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INTRODUCTION

For almost three years, beginning in July 1997, Malaysia's economy was badly affected by the financial crisis. The crisis affected both Local Majority Equity Companies (LMECs) and Foreign Majority Equity Companies (FMECs) listed on the KLSE.

Following the definition given by Department of Statistics (DOS), the Local Majority Equity Companies (LMECs) were identified as companies with over 50 percent of their equity owned by local shareholders. The LMECs in Malaysia can be recognized through few characteristics. Most of the LMECs were Government-Linked Companies (GLCs) such as Petronas Gas Berhad and Hicom Holdings Berhad. According to Lee (1994) GLCs were classified into two types of companies, which are public enterprises that were privatised and private companies which government has substantial equity participation of 34 percent or more.

It was also implied that majority equity of LMECs were owned by the government and trust agencies. For example, the trust agency, Permodalan Nasional Berhad held 30 percent stake in KFC Holdings (early 1990s). In Petronas Gas Berhad (2000), 0.33 percent of equity was held by government through Khazanah Nasional Berhad and 41.56 percent held by trust agencies. According to the Second Outline Perspective Plan 1991 – 2000, Malaysian government supported the local companies through the allocation of contracts, quotas, the provision of education and training and credit facilities to execute their business. The public enterprises and trust agencies also provided effective support for the development of local businesses.

Meanwhile, the Foreign Majority Equity Companies (FMECs) were defined as companies with the equity owned by foreign investors exceeding more than 50 percent. This definition has given by the Department of Statistics (DOS).

Most of the FMECs were subsidiaries to the established Multinational Corporations (MNCs). The study done by Fong (1990) regarding 10 MNCs in Malaysia stated that these companies had good linkages with their parent companies, mainly from USA and Japan. The study showed that technology was transferred through importation of capital equipment and acquisition of technical know-how from their parent companies. According to Phang (1994) foreign companies brought in improved technology, marketing channels and managerial inputs, which facilitated production and improved competitiveness of Malaysia products in the world market. The Malaysia Government also designed an attractive package of fiscal incentives in the forms of pioneer status, labor utilization, special incentives for export-oriented industry and investment tax credit to foreign companies as mentioned by Chee and Lee (1979).

In addition, based on market capitalization of all samples in this study (Appendix 1 and Appendix 2), it indicated that the FMECs had bigger market capitalization as compared to the LMECs although they were comparable in size. This report concurs with Phang (1998) who showed that although local firms are comparable in size with foreign firms but in general foreign firms are bigger in size.

During the 1997 – 1998 financial crisis, the local stock market was badly affected. The Economic Report of 1997/98 stated that the KLCI is fall to its lowest level since 20 April 1993 of 675.15 points in September 4, 1997. Companies with excessive borrowing had to struggle against the currency volatility in order to survive due to the weakening of the Ringgit. The situation became critical when some local companies suffered debt problems. For instance, Hicom and Gadek were among the companies that face debt problems. This is due to the companies being exposed to foreign loans and dealings with foreign currency. Nor Azizan (2000) in her study explained further that Bumiputera-controlled companies and non-Bumiputera companies suffered during the crisis due to debt problems.

However, foreign companies had unlimited sources of capital and were fully backed up by parent or holding companies, agreed by Fong (1990), Rasiah (1995) and Phang (1998). In view of this, it can be expected that foreign companies were able to withstand the crisis better than local companies. Furthermore, the weakening Ringgit did not affect them much as they were dealing with US Dollar.

1.1 OBJECTIVES OF STUDY

This study attempts to examine the performance of the local and foreign companies listed on the Kuala Lumpur Stock Exchange (KLSE) before and during the financial crisis by analyzing the companies' stock return. In this research, the samples of the listed companies on the KLSE were categorized into two groups, namely, the Local Majority Equity Companies (LMECs) and the Foreign Majority Equity Companies (FMECs).

In line with these, the specific objectives are:

1. To analyze the performance of the Local Majority Equity Companies (LMECs) before and during the crisis.

2. To analyze the performance of the Foreign Majority Equity Companies (FMECs) before and during the crisis.

3. To compare the performance of the LMECs and FMECs before the crisis, during the crisis and due to the crisis (during the crisis minus before the crisis).

4. To examine the wealth impact of the crisis on the LMECs and FMECs.

In order to see the effect of the financial crisis, this study analyzed the performance of the Local Majority Equity Companies (LMECs) and Foreign Majority Equity Companies (FMECs) before and during the crisis. It would be expected that the Local Majority Equity Companies (LMECs) were more affected during the crisis as compared to Foreign Majority Equity Companies (FMECs). The study by Phang (1998) explained that local companies had limited sources of capital. In addition, majority of local companies had involved in debt problems (Nor Azizan, 2000).

This study is also expected to show the wealth impact of financial crisis on stock return of the LMECs and FMECs in order to prove the hypothesis that LMECs were more affected due to the financial turmoil.

1.2 CONTRIBUTION

The need to study the performance of local companies and foreign companies was significant in Malaysia due to few reasons. First of all, the foreign participation in Malaysia remains the highest in Asian Region (Business Times, 2000). Second, many people believed that foreign companies contributed more to the economic development as Rasiah (1995) mentioned that the need to foreign capital was crucial in the growth of manufacturing sector in Malaysia. Third, very limited empirical studies concerning the performance of local companies and foreign companies in Malaysia have been done previously.

In the two local research that was done separately by Rasiah (1995) and Phang (1998), both generally showed that the foreign companies were better than local companies. However, both of the research were carried out by using the interpretative and survey method. Rasiah (1995) did the study during the bullish market while Phang (1998) studied it during the bearish market condition. As such the current study is the first attempt to study the performance of local companies and foreign companies by applying the empirical and event study method. Using the daily and monthly closing prices, this study extends the data sample to the most recent periods (January 1995 to December 1999) that covered the bullish and bearish market period.

The findings of this study can provide an overview of the performance of the Local Majority Equity Companies (LMECs) and Foreign Majority Equity Companies (FMECs) in Malaysia. This study also aims to contribute to an overview of the impact of the crisis on the local companies and foreign companies listed on the KLSE. Thus it will provide investors and policy maker with valuable information for decision making pertaining LMECs and FMECs. Finally, the results of the study can also be useful to everyone involved in the capital market.

1.3 ORGANISATION OF THE CHAPTERS

This study is organized into five chapters as follows; Chapter one gives the background of the research. It contains the importance of the study and objectives. It also explains the contribution of the study.

Chapter two discusses the existing literature on the topic. It reviews the financial crisis in Malaysia in relation to the local and foreign share equity performance. This chapter also reviews the participation of foreign equity and the relation to the increasing percentage of foreign fund. Finally it also looks at previous studies and theoretical issues regarding the topic.

Chapter three outlines the detail hypotheses and the research methodology used. It includes the discussion about sample selection, data sources and the duration of the study. Furthermore, the analysis techniques and statistical model used in this study were also explained.

Chapter four analyzes the research results obtained based on data analysis techniques and statistical tests.

Finally, chapter five summarizes the conclusions, recommendations and limitations of the study. It also includes suggestions for further studies.