CHAPTER – 2
LITERATURE REVIEW
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Finance is the life blood of business. A unit may fall sick because of a major lubricant i.e., finance. There are various mechanisms available to a firm for revival. Financial Restructuring is a favoured mechanism for firms in red. Does financial restructuring help in improving the financial performance of a firm? An attempt has been made in this Chapter to undertake extensive literature review in this area both in National and International context.
2.1 IN THE INDIAN CONTEXT

- Pradeep Khandwala (1988) in his research confirmed that the major cause of sickness is inefficient management. External causes such as labour and competitions are essentially secondary factors although they are primary in particular instances. As per the said study, the prime responsibility for preventing sickness obviously rest with the units and their management. However, Government and financial institutions/banks have major responsibility of taking incipient sickness and preventing it which includes careful project appraisal, continuous monitoring of units especially during project implementation, professional and speedy and coordinated institutional response of the problems of the units, installation of required systems at the unit and incentive for remaining healthy units and disincentives for actions contributing to sickness.

- M.S. Narayanan (1994) examined the performance of BIFR by analyzing 472 cases disposed of by BIFR during 1987-1991. The study attributed the prolonged decision making process of BIFR, its nature of power which are more of a persuasive than of directive and to the approach of respective state governments as the prominent stake holder. The study opined that BIFR may be viewed as successful institution by evaluating and apprehending its performance in terms of disposal of cases that have been successfully survived.

- Reena Aggarwal (1999) analyzed the market performance of 131 sample firms emerging from bankruptcy during 1980 to 1993. The study was mainly based on the controlled firm approach indicated that firms emerging from bankruptcy generated abnormal returns varying from 24.6% to 138.8% depending on various expected returns models.

- Rahel Falk (2005) studied the sickness in the Indian manufacturing industry and tested the theoretical model which has addressed the political economy of industrial sickness in India. According to this study
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politicians benefit from, and accordingly pay for sickness. More so he has concluded that sickness law certainly provides several ways for the firm/stake holders to find advantages in sickness and thereby to get rid of their financial responsibility.

➢ The study by Rosemary and Omkarnath (2006) documented the trends and patterns of industrial sickness during pre and post reform period and critically evaluated the performance of BIFR, in line with changed policy framework. The study revealed that the massive sickness in SSI sector during pre reform period but it has shown significant reduction during the post reform period except a spurt during 1997 due to recession. The study also found out that there has been a significant rise in the sickness of non SSI units after recession in 1997. The study further observed that introduction of SARFAESI Act 2002 gives exclusive rights to the banks regardless of reference to BIFR and has undermined the role of BIFR in reorganizing the viable industrial units which in turn, has exposed that a structural change in BIFR function is needed.

➢ Surendra Komera and Jijo Lukose (2009), undertook an empirical analysis of post bankruptcy performance. They have examined stock returns and operating performance of 101 firms that emerged as “no longer sick” from the BIFR proceedings during the period 1992 to 2006. As per the short term and long term analysis of market performance using various expected return models and estimates, shows no sign of significant abnormal returns in comparison to the results from the US market. The US market analysis indicates that the market for stocks of four quarters earning of the similar kind of company is informationary efficient. On the other hand, the analysis of operating performance of the Indian sample firms is evident that they are neither making superior operating margin nor utilizing the assets efficiently after emerging from BIFR proceedings. They had also raised doubts about the efficiency of BIFR proceedings and it may be possible that the proceedings may allow inefficient firm to reorganize and survive.
2.2 IN THE INTERNATIONAL CONTEXT

➢ In a study undertaken by Useem (1990), restructuring should be viewed as part of a broader transformation in the organization of ownership and managerial control of the corporation. A conclusion is drawn that considerable managerial discretion remains in shaping company response to the restructuring pressure. Although market and organizational factors are sure to act as constraints, top management, whether relatively autonomous non-owning management group or an owner – dominated management, retains an important independent capacity to exercise strategic choice.

➢ Christopher and Neill Marshal (1992) conducted a study on Corporate Restructuring in the Financial Services Industry and contended that large firms transmit the dynamics of contemporary restructuring and in turn, establish a symbolic relationship with places. The paper concludes that closer market integration results in divergent organizational forms, with district geographical expressions.

➢ In a study conducted by John, Lang and Netter (1992) found that in 1980s, the market for corporate control had an enormous impact on management decision making and the restructuring of firms in response to changing economic conditions. They found that 37% of a sample of large firms with poor performance underwent a change in corporate control in the 1980s. However, for various reasons, it is unlikely that in the foreseeable future the market for corporate control will be a major force in disciplining management.

➢ Further in a study conducted by Bowman and Harbir Singh (1993) on Corporate Restructuring, they have concluded that Financial restructuring, when accompanied with investment in key strategic activities, can be effective for the firm.
In another study carried out by Bethel and Liebeskind (1993), they concluded that block holder ownership is associated significantly with corporate restructuring, suggesting that many managers restructured their corporations during the 1980s only when pressured to do so by large shareholders.

Gibbs (1993) in his study stated that there occurs three types of corporate restructuring transactions: 1. Financial restructuring including recapitalizations, stock repurchases, and changes in capital structure, 2. Portfolio restructuring involving divestment and acquisitions and refocusing on core business, resulting in change of the diversity of business in the corporate portfolio; and 3. Operational restructuring including retrenchment, reorganization, and changes in business level strategies. These three types of restructuring are not mutually exclusive; and in fact, frequently occur together. The findings of the study support agency conflicts as a partial explanation of corporate restructuring and confirm the importance of outside directors, stock-based management compensation, and an active, well-functioning market for corporate control in preventing and correcting agency problems.

Edith S. Hotchkiss (1995) examined the post bankruptcy operating performance of the firms that filed protection under Chapter XI from 1979 to 1988. The study examined the return on assets and operating margin as the measures of operating performance and stated that there is an improvement in the operating performance during the post bankruptcy period. The study has concluded that 40.7% of the sample firms continue to report negative operating income in 3 years following the emergence from bankruptcy and 32% of sample firms have not earned significantly after coming out of Chapter XI.

Hatfield, Liebeskind, Opler (1996) conducted a study on the effects of Corporate Restructuring on aggregate industry specialization across a broad sample of US industries. As per their study, no evidence that change in the ownership of industry assets was detriment of change in aggregate industry specialization. More important finding suggested that restructuring
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through plant closure and plant addition, and industry entry played a far more important role in changing competitive conditions at the industry level during 1980s than did corporate control transactions.

- Alderson (1999) analyzed the post bankruptcy performance of 89 samples emerged from bankruptcy during 1983-1993. The study applied total cash flow approach and reported that sample firms neither under- performed nor over performed the industry median performance. The study concluded that though the post bankruptcy operating performance is poor, the sample firms were neither being over estimated nor under estimated by the market.

- Mckinley and Scherer (2000) carried out a research on Some unanticipated consequences of organizational restructuring and concluded that an important problem top executive faced during organizational restructuring is maintaining subordinate “buy-in” to restructuring activities that the subordinates often perceive as chaotic.

- Djankov and Colln Xu (2000) made comparative study of the growth and financing patterns of East Asian Corporations in the years before the crisis with those in other countries. The conclusion was drawn that the East Asian financial crisis showed that risks arising from the corporate sector typically occurred because of institutional weaknesses, including weak property rights, poor bankruptcy and accounting procedures, lack of transparency, and weak or perverse incentives.

The literature review reveals that there is not much research undertaken as far as the sickness of industries in the Indian context is concerned. Again, the researches undertaken by various researchers till date are more of a study in identifying the factors/reasons for the sickness, sickness in general or sickness and revival of a particular industry or functioning of BIFR cases post restructuring as compared to similar cases of restructuring of other countries. More so, with the changes in the overall economic policy, business environment and legal system, a sea change in the industrial
sickness as well as revival measures adopted by promoters, financial institutions, banks, Reserve Bank of India and the Government of India has been observed. There are very few empirical studies on the impact of financial restructuring on corporate performance. Empirical research is needed to find whether financial restructuring helps in the improvement of sales, profits, networth etc. Moreover, financial restructuring is effective in which types of firms i.e. large, medium or small size firms. This study attempts to fill these gaps identified through literature review.