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# **Firm Risk and Performance: The Role of Corporate Governance in Hwa Tai Sdn Bhd**

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# **Firm Risk and Performance: The Role of Corporate Governance in Hwa Tai Sdn Bhd**

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## **Abstract**

The main purpose of this study is to examine the relation between the overall performance of Hwa Tai Sdn Bhd with firm specific risk and some macroeconomics factor involved. The data collected are from Hwa Tai Sdn Bhd's annual report starting from 2011 until 2015. The calculation of liquidity ratio, profitability ratio and operating ratio are used to see the overall performance of Hwa Tai Sdn Bhd. A correlation model comprise of dependent variable which is ROA and numerous independent variable was used to analyse the performance of Hwa Tai Sdn Bhd. This study empirical results showed that ROI is the most significant meaning in the performance of Hwa Tai Sdn Bhd.

**Keywords: firm specific risk, macroeconomics factor, liquidity ratio, profitability ratio, operating ratio, ROA, ROI**

## **1.0 Introduction**

### **Hwa Tai Industries Berhad**

Hwa Tai Industries Berhad is one in all the premier and longest established biscuit makers in Asian country. Established in 1962 and stand with a name of Hwa Tai Food Industries Sdn Bhd which existed until 1974 and listed on the exchange Asian country on 1992. The registered headquarters of the company is located in Balakong, Selangor Darul Ehsan. The company is publicly traded on the Kuala Lumpur Stock Exchange under the ticker symbol HWATAI. Since then, this quick increasing company has big to be the most important players within the biscuits business within the country and manufacture a fine, big selection of superior quality biscuits.

It has been with success marketed domestically and internationally through Hwa Tai's own vast and comprehensive distribution network. Hwa Tai focuses on the assembly of sugar, cream,

cheese, nutrition and mineral mini wacky, additionally as cheese mini crackers, different biscuits, mixed fruit flavor sandwiches, chocolate cream cookies, sandwich biscuits, herb topping puffs, low biscuits, and soda, multi grain and cereal crackers. The corporate conjointly offers oatmeal cookies, white choco chips cookies, peanut cream sandwich biscuits, cheese cream sandwich biscuits, lemon cream sandwich biscuits, chocolate cream sandwich, peach cream sandwich, sweet corn cream sandwich and vanilla cream sandwich, among others. The company's product is found domestically from little sundry retailers to huge hypermarkets, fast-food chains, airlines and alternative mass consumption industries beneath the logos Hwa Tai, Luxury, Lucia, Palmers, Organic Luxury, D-Layer, Cracker and, Cream Sandwich Biscuits, crisp fatless, D'Licious Cookies, World & Generation and Oatmeal Cookies. (Worldwide Company Profile, 2017)

Hwa Tai is additionally concerned within the commercialism of confectioneries, the availability of construction and insurance agency services, and property holding activities. The corporate has distribution sites placed in Kelantan, Perak, Selangor, Kuala Lumpur, Johor, Pahang & Terengganu, Perlis, Kedah & Penang. It exports its merchandise in North America, North East Asia, Africa, Oceania, West Asia, South East Asia, South Asia and Europe. The corporate also has absolutely integrated ISO 9001:2000 and MS ISO 9002 certification for food and safety quality management. It operates below the supervising and management of Soo Thien Ming, Chairman. Hwa Tai Industries Berhad pride of it wonderful innovation and prime quality product that have firmly entrenched us not solely in Asian country however conjointly in over 50 countries round the world. It keenly concerned within the integrated provide chain of their product, from intensive and comprehensive distribution network, they also carrying product / brands by different principals for the Malaysian market. (Hwa Tai Industries Berhad, 2012).

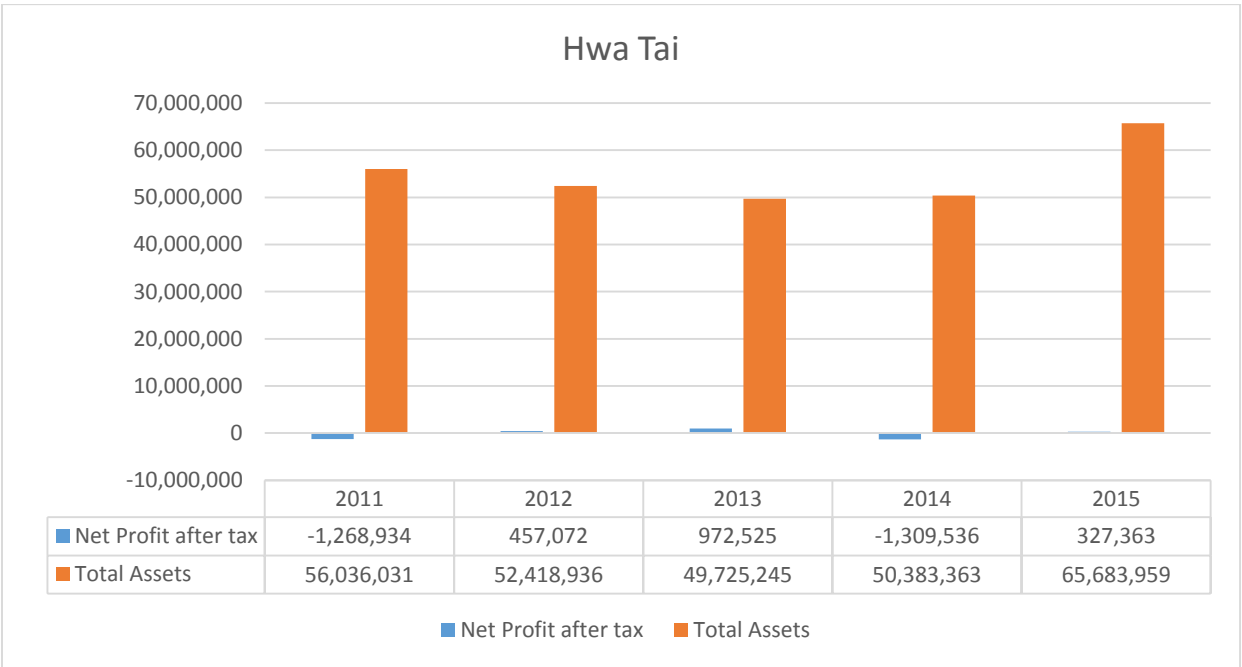
Hwa Tai vision stressed out to be a leading biscuits and confectionery manufacturer in the region known for its product quality and variety.

It can be said that Hwa Tai is committed in producing the best quality biscuit products for their customer all over the world and creating a big business activities for their partners. By having more than 50 years of manufacturing experience they have an ability to manage their entire value chain, from procurement of raw materials to distribution of finished products. Hwa Tai's top management recognized that the skilled and dedicated people who work for them are critical to

their success. They put a high expectation from their staff and luckily they totally committed to the provision of the highest quality service in the business.

Some of its achievements and awards are as an energetic and enterprising company, they have a tendency to participate within the Monde choice in Kingdom of Belgium with four of our merchandise, like duchess Cookies, Sesamio, Siang-Siang cream crackers & Choose, and that they were awarded with two gold & two silver medals severally. Within the year 2000, Hwa Tai Industries Berhad won two gold medals from the Monde selection once more for Luxury Original metal crackers and Luxury Vegetable crackers. (Halal Exporter, 2011)

Hwa Tai has successfully established a strong presence in Malaysia and has built up a wide international market. Nowadays, their products can be found locally from small sundry shops to big hypermarkets, fast-food chains, airlines and other mass consumption industries. A total of 40% of their company's production is exported internationally to countries such as China, Taiwan, Hong Kong, Singapore, Brunei, USA, Mauritius, Middle East, Papua New Guinea, Maldives, Nigeria and 28 other countries. And they are still in a growing phase which support facilities are constantly being upgrade, with their continuous goal of producing the finest product ranges possible (Hwa Tai Industries Berhad, 2012).



Graph 1: Net Profit after tax and Total Assets

## 2.0 Literature Review

Inflation means a sustained increase in the aggregate or general price level in an economy. (EconomicsHelp.org, 2016). Inflation also can be said there is an increase in the cost of living. Numerous studies have attempted to explain about the impact of inflation company activities. Shu (2002) opine that acceleration in credit expansion will lower default rate as higher inflation prevail due to the fact that inflation enable borrowers to service their loan from the availability of funds. Moreover, Castro (2013) opined that high inflation can make debt servicing easier by reducing the real value of outstanding loans. But at the same time, it can weaken borrowers' ability to service debt by reducing real income. The finding of study supports Mkukwana (2013) shows that higher inflation rate forcing borrowers to miss loan repayment in order to fulfill basic need on necessities goods and service. Thus, Hwa Tai Industries Berhad does not perform well and earn a negative value for its ROA because of higher interest rate on that particular year. It can be assume that they face a problem in collecting back their money from its borrower.

Liquidity is a measurement of the extent of the individual or organization has a cash to meet its immediate and short-term obligations or assets that can be immediately converted to cash. (WebFinance, 2017). Bourke (1989), Kosmidou and Pasiouras (2005) found a significant positive relationship between liquidity and ROA. The finding is consistent with previous studies Ghazali (2008), who found a positive relationship between liquidity and ROA. Contradictory to the findings of Choon et al. (2012) who found that liquid is negatively significant to ROA which implies that more financing were made by Islamic bank with lower liquidity. In my study, there is no relationship between the ROA and liquidity. This is because, some of the year, Hwa Tai doesn't gain net income and incurred loss for that particular years (2011 and 2014). Massive fluctuation in ROA affect the liquidity of the company.

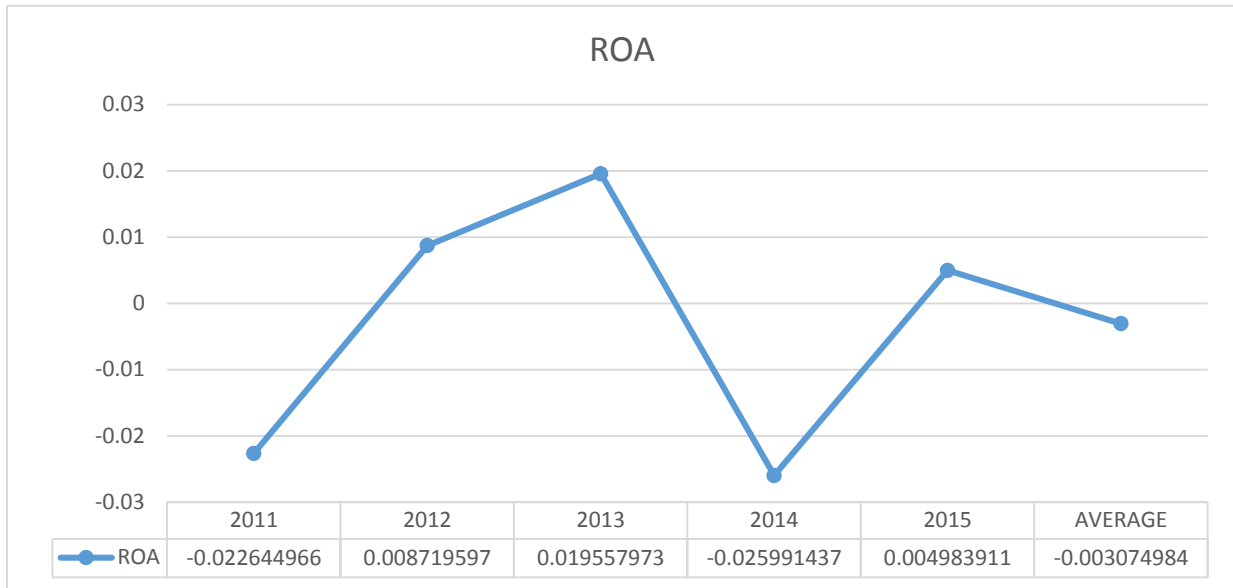
Shariah governance is related to the Islamic Finance and it is now go international in scope and depth. It should be more aligned to the globalization trends within the Islamic Finance Institutions (IFIs). (IB Insights, 2013). Alman (2012) said that Shariah Supervisory Board (SSB) is one of internal governance mechanisms which involves the monitoring of Islamic banks' activities in accordance to the Sharia (i.e. Islamic law) specifically on its implementation and compliance. Moreover, Bhatti and Bhatti (2010) found that since shariah governance is part of corporate governance, thus, good and effective SSB should reflect the issue of independence,

transparent, accountable, responsible, and fair. Contradictory to the finding of Waemustafa and Abdullah (2015) who found that although the existence of SSB seemed able to monitor Islamic banking activities, there are still Islamic banks have experienced failure similar to that of conventional in the recent year. Somehow, Hwa Tai doesn't practice the Shariah Supervisory Board because of its organization as well who own by non-muslim and practice a family company. However, Hwa Tai still need to consider the four main pillar of good corporate governance which are accountable, fairness, transparent and independence in order to be a good company with good practice of corporate governance.

Board of directors is a group of person that are elected to represent the stockholders and to establish corporate management related policies and the most important part is to make decisions on a major company issues. (investopedia, 2017).Lipton and Lorsch (1992), Jensen (1993) verified that although larger board size initially facilitates key board functions, there comes a point when larger boards suffer from coordination and communication problems and hence board effectiveness and firm performance declines. Contradictory, Coles, Daniel and Naveen (2008) find that the impact of board size on firm value is positive for large firms, and hence large board size may be an optimal value maximizing outcome for such firms. From my study, Hwa Tai Board of Directors consist of 5 person and the Chief Executive Officer have an interest relationship with the company where as the Chairman is his own father. As a result it effect the company performance where Hwa Tai incurred a loss for the certain years and show that it is not well-managed. The Board of Director size really influence the performance of the company.

Diversification definition explained by Nasdaq (2011) are investors tend to invest in different type of assets and instruments in order to minimize total investment risk. Markowitz (1952) diversification theory verify that the function of the means, variances and pair –wise of risk assets are the optimal diversifications start. Later, Zweig (1988) suggest that, to minimize future regret, there should have fifty-fifty split between equities and bonds. Even though, Hwa Tai incurred loss in certain years the company still invest to cover up their loss and it shows that Hwa Tai is a risk taker company.

### 3.0 Descriptive Analysis

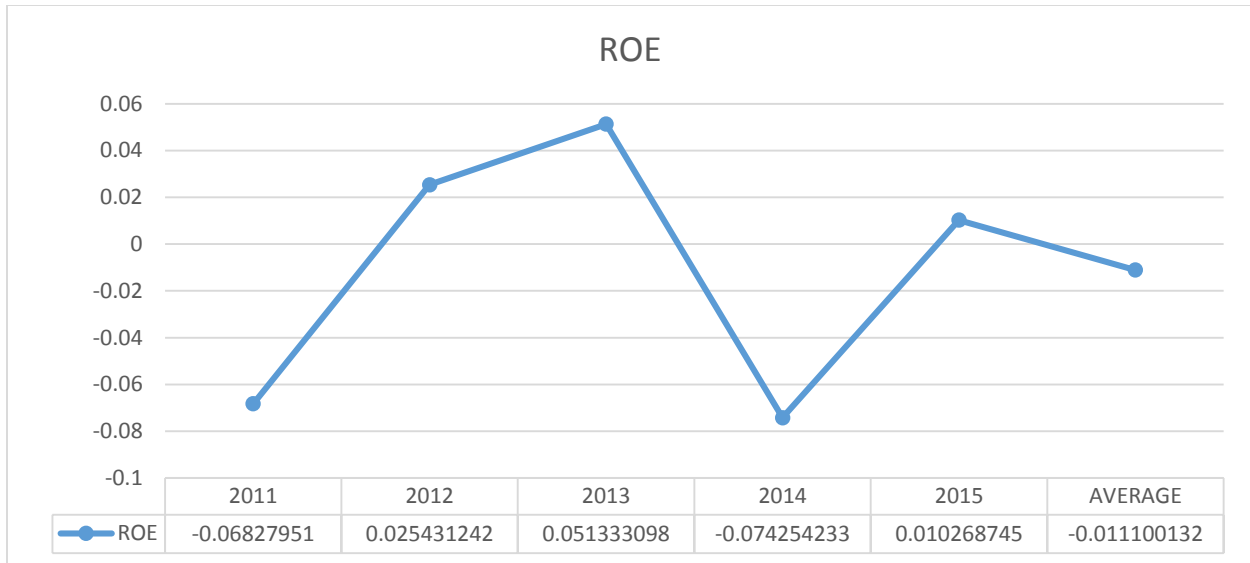


Graph 2: Return on Asset (ROA)

Return on assets (ROA) is a measurement of how profitable a company is to its total assets. It also indicate how efficient the company is at using its assets to generate income. The higher the ROA, the more money the company is making with less capital investment. (Harrison, 2012)

Overall, Hwa Tai's ROA seems to be fluctuate over the five years. In year 2011, Hwa Tai incurred a negative amount of percentage which is -2.26%. A negative ROA suggests that the company is not properly utilizing its capital and not well-managed. It also means that Hwa Tai is investing a high amount of capital into its production and at the same time receiving a little income. It slightly increase in 2012 to 2013 which are 0.87% and 1.96% respectively. But, it drop drastically in 2014 to -2.60% and increase back in 2015 which is 0.49%. By this amount generated for over the five years, the outcome for the average is about -0.30%.

With that I can figured out among the five years, in 2013 was the highest ROA (1.96%) and in 2014 was the lowest ROA (2.60%)



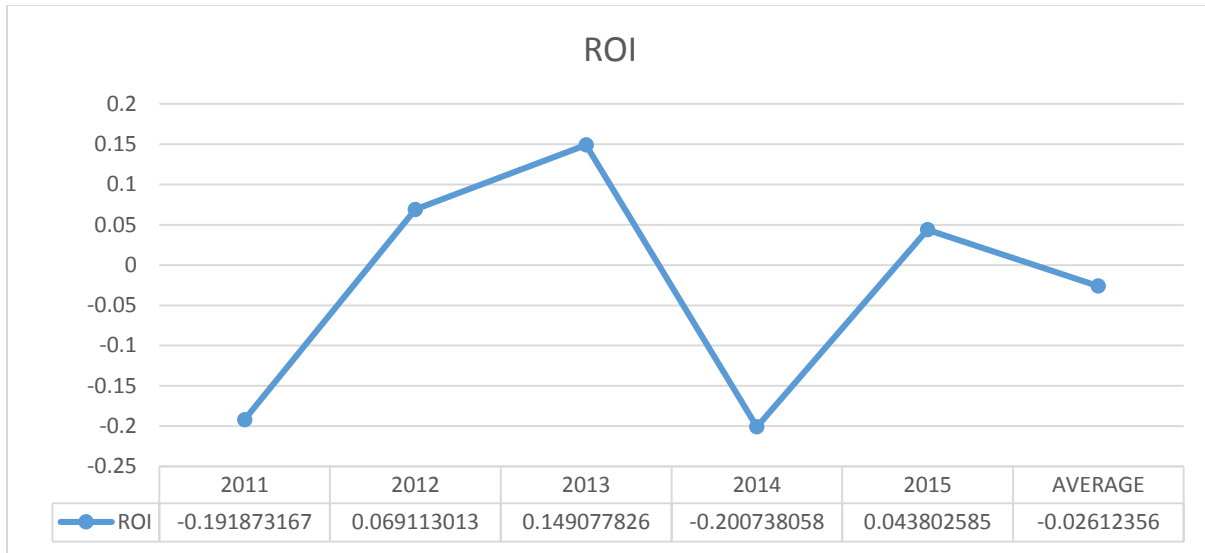
Graph 3: Return on Equity (ROE)

Return on equity (ROE) is a measurement of profitability that shows how many ringgit of profit a company is generate with each ringgit of shareholders' equity. It sometimes called "return on net worth". (InvestingAnswers, 2017)

The trend for the past five years are similar with the ROA which is -6.8% in 2011, increase slightly in 2012 to 2013 which are 2.54% and 5.13% respectively and drop drastically in 2014 which is -7.43% and increase back to 1.02% in 2015. With this huge gap between the years it give negative average which is -1.11%.

With that, I can figured out among the five years, in 2013 was the highest ROA (5.13%) and in 2014 was the lowest ROA (-7.43%).



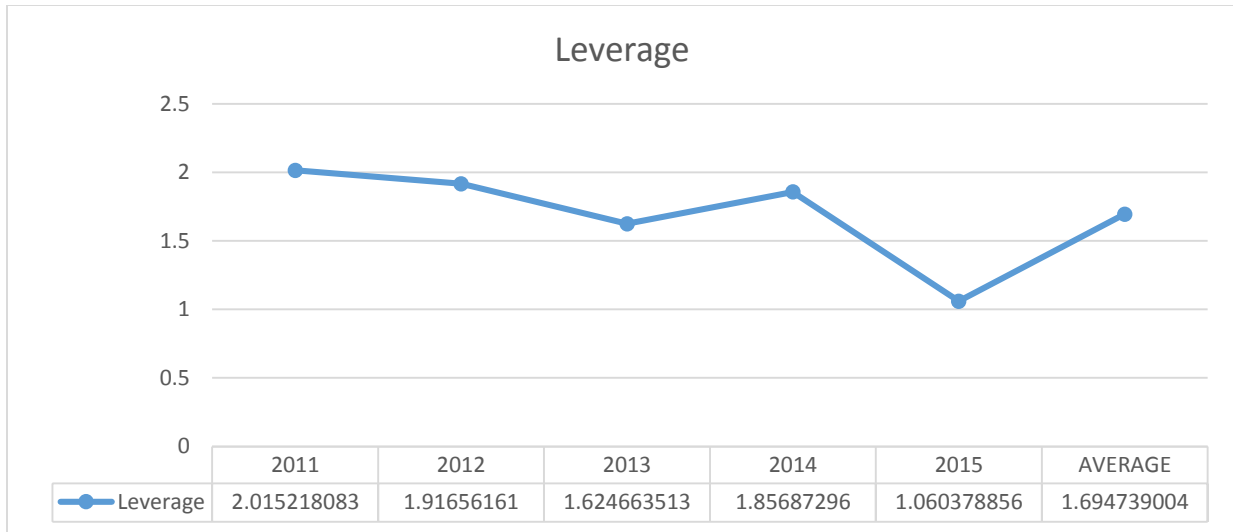


Graph 4: Return on Investment (ROI)

Return on investment (ROI) is a measurement of profitability that evaluates the performance of the company. It is also a mathematical formula that from this, investors can use to estimate their investments and judge how well a particular investment has performed compared to others. (Margaret Rouse, 2007)

Hwa Tai's ROI trend also similar with its ROA and ROE because this three ratio calculated by the same amount of net income in every particular year. In 2011 Hwa Tai incurred negative amount of percentage which is -19.19% and increase slightly for year 2012 and 2013 which are 6.91% and 14.91% respectively. Again, it decrease drastically in 2014 which is -20.07% and increase back in 2015 which is 4.38%. It give an average for about -2.61%.

With that I can figured out among the five years, in 2013 was the highest ROI (14.91%) and in 2014 was the lowest ROI (-20.07%).

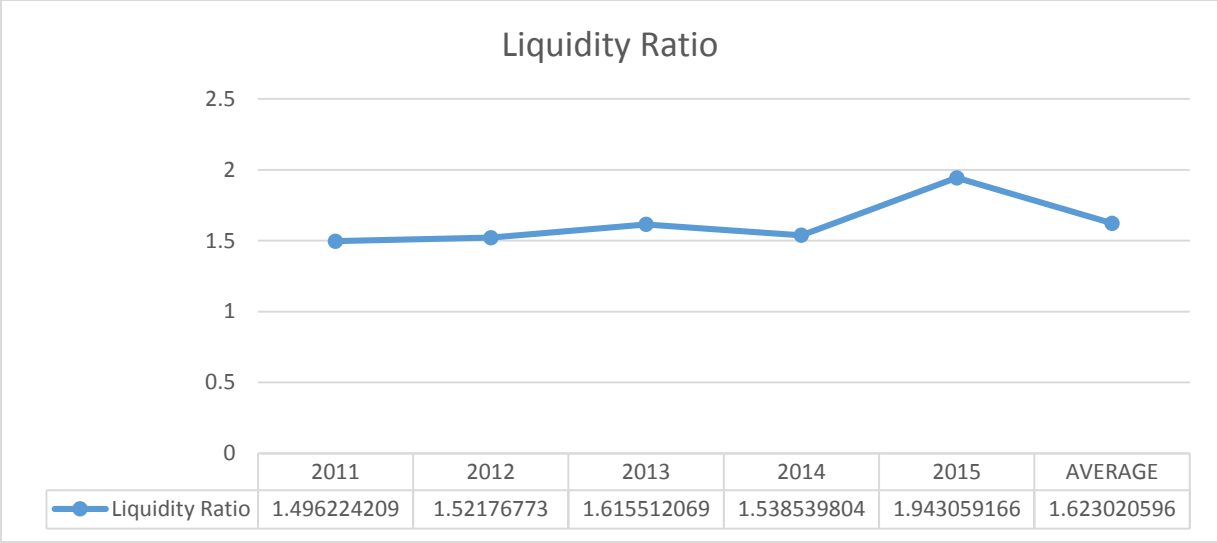


Graph 5: Leverage

Leverage or also known as debt to equity ratio is a measurement of the relationship between the capital contribute by creditors and contributed by the owners. It also indicate the shareholders' equity can fulfill a company's obligations to creditors in the event of a liquidation. (InvestingAnswers, 2017)

From year 2011 to 2015, Hwa Tai generated more than 1.0 for its leverage. This shows that, Hwa Tai has a lot of debt relative to its equity. In 2011 the leverage is 2.02 and it decrease slightly in 2012 and 2013 which are 1.92 and 1.62 respectively and increase in 2014 which is 1.86 but decrease in 2015 which is 1.06. So, the average ratio for Hwa Tai's leverage for the past five year is 1.69.

With that I can figured out among the five years, in 2011 was the highest leverage (2.02) and in 2015 was the lowest leverage (1.06).

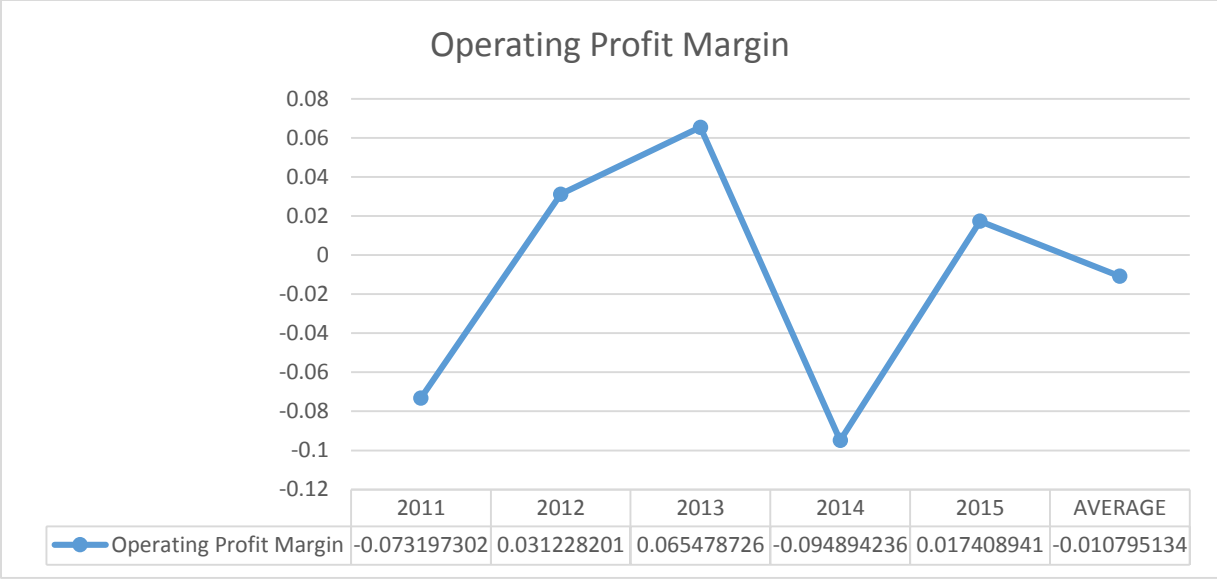


Graph 6: Liquidity Ratio

Liquidity ratio is a measurement of the company’s ability to pay debt obligation. Suggested that the higher the liquidity ratio it indicates that the company is more liquid and has a better coverage of its outstanding debts. (investopedia, 2014).

Hwa Tai’s liquidity ratio shows a good sign because the higher the ratio, the more the company can pay its debts. In 2011, the liquidity ratio is 1.50 and slightly increase to 1.52 in 2012 and keep increasing to 1.62 in 2013 but slightly decrease in 2014 which is 1.54 but increase back to 1.94 in 2015. So, the average liquidity ratio for Hwa Tai is 1.62.

With that I can figured out among the five years, in 2015 was the highest liquidity ratio (1.94) and in 2011 was the lowest leverage (1.49).



Graph 7: Operating Profit Margin

Operating profit margin is defined of how much profit the company can earn after paying for variable costs of its production. It also shows the efficiency of the company in controlling the costs and expenses associated with the company operations. (Wilkinson, 2013)

Hwa Tai’s operating profit margin in 2011 is -0.07. Even though it is negative, the closer the ratio is to zero, the better. And it increase in 2012 and 2013 which are 0.03 and 0.06 respectively. But then, it decrease drastically in 2014 which is -0.09 and increase back in 2015 which is 0.02. The average for Hwa Tai’s operating profit margin is -0.01.

With that I can figured out among the five years, in 2012 was the highest liquidity ratio (0.03) and in 2014 was the lowest leverage (-0.09).

#### 4.0 Discussion and Recommendation

##### Descriptive Statistics

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	Mean	Std. Deviation	N
ROA	.016379576716258	.009086826258478	5
Net Profit after tax	867086.00	454910.320	5
Total Assets	54849506.80	6536538.993	5
Leverage	1.69473900440	.382597340590	5
Liquidity Ratio	1.623020595680308	.184355319538646	5
ROE	.04591336560	.027490357603	5
ROI	.13092092980	.071290083583	5
Operating profit margin	.05644148120	.031623932270	5
GDP	5.300	.4950	5
Inflation rate	2.440	.6693	5
Remuneration BOD	1131824.000	70657.7101	5

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Table 1: Descriptive Statistics

The results of descriptive statistics for the variables are in table above. For average five years Hwa Tai makes 1.6% profit from asset. The small amount is because of Hwa Tai having a rough phase went its incurred loss in the year 2011 and 2014. Even though the standard deviation is small it doesn't mean a good sign because Hwa Tai loss in earning a profit and it is very volatile. Leverage tells that proportion of debt to equity, in the table above shows that every 1 ringgit of

debt is sponsored by 1.69 ringgit on average. For five respective years, Hwa Tai have an average of 1.62 liquidity ratio.

This study include two macroeconomic independent variable which is mean of GDP is 5.300 and mean of inflation rate is 2.440.

Based on the table 4.2 (refer appendix) we can see the relationship using Pearson Correlation between the variables and ROA. This study uses SPSS to see the relationship in correlation ROA as dependent variable with others independent variables. Based on table 4.2, net income is strongly positive relationship with ROA which is 99.2%, this indicate when ROA increase net income will increase by 99.2%. It shows that net income of Hwa Tai is making a large profit from its total asset.

Liquidity ratio has a negative relationship with ROA which is -0.67. It means that when ROA increase, liquidity ratio decrease. Hwa Tai use more fix asset that current asset to generate income and this causes a high liquidity risk because the high ability to convert into cash.

Remuneration BOD and ROA having a negative relationship which is -0.135. This indicate that the higher the remuneration of BOD the lower the ROA means that even though Hwa Tai increase the salary, the performance of the company is not aligned with the additional salary that were given to the BOD.

Based on this Durbin Watson Pearson Correlation shows leverage ratio is 0.638. It shows the positive relationship with ROA and the leverage on average. The higher the ROA, the higher the leverage. It shows that, Hwa Tai generates it income more by debt.

Macroeconomics variables that used are GDP and inflation rate. GDP has a weak relationship with ROA on average which told that this factor does not affect much in Hwa Tai performance. Meanwhile, inflation rate has a strong relationship with ROA and this shows changing in inflation rate will affect the Hwa Tai's performance. This is because, Hwa Tai mainly business is focused on domestic area and this might be the main factor of Hwa Tai effected with inflation rate.

ANOVA<sup>a</sup>

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.000	1	.000	269.341	.000 <sup>b</sup>
	Residual	.000	3	.000		
	Total	.000	4			

Table 2: ANOVA

a. Dependent Variable: ROA

b. Predictors: (Constant), ROI

In this ANOVA the sigma show the variable used in this study whether it is significant or not. If the value is less than 0.05 there is a statistically significant difference. The sigma for Hwa Tai is 0.000 which is less than 0.05 and this shows a significant different between return on asset and return on investment.

Model Summary<sup>b</sup>

Model	R	R Square	Adjusted Square	R Std. Error of the Estimate	Durbin-Watson
1	.994 <sup>a</sup>	.989	.985	.0011012487	1.216

Table 3: Model Summary

a. Predictors: (Constant), ROI

b. Dependent Variable: ROA

In model summary, R square indicate the percentage of variation of response. Hwa Tai R Square the percentage is 98.9% and noticed that R Square increase by 98.5%.

## Recommendation

Based on my study about Hwa Tai's company its ability to generate income are quite weak. Hwa Tai recorded losses twice in a past five years which are in 2011 and 2014. With this losses it bring an impact to calculate its ROA, ROI as well as ROE. The leverage of this company also high means that Hwa Tai use more money to pay their debt. Negative amount of profit after tax reduce the investors' confidence level to invest in this company. With this certain reasons, Hwa Tai should be more sensitive when the company want to invest in something that can increase their profit and reduce the amount of debt that need to be paid.

Hwa Tai doesn't diversified the gender in their Board of Directors. If there attempt to find a female to their BOD members it might help the company to look at other viewpoint of idea in increasing their company performances as well as to manage the company.

Other than that, in the aspect of committee group. Hwa Tai does not have risk management committee. With the implement of risk management committee it can be ensure that the company can manage the risk more efficiently and this will give a good sign to the company achievement as well as to maintain their performance. The more group of committee that the company have, the better the company is managed.

In terms of the number of meeting that have been held, roughly Hwa Tai only have 5-6 meetings per annum. Going internationally should force the company to do the meeting frequently so that Hwa Tai can always keep on track on how far the company is doing in market condition.

Last but not least, Hwa Tai also can take into consideration to introduce the Shariah Supervisory Board. This is one of the way to attract more investor to invest in this company because can't be denied that there is an investor whom looking for Islamic investment instruments.

## 5.0 Conclusion

As a conclusion, Hwa Tai is known as one of the company that well established in biscuit manufacturer for a long time ago. Maintaining their performance and image are really important because Hwa Tai is a high trusted seller in producing their products.

Even though nowadays there is a lot of competitors, Hwa Tai still can survive in the industry because it maintain their corporate social responsibility such as Hwa Tai sponsored a



Breast Cancer Awareness Campaign in 2011 and 7<sup>th</sup> Taste Fully Food & Beverage Expo in 2014. This ensure that consumer still aware of Hwa Tai product and to increase their confidence level.

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