

**EARNINGS MANAGEMENT AND PERFORMANCE
OF MALAYSIAN IPO FIRMS**

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ABSTRACT

This dissertation examines several issues related to the initial public offering (IPO) firms in Malaysia. The main aim of this study is to investigate whether IPO firms in Malaysia that goes public during the period of 1997-1998 have reported earnings in excess of cash flows by taking positive accruals. A sample of 84 IPO firms listed on the KLSE during that period is used in this study.

The results reported in this study suggest that IPOs in Malaysia during the period 1997-1998 manage their earnings upwards prior to public listing. This study views that IPO firms experienced poor long-run performance after being listed on the Kuala Lumpur Stock Exchange. In measuring the IPOs share price performance, the study measures abnormal returns using a buy-and-hold return approach. Abnormal returns are calculated based on the difference between the holding period returns of sample firms and control companies. Control companies matched by industry and size are selected from the population of non-equity offering in that particular year.

The statistical tests performed confirmed that the IPO firms experience a significant positive abnormal return during the initial period and a significant poor long run share price performance relative to non-IPO firms after being listed on the KLSE. However, there is no evidence found in the study to suggest that the pre offering earnings management is able to predict the post issue on negative abnormal returns. Thus, the results reveal that Malaysian IPOs, which manage earnings upward prior to public listing, may not have the intention to mislead their investors.

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CHAPTER ONE

INTRODUCTION

1.0 Introduction

The general purpose of financial statement is to provide information about the financial position, performance and cash flows of an enterprise that is useful to a wide range of users in making economic decisions. In addition, Skinner and Dechow (2000) affirm that the primary focus of financial reporting is information about an enterprise's performance provided by measures of earnings and its components. Accruals accounting attempts to record the financial effects on an entity of transactions and other events and circumstances that have cash consequences for the entity in the periods in which those transactions, events, and circumstances occur rather than only in the periods in which cash is received or paid by the entity.

The principal goal of accrual accounting is to help investors assess the entity's economic performance during a period through the use of basic accounting principles such as revenue recognition and matching. There is evidence that as a result of the accruals process, reported earnings tend to be smoother than underlying cash flows and that earnings provide better information about economic performance to investors than cash flows (Skinner and Dechow, 2000).

However, Wan Yusoff (2001) argues that the inappropriate practice of an increasing number of public listed companies in managing and smoothing reported earnings is drawing serious concerns from various users of accounting information. The issue of earnings management continues to attract debate and controversy. Until this year (2001), the practice of earnings management is often viewed with negative connotations with blames placed on the ulterior motives and unethical practices by managers to achieve personal gains. Burns and Merchant (1990) affirm that these practices could be misleading to users of the information and, over time, reduce the credibility of accounting numbers and thereby damage the reputation of the accounting profession.