Relationship Between Level of Firm Performances and Risk in Food and Beverages Industry: Empirical Analysis on Khee San Berhad

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Abstract

The main objective of this study was to identify the relationship between risk management and its impaction in the profitability of food and beverage industry. Specifically, this study examined liquidity risk, credit/counterparty risk, operating risk and leverage and how risk will affect to the profitability. For the profitability was measured with using Return on Asset (ROA). In this study it found that a strong relationship exists between the risk management practices under study and the firm's profitability. The result of this study indicate that consideration firms' in risk management will give good impact to the firm profitability.

keywords: credit risk, liquidity risk, market risk, leverage and profitability risk.

1.0 Introduction

1.1 Background of the Study

Khee San Food Industries ("KSFI") is a subsidiary of Khee San Berhad, a company listed on the Main Board of Bursa Malaysia. KSFI is based in Selangor, Malaysia with its principal premises at Seri Kembangan being just a short 30 minutes driving time from Kuala Lumpur and its secondary premises at Telok Panglima Garang. The former comprises of the candy manufacturing facilities while the latter produces the wafer products.

Khee San is the largest domestic manufacturer of candy and sweets in Malaysia with an illustrious history going back more than 50 years and famous heritage products such as the Torrone Barley Mint candy which is instantly recognisable to Malaysians bits young and old. It is also the only manufacturer that produces a 5 different type of candies which is chewy candies, tablet candies, hard candies, chewing gum, deposited candies and bubble gum. It also carries a wide assortment of wafers such as wafer bars, wafer cubes and coated wafer. These products are marketed under several famous and well-known brands such as "Fruit plus" and "Torrone" and new products have also been introduced under new brand names which the company hopes can grow to become new iconic names to a new generation of children all over Malaysia and the ASEAN region.

For the performance of Khee San the revenue in Group went up by year to year, in year 2015 by 23.40% to RM142,662,988 from RM115,604,193 in previous year. The Group, has registered an operating profit before income tax of RM5,095,474 as compared to an operating profit before income tax of RM5,269,377 for the year ended 30 June 2014. Profit after income tax for the year ended 30 June 2015 was at RM4,070,717, a slight decrease of RM348,966 with RM4,419,683 reported in the previous year. The Group basic net earnings per share for the financial year ended 30 June 2015 was 5.36 sen (2014 – 7.31 sen), while on a weak basis, it is calculated at 5.36 sen for 2015 and 6.91 sen for 2014. Net assets per share down to RM1.54 as against RM1.67 in the previous financial year, in push with the increase in paid-up share capital.

The financial risk management in company Khee San which is credit risk, the Group company to evaluate customers required to credit for over in certain amount or period. With high creditworthiness to minimized credit risk and is monitored by set a limit in the group associations to the business partners. Group’s management are reporting procedures to monitored trade receivables on an ongoing basis. Directors are monitor the credit exposures by continuously and the group does not hold any collateral. The trade receivables and measure of impairment are as disclosed for the ageing analysis. Next, for the liquidity risk to make sure all the repayment and funding needs are met, the group actively manages its operating cash flow and the availability of funding. The group in the Khee San keep sufficient ranks of cash and cash equivalents to meets its working capital desires and carefully in balances its portfolio of short term and long term funding desires is to overall prudent liquidity management.

2.0 Literature review

According to James Clausen (2009), in their article he already explained about liquidity ratio. He stated to measure company performance it used analysis of the financial statement. Other than that, he also analyses for the income statement and balance sheet. To determine a profitability and liquidity will be use ratio analysis of the financial statements it often by investors and lending institutions. He said investors may be reluctant to invest when the ratios indicate poor performance. Thus, to measures current assets against current liabilities it will be use current ratio or working capital ratio. To know how the company will pay back with short terms debt obligations with its current asset it is function for current ratio. He thinks the company better equipped to pay off short term debt with current asset must be a higher in ratio. So, measure quick assets against current liabilities is a quick ratio. Assets that can be convert into cash quickly it is quick assets.

According to Maria Zain (2008), in their articles he discusses about shows the company's ability to use its assets to generate income it will be used return on assets in an important percentage. He stated that the company's in high percentage when doing a good utilizing and used assets to generate income. He informed how to calculate the return on assets percentage. The formula of the return on assets is net profit will be divide by total assets. For the net profit figure must be used the amount of income after all expenses it was including the taxes. He explained when the company in low percentage its mean the company will have complication meeting with debt obligations. For operating performance, he gives the explanation that to show profit margin it used percentage in relationship between sales and profits. To calculate the profit margin is net profit divide with net sale.

According to Boumediene (2011) when customer option cancel wants to buy the commodity he suggests that credit risk occurred in Islamic bank's Murabahah financing it will cause the bank to be liable for losses when failing to complete the instalment of repayment for the goods as specified also will cause credit risk to Islamic banks. Backed by asset as collateral as a result of the risk is removed to customers when Islamic banks want to practically bear no risk when engaging in Murabahah financing (Samad, 2004). Which has been delivery by banks Murabahah is visible to credit risk when client failed to payback for the assets as in the scheduled repayment (Swartz, 2013). According to Waemustafa and Sukri (2016) interaction between liquidity and credit risk is vital to derive for empirical of evidence in Bank Specific and Macroeconomics Dynamic Determinants of Credit Risk in Islamic Banks and Conventional Bank nature of liquidity and its effect on credit risk.

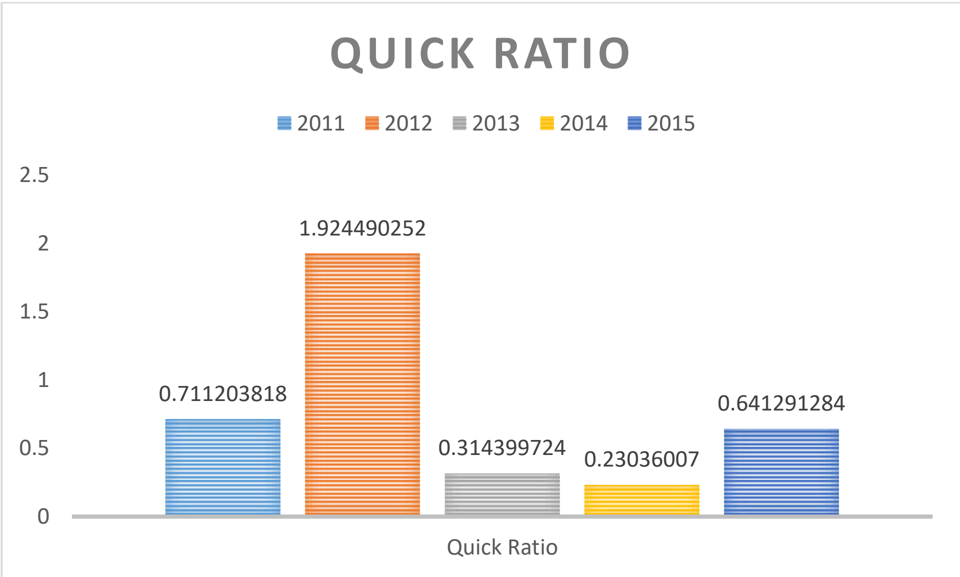
Values identified current assets and current liabilities in the Statement of Financial of Position is rely on the current ratio and the quick ratio. By dividing the total current assets by the total current liabilities to arrive at a ratio between the two amounts is simply for the current ratio. Narrower focus and is concerned with only those items are provides by the quick ratio. Otherwise, in the total current assets it is also included such as cash, marketable securities, and accounts receivable. To provide a ratio between the two amounts it will reduce amount with divide by the total current liabilities. Being an indicator of the ability to pay for every dollar that is currently liable it is the analysis in very simple terms relies on the ratio. To be a valuable guide to the analysis process industry benchmarks are considered however, a rule of thumb is generally used where these are not available. on an annual basis will be calculated and included for analysis purposes as part of this research an industry standard (Kirkham, 2012).

Basically, for the controlling of liquidity risk it is unpredictable without accurate knowledge of risk. Before arranged to a further stage for the process management of liquidity risk, it is critical to primary categorize the method of risk formation. Liquidity will give the solution to solvent bank into collapse since it must to sell their assets far below with value to achieve its current financial duties. The management of risk at the basic level will allows Islamic Banker to take defensive slightly than reactive measure when adapt with risk. It is allowing the possible financing to run part by part with more secure situation and suitable risk in manage process at the bases level (Waemustafa and Sukri, 2016).

3.0 Descriptive Analysis

3.1 Quick Ratio

Year	**2011**	**2012**	**2013**	**2014**	**2015**
Quick Ratio	0.7112	1.9245	0.3144	0.2304	0.6413

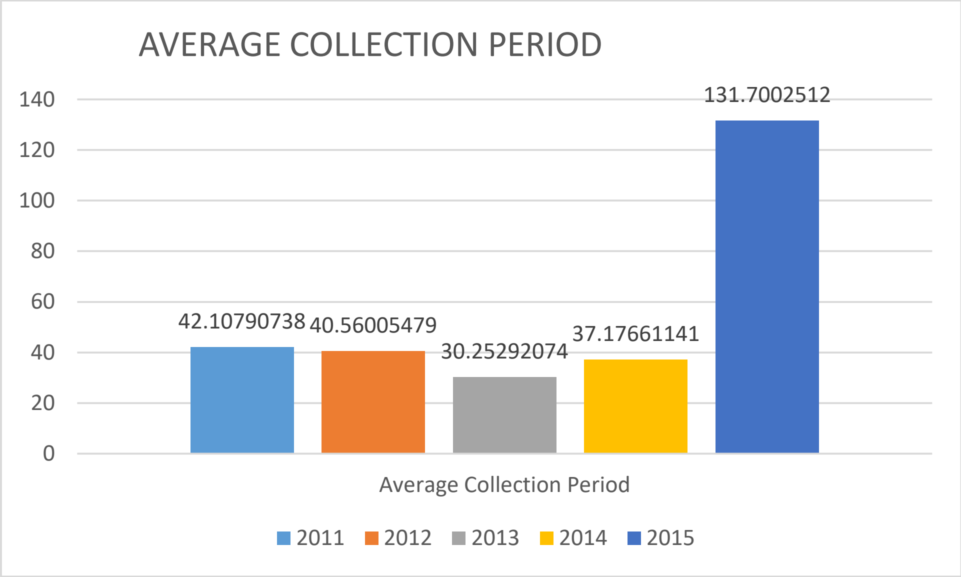


Basically Quick Ratio indicates company's ability to meet its short-term obligations with its most liquid assets. The quick ratio also tests whether a business can meet its requirements even if adverse conditions occur. Therefore, the quick ratio figure will give the investors an idea how effectively the company in ability to meets its short-term liquidity. To calculate the quick ratio is current assets minus inventories and divide by current liabilities.

Based on the above chart, it shows the quick ratio of Khee San for 5 consecutive years which is 2011 until 2015. Here, it indicates that for year 2012 the quick ratio was the highest which is 1.9245 times compared to year 2014 the quick ratio was the lowest which is 0.2304 times. Thus, we can conclude that company the year 2012 are strong compared to other years in ability to meets its short term liquidity.

3.2 Credit/Counterparty Risk

Year	2011	2012	2013	2014	2015
Average Collection Period	42	41	30	37	132



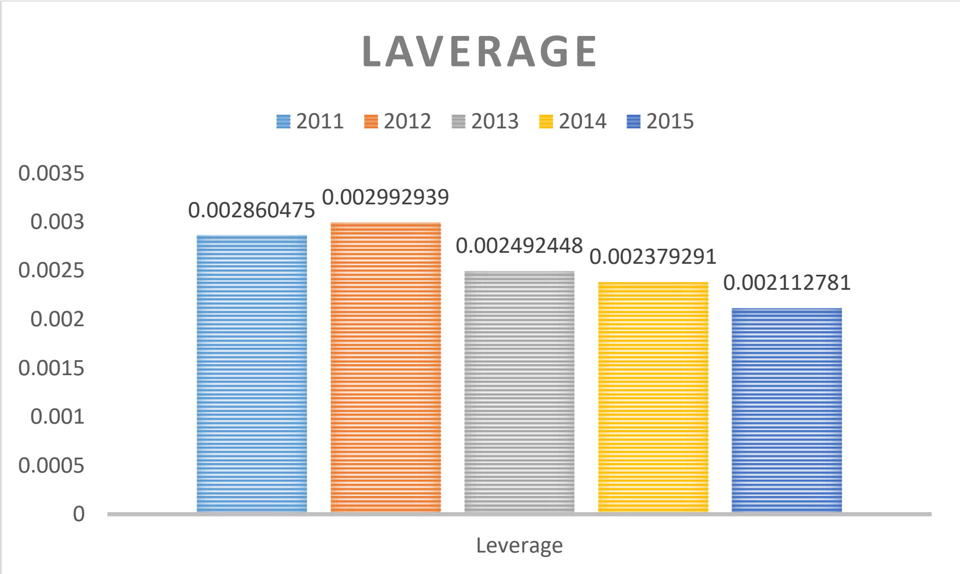
The average collection period is the estimate amount of period time that it takes for a business to receive payments owed in terms of account receivable (Investopedia, 2017). Therefore, the average collection period figure will give the investors an information of how long time the company takes to receive payments owed for their business.

To calculate the average collection period is calculated by dividing the account receivables with annual credit sales. Then, credit sales will divide by number of days in the period. The highest average collection period indicate that the long periods take by the debtor to payback the debt to the company.

Refer to the above chart, it shows the average collection period of Khee San for the year 2011, 2012, 2013, 2014 and 2015. We can see that for year 2015 the average collection period was the longer which is 132 days compared to year 2013 the average collection period was the lowest which is 30 days. Whereby, in year 2015 shows that company get in long time to get the payment from their debtor.

3.3 Leverage

Year	**2011**	**2012**	**2013**	**2014**	**2015**
Leverage	0.29%	0.30%	0.25%	0.24%	0.21%

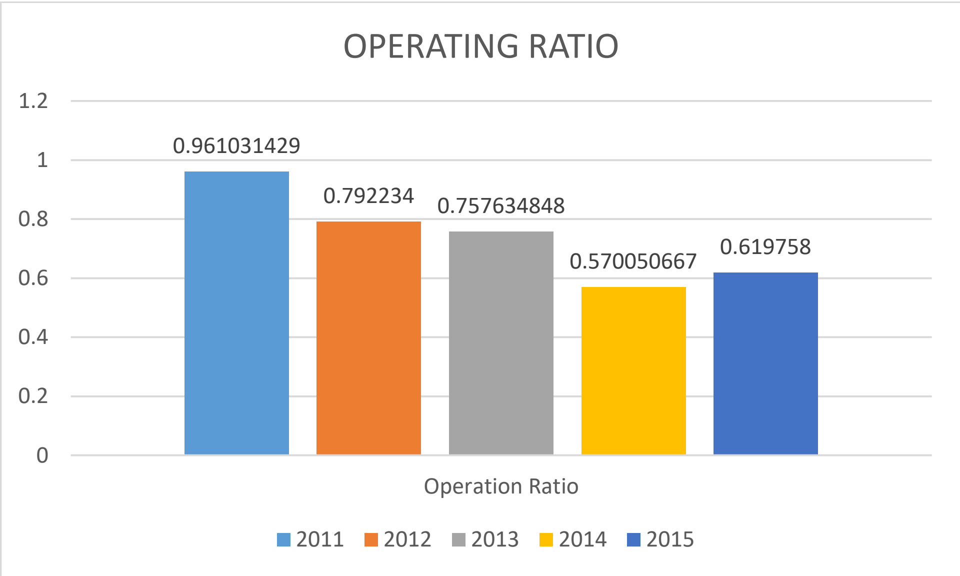


The assets of the company are comprised of both debt and equity. Both of these types of financing are used to fund the operations of the company. Therefore, the leverage ratio figure will give the investors an idea how much debt in the company. To calculate leverage ratio is calculated by total liabilities divide by total equity.

A leverage ratio is to measure how much capital comes in the form of debt or assesses the ability of a company to meet financial obligations (Investopedia, 2017). Based on the above chart, it shows the leverage ratio of Dutch Lady for 5 consecutive years which is 2011, 2012, 2013, 2014 and 2015. Here, it indicates that for year 2012 the leverage ratio was the highest which is 0.30% compared to year 2015 the leverage was the lowest which is 0.21%. This tells us that, in year 2012 the leverage of Khee San has been aggressive its growth with debt in financing. Investors will not have interested with company that have too much debt in their financing, it will be effected to the company.

3.4 Operating Risk

Year	2011	2012	2013	2014	2015
Operating Ratio	96.10%	79.22%	75.76%	57.01%	61.20%

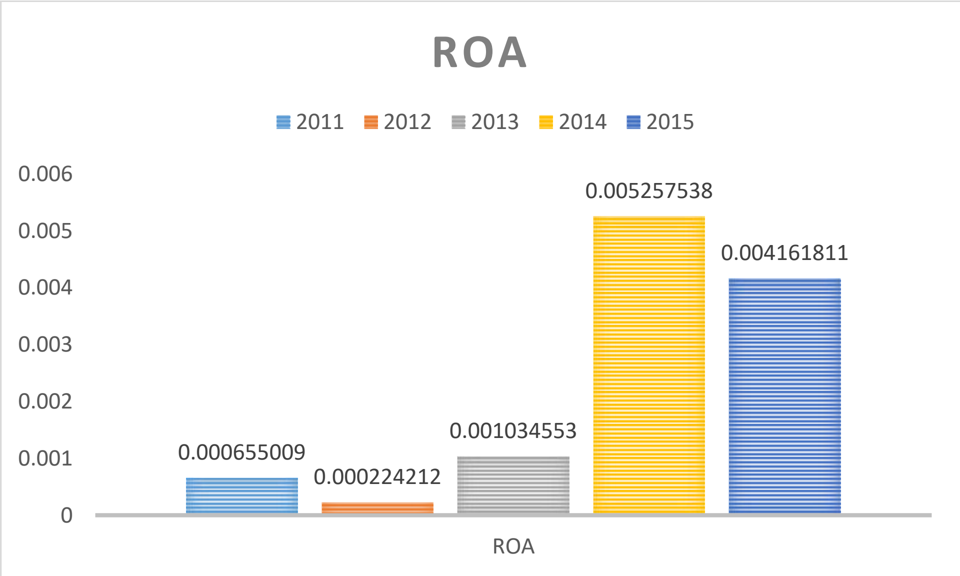


The operating ratio by comparing operating expense to net sales to shows the efficiency of a company's management. The greater the organization's ability to generate profit if revenue decrease when the ratio was smaller. For operating ratio, investors must be known that it does not take debt repayment or growth into account (Investopedia, 2017)

The formula to calculate operating ratio is operating expenses divide by net sales. Refer to the above chart, it shows the operating ratio of Khee San for 5 consecutive years which is year 2011 until 2015. Here, we can see that for year 2011 the operating ratio was the highest which is 96.10% compared to year 2014 the profit margin was the lowest which is 57.01%. Therefore, we can conclude that Khee San in year 2014 efficiency in a company's management and greater ability of the company to generate profit.

3.5 Return on Asset (ROA)

Year	2011	2012	2013	2014	2015
ROA	0.07%	0.02%	0.10%	0.53%	0.42%



The assets of the company are comprised of both debt and equity. Both of these types of financing are used to fund the operations of the company. Therefore, the return on assets figure will gives the investors an idea of how effectively the company in converting the money it has to invest into net income.

Return on assets is the amount of profit earned on each dollar invested in assets. Based on the above chart, it shows the return on assets of Khee San for 5 consecutive years which is year 2011 until 2015. Here, it indicates that for year 2014 the return on assets was the highest which is 0.53% compared to year 2012 the return on assets was the lowest which is 0.02%. This tells us that Khee San, in accounting sense, generates a little less than 0.60 cent in profit for every ringgit in assets for year 2014.

Thus, we can conclude that the company is not efficient in managing its assets to generate earnings. This is because the higher the return, the better, because it shows that the company is earning more money on less investment and the company is more effective in management to utilized its asset base.

3.6 Descriptive Statistics

	Mean	Std. Deviation	N
ROA	.00226662460	.002281668740	5
Index	.820	.1095	5
BOD_Remuneration	153320.00	13646.868	5
Size (Total Asset)	68006595.80	12953464.190	5
Leverage	.0025449560	.00036807323	5
Quick Ratio	.764349030000000	.680348048000000	5
Average Collection Period	56.359549100000000	42.363002280000000	5
Operation Ratio	.740141789000000	.154300911000000	5
GDP	5.300	.4950	5
Inflation	2.440	.6693	5

From the table above, we can see that Khee San Company is making 0.23% of return by incurring 0.23% of risk (standard deviation). In this situation, the mean and the risk are in the same percentage. We knew that the higher the risk, the higher the return, thus in order for Khee San company to increase their asset, they should go for higher risk. In addition, for Leverage the mean is 0.25% with the risk of 0.37%. so that, the company should be more efficient and effective to reduce the risk of the company. For the Leverage, the risk is higher than the mean.

3.7 Correlation

		ROA	**Leverage**	**Average Collection Period**	**Quick Ratio**	**GDP**	**Inflation**
Pearson Correlation	ROA	1.000	-.261	-.291	.514	-.817	-.242
	Index Score	-	-	-	-	-	-
	BOD_Remuneration	.039	.015	.148	-2.31	.133	-6.77
	Size (Total Asset)	.062	.850	-.737	-0.13	.318	.407
	Leverage	-.261	1.000	-.812	-.472	.346	.348
	Average Collection Period	-2.91	-.812	1.000	.269	.242	-206
	Quick Ratio	.514	-.472	.269	1.000	.107	.405
	GDP	-.817	.346	.242	-.107	1.000	.468
	Inflation	-.242	.348	-.206	.405	.468	1.000

Based on the SPSS Correlation table, which is illustrate the results of correlation matrix of Khee San, it shows that basically the company have a relationship between profitability for ROA and Board of Director Remuneration. The relationship between them which is – 0.443. Next, the relationship between Size (Total Asset) with ROA it is 0.627, whereby it shows that the higher the size of the company, so the more company can generate their profit. A good asset management also enables the company to increase the shareholder trust as they are certain that the company are efficient in converting their asset into a profit. In addition, based on the SPSS table shows that the relationship between Leverage and Profitability (ROA) is –0.754. in this relationship get the negative significant.

According to Waemustafa and Sukri (2016) the finding on their study shows that liquidity ratio (LIQUID) is positively significant with ROA this implies that Islamic banks adopt a conservative strategy in managing liquidity problem by maintaining sufficient cash reserve and at the same time these banks are able to generate profit. Based on the table SPSS shows that Liquidity Risk (Quick Ratio) also have relationship with Profitability (ROA) which is -0.573. Besides that, based on the SPSS Correlation table, it shows that for the GDP and Inflation have a relationship with Profitability (ROA) it shows in positive sign. The relationship GDP and Profitability (ROA) is 0.411 and for the relationship Inflation and Profitability (ROA) is 0.333 both of these types in a good average.

4.0 Discussion and Recommendation

4.1 Discussion

The main objective of this study was to investigate the relationship between Profitability and its impaction risk in food and beverage industry. In the descriptive analysis for the consecutive year 2011 until 2015, overall performance results to measure the risk. Profitability is the important issue in order to show a good performance in company. It is because have good profit will attract investor to join invest in the company. The relationship between size (Total Asset) and ROA in a positive relationship. When total asset in good average so, Khee San can improve the profit and get the best interest for shareholder. Next, to measure the risk which is Liquidity Risk (Quick Ratio), Credit/Counterparty Risk (Average Collection Period) and Operating Ratio. For the quick ratio SPP table show it is in negative relationship, for the average collection period it is in positive sign. Operating ratio also in negative relationship. Other than that, for the measure Profitability it uses ROA to show the profit. For the ROA of the company Khee San it is in good performance and will make profit and survive the company. Other than that, relationship ROA and Quick Ratio also in negative average.

4.2 Recommendation for Improvement

Profitability is a basic factor in give impaction to the business. From the relationship between ROA and quick ratio it shows in negative significant. The quick ratio is the key factor to give the investors an idea how effectively the company in ability to meets its short-term liquidity. When the relationship is negative, so shareholder become not interest to invest in the company. Chairman and BOD of the company Khee San must take the action to improve in ability to meets its short term liquidity. Management are important in any institution to make sure all the process is smooth in the company. Negative average for operating ratio also must to improve. The operating ratio by comparing operating expense to net sales to shows the efficiency of a company's management. The greater the organization's ability to generate profit if revenue decrease when the ratio was smaller. Khee San must make sure the ratio will be in positive relationship with ROA to give investor more confidence to invest in the company. The best performance when all the ratio and the average in positive relationship, so the company of Khee San must improve the operating in the business to generate the best profit.

5.0 Conclusion

For the conclusion, refer to the main objective of this study was to identify the relationship between risk management and its impaction in the profitability of food and beverage industry. Then, from the result of this study indicate that consideration firms' in risk management will give good impact to the firm profitability. To make the best profit in the business, it must make sure company of Khee San manage the risk with the best action. The risk is an uncertain future events which could influence the achievement of the organisation's strategic, operational and financial objectives (International Federation of Accountants,1999). We not know the risk will present, but it must identify the risk become present when do the business. The risk will mitigate if the company of Khee San have a good in risk management. It must take the best action to mitigate the risk. Risk management is a how it should be conducted and what it is for, rapidly developing discipline and there are many and varied views and descriptions of what risk management involves (IRM, 2012). Company of Khee San will maintain the performance if the profit always in positive average. It also will show to the investor the company of Khee San is the best one to be invest the share and get the best interest.

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