Effects of Financial Distress Condition on the Company Performance: A Malaysian Perspective

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Abstract: This study was aim to assess the performance of Malaysian companies after suffering from a financial distress condition. Many companies post abnormal profits during their first few years, but the profits are not sustainable. So they face another restructuring petition or face winding up completely. To be able to show positive results after emergence, companies must improve their performance compared to previous financial results which led to downturn. The performance of companies emerging from a distress condition was assessed by the improvement of stock prices and other financial ratios that indicated the company is performing better compared to pre-bankruptcy period. This is a qualitative study where data collected from Bursa Saham Malaysia. The results show that company performance (ROE, EBIT/TA, EPS), successful company reorganisation, and management change affect stock prices positively. Whereas, the performance of second distress condition companies affect stock price performance negatively.

JEL **Classifications:** G1; G11; M1; M10
Keywords: Stock price, Return on equity ratio, Earning per share

1. Introduction

The Asian financial crisis in 1997 caused massive restructuring in many Malaysian companies. On 14 July 1997 the Malaysian central bank announced that it could no longer defend the Malaysian Ringgit. For the six month period to 31st December 1997 the Malaysian ringgit had devalued by almost 50%. Also on the Malaysia's stock market there was a decline of 54% for the six month period ended 31st December 1997 creating a severe effect on country's economy. The Asian financial crisis in 1997-1998 affected Indonesia, Korea, Malaysia, and Thailand the most. There were different causes which had contributed to the crisis in these countries. At the same time, there are features common to all of them. In Malaysia, private debt played a big role, principally by companies whose shares are listed for trading on the Bursa Malaysia (Kuala Lumpur Stock Exchange (KLSE) at that time caused distress to the banking system, which triggered the collapse from July 1997. A very large proportion of such debt was corporate debt, principally borrowings by public companies listed on the KLSE

which was largely affected in 1998. Due to many companies defaulting on their private debt and failing to meet their obligations, the Bursa Malaysia Berhad introduced Practise Note 4/2001 (PN4) paragraph 8.14 with effect from 15th of February 2001. It has classified the distressed companies under PN4 which refers to listed companies who are in poor financial condition and who are required by Bursa Malaysia to provide proposals to restructure or revive the company.

The purpose of this study was to assess the performance of Malaysian companies after suffering from financial distress condition. The performance of companies emerging from a distress condition was assessed by the improvement of stock prices and other financial ratios indicated that the company was performing better compared to pre-bankruptcy period. Most researches have shown that the companies emerging from bankruptcy show abnormal profits, but there are contradicting researches such as that of Hotchkiss (1995) which shows poor performance post-bankruptcy.

2. Literature Review

2.1 Post-Bankruptcy Performance

Eberhart *et al* (1998) and Sandler & Lowenstein (1991) suggested that investors do invest in companies that have been bankrupt before. These studies have shown that the equity performance of a company emerged from bankruptcy is positive. They assessed that the stock return performance of 131 firms emerging from Chapter 11. Using differing estimates of expected returns, their study consistently find evidence of large positive excess returns in 200 days following emergence. Whereas, Hotchkiss (1995) suggested that post bankruptcy performance is poor because accounting performance is weak, debt ratios are high and further debt restructuring is frequently required. He examined the performance of 197 public companies that emerged from Chapter 11, her study finds over 40% of the sample firms continue to experience operating losses in the three years following bankruptcy, and 32% re-enter bankruptcy or privately restructure their debt. Ahmad & Hamzah (2008) supports Hotchkiss in their study of Malaysian companies' share price performance after they are removed from the PN4 classification (Practice Note 4 in Bursa Malaysia).

Alderson and Betker (1999) concluded that firms neither under nor over perform following bankruptcy after examining the post-bankruptcy performance of 89 firms by evaluating the total cash flows produced by the firm's assets for the five years after emerging from bankruptcy. Altman *et al* (2009) analysed whether one could predict which firms emerging from bankruptcy are more likely to suffer subsequent problems and file again under "Chapter 22.". Using the Z"-Score distress prediction model, they found that those firms that filed a subsequent bankruptcy petition had a significantly worse financial profile than did a sample of firms which emerged as a going concern and continued in that condition. Firms which file for bankruptcy a second time emerged as significantly less profitable with significantly more leverage than those that emerge and remain as going concerns.

2.2 Financial Distress Models

The financial distress models predicted that the financial failure of a business before it actually happened. Bankruptcy prediction models are useful to the stakeholders of a company in analysing the performance of the company after emerging from a bankruptcy or distress condition. Altman (1968) attempted to assess the issue; the quality of ratio analysis as an analytical technique with a set of financial and economic ratios to be investigated. The discriminant-ratio model proved to be extremely accurate in predicting bankruptcy correctly in 94% of the initial sample with 95% of all firms in the bankrupt and non-bankrupt groups assigned to their actual group classification. Also, Kaminski *et al* (2004) provide empirical evidence of the limited ability of financial ratios to detect and/or predict fraudulent financial reporting. Also, Appiah & Abor (2009) assessed the usefulness of financial ratios together with a suitable Z-score model using multiple discriminant analysis (MDA) and then applying it in order to measure the financial health and the risk of failure of UK manufacturing, distinguishing between failed and non-failed companies. In a study of 86 listed UK companies that filed for

bankruptcy in the period 1977 to 1983, it was found that only 21 of these companies (i.e. slightly less than 25%) were qualified on a going concern basis in their last financial statement prior to bankruptcy (Taffler and Tsueng, 1984). Raghunandan and Rama (1995) reported that only 90 (i.e. 51%) of their sample of 195 US bankrupt companies were qualified on a going concern basis prior to bankruptcy (Koh & Low, 2004).

2.3 Restructuring Plan

Eberhart *et al* (1998) reported that publicly traded reorganised firms produce abnormally high ordinary shares returns. Most companies perform a corporate restructuring of their organisations and cancel the old stocks and issue new common stocks. When the performance of a company shows a strong and stable condition after emergence, it gives good impression on shareholders and it is a valuable tool in determining the ability of a distressed company to be able to turn around and continuing doing business, (Kuruppu *et al* 2003, Koh & Low 2004). Furrer *et al* (2005) in their study, finds that the beta excess return measures captured the hypothesized relationships between strategy and shareholder value for the sample firms studied. Smith & Graves (2005) suggested that several stakeholders would be interested in a model that could identify distressed companies that have recovery potential. Francis & Desai (2005) and Smith & Graves's (2005) analysis of the results reveals that successful turnarounds are associated with the severity of the distressed state. Dawley *et al* (2003) pointed out that, companies' when filing for bankruptcy, first they can request time to formulated a reorganisation plan with intent of continuing business can turn over control of the organisation's assets to court appointed trustee who sell the assets and distribute funds to creditors (Chapter 7, Liquidation).

Lin *et al* (2008) finds that delisting risk for companies listed in the Stock Exchange increases when companies undertake repetitive reorganisations, huge employee reductions, and large-scale asset downsizing. Betker (2000) pointed out that the efficient bankruptcy system should assist the liquidation of bad companies and allowed good companies to continue operations under the chapter 11, which allow them to reorganise their debts and restructure the organisation. Heron *et al* (2008) finds in their study that when emerging from a Chapter 11 reorganisation, they substantially reduce their debt burden, but yet they emerge with higher debt ratios than what is typical in their respective industries. Heron *et al* (2008) also find that firms that reported positive operating income leading up to Chapter 11 emerge faster, suggesting that it is quicker to solve financial distress than economic distress.

2.4 Management as a Cause of Failure

Ooghe & Prijcker (2008) pointed out the causes of corporate failures or bankruptcy to be the characteristics of management e.g. inappropriate management qualities and skills, and corporate policy and poor strategies. Scherrer (2003) noted that often management does not recognise the internal signals of failure and blame external changes for their business's decline. Hotchkiss (1995), examined the relationship between management changes and post-bankruptcy performance. Over 40% out of 197 public companies that emerged from Chapter 11 between 1979 and 1988 continued to experience operating losses in three years following bankruptcy, 32% re-enter bankruptcy or privately restructure their debt. Hotchkiss (1995) suggested that the continued involvement of pre-bankruptcy management in the restructuring process is strongly associated with poor post-bankruptcy performance. Her results show that retaining pre-bankruptcy management is strongly related to worse post-bankruptcy performance. Her findings were in contrast with that of Eberhart *et al* (1998) who used 131 companies emerging from Chapter 11 during 1980 to 1993 and found large positive excess returns up to 200 days following the emergence. Dawley *et al* (2003) suggested that because of slack resources, larger companies should have a greater probability of surviving bankruptcy and they should have shorter recovery times from bankruptcy than smaller companies. Dawley *et al* (2003) studied on the effect of organizational size on the relationship between type of diversification strategy and post-bankruptcy performance outcomes. This found out that size would affect probability of recovery and

recovery time from a Chapter 11 filing. Francis & Desai (2005) supported this argument that factors such as the urgency and severity of decline, firm productivity and the availability of slack resources, and firm retrenchment can determine the ability of companies to turnaround.

3. Methodology

3.1 Data Collection

This study was conducted primarily using secondary data. Financial data of the selected samples were extracted from the published annual reports obtained from the Bursa Malaysia's announcement section and the respective companies' websites. The period of analysis in this study covers two financial years following the date of reclassification back into the normal listings as a listed company not under Practice Note (PN4, PN17 or Amended PN17), this means after coming out of the PN classification. The years will be marked as Yr1 and Yr2 respectively, indicating that Yr1 is the immediate full financial year following reclassification out of Practice Note followed by Yr2 in order to observe the overall performance after whole financial year has gone by. The sample selection process was conducted using the following guidelines:

a) The exited company was classified as affected listed company mainly due to deterioration in its financial condition as from the date PN4 was introduced in 2001.

b) The exited company must be listed on Bursa Malaysia Securities for a period of at least two years after the date of reclassification into the normal listings, in order to ensure the necessary financial information after reclassification is available for analysis. Exited company must have continuous financial data available for two years after coming out of the PN classification.

c) In order to avoid repetition or duplication of samples into the selection, the study took the first class under which the company was classified; for example, if the company was first classified under PN4 and later under PN17 or Amended PN17, the study will take the first PN4 classification as sample.

d) The exited company's stock must remain active for trading on the Bursa Malaysia and not suspended for at least two years after reclassification into normal listings in order to determine the performance of stocks in the stock exchange after the distress condition.

3.2 Research Framework and Hypotheses Development

The performance of Malaysian companies emerging from a distress condition will be assessed by the improvement of stock prices and other financial ratios that will indicate the company is performing better compared to pre-distressed period. Some US and other European companies have reorganise successfully and emerge stronger, but Malaysian companies have been different from those of the US and other European countries by showing poor performances during post-bankruptcy and forced them to wind up, a study by Ahmad & Hamzah(2008) has shown. Therefore, this study will test the following hypotheses:

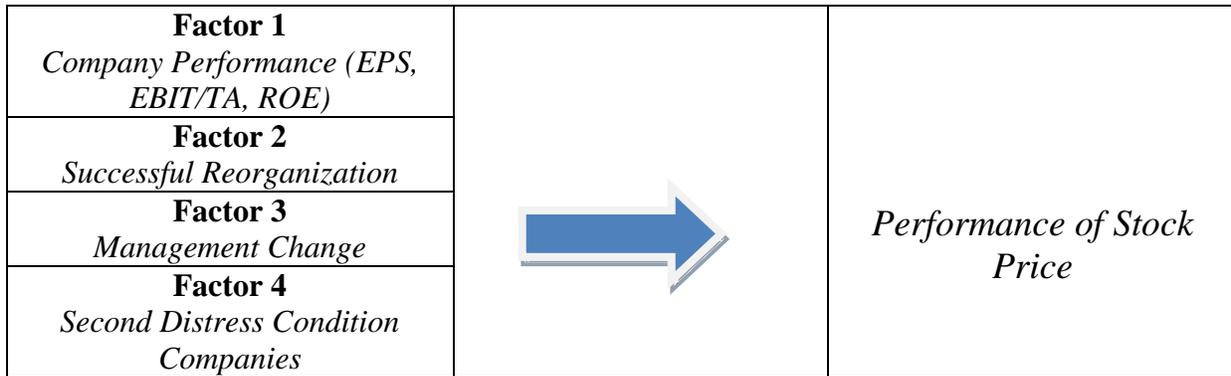*H1: Higher EPS, EBIT/TA and ROE are positively related to performance of stock price*
H2: Successful company reorganisation is positively related to performance of stock price
H3: Management change is positively impacting performance of stock price
H4: Former distressed companies are likely to fall into a second distress condition and this will impact negatively on stock price performance

All these hypotheses are from the idea that company performance, successful reorganization, management change and second distress conditions are the four key factors to the performance of stock price. This idea to be tested is also shown in the chart 1 on the next page.

Chart 1 The relationship between ROE, EBIT/TA, EPS and stock price

Factor 1 *Company Performance (EPS, EBIT/TA, ROE)*		
Factor 2 *Successful Reorganization*		*Performance of Stock Price*
Factor 3 *Management Change*		
Factor 4 *Second Distress Condition Companies*		

Source: Appiah & Abo1r (2009); Ooghe & Prijcker (2008); Heron *et al* (2008); Ahmad & Hamzah (2008)

4. Findings and Discussions

In this study, Z-score is used as a measurement of financial health of companies involved and also, as a predictor of second financial distress condition.

The classic Z-Score Model (Altman (1968)) is specified as

$$Z = 1.2 \, X_1 + 1.4 \, X_2 + 3.3 \, X_3 + 0.6 \, X_4 + 1.0 \, X_5$$

Where: X_1 = working capital/total assets

X_2 = retained earnings/total assets

X_3 = earnings before interest and taxes/total assets

X_4 = market value of equity/book value of total liabilities

X_5 = sales/total assets

Z = overall Index

Companies with a Z-score of greater than 2.99 clearly fall into the "non-bankrupt" sector, while those firms with a Z-score below 1.81 are all going to be bankrupt. The area between 1.81 and 2.99 will be defined as the "zone of ignorance" or "grey area".

Where: 3.0 or higher indicates that bankruptcy is not likely.

2.71 to 2.99 indicates possibility of bankruptcy.

1.81 to 2.70 indicates a high probability of bankruptcy. ⎫ Zone of Ignorance

1.8 or less indicates a very high probability of bankruptcy.

The linear discriminate analysis for companies with different Z-scores is illustrated in figure 1 on the next page.
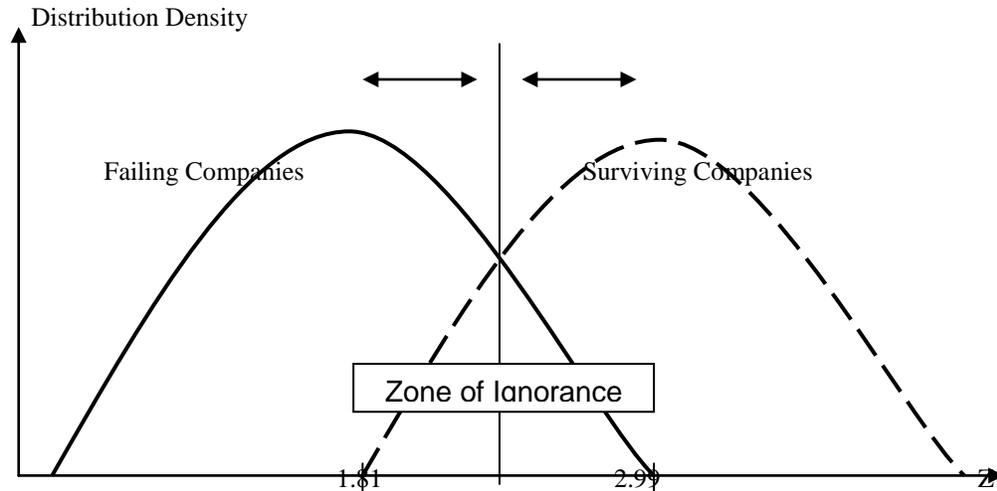
Figure 1. Linear discriminate analysis (*Source:* Pogue(2008))

4.1 Results of Altman's Z-Score

The Z-Score Model: $Z = 1.2\,X_1 + 1.4\,X_2 + 3.3\,X_3 + 0.6\,X_4 + 1.0\,X_5$

Year 1:

$1.79 = 1.2 \times 0.183 + 1.4 \times (-0.226) + 3.3 \times 0.064 + 0.6 \times 1.604 + 1.0 \times 0.714$

Year 2:

$1.68 = 1.2 \times 0.165 + 1.4 \times (-0.249) + 3.3 \times 0.037 + 0.6 \times 1.584 + 1.0 \times 0.761$

The overall Z-score for Yr1 is 1.79 and for Yr2 is 1.68, this suggests that the companies have performed poorly after their emergence from a PN classification. The results of this study are consistent with Hotchkiss (1995) who suggest that post bankruptcy performance is poor because accounting performance is weak, debt ratios are high and further debt restructuring is frequently required. She examines the performance of 197 public companies that emerged from Chapter 11, her study finds over 40% of the sample firms continue to experience operating losses in the three years following bankruptcy, and 32% re-enter bankruptcy or privately restructure their debt. This study shows that 51.1% of companies' Z-score decreased from Yr1 to Yr2, and 42.2% of companies Z-score increased from Yr1 to Yr2, only 6.7% of companies show no difference between the two years (see appendix 4b). From initial sample, 4 companies which exited from PN4 Classification have been de-listed and went into private restructuring; one company's shares are frozen from trading in the Bursa Malaysia until further restructurings. Ahmad & Hamzah (2008) supports Hotchkiss in their study of Malaysian companies' share price performance after they are removed from the PN4 classification, they also concluded there are large, negative abnormal returns in 200 days following emergence from PN4. The findings are opposite compared to the results in the US which have shown positive abnormal returns for companies emerging from financial distress.

The findings of this study compliments Hotchkiss (1995) and Ahmad & Hamzah (2008). The study found that 64.4% of companies have a Z-score of 1.8 or lower which is a very high probability of bankruptcy (see appendix 4a), 15.6% of companies have a Z-score between 1.81 and 2.70 which indicates a high probability of bankruptcy, just 2.2% of companies have a Z-score between 2.71 and 2.99 which indicates possible bankruptcy, and 17.8% of companies emerged from the distress condition have shown a Z-score of 3.0 and above which indicates that bankruptcy is not likely. Also, other studies such as Alderson and Betker (1999) concluded that firms neither under nor over perform

following bankruptcy after examining the post-bankruptcy performance of 89 firms by evaluating the total cash flows produced by the firm's assets for the five years after emerging from bankruptcy. But this is not the case in most studies, as this study has show that either the companies perform or underperform. For Malaysian companies, this study has shown that a successful reorganisation is required in order to emerge with a stronger company that can be able to sustain tough economic conditions.

4.2 Results of Hypotheses Test

Hypothesis 1: Performance (EPS, EBIT/TA and ROE) is positively related to performance of stock price

<p align="center">**Table 1** Pearson correlations</p>

		Stock price	Mn performance
Stock price	Pearson Correlation	1	0.441[**]
	Sig. (2-tailed)	45	0.002
	N		45
Mn performnace	Pearson Correlation	0.441[**]	1
	Sig. (2-tailed)	0.002	
	N	45	45

**. Correlation is significant at the 0.01 level (2-tailed).

As table 1 shown, performance is positively related to stock price. Stock price has shown relationship to performance because there is a positive correlation of 0.441 at a significant level of 0.01; this means that there is a significant relationship exists between performance of EPS, EBIT/TA, ROE and stock performance. Therefore, hypothesis 1 is accepted.

Hypothesis 2:   Successful company reorganisation is positively related to performance of stock price
<p align="center">**Table 2** Descriptive statistics for Hypothesis 2</p>

	N	Minimum	Maximum	Mean	Std. Deviation
ROE growth	45	-1.37	0.93	-0.0072	0.29627
EBIT/TA growth	45	-0.19	0.32	0.0273	0.08996
EPS growth	45	-32.30	48.83	1.8151	11.68887
Valid N (list wise)	45				

Successful reorganisation is partially significant to Stock price due to EBIT/TA and EPS are positively improved but not for ROE. Growth for ROE shows a negative mean of -0.0072 and growth for EBIT/TA and EPS have positive means of 0.0273 and 1.8151 respectively. So we should accept partial hypothesis 2 because two variables show positive impact and only one variable show negative impact.

Hypothesis 3: Management change has a significant impact on company's performance

The ANOVA table on Table 3 indicates analysis of variance. The first model regress the ROE on company performance and the second model is running on the ROE, management change and EBIT that regress on company performance.

Table 3 Analysis of variance (ANOVA)

	Model	Sum of Squares	d. f.	Mean Square	F	Sig.
1	Regression	149.395	1	149.395	88.722	0.000[a]
	Residual	72.406	43	1.684		
	Total	221.801	44			
2	Regression	168.627	2	84.313	66.596	0.000[b]
	Residual	53.174	42	1.266		
	Total	221.801	44			

a. Predictors: (Constant), ROE

b. Predictors: (Constant), ROE, Dummy

c. Dependent Variable: mnperformance

According to Table 4 below, the model summary shows that model 2 with the consideration of management change would improve the R^2 value from 67% to 75% where it contributes to 8% impact stock preformance. Therefore, the result illustrates the impact of management change towards the improvement of company performance statistically.

Table 4 Model summary

					Change Statistics				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	R Square Change	F Change	df1	df2	Sig. F Change
1	.821[a]	.674	.666	1.29764	.674	88.722	1	43	.000
2	.872[b]	.760	.749	1.12519	.087	15.190	1	42	.000

a. Predictors: (Constant), ROE

b. Predictors: (Constant), ROE, Dummy

The coefficients table on Table 5 below further supports the formulation of regression model which should be constructed with the manner:

Company performance = 0.018 + 10.918ROE + 17.625ManageChange*EBIT + error
R^2 = 76%.

Table 5 Coefficients

		Unstandardized Coefficients		Standardized Coefficients		
	Model	B	Std. Error	Beta	t	Sig.
1	(Constant)	0.776	0.218		3.554	0.001
	ROE	17.015	1.806	0.821	9.419	0.000
2	(Constant)	0.018	.271		0.065	0.948
	ROE	10.918	2.214	0.527	4.931	0.000
	Dummy	17.625	4.523	0.416	3.897	0.000

a. Dependent Variable: mnperformance

Hypothesis 4: Former distressed companies are likely to fall into a second distress condition and this will impact negatively on stock price performance

Table 6 One-sample statistics

	N	Mean	Std. Deviation	Std. Error Mean
Z1	45	1.7916	1.77957	0.26528
Z2	45	1.6829	2.18286	0.32540

Table 7 One-sample test

	Test Value = 0					
					95% Confidence Interval of the Difference	
	t	df	Sig. (2-tailed)	Mean Difference	Lower	Upper
Z1	6.753	44	0.000	1.79156	1.2569	2.3262
Z2	5.172	44	0.000	1.68289	1.0271	2.3387

The T-test for hypothesis 4 in table 7 shows the mean difference is 1.79156 and 1.68289 for Z1 (Z-score for year 1) and Z2 (Z-score for year 2) respectively. This indicates that the Z-score has dropped from 1.79156 in year 1 to 1.68289 in year 2. So if there is a drop in Z-score which is the indicator of the financial health of the company, it means that companies are likely to fall into a second financial distress condition. So we should accept null hypothesis 4 that former distressed companies are likely to fall into a second distress condition. Therefore, we can conclude that former distressed companies are likely to fall into a second distress condition and this will impact negatively on stock price performance.

4.3 Z-score Results

The Altman's Z-score has been an important tool in determining the financial health of a company. For this study, it has shown that the financial health of some of the companies was weak and very few which were healthy as they emerge from a financial distress condition. As this study discuss, this may be due to a number reasons which were ultimately down to how the companies reorganise themselves in the period when they were under the restructuring plan.

The Z-score of 1.79 for the first year and 1.68 for the second year from emergence shows that according to Altman, they indicate a very high probability of bankruptcy because they fall under the Z-score of 1.80 as an indicator. The low Z-score may be due to increased losses or reduced profits. The retained earnings of company may be depleted because of a series of losses year after year and turn them into accumulated losses. Only 9 companies (20% of the sample) have shown positive retained earnings in the period of two years right after emergence from the PN classification (see appendix 5). Only 3 companies (6.7%) had a mixture retained earnings and accumulated losses, and the rest of the 33 companies (73.3%) have shown accumulated losses. Out of the entire sample, only 15.6% of companies had an increase in retained earnings from the first year to the second year, 6.7% have seen their retained earnings reduced between the two years. In accumulated losses, 28.9% of companies have seen their accumulated losses keep getting deeper and deeper, this may be due the increase in expenses in their operations and reduced sales due to low demand caused by the global economic downturn, but 48.9% have tried to reduce their accumulated losses.

The earnings before interest and tax (EBIT) also contributed to low Z-score because the companies are not generating enough operating profits to be able to finance their finances such as financial costs (interest payments). 62.2% of companies have reduced EBIT since the first year, and

only 37.8% show an increase in EBIT (see appendix 6). The profit after tax also has shown a decrease of 53.3% of the sample. This may lead to companies seeking to acquire more debt in order to refinance their finances. As this study had find out that 55.6% of companies had their total debt increased between the first and the second year causing the companies to be in more debt than before. Ultimately, the increase of total debt will contribute to company's failure because when the financial obligations are due to be paid and there is no enough money to pay that is when the company will fall into a financial distress condition.

H1: Performance EPS, EBIT/TA and ROE are positively related to performance of stock price

The test results for hypothesis 1 have shown that we accept the hypothesis 1. Performance is positively related to stock price. Stock price has shown positive relationship to performance because there is a positive correlation of 0.441 at a significant level of 0.01; this means that there is significant correlation at 99%. This is a strong correlation considering ROE, EBIT and EPS were used to test the hypothesis. This shows that these ratios are good indicators of performance as figure 2 have shown below. This graph figure 2 shows how stock price moves in relation to performance over a period of years. Even though, EBIT/TA (Earnings before Interest and Tax / Total Assets) shows a drop, other variables show slight increase. This drop is caused by companies which have lower or negative EBIT/TA for Yr1 and Yr2. This could be made by other factors such as high expenses for that year, but the overall performance is looking good. Take a look at EPS (Earnings per Share), EBIT/TA (Earnings before Interest and Tax / Total Assets) and ROE (Return on Equity), they all show an improvement from Yr1 to Yr2, That is why, there is also a slight increase in stock prices from 0.79 in Yr1 to o.80 this shows as performance increase, which is measure by EPS, EBIT/TA and ROE ratios; it has an impact on stock prices as well. Investors check the financial highlights of the company and make decisions to buy the stock if the performance was positive, thus, increase the price of stock.

H2: Successful reorganisation is significantly related to positive performance

The results for hypothesis 2 testing have shown that successful reorganisation is partially significant to Stock price due to EBIT and EPS are positively improved but not for ROE. Growth for ROE shows a negative mean of -0.0072 and growth for EBIT and EPS have positive means of 0.0273 and 1.8151 respectively. EBIT and EPS have shown positive improvement relative to ROE. If earnings are negative, that is if companies are making losses, there will be a negative ROE. From this study, ROE did not improve much in the second year compared to first year. Some companies had made losses, thus negative earnings, therefore contributed to negative ROE. Strong earnings growth may be accounted by efficient sales and high profit margin strategy. For example, between 1998 and 2003, Dell Computer's highly efficient direct sales and high profit-margin strategy paid off in terms of strong earnings growth and a double-digit ROE of 46%. During that same period Dell shares soared 91.95% raining money on shareholders (InvestmentU.com). The only way this ratio can stay high or increase is by maintaining or increasing the bottom line, net income through good management, which is why ROE is a good indicator of management effectiveness. In order to improve ROE, companies need at least the following, higher sales, wider margins on sales, more and cheaper leverage, and lower taxes.

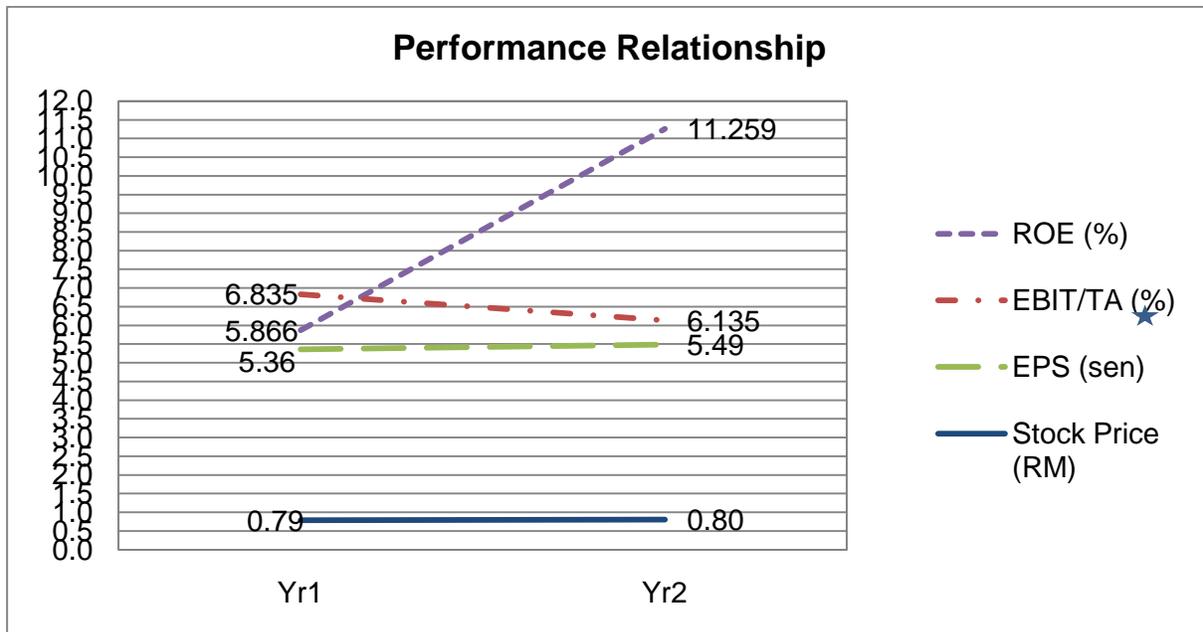### *H3: Management change has a significant impact on company's performance*

The results of Hypothesis 3 from Figures 5a to 5c have shown significant results. It is shown from the model summary results the model 2 with the consideration of management change would improve the R^2 value from 67.4% to 76% with significant improvement of 8.6%. Therefore, the result shows the impact of management change towards the improvement of company performance statistically. When there are management changes in the company which was suffering from a distress condition, the performance will improve. This is because new management team will bring in new ideas and strategies to improve the company and ultimately improve performance. This study compliments

Hotchkiss 1995 that management changes affect the post-bankruptcy performance. Poor management and negligence can lead to poor performance and ultimately bankruptcy. For example, in May 2007, Transmile Group Bhd, a Malaysian global aviation company, its shares drop massively after the announcement by Auditors of unreliable financial results due accounting fraud of overstating profits up to RM530 million. The Securities Commission had charged three former executives of Transmile Group Bhd, including its founder, with giving misleading financial statements (Wikipedia). Perhaps, two of the biggest cases at the time involving accounting fraud were Enron in 2001 followed by WorldCom 2002, all file for Chapter 11 Bankruptcy. Enron's fall started after it was revealed that much of its profits and revenue were the result of deals with Special Purpose Entities, which were one of the main tools used by executives at Enron, in order to hide losses and fabricate earnings, many of Enron's debts and the losses that it suffered were not reported in its financial statements. Also Enron executives were involved in Insider Trading when the company was going down; they sell their shares quickly before the company collapsed. In WorldCom, the executives used fraudulent accounting methods such as inflating sales and bogus accounting entries, to cover its declining earnings by showing a false picture of its financial growth and profitability in order to shoot up the stock price of WorldCom (Wikipedia). Today, Lehman Brothers had surpassed Enron and WorldCom as the largest collapse in history.

H4: *Former distressed companies are likely to fall into a second distress condition and this will impact negatively on stock price performance*

The results for T-test in hypothesis 4 has shown the mean difference is 1.79156 and 1.68289 for Z1 (Z-score for year 1) and Z2 (Z-score for year 2) respectively. This indicates that the Z-score has dropped from 1.79156 in year 1 to 1.68289 in year 2. So if there is a drop in Z-score which is the indicator of the financial health of the company, it means that companies are likely to fall for a second financial distress condition. This indicates that companies are still facing difficulties after exiting from financial distress condition. It is difficult for a former distress company to borrow money through lenders because of what had happen previously. Lenders may lose the confidence to lend money again to a company which had suffered a financial distress condition because they are not sure if the company will be able pay back. Therefore, it is in the company's best interest to reorganise properly and successfully in order to gain back the confidence of lenders. That is why, after a successful reorganisation plan, companies need to emerge stronger with a clear and better plan that guide them to a sustained future and avoid a second reorganisation plan or fall into another bankruptcy. They need to have the ability to rapidly respond to 'change' that will enable their survival and provide a considerable comfort and confidence to investors. In order to do so, *"stress tests"* are performed by the authorities, financial institutions and business alike, in order to determine which company can hold on and survive to the various economic conditions and global challenges of the business world.

Financial institutions also perform credit worthiness checks such as the 6C's (Character, Capacity, Capital, Collateral, Conditions, and Confidence) so as to avoid lending money to companies which will not be able repay back and default. Since the Asian financial crisis of 1997, Malaysia has employ strict rules and regulations for companies in order to avoid company failures or at least reduce the number of companies likely to fail when there are tough economic conditions. That is why, there are a lot of differences during the recent global financial crisis, when Western companies suffered tough financial crisis while Malaysian companies where not highly affected by the crisis. In this sense, US companies such as General Motors (GM) and Chrysler where put under Chapter 11 Bankruptcy protection and had to receive Government bailouts in order to reorganise their finances and their business units and emerge with strong outlook for a sustainable future. Companies such as these now operate under a close watchful eye of the Government not to fall down again because they have received tax-payers money and they have to pay back, but also to avoid a second failure. These examples support hypotheses H4.

Figure 2 Performance relationship for sample companies

5. Conclusions and Recommendations

5.1 Conclusions

The objective of this study was to assess the performance of Malaysian companies after suffering from a financial distress condition. This study has attempted to focus on how companies that are performing after going through a distress condition. Many companies post abnormal profits during their first few years, but the profits are not sustainable. So they face another restructuring petition or face winding up completely. To be able to show positive results after emergence, companies must improve their performance compared to previous financial results which led to downturn. The performance of companies emerging from a distress condition was assessed by the improvement of stock prices and other financial ratios that indicated the company is performing better compared to pre-bankruptcy period.

5.2 Recommendations

The companies need to understand what position they are in after emerging from a distress condition. This study has attempted to focus on how companies are performing after going through a distress condition. Recommendations for this will be that because some companies post abnormal profits during their first few years, but the profits are not sustainable. So the performance of companies must be influenced by a number of factors, in order to boost performance after a distressed condition, the share prices of companies must emerge with a stronger outlook to influence investors that the company is in a good position to continue generating positive returns for shareholders for a sustainable future. A suitable restructuring plan must be in place which highlights all the problems that caused their downfall and even bring in new ideas that drive the company forward.

In order to avoid another restructuring petition or face winding up completely, companies must be able to show positive results after emergence, companies must improve their performance compared to previous financial results which led to downturn. A number of factors must be considered to try to turn things around; one of these factors is management. So avoiding factors such as poor management,

poor business planning, poor financial planning, and poor marketing will certainly improve their condition. Many companies are getting stuck in the current economic climate because they are not prepared for change. They start working on the problem after it has already arisen. By the time their plan of attack is implemented, the impact has already caused serious damage to earnings, cash flow and the overall viability of the business. Businesses need to understand first how they would be impacted by an economic downturn on a 'worst case scenario' basis, and then take appropriate defensive action.

Businesses failed due to management not recognising their failings and not seeking help, followed by insufficient relevant business experience, not delegating properly and hiring the wrong people are additional major contributing factors to business failure. The problem of management, during the reorganisation process, the main thing for companies to do is change the management team so as to bring fresh and new ideas into the company that will bring positive returns, and also, improve the confidence of investors because when the company was falling, the investors looses the confidence in managers who are running the company and see them as failure. A financially distressed company will affect investors' confidence, and when confidence is shaken, investors will just sell to cut losses. But new managers will give them hope that the company will be better compared to previous management. This shows that the organised companies are better and in good position to turn things around.

When companies show negative results from the beginning of exiting the reorganisation plan, the problems will start from there. If the company keeps getting losses and the performance is not improving, they may be forced into a second distress condition. Recommendations for this question will be that in order to avoid a second financial distress condition is to use a suitable exiting plan that will carry them to better profits and sustainable futures, but also they must understand their reasons for failure in the first place because when you identifying reasons for failure it will be a solution for prevention next time. Companies must formulate successful business strategies that will improve their operations and performance. Identify their core competences in order to target precisely on their weaknesses and improve on their strengths. Companies must focus on the specific markets by offering differentiated and unique products to their competitors that will meet customers' needs, reduce costs by avoiding costing projects that do not bring any profits, and also the company must have the need to grow, because when they have less ambitious objectives, they will not survive in the market place, and a second distress condition highly likely. Businesses must try to understand the impact of the first bankruptcy and make necessary amendments to try and avoid the second bankruptcy. This will help business to be more organised in their reorganisation process and be more thorough in restructuring in order to be able to have a new and stronger share price that will contribute to a sustainable performance of the business. Sustaining a positive restructuring process will need high level of commitment and strong strategies to tackle the problems which led them into difficulties in the first place.

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