Risk and performance of ltkm berhad

Jafree, Anis Nashuha

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ANIS NASHUHA BT JAFREE

Universiti Utara Malaysia

Abstract

The purpose of this study sought to examine the overall performance of LTKM Berhad with specific risk factors and macroeconomic factor on profitability performance. The data obtained from annual report of LTKM Berhad starting from 2011-2015. The measurement of liquidity ratio and operating ratio used to see the overall performance of LTKM Berhad in 5 years which allegedly beyond benchmark. To see the relationship of risks factors to the profitability, this paper is utilizing liquidity (current ratio), GDP and operating ratio. Data was analyzed by utilizing regression and bivariate correlation. The regression analysis and bivariate correlation shows only one factor of profitability is significant to operating ratio which is ROA with the highest impact to the profitability .

Keywords: Liquidity Risk, Operational Risk, Counterparty Risk, Leverage Ratio and Return On Assets .

1.0 INTRODUCTION

i. Sector background

LTKM Berhad is one of the leading chicken egg producers in Malaysia and is listed in the Main Market of Bursa Malaysia since 2000. LTKM Berhad are the pioneer in producing Omega-3 enriched eggs in collaboration with Malaysia Agriculture Research and Development Institute (MARDITECH) in the country. Whilst LTKM Group's core business is in the production and sales of eggs, it has embarked on property development.

The company operates a sophisticated, highly automated layer farm in Melaka spanning over 450 acres. A total of over 2 million chickens accommodate advanced multi-deck housing systems that produce over one million chicken eggs per day.

ii. Products and services

LTKM Berhad is a Malaysia-based investment holding company and engaged in the provision of management services. The Company operates in four business segments: production and sale of poultry and related products, which includes the production and sales of chicken eggs, chickens and organic fertilizers; extraction and sale of sand, which include the mining and trading of sand; investment holding, which include investment activities in quoted and unquoted securities held by the Group on a long term basis, and manufacture and sale of processed glass. The Company's subsidiaries are engaged in production and sale of chicken eggs and chickens, manufacturing and sale of organic fertilizers, extraction and sale of sand and manufacturing and sale of processed glass .

iii. Risk management committee

The Group's Risk Management function sets out its underlying approach in managing risks while pursuing its business objectives. Risk management is firmly embedded in the Group's management system through its business units and departmental functions. There is an ongoing process to identify, analyse, evaluate, prioritise and mitigate risks . This committee also responsible to review the business risk and monitor the exposure to credit risk .

2.0 LITERATURE REVIEW

Liquidity risk is the risk that a company may be unable to meet short term debt obligations. This usually occurs due to the inability to convert an asset to cash without a loss of capital or income in the process. The management of liquidity risk is merely unreliable without proper knowledge of risk formation in Islamic mode of financing (Waemustafa, 2016). Managing risk effectively is essential for any organization so that the business will continue to grow and provide sustainable profits. Liquidity risk occurs when the bank had to sell its assets at very low prices to pay off debt and unable to convert an asset into cash without giving up capital (Waemustafa, W., 2016).

Therefore, liquidity risk can be considered as a financial risk that arises when a firm either does not have enough funds to allow it to meet its due obligations or can get such funds only at an excessive cost (Vento *et al.*, 2009). Banks will face liquidity risk if they do not have enough cash when depositors want to redeem their deposits. In this case, banks have to balance assets and liabilities. Assets and liabilities should be monitored and managed more efficiently, otherwise they will face the problem of insolvency (Iqbal, 2012). The goals of liquidity risk management are to ensure that obligations are met in full and on time, and that the bank continues to fulfill its lending commitments, medium-term investments and strategic goals (Parashar and Venkatesh, 2010). Banking risk management generally is about how banks deal with risk and the pay-off associated with it, and the strategies used in dealing with them; it is also about the identification and classification of banking risk, and methods and procedures used to measure, monitor, mitigate and control risks (Tektas et al., 2005).

Interest-free financial institutions demolished the traditional relationship between the lender and borrower which was based on interest when they approve financial facility to their customers. Islamic banks operate on the basis of profit and loss sharing where the principle and agent relationship is on the basis of capital provider and entrepreneur. (Waemustafa, W., 2016). An inefficient liquidity management could increase the cost of borrowing and have negative effects on earnings of banks (Ivanov, 2010). The effective management of liquidity requires medium-term planning and immediate reactions to the fast changes taking place in the present business environment. Liquidity management is a discipline that seeks proper policies for managing short-term assets and liabilities and practical mechanisms for enhancing the benefits from managing liquid capital (Saini and Sharma, 2009).

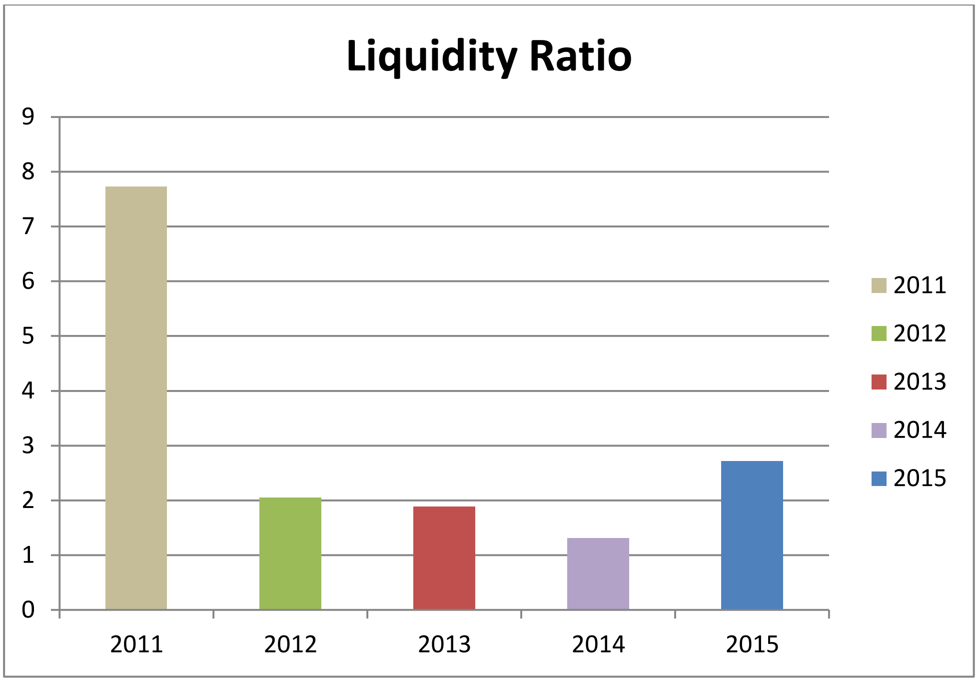
3.0 DESCRIPTIVE FINDINGS

Liquidity Ratio

Year	2011 (RM'000)	2012 (RM'000)	2013 (RM'000)	2014 (RM'000)	2015 (RM'000)
Current Asset	183,341,925	52,010,783	59,089,052	64,069,372	76,325,064
Inventory	10,815,078	11,603,549	12,753,072	17,500,317	11,743,836
Current Liabilities	22,339,662	19,772,346	24,638,111	35,482,099	23,773,658
Liquidity Ratio	**7.722894241**	**2.043623655**	**1.880662848**	**1.312466182**	**2.716503619**

Table 1: Liquidity Ratio

Bar Graph 1. Descriptive Results



According to investinganswers.com, liquidity risk is the risk that a company may be unable to meet short term financial demands. This usually occurs due to the inability to convert a security or hard asset to cash without a loss of capital and income in the process. Liquidity risk generally arises when a business or individual with immediate cash needs, holds a valuable asset that it can not trade or sell at market value due to a lack of buyers, or due to an inefficient market where it is difficult to bring buyers and sellers together.

In the year 2011, the liquidity ratio for LTKM Berhad is 7.72. While in the year 2012, the liquidity ratio of LTKM Berhad is 2.04. By comparing the liquidity ratio for both year, we can see that in the year 2011 has a more favourable liquidity ratio than in the year 2012. In the year 2013, liquidity ratio of LTKM Berhad has decreasing from 2.04 to 1.88 and continuing to decrease to 1.31 in year 2014 . But in the year 2015, the liquidity ratio for LTKM Berhad risen sharply from 1.31 to 2.72 . The most favourable liquidiity ratio is in the year 2011 where LTKM Berhad has the highest liquidity ratio compared to other years within 2011 until 2015 .

It can be seen that the current assets of LTKM Berhad in the year 2011 is the highest value compared to another year, this factor may cause to the liquidity ratio to increase. In the year 2014, the liquidity ratio continued to decrease where the current asset in that year only amounted RM 64,069,372,000 . Besides that, the current liabilities for year 2014 is the highest compared to other years . It can be seen that the current liabilities of LTKM Berhad in the year 2014 increase from RM 24,638,111,000 to RM 35,482,099,000.

The ability of LTKM Berhad to repay its current liabilities increases when the highest the amount of current assets, the more it can cover the current liabilities incurred by LTKM Berhad.

Operational Risk

Year	**2011 (RM'000)**	**2012 (RM'000)**	**2013 (RM'000)**	**2014 (RM'000)**	**2015 (RM'000)**
Operating Expenses	1,152,154	1,271,085	1,072,755	1,097,379	1,188,819
Revenue	157,162,620	12,516,000	2,384,000	9,384,000	15,384,000
Operating Ratio	**0.007330967**	**0.101556807**	**0.449981124**	**0.116941496**	**0.077276326**

Table 2: Operational Risk

Bar Graph 2. Descriptive Results

According to investopedia.com, operational risk summarizes the risks a company undertakes when it attempts to operate within a given field or industry. Operational risk is the risk not inherent in financial, systematic or market-wide risk. It is the risk remaining after determining financing and systematic risk, and includes risks resulting from breakdowns in internal procedures, people and systems.

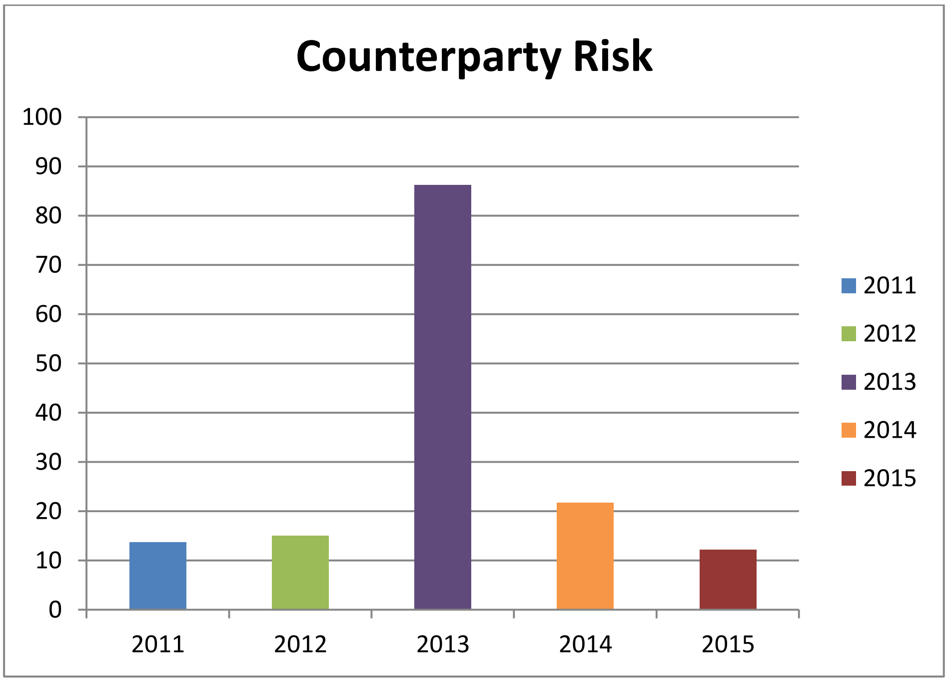
From the graph and table above, we can see that in the year 2011, the operating ratio for LTKM Berhad is 0.01 . While in the year 2012, the operating ratio of LTKM Berhad is 0.10 . By comparing the operating ratio for both year, we can see that in the year 2011 has a more favourable operating ratio than in the year 2012 because the smaller the ratio, the greater the organization's ability to generate profit. In the year 2013, operating ratio of LTKM Berhad has rising from 0.10 to 0.45 . This shows that LTKM Berhad's ability to generate profit for that year decline in year 2013. But in year 2014, the operation ratio decrease to 0.12 and this decreasing is indicate that LTKM Berhad more efficient in operating compared to the year before. In the year 2015, the operational ratio for LTKM Berhad continuing to decrease to 0.08 . The most favourable operating ratio is in the year 2011 where LTKM Berhad has the lowest operating ratio compared to other years within 2011 until 2015 . This shows that LTKM Berhad have the greatest ability to generate profit in year 2011.

Counterparty Risk

Year	2011 (RM'000)	2012 (RM'000)	2013 (RM'000)	2014 (RM'000)	2015 (RM'000)
Account Receivable	5,971,908	524,316	570,876	566,133	522,790
Annual Credit Sales/ 360	436,563	34,767	6,622	26,067	42,735
Counterparty Risk	13.67937796	15.08099712	86.20610738	21.71865729	12.23329823

Table 3: Counterparty Risk

Bar Graph 3. Descriptive Results



According to investopidia.com, counterparty risk is the risk to each party of a contract that the counterparty will not live up to its contractual obligations. Counterparty risk is a risk to both parties and should be considered when evaluating a contract. In most financial contracts, counterparty risk is also known as default risk. In an efficient market, higher levels of credit risk will be associated with higher borrowing costs.

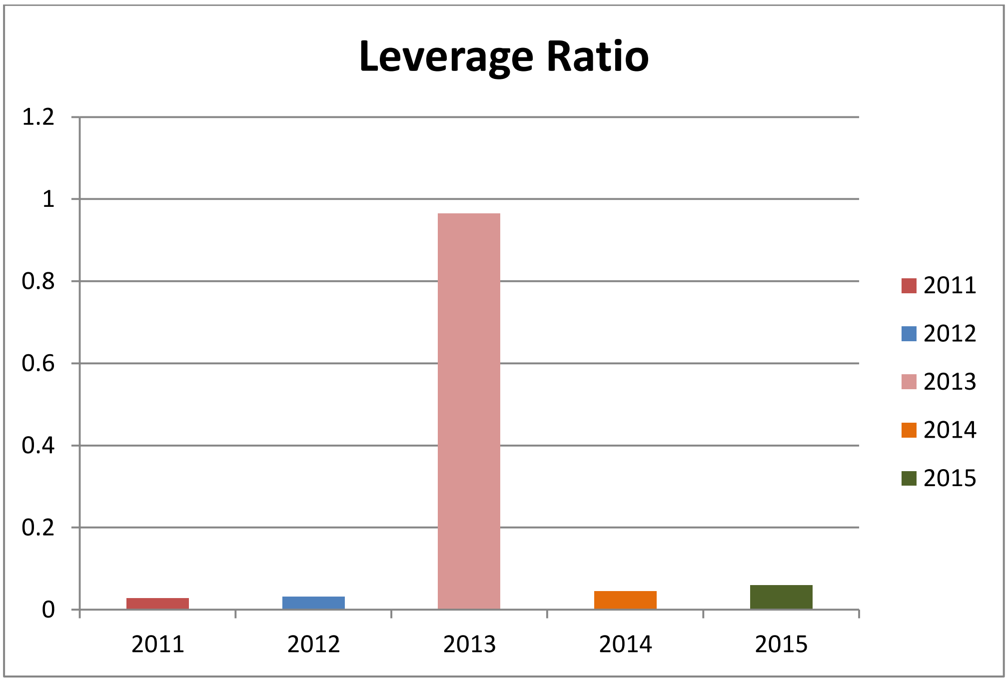
In the year 2011 , LTKM Berhad has a counterparty risk ratio of 13.68 and increase to 15.08 in the year 2012 . While in the year 2013, a counterparty risk ratio of LTKM Berhad has risen sharply from 15.08 to 86.21 . It is shows that in the year 2013, LTKM Berhad have high default risk . However, in the year 2014 and 2015 , LTKM Berhad has a counterparty risk ratio of 21.72 and 12.23 respectively . It means that, the most favorable counterparty risk ratio is in the year 2015 where the ratio is lowest compared to other years . According to the graph above, LTKM Berhad counterparty risk ratios are increasing from year 2011 until 2013 and are decreased in gradual way starting in the year 2013 until 2015 . It is a good things for the company to have more total annual credit sales . Based on the table above, the total annual credit sales for year 2013 is the lowest which is amount RM6,622,000 and in this year LTKM Berhad has the higher risk . This may be arises due to borrowers are unable to pay due willingly or unwillingly.

Leverage Ratio

Year	2011 (RM'000)	2012 (RM'000)	2013 (RM'000)	2014 (RM'000)	2015 (RM'000)
Total Debts	2,579,817	2,632,158	78,095,361	3,729,211	5,473,911
Total Assets	95,172,006	82,762,074	80,998,375	83,440,300	91,631,446
Debt Ratio (Times)	**0.027106889**	**0.031803915**	**0.964159602**	**0.044693164**	**0.059738346**

Table 4: Leverage Ratio

Bar Graph 4. Descriptive Results



Debt ratio is a solvency ratio that measures a firm's total liabilities as a percentage of its total assets. In a sense, the debt ratio shows a company's ability to pay off its liabilities with its assets. In other words, this shows how many assets the company must sell in order to pay off all of its liabilities. This ratio measures the financial leverage of a company. Companies with higher levels of liabilities compared with assets are considered highly leveraged and more risky for lenders. This helps investors and creditors analysis the overall debt burden on the company as well as the firm's ability to pay off the debt in future, uncertain economic times.

In the year 2011 , LTKM Berhad has a debt ratio of 0.027 or 2.7% and increase to 0.03 or 3% in the year 2012 . While in the year 2013, a debt ratio of LTKM Berhad has risen sharply from 0.03 or 3% to 0.96 or 96% . It is shows that in the year 2013, LTKM Berhad have high debt . However, in the year 2014 and 2015 , LTKM Berhad has a debt ratio of 0.04 or 4% and 0.06 or 6% respectively . It means that, the most favorable debt ratio is in the year 2011 where the ratio is lowest compared to other years . According to the graph above, LTKM Berhad debt ratios are increasing from year 2011 until 2013 and are decreased in gradual way starting in the year 2013 until 2015 . It is a good things for the company to have more total assets and low total debts . Based on the table above, the total assets for year 2011 is the highest which is amount RM 95,172,006,000 and at the same year the total debts only RM 2,579,817,000 which is the lowest total debts . This prove that LTKM Berhad has the ability to pay of its debt with its assets .

Therefore, in order to achieve or maintain a favorable debt ratio in the future, LTKM Berhad must lower its total debts and at the same time increase its total assets.

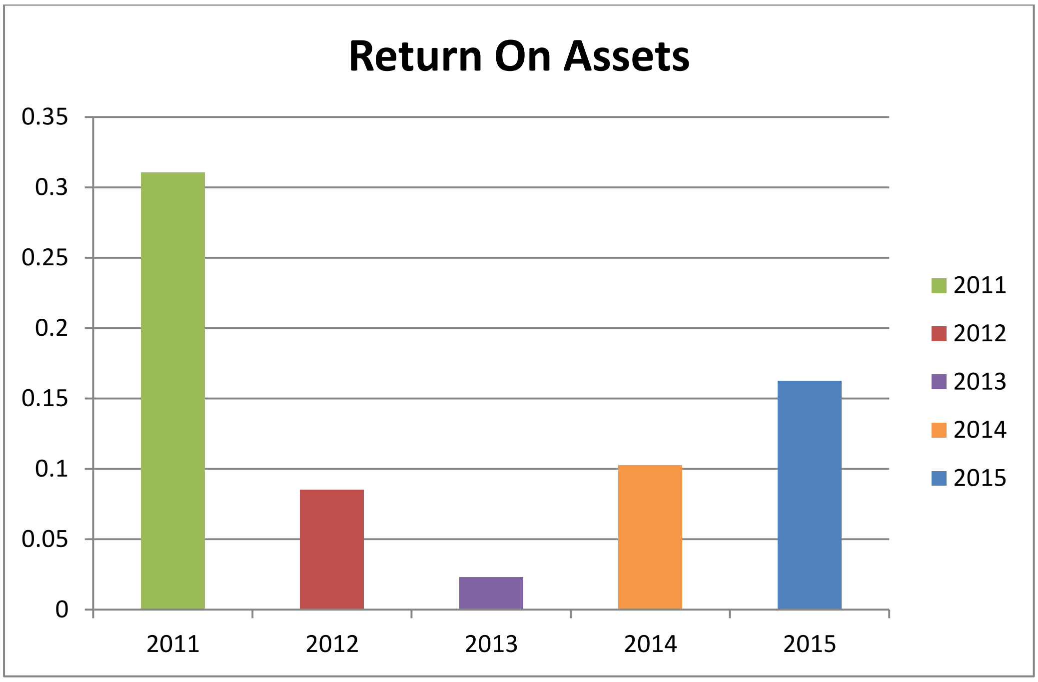
4.0 Company Performance

Return on asset

Year	2011 (RM'000)	2012 (RM'000)	2013 (RM'000)	2014 (RM'000)	2015 (RM'000)
Net profit after tax	29,555,949	7,027,612	1,868,586	8,554,608	14,886,515
Total Assets	95,172,006	82,762,074	80,998,375	83,440,300	91,631,446
Return On Asset	**0.310552969**	**0.084913435**	**0.023069426**	**0.102523697**	**0.162460767**

Table 5 : Return On Asset

Bar Graph 5. Descriptive Results



Return on assets is used to illustrates how the company or management use the company's total assets to gain or generate profit . This ratio indicates how profitable a company is relative to its total asstes . ROA figure also useful to compare the company's performance from one year to one year . The higher the return, the more efficient management is in utilizing its asset base.

In the year 2011, the ROA ratio for LTKM Berhad is 0.31. While in the year 2012, the ROA ratio of LTKM Berhad is 0.08 . By comparing the current ratio for both year, we can see that in the year 2011 has a more favourable ROA ratio than in the year 2012 . In the year 2013, ROA ratio of LTKM Berhad has decreasing from 0.08 to 0.02. But in the year 2014, the ROA ratio for LTKM Berhad risen sharply from 0.02 to 0.10 and continuing to increase in year 2015 . The most favourable liquidiity ratio is in the year 2011 where LTKM Berhad has the highest liquidity ratio compared to other years within 2011 until 2015 .

There is increase in ROA ratio due to the increase in total assets . It can be seen that the total assets and net profit after tax of LTKM Berhad in the year 2011 has the highest value directly cause the ROA ratio for year 2011 to increase . In the year 2013, the ROA ratio continued to decrease and lowest because the total asset and net profit after tax in the year 2013 only amounted RM 80,998,375,000 and only RM 1,868,586,000 for net profit after tax. It can be seen that the net profit after tax and total assets of LTKM Berhad start to rising from year 2013 to 2015 .

The ability of LTKM Berhad to manage and use the company's total assets to gain or generate profit increases when the highest the amount of total assets. The more the total assets and net profit after tax, the more profit company can gain . Based on the graph above, it shows that LTKM Berhad's ROA start to increase from year 2013 to year 2015 .

Table Result 6. Enter Regression Analysis for LTKM Berhad Specific Risk Determinants to Profitability Profitability

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.987[a]	.973	.893	.0356526

a. Predictors: (Constant), Counterparty Risk, Liquidity Ratio, Operational Risk

Table Result 7. Anova Regression Analysis for LTKM Berhad Specific Risk Determinants to Profitability Profitability

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.046	3	.015	12.162	.207[b]
	Residual	.001	1	.001		
	Total	.048	4			

a. Dependent Variable: ROA

b. Predictors: (Constant), Counterparty Risk, Liquidity Ratio, Operational Risk

4.0 DISCUSSION AND RECOMMENDATION

4.1 Discussion

During the consecutive year 2011-2015, overall performance of LTKM Berhad was showing favorable in the performance result for all measurements of liquidity and operation in annual basis. The effective conversion asset into cash to repay the debt without any issue and the efficient operation without incurring any additional expenses are reflected to the overall performance of LTKM Berhad. One of profitability measurement has a significant relationship which is ROA to operate variable. With this high impact of operate to profitability and one of profitability measurement is significant relationship to operate.

4.2 Recommendation for Improvement

4.2.1 Increase the Gross Margin

There are several ways that can be done by companies to improve gross margin ratio of which is to build the brand. Thus, customers will be more confident to pay more for the product, even when the cost of the acquisition remain the same, can be a very successful approach . Businesses need to generate income and most businesses depend on sales. Better internal communications within the sales department is a good start and can be highly beneficial, as it allows for a more efficient use of time and resources. When employees and leaders across different levels and departments within the organization communicate effectively, many potential problems may be averted.

4.2.2 Increase the Operating Margin

Organizations that want to improve the operating margin should wisely manage the company's expenses either spend less money by reducing operating expenses, or bring in more money by increasing sales. Companies can reduce the loan and cut unnecessary expenses. Thus, operating margin of the company will increase. In addition, LTKM Berhad can increase sales because more sales, more revenue to the organization .

4.2.3 Increase the Profit Margin

The profits of a company can be assessed using the profit margin. Profit margin is very useful for companies to evaluate and compare the profitability of the company with competitors in their industry. The higher the profit margin of a company means that it is more profitable than competitors. Therefore, LTKM Berhad need to increase profit margins in order to remain competitive in the industry.

4.2.4 Increase the Return On Assets

The annual income of a company coming from business assets that are used throughout the year. As ROI, ROA is a tool to assess the company's ability to use its assets to generate profits. The higher a company's return on assets, the more money it can make. To improve the return on assets, LTKM Berhad should increase their net income or decrease the amount of assets. LTKM Berhad need to raise product prices without dropping demand and increased sales volume. With this, the return on assets LTKM Berhad will increase.

5.0 CONCLUSION

In conclusion, it is clear that liquidity risk, operational risk , and counterparty risk is faced to all the companies especially in the study of food and beverage industry. LTKM Berhad could handle the liquidity risk and operational risk effectively and efficiently with the ratio is beyond and below the standard of benchmark. The liquidity and operational performance annually shows this company is not having problem to settle the obligation and operates efficiently that could generate more profit. In addition, to maintain the performance in 2015 onwards, from the findings, one of variable is significant (ROA) as a profitability variable to the operation with the highest impact compared to all of variables. Therefore, this company should concern more to the gross margin, operating margin , profit margin and return on assets in generating more profit. Also, to maintain and improve continuous profitability of this company, the implementation of liquidity management and inventory control with following the trend or cycle of market should put into consideration as a part of profitability contribution .

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