An Analysis of the Internal and External Factors that Affect United Continental Holdings

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Abstract

The purpose of this study is to examine the overall performance of United Airlines as airlines industry in United States. Overall performance is measured from 2014 to 2018 as the measurement of credit risk, operating risk, liquidity risk, and market risk which involves economic situation to look at the company's success in the airline industry. Return on Assets (ROA) measures the performance of the company. The results suggest that the equations used in this analysis have different effects on the company's efficiency. The findings throughout this study show that there is positive relationship between corporate governance and ROA. The ROA has a negative relationship with four variables, namely liquidity risk, operating risk, credit risk and market risk.

Keywords: *Return on Asset, profitability, credit risk, liquidity risk and market risk.*

1.0 Introduction

1.1 Background of Company

United Airlines, an international American airline that serves North America, Asia, Latin America, the Caribbean, and Europe. The parent company of the airline company, United Continental Holdings, is headquartered in Chicago. United Airlines stretches back to 1929 when William E. Boeing (1881–1956), Frederick B. Rentschler (1887–1956) and his associates founded the United Aircraft Transport Corporation, an aircraft manufacturing, and air transport subsidiary. In 1930, four mail carriers had been acquired which is Boeing Air Transport (formed in 1927), Pacific Air Transport (1926), Varney Air Lines (1926), and National Air Transport (1925). United Airlines, Inc. was founded in Chicago in 1931 as a parent company providing the four operating divisions. In 1934, under U.S. Congressional pressure, aircraft multinationals were forced to dissipate, dividing aircraft production from air transport. United Airlines, Inc. has become an independent operating company, completely unifying all transport divisions.

By 1930, the airline would have a network of routes by New York City to San Francisco and Seattle together with a range of north-south routes in the west, and that year, the first stewardesses of the company were trained and put into service on the Chicago – San Francisco flights. New York's transcontinental flights followed. U.S. routes and services expanded after World War II. In 1961, after its consolidation with Capital Airlines, United has become the largest airline in the World (in terms of number of passengers), exceeding only the Aeroflot of the Soviet Union globally; United maintained the first rank for a few decades. Due to growing financial problems in a burdened airline industry, United suffered a duration of massive restructuring throughout the late 21st century, that included a reduction in flight routes, a reduction in seating capacity, and layoffs for employees and job losses. United launched its low-fare airline Ted Airlines in 2004, which is terminated in 2009, and purchased a shareholding in Aloha Airlines in 2007. United partnered with Continental Airlines the next year to widen its flight options and combined with Continental in 2010.

1.2 Issues in United Airlines

Crisis on UAL started when an airline police officer at Chicago's O'Hare International Airport pulled a man out of a United Airlines aircraft. In a clip posted to Facebook by Passenger Audra Bridges, the officers are seen forcefully catching, and then drag, the passenger down the aisle of the aircraft bound for Louisville. United said that four passengers had been chosen by airline representatives to exit the aircraft at randomly based on ticket class, frequently flying status and check-in time and that one man had refuse to leave his seat. Officials personally requested the assistance of the authorities, who still forcefully removed the person. Bridges has said that the seats had been cleared for airline staff on standby who also probably needed the airline to move to Louisville. Later, the Chicago Aviation Department clearly stated that one of the first officers had not yet complied with the procedure and might have been placed on leave before a review had been carried out. In this situation, United staff have been at blame due to a massive lack of corporate governance. CEO Oscar Muñoz and his team members were accountable for the enormous gap between the image of the product and the organizational culture of the company. Companies have completely ignored to engage, educate and encourage staff in an appropriate manner.

Some of its competitors still slowdown behind the company's operational and financial performance, and efficiency does not lead to a high level of customer service. Although Munoz had already carried action to improve the United Culture, it might not be enough, as said by Charles Leocha, president of the Travelers United Airline Passenger Advocacy Group. Leocha is going to talk to United staff over most of the years and has noticed that, despite recent improvements, the historically close relationship between the airline's management and low-level staff exists. The resentment came to light early this month, once the company slightly replaced quarterly performance-based incentives with a lottery which would give a smaller number of larger rewards–and tried to portray itself as a positive move. During a weekend of staff ' indignation and unpleasant media, the company stopped the change to "realise the proper way forward." The company's approach to its staff has shown that it might be more empathetic to Munoz's issues, however the truth that it decided to change its compensation system, when trying to persuade its staff that the improvements were great for them, indicates that the more work is needed. In fact, a United Customer recorded an argument one of the airline staff in May, which seemed to include an overweight bag that the customer decided to check. Once the customer started recording the argument the ticket agent took her phone and started recording the customer and decided to suspend the ticket.

1.3 Research Objective

1.3.1 To identify internal factors affecting the performance of the company

1.3.2 To identify external factors affecting the performance of the company

1.3.3 To identify the internal and external factors that influence corporate governance

1.3.4 To identify significant impact between credit risk, liquidity, operating risk, market risk and company performance.

1.3.5 To identify the effect of a macroeconomic variable on company performance

1.4 Research Questions

1.4.1 How internal factors affect the company performance?

1.4.2 How external factors affect the corporate governance?

1.4.3 How internal factors and external factors affect the company performance?

1.4.4 Is there any significant effect between credit risk, liquidity, operational risk, market risk and company performance?

1.4.5 Is there any relationship between corporate governance towards company performance?

2.0 Literature Review

According to Miles, Snow, Meyer, & Jr. (1978), an attempt has been made to mitigate the company's risks in order to make a profit. There are several risks which a company may head, like financial risk, liquidity risk, market risk and operational risk. It consists of volatility, demand and credit risk. Based on United Airlines ' annual report from 2014 to 2018, liquidity risk is also one of the key factors to address in order to avoid this group's deterioration. Since liquidity risk must be understood by every company that operates a business and an effective liquidity risk management system must be established (Waemustafa & Sukri, 2016).

Operational risk also has a significant effect on performance and risks of the company. Top management is vitally important for a business organization to improve performance, as well as to give trust to its customers and increase its credibility. Hence it is important to identify all risks to mitigate and prevent possible exposures from happening. In addition, several studies have found which the financial ratio is important to have been reviewed in order to identify the quality, indicating that the performance assessment would be stricter when the financial ratio is considered (C.- M. Feng, 2000).

Some further study to determine the foreign exchange rate has been one of the important factors for the company's performance. A lower rate of exchange indicates that almost all businesses are likely to be exempted from dangerous zone, that would not effectively lead to the end of the company (Meeks, 1991). Many companies particularly in the airline industry, must be cautious about currency exchange and take advantage of the ability to make profit from global trade. Nonetheless, there's some risk due to fluctuating currency market movements.

Other studies have shown whether there is a significant relationship between inflation and company profits. The study shows that there's only negative insignificance in relation to ROA as profits. This indicates how it maintains an increase in the cost of goods and services with little profit that could be gained by a company. One study found that somehow big companies will also stand to benefit from inflation rates and if it is slightly lower only because of the costs they use for product materials, especially at a time for industries (Feldstein, 1997). This study shows which low inflation is likely to bring benefits to companies when it comes to lower costs for materials.

Another study found how a company will decide sustainable growth and create a company that needs to be concerned with compliance with Shariah. When the company develops, that use equity financing depending on Musharakah and Mudarabah, it'll become an aggregate measure for those stakeholders of the company (Waemustafa, 2013). In order to increase performance, a company will try to understand not to use the debt to fund the company, even though there is a way to increase shareholder wealth. But an equity-based financing company is not likely to face more credit risk due to progressive actions that will not use liabilities to fund the company. Shortly, a company should be able to remain profitable and productivity need to be more concerned about how to fund, for example, a Shariah-compliant company would not have many credit risk problems because the company was an all-equity company.

2.1 Corporate Governance

According to Ching et al (2006), corporate governance could be described as a group of processes and structures of monitoring and managing a company. It's also a set of principles governing relations between management, shareholders, and stakeholders. Corporations are becoming a dominant and effective organization. They also exceeded each corner of the world in different sizes, capacities and factors that influence. Governance has had an impact on economies and different aspects of the social climate. Shareholders were seen to lose trust, and value has been extremely affected. In fact, there has been more deterritorialization with the growth of globalization as well as less government involvement, resulting in a greater need to have accountability (Crane and Matten, 2007). Corporate governance has thus been an important factor in the management of organizations throughout the global and expansive environment.

3.0 Research Methodology

3.1 Sampling Technique

Among this research, the analysis of the collected data is based on the quantitative method. The data was taken from the company's annual financial reports for a period of 5 years from 2014 to 2018. In five years from 2014-2018, data is collected from the annual reports. Apart from that, the corporate governance index is to determine if the company has good corporate governance. For the corporate governance index the ratings are combined to create an index.

3.2 Statistical Technique

The data from annual report was used to conduct these researches. These researches consist of five years from year 2014 to 2018. Financial information from the statement of income has been used to analyse the financial report from the statement of income and the balance sheet of the company. Return on assets and return on equity will be measured using the data from the annual reports. Using the Excel worksheet, independent variable data have been used to calculate the data analysis. Once the data has been measured, the data would be moved to SPSS for the analysis to begin. SPSS has been developed at Standford University by Norman H. Nie, C. Hadlai (Tex) Hull and Dale H. Bent. The regression analysis includes descriptive statistics, correlation and coefficients the Enter Method. Enter method mean will choose the significant one among all the variables. Using this method, only the most significant variable in this research used to analysis. For descriptive statistics, the mean and standard deviations of a company for the preceding five years are shown. The relationship describes the relationship between the variables of either positive or negative relationships. For the macro-economic factors, data on the Gross Domestic Product (GDP), inflation, interest rate and exchange rate were collected for the preceding five years from 2014 to 2018.

3.3 Data Analysis

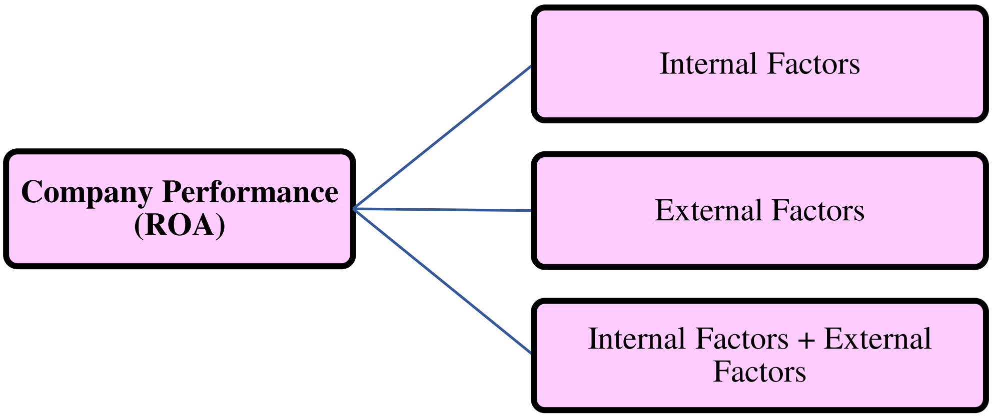


Figure 1: Research Framework

In the following table, the internal factors and external factors indicating the independent variables are defined:

Factors		Measurement
Internal Factors	Company Performance	ROA, ROE
	Liquidity Risk	Current Ratio, Quick Ratio
	Credit Risk	Average Collection Period, Debt-Income Ratio, Debt-Equity Ratio
	Operational Risk	Operating Ratio, Operating Margin
	Corporate Governance	Index Score
External Factors	Market Risk	GDP, Inflation Rate, Interest Rate, Exchange Rate, Beta

Table 1: Independent Variables

3.4 Analytical Framework

Multiple linear regression is a method of modelling the linear relationship between one dependent and one or more independent variables. It is one of the most widely used methods of statistics Regression analysis seems to be a very common method in use in banking and financial literature to describe the factors that influence of bank success (Ongore and Kusa, 2013; Sharifi and Akhter, 2016) for three different dependent variables based on a common five independent variables. The general form of the multiple linear regression equation is as follows:

$$\gamma = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \cdots + \beta_k X_k + \bar{e}$$

Where,

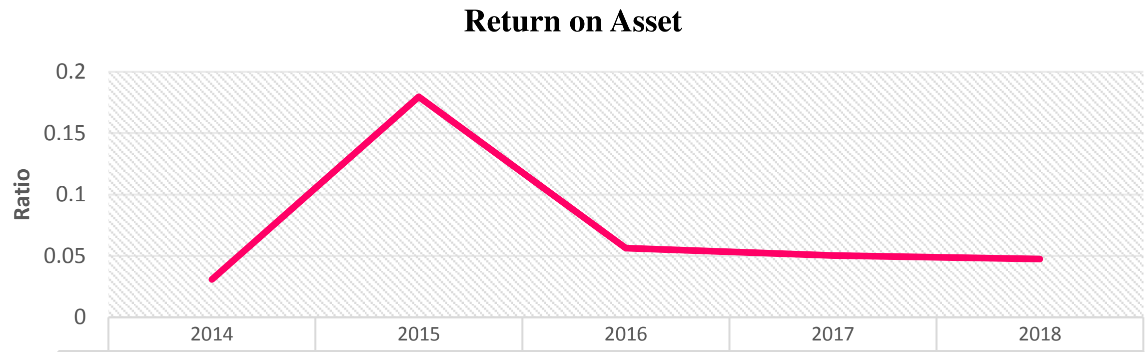
$\boldsymbol{\gamma = Dependent\ Variable}$
$\boldsymbol{X_i = i^{th}\ Independent\ Variable}$
$\boldsymbol{\beta_0, \beta_1, \beta_2, \beta_3, \ldots . \beta_x =}$ $\boldsymbol{the\ partial\ regression\ coefficients\ of\ respective\ independent\ variables}$

3.5 Empirical Results of Three Models

First Model	$CP_{ROA} = \beta_0 + \beta_1 ROE + \beta_2 \text{LiquidityRisk} + \beta_3 \text{CreditRisk} + \beta_4 \text{OperationalRisk} + \beta_5 CGI + \bar{e}$
Second Model	$CP_{ROA} = \beta_0 + \beta_1 GDP + \beta_2 Inflation + \beta_3 InterestRate + \beta_4 ExchangeRate + \bar{e}$
Third Model	$CP_{ROA} = \beta_0 + \beta_1 Internal + \beta_2 \text{External} + \bar{e}$

4.0 Analysis Findings

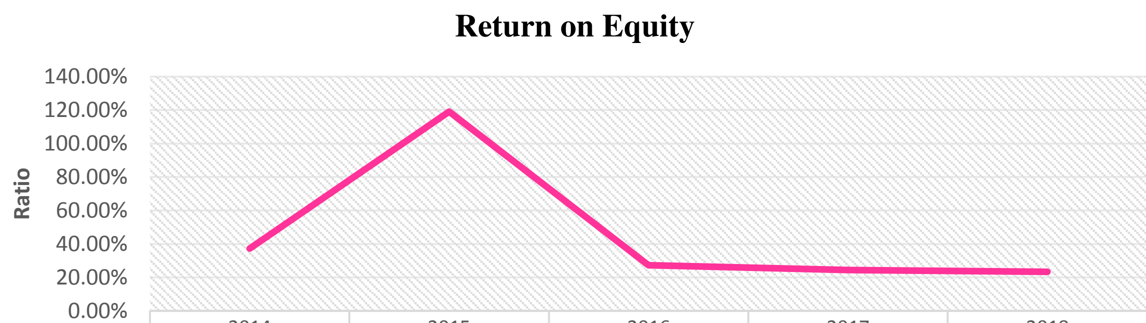
4.1 Profitability Ratio



	2014	2015	2016	2017	2018
ROA	0.0309	0.1796	0.0564	0.0503	0.0475

Figure 1: Return on Asset

Return on assets is sometimes referred to as return on investment. This refers to the amount of profit generated for each dollar earned in capital and management performance in resource utilization. United Airlines has the highest return on assets in 2015, which is 17.96 % and the lowest return on assets in 2014, which is 3.09 %. The higher the value the better as United Airlines is earning more money on less capital due to the quality of resource use.



	2014	2015	2016	2017	2018
ROE	37.16%	119.10%	27.31%	24.50%	23.34%

Figure 2: Return on Equity

According to the table above, ROE increased dramatically from 52.5 % (2014) to 119.10 % (2015) and then declined to 27.31 % (2016). ROE is measured for the potential of the company to generate profits from investors' investments. United Airlines ' ROE has a strong growth potential between the five years, despite the declining performance of ROE in 2017 and 2018. Therefore, it can be said that United Airlines management has a high efficiency in financing the operation and allows the company to grow between the five years.

4.2 Liquidity Ratio

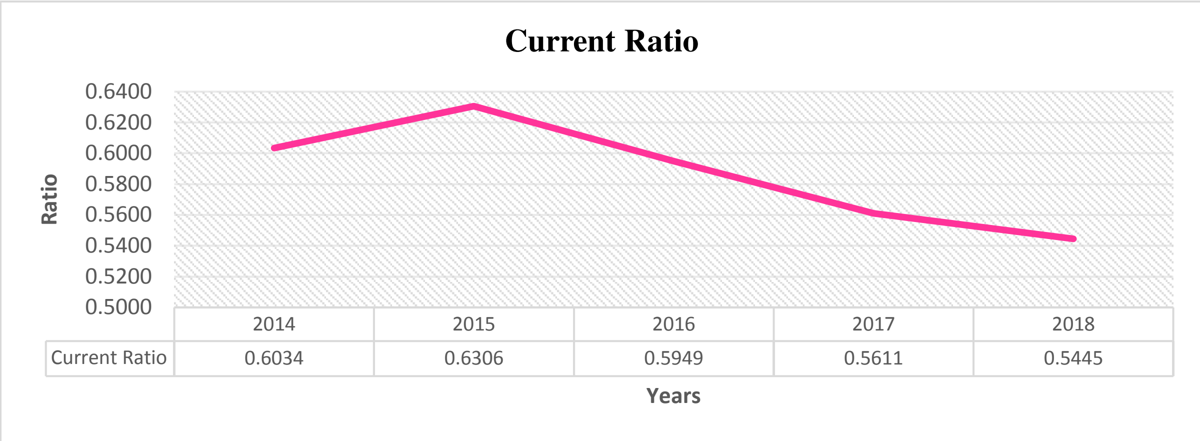


Figure 3: Current Ratio

Overall, the current ratio has also dropped slightly from 0.6034 in 2014 to 0.6306 in 2015 to 0.5949 in 2016. The current ratio of United Airlines is below 1 indicates that it is difficult for United Airlines to pay off its short-term liabilities with cash. That indicates a company's poor financial performance. The appropriate current ratio for safe companies is usually between 1.5 and 3. The higher the ratio, the more efficient the company will be.

4.3 Leverage Ratio

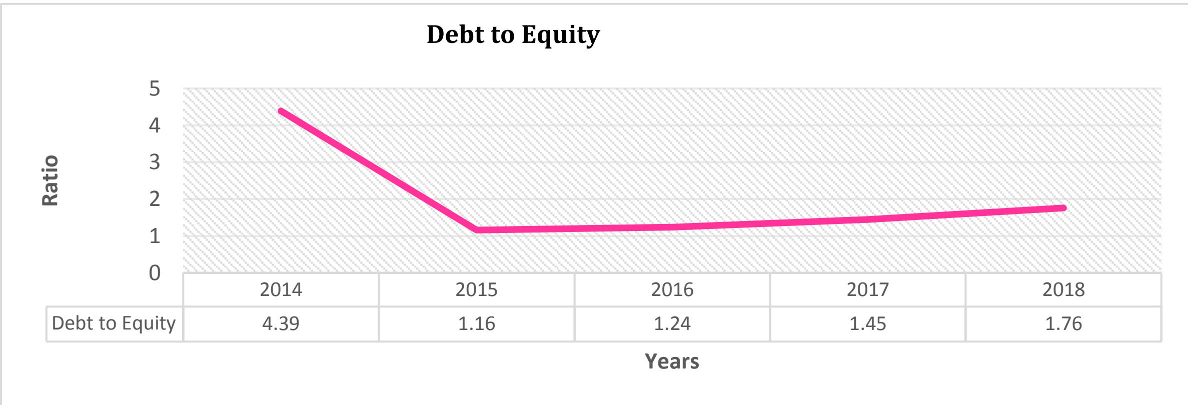


Figure 4: Debt to Equity

From the table above, United Airlines has the highest debt-to-equity ratio of 4.39 in 2014, slightly down to 1.16 in 2015 and slightly back to 1.24 in 2016. The debt-to-equity ratio for United Airlines is greater than 1 indicating that debt has funded more than 50% of United Airline's assets. The increase in the United Airlines ratio from 2016 to 2018 shows that the debt burden of United Airlines is rising.

4.4 Regression Analysis

4.4.1 Descriptive statistics of ROA and other variables

	Mean	Std. Deviation
ROA	.0730	.06037
ROE	.4628	.41068
CurrentRatio	.5869	.03429
QuickRatio	.4509	.04732
AverageCollectionPeriod	11.4853	.88150
DebtEquityRatio	2.0000	1.35604
DebtIncomeRatio	19.3017	9.54157
OperatingRatio	.9022	.03014
OperatingMargin	.0777	.03339
CGI	1.00	.000

Table 1: Descriptive Statistics

From the table above, the standard deviation of the current ratio and the quick ratio shows that there are small fluctuations in liquidity where the value of the current asset and the value of the current liabilities are totally different between those five years. Whereas 0.58 and 0.45 are the mean of the current ratio and the quick ratio, which is below 1 considered an unhealthy company. This indicates that United Airlines has a lower capacity to meet its short-term obligation to turn inventories into cash as soon as possible.

The mean operating ratio is 90 % which is satisfactory, as the average ratio is slightly below the accepted ratio indicating that United Airlines is operating efficiently. Next, the mean operating margin is 8%, which is between 80% and 90% below the benchmark. It is unsatisfactory as the average ratio is far from the accepted ratio, which indicates that United Airlines is inefficient in operation. The standard deviation also indicates that there has been little improvement in the ratio between 2014 and 2018.

United Airlines shows that the debt to equity is 2.00, which is above 1. It shows that more than 50% of United Airline's debt-funded assets since 2014, amounting to $34,199 million, have been downgraded to $31,895 million in 2015. It indicates that the organization is unable to fulfil its long-term financial obligations when there are periodic cash flow problems. While the standard deviation of credit for United Airlines is 1.356, it means that there is a slight difference in credit between that consecutive year 2014-2018. The score for accountability, transparency, independent, fairness and sustainability are 100% indicates that United Airlines has a strong and sound corporate governance structure that can be more productive and efficient in terms of profits and output.

4.5 Relationship of Liquidity ratio (current ratio), GDP and Operational ratio to the Profitability (ROA)

Correlations					
		ROA	**CurrentRatio**	**OperatingRatio**	**GDP**
Pearson Correlation	ROA	1.000	.664	-.810	-.865
	CurrentRatio	.664	1.000	-.520	-.423
	OperatingRatio	-.810	-.520	1.000	.852
	GDP	-.865	-.423	.852	1.000
Sig. (1-tailed)	ROA	.	.111	.048	.029
	CurrentRatio	.111	.	.185	.239
	OperatingRatio	.048	.185	.	.034
	GDP	.029	.239	.034	.

Table 2: Correlation United Airlines to Determine the Profitability

Coefficients						
Model		**Unstandardized Coefficients**		**Standardized Coefficients**	**t**	**Sig.**
		B	Std. Error	Beta		
1	(Constant)	-.092	1.531		-.060	.962
	CurrentRatio	.617	.779	.350	.792	.573
	OperatingRatio	-.126	1.532	-.063	-.082	.948
	GDP	-.064	.070	-.664	-.920	.526
a Dependent Variable: ROA						

Table 3: Coefficients United Airlines to Determine the Profitability

4.5.1 Liquidity to Profitability

Liquid measured by the current ratio of P (0.573) > 0.05 indicates that liquidity in all measurement variables has a negative and insignificant relationship to profitability. This finding is consistent with the findings of Assaf (2003), which implies that as low as high liquidity can be undesirable. In general, current assets are less profitable than fixed assets. It means that the money invested in current assets yields less return than fixed assets, including costs of investment and maintenance that can decrease the productivity of the company.

4.5.2 GDP to Profitability

The GDP variable measured with P (0.526) > (0.05) shows an insignificant relationship to productivity as part of the macroeconomic function. Negative related with correlation coefficients are variable operational potency ratio (-0.664). The inapplicable value benefit is strengthened by the appearance of (Alper and Anbar, 2011; Athanasoglou and Staikouras, 2006) and supports the immaterial negative value impact (Khrawish, 2011). In contrast, the inapplicable negative value relationship is divided into the belief that cash growth increases benefits and antagonistic downswing affects suspense earnings.

4.5.3 Operating Ratio to Profitability

Model Summaryb					
Model	**R**	**R Square**	**Adjusted R Square**	**Std. Error of the Estimate**	**Durbin-Watson**
1	.810a	.656	.541	.04088	2.246
a Predictors: (Constant), OperatingRatio					
b Dependent Variable: ROA					

Table 4: Enter Regression Analysis for United Airlines to Profitability

ANOVAa						
Model		**Sum of Squares**	**df**	**Mean Square**	**F**	**Sig.**
1	Regression	.010	1	.010	5.722	.097b
	Residual	.005	3	.002		
	Total	.015	4			
a Dependent Variable: ROA						
b Predictors: (Constant), OperatingRatio						

Table 5: Anova Regression Analysis for United Airlines to Profitability

After the test was carried out and all the variables were added. The enter method shows that the value of R is 0.926 and shows a high degree of correlation between variables. R^2 is 0.857 and indicates that 43% of the ROA variation is explained by independent variables. For the relationship between profitability and operating ratio, p > (0.097) can be calculated in 3 out of 4 measurements tested showing negative insignificant relation to profitability. This negative relationship suggests that the service of United Airline cannot improve the company's profitability and is not enough to handle its operating income and operating expenses. United Airline will find it difficult to maximize its annual profits due to the increasing operating costs that have a negative impact on the company.

5.0 Conclusion and Recommendation

The performance of United Airlines Bank from 2014 to 2018 shows that the quality of liquidity and operating efficiency were adverse by the year. United Airlines has been unable to convert its assets into cash for purposes of debt settlement. Not only, United Airlines is not efficient in managing its expenses and will affect profits and performance of the company. ROA is one of the indicators that measure the profitability of United Airline and indicate the insufficient profit of the company. It also indicates that United Airlines is impractical in service and has incurred external operating expenses. Several changes and improvements that need to be made by United Airlines to achieve their goals and increase the profitability of the company.

5.1 Recommendation

5.1.1 Improve future cash forecasting: trust matters

Future cash flows are one of the most critical risk management tools for the business. Trust in forecasting should not only provide insight into risk, but also help to protect against risk factors. Lack of accuracy, however, is also one of many key deficiencies in the forecast process. This should be a problem for United Airlines.

5.2.2 Improve in liquidity

Unproductive capital does not yield any revenue from United Airlines. If the company has a lot of such assets, they just must get rid of it. Because they can spend more money on properties such as buildings, equipment and airplanes to generate revenues. More capital can be produced to make more profit. First, one of the best ways to improve liquidity quality is to evaluate the productivity of various services and products. Evaluate where prices can be extended to maintain or increase profitability on a regular basis. Prices may also need to be managed as costs rise and markets shift. Then, evaluate overhead expenses and verify that opportunities are available to reduce them. It can have a direct impact on the gain to reduce the overhead. Overhead expenses, including leasing, sales, and consulting fees, are indirect costs borne by United Airlines outside direct material and direct jobs.

5.2 Conclusion

However, there are several threats faced by United Airlines, including liquidity risk, operational risk, credit risk, and market risk. United Airlines also tends all the risks and tries to minimize the risks. All risks are difficult to prevent, and the company will have to deal properly to avoid some loss and also to affect the profits of United Airlines. It will be complicated for United Airlines to resolve its responsibility and to operate properly for liquidity and operational risk. United Airlines focuses on improving its performance by managing the risk and keeping the profits. The findings suggest a variety of implications. Last, considering that United Airlines ' credit risk remains high, requiring attention to United Airlines' risk assessment, especially in the context of factors that have a direct impact on company credit risk.

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