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The Voluntary Restructuring of Large Firms in Response to Performance Decline

KOSE JOHN, LARRY H. P. LANG, and JEFFRY NETTER*

ABSTRACT

Much of the research on corporate restructuring has examined the causes and aftermath of extreme changes in corporate governance such as takeovers and bankruptcy. In contrast, we study restructurings initiated in response to product market pressures by “normal” corporate governance mechanisms. Such “voluntary” restructurings, motivated by the discipline of the product market and internal corporate controls, will play a relatively more important role in the 1990s due to a weakening in the discipline of the takeover market. Our data suggest that the firms retrenched quickly and, on average, increased their focus. There is no evidence of abnormally high levels of forced turnover in top managers. There is, however, a significant and rapid cut of 5% in the labor force. Further, the cost of goods sold to sales and labor costs to sales ratios both decline rapidly, more than 5% in the first two years after the negative earnings. The firms cut research and development, increased investment, and also reduced their debt/asset level by over 8% in the first year after the negative earnings. We also document the reasons management and analysts reported for the negative earnings. Overwhelmingly the firms blame bad economic conditions and, to a lesser extent, foreign competition.

THE 1980S PROVIDED AN unprecedented opportunity for financial economists to study the disciplinary role of the market for corporate control and economists responded with a vast amount of valuable research. Less attention has been paid, however, to restructurings motivated by other sources of management discipline such as the product market or internal corporate controls. This paper, which examines restructurings made in response to pressures from

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the product market, hopefully fills in some of the gaps in our understanding of the workings of different sources of management discipline.

We study the normal workings of corporate governance mechanisms in responding to market pressure. In contrast to lessons drawn from restructurings caused by takeovers or bankruptcy, which are extreme events in the life of the corporation, the insights from this study are more typical of the routine functioning of the internal corporate governance system in initiating restructurings to cope with performance shocks. Understanding such voluntary restructurings will become relatively more important in the future as a result of the weakening disciplinary role of the takeover market and declining corporate debt.

We examine voluntary restructurings of 46 large firms in the 1980s made in response to declining performance. We call the restructurings voluntary because we limit our study to firms that were not taken over (although there may have been threats of hostile takeovers). Specifically, the sample is composed of firms with more than one billion dollars in assets that had at least one year of negative earnings from 1980 through 1987, followed by at least three years of positive earnings. In addition, the firms were not subject to successful takeovers, Chapter 11 filings, or liquidations.

We document the reasons given by management and analysts for the negative earnings and the responses. The published reports overwhelmingly blame the negative earnings at least in part on poor economic conditions (95% of the firms). More than half the firms blame competition, especially foreign competition, for their poor performance, but other explanations include accounting changes, overexpansion, high costs, and too much debt. The reported responses to the negative earnings are more varied but in general they tell a story of contraction and cost cutting. Asset sales were mentioned most often, followed by employment cuts and debt reduction.

We also document the actual changes that occurred in the firms. When it is informative and possible, we compare our findings with those in other studies for evidence on the relative importance of the changes in the sample firms. For example, we find no evidence of an abnormally high level of forced top management turnover.

We find stronger evidence of changes in operations and investment. The data suggest that the firms retrenched quickly, and on average, concentrated their focus. In the year following the negative earnings, average employment fell by about 5% (almost 2000 workers per firm) and the average number of business segments declined. Costs also fell, especially in the first two years after the negative earnings. In the longer run, however, sales and assets grew slightly, which combined with the reduced costs suggests increased efficiencies. The firms cut research and development (R & D), but increased investment. We also find evidence of changes in financial policies. On average, the firms reduced their debt/asset levels in the first year after the negative earnings, and many firms also cut dividends.

We call these restructurings voluntary because the firms were not taken over, though there is some evidence that the firms were subject to a relatively

high level of takeover threats. Our approach differs from most other studies of restructurings because we study firms which exhibited a certain pattern of performance and examine their responses, instead of starting with a sample of restructurings. Brickley and Van Drunen (1990), for example, start with restructured firms and examine changes in internal organization. They conclude that, on average, the changes increase shareholder wealth and give information about investment opportunities and increased efficiency.

Studies that examine how firms react to changes in economic conditions without changes in control will become relatively more important since various factors have hobbled the market for corporate control. Jensen (1991) argues that the disciplinary forces over corporate management include the corporate control market, the capital market, competition in the product market, internal corporate controls, and regulation. He suggests that managements have used the political process to insulate themselves from discipline by the control market and that, at best, regulation is ineffective in disciplining management. Jensen argues that it will become increasingly important to examine the workings of product market discipline and internal corporate controls.¹ Our sample of firms that responded to performance declines with changes made by the existing managements, provides evidence on these alternative disciplinary mechanisms.

I. Research Approach

This study documents the reported reasons for and responses to negative earnings and examines observable changes in control, operations, investments, and financial policies. We recognize that using negative earnings as a measure of firm performance has limitations since it is to some extent a variable that management can manipulate. For example, DeAngelo and DeAngelo (1991) argue that management may reduce reported earnings during labor negotiations to strengthen their bargaining position. However, while earnings are potentially manipulated by management, firms (especially large firms) attempt to smooth earnings (see Ronen and Sadan (1981), Moses (1987) and Schipper (1989)). Thus, the fact that a large firm reports negative earnings is an important event and we believe that it serves as a useful proxy for poor performance.²

In a sense, our study is an extension of Donaldson's (1990) study of the voluntary restructuring of General Mills. He finds that the restructuring of General Mills reversed the diversification strategy of the 1960s and 1970s. This internally motivated corporate restructuring took about ten years and

¹ Actually, Jensen argues that product market discipline may not be effective because firms may successfully seek protection from foreign competition. Consistent with this prediction, we find that almost half of the firms in our sample blame their decline on foreign competition and 17% call for increased regulation.

² Researchers have used many different measures of financial distress, for example Asquith, Gertner, and Sharfstein's (1991) measure uses interest coverage ratios and Gilson, John, and Lang (1990) use poor stock performance.

was not in response to explicit takeover threats.³ Our approach is also similar to DeAngelo and DeAngelo's (1991) analysis of policies such as changes in managerial compensation, dividends, and financial reporting undertaken by seven major steel producers during negotiations for union givebacks. Our research design, combining data from various sources including business publications, also borrows from the research approach used to study hostile takeovers by Bhidé (1989) and Bhagat, Shleifer, and Vishny (1990).

One difficulty in our empirical work is that there are differences among firms in the timing of the release of financial reports during the calendar year and in the timing of financial reports relative to other news resources. In general our approach is to compare data in the firms' and analysts' reports for Year 0 with the same data in Years 1, 2, and 3. This provides a consistent base for comparison although it biases our results against finding changes because the firms may begin their responses during the year of negative earnings (or even before). However, in the case of variables when we can pinpoint the exact date of the change (managerial turnover, dividend changes, repurchases) we include changes in Year 0 if they occurred after the announcement of negative earnings. Thus, the time period for changes in such variables (especially management turnover) may be up to four years for some firms.

II. Overview of Sample and Data Sources

A. Sample Selection of Large Firms with Negative Earnings

We used Compustat data to identify all firms in the 1980s that had an annual average of at least \$1 billion dollars in assets. We excluded foreign firms and firms in the highly regulated industries of financial services and utilities, firms that did most of their business with the government (such as defense contractors), firms that were subsidiaries of other firms, and firms with insufficient Compustat data. The firm had to have at least one year of negative earnings between 1980 and 1987, followed by three years of positive earnings. The goal of the selection process was to identify large firms that were subject to financial distress, but that reestablished positive earnings while avoiding takeovers or bankruptcy.

We identified 82 firms matching our criteria. We searched the *Wall Street Journal* and other business publications to determine which firms had been targets of successful takeovers (including mergers, tender offers or leveraged buyouts) during the 1980s or filed for Chapter 11. Thirty-four firms met one or more of these criteria. Of these 34 firms, one (PHL Corp, formerly Baldwin United), filed for Chapter 11 and was also later taken over. Two firms were

³ Baker (1991) performs a similar study of Beatrice.

dropped because we did not have access to all the SEC filings.⁴ This leaves the 46 firms for our full analysis.⁵

B. Data Sources

We searched public filings including annual reports, 10Ks, and proxy statements for reports by management on firm actions as well as for information on insider holdings, segment data, foreign sales, and management turnover. Business publications such as the *Wall Street Journal*, *Fortune*, *Business Week*, *Financial World*, *Forbes*, *Barrons*, *Dow Jones News Retrieval Service*, *Value Line*, *Moody's Industrial Reports*, *S & P reports*, and *Value Line* provided details on analysts' views of the firms and more coverage of significant changes in the firms' activities. In addition, Compustat is the source for most financial data on the firms.

III. Empirical Results

A. Full Sample and Relative Frequency of Takeovers and Chapter 11 Filings

Table I presents an overview of what happened to the 82 firms that met our sample selection criteria. Thirty of the 82 firms (37%) were targets of successful takeovers or merged firms of a similar size (for example Baker International and Hughes Tool merged to become Baker-Hughes) after the negative earnings.⁶ Apparently in most cases the takeover was a response to the poor performance, rather than the reverse since only four of these 30 firms had negative earnings in a year after the successful takeover. Of the 30 firms, 17 disappeared from Compustat and three of the takeover firms went private.

Four of the 82 firms filed for Chapter 11. The small number of Chapter 11 filings is consistent with the evidence presented by Bradley and Rosenzweig (1992) that firms listed on the NYSE or AMEX rarely file for Chapter 11.⁷ In addition, one firm liquidated and sold its assets.

There is evidence that the occurrence of takeovers in the 82-firm original sample is slightly greater than what occurred among firms in general, and that the level of takeover threats among the firms that remained independent

⁴ The two firms are Imcera Group and Navistar (International Harvester). A review of analysis of these firms in business publications suggests their behavior was similar to the other firms in our sample.

⁵ Thus, firms that had negative earnings in 1988 or 1989 would not be included in the sample since we did not have SEC filings data for 1991 or 1992. A firm was not necessarily excluded if it had negative earnings in 1990, but would have been excluded if its last year of negative earnings in the period from 1980 through 1987 was 1987 and thus did not have three years of positive earnings after the negative earnings.

⁶ Gordon Donaldson (1990) said this number shows the "fragility of the corporate form."

⁷ Two Chapter 11 filings (Texaco and Manville) were in response to unfavorable litigation results.

Table I
Outcomes for Firms Meeting Sample Selection Criteria

Independent firms listed on Compustat with greater than one billion in assets and reported income in the 1980s, at least one year of negative earnings from 1980–1987, positive earnings in 1988 and 1989, not operating in heavily regulated industry (utilities, financial services).

	Number
Firm was a target of successful takeover including mergers, successful tender offer, leveraged buyout, or going private transaction (two of the firms merged with each other)	30
Takeover firm disappeared from compustat	17
Negative earnings occurred in a year after takeover	4
Takeover firm went private	3
Filed for Chapter 11 from 1980–1989	4*
Chapter 11 filing the same year as negative earnings	2
Chapter 11 filing in between years of negative earnings	1
Chapter 11 after negative earnings	1
Liquidated	1
Total number of different firms that were either a takeover firm, filed for Chapter 11, or liquidated	34*
Firm where annual report, proxy, and 10K data not available to us	2
Sample used in following analysis	46
Firms subject to takeover attempt or rumors	16
Total	82*

* One firm both filed for Chapter 11 and was then taken over. It is only counted once in the totals.

was high. We use for comparison the Mitchell and Lehn (1990) analysis of takeovers in a sample of 1153 *Value Line* firms from 1980 to 1988. The Mitchell and Lehn sample is very similar to ours in terms of time period and the industries they exclude, but their average firm size is presumably much smaller than in our sample. Thus, based on the smaller sized firms there would probably be more takeover activity in the Mitchell and Lehn sample. On the other hand, the poor performance of the firms in our sample would predict more takeover activity in our sample. In comparison to our 37% being subject to a takeover, Mitchell and Lehn found that 31% of their sample experienced control changes. Thus, there was a slightly higher level of successful takeovers in our full sample than in the Mitchell and Lehn sample.⁸

We also determined the extent of takeover threats faced by the 46 firms that remained independent. During the year of the negative earnings and the following three years, 16 (35%) of the firms experienced takeover threats,

⁸ As expected, since there was evidence of financial distress among the firms in our sample, our 82 firm sample had a higher level of Chapter 11 filings (5%) than in the Mitchell and Lehn (1990) sample (2%).

either a takeover proposal, rumors of a proposal, a large stake acquired by a potential raider, a proposed merger, or a proposed leveraged buyout. As a rough comparison, Lehn and Poulsen (1989) find that in 43% of their sample of going private transactions from 1981 through 1987, the transactions were preceded by takeover rumors or bids. In a sample of matched firms that did not go private, Lehn and Poulsen (1989) find only 15% experienced takeover speculation. However, there are two reasons to expect the Lehn and Poulsen (1989) matched control sample would tend to have more takeover speculation than our 46 firm sample; (1) the sample was composed of smaller firms, and (2) the sample was drawn from industries where a matched firm did go private. Thus, the fact that 35% of the firms in our sample of firms that remained independent experienced takeover speculation, which is much more than the 15% in the Lehn and Poulsen matched sample and close to the 43% in the Lehn and Poulsen sample of firms that did go private, suggests that the threat of takeovers was relatively high among firms in our sample.

B. Overview of Sample

Table II lists the sample of 46 firms, the year of their last loss and their four-digit industry as reported by Compustat. Based on the Compustat classification, the 46 firms operated in 24 different four-digit industries although Compustat only reports the major line of business, and these tend to be diversified firms. There are similarities among the firms. In general, the firms do not produce consumer goods.⁹ Petroleum is important for many of the firms; using the Compustat four-digit SIC classification, six firms are petroleum refiners, while several others construct oil facilities or produce equipment for drillers.¹⁰ There are several mining firms as well as firms that produce capital equipment for mining firms. Transportation is represented with three airlines and two railroads. Additionally, there are three steel firms.

Twenty-one of the 46 firms (46%) had more than one year of negative earnings from 1980 through 1987. In our analysis, however, we concentrate on the reaction in the three years following the last negative earning year, so that we have equal length period for comparison. We recognize that some policy changes in response to the poor performance could have begun before the year of negative earnings, especially in those firms with more than one year of negative earnings. In some cases (especially with respect to writeoffs), the negative earnings may have been a result of policy changes to deal with poor performance.

⁹ The exceptions are the three major U.S. auto manufacturers, Black and Decker, which produces household appliances, three airlines, Warner Lambert, a drug company, and Whitman, which is a diversified firm producing some consumer goods (Whitman Sampler).

¹⁰ To ensure that changes in the prices of petroleum did not drive our results, we examined changes in the firms after excluding the 15 firms heavily influenced by petroleum prices and found essentially the same results.

Table II
Sample of Firms

Firms with more than one billion dollars in assets that had at least one year of negative earnings from 1980–1987 and were not taken over or did not file for Chapter 11.

Name	Last Loss	Industry (1990 Compustat)
Amerada Hess	86*	petroleum refining
AMR	82*	Air transport, scheduled
AMAX	86*	Primary production of aluminum
Asarco	85*	Primary smelting, refining nonferrous metals
Armco	86*	Steel works and blast furnaces
Alcoa	85*	Primary production of aluminum
Ashland Oil	84	Petroleum refining
Bethlehem Steel	86*	Steel works and blast furnaces
Black and Decker	85	Metalworking machinery and equipment
Burlington Northern	86	Railroads, line-haul operating
Caterpillar	84*	Construction machinery and equipment
Champion International	84	Paper mills
Coastal	81	Natural gas transmission
Chrysler	82*	Motor vehicles and car bodies
Delta	83	Air transport, scheduled
Deere	87*	Farm machinery and equipment
Dresser Industries	85	Construction, mining, handling equipment
Eaton	82	Motor vehicle parts and accessories
Enserch	85	Natural gas transmission and distribution
Fluor	87*	Heavy construction, not building construction
Ford Motor	82*	Motor vehicles and car bodies
GATX	83	Transportation services
General Motors	80	Motor vehicles and car bodies
Grace WR	86	Chemicals and allied products
Halliburton	86	Heavy construction, not building construction
Ingersoll Rand	83	General industrial machinery and equipment
Inland Steel	85*	Steel works and blast furnaces
Intel	86	Semiconductor, related devices
Kerr McGee	86	Petroleum refining
Louisiana Pacific	82	Sawmills, planing mills
Mead	82	Paper and allied products
Monsanto	85	Chemicals and allied products
Murphy Oil	87*	Petroleum refining
Olin	85	Chemicals and allied products
Phelps Dodge	84*	Primary smelting, refining nonferrous metals
Reynolds Metals	85*	Primary production of aluminum
Sonat	86*	Natural gas transmission
Texas Instruments	85*	Semiconductor and related devices
Union Carbide	85*	Plastics, resins, elastomers
Union Pacific	86	Railroads, line-haul operating
UAL	87*	Air transport, scheduled
USX	86*	Petroleum refining
Valero Energy	86	Petroleum refining
Warner Lambert	85	Pharmaceutical preparations
Williams Companies	85	Natural gas transmission
Whitman (was IC Industries)	86	Food, kindred products

* More than one year of losses from 1980–1987.

We do not determine the success of the firms in improving performance in any way other than by requiring the firms to have three years of positive earnings following the negative earnings year. For 39 of the firms (85%), however, analysts or management mentioned that performance had improved.

We collected for each firm the reported reasons for the negative earnings and the reported responses to the negative earnings.¹¹ These reasons are taken from management's discussion of firm performance in the annual report and 10K filings and the research by *Value Line*, *Moody's*, and business publications for the year of the negative earnings and the following three years. (Note that analysts for financial publications often obtain their information directly from management or from firm filings.) We used our judgement in synthesizing the reports. For example, we tried to concentrate on the reason for the last year of negative earnings even if the firm had more than one year of poor performance although the reasons would usually be similar. We do not report a reason if it was only mentioned for one firm.

C. Reasons for the Negative Earnings

In Table III we classify the reported reasons for the negative earnings into factors we consider exogenous and endogenous. The distinction is somewhat arbitrary since sensitivity to certain macroeconomic changes or exogenous

Table III
Reported Reasons for Negative Earnings

Reason	Number of Firms (%)
Exogenous factors	
Economic conditions	42 (95)
Competition	26 (57)
Foreign competition	20 (43)
Deregulation	6 (13)
Strong dollar	5 (11)
Fuel prices	2 (4)
Endogenous factors	
Accounting: writeoffs or writedowns, or change in accounting techniques	17 (37)
Failed acquisition, overdiversification, or overexpansion	12 (26)
High costs, inefficiency	7 (15)
Strike	7 (15)
Too much debt	6 (13)
Bad management or mistakes	6 (13)
Costs of developing new product or production method	4 (9)
Poor product mix	2 (4)

¹¹ These are discussed in the appendix.

factors might actually be under a firm's control, for example, Nicholas Brady. Amerada Hess's investment banker, suggested the firm should have hedged against price declines in oil. Nonetheless, the classification is instructive since it shows that published reports are much more willing to blame firms' negative earnings on exogenous than on endogenous factors.

The most common reason given for the negative earnings (95% of the firms) is poor economic conditions (recession, poor market conditions). The second most common reason is competition (57%), especially foreign competition including imports and increased competition in overseas markets. Among factors internal to the firm the most commonly mentioned factor is accounting (37%): writeoffs or writedowns (often associated with a restructuring) or change in accounting techniques.¹² The fifth most commonly mentioned reason (by 26% of the firms), failed acquisition, overdiversification, or overexpansion, is the first case in which reports suggest the firm made an economic mistake: Management, at least, does not generally blame itself for the poor performance.

The accounting reason for negative earnings represents the one case where the negative earnings are not due directly to real economic changes. Instead the writeoffs may indicate the firm has undertaken restructuring in response to changing economic conditions. The importance of accounting reasons for negative earnings is consistent with Brickley and VanDrunen (1990) who find reported earnings often decline after restructurings. Depressed earnings in some firms may also be due to the factor identified by DeAngelo and DeAngelo (1991) that firms may reduce earnings as a negotiating tool against workers. To ensure that there was nothing fundamentally different about the firms that reported an accounting reason for negative earnings, we repeated our empirical analysis using Compustat data excluding these firms and found essentially the same results as with the full sample.¹³

D. Reported Responses to the Negative Earnings

There is substantial variation in the reported responses to the negative earnings, aggregated in Table IV.¹⁴ We classify responses into several broad groups: contraction policies (which represent policies that shrink the size of the firm or its control of resources), expansion policies (which increase the size of the firm or its control over resources), change in marketing or pricing, change in production methods or management structure, and other responses. An overview suggests that contraction policies are the predominant

¹² Only one firm, Champion International, mentioned writeoffs accompanying a restructuring as the sole reason for the negative earnings. Champion acquired St. Regis as a white knight and began a restructuring that included asset sales. Champion's governance remained much the same, it in our judgement acquired St. Regis and began to sell the pieces. Thus, it was unlike the mergers in our sample where we eliminated the firm because the firms governance and structure changed in the combination.

¹³ Elliot and Shaw (1988) show poorly performing firms use writeoffs. Thus, writeoffs may be evidence of poor performance, which is the goal of our sample selection process.

¹⁴ We directly examine dividend changes, share repurchases, and pension terminations in Table VIII not here.

responses, the five most common responses are contraction policies: asset sales, divestitures, spinoffs, employment reduction, debt reduction, emphasis on core business, and plant shutdowns. While these reasons are not independent (plant closings and employment reductions, for example), the magnitudes of these numbers, especially the 63% of the firms that sell assets or divest, suggest shrinkage and consolidation as a response to the negative earnings.¹⁵ The percentage of firms that have asset sales (63%) and concen-

Table IV
Reported Responses to Poor Performance

Response	Number of Firms (%)
Contraction policies	
Sell assets, divest, spinoff, sell businesses of subsidiaries	29 (63)
Reduce employment	20 (43)
Reduce debt	18 (39)
Emphasize core business	13 (28)
Close plant	12 (26)
Cut wages	9 (20)
Reduce capacity	5 (11)
Reduce capital expenditures	4 (9)
Expansion policies	
Acquire raw materials	12 (26)
Introduce new product	11 (24)
Enter new markets	7 (15)
Increase debt	4 (9)
Diversify	4 (9)
Issue equity	3 (7)
Change marketing or pricing	
Change marketing	4 (9)
Change name	3 (7)
Change pricing	2 (4)
Change production methods or management structure	
Modernize or improve efficiency with new production techniques or equipment	11 (24)
Embark on joint venture	6 (13)
Change management structure	6 (13)
Move production overseas	4 (9)
Change inventory investment or inventory production policies	3 (7)
Other	
Change focus (product or market mix) of the firm	9 (20)
Call for regulation	8 (17)
Improve quality	5 (11)

¹⁵ Other researchers document contraction as a response to declining performance, for example, Lang, Poulsen, and Stulz (1992) show firms in financial distress sell assets and Blackwell, Marr, and Spivey (1990) show the major reason for plant closing is declining firm profitability.

trate on core businesses (28%, not mutually exclusive) suggest failed diversification may be a greater problem than it would appear based on the reported reasons for the negative earnings. Additionally, some firms reduced capacity within their core business.

Similar policies, which also suggest a need to revamp production methods, or organizational structure were those actions that represented changes in production methods, or management structure. For example, 24% of the firms reported modernization or improved efficiency as a response, while 13% reported a change in management structure. Other responses in this general area included joint ventures and moving production overseas.

On the other extreme, there were cases where firms expanded their control over resources including acquisitions, new products and market development, and diversification. However, even the most common response from the expansion group (acquisitions, by 26%) to some extent represents consolidation at an industry level because we include acquisition of reserves and other raw materials in that group. Several of the refining firms bought relatively cheap oil reserves and several mining firms expanded through acquisition of mines. Twenty percent of the firms said they would in some way change the focus of the firm, as distinct from the 13 firms who indicated they were concentrating on core business. (This is the only case in the sample where a firm could not be counted in two categories.) Finally, 17% of the firms explicitly called for regulation to help the firm or its industry, usually trade barriers against unfair foreign competition. This is consistent with the large number of firms that blamed competition and especially foreign competition for their plight.¹⁶

In sum, we document the reported reasons for the negative earnings and the reported responses in the three years following the last year of negative earnings. Several patterns emerge. First, reports tend to blame the negative earnings at least in part of factors exogenous to the firm especially poor economic conditions and foreign competition. Second, responses tend to shrink the firm often with the goal of reversing the effects of past diversification and refocusing the firm on its core business. Contraction also often means reduction in the scale of the firm's core business. Our finding that many firms shrunk as a response to the negative earnings can be related to the theoretical and empirical evidence on takeovers. For example, Jensen (1986) argues that the motivation for many takeovers in the 1980s was the disgorgement of free cash flow which management could have wasted on negative NPV projects.¹⁷ The refocusing on core businesses may reflect management's termination of negative NPV projects. The threat of takeovers was likely a

¹⁶ Interestingly, this parallels another development in the 1980s, when corporate managements responded to the threat of takeovers by successfully lobbying for strict state antitakeover laws (see Ryngaert and Netter (1988), Karpoff and Malatesta (1989), and Jensen (1991)). More generally Roe (1990) shows the historical pattern of government regulation of control of capital.

¹⁷ Empirical Support for Jensen's argument is contained in Mitchell and Lehn (1990), Kaplan (1990), Lehn and Poulsen (1989), Lang, Stulz, and Walkling (1989, 1991).

motivation behind some of the restructurings, as evidenced by the fact that 35% of the firms were rumored to be or were actual takeover targets.

IV. Observable Changes in the Troubled Firms

In this section we use a variety of data sources including SEC filings, business publications, and Compustat to document observable changes in the firms over the period beginning in the last year of negative earnings.

A. Changes in Control of the Firm

In Table V we report data on changes in the most senior manager of the firms. We find that in 23 of the 46 firms (50%), the senior manager changed during the sample period (there were two changes in one firm), while in the other 23 firms there were no changes.

The 50% turnover rate of the top manager in the year of negative earnings and the three following years (12.5–16.6% per year) is consistent with (perhaps slightly higher than) general turnover rates found by other

Table V
Reason for Change in the Top Manager and Information on
the Old Manager and Replacement in the Sample Period as
Reported in the *Wall Street Journal*, Business Publications, or
Annual Reports

A management change is defined as any change in the identity of the firm's top senior manager.

	Number	Replaced by Insider	Replaced by Second Ranking Manager*	Old Manager Remains on the Board
Retires	17	17	15	13
Resigns	1	1	1	0
Board removes	4	1	1	1
Dies/poor health [†]	2	0	0	0
Total	24	19	17	14
Total number of firms with change	23	19	17	14
Number of firms without a change	23	—	—	—

* In two cases the second ranking manager was brought in from outside to take the second ranking position. They are counted as inside replacements, however, since they were insiders at the time they moved up to the top position.

[†] In both cases the change was at the same firm (Whitman). This is the only instance in the sample of more than one change at any one firm.

researchers. Coughlan and Schmidt (1985) find an annual turnover rate for chief executive officers of 12.7%, Weisbach (1988) finds an annual turnover (resignation) rate of chief executive officers of 7.7%, and Klein and Rosenfeld (1988) find an annual turnover rate for the top manager of 9.3%. Thus, we do not find an abnormally high annual turnover rate, despite the findings of Warner, Watts, and Wruck (1988), and Weisbach (1988) that turnover is higher following a period of poor performance and of Martin and McConnell (1991) that the turnover of the top manager increases from approximately 10% in each of the five years preceding a takeover to 41.9% in the year after a takeover.

We analyze who initiated the change in the top manager based on press reports and discussion in the annual reports. In general, the change was the result of ordinary succession and in the cases where the change was forced it was due to pressure from the board, not an outside blockholder. Seventeen of the 24 changes (71%) were retirements and in each case the top manager was replaced by an insider, generally the second-ranking manager. Furthermore, in 76% of the retirements the old top manager remained on the board.¹⁸

In several cases, however, the change in the top manager appears to be forced. Gilson (1989) defines forced departure as all changes except retirement, normal management succession, and death or illness. In our sample, the board removed the top manager in four firms, while in one case the top manager resigned. Using Gilson's (1989) definition, 21% of the departures were forced. This forced turnover rate is lower than what Gilson reports or the general samples of Warner, Watts, and Wruck (1988) (28%) and Weisbach (1988) (38%). Gilson's sample of firms in financial distress has a forced turnover rate of 83%.

Additionally, Gilson reports in his sample that in 43% of all turnovers the manager is replaced by an outsider, while the random sample of changes by Warner et al. (1988) has an outsider appointment rate of 19%. We find that in five of the 24 changes (21%), the senior manager was replaced by someone from outside the firm. This is consistent with the findings of Warner et al. (1988), but much lower than Gilson's (1989) findings for financially distressed firms. In three of the five cases where the board went outside the firm (60%) it was after a forced turnover of the top manager.

We also examine turnover in the second ranking manager in those cases in which the top manager did not change to check for the possibility that the firms responded to poor performance with changes at this level of management instead of at the top. In 10 of the 23 firms without top manager turnover (43%), the second ranking manager changed (there was no more than one change in any firm). There were five retirements, one change due to health reasons, and one case where the restructuring of the firm (Burlington Northern) created a new second rank position. There are no cases of forced turnover (although there was forced turnover of the second ranking manager

¹⁸ In two other cases (both in Whitman, the only firm with more than one change in the top manager) the top manager changed because of death or poor health.

in several of the firms where the top manager changed). Finally, when the second ranking manager was replaced he rarely stayed with the firm in any position, only two of the ten (20%) remained with the firm.

In sum, there is little evidence of an abnormally high level of managerial turnover or forced departures (although it is possible that they were forced departures there were kept hidden). Unlike the findings of Gilson (1988) and others that financial distress motivates management replacement, the replacement of the senior manager in our firms occurred in a typical way. Further, there was little exceptional about the turnover of the second ranking manager.¹⁹

B. Changes in Operations and Organizational Structure: Size, Costs and Investment

In this section we report changes in the firms' operations and organization, including changes in size, focus, costs of production and investment policies. Much of the analysis uses Compustat accounting data. Similar results are obtained with and without adjusting for industry changes. We do not report, however, the industry-adjusted results for two reasons. First, we are interested in the absolute changes in these firms. Second, since our sample is composed of large firms, the sample firms generally account for a large portion of the industry and thus adjusting for industrywide effects is not meaningful.

B.1. Changes in Size and Focus

Table VI reports measures of changes in the size of the firm: mean and median percent change in total assets, net sales, employment, and changes in the number of business segments.²⁰ Taken together, the changes in the size measures suggest the firms were able to retrench and produce more efficiently since they broadly indicate firms continued to grow with reduced or constant numbers of employees.

Total assets and sales both increased on average, especially by years two and three. Total assets increased on average by 0.5% from Year 0 to 1 (median 0.63%), and significantly from Year 1 to 2, Year 2 to 3, and 4.75% over the whole period Year 0 through 3 (median 3.61%, both statistically different from 0). Net sales increased on average 6.19% from Year 0 to 1

¹⁹ We also checked changes in two other measures of control—director turnover and insider ownership. On average 24.4% of the directors in these firms in Year 3 were not directors in Year 0, where the percentage ranged from 0 to 54%. There was little change in insider ownership from an average of 3.99% to 3.90%, and the insider ownership did not change by more than 2% for any firm. This relatively low level of insider ownership is due to the size of the firms (Mikkelson and Partch (1989) report the average (and median) votes controlled by officers and directors is 13.9% in their sample of 715 NYSE and AMEX firms).

²⁰ Unless noted otherwise the reported mean changes are the mean of the mean changes for each firm.

Table VI
Measures of Change in Size and Focus of Firm in Sample Period

Size Measure	Percentage Change from Year <i>i</i> to Year <i>j</i>			
	0 to 1	1 to 2	2 to 3	0 to 3
Total assets	<i>N</i> = 46	<i>N</i> = 46	<i>N</i> = 46	<i>N</i> = 46
Mean	0.50	7.10	6.66	4.75
(<i>t</i> -statistic)	(0.28)	(2.72)*	(4.82)*	(3.32)*
Median	0.63	4.08*	6.66*	3.61*
Net sales	<i>N</i> = 46	<i>N</i> = 46	<i>N</i> = 46	<i>N</i> = 46
Mean	6.19	10.08	12.50	9.59
(<i>t</i> -statistic)	(1.38)	(2.03) [†]	(4.70)*	(4.72)*
Median	3.14	10.06*	11.50*	8.54*
Employment	<i>N</i> = 45	<i>N</i> = 45	<i>N</i> = 46	<i>N</i> = 46
Mean	-5.66	1.24	-0.96	-1.62
(<i>t</i> -statistic)	(-2.92)*	(0.54)	(-0.46)	(-1.09)
Median	-4.42*	1.32	1.34	-1.60
Change in number of segments from year 0 to year 3				
Increased	8			
Decreased	15			
No change	23			

* For a *t*-statistic denotes the mean is statistically different from 0 at the 1% level, for a median indicates the median is statistically different from 0 at the 1% level using a Wilcoxon sign rank test.

[†] For a *t*-statistic denotes the mean is statistically different from 0 at the 5% level, for a median indicates the median is statistically different from 0 at the 5% level using a Wilcoxon sign rank test.

(median 3.14%), significantly from Year 1 to 2, from Year 2 to 3, and 9.59% from Year 0 through 3 (median 8.54%, both statistically different from 0). While these numbers are biased upward since they are not inflation adjusted, they at least suggest, on average, that the firms did not shrink in their scale of operations.²¹

In contrast, the employment and number-of-segments data indicate re-trenchment. Mean employment fell 5.66% from Year 0 to 1 (median -4.42% both statistically different from 0), and fell 1.62% during the whole three year period (median, -1.60%). Mean and median employment changed relatively little, however, from Year 1 to Year 2 and from Year 2 to Year 3. Thus, on average the firms cut employment and they did it rapidly after the negative earnings; an average reduction of 1990 employees per firm from Year 0 to Year 1.²² The employment cuts are similar to the 5.7% reduction

²¹ There is little change in percentage of sales from foreign operations for the 24 firms with foreign sales data (a mean increase from 25.7% of sales in Year 0 to 28.6% of sales in Year 3).

²² The 1990 figure is taken from the aggregate employment figures which suggest the magnitude of the employment decline. Mean employment (calculated by summing total employment for all the firms and dividing by the number of firms in the sample) in thousands was 54.16 in year 0, 52.17 in Year 1, 51.48 in year 2 and 52.21 in Year 3.

found by Bhagat, Shleifer, and Vishny (1990) in the aftermath of successful hostile takeovers.

The segment data reveal similar information on the retrenchment of the firms. Eight firms (17%) increased the number of segments while almost twice as many ($N = 15$; 33%) reduced the number of segments. This is consistent with Comment and Jarrell's (1991b) findings that there was a trend toward increasing corporate focus among American firms in the 1980s.

B.2. Changes in Costs

Table VII reports evidence on changes in two variables that proxy for cost conditions—the percentage change in the ratio of the cost of goods sold to sales and the ratio of labor cost to sales. The cost of goods sold/sales measures the cost of generating sales, while labor costs/sales measures the labor costs of generating sales. Both variables suggest that in the short run the firms were able to reduce costs. Overall, from Year 0 to 3 the cost of goods sold/sales fell 1.97% (median -1.63% , both statistically different from 0), while labor cost/sales dropped 3.43% (median -4.24% , both statistically different from 0). The data from Year 0 to Year 1 and from Year 1 to Year 2 indicate that the firms cut these costs quickly.

B.3. Changes in Investment, R & D, and Advertising

Despite their financial difficulties the sample firms on average did not cut back on investment, especially when measured over the longer window. Mean investment/total assets increased 5.20% from Year 0 to Year 1 (median -2.16%), increased 39.22% (median 15.85%, both statistically different from 0) from Year 1 through Year 2, increases 22.79% (median 15.97%, both statistically different from 0) from Year 2 through Year 3, for an overall increase from Year 0 through 3 of 22.40% (median 10.30% both statistically different from 0).

On the other hand, the sample firms cut R & D quickly. For the approximately 26 firms with R & D data mean R & D/sales fell 5.32% (median 5.92%, both statistically different from 0) from Year 0 through Year 1, fell 9.18% (median -7.16% , both statistically different from 0) from Year 1 through Year 2, and overall dropped 5.25% (median 4.35%, both statistically different from 0) from Year 0 through 3.

Finally, there is evidence the firms with advertising expenditures cut those expenses quickly. Mean advertising/sales fell 6.48% from Year 0 to 1 (median -5.38%) and fell -4.72% (median -4.01%) over the period from Year 0 to 3. While none of these declines are statistically different from 0 this is in part due to the small sample size.

Thus, we find the sample firms increased investment while reducing R & D and advertising. Other research has examined changes in these variables after takeovers. For example, Smith (1990), Kaplan (1989), Lehn, Netter, and

Table VII
Measures of Change in Cost, Investment, R & D, and Advertising in Sample Period

Cost Measure	Percentage Change from Year <i>i</i> to Year <i>j</i>			
	0 to 1	1 to 2	2 to 3	0 to 3
Cost of goods sold/sales	<i>N</i> = 44	<i>N</i> = 44	<i>N</i> = 45	<i>N</i> = 44
Mean	-4.16	-1.49	-0.44	-1.97
(<i>t</i> -statistic)	(-4.82)*	(-1.56)	(-0.59)	(-3.94)*
Median	-3.39*	-1.41*	0.20	-1.63*
Labor cost/sales	<i>N</i> = 22	<i>N</i> = 21	<i>N</i> = 21	<i>N</i> = 22
Mean	-3.04	-3.91	-2.24	-3.43
(<i>t</i> -statistic)	(-1.33)	(-2.00) [†]	(-1.34)	(-2.38) [†]
Median	-5.68 [§]	-6.91 [†]	-2.39	-4.24 [†]
Investment, Research and Development, and Advertising Measures				
Investment/total assets	<i>N</i> = 45	<i>N</i> = 45	<i>N</i> = 45	<i>N</i> = 45
Mean	5.20	39.22	22.79	22.40
(<i>t</i> -statistic)	(0.63)	(2.33) [†]	(2.83)*	(3.87)*
Median	-2.16	15.85 [†]	15.97*	10.30*
R & D/sales	<i>N</i> = 26	<i>N</i> = 25	<i>N</i> = 26	<i>N</i> = 27
Mean	-5.32	-9.18	0.28	-5.25
(<i>t</i> -statistic)	(-1.77) [§]	(-2.40) [†]	(0.07)	(2.90)*
Median	-5.92 [†]	-7.16*	1.18	-4.35*
Advertising/sales	<i>N</i> = 15	<i>N</i> = 14	<i>N</i> = 12	<i>N</i> = 15
Mean	-6.48	-2.82	0.24	-4.72
(<i>t</i> -statistic)	(-0.79)	(-0.41)	(0.07)	(-1.09)
Median	-5.38	-11.84	3.10	-4.01

* For a *t*-statistic denotes the mean is statistically different from 0 at the 1% level, for a median indicates the median is statistically different from 0 at the 1% level using a Wilcoxon sign rank test.

[†] For a *t*-statistic denotes the mean is statistically different from 0 at the 5% level, for a median indicates the median is statistically different from 0 at the 5% level using a Wilcoxon sign rank test.

[§] For a *t*-statistic denotes the mean is statistically different from 0 at the 10% level, for a median indicates the median is statistically different from 0 at the 10% level using a Wilcoxon sign rank test.

Poulsen (1990), and Muscarella and Vetsuypens (1990) find that leveraged buyout firms reduce capital expenditures after the transaction. Smith reports that from Year -1 to Year 1 around a management buyout the median capital expenditures as a percent of sales fell 18%. In comparison, other researchers have found little changes in R & D after takeovers (see for example Hall (1988) and Smith (1990) who finds statistically insignificant cuts in R & D intensity after a management buyout).

In sum, we find for our sample of firms under severe pressure from the product markets a greater willingness to increase investment and reduce R & D than firms directly subject to the discipline of the takeover market. We

Table VIII
Measures of Changes in Financial Policies in Sample Period

Capital Structure	Percentage Change from Year <i>i</i> to Year <i>j</i>			
	0 to 1	0 to 2	0 to 3	
Debt/Total assets	<i>N</i> = 46	<i>N</i> = 46	<i>N</i> = 46	<i>N</i> = 46
Mean	-8.43	-1.91	-0.96	-3.77
(<i>t</i> -statistic)	(-1.61)	(-0.48)	(-0.23)	(-1.88) [§]
Median	-12.60*	-6.06	-6.69	-7.05 [†]
Changes in Dividend Policy	<i>N</i> (%)			
Up	19 (41)			
Down	8 (17)			
No change	5 (11)			
Down & up	13 (28)			
Up & down	0 (0)			
Never paid	1 (3)			
Omitted dividends				
During sample period	7 (15)			
Restored in sample period	6			
Before sample period	6 (13)			
Restored in sample period	5			
Stock repurchase	19 (41)			
Pension termination	6 (13)			

* For a *t*-statistic denotes the mean is statistically different from 0 at the 1% level, for a median indicates the median is statistically different from 0 at the 1% level using a Wilcoxon sign rank test

[†] For a *t*-statistic denotes the mean is statistically different from 0 at the 5% level, for a median indicates the median is statistically different from 0 at the 5% level using a Wilcoxon sign rank test.

[§] For a *t*-statistic denotes the mean is statistically different from 0 at the 10% level, for a median indicates the median is statistically different from 0 at the 10% level using a Wilcoxon sign rank test.

do not know, of course, whether the differences are due to the different characteristics of firms that remain independent from those taken over or because there is a difference in the way firms respond to the disciplining effects of the takeover market as compared to that of the product markets.

C. Changes in Financial Policies

In Table VIII, we report data on changes in financial policies, including the percent change in the debt/total asset ratio, dividend payment changes, stock repurchases, and pension terminations. On average the sample firms reduced leverage quickly. From Year 0 to Year 1, mean debt/total assets declined by 8.43% (*t* = -1.61) while the median fell a statistically significant 12.60%. Overall from Year 0 to 3 mean debt/total assets declined 3.77%, while the median fell 7.05%, both statistically different from 0.

In the year of negative earnings, the firms had an average debt/total assets ratio of 26.1%. Similarly, Friend and Lang (1988) find this ratio to be about 25% for all NYSE firms and Weston, Chung, and Hoag (1990, p. 123) report the average 1986 total debt/asset ratio of manufacturing firms to be 26%. After the firms reduced leverage, however, the average debt/asset ratio had fallen by Year 3 to a mean debt/asset ratio of 21.3%.

Most of the sample firms, 41 (89%), changed their dividend policies and on average they were more willing to cut dividends than firms in general. During the sample period, 41% of the firms raised dividends, 17% lowered dividends, an additional 28% first lowered and then raised dividends and 3% never paid dividends. Contrast this with the data in *Moody's Dividend Record* which reports dividend changes yearly for 8500 publicly held issues. According to *Moody's*, from 1980 to 1988 on average 41% of the issues per year raised dividends and 4% per year lowered or omitted dividends. In our sample 45% of the firms cut dividends at some point in the sample period, and were more willing to cut dividends than firms in general. The firms in our sample, however, did not cut dividends as often as those studied by DeAngelo and DeAngelo (1990) in their study of NYSE firms in severe financial distress. They find that 97.5% of the financially distressed firms eventually cut or omitted dividends. Factors such as debt covenants, however, may have mandated dividend cuts in their sample. Additionally, our firms did not cut dividends as often as the seven steel firms studied by DeAngelo and DeAngelo (1991), where every firm cut dividends and all but one omitted dividends, in part to aid in negotiations with unions.

We examine two other financial policies popular in the 1980s, share repurchases and pension terminations. In our sample, 19 firms (41%) announced a share repurchase. This is slightly lower than one would expect extrapolating from Comment and Jarrell's (1991a) finding that 1197 exchange-listed firms announced repurchases from 1985 through 1988. While the samples are not strictly comparable, the data indicate that our sample firms repurchased shares at a relatively low rate, presumably due to the financial distress. Six firms (13%) raised cash by terminating their overfunded pension funds using the sample of pension terminations developed by Mitchell and Mulherin (1989). The percentage of pension terminations is similar to that found after takeovers by Pontiff, Shleifer, and Weisbach (1990).

V. Conclusion

The corporate restructuring wave of the 1980s provided an unprecedented opportunity for financial economists to study various aspects of firm and management behavior. Our understanding of the firm has been enhanced with evidence from takeovers, defensive actions, regulatory responses, new financial instruments, restructurings, leveraged buyouts, managerial compensation, bankruptcies, and financial distress. In this paper we attempt to fill in a neglected area in the study of firms, how firms that do not have a change in control respond to performance declines.

We examine the responses to performance declines (negative earnings) by a sample of 46 large firms that were not taken over and did not file for Chapter 11. We document the reported causes and responses to the negative earnings. More importantly, we examine the restructurings the firms undertook as responses to poor performance. When possible, we compare our findings with those in other studies for evidence on the relative importance of the changes in the sample firms.

We find systematic patterns in both the reported causes of the negative earnings and the reported responses. Overwhelmingly, the firms and analysts blamed the poor performance on exogenous factors including economic conditions and competition (especially foreign). Reported responses generally focus on cost cutting and shrinkage.

More importantly we examine observable changes in the firms' control, operations, and financial policies. First, there is no evidence of unusual changes in the management succession process; the frequency of management turnover in the sample firms is consistent with that found on average across all firms, and is less than what other research has found for firms in financial distress or following a takeover.

In contrast, the evidence indicates significant changes in operations and financial policies. The data suggest that the firms retrenched quickly and increased their focus. There were significant cutbacks in employees; in the year immediately following the negative earnings, average employment fell by around 5% (almost 2000 workers per firm). There was also a decrease in the number of segments in which the firms operated and costs of production fell. In the longer run, however, sales and assets grew slightly. The firms also cut R & D, but increased investment. Finally, the firms changed their financial policies by cutting debt and dividends. On average the firms reduced their debt/asset levels 8.43% in the first year after the negative earnings, and tended to cut dividends more than firms in general.

In the 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. We find, for example, 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. Therefore, it is important to understand the workings of other sources of discipline of corporate managements such as the product markets and the internal corporate governance system. This study of the responses of firms to severe product market pressure will hopefully add to this understanding.

Appendix

Responses to poor performance. Reasons for decline in parentheses, outside changes that affected firm's recovery in brackets,* indicates that there was some mention of recovery or turnaround.

Amerada Hess—purchased reserves, initiated successful drilling, repurchased stock, called for regulation, increased natural resource base, reduced capital expenditures, lowered debt, cut employment, changed to LIFO accounting, suspended dividend (decline and low level of crude oil prices, high costs of finding reserves, FIFO accounting, poor acquisitions)

*American Airlines**—cut costs especially labor costs, expanded into new domestic markets (recession, deregulation, competition lowered prices, high fuel prices), [economy recovered, lower fuel prices]

*Asarco**—cut costs including wages and employment, reorganized to reduce levels of management, reduced debt, restructured from being a smelter to becoming a low cost metal producer, acquisitions including reserves, took cash from overfunded pension fund (low metal prices), [change in copper prices]

Alcoa—cut costs including managers' pay, after period of diversification, went back to core business, sold subsidiaries, closed plants, reduced capacity, reduced debt, improved quality (price of aluminum falls, recession, weak dollar helps foreign competition, world overcapacity), [price of aluminum increases]

*Ashland Oil**—emphasized the core business through divestitures, expanded growth businesses, concentrated on core, cut expenses, reduced debt and redeemed preferred stock, repurchased stock, called for regulation against subsidized foreign competition (writeoffs from divestitures in a restructuring) [lower oil prices, increase in demand for chemical products]

*AMAX**—the board replaced the CEO, sold unprofitable businesses, issued equity, acquired aluminum company, replaced officers, expanded gold operations, (recession, low metal prices, excess capacity, too much debt, world competition, over diversified) [price of aluminum increases shortly after the acquisition of an aluminum company, increase in gold prices]

*Armco**—restructured toward core, sold the non-steel businesses, modernized (improper diversification, bad management took too many risks, recession, oil downturn, too much debt) [import quotas, improvement in industry conditions]

*Bethlehem Steel**—sold assets to downsize, renegotiated borrowing and reduced debt, modernized and changed product mix, reduced wages, modernized and closed plants, reduced capital expenditures, lobbied for import restrictions, replaced top manager (too much debt, imports, recession, inefficient, poor product mix, poor quality and delivery) [falling dollar and restrictions on imports]

*Black and Decker**—cut costs, changed production methods, closed plants, reduced overhead, moved production overseas, developed new products, invested in inventory, acquired GE small appliance division, changed marketing to capitalize on brand name (worldwide competition increased, writeoff from restructuring, more advertising) [weak dollar]

Burlington Northern—restructuring split company into two focused firms: rail (spinoff to shareholders) and energy (sold to public), retired debt and then raised debt (deregulation, writedowns, lower oil and natural gas prices)

*Caterpillar**—cutback, closed plants, reduced employment, changed management structure, implemented foreign sourcing, price concessions from suppliers, entered new markets, developed new products, cut prices (strike, overcapacity, high dollar, recession, foreign competition, poor U.S. relations with Soviets) [demand for highway repair increased product demand]

*Champion**—divested, reduced debt, decentralized management structure reducing layers of management, reduced capital expenditures, reduce employment, concentrated on paper (accounting charges for restructuring after acquisition) [higher paper prices]

Coastal—cut costs, reduced debt, improved efficiency, refocused, changed product mix (oil prices fall, deregulation, strike, loss for mothballing super-tanker) [cold weather]

*Chrysler**—sold assets, cut costs, cut employees and wages, brought in new managers, increased efficiency, instituted federal loan guarantee, new products, and acquisition (bad products, costs too high, foreign competition, inflation—economy) [import quotas, economy improved, tax cut]

Delta—cut costs, reduced wages, sold old planes and purchased new planes, improved marketing, increased debt, expanded into new markets (price cuts due to competition, recession, high labor costs) [strike at competitor, improving economy]

*Deere**—cut costs, downsized, reduced employment, improved production efficiency, refocused on core, introduced new products, lobbied for free trade, lowered debt (foreign competition, depressed agriculture markets, strike) [economic recovery]

Dresser—restructured to downsize and focused on strength and divestitures, reduced debts, shared repurchase, embarked on joint venture [declining oil and gas—especially drilling—market, debt]

*Eaton**—restructured to reduce production costs by: eliminating capacity and selling unprofitable business, acquired compatible businesses, cut debt, developed new products, improved inventory efficiency (recession, high interest rates, foreign competition, diversification) [economic recovery]

*Enserch**—sold assets, spin-offs to partnerships and public, entered new business, reduced employment, argued to restrict imports (depressed energy markets) [gas price increase]

*Fluor**—asset sales, reduced debt, focused on core in restructuring, changed markets (low precious metal prices, weak construction demand, competition in foreign markets) [capital spending increases including increases in states' spending on infrastructure repair]

*Ford**—cut costs, reduced capacity, reduced workforce, used new production techniques, introduced new products, argued for protectionism, expanded foreign sales, improved quality (recession, high interest rates, import competition, costs of retooling) [economic recovery, restrictions on imports]

*GATX**—sold assets, concentrated on becoming service company, (over-supply of petroleum and coal, debt, bad acquisitions, recession, increased maintenance costs)

General Motors—reduced costs, cut wages, and employment, introduced

new products, embarked on joint ventures, implemented new production methods (recession, high interest rates, foreign competition, change in market toward small cars) [economic recovery]

*Grace (W.R.)**—divested, invested in core business, (poor management, slump in agriculture, poorly performing businesses, purchase of blockholder's shares with debt)

*Halliburton**—restructured to downsize, cut costs, reduced capital expenditures, cut management layers, embarked on joint venture, (depressed drilling and oil market) [economic recovery]

*Ingersoll Rand**—downsized, cut costs, closed plants, reduced employment, began joint venture, exited from unpromising businesses, (recession, world competition) [weak dollar, import curbs, economic recovery]

*Inland Steel**—cut costs, reduced employment, cut wages, closed plants, reduced capacity, entered new markets (depressed industry, foreign competition, slow to make cuts) [import quotas, weak dollar]

*Intel**—new products, closed plants, reduced work force, increased capital and R & D expenditures, exited from some businesses, new markets (costs of developing new product, restructuring costs, market weakness, foreign competition, poor marketing)

*Kerr McGee**—cut costs, reduced employment, sold assets, reduced debt (fall in energy prices, writedowns) [price changes]

*Louisiana Pacific**—lowered inventories, changed product mix, lobbied government for timber regulation, lowered wages through concessions and decertified unions, bought land (high interest rates, depressed housing market, worldwide competition) [economic recovery, favorable result in reimbursement from government for land]

*Mead**—reduce debt, consolidated to cut costs, divested, expanded in growth areas including government market, (recession, litigation settlement, interest expense, strike, import competition, overexpansion)

*Monsanto**—sold assets and exited from some businesses, changed product mix, changed from chemical company to biotech company, introduced new products (debt, slump in markets, acquisition)

Murphy Oil—waited for oil prices to recover, reduced debt and purchased reserves (natural gas price decline, low lumber prices) [higher oil prices]

*Olin**—closed plants, divested, made acquisitions and joint ventures, shared repurchase, increased debt (recession, startup costs, falling prices, foreign competition)

*Phelps Dodge**—cut costs, sold businesses and mines, spent on new technology, closed high cost smelters, lowered wages, reduced employment, spent on low cost production facilities, sold new equity (falling copper prices, foreign competition) [demand for copper increases, third world producers have difficulties]

*Reynolds Metals**—lowered production costs by increased foreign production and use of recycled aluminum, diversified through acquisition entering new markets, closed plants (recession, low cost competition, high production

costs, writeoffs, capital spending) [increase in aluminum prices, big gold discovery on bauxite property]

Sonat—reduced costs and employment, sold assets, changed contracts, made joint venture (economic conditions, oil and natural gas price low, restructuring costs, competition)

*Texas Instruments**—cut costs, reduced employment, cut wages, closed plants, sold assets, improved quality, improved marketing and consumer relations, introduced new products, (economic conditions, competition, strong dollar, management mistakes focusing on production not marketing) [market recovery]

*Union Carbide**—became more focused, reduced employment, sold assets, repurchased stock, increased debt then reduced debt (foreign competition, strong dollar, restructuring charges, management problems) [weak dollar, lower interest rates, increased foreign sales]

*Union Pacific**—cut costs, closed plants, reduced employees, moved offices, reduced management layers, new equipment and acquisition, improved customer service, repurchased stock, tied executive bonuses to performance, hired new CEO (too many employees, wages too high, special charges and writedown, poor management, deregulation, bad acquisitions)

United Airlines—lowered costs, reduced employment, reduced debt, hired new CEO, diversified into new markets then returned to core through divestments, changed name, reduced and changed management (deregulation, strike, high fuel costs, failed diversification)

*United States Steel**—lobbied for trade restrictions, downsized steel, cut employment, cut capacity, moved toward energy, diversified, changed name, sold assets, reduced debt, improved pricing, repurchased stock (recession, strike, cost of acquisition, low oil prices, foreign competition)

*Valero Energy**—spinoff pipeline to limited partnership, divested, restructured and reduced debt (price of oil down, poor hedging, writedown from asset sales) [oil price increases]

*Warner Lambert**—controlled costs, divested, shifted production overseas, improved products, introduced new products (poor acquisitions, writedown, too little R & D, unanticipated side effects from product) [weak dollar helps foreign sales]

*Whitman**—became more focused, constantly restructured, divested, made acquisitions, changed name (writeoffs from restructuring)

*Williams Companies**—reduced size, became more focused, divested, issued equity, reduced debt, moved into new markets (competition, deregulation, warm weather, poor real estate investment) [lower taxes]

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