Performance and Risk of IOI Corporation Berhad

Harun, Nur Ilyani

Universiti Utara Malaysia

29 March 2017

Performance and Risk of IOI Corporation Berhad

Nur Ilyani Harun

Universiti Utara Malaysia

ABSTRACT

The study aims to measure corporate governance and its impact firm performance and risk of IOI Corporation Berhad (IOI). The method of the study is regression analysis of IOI by using SPSS System. The study found that IOI has a positive relationship between return on asset and return on equity. The ROA and leverage ratio also was a positive relationship. Meaning that the company has earns more profit, at the same time the company does not do any credit businesses. The regression analysis show that 3 out of 13 factors are significantly influence the profitability of IOI.

Keywords: credit risk, liquidity risk, profitability, and macroeconomics

1. INTRODUCTION

IOI Corporation Berhad, commonly referred as IOI. It was established on 31 October 1969 as Industrial Oxygen Incorporated Sdn Bhd. IOI Corporation Berhad actually is an investment holding company. The company core business are cultivation of oil palm, processing of palm oil and investment holding through its subsidiaries .The company operates in two segments which are Plantation and Resource-based manufacturing.

For information, IOI Group have a good corporate governance because the company practices the company sound governance and ethical business conduct to maintain a strong leadership. IOI also balance the interest of stakeholders and regulatory laws imposed in the countries where the company operated. In addition, the company is instilling the corporate culture and core values to each and every employee by providing them with a moral compass essentially drives the Group's commitment on doing business with integrity to achieve sustainable growth.

Besides, the present chairman of IOI is Tan Sri Dato' Lee Shin Cheng is Malaysian, age 77. He was first appointed to the Board on 21 July 1981. He is also the founder of IOI Group which was listed on Bursa Malaysia Securities Berhad on 28 July 1980. He got various of awards which are FIABCI Malaysia Property Man of the Year 2001, Honorary Doctorate Degree in Agriculture by Universiti Putra Malaysia, Fellowship of the Incorporated Society of Planters ("FISP"), Honorary Fellowship of the Malaysian Oil Scientists' and Technologists' Association ("MOSTA"), Malaysian Palm Oil Association ("MPOA") Recognition Award 2011, Palm Oil Industry Leadership Award by Malaysian Palm Oil Council ("MPOC"). In addition, he attended seven (7) out of the eight (8) Board Meetings held during the financial year ended 30 June 2015.

As of September 2015, IOI Group employed more than 30,000 persons from more than 25 countries. The businesses span all over Malaysia as well as in countries such as Singapore, China, Netherlands and USA. With the net profit of IOI Corporation Bhd was RM 407.4 million, IOI is market leaders in their respective sectors.

2. LITERATURE REVIEW

According to Giner (as cited in Ridhima, 2017), profitable companies disseminate information, to stand out from less profitable firms. Contrary to the theoretical perspective empirical studies on risk disclosure have found an insignificant relationship between risk disclosure and firm's profitability as cited in Ridihima (2017). To measure profitability of a firm, return on assets that is the ratio of operating income to total assets is used. However, the findings of ROA in IOI Corporation Berhad (IOI) is profit net of tax to total assets is used.

Next, the findings of this study shows is a positively to the findings of previous studies which are Ghazali (as cited in Waemustafa and Sukri, 2013), who found a positive relationship between liquidity and ROA. Bourke (1989). Kosmidou and Pasiouras (as cited in Waemustafa and Sukri, 2013) also found a significant positive relationship between liquidity and ROA. The findings found that the ROA and liquidity of IOI was a negative relationship. The study by Köhler (as cited in Waemustafa and Sukri, 2013) suggested that banks with a larger proportion of liquid assets are more stable enabling them to buffer against shock when needed.

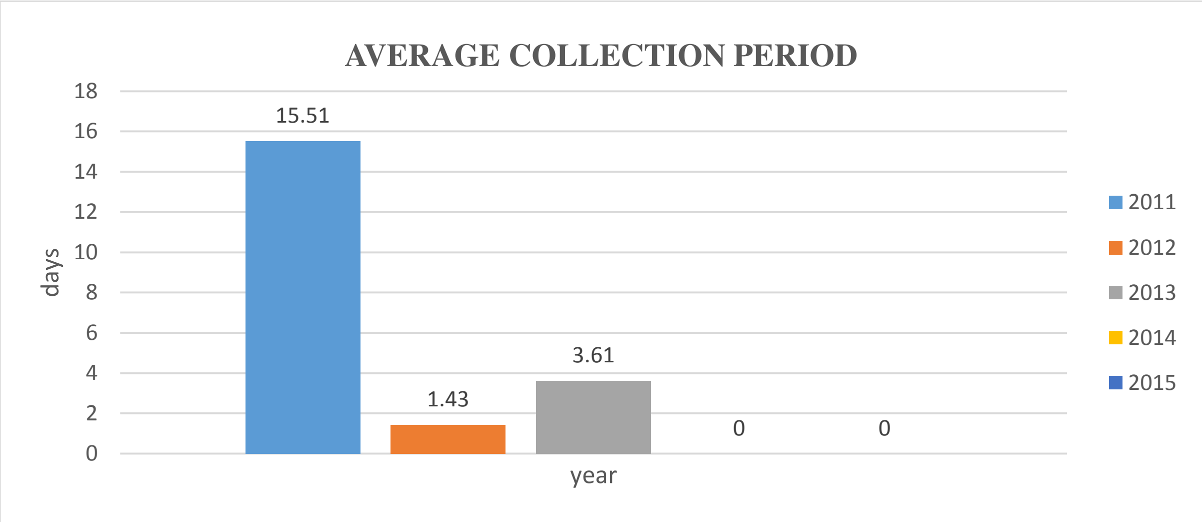
Besides with respect to capital structure of a firm, some risk disclosure studies explained by Deumes and Knechal (as cited in Ridhima, 2017) have found firm's leverage positively and significantly affect the level of risk disclosure whereas, Dobler (as cited in Ridhima, 2017) has found negative association between firm leverage and risk disclosure. On the other hand some studies as cited in Ridhima, (2017) have found insignificant relationship. Level of firm risk is measured using beta, which is covariance of company's market return relative to market index. Capital structure of the firm is measured using a total debt equity ratio.

Last but not least, the formation of credit risk include, inappropriate credit policies, poor lending practice, limited institutional capacity, volatile interest rate, poor management, inappropriate laws, direct lending, massive licensing of banks, 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 (Kolapo and Kithinji, as cited in Waemustafa and Sukri, 2015). In the findings, the relationship between liquidity and credit risk was a positive relationship. It was contrary with Cornet (as cited in Waemustafa and Sukri, 2015) was stated that the higher the liquidity the lower credit risk exposure.

Lastly, as we know, major corporate scams and failures at the international level such as Enron, Worldcom, Adelphia involving accounting irregularities, highlighted the need for good corporate governance regulations to be implemented by the corporations worldwide (Rajab and Schachler, 2009). In addition, the elements of effectiveness which is proposed in conventional corporate governance model are composition, adequate authority, resources and diligence by Ika, S.R., Ghazali, DeZoort, Hermanson, Archambeault, and Reed, (as cited in Waemustafa and Abdullah, 2015). In IOI, the company have larger board that can have a positive influence on corporate disclosures including risk exposure. It can be one of example good corporate governance. The Agency theory by Jensen and Meckling (as cited in Ridhima, 2017) suggests that board of diverse gender can increase board independence and improve managerial monitoring.

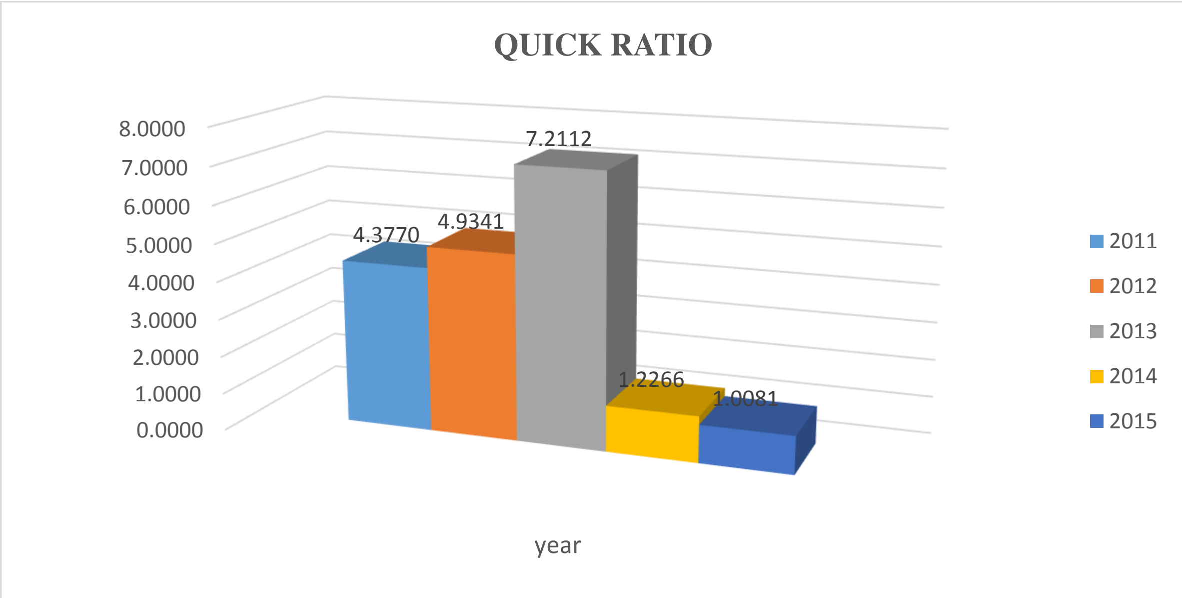
3. DESCRIPTIVE ANALYSIS

I. CREDIT RISK



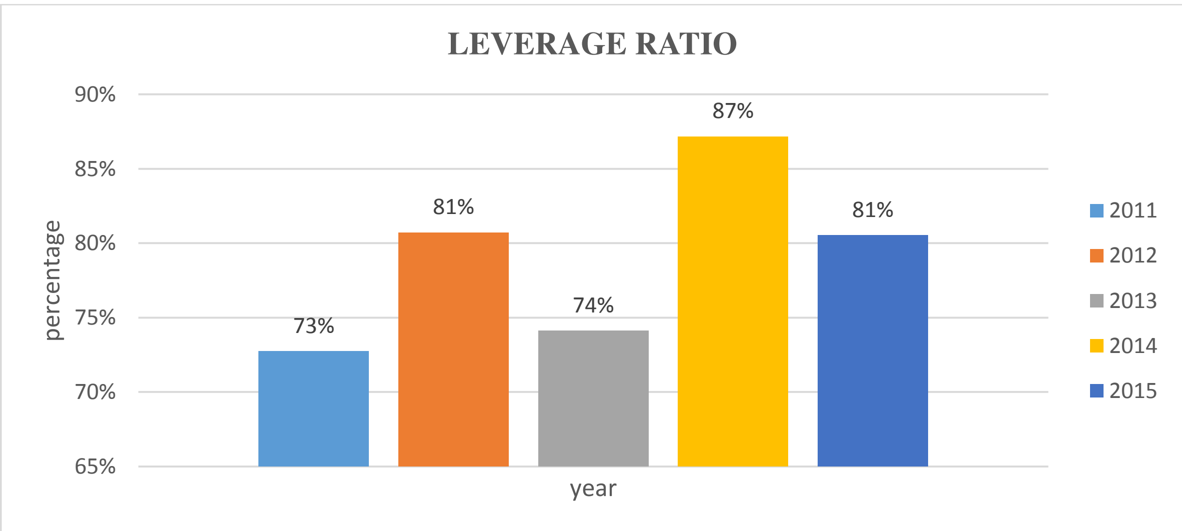
Credit risk is the risk that company must bear as result of a borrower or client might not repay the loan accordingly or unable to repay all of the debt to the company. The bar graph given above is average collection period indicate the approximate amount of time that it takes for a business to receive payments owed in terms of accounts receivable between the years 2011 until 2015. It can be seen that the days of account receivable to repay the debt was sharply decreased from 15.51 days in 2011 to zero days in 2015. In 2014 and 2015, the company maybe did not make any credit business for the clients due to the company already has high leverage. Overall, we can see clear that average collection period was decreasing year by year. This indicates that a company will have a lower receivables turnover when a shorter time period is considered due to having a larger portion of its revenues awaiting receipt in the short run.

II. LIQUIDITY RISK



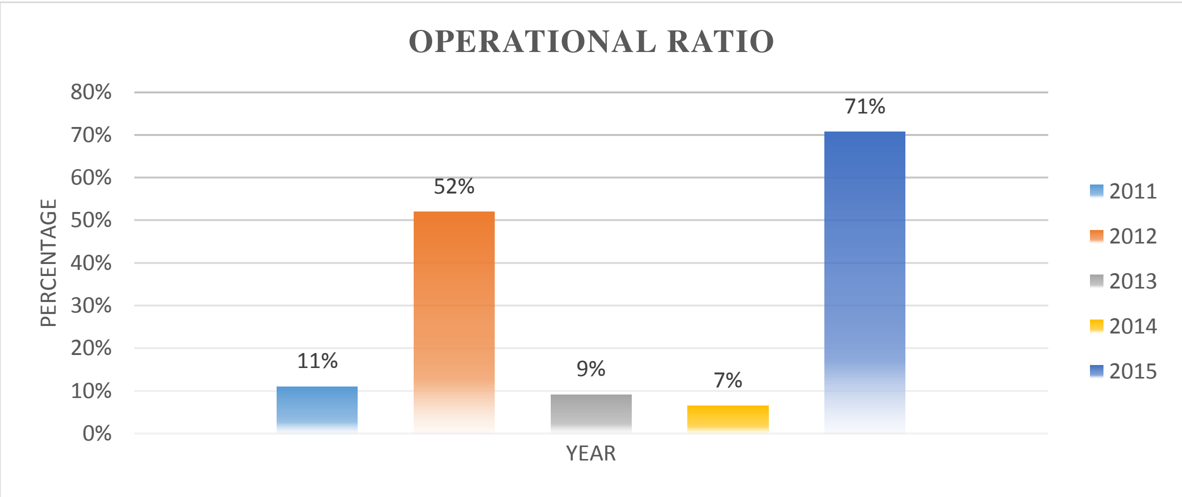
As we can see from the bar chart above, the graph show that it was decreasing and increasing trends between 4.3770 in 2011 to 1.0081 in 2015. The highest quick ratio of IOI was 7.2112 in 2013 indicates that the company can meet its current financial obligations with the available quick funds on hand. However, the lowest of liquidity in the company was 1.0081 in 2015 due to the company maybe relies too much in inventory or other asset to pay its shot-term liabilities. After 2013, the quick ratio of the IOI drastically decreased until 2015. IOI could be facing liquidity problem during 2014 until 2015.

III. LEVERAGE RATIO



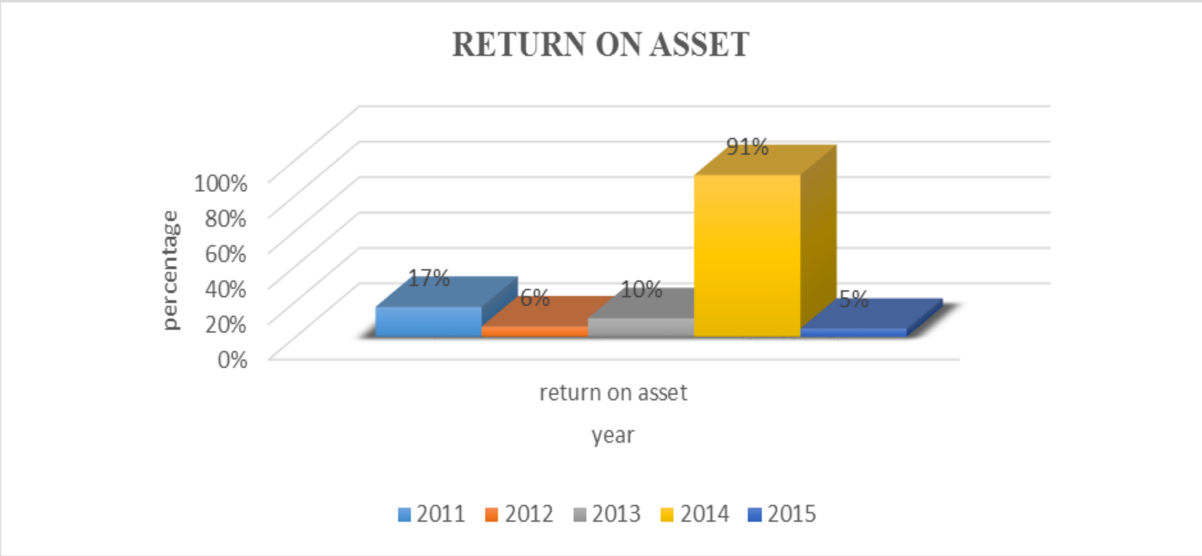
A leverage ratio is means to evaluate a company's debt levels. The most common leverage ratios are the debt ratio and the debt-to-equity ratio. The graph above shows fluctuated trends of the leverage ratio in 2011 to 2015. As indicated at the graph, the higher leverage ratio was 87% in 2014 while the lowest was 73% in 2013. The higher leverage ratio could be exposed with the higher risk whereas the lower leverage ratio might will have strong equity position. So, the IOI could be exposed with the higher risk due to their debt was high in 2014. However, all of leverage ratio was below 1.0 indicates that the company has more assets than debt. Thus, the company was doing well during 2011 until 2015.

IV. OPERATIONAL RISK

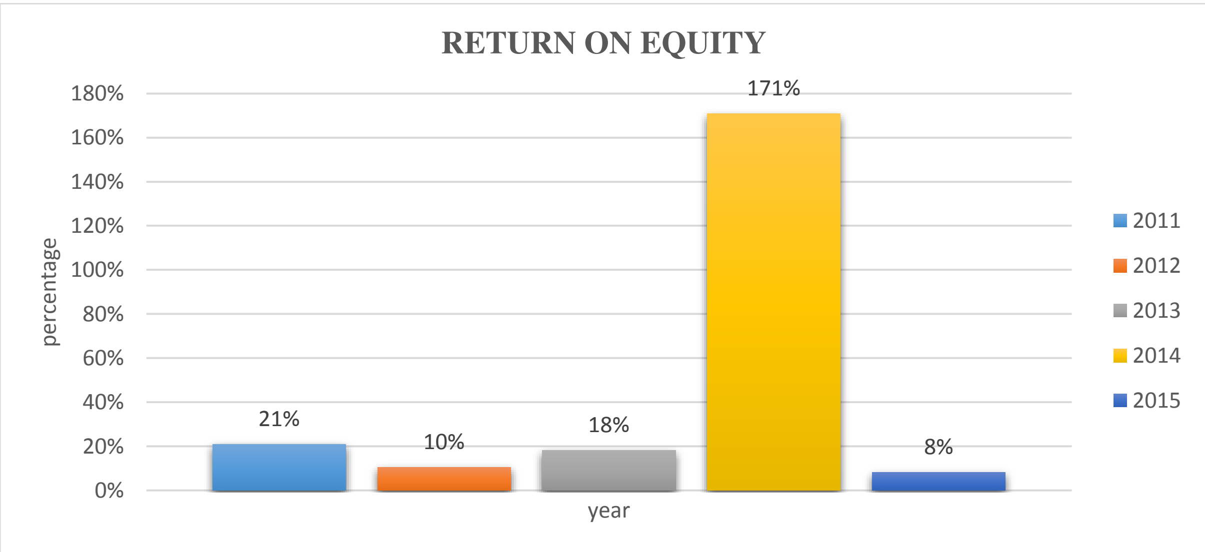


The operating ratio shows the efficiency of a company's management. The bar chart above shows the increased and decreased trends of operational ratio. The smaller the ratio, the greater the organization's ability to generate profit if revenues decrease. As we can see from the graph above, in 2014 was the lowest of operating ratio indicates that it has efficient operating environment in which operating expenses are increasingly a smaller percentage of sales whereas in 2015 has the largest operating ratio was 71%. The higher the ratio, the smaller the company's ability to generate profit.

V. PROFITABILITY RATIO



One of the way to measure company performance is by calculating Return on Asset (ROA). ROA is net profit to total asset that has been used to measure company performance. The higher of ROA indicates that the company have higher profitability. From the graph, we can see that it is fluctuate trends in percentage of ROA. Regarding to the bar graph above, the good IOI's performance was in 2014 with 91%. The higher percentage indicates that the company has higher profitability at that moment. The lowest ROA was in 2015 with 5% indicates that IOI has lower profit during that year. In addition, 86% of ROA drastically decreased from 2014 to 2015 because maybe the company did not earn more profit.



Return on equity (ROE) is the amount of net income returned as a percentage of shareholders equity. Return on equity measures a corporation's profitability by revealing how much profit a company generates with the money shareholders have invested. According to the graph above, the highest ROE was in 2014 while 2015 was the lowest one which 171% and 8% respectively. In 2011 the ROE was 21%, 2012 was 10% and 2013 was 18%. So, the ROE fluctuated year by year. In findings, the performance of company could depends on internal and external factor. An example, size of board of director sometimes affects the profitability of the company as result of greater diversity in term of expertise.

4. DISCUSSION

i. Descriptive statistics of dependent and company specific variables

Profit of average of return on asset (ROA) for five years (N=5) of the IOI Corporation Bhd is 25.76% (Table 1). It is average profit of the company earns from the assets whereas the standard deviation of ROA shows that large variations in term of profitability with 36.91% (Table 1). The standard deviation is very high than mean because the data is widely spread (less reliable). Meaning that some year very small or very big in other word it is volatility. In that case, the standard deviation higher than mean. Normally, the organization do not want the risk and profitability being volatile. For information, standard deviation is applied to the annual rate of return of an investment to measure the investment's volatility. Standard deviation is a statistical measurement that sheds light on historical volatility. The findings, the high standard deviation from the mean could due to the risk and profitability being volatile in IOI Corporation Bhd.

The mean of the liquidity of the IOI is 3.7514 while the standard deviation is 2.6297 (Table 1). This shows that the standard deviation is low not so far from average. In addition, SPSS statistics shows that the mean of average collection period is 4.1100 whereas the standard deviation is 6.5417 (Table 1). This could be explained that the company experienced different of the credit risk exposure each year. Other than that, the leverage ratio shows that every one dollar of debt is sponsored by 79.05% equity (Table 1). The study included four macroeconomic variables for IOI namely Growth Domestic Product (GDP) mean 5.300, Inflation mean 2.440, Exchange Rate mean 3.4600 and unemployment rate mean 3.0660 (Table 1).

ii. Correlation

Table 2 exhibits the result of the Pearson correlation of IOI variables. The findings of this study shows that ROA is negatively with the liquidity ratio (LIQUID) with 1 and -0.488 respectively. Means that the more profit the company earn the less cash they have. So, this study shows is contradictory to the findings of previous studies which are Ghazali (as cited in Waemustafa and Sukri, 2013), who found a positive relationship between liquidity and ROA.

Besides, ROA compared to ROE is 100% related (Table 2). So, this relationship is a positive relationship between dependent due to ROE increase when ROA increase. Other than that, the ROA and leverage ratio is a positive relationship which are 1 and 0.699 respectively (Table 2). This could due to when IOI earns more profit, at the same time the debt of the company remain unchanged or decreased. In addition, index score, BOD remuneration, GDP and inflation show a positive relationship with ROA (Table 2). The GDP is positively to ROA because of the positive economy growth that make the IOI earn more profit. However, size, average collection period, operating ratio, exchange rate and unemployment rate are negatively to ROA (Table 2).

For information, the really positive or significant can be measure by using P-value. The p value is significant must not more than 0.1. In IOI the really positive or significant are BOD remuneration, ROE, leverage ratio and GDP (Table 2). However, index score, size, average collection period, operational ratio, quick ratio, inflation, unemployment rate and exchange rate are not relevant.

iii. Coefficient

Table 3 shows a coefficient of IOI Corporation Bhd. There are four suggestions model of coefficient of IOI which are Model 1, Model 2, Model 3 and Model 4. The SPSS statistics suggest that model three is the best model compared to other models because it have more significant. Coefficient is a bit extra compared to correlation that tell us about significant, beta which direction relationship influence whether positive influence or negative influence and t- value about how big is the influence.

According to table 3, t-value of ROE have a big influence to the company which is 7242.872 while the significant is 0.000. Normally, the smaller number of significant, the biggest of t Value. In the findings, the beta of ROE is 1.009 indicates that it is positive influence to the company. However, the leverage ratio have negative influence to the company. The number of significant of leverage ratio is 0.013 while the t-value is -0.10. Besides, average collection period also give positive impacts to the company. This is because the significant is 0.014, t value is 46.673 and beta is 0.007. From the suggestions, the company must manage three main things in the company which are return on equity, leverage ratio and average collection period .This is because these three are the only relevant variables among other variables. Based on the SPSS statistic, the most significant is return on equity followed by average collection period and leverage ratio.

5. CONCLUSION

IOI Corporation Berhad is an investment holding company. The company, through its subsidiaries is engaged in the cultivation of oil palm, processing of palm oil and investment holding. The company operates in two segments which are Plantation and Resource-based manufacturing. The corporate governance of the company was doing great during 2011 until 2015. This is because the company index score was almost 100%. In this case, the company have larger board that can have a positive influence on corporate disclosures including risk exposure. It can be one of example good corporate governance.

According to SPSS statistics (table 2), the profit and the leverage of the company was a positive relationship. This shows that their debt not increased even though they earn profit. It is maybe the company has settled the debt or not do any credit business. In case, their liquidity has negative relationship with profitability. This is because it could be due to the company has been using the cash for their operations or settle the existing debt. The relationship between ROA and ROE was a positive relationship. Meaning that when ROA increased, ROE also increased. However, the profit of the company was decreasing in 2015. This indicates the IOI performance decreased.

In conclusion, SPSS statistics suggests the company must manage three main things in the company which are return on equity, leverage ratio and average collection period .This is because these three are the only relevant variables among other variables. Based on the SPSS statistic, the most significant is return on equity followed by average collection period and leverage ratio.

6. REFERENCES

Ridhima Saggar Balwinder Singh, (2017)," Corporate Governance and Risk Reporting: Indian Evidence ", *Managerial Auditing Journal, Vol. 32 Iss 4/5 pp. –*

Singh, R. S. (2017). CORPORATE GOVERNANCE AND RISK REPORTING: INDIAN EVIDENCE. *Managerial Auditing Journal*, 11-12.

Waemustafa, W., & Sukri, S. (2015). Bank Specific and Macroeconomics Dynamic Determinants of Credit Risk in Islamic Banks and Conventional Banks. *International Journal of Economics and Financial Issues*, 476.

Waemustafa, W., & Abdullah, A. (2015). Mode of Islamic Bank Financing: Does Effectiveness of Shariah Supervisory Board Matter? 1-2.

Waemustafa, W., & Sukri, S. (2016). Systematic and Unsystematic Risk Determinants of Liquidity Risk Between Islamic and Conventional Banks. *International Journal of Economics and Financial Issues*, 1323-1326.

APPENDIX

TABLE 1: DESCRIPTIVE ANALYSIS

Descriptive Statistics

	Mean	Std. Deviation	N
ROA	.257660	.3691003	5
INDEX SCORE	.8680	.04919	5
BOD_REMU	59756200.00	40013861.510	5
SIZE	11099591800.00	1321502268.000	5
ROE	.473340	.6947031	5
AVG.COLLECTION PERIOD	4.1100	6.54172	5
OPERATING RATIO	.298640	.2952731	5
LEVERAGE RATIO	.790500	.0581167	5
QUICK RATIO	3.751400	2.6296711	5
GDP	5.300	.4950	5
INFLATION	2.440	.6693	5
EXCHANGE RATE	3.4600	.49168	5
UNEMPLOYEMENT RATE	3.0660	.14758	5

TABLE 2: CORRELATION

Correlations

		ROA	INDEX SCORE	BOD_REMU	SIZE	ROE	AVG.COLLECTION PERIOD	OPERATING RATIO	LEVERAGE RATIO	QUICK RATIO	GDP	INFLATION	EXCHANGE RATE	UNEMPLOYEMENT RATE
Pearson Correlation	ROA	1.000	0.135	0.939	-0.066	1.000	-0.231	-0.539	0.699	-0.488	0.785	0.644	-0.023	-0.321
	INDEX SCORE	0.135	1.000	0.012	-0.439	0.147	-0.974	0.357	0.608	-0.133	0.000	-0.635	0.330	0.250
	BOD_REMU	0.939	0.012	1.000	0.278	0.936	-0.052	-0.735	0.512	-0.186	0.759	0.643	-0.358	-0.627
	SIZE	-0.066	-0.439	0.278	1.000	-0.074	0.568	-0.612	-0.471	0.772	0.064	0.131	-0.983	-0.915
	ROE	1.000	0.147	0.936	-0.074	1.000	-0.243	-0.529	0.708	-0.493	0.787	0.635	-0.016	-0.315
	AVG.COLLECTION PERIOD	-0.231	-0.974	-0.052	0.568	-0.243	1.000	-0.434	-0.746	0.347	-0.145	0.543	-0.445	-0.351
	OPERATING RATIO	-0.539	0.357	-0.735	-0.612	-0.529	-0.434	1.000	0.187	-0.356	-0.201	-0.669	0.574	0.773
	LEVERAGE RATIO	0.699	0.608	0.512	-0.471	0.708	-0.746	0.187	1.000	-0.712	0.742	0.032	0.314	0.140
	QUICK RATIO	-0.488	-0.133	-0.186	0.772	-0.493	0.347	-0.356	-0.712	1.000	-0.535	-0.328	-0.707	-0.583
	GDP	0.785	0.000	0.759	0.064	0.787	-0.145	-0.201	0.742	-0.535	1.000	0.468	-0.198	-0.339
	INFLATION	0.644	-0.635	0.643	0.131	0.635	0.543	-0.669	0.032	-0.328	0.468	1.000	-0.090	-0.284
	EXCHANGE RATE	-0.023	0.330	-0.358	-0.983	-0.016	-0.445	0.574	0.314	-0.707	-0.198	-0.090	1.000	0.944
	UNEMPLOYEMENT RATE	-0.321	0.250	-0.627	-0.915	-0.315	-0.351	0.773	0.140	-0.583	-0.339	-0.284	0.944	1.000
Sig. (1-tailed)	ROA		0.414	0.009	0.458	0.000	0.355	0.174	0.095	0.202	0.058	0.121	0.486	0.299
	INDEX SCORE	0.414		0.492	0.230	0.407	0.002	0.278	0.138	0.416	0.500	0.125	0.294	0.343
	BOD_REMU	0.009	0.492		0.325	0.010	0.467	0.079	0.189	0.382	0.068	0.121	0.277	0.129
	SIZE	0.458	0.230	0.325		0.453	0.159	0.137	0.211	0.063	0.459	0.417	0.001	0.015
	ROE	0.000	0.407	0.010	0.453		0.347	0.179	0.091	0.199	0.057	0.125	0.490	0.303
	AVG.COLLECTION PERIOD	0.355	0.002	0.467	0.159	0.347		0.232	0.074	0.284	0.408	0.172	0.227	0.281
	OPERATING RATIO	0.174	0.278	0.079	0.137	0.179	0.232		0.382	0.278	0.373	0.108	0.156	0.063
	LEVERAGE RATIO	0.095	0.138	0.189	0.211	0.091	0.074	0.382		0.089	0.076	0.480	0.303	0.411
	QUICK RATIO	0.202	0.416	0.382	0.063	0.199	0.284	0.278	0.089		0.177	0.295	0.091	0.151
	GDP	0.058	0.500	0.068	0.459	0.057	0.408	0.373	0.076	0.177		0.213	0.375	0.289
	INFLATION	0.121	0.125	0.121	0.417	0.125	0.172	0.108	0.480	0.295	0.213		0.443	0.322
	EXCHANGE RATE	0.486	0.294	0.277	0.001	0.490	0.227	0.156	0.303	0.091	0.375	0.443		0.008
	UNEMPLOYEMENT RATE	0.299	0.343	0.129	0.015	0.303	0.281	0.063	0.411	0.151	0.289	0.322	0.008	
N	ROA	5	5	5	5	5	5	5	5	5	5	5	5	5
	INDEX SCORE	5	5	5	5	5	5	5	5	5	5	5	5	5

BOD_REMU	5	5	5	5	5	5	5	5	5	5	5	5	5
SIZE	5	5	5	5	5	5	5	5	5	5	5	5	5
ROE	5	5	5	5	5	5	5	5	5	5	5	5	5
AVG.COLLECTION PERIOD	5	5	5	5	5	5	5	5	5	5	5	5	5
OPERATING RATIO	5	5	5	5	5	5	5	5	5	5	5	5	5
LEVERAGE RATIO	5	5	5	5	5	5	5	5	5	5	5	5	5
QUICK RATIO	5	5	5	5	5	5	5	5	5	5	5	5	5
GDP	5	5	5	5	5	5	5	5	5	5	5	5	5
INFLATION	5	5	5	5	5	5	5	5	5	5	5	5	5
EXCHANGE RATE	5	5	5	5	5	5	5	5	5	5	5	5	5
UNEMPLOYEMENT RATE	5	5	5	5	5	5	5	5	5	5	5	5	5

TABLE 3: COEFFICENTS

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Collinearity Statistics	
		B	Std. Error	Beta			Tolerance	VIF
1	(Constant)	0.006	0.003		1.955	0.146		
	ROE	0.531	0.004	1.000	130.999	0.000	1.000	1.000
2	(Constant)	0.093	0.018		5.255	0.034		
	ROE	0.538	0.002	1.013	276.803	0.000	0.499	2.003
	LEVERAGE RATIO	-0.114	0.023	-0.018	-4.916	0.039	0.499	2.003
3	(Constant)	0.053	0.001		51.859	0.012		
	ROE	0.536	0.000	1.009	7242.872	0.000	0.316	3.164
	LEVERAGE RATIO	-0.064	0.001	-0.010	-49.566	0.013	0.149	6.710
	AVG.COLLECTION PERIOD	0.000	0.000	0.007	46.673	0.014	0.281	3.560
4	(Constant)	0.060	0.000					
	ROE	0.536	0.000	1.009			0.179	5.597
	LEVERAGE RATIO	-0.066	0.000	-0.010			0.038	26.251
	AVG.COLLECTION PERIOD	0.000	0.000	0.006			0.006	154.090

INDEX SCORE	-0.006	0.000	-0.001			0.011	92.133
a. Dependent Variable: ROA							