The Relationship Between Risk Factors And Profitability of SP Setia Berhad

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Abstract

The objective of this study is in order to examine the profitability of property company that is SP SetiaBerhad with some risk impact factor which is liquidity ratio, credit ratio, operating ratio. In addition, this study also identify the possible variable that will cause the impact to profitability which include leverage, gross domestic product(GDP), inflation rate and exchange rate. The data of SP SetiaBerhad from 2011 to 2015 was found from the Bursa Malaysia website. According to the historical data, we found that the measurement of credit ratio is the main factor to influence the profitability of SP Setia Berhad. The profitability of this company is not volatile and more stable. Therefore, the investor who is risk adverse to be considered suitable to choose this kind of company. On the other hand, the variable such as leverage and gross domestic product(GDP) show it is positive insignificantly relationship with the ROA and however the inflation rate and exchange rate indicate they are negative insignificantly with ROA.

Keywords: liquidity ratio, credit ratio (counterparty risk), operating ratio, leverage, gross domestic product(GDP), inflation rate and exchange rate.
1.0 Introduction

SP Setia Berhad was founded in 1974 as an investment holding company based in Malaysia. SP Setia Berhad Group has grown into one of Malaysia's largest real estate developers.

SP setia is engaged in building contractor business. Its subsidiaries are engaged in property development, operating clubs, property investment holding, project management, contractors, building shrinkage, prefabrication, installation, sale of wood products, and provision of kiln dry service.

The company's business in Malaysia. The company is divided into three parts: real estate development, development of property; construction, construction and infrastructure construction, other, covering manufacturing, trade and investment.

The company's financial strength is defined as the company's financial position. Companies with good financial health are usually able to meet their financial situation well, pay in a timely manner, and know how to manage their money. Most investors are looking at the company's financial strength, if it is a stable outlook, means that investors can have confidence to invest.

In the SP SetiaBerhad Group's financial statements, the asset quality in 2010 was much higher than the asset quality in 2009. In 2009, total assets were $ 39.5 billion. However, this figure increased to RM43.8 billion. This means that the company is getting bigger and bigger.

Although the liabilities of SP SetiaBerhad in year 2010 is higher than year 2009, but the asset of it also increase. The company’s net worth or equity in 2010 is greater than year 2009, this mean that it is a healthy company. In a healthy company, the net worth should be constantly rising.

Although SP SetiaBerhad's debt in 2010 was higher than in 2009, its assets also increased. The company's net worth or share price in 2010 was greater than that in 2009, which means it was a healthy company. In a healthy company, the net worth should continue to rise.
2.0 Literature Review

The more complex the type of risk, the more professional management, concentration and control. Risk management is defined as the process by which banks act to control their financial risks. The process of risk management includes the basic steps of risk identification, risk analysis and assessment, risk audit monitoring, risk management or control. While the risk in simple terms can be measured using standard deviations, some risks may be difficult to measure and require more complex risk measurement methods. Good risk management is not only a defence mechanism, but also the company's aggressive weapons, which depends to a large extent on the quality of leadership and governance.

The formation of credit risk includes inappropriate credit policies, nonperforming loan practices, limited institutional capacity, fluctuate interest rates, mismanagement, inappropriate laws, direct loans, large bank licenses, low capital and liquidity risk, loose credit assessment, Poor underwriting, poor loan practices, inadequate supervision by the central bank, government intervention, and lack of knowledge about borrowers. Jensen (1986) pointed out that when the level of liquidity is low, working capital is insufficient, the enterprise is tense. This is because of lack of liquidity or excess liquidity may cause damage to the smooth functioning of the organization (Janglani and Sandhar, 2013).

The management of risk, assets and liabilities remains the core function of the listed company. Early signals of listed company crises can be observed from fluctuations in liquidity risk. The reduce in the inflation rate is encouraging company to active involve in the market. The increase in inflation could hurt company because the purchasing power reduce by the money.

The operational risk is the failure of process, people, system and procedure. One area that may involve operational risk is to maintain the necessary systems and equipment. If two maintenance activities are required, but it is determined that only one maintenance activity is available at the time, selecting a maintenance activity depends on which system is discarded and change the operational risk. If the system fails, the negative impact is directly related to operational risk.
In conclusion, company faces various risks such as interest rate risk, foreign exchange risk, political risk, market risk, liquidity risk, operational risk and credit risk. So that, board and management should develop policies and procedures to ensure that company have a good credit process, a strong combination of management methods, caution restrictions, effective credit review and loan classification procedures and appropriate methods used to handle problem risk. The early company prepare before crisis, the less risk exposure company may face.
3.0 Risk Assessment

For SP Setia Berhad, the liquidity ratio is higher in the 2011 compared with other years that is 2.61. That means the company less ability to pay debt obligations and its margin of safety is low in this year. The liquidity ratio is very low in the year of 2012 that is 1.74 only. This indicates that the organization have already improved such as increased total assets and decreased total liability. The company faces the lower liquidity risk in the overall 5 years.

The organization’s credit ratio is highest in the year of 2012 in the overall 5 years which is 170.53. This is because SP Setia invested a strategies location which is located at JalanAmpang, Kuala Lumpur, also known as the Embassy Row. It is nearby to Petronas Twin Towers. It cause the company faces a high risk if the project is not success. However, the company improved gradually in the following years. As a result, the company reduces the credit risk from 170.53 to 114.40 from the year
of 2012 to the year of 2015, that reduced 32.91% of its credit risk. From the data, the company may success to conduct its project of JalanAmpang, Kuala Lumpur because of its credit ratio shows down trend.

![Operating ratio chart]

For the operating risk, the company always increase from the year by year. It is 3.18 in the year of 2011 to 2.11 to the year of 2015, that reduced 50.71%. This indicates that the company is not effectively control its internal procedures, people and systems. They do not gather the latest and comprehensive information and make the right decision. It cause the company failure to take the optimum decision that can bring the positive impact for maximizing shareholder’s value.

4.0 Company performance

**Descriptive analysis :**

![Relationship Between liquidity ratio, operating ratio and ROA chart]
Based on the liquidity ratio and ROA in this company, they are insignificantly positive. ROA decrease from the year of 2011 to the year of 2012, that is from 0.058 jump to 0.041. Liquidity ratio also drop from the year of 2011 to the year of 2012, which is from 2.61 to 1.74. According to the graph, while in the period of 2012 to 2013, the liquidity ratio shows it is uptrend signal from 1.74 in 2012 to 1.8 in 2013 whereas the ROA shows the downtrend signal from 0.041 in 2012 to 0.034. In the period of 2013 to 2014, ROA rise from 0.034 to 0.039 and liquidity ratio also increase from 1.80 to 1.98. In the 2014 to 2015, ROA increases from 0.039 to 0.062 while liquidity ratio reduces from 1.98 to 1.95. This illustrate that the both relationship between liquidity ratio and ROA is neutral relationship between each other. The result also indicates that the liquidity ratio is not a big factor to impact on the profitability of this company.

Besides, operating ratio and ROA is not directly relationship between each other from this company. In the year of 2011 to 2012, ROA reduces from 0.058 to 0.041 while operating ratio also from 3.18 to 2.45. Although the year of 2011 and 2012 indicate the both ratio is positive relationship. However, it shows different result in the year of 2012 to 2013. When ROA decreases from 0.041 in 2012 to 0.034 in 2013, the operating ratio increases from 2.45 in 2012 to 2.88 in 2013. In the year of 2013 to 2014, ROA increase from 0.034 to 0.039 while operating ratio drop from 2.88 to 2.43. In the year of 2014 to 2015, ROA increase from 0.039 to 0.062 while operating ratio also from 3.18 to 2.45. Therefore, we can conclude that both of the ratio is not have the directly relationship.

According to the graph, when the credit ratio increase from 2011 to 2012, the ROA decrease its ratio within this period. While in the period of 2012 to 2013, the
credit ratio shows it is reducing whereas the ROA shows the downtrend signal also. In the period of 2013 to 2014, ROA rise from 0.034 to 0.039 and credit ratio decrease from 167.05 to 150.93. Both of its shows the negative relationship. In the 2014 to 2015, ROA increases again from 0.039 to 0.062 while credit ratio reduces from 0.039 to 0.062. From the overall 5 years of ROA and credit ratio, we can conclude that credit ratio and ROA are insignificantly negative relationship.

SP SetiaBerhad's has been affected by the global economic slowdown and political unstable in Malaysia in the year of 2012. Its asset is not working efficiently due to lower inventory turnover. This scenario happen when the asset rises and the rate of return does not increase in the same proportion.

<table>
<thead>
<tr>
<th>Descriptive Statistics</th>
<th>Mean</th>
<th>Std. Deviation</th>
<th>N</th>
</tr>
</thead>
<tbody>
<tr>
<td>ROA</td>
<td>.04680</td>
<td>.012398</td>
<td>5</td>
</tr>
<tr>
<td>Liquidity ratio</td>
<td>2.0160</td>
<td>.34689</td>
<td>5</td>
</tr>
<tr>
<td>Credit ratio</td>
<td>148.2200</td>
<td>22.93492</td>
<td>5</td>
</tr>
<tr>
<td>Operating ratio</td>
<td>2.6100</td>
<td>.42006</td>
<td>5</td>
</tr>
<tr>
<td>Leverage</td>
<td>57.478529857485340</td>
<td>9.695726142113577</td>
<td>5</td>
</tr>
<tr>
<td>GDP</td>
<td>5.300</td>
<td>.4950</td>
<td>5</td>
</tr>
<tr>
<td>Inflation rate</td>
<td>2.440</td>
<td>.6693</td>
<td>5</td>
</tr>
<tr>
<td>Exchange rate</td>
<td>3.4600</td>
<td>.49168</td>
<td>5</td>
</tr>
</tbody>
</table>

From the descriptive statistics, the standard deviation of ROA only 0.04680 shows that the values are closely to its mean which is 0.012398 within 5 years. That means the company’s ROA is low volatile and low risk signal. The risk-adverse investor who prefer lower risk is suggested to invest in this company. While the standard deviation of the credit ratio is 22.93492. It is really risky. That means the fluctuates of credit ratio is uncertainly and high volatile. The fluctuation of credit ratio of SP SetiaBhd is really uncertain within 2011 to 2015.
Table 2.0: Correlation Matrix SP SetiaBerhad Specific Risk Determinants to Profitability

Based on the table 2.0, liquidity ratio has a positive insignificantly relationship with ROA. This means that if the liquidity ratio decreases, the ROA will be decreases also. Besides, the relationship between ROA and credit ratio is negative significantly which is -0.895. It indicate that when credit ratio increase, ROA will be decrease. Furthermore, ROA and operating ratio show the negative insignificantly relationship. The rising of operating ratiowill cause the reducing of ROA. From the macroeconomic, the leverage and GDP variable shows positive insignificant relation to ROA while the inflation rate and exchange rate illustrate positive insignificantly relationship with ROA. In brief, credit ratio is the only significant variable for SP SetiaBhd with P value < 0.10 from the seven variable. That means the company should manage well of the counterparty risk. If not, it may cause the company failure in the future.

<table>
<thead>
<tr>
<th>Correlations</th>
<th>ROA</th>
<th>Liquidity ratio</th>
<th>Credit ratio</th>
<th>Operating ratio</th>
<th>Leverage</th>
<th>GDP</th>
<th>Inflation rate</th>
<th>Exchange rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pearason Correlation</td>
<td>1.000</td>
<td>0.599</td>
<td>1.000</td>
<td>1.000</td>
<td>1.000</td>
<td>1.000</td>
<td>1.000</td>
<td>1.000</td>
</tr>
<tr>
<td>Liquidity ratio</td>
<td>0.599</td>
<td>1.000</td>
<td>-0.441</td>
<td>1.000</td>
<td>1.000</td>
<td>1.000</td>
<td>1.000</td>
<td>1.000</td>
</tr>
<tr>
<td>Credit ratio</td>
<td>-0.895</td>
<td>-0.441</td>
<td>1.000</td>
<td>1.000</td>
<td>1.000</td>
<td>1.000</td>
<td>1.000</td>
<td>1.000</td>
</tr>
<tr>
<td>Operating ratio</td>
<td>1.122</td>
<td>0.624</td>
<td>0.317</td>
<td>1.000</td>
<td>1.000</td>
<td>1.000</td>
<td>1.000</td>
<td>1.000</td>
</tr>
<tr>
<td>Leverage</td>
<td>-0.885</td>
<td>-0.973</td>
<td>0.811</td>
<td>-0.652</td>
<td>1.000</td>
<td>1.000</td>
<td>1.000</td>
<td>1.000</td>
</tr>
<tr>
<td>GDP</td>
<td>-0.143</td>
<td>0.100</td>
<td>0.115</td>
<td>0.204</td>
<td>0.330</td>
<td>1.000</td>
<td>1.000</td>
<td>1.000</td>
</tr>
<tr>
<td>Inflation rate</td>
<td>0.206</td>
<td>0.784</td>
<td>0.281</td>
<td>0.454</td>
<td>-0.603</td>
<td>0.488</td>
<td>1.000</td>
<td>1.000</td>
</tr>
<tr>
<td>Exchange rate</td>
<td>0.561</td>
<td>0.116</td>
<td>-0.828</td>
<td>-0.682</td>
<td>-0.178</td>
<td>-0.198</td>
<td>-0.900</td>
<td>1.000</td>
</tr>
</tbody>
</table>

Sig [2-tailed] | ROA | Liquidity ratio | Credit ratio | Operating ratio | Leverage | GDP | Inflation rate | Exchange rate |
<table>
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<tr>
<th></th>
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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Liquidity ratio</td>
<td>0.143</td>
<td>0.228</td>
<td>0.228</td>
<td>0.228</td>
<td>0.228</td>
<td>0.228</td>
<td>0.228</td>
<td>0.228</td>
</tr>
<tr>
<td>Credit ratio</td>
<td>0.429</td>
<td>0.130</td>
<td>0.302</td>
<td>0.302</td>
<td>0.302</td>
<td>0.302</td>
<td>0.302</td>
<td>0.302</td>
</tr>
<tr>
<td>Operating ratio</td>
<td>0.110</td>
<td>0.027</td>
<td>0.137</td>
<td>0.137</td>
<td>0.137</td>
<td>0.137</td>
<td>0.137</td>
<td>0.137</td>
</tr>
<tr>
<td>Leverage</td>
<td>0.410</td>
<td>0.426</td>
<td>0.426</td>
<td>0.426</td>
<td>0.426</td>
<td>0.426</td>
<td>0.426</td>
<td>0.426</td>
</tr>
<tr>
<td>GDP</td>
<td>0.370</td>
<td>0.426</td>
<td>0.426</td>
<td>0.426</td>
<td>0.426</td>
<td>0.426</td>
<td>0.426</td>
<td>0.426</td>
</tr>
<tr>
<td>Inflation rate</td>
<td>0.183</td>
<td>0.056</td>
<td>0.224</td>
<td>0.224</td>
<td>0.224</td>
<td>0.224</td>
<td>0.224</td>
<td>0.224</td>
</tr>
<tr>
<td>Exchange rate</td>
<td>0.183</td>
<td>0.056</td>
<td>0.224</td>
<td>0.224</td>
<td>0.224</td>
<td>0.224</td>
<td>0.224</td>
<td>0.224</td>
</tr>
</tbody>
</table>
In the model summary, according to the R Square, it indicates that almost 80.1% of the ROA are explained by the credit ratio. Only 19.9% of ROA are explained by others. The adjusted R-Square of 0.735 indicates that ROA will be adjusted by the credit ratio in this property industry. This means that there are positive relationship between the amount of ROA, and credit ratio.

The exclude variable which is liquidity ratio, operating ratio, leverage, GDP, inflation rate and exchange rate. That is two positive variable and four negative variable with ROA. The positive variable includes liquidity ratio and operating ratio while negative variable which is leverage, GDP, inflation rate and exchange rate.
With the $P < 0.10$, this ANOVA model shows that the credit ratio has high influence to profitability.

Y=0.119+0(credit ratio)

The above showed the coefficient table for ROA and credit ratio. The coefficient showed that $Y=0.119+0$(credit ratio), where each increase of one unit brings no effects to ROA. The model means that profits are not dependent on the counterparty risk. Thus, even if that is high counterparty risk to SP SetiaBhd, however the company will still earn profits. This means that there is no relevant between profitability and counterparty risk. Ordinarily, SP Setia Bhd. should focus on other factors rather than the counterparty risk.
4.0 Discussion and Recommendation

**Enhancing and strengthen corporate governance structure**

The company have to stronger their board and management with the four pillars. The four pillars include accountability, fairness, transparency and independence. The chairman have to ensure the management is accountable to the whole board and every decision taken by whole board is responsible for shareholders. In addition, they should be protect shareholders right and put it as the company’s main purpose before take any action. Furthermore, the transparency of a board is really essential part to increase the efficient employee. Employee feel more involve in the company due to know about something what is going on and latest information directly relate to their task. For example, financial situation, performance, ownership and corporate governance. Besides that, the independent director should free from control by others. The role of independent director is supervise and evaluate the performance of company. Therefore, he should not have conflict of interest and must be objective in every decision also.

**Always update the latest knowledge about risk management tools and techniques**

Due to the company has risk management team already. So that, the team have to always enrich their knowledge and refresh it according to the latest global and real situation. The risk will happen while you are not realize about it. Company should always identify, evaluate and improve their risk management plan regularly according to changing environment. Periodic review of risk management plans is critical to identifying new risks and monitoring the effectiveness of risk management strategies. The risk management plan should be part of a broader business continuity plan, including strategies for responding to and resuming events if an event occurs. Thus, ensuring that business continuity plan is reliable and up-to-date will help company quickly resume operations and reduce the negative impact on the business after the event happen.
5.0 Conclusion

In conclusion, according to the R Square, it indicates that almost 80.1% of the ROA are explained by the credit ratio. From the correlation matrix, the relationship between ROA and credit ratio show it is negative significantly. With the P < 0.10, this ANOVA model shows that the credit ratio has high influence to profitability. However, only the unstandardized coefficients model illustrates that profits of SP Setia Berhad are not dependent on the counterparty risk. The other dependent variable which is operating ratio, liquidity ratio, leverage, gross domestic product(GDP), inflation rate and exchange rate considered be exclude variable that means the performance of SP SetiaBerhad will not easy affected by them. Due to the economic environment Malaysia, property company nowadays facing the big challenge. Most of the individual is not ability to purchase the real asset even with the lowest interest rates. The high living cost and low salary cause the Malaysian reduces their purchasing power. This situation brings the negative impact to the property company. In order to develop the company performance, restructure corporate governance and having the latest information about risk management tools is essential for the property company to take parts about it.
7.0 Reference


