Empirical Evidence of Risk and Performance: Top Glove Corporation Berhad

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Abstract

The purpose of this study is desired to examine the profitability performance of Top Glove Corporation Berhad with some risk factors (liquidity risk, operating risk) and macroeconomic factors. This study was according to the annual report data of Top Glove from year 2011 to year 2015. It shows that there are negative relationship between the company's profitability and the operating ratio. By using the IBM SPSS Statistics software and add some measurement such as GDP, inflation rate, asset size to get more accurate statistics. After the calculation, profitability performance of top Glove has an insignificant negative correlation relationship with liquidity ratio, operating ratio, leverage and GDP. There are only one factor shows inflation is significant to the profitability of the company.

Keywords: Profitability, Credit Risk, Liquidity, Performance and Macroeconomic

1.0 Introduction

1.1 Background of the company

Top Glove, is the world's largest rubber glove manufacture that established since 1991. It is a company that producing a wide and diverse product range of gloves such as household gloves, latex examination gloves, nitrile examination gloves, surgical gloves, vinyl gloves, cleanroom gloves and so on.

As a world's largest rubber glove manufacture company Top Glove has exports to more than 195 countries worldwide like USA, Canada, Brazil, Germany, Australia, Japan, Thailand so other countries. From 2011 to 2015, over this six years period Top Glove's nitrile glove sales volume has grown 646%, at the same time natural rubber glove sales volume also rise steadily.

It is a company that every year achieved a new levels of excellence, gained many of international quality awards and certifications. There are few awards in year 2015 like ASEAN Corporate Governance Outstanding Achievement Awards, ASEAN Business Awards Malaysia and Best Mid-Cap Public Company Asia's Best Companies.

Top Glove in its 6 years financial review they are always make more than RM2000 million revenue and always with positive net profit around RM100 million to RM280 million. Other than that, the company are always having net cash in hand around RM150 million to RM300 million during this 6 years.

As a multinational company, Top Glove was exposure to market risk, credit risk, liquidity risk, interest rate risk, and foreign currency risk. The company are highly governing all financial risk to ensure that all the risk management activities are per the company's policies and risk objectives.

2.0 Literature Review

Moosa, I. (2007) indicates that the role of a risk committee is to identify the risk profile, ensure that resources are properly allocated and that risk issues are addressed, as well as approving policies, including capital allocation.

Most of researchers figure out the company's performance through the ratio generated and calculated from the financial statement of annual report data. One of the factor to be analyzed is the liquidity which it has not been a priority to be analyzed (Vodova, P., 2011).

W., Waemustafa and A., Abdullah (2015), presented that while manage a liquidity risk there must with a proper knowledge of risk information and it is also important to identify the risk information first before proceeding to the further action on risk management process. Saleem, Q., & Rehman, R. U. (2011) mention that liquidity management is very important for every organization that means to pay current obligations on business, the payment obligations include operating and financial expenses that are short term but maturing long term debt. In the view of Goodhart, C. (2008), liquidity and solvency are interrelated and not easy to distinguishable.

Based on the research of W., Waemustafa and A., Abdullah (2015), it shows that the effective Shariah Supervisory Board does not really have significant bearing towards the choice of Islamic mode of financing in Malaysia but their remuneration have.

Waemustafa (2013) and Waemustafa and Sukri (2013) opined that there is need to understand how credit risk is formed in Islamic banks and conventional banks considering internal and external factors determinants. According to Kolapo et al. (2012) and Kithinji (2010) the formation of credit risk include, inappropriate credit policies, poor lending practice, limited institutional capacity, volatile interest rate, poor management, low capital and liquidity risk, laxity in credit assessment, poor loan underwriting, poor lending practice, inadequate supervision by central banks, government interference and inadequate knowledge about borrowers.

The BCBS (2004a, p. 137) indicates that operational risk as the risk of loss resulting from inadequate or failed internal processes, people, and systems or from external events.

Credit risk can be defined as 'the potential that a contractual party will fail to meet its obligations in accordance with the agreed terms', Brown, K., & Moles, P. (2012). Credit risk can also name as default risk, performance risk or counterparty risk.

All the financial risk they are all interrelated with the company's performance at the most of the time. So identify the risks and manage the risks are one of the important activities in company that cannot be ignore not and should have a proper action to face it.

3.0 Descriptive Analysis

3.1 Performance of Top Glove

Let the return on asset (ROA) indicate the performance of the company. From the annual report of the company, ROA is calculated as below:

ROA = Net income / Total assets

Graph 1: Return on Assets

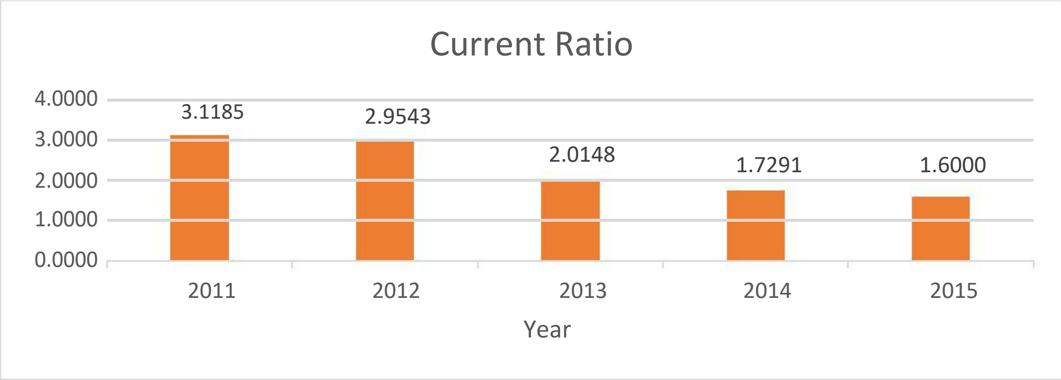
ROA shows that the efficiency of the company at using its assets to generate profits. The ROA in year 2011 rise from 8.09% to 12.97% in year 2012 was due to the increase in demand for nitrile gloves and natural rubber from all over the countries especially among the developing countries, the factor of the favourable latex prices and the foreign exchange rate. In year 2013 and 2014 the ROA faced a down trend and grown in year 2015 which is 10.46%. This is due to the net profit of year 2013 and 2014 was around 2% lower than previous year and the company has improved their operationally at the same time increase their total asset. In year 2015, because of the outperform company exports, the sales volume increase 8% drive up the profit.

3.1.1 Asset size of Top Glove

Graph 2: Asset Size

Asset size of the company can obviously see that is an uptrend from year 2011 to year 2015. This is because in order to fulfil the strong demand of the company's product from all over the world, Top Glove have to continue expand its capacity and expanding its factory. Company need more asset to do all this investment and towards better profitability.

3.1.2 Liquidity Risk of Top Glove



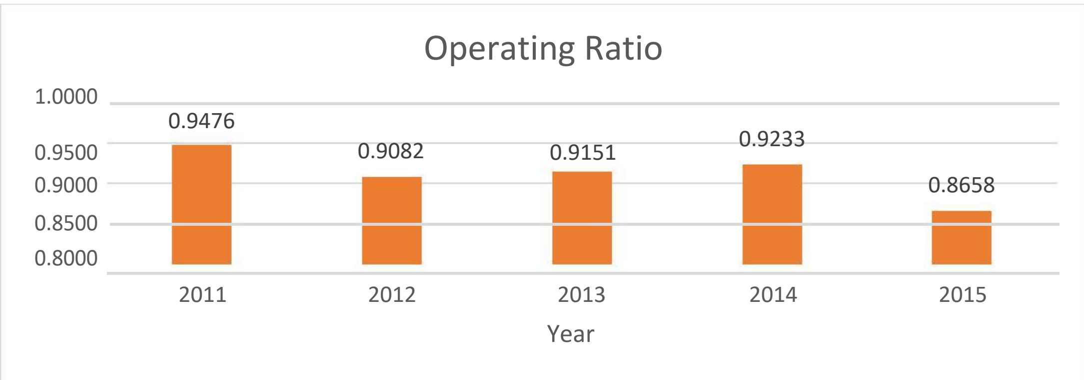
Graph 3: Current Ratio

Liquidity risk can interpret from the current ratio. From the annual report can get the data and calculate it as below:

Current Ratio (CR) = Current Assets/Current Liabilities

The liquidity risk means that the company cannot meet short term debt obligation or facing a greater loss when have to turn the asset to cash quickly. From the graph 3, current ratio of Top Glove has decline from year 2011 to 2015. The company has increased their current liabilities to fund for some equipment, plant, property but at the same time the company also invest a lot in the securities. Top Glove have to control the ratio because during the 5 years the trend is going downward, it is not a very good indicator.

3.1.3 Operational Risk of Top Glove

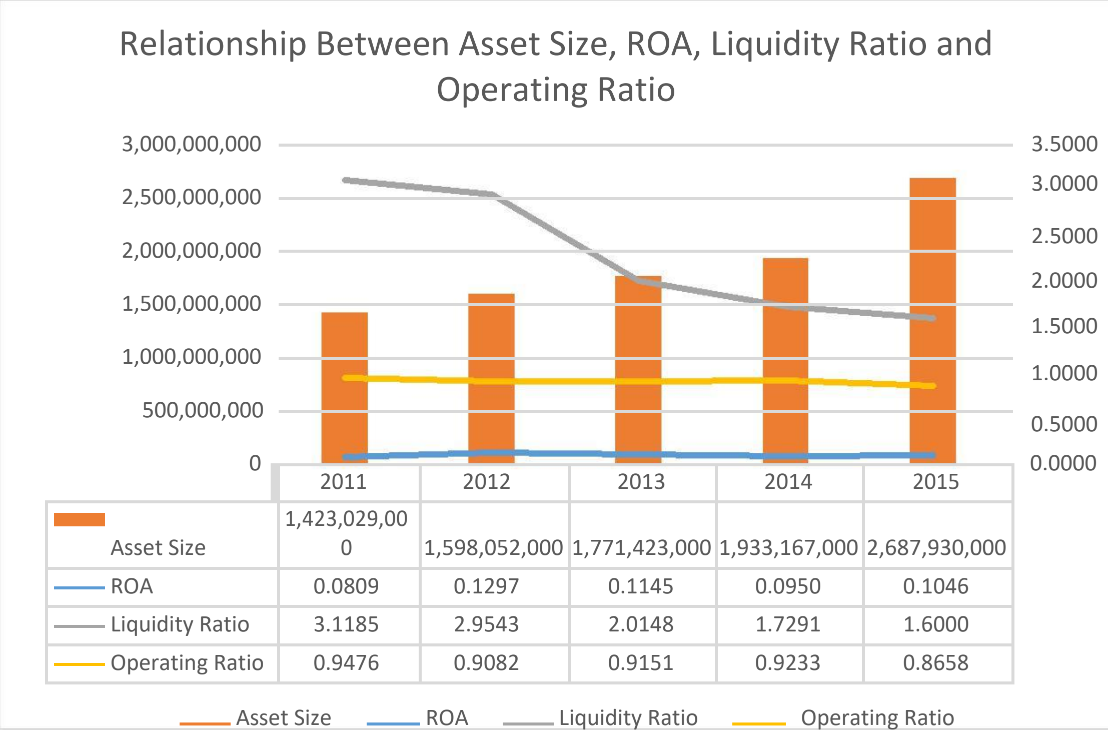


Graph 4: Operating Ratio

This ratio represents the efficiency of a company's management using the comparison of operating expenses and net sales. While the ratio getting smaller it is mean the greater the company's ability to earn profit. It can be calculate as below:

Operating Ratio = Operating Expenses / Net Sales

Over the 5 year, the operating ratio was fluctuated but it can be noticed that overall was in the downtrend. Company trying to reduce the operating cost by invest the research and development department to create or achieve new technologies in producing high quality gloves with lower costs.



	2011	2012	2013	2014	2015
Asset Size	1,423,029,000	1,598,052,000	1,771,423,000	1,933,167,000	2,687,930,000
ROA	0.0809	0.1297	0.1145	0.0950	0.1046
Liquidity Ratio	3.1185	2.9543	2.0148	1.7291	1.6000
Operating Ratio	0.9476	0.9082	0.9151	0.9233	0.8658

Graph 5: Relationship between Asset Size, ROA, Liquidity Ratio and Operating Ratio

From the graph above, Top Glove's asset size present an uptrend while the liquidity ratio go an opposite way. This situation is due to the company asset size most of them are non-current assets. The ROA and operating ratio also show a negative relationship. While ROA increase the operating ratio decrease. This is just simple due to the expenses decline and drive up the profit of the company.

Correlations

		ROA	Size	Index Score	Board Remuneration	Leverage	Liquidity risk	Operating Ratio	GDP	Inflation	Unemployment rate	Exchange rate
Pearson Correlation	ROA	1.000	.060	.	-.363	-.059	-.005	-.461	-.208	-.926	-.010	-.146
	Size	.060	1.000	.	.295	.990	-.814	-.896	-.203	-.237	.921	.975
	Index Score	.	.	1.000	.	.	.	.	.	.	.	.
	Board Remuneration	-.363	.295	.	1.000	.386	.141	-.248	-.592	-.011	.613	.437
	Leverage	-.059	.990	.	.386	1.000	-.769	-.852	-.185	-.144	.946	.996
	Liquidity risk	-.005	-.814	.	.141	-.769	1.000	.614	.080	.010	-.541	-.757
	Operating Ratio	-.461	-.896	.	-.248	-.852	.614	1.000	.325	.636	-.866	-.805
	GDP	-.208	-.203	.	-.592	-.185	.080	.325	1.000	.470	-.339	-.198
	Inflation	-.926	-.237	.	-.011	-.144	.010	.636	.470	1.000	-.276	-.071
	Unemployment rate	-.010	.921	.	.613	.946	-.541	-.866	-.339	-.276	1.000	.944
	Exchange rate	-.146	.975	.	.437	.996	-.757	-.805	-.198	-.071	.944	1.000

Sig. (1-tailed)	ROA	.	.462	.000	.274	.462	.497	.218	.368	.012	.494	.408
	Size	.462	.	.000	.315	.001	.047	.020	.372	.351	.013	.002
	Index Score	.000	.000	.	.000	.000	.000	.000	.000	.000	.000	.000
	Board Remuneration	.274	.315	.000	.	.260	.410	.344	.146	.493	.136	.231
	Leverage	.462	.001	.000	.260	.	.064	.034	.383	.409	.007	.000
	Liquidity risk	.497	.047	.000	.410	.064	.	.136	.449	.494	.173	.069
	Operating Ratio	.218	.020	.000	.344	.034	.136	.	.297	.124	.029	.050
	GDP	.368	.372	.000	.146	.383	.449	.297	.	.212	.289	.375
	Inflation	.012	.351	.000	.493	.409	.494	.124	.212	.	.327	.455
	Unemploymen t rate	.494	.013	.000	.136	.007	.173	.029	.289	.327	.	.008
	Exchange rate	.408	.002	.000	.231	.000	.069	.050	.375	.455	.008	.

Model Summary[e]

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.926[a]	.857	.810	.008106887812662	

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.001	1	.001	18.035	.024[b]
	Residual	.000	3	.000		
	Total	.001	4			

Based on the table above, profitability of the company have affected by the many variables that put in the correlation matrix to calculate. ROA only shows positive relationship with the asset sizes of the company. There is also a research showed positive relationship between firm size and profitability was found by Vijayakumar and Tamizhselvan (2010). Other variables such as liquidity ratio, GDP, inflation, operating ratio show negative relationship with ROA. However, only the inflation variable statically show significant relationship with the ROA. It carry correlation value negative 0.926 and significant value 0.012. Inflation influence the cost of production and further cut down the net profit of the company. Operating ratio also one variable that held a high insignificant negative correlation that is -0.461. This is normal with low down the operating expenses to push up the revenue that many company will set as one of the objective.

After the test conducted and all of variables added. With the stepwise method shows that R value is 0.926 and shows a high degree of correlation between variables. R. is 0.857 and indicates that 85.7% will influence by other variables ratio and the remaining will influence by the variables that not inside the variables. Besides that, the regression is significant with 0.024 significant value based on table Anova illustrate that the inflation is significant to performance (ROA) of company.

4.0 Discussion and Recommendation

4.1 Discussion

Top Glove had 25 years history started in 1991 from a local manufacturing company become the world's largest rubber glove manufacturing company. The company surely had some power to do so. From the year 2011 to year 2015, the company's overall performance is quite good. All variables have a negative relationship with the performance of the profitability except the variable of asset size. One of the measurement has a significant relationship which is ROA to inflation variable. This shows that the inflation give a big impact to the company's profitability. Therefore, company can put more attention and come out some strategies to make sure company's profitability can keep on increasing start from year 2015 onwards.

4.2 Recommendation

As a world's largest rubber glove manufacture, technology is one of the important part that cannot be ignored. Research and development have to continuously be investing by company for machine and equipment upgrade not only maintain the title of world no.1 also enables the company can keep producing a high quality product at efficient low cost. This can prove from the asset size become bigger to access more profit. New technology and new development done by the company can ensure the competitiveness in the international marketplace.

The analysis show that the inflation giving a significant impact to the company's profitability. Inflation not only will affect the raw material price the currency exchange especially for an export company. Company can do more investment to minimize the risk that affect by the inflation. Company can do some hedging to overcome the uncertainties about the future value no matter for raw material or foreign currency risk. Furthermore, liquidity ratio also shows a decline trend during the past 5 years. Top Glove Company's exposure to liquidity risk arises primarily from mismatches of the maturities of financial assets and liabilities. Company can try to maintain a balance that fixed in the policy between continuity of funding and flexibility through the use of standby credit facilities. This is because have a minimum balance can protect the company go into solvency.

5.0 Conclusion

In conclusion, Top Glove Company same as many other companies will face the liquidity risk, market risk, operational risk and worry about the company's profitability. Overall performance of the company doesn't much more have to worry but the liquidity risk indicate from the current ratio although still in the healthy position but in a trend that continuously decrease. In the study, inflation give a significant impact to the profitability so company have to put more effort to that particular part to make sure profit of company not affected so much by this variable. Other than that, to maintain the profitability of company one of the variable also have to take note that is asset size of the company. During the previously 5 years asset size has a uptrend shown and give a good impact to the profitability, keep going develop some new technology and build more factory to increase the production. The unemployment rate and the GDP not much affect the profitability of the company. In a nutshell, financial risk management of the company can keep moving on in the year 2015 onwards, because there are many senior management in the team who have the appropriate skills and experiences that already identify a lot of good objectives and policies.

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