

**New York University  
Leonard N. Stern School of Business**

**Corporate Bankruptcy & Reorganization  
B40.3198**

**Professor Edward I. Altman  
Spring 2005 (2<sup>nd</sup> Half)  
Mon/Wed 10:30-11:50 a.m.  
Room:**

This is a unique course in business administration curricula and has evolved in an interesting way over the twenty plus years that I have taught it. The original focus was on discussing and using corporate distress prediction models from an external fixed income security perspective. These statistical-multivariate models utilizing financial statement and market valuation variables have become standard analytical procedures in the financial world, especially as financial institutions prepare for Basel II. They are now complemented by a number of newer analytical approaches, including option pricing and artificial intelligence models.

While the financial distress prediction aspect is still an important part of the course, perhaps the more important perspective is now the valuation and analysis of distressed firms and their outstanding securities, primarily bonds and bank loans. Indeed, this course can now be followed by a companion mini-course on “Investing in Distressed Securities” (taught as an additional mini-course with the Bankruptcy & Reorganization course). Discussion and analysis of the high yield, junk bond market complements the distressed securities materials. Reorganization in bankruptcy cases explore this unique period in a company’s “life.”

The pedagogy of the course includes traditional lectures, case studies, guest speakers in bankruptcy law, turnaround management, corporate restructuring and “vulture” investing and a choice of either a take-home project (usually a complex case study), or a term paper related to the theme of the course. The latter project is discussed early in the course but is not due until the full semester is over. Students have the opportunity to present the findings of their term projects in a special, extra session at the end of the term. Incidentally, Stern has “hatched” at least four dozen vulture investors and traders of distressed securities over the years and this course is oftentimes the “breeding ground” for these successful “birds.”

Call me at (212) 998-0709 or visit my web site at [www.stern.nyu.edu/~ealtman](http://www.stern.nyu.edu/~ealtman) or email: [ealtman@stern.nyu.edu](mailto:ealtman@stern.nyu.edu)

## Course Outline

### I. General Course Description & Objectives

An in-depth study of practical and theoretical financial aspects and implications of corporate bankruptcy, credit analysis, and leveraged and distressed restructurings. Among the topics discussed are the bankruptcy-reorganization process; techniques and procedures to value firms in distress and/or reorganization; global implications of credit risk, predicting impending problems of various types of companies including manufacturing firms, retailers and commercial banks; the effect of bankruptcy on total share valuation; investment strategies relevant to distressed companies' securities; financial restructuring; high yield "junk" bonds; the emerging-market corporate debt market; and the implications of bankruptcy analysis to financial lending institutions and non-financial corporate management personnel. References will be made to recent corporate failures and cases as well as to empirical and theoretical scholarly and professional studies.

### II. Course Requirements & Instructions

The pedagogy of the course includes seminar-type discussion of issues and latest research in the field, analysis of case studies, guest speakers, and student presentations of their case-research reports. The major written requirement will be an in-depth report of a significant corporate bankruptcy or a paper related to the theme of the course. On some themes, students can work in small groups of two members. See partial list of bankrupt firms and paper themes attached. Each student is responsible for only one bankruptcy or one theme and therefore this report should reflect a major effort. It is possible to work on term projects with a partner. A take-home final exam is possible as an alternative to the paper. Participants of the course are also responsible for the required readings of each session's discussion and the case studies **(worked on by groups of two-three students)**.

This section is given in the first half of the semester followed by another mini-course on "Investing in Distressed Securities" taught by Professor Allan Brown. Students who are interested in the bankruptcy and distressed securities industry are encouraged to consider both of these courses.

## Required Materials:

- A. Edward I. Altman, **Corporate Financial Distress & Bankruptcy**, 2<sup>nd</sup> ed., John Wiley & Sons, 1993 or this book combined with selected chapters from **Managing Credit Risk, mentioned below in suggested Books list.**
- B. Packet of Handouts and Exhibits (provided in class)
- C. **Suggested** books (If “Investing in Distressed Security” and/or “Managing Credit Risk” is very important to you)
  - a. E. Altman, **Distressed Securities: Analyzing & Evaluating Market Potential & Investment Risk**, Probus, 1991, reprinted by Beard Books, 1999
  - b. J. Caouette, E. Altman & P. Narayanan, **Managing Credit Risk: The Next Great Financial Challenge**, John Wiley & Sons, 1998
  - c. H. Rosenberg, **The Vulture Investors**, John Wiley & Sons, 2000

## IV. Detailed Course Outline

### Session

### Dates Subject and Readings

- 3/10 **The Corporate Bankruptcy Phenomenon**
- Introduction to Corporate Financial Distress
  - Business failures and bankruptcies – chapter 1, 2
  - Defaults and bankruptcies in 2000-2003
  - Macroeconomic influences on business failures
  - Major players in the reorganization process
  - Valuation theory in a distressed reorganization – review basic concepts
  - Discussion of term projects
- 3/22 **The Bankruptcy-Reorganization Process – Legal & Economic Issues**
- The turnaround management industry – **guest speaker (representative of the TMA) best paper award competition**
  - The chapter 11 process – chapter 3
  - Emerging (emerged) trends – chapter 4
- 3/24 **Managing Credit Risk: A Global Challenge** – power point (PP file) article on Credit  
3/29 Risk and/or book on Managing Credit Risk (optional)
- Topic overview – key risk management area
  - Importance in low and high credit risk regions of the world
  - BIS regulatory issues
  - Default and recovery rates
  - Securitized credit instruments

- Traditional and new portfolio management techniques
- Introducing the **Duplan Case** – chapter 13 in text

**The Duplan Case should be worked out carefully; it will be discussed and collected on April 7. You must work in teams of two or three students.**

- 3/31 **Credit Scoring Models: Predicting Financial Distress**
- Chapter 8 – Z-Score and Z<sup>''</sup>-Score analysis
  - Chapter 9 – ZETA, KMV, Neural Networks, etc. (PP file)
  - For emerging markets-expanded version of Z<sup>''</sup>-Score
- 4/5 **Implications & Applications of Financial Distress Prediction Models**
- For investors – chapter 7
  - For bankers – chapter 10
  - For managers – the corporate renewal process – chapter 11 (in book)
  - Enron/WorldCom discussion
- 4/7 **Discussion of the Duplan Case**  
Chapter 13 (Case should be handed in; you must work with one or two other students).
- 4/12 **Corporate Restructurings: Leveraged & Deleveraged** (Chapter 6 and PP file)
- Asset and liability restructuring
  - Leveraged management buyouts
  - Linking theory with practice
  - Lessons from the 1980's and 1990's
- 4/14 **Adding Value through Restructuring** (PP file)
- Debt for equity swaps
  - Leverage management buyouts
  - Deleveraging strategies
- 4/19 **Guest Speaker on Corporate Distressed Restructurings from an IB firm standpoint: from Blackstone or Lazard Freres**
- Distressed financial restructuring
  - Investment bankers and turnaround management
  - Enron and Xerox restructurings
  - Current issues and career opportunities
- 4/21 **Guest Speaker on Turnaround Management from a Turnaround Manager's standpoint: Holly Etlin, Principal, XRoads Solutions Group, and President, TMA (International)**
- 4/26 **The High Yield Bond and Distressed Securities Markets** (PP files)
- Evolution and current status of the market
  - Risk and return analysis

- Traditional default and mortality rate methods
- Estimating the probability of default
- Major players and distressed investing strategies

4/28 **Guest Speaker on “Distressed Investing” – Allan Brown, Portfolio Manager, (*Concordia Capital*) or Marti Murray, President, (*Murray Capital*)**

- Are they really vultures?
- Selected case studies
- Some recent prominent situations
- Career opportunities

5/3 **Take-home final due (for those not doing term paper)  
and**

5/3 **Student presentation of term reports: all reports due**

- Attendance mandatory for all students, unless conflicting with other courses
- Date is tentative

**Grading:** Will be based primarily on the term project/take-home exam with smaller weights for cases and in-class contribution. Term project discussed in handout packet.

**Office Hours/Location:** Tuesday/Thursday: 2:00 – 4:00 p.m.  
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## POSSIBLE BANKRUPTCY PAPER TOPICS

### Sample Themes

Abuses of the Bankruptcy Code  
Accountants roles in bankruptcies  
Airline deregulation & bankruptcies  
Airline industry prediction model  
Argentina bank crisis  
Asset management companies (AMCs)  
Bankruptcy in e-commerce land  
Bankruptcy in the telecommunication industry  
Bankruptcy as a business strategy  
Bankruptcy and pension plans (PBGC)  
Bankruptcy and reorganization in the airline industry  
Bankruptcy expert systems  
Bankruptcy in Central and Eastern Europe  
Busted convertibles  
China's experiment in bankruptcy  
Claims purchases as a takeover technique  
Computer and electronic industry  
Corporate abuses and bankruptcy  
Corporate fraud and indirect bankruptcy costs  
Crisis in Japanese banking  
Critical events analysis and bond price reaction  
Debtor-in-possession (DIP) financing  
Emerging market debt models  
    -Corporates  
    -Sovereign  
Emerging Equity Investing  
Energy industry prediction model  
Equity performance after bankruptcy  
European Distressed Debt Market  
Fallen angels  
FASB 107 Disclosures  
Financial reporting consolidation (captives) & Z-Scores  
Foreign bankruptcy law  
Fraudulent conveyance  
Highly leveraged transactions (HLT)  
Investing in bankrupt equities  
Japanese bank problem loans  
Macro-default models  
Macro-influences model  
Municipal defaults  
Option pricing default models  
Power companies and public utilities  
Pre-packaged bankruptcies  
Rating Agencies  
Rating downgrade triggers  
Retail industry prediction model  
S&L debacle  
Telecommunications industry prediction model  
The new BIS regulation on credit assets  
Z-Scores for Japanese firms  
Z-Scores and investing

### Sample Companies

Adelphia  
Allegheny International/Sunbeam  
Allied & Federated Department Stores  
Ames Department Store  
Arch Wireless  
Armstrong World  
Bethlehem Steel  
Boston Chicken  
Braniff International (Chapter 33)  
Caldor  
Canary Wharf  
Columbia Gas System  
Continental Airlines (Chapter 22)  
Dow Corning  
Enron  
Euro Tunnel  
Federated Department Stores  
Gillette Holdings  
Global Crossing  
Globalstar  
Grand Union (Chapter 33)  
Greyhound  
Hills Department Stores  
Hillsborough (Jim Walter)  
Iridium  
ICO Global Communications  
Johns Manville  
Kaiser Aluminum  
Kmart  
Loewen  
Loral Space & Communication  
Montgomery Ward  
National Gypsum  
Olympic & York  
Pacific G&E  
Parmalat  
Polaroid  
Prime Motor Inns  
R. H. Macy & Company  
Resorts International  
Revco Corporation  
Spectrasite  
Southland  
Storage Technology  
Swissair  
Trump Plaza  
United Airlines  
USAirways (Chapter 22?)  
Wang Laboratories  
WorldCom  
Xerox Corporation  
Zale