of firms to acquire more general knowledge about transactions from inter-organizational relationships, we propose that for different types of divestiture the prior inter-organizational collaborative relationships between divesting and acquiring firms prior to the divestiture deal is positively associated with dyadic resource exchange and combination.

Then, a learning view suggests that firms that have gained experience with different modes of reconfiguration have constructed reconfiguration skills (Zollo & Winter, 2003). For instance, alliance experience improves abilities of screening and selection of partners, contract design and management, complex coordination (Kale, Dyer, & Singh, 2002). Respectively, divestiture experience increases the firms’ abilities of buyers selection and coordination of divested activities (Brauer, Mammen, & Luger, 2017). The literature on relational capabilities proposed that the firms tend to learn from past experiences with specific type of inter-organizational relationships and tend to pursue the same type in the future and that the choice to enter an alliance is also dependent on the embeddedness of firms into the prior alliances, also it influences the frequency with which these alliances are formed. They have also shown that the management capabilities of such partnerships are not significant compared to the experience, because of developed administrative control procedures (Gulati, 1999). But according to Wang and Zajac (2007) firm with higher alliance activity might be more active in divestiture deals. The alliances are those form of interfirm relationships that are more "versatile" because provides both specific pieces of knowledge about the exact type, but also general knowledge about different interfirm combinations (Wang & Zajac, 2007). The choice of reconfiguration modes depends on the properties of the firm's resources. The choice among alternative governance structures, be it alliances and acquisitions by investigating by relying on the resource-based view and knowledge-based view the dyadic factors and characteristics of both firms, such as resources' similarity and complementarity, combined relational capabilities and partner-specific knowledge. In the case of high resource similarity firms tend to pursue acquisitions, in the case of complementarity – alliances. The combined alliance capabilities are associated with both alliance and acquisition, because the knowledge with one type of interfirm experience may be transferred to another one. However, the effect of the alliance capabilities was a stronger trigger for further alliance formation. In the meantime, combined acquisition capabilities favour acquisition creation, but are found to be insufficient for the creation of an alliance due to the presence of continuous interaction in alliances and finished after the deal for acquisitions. There are two different forms of knowledge for interfirm resource combinations: general knowledge applied to different types of relationships and specific knowledge applied to one type: alliances are those that provide more general knowledge in addition to specific knowledge (Wang & Zajac, 2007). Thus, not just the knowledge of the buyer can lead the divestor to sell its assets to this specific acquirer, but also general knowledge of alliance formation can lead to future divestiture deals. The prior inter-organisational relationships between divestors and acquirers create knowledge networks and experiences, whereas absorptive capacity is formed. Firm's prior level of related knowledge gives a capability to seize information from external environment (Cohen & Levinthal, 1990). Therefore, divestor is having a capacity to recognize the potential acquirer of businesses-to be divested.

Proposition 1: Prior inter-organizational relationships between divestor and buyer lead to higher propensity of divestiture deal between two parties.

2.2. POST-DIVESTITURE INTER-ORGANISATIONAL RELATIONSHIPS

A corporate divestiture allows to separate some activities from the firm's portfolios, but simultaneously retain an access to divested entities. It allows to ensure that divestiture implementation is leading to desired outcome. The disentanglement can be problematic due to a high level of historical interdependence between actors (Wiedner & Mantere, 2018) and previously existing ties between divestor and divested activity are hard to abandon (Feldman, 2016; Moschieri & Mair, 2012). For instance, during spin-offs dual directors (Feldman, 2016), continued ownership and board member from the parent (Semadeni & Cannella, 2011) are methods to preserve links between parent firm and spun-off entity. The maintained relationships after divestiture enable access to innovation and resources which triggered better performance outcomes (Moschieri & Mair, 2012). However, the performance implications may be devasting (Semadeni & Cannella, 2011), especially in the case of the influence of more powerful divestors (Walter et al., 2014). Post-divestiture cooperation and support from the parent was studied for spinouts and spin-offs but remains unrecognized for other divestiture types, like sell-offs.

The sale of assets is often a result of refocusing strategy (Brauer, 2006; Johnson, 1996) and is associated with the loss of access to resources (Moschieri, 2011). However, parent firm can retain the relationship with divested business in post-divestiture period. The benefits of maintained relationship include an increase in divested unit performance (Semadeni & Cannella, 2011), a decrease of contracting and coordination cost (Ito, 1995), and a facilitation of innovation development (Moschieri & Mair, 2011).

Control, moral, value creation or hedging reasons are cited as the motives to retain a parent-divested units' relationship. Control reason is highly important if the technologies, patents, brand image and investments of the parent company are still present in the divested unit. The support of the divested unit enables its proper operations, continuity, and legitimacy of divested businesses. In terms of value creation logics, the further relationships can enable the parent company to access innovations and knowledge produced in divested business and during their assessment to perform proactive management of the corporate portfolio, as reacquisition of business lines in case it brings additional value to the parent company. Then, hedging strategies help to prevent the behaviour of the divested unit as a new competitor and to react in case of threat of takeover with the acquisition of business lines (Moschieri & Mair, 2012). In divestiture setting, inter-organisational relationships include outsourcing contracts, commercial agreements or dual board membership (Moschieri & Mair, 2012). These actions favour reacquisitions (Damaraju et al., 2015), continuous access to the knowledge produces in carve-out entity (Moschieri & Mair, 2012), delivering sense of continuity and legitimacy to employees (Moschieri, 2011). These inter-organizational links in post-divestiture period provide acquirers and divestors with ability to pool specific assets, knowledge-sharing, complementary resources and capabilities and effective governance (Dyer & Singh, 1998), and to ensure the steady divestiture's separation process. Moreover, the maintenance of the relationship for divestor enables to decrease the costs by using the shared functions that were previously also provided to divested activities (Porter, 1998). Besides, the separation of distinct organizational entities with its concurrent maintenance during divestitures is facilitated by respect and communication leading to autonomy development (Wiedner and Mantere 2018).

The creation of various inter-organizational relationships with the acquirer after the divestiture may be explained by the attachment to these legacy businesses (Capron & Mitchell, 2012). Feldman (2013) researched the divestitures of legacy businesses, like those which historically be the first businesses the companies operated at the time of the creation. The legacy businesses comprise the set of key organizational routines, that are created in a path-dependent manner, therefore should involve the considerable interdependencies with the other firm's businesses (Feldman, 2014). Leonard-Barton (1992) studied the core capabilities in terms of new product development. He defined core capabilities as "part of an organization's taken for granted reality, which is an accretion of decisions made over time and events in corporate history". As the firms tend to pursue the path-dependent development, they apply the tacit knowledge and organizational routines from a firm's established businesses to the other business units: this application of the knowledge is thus resulting in the generation of significant interdependencies (Leonard-Barton, 1992). Therefore, the divestiture of highly embedded and taken for granted business may cause the disruption of the functioning in the remaining parent firm operations. The higher the complexity of a divestiture of highly related businesses requires more time and managerial attention.

Proposition 2: The higher the business relatedness between divested activity and remaining operations, the higher the propensity of creating of inter-organizational relationships between divestor and buyer in post-divestiture period.

DISCUSSION

The previous discussion examines the inter-organizational relationships in pre- and post-divestiture periods. Central to the framework the notions of embeddedness of the divestor firm regarding its inter-organizational relationships and the notion of relatedness of the business to-be-divested to the remaining operations. Taking into considerations that firms are embedded in various social and economic networks, their divestiture decisions may be thus impacted by prior inter-organizational relationships. For instance, the information availability from the existing inter-organizational network may lead to the choice of specific buyer for divestor's former assets. The transaction costs might be reduced due to simpler negotiation and coordination during divestiture process among parties. Then, the nature of assets-to-be sold, more specifically their interdependence with remaining operations that is often a source of intra-relatedness can lead to the creation of the linkages between divestor and the buyer in post-divestiture period. Several benefits of the inter-organizational relationships after divestiture deal include the smoother separation and preserved access to divested activities leading to better performance and innovation sourcing.

This framework implied two proposition that require testing. The challenge lies in observing the network changes and identifying measures of embeddedness and relatedness. Social network analysis is actively used approach to seize the embeddedness concept. Similarities in location, membership, attributes, interaction and flows are the types of ties studied in social network analysis (Borgatti, Mehra, Brass, & Labianca, 2009). Meanwhile, standard industrial classification codes are the most common measure of business relatedness in strategic management literature (Robins & Wiersema, 1995). Also, similarity among resources, technologies and processes was assessed by similarity in product-market attributes (Bergh, 1995), resource attributes (Montgomery, 1982; Montgomery, Thomas, & Kamath, 1984), value chain attributes (Tsai, 2000; Tsai & Ghoshal, 1998). However, concept of relatedness being multidimensional should include more integrative measures (Pehrsson, 2006). A more complex investigation of the relatedness is needed: share of the same patents among the businesses, customer base, supply chain components. These might be theorised based on social processes observation with the use of qualitative approaches (Gehman et al., 2018).

The framework shows that managers should take into consideration the links between the network embeddedness and business relatedness while considering divestiture deals. These may inform about best owners on the marketplace for the assets to-be-divested, but also about new inter-organizational arrangement in post-sale period.

In conclusion, divestitures have been proved to be actively used by practitioners for value-maximization in multi-business firms but remain relatively underexplored area in scientific literature. This framework should be a starting point to explore the possible impact that networks, including board, executive interlocks and alliances, might have on divesting firms.

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