Firm Performance And Risk In Real Estate Industry : Relationship Between Corporate Governance

badron, nur fateha

universiti utara malaysia

18 April 2017

FIRM PERFORMANCE AND RISK IN REAL ESTATE INDUSTRY : RELATIONSHIP BETWEEN CORPORATE GOVERNANCE

Nur Fateha Binti Badron

Universiti Utara Malaysia

ABSTRACT

Corporate governance is an important tools in a company so the company will be manage in a good way and based on the MCCG 2012. It also will help the company to manage their risk. Performance of a company is important as they will show how is the company be manage. Other than that it will help the company get investment from other investor. In this assignment we will see if the corporate governance give a good or bad impact to the company. We also will see if the company are exposed other factor that may be effected their performance and risk.

Keyword: Credit risk, liquidity, profitability and macroeconomic

1.0 INTRODUCTION

1.1 Background of Company

KLCC Property Holdings Berhad ("KLCCP") was fused as an open restricted organization under the Organizations Act 1965 on 7 February 2004 and was recorded on the Main Board of Bursa Malaysia Securities Berhad on 18 August 2004. KLCCP group was transformed into stapled structure that known as KLCCP Stapled Group. It was one of restructuring practice that has been implemented by KLCCP in 2013.

The existing ordinary share of KLCCP has been merge with KLCC Real Estate Investment Trust (KLCC REIT) and forming KLCCP Stapled Securities. This share has been listed under sector of REIT in Main Market of Bursa Malaysia Securities Berhad. PETRONAS Twin Towers, Menara Exxon Mobil and Menara 3 PETRONAS office building that held by subsidiaries of KLCCP now owned by KLCC REIT.

Suria KLCC (a leading shopping mall) and Mandarin Oriental, Kuala Lumpur (a luxury hotel) is still owned by KLCCP which is under KLCC Development. 33% interest of Menara Maxis is owned by KLCCP. Other than that KLCCP also owns Kompleks Dayabumi which is located within the older central commercial area of

Kuala Lumpur. This is one of the property that owns by KLCCP beyond of KLCC Development. KLCCP also fully owns KLCC Urusharta Sdn Bhd and KLCC Parking Management Sdn Bhd. Both of it is subsidiaries to KLCCP and providing facility management services and car parking management services respectively.

KLCCP has appoint KLCC REIT Management Sdn Bhd which is its subsidiary to manage and administer the KLCC REIT parallel with their objectives and investment policy. KLCCP Stapled Group's becomes one of the most strongest company because of their premium asset within KLCCP Development which is one of the real estate that has been integrated develop in the world.

Property investment and facility management services is the niche for KLCCP Stapled Group. The company is planning to maintain their performance of operational at a high standards, build up its premium strength asset to increase their profit and sustain development by exploring prospect. View in appendix 1 for KLCCP Stapled Group Structure and appendix 2 for KLCC REIT Structure.

Based in appendix 3 it shows the price change of the company for the past 5 years. The mean of price change of the company is 0.0051% which is good for a company. While their standard deviation of price stock change in previous 5 years is 0.1086%. Based on this appendix the lowest price you will see for previous 5 years is -0.6. While the maximum price is 0.84.

1.2 Corporate Governance Structure

View appendix 4

2.0 LITERATURE REVIEW

Nowadays, corporate governance become an important elements in a company to determine their performance of firm and impact on their risk. As state in MCCG 2012 it is legal for company to implement Code of Conduct Corporate Governance in company that has listed in Bursa Malaysia Securities Berhad. A company will be punished if they did not practice their corporate governance as state in every annual report of their company.

Shleifer and Vishny (1997) states that governance is a set of procedure, rules and structure that conduct by a manager to ensure that their investors getting back their returns of funds without any misleading. It is parallel with Karatzias Vassileios (2011) which state that managers has to conduct the corporation in order to take a good care the value of owner which is shareholders. Garvey and Swan (1994) authenticate that governance is decisions that have been made by top manager of a company or firm. There is no exact meaning that can give a clear picture about governance.

Since early 80's the discussion about corporate governance has been started. It is because of carelessness among American managers towards their interest of shareholders. OECD (Organization for Economic Co-operation and Development) has implemented corporate governance through many years as it give an impact to the performance of company(Igor Todorović,2013).

Based on the definition above it show that to increase the value of shareholders besides the interest of stakeholders a company have to increase their corporate performance and accountability. Other than that a company have to direct and manage based on the process that have been structured by the company. Therefore, a company have to implement both enterprise (performance) and accountability in order to be a good corporate governance.(The Ministry of Finance, Singapore,2001). As corporate governance is important for them to maintain a good corporate governance as it will give an impact to their company such stated by Waeibrorheem Waemustafa and Azrul Abdullah (2015) that an Islamic Bank will achieve their objectives if the bank implied Shariah and good corporate governace. This is situation is same goes to a company.

Igor Todorović (2013) a good corporate governance will give a good impact to the performance of company. As a good corporate governance have been implemented in a company it can prevent the company from scandal issue, civil problems, and company criminal liability. A good corporate governance also is a features to create an attractive investment environment for the shareholders invest as it is needed in a good competition between the competitive company in order to achieve a strong financial position (Humera Khan,2011). Moreover it is needed to facilitate the success of a company as it will increase the company reputation and become more attractive to stakeholders. There are many proof shows that a good corporate governance will lead to profit and become more competitive. (Igor Todorović,2013)

As in research of Okeahalam and Akinboade (2003), it stated that important for a company to have a good corporate governance. It have been proof when there is many misleading and corruption in business environment that happen in Africa as it shows that transparency and safeguard can be create from an effective of corporate governance. It can help to promote the company to the investor outside of the country.

But there is also a negative impact to the company as the corporate governance become bigger and the ownership of a company increase. As it will become add cost to the company expenses (Baysinger et al.1991; Bushee, 1998; Wahal and McConnell, 2000). Especially in R&D , capital(Wahal and McConnell, 2000) , possibility and forecast of a management (Ajinkya, Bhojraj, and Sengupta,2005), increase comprehensive social, ethical and environmental exposure (Solomon and Solomon, 2006), and decrease management profit (Hsu and Koh, 2005).

Risk management will get the same impact as performance company based on corporate governance. It become important in a company since last fifteen years. Globalization will develop capital market and increasing of uncertainty volatility at corporate sector. Company will be impact on capital structure and their performance. A development of financial management will be focusing on the resources of risk which is interest rate, foreign exchange, equity and commodity (Petre Brezeanu, Mohammed Subhi Al Essawi, Dorina Poanta, And Leonardo Badea, 2011)

Investors will concern about risk of a company. It is important for a company to manage their risk which is include monitoring the level of risk in order to take a good care shareholder interest. It is better if there is separation or create a risk management committee that can give advice to the board or warning them about the exposure risk(Walker, 2009). Waemustafa and Sukri(2016) it is good for an Islamic Bankers to prevent the risk before happen than measure the risk. As a company e should take this action as it give good impact for our company.

Agency conflict happen because of the instability of the firm earning (Bathala and Rao, 1995). Governance practices need to be design in prevent sub-optimal risk-taking. Christy, Matolcsy, Wright, and Wyatt (2013) had been using the instability of stock return to measure the risk and the relationship between the corporate governance variables and risk. They state that there is negative relationship between the governance variable, board independence and qualifications. But it is differ with Humera Khan (2011) that state manager need to concern with the market risk and the risk of the stock return as their firm depends on it in order to take a good care of shareholder interest.

3.0 DESCRIPTIVE ANALYSIS

a) Return on Asset

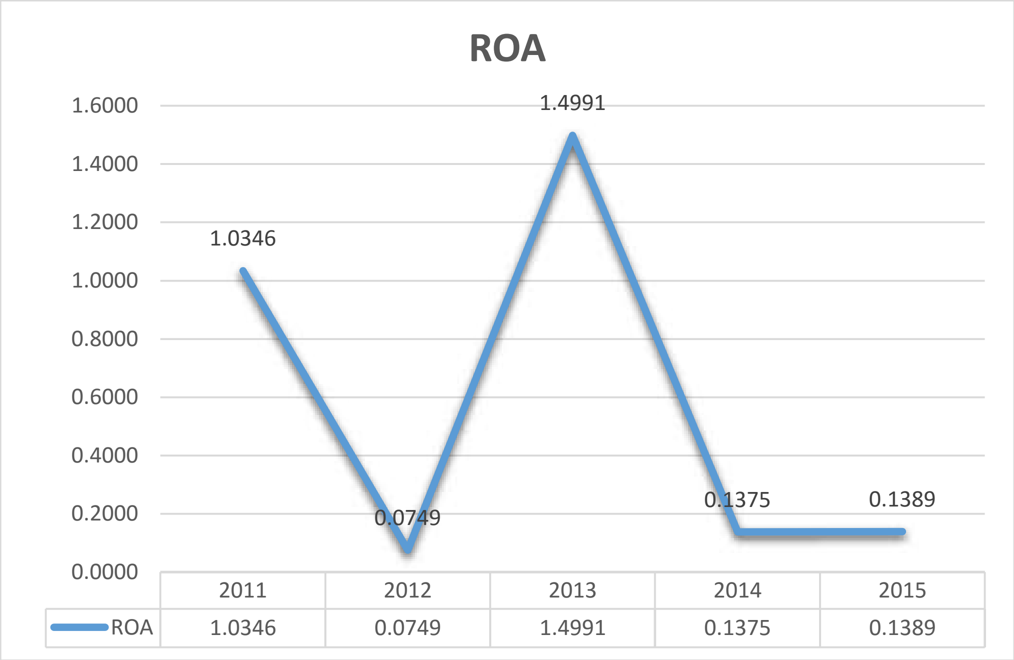
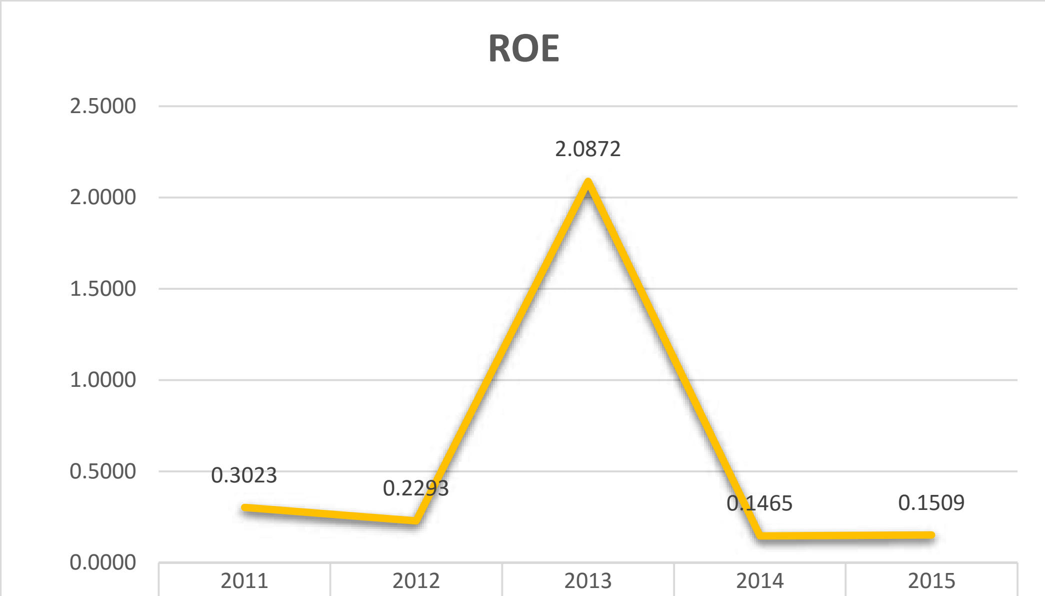


Figure 1

Return on asset (ROA) is the indicator to measure the reliability of profit towards its total asset of a company. It is one of the indicator that shows how efficient of a company manage their asset to gain profit. It help investors and management to see how well their company convert their investment asset into profit. The higher the percentage, the better it is in generate profit. As we can see from figure 1, ROA of the company in 2012 is lowest among 5 years which is 0.0749%. It show a significant changes from year 2011. It has decline 0.9597% from 1.0346%. While in 2013 ROA has been increase 1.4242% which make ROA for that year highest among other years and it shows that the company had manage their asset efficiently compare other years. But it decline again in 2014 with 1.3616% different from 2013 and increase 0.0014% in 2015.

b) Return on equity



	2011	2012	2013	2014	2015
ROE	0.3023	0.2293	2.0872	0.1465	0.1509

Figure 2

Return on equity is the percentage that the investor will get based on the profit that the company will generate. Shareholders equity is not included preferred share. It will help the investor knowing their return on the investment that they have been done. Based on figure 2 it shows that the higher percentage of return that investor get is on 2013 with 2.0872%. It means that the company has generate higher profit on that year. While the lowest percentage return on equity is in 2014 with 0.1465% . But there is other factors that may influence the return on equity of the shareholders as their profit on that year is not the lowest among other years.

c) Return on Investment

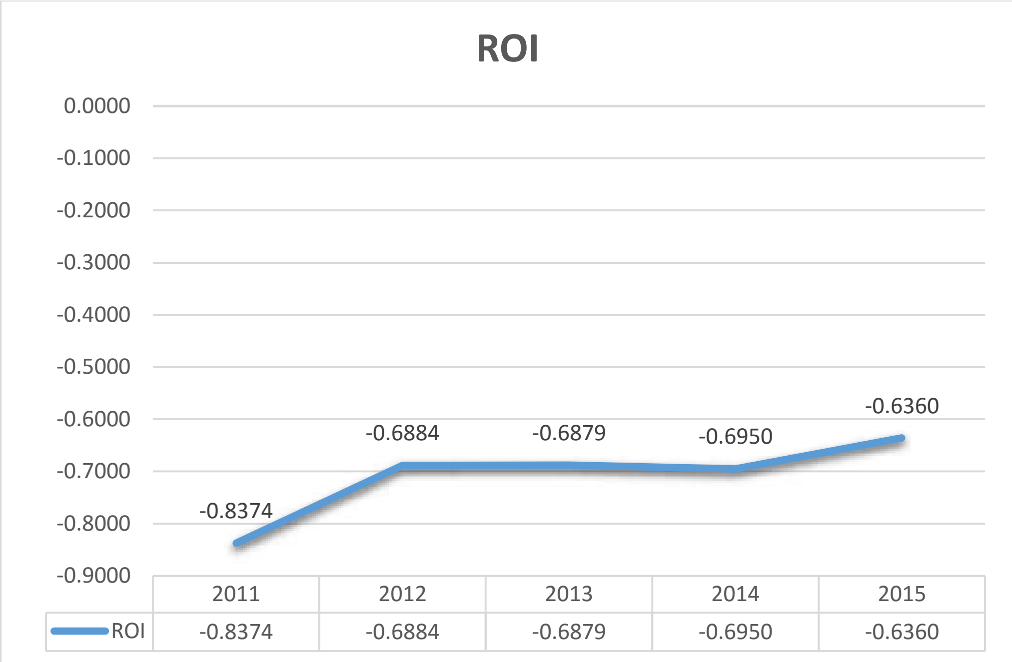


Figure 3

Return on investment is one of the profitability indicator. This indicator is use to know the investment that are most efficient between other investment. The amount return on investment are related to the investment cost on that year. It is the basic measure of an investment profitability. It will help the investor evaluate the investment in a simple or easy way. The investor will know the most investment that are preferable for them. In the figure 3 we can see that the return on investment is increasing from year to year. The lowest percentage return on investment is in 2011 with -0.8374% while the higher percentage return on investment is in 2015 with -0.6360%. It is good for the company investment as it increase from year to year.

d) Current ratio

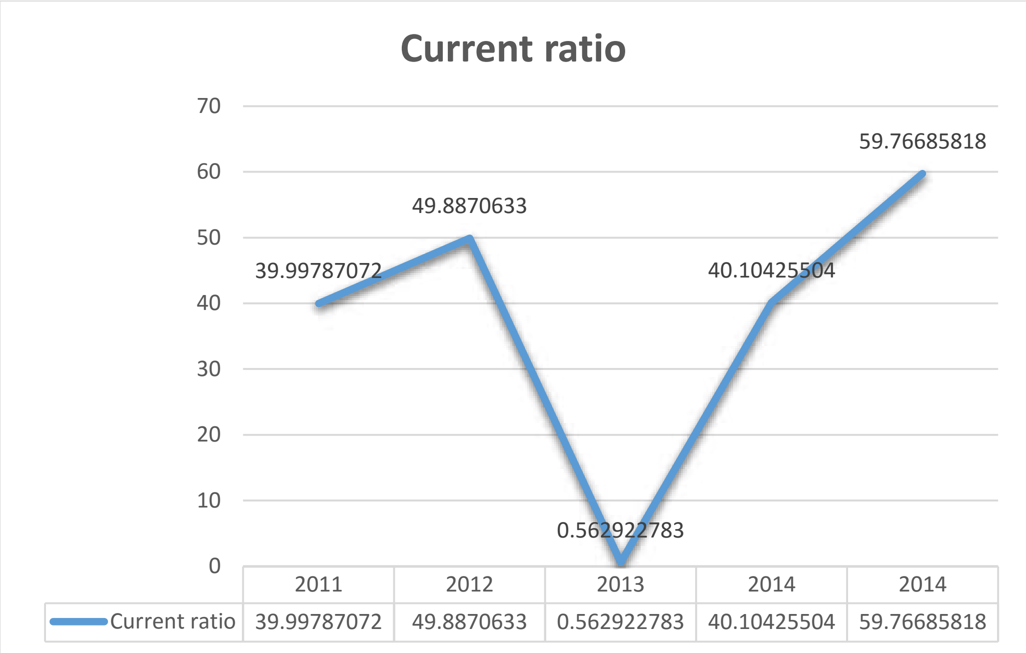
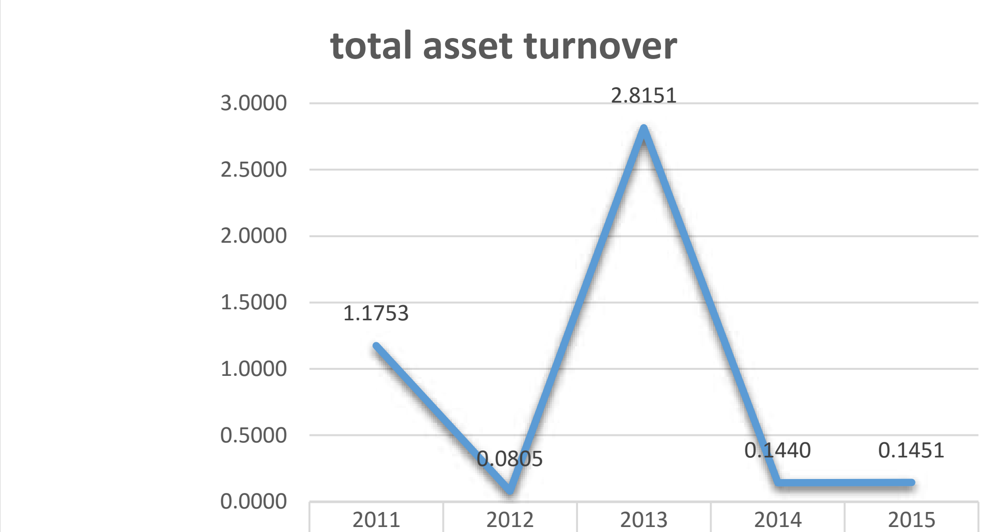


Figure 4

Current ratio is one of the indicator that can be used to measure the ability of a company to pay back their liabilities in a year. It also help to show the company performance in a year and how they manage their asset against their liabilities. The higher the percentage of current ratio it shows that the company are capable or loyal to pay back their liability and efficient in manage their asset. In figure 4 it show that on 2013 the percentage of current ratio is the lowest among others year with 0.5629%. The company has less liquidity in that year and high risk for the company payback their liability. While in 2015 the liquidity of the company is highest among others year with 56.7668% and low risk in payback their liability. It is one of the factor that may consider by an investor in choosing their investment. They will be confident in choosing the investment as they know that company is able to pay their return. It also is an advantages to the company if they need to apply loan with bank.

e) Total asset turnover



	2011	2012	2013	2014	2015
total asset turnover	1.1753	0.0805	2.8151	0.1440	0.1451

Figure 5

Total asset turnover is one of the activity ratio indicator. It measure the cycle of using asset in a company to generate their annual sales. The highest the percentage of total asset turnover is better for company. Even it is not good for shareholders as it increase their cost fund and decreased their return but it is good for the company because it show how fast they generate their profit. Which means the company generate a good sales in a year as the asset keep changing or keep restock. It also show the efficiency of a company in manage their asset to generate sales. In figure 5 shows that in 2011 KLCC REIT success to make 1.175% of total asset turnover and it decrease 0.3703% in 2012. While in 2013 KLCC REIT success to manage their asset in generate sales or cash as it was the highest percentage of total asset turnover among other years with 2.8151%. In 2014 and 2015 the percentages of the total asset turnover was almost the same as with just 0.001% different.

f) Debt ratio

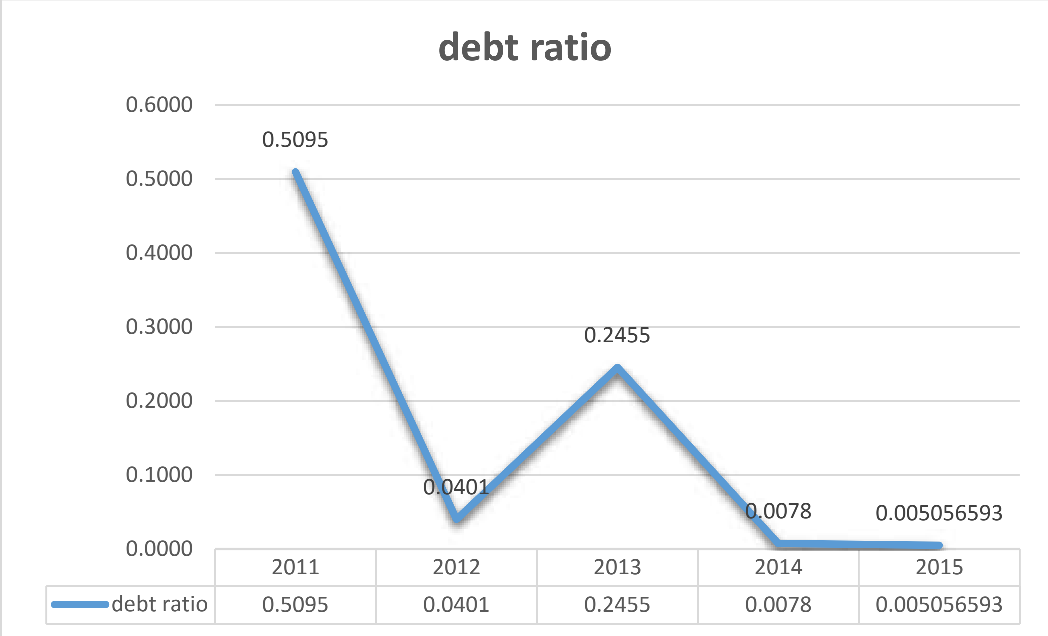


Figure 6

This ratio will measure the size of leverage in a company. It also shows the proportion of a company asset that are financed by debt. The higher the percentage of debt ratio the bigger is their leverage and it will be more riskier for the company. At the same time it will be an important tool to the company as it help the company to grow and develop. Based on the data in figure 6, it show us that in 2011 the company has bigger leverage than other years with 0.5095%. which make their leverage almost 100%. The lowest percentage is 0.0050% in year 2015. The ratio that are lowest than 100% is better for a company as it shows that their asset is more than their debt and vice versa. By using this ratio it helps the investor to know the risk of the company.

4.0 DISCUSSION AND CONCLUSION

Performance of a company will be affected by two factors which is systematic risk and unsystematic risk. We should consider both of this factor in evaluating a company. Systematic risk is the risk that can not be controlled by the company. This risk will give impact to all market in Malaysia and not for particular market. This type of risk is unpredictable and can not be avoid. It is also cannot be avoid by diversification but only through strategy of asset allocation.

While unsystematic risk is can be reduced by diversification. Such an investor that have diversified stock at diversify company or industry. So they are nor really exposed to the risk but they can control it by diversification.

As we can see in this company they are exposed to market risk, credit risk and liquidity risk. We can see their future performance through SPSS analyzation which is in appendix 5. In the analysis it shows that their profit which is ROA will be negatively correlated to GDP. Which means that when GDP decrease ROA of the company will increase. We can analyse it by compare data in ROA(figure 1) with Malaysia Economy Outlook (figure 6). Other than that we also can see that their ROA will have significant to the factor variables which is ROI, liquidity, laverage, and GDP.

Based on the SPSS data it shows that there are 1 dependant variable which is ROA and 4 independent variable which is ROI, liquidity, laverage, and GDP. The data shows that the mean or average profit that the company can get in previous 5 years is 0.5771% while their standard deviation for profit every 5 years is 0.6513%.

We conclude here that the performance for the company for previous 5 years is in a good condition as they can manage their asset efficiently. They also manage their internal control or corporate governance based on the MCCG 2012. So, based on this assignment we can conclude that this company have negatively relationship with the risk and performance of the company. Which means that their corporate governance will not give impact to their performance and risk as they expose to the systematic risk

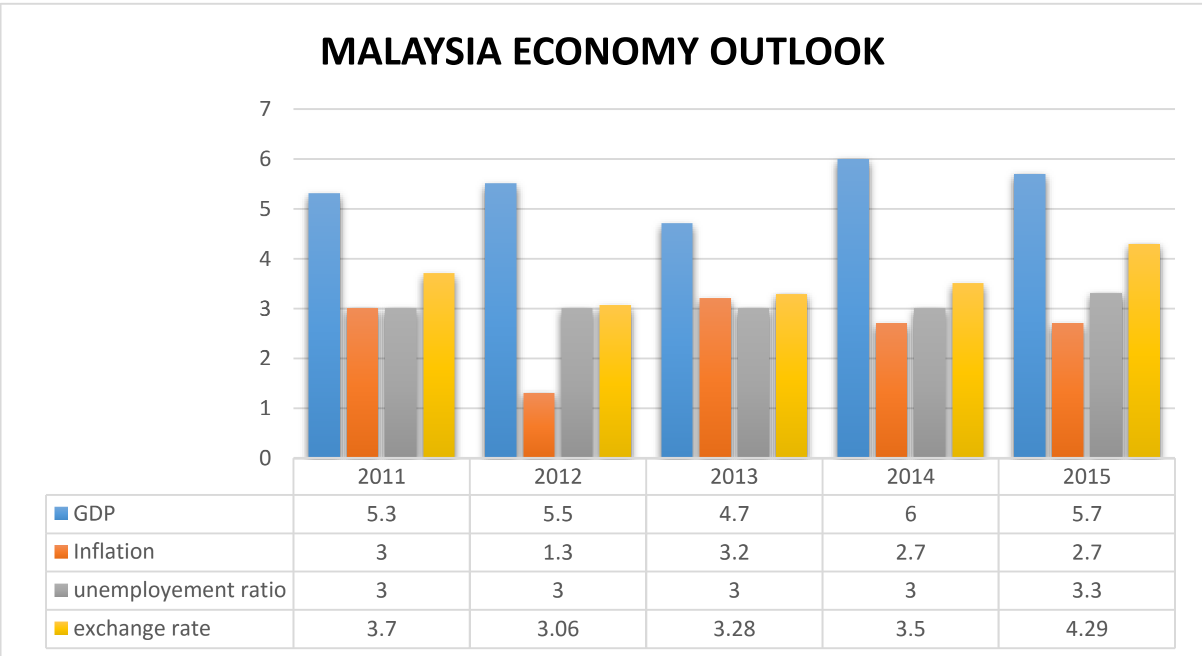


Figure 7

References

Ajinkya, B., Bhojraj S., and Sengupta, P. (2005). The association between outside directors, institutional investors and the properties of management earnings forecasts. *Journal of Accounting Research*, 43(3): 343-376.

Bathala, C. T., and Rao, R. P. (1995). The determinants of board composition: An agency theory perspective. *Managerial and Decision Economics*, 16, 59-69.

Baysinger, B.D., and Hoskinson, R. (1990). The composition of boards of directors and strategic controls: Effects on corporate strategy. *Academy of Management Review*, 15(1): 72-87

Christy, J.A., Matolcsy, Z.P., Wright, A., and Wyatt, A. (2013) Do board characteristics influence the shareholders' assessment of risk for small and large firms? *Abacus*. Doi: 10.1111/Abac.12005

Todorović. I, (2013), "Impact Of Corporate Governance On Performance Of Companies", *Motonegrin Journal of Economics*, vol 9, no 2.

Hsu, G.C.M. and Koh, P.-S. (2005). Does the presence of institutional investors influence accruals management? Evidence from Australia. *Corporate Governance*, 13(6):809-823

Khan.H., (2011), "A Literature Review of Corporate Governance", International Conference on E-business*, Management and Economics* IPEDR Vol.25

Okeahalam C., and Akinboade. O. A., (2003), "A Review of Corporate Governance in Africa:Literature, Issues and Challenges", *Global Corporate Governance Forum*.

Solomon, J. F. and Solomon, A. (2006) Private social, ethical and environmental disclosure. *Accounting, Auditing & Accountability Journal*, 19(4): 564-591

Waemustafa. W. and Abdullah. A., (2015), Mode of Islamic Bank Financing: Does Effectiveness of Shariah Supervisory Board Matter?, *.Aust. J. Basic & Appl. Sci*., 9(37): 458

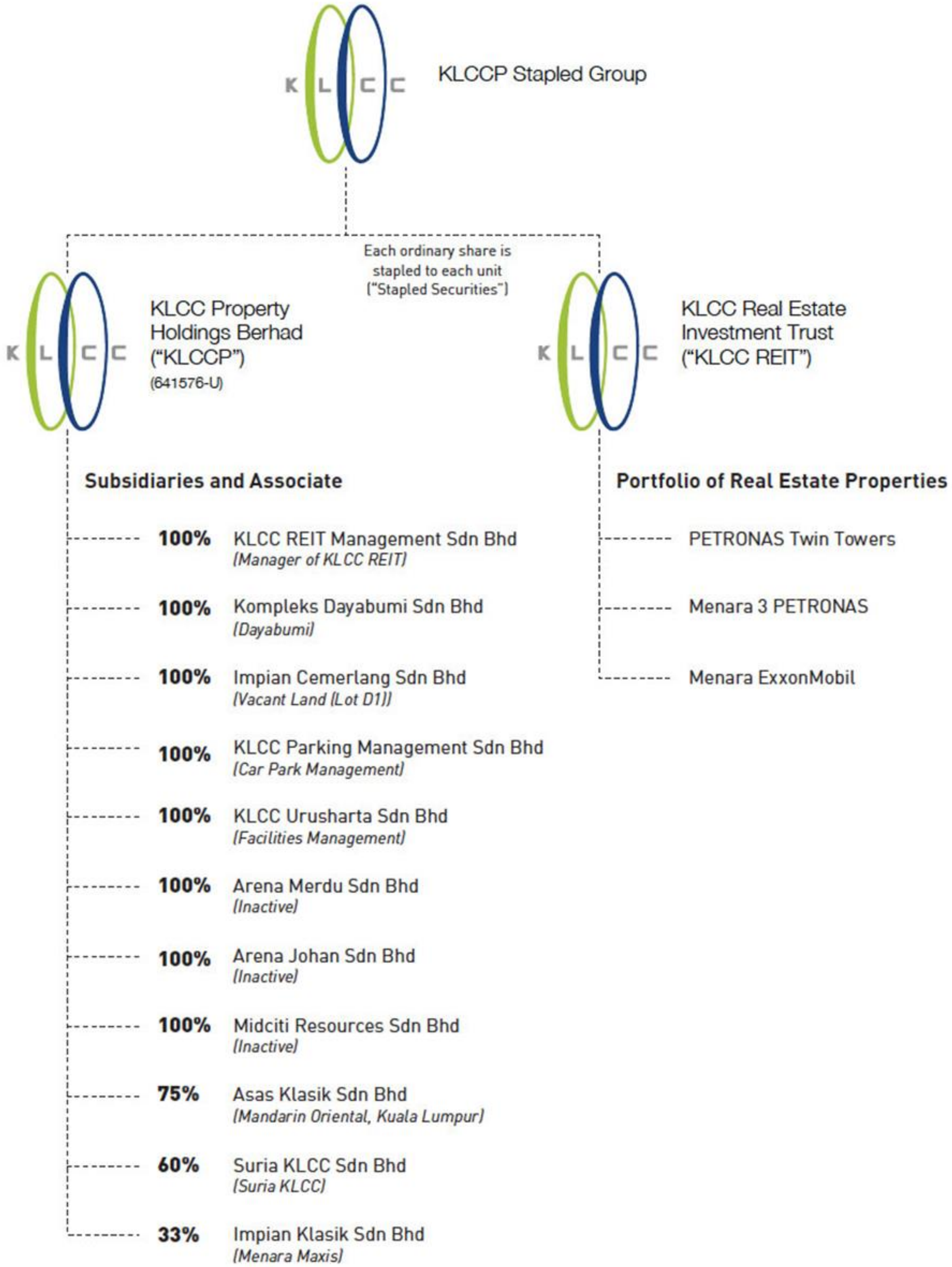
Waemustafa. W. and Sukri.S., (2016), Systematic and Unsystematic Risk Determinants of Liquidity Risk Between Islamic and Conventional Banks, *International Journal of Economics and Financial Issues*, 2016, 6(4), 1321-1327.

Wahal, S., and McConnell, J.J. (2000). Do institutional investors exacerbate managerial myopia? *Journal of Corporate Finance*, 6: 307–329

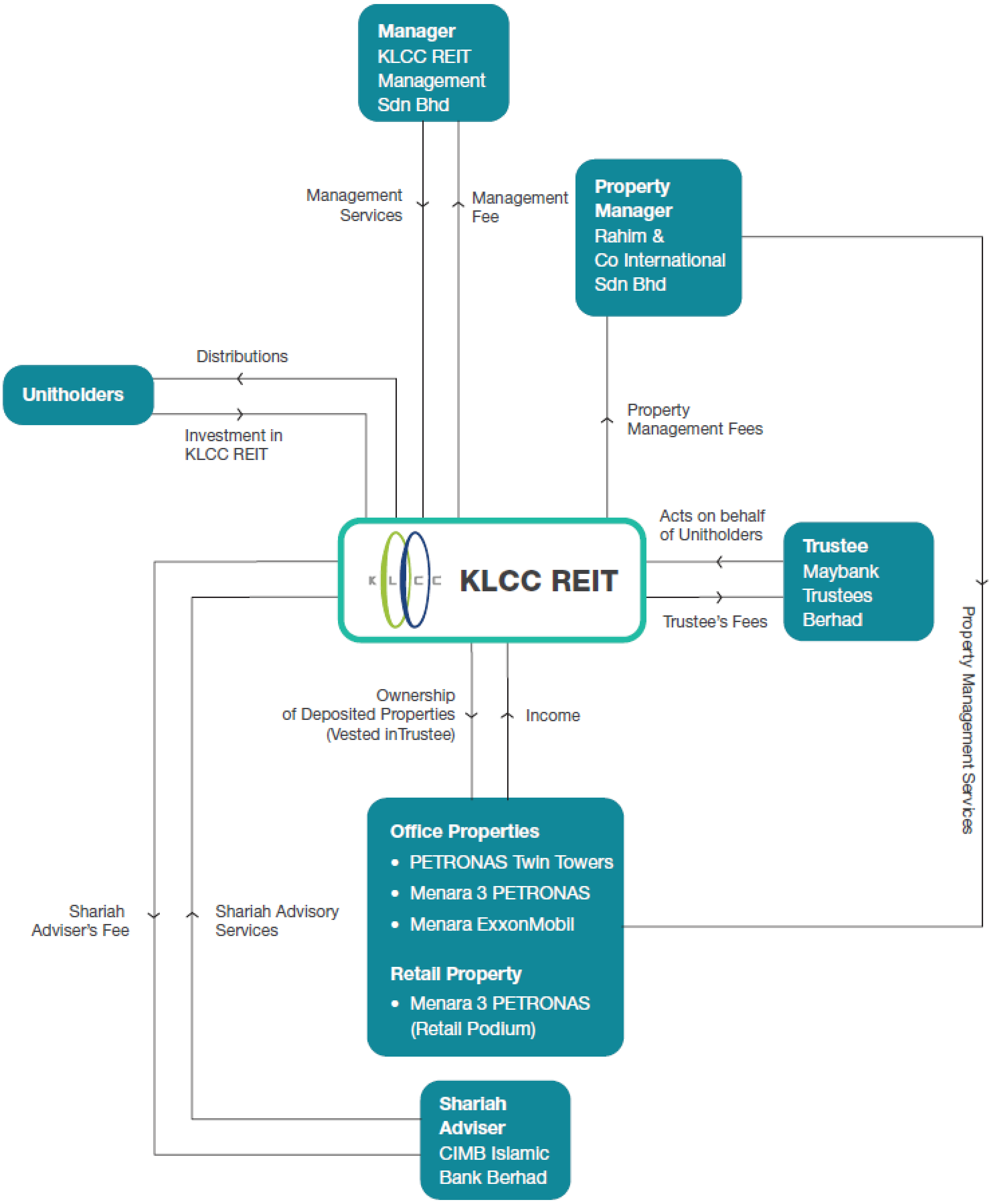
Walker, D. (2009). A review of corporate governance in UK banks and other financial industry entities: Final recommendations. Retrieved 20 May 2010. From http://www.hmtreasury.gov.uk/d/walker_review_261109.pdf.

Appendix 1

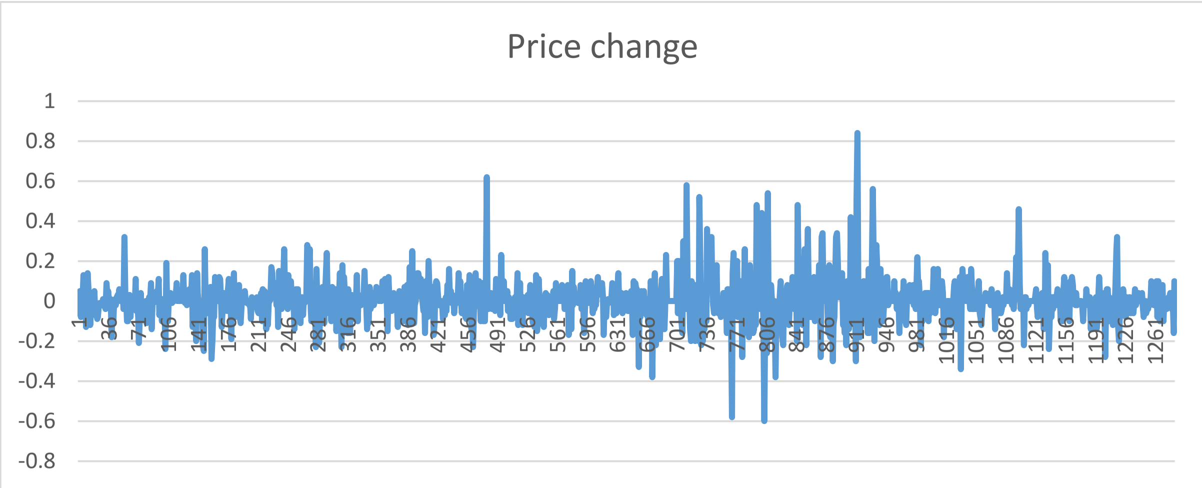
KLCCP STAPLED GROUP STRUCTURE



KLCC REIT STRUCTURE



Appendix 3



Price change
1
0.8
0.6
0.4
0.2
0
-0.2
-0.4
-0.6
-0.8
1
36
71
106
141
176
211
246
281
316
351
386
421
456
491
526
561
596
631
666
701
736
771
806
841
876
911
946
981
1016
1051
1086
1121
1156
1191
1226
1261

KLCC REIT CORPORATE GOVERNANCE STRUCTURE

	2011	2012	2013	2014	2015
Nationality Foreign	-	-	-	-	-
Local	/	/	/	/	/
Qualification	/	/	/	/	/
Gender diversity	/	/	/	/	/
Risk management committee	/	/	/	/	/
Audit committee	/	/	/	/	/
Remuneration committee	/	/	/	/	/
Size	/	/	/	/	/
Actual size	8	8	8	8	8
Meeting	/	/	/	/	/
Actual meeting	3	5	6	5	5
Experience	/	/	/	/	/

Appendix 5

SPSS ANALYSIS DATA

Descriptive Statistics

	Mean	Std. Deviation	N
ROA	.577000	.6513184	5
ROE	.583240	.8431720	5
ROI	.708940	.0756325	5
LIQUID	38.063820	22.5002048	5
LEVERAGE	.1616	.21851	5
GDP	5.4400	.48785	5

Correlations

		ROA	ROE	ROI	LIQUID	LEVERAGE	GDP
Pearson Correlation	ROA	1.000	.827	.445	-.854	.762	-.894
	ROE	.827	1.000	-.090	-.941	.280	-.882
	ROI	.445	-.090	1.000	-.120	.892	-.206
	LIQUID	-.854	-.941	-.120	1.000	-.387	.797
	LEVERAGE	.762	.280	.892	-.387	1.000	-.574
	GDP	-.894	-.882	-.206	.797	-.574	1.000
Sig. (1-tailed)	ROA	.	.042	.226	.033	.067	.020
	ROE	.042	.	.443	.009	.324	.024
	ROI	.226	.443	.	.424	.021	.370
	LIQUID	.033	.009	.424	.	.260	.053
	LEVERAGE	.067	.324	.021	.260	.	.156
	GDP	.020	.024	.370	.053	.156	.
N	ROA	5	5	5	5	5	5
	ROE	5	5	5	5	5	5

	ROI	5	5	5	5	5	5
	LIQUID	5	5	5	5	5	5
	LEVERAGE	5	5	5	5	5	5
	GDP	5	5	5	5	5	5

Variables Entered/Removed[a]

Model	Variables Entered	Variables Removed	Method
1	GDP	.	Stepwise (Criteria: Probability-of-F-to-enter <= .050, Probability-of-F-to-remove >= .100).

a. Dependent Variable: ROA

Model Summary[b]

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.894[a]	.800	.733	.3366198	2.657

a. Predictors: (Constant), GDP

b. Dependent Variable: ROA

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1.357	1	1.357	11.975	.041[b]
	Residual	.340	3	.113		
	Total	1.697	4			

a. Dependent Variable: ROA

b. Predictors: (Constant), GDP

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Collinearity Statistics	
		B	Std. Error	Beta			Tolerance	VIF
1	(Constant)	7.072	1.883		3.756	.033		
	GDP	-1.194	.345	-.894	-3.460	.041	1.000	1.000

a. Dependent Variable: ROA

Excluded Variables[a]

Model		Beta In	t	Sig.	Partial Correlation	Collinearity Statistics		
						Tolerance	VIF	Minimum Tolerance
1	ROE	.173[b]	.261	.818	.182	.221	4.516	.221
	ROI	.273[b]	1.051	.404	.596	.958	1.044	.958
	LIQUID	-.386[b]	-.866	.478	-.522	.365	2.736	.365
	LEVERAGE	.371[b]	1.303	.322	.678	.670	1.492	.670