

IMPROVING FINANCIAL HEALTH (CASE OF MAIN BRANCH PT. G)

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Abstract. PT G is a private family company that operates in the seafood industry. The company started with processing and exporting frozen shrimps, specializing in vannamei shrimp. PT G main branch only have general suspicion about that the financial health is doing bad, the need to be a confirmation of the general financial health, not only the profitability level. The financial health analysis was done by using financial ratios. The first indicator that the finance of the company isn't healthy was the continuous loss that they experience and the retained loss that was carried through until 2018 with the value of minus 12 billion rupiah. As bad as the profitability level, the other financial ratios that indicate problem is the solvency ratios. Improving the financial health means turn the company retained loss must be turned into retained earnings which can be done by forecasting with financial target. There are two types of forecasting the internal and external. The end result is that the external target forecasting yields a more plausible solution to improve their financial situation that is to aim increase the sales by 5% each year, keeping the COGS by 87% and supporting it by switching capital structure by taking in long term debt.

Keywords: Financial Health, Financial Ratios, Forecast, Net Profit Margin, Retained Earning

Since 1987, Indonesia has become one of the most important suppliers of shrimp in the world as stated in Directorate of Agricultural and Forestry Product Export 2012 Indonesia Agriculture for the world. Supplying at least 145,077.9 metric tons or equal to 1,311,010.9 thousand USD of shrimps in 2015 to the whole world. This striving industry is competing with, not only domestic companies but with global competitors such as company from India, Thailand, Vietnam, and others. A competitive business ecosystem compels companies to create strategies that can sustain them, especially if a few years the company financial health suffers. Mr. E (alias), the financial supervisors or 'controller', as he would like to call it, of PT G. is tasked with improving the financial condition (2018) of the main branch of PT G for the next five years (2019-2023).

PT G is a private family company that operates in the seafood industry. The company started with processing and exporting frozen shrimps, specializing in *vannamei* shrimp. They marketed the products to USA, Europe, Middle East, Africa and Asia. The company is a part of the a larger group called ISG that is owned by Mr.S (alias) as the majority shareholder. PT G first facility was built at the end of 2008 in Sidoarjo, East Java, Indonesia. The founder created the company because he saw an opportunity to operate in East Java as he previously experienced success from his shrimp processing company in Lampung and was looking to expand the business under a new name. PT G owns a processing facility which processes the raw material from outsourced farmers and other supplying companies in Sidoarjo. PT G strategy is about providing specialized frozen shrimp products, catering to the needs of the customers. In 2011, PT G expanded the business in marine product processing by adding a new line of product, pasteurized crabmeat, and building another facility in Gresik. In the same year, the company expanded again to Kendari, Southeast Sulawesi with the same line of product, shrimp, and adding other products such as octopus and fish. PT G continues to expand the business by providing new lines of products at the end of 2014. They started to produce and export canned sardines, mackerel, tuna, shrimp and crabmeat with location at Muncar, all located in Indonesia. All these new ventures are built as the subsidiaries of the main PT. G branch.

THE PROBLEM

The business went well, the sales kept on coming and operation kept on producing. In 2015 something unexpected happen. The parent company, PT G, suffers losses in the form of negative net income and deficit retained earnings. At first, the company suspected the reason of this happen due to the devaluation of USD, the main payment currency, but this loss kept on continuing into 2017. In 2018, they finally got a positive income but still have a large amount retained loss, around 12 billion rupiah. The finance division in the main branch had trouble figuring things out because of the lack of personnel to tackle this problem. PT G main branch finance team consist of 5 people who all handled different things: one person for bank transaction, one for sales transactions, one person for operational transactions and one for the accounting problem. As such, Mr E, who is the controller of finances for all PT G was called to solve the problem. Previously, he was station at the other branches such as Kendari and Gresik branches to help solve the problems there. He managed to solve the problem in the subsidiaries, now it is time to solve PT G main branch problem.

As PT G main branch only have general suspicion about that the financial health is doing bad, the need to be a confirmation of the general financial health, not only the profitability level. They had never done a financial analysis to examine the company (Nugraha, 2019). Financial analysis should be done because it can evaluate the company performance, compare firm different

performance in term of financial performance, prepare financial projections, giving info on weakness and strength of a company (Sheridan Titman, 2018). They also never done comparative analysis before, which is crucial for the company to understands better their financial performances in comparison to the industry. When the result of the financial health is known, then a plan to improve the situation can be thought. One of the ways is to set financial targets. Financial targets can be tested by forecasting which PT G never done when they set a target for future plan.

HOW IS THE FINANCIAL HEATH OF PT. G IN 2015-2018?

There are three standard indicators that can determine if a company is generally healthy. The first indicator that the finance of the company is not generally healthy is the negative net profit margin (NPM) they experience in a period. If the NPM shows to be continuous negative then that company does not make any profit in their operations. The second indicator is a retained loss. Deficit RE mean the company has incurred more losses in its existence than profits which is a bad sign since it means that there is no surplus money after paying the dividend that can be used to re-invest in the company again. The last one is if the company has continuous negative cash flows in the period. The key point here is that the cash flow statement, rather than the income statement, provides the best information about a highly leveraged firm's financial health (Samonas, 2015). To gain further depth of which part of the financial conditions that is unhealthy, financial analysis should be done.

PT. G managed to show that they are not generally healthy in that period because they show the first two signs. They shows an average NPM of – 2.34% and the retained loss that was carried through until 2018 with the value of minus 12 billion rupiah. As bad as the profitability level, the other financial ratios that indicates problem is the solvency ratios. The effectiveness ratios are very good, due to low level of assets and the liquidity ratio are okay. The ratios, may give insights to the financial health of PT G, but to get the wider picture, a comparison have to be made with the industry as a benchmark. PT G, had not have the chance to make a competitor analysis. A competitor analysis is crucial to measure how the company is doing and to see possibilities that can be achieved. Through competitor analysis the company can get a glimpse of how their peers strategize their business.

HOW IS THE FINANCIAL PERFORMANCE COMPARED TO PT G PEERS?

To answer this question, what will be done is comparing the resulting financial analysis with the benchmark in that industry, or in this case the sub industry. The benchmarks of the industry will be PT Central Proteina Prima Tbk. (CPRO), PT Dharma Samudera Fishing Indonesia Tbk. (DSFI), and PT Sekar Bumi Tbk. (SKBM). The reason they are chosen is because they are the only companies publicly listed on Indonesia Stock Exchange as marine and fishing. If we move one level up the industry, which is the Agriculture industry, it will not be an apple to apple comparison. Below is the highlight of the analysis.

Table 1 Financial Analysis Comparative Result

Ratios	Financial Ratios Result					Indicator
	2016	2017	2018	PT G AVERAGE	Industry Average	
Gross Profit Growth	3.07%	6.32%	9.25%	6.21%	14%	low profitability
Operating Profit Margin	-1.83%	0.13%	1.33%	-0.12%	3%	low profitability
EBIT Margin	-2.30%	-0.66%	2.51%	-0.15%	3%	low profitability
Net Profit Margin	-3.97%	-2.03%	1.36%	-1.55%	1.2%	low profitability
ROA	-4.42%	-2.32%	1.54%	-1.74%	1.7%	low profitability
ROE	-24.60%	-13.93%	8.71%	-9.94%	4%	low profitability
Debt ratio	0.82	0.83	0.82	0.83	0.69	higher solvency
Debt to Equity	4.56	4.99	4.67	4.74	1.12	Higher D/E
Financial Leverage	556%	576%	582%	572%	212%	Higher financial leverage

As seen from the table, PT. G performance regarding profitability can be seen that it is significantly lower than the industry. The solvency also shows that they have a higher D/E ratio, almost 4 times of the industry. This can be answered due to the company low NPM and not being public which restrain their ability to get equity, so they do have to rely much on debt as their source of funding. But that could be a benchmark for the company to try and target that ratio to support their profitability performances in the future. As for the liquidity ratio PT. G is on par with the industry averages of 1.2 and for the efficiency ratios, PT.G is above the industry in term of fixed asset management and inventory management. The average fixed asset turnover is 3.85 and 7.3 for inventory, PT.G fixed asset turnover is 28.5 rimes and 15.3 for inventory.

HOW TO IMPROVE PT.G FINANCIAL HEALTH?

Not only quantitative examinations is done to give recommendations for this case, but qualitative as well. Through interviewing the key players and company visit, some insights are gained. The way the main branch work was that there is no yearly forecast that the company have. They have vague target for the future but no time frame and concrete way to achieve it. The finance division, mostly only act in an accounting way as the company progressed. Their main function was to track and document the transactions going on through the working hours. Strategy was the last in their mind, as every member is swamped from their duties to track the transaction. Currently they are still using excels to document everything and are trying to move to accounting application called Zahir. When interviewed a few times, Mr. E cannot give the financial target for the future. They did not have a concrete target forecast. Until the company visit, then Mr. E gave the rough target which PT G wants to achieve in future. They want the sales to be able to raise until 6% per year, GPM of 20% in 5 years, OPM of 5%, EBTM of 10%, and ROA of 2% (Nugraha, 2019).

Improving the financial health means to turn all the factors that they did not pass into something that pass, the company NMP must turn into positive and retained loss must be turned into retained earnings. As such a plan must be form to reach the target but to check whether or not the target is achievable, a forecast will be done. The forecast is aimed to determine if the retained earning can be positive within the five year range with the target ratios that they want. There are two forecasts done, the internal base forecast which is based on the PT G target and the external based forecast which is based on external demand of Indonesia shrimp exports level and industry average ratios as the target. The result of this forecasts, yields two different period results. Internal forecast have these target: the sales to be able to raises until 6% per year, GPM of 20% in 5 years, OPM of 5%, EBTM of 10%, and ROA of 2% (Nugraha, 2019). These targets were sets based on the positive wants of the company without calculation it first. As such the results did improve the NPM into positives and that the retained earning managed to be positive in 2021. The results also have positive cash flows. Of course the targets yielded positive results because but what is the cost to support this increase. To receive certain sales, a company must be able to somehow finance their operations that are forecasted in the internal method.

Table 2 Income statement Internal Forecast Result

Internal	2019F	2020F	2021F	2022F	2023F
Revenue	245,171,327,559.91	252,526,467,386.71	262,627,526,082.18	275,758,902,386.28	292,304,436,529.46
Gross Profit	29,420,559,307.19	33,833,643,203.27	40,600,371,843.92	48,720,446,212.71	58,464,535,455.25
Operating Profit	6,008,400,675.38	7,355,139,826.80	8,838,426,358.53	10,505,101,043.29	13,787,945,119.31
Net Profit	4,736,013,419.65	7,372,751,534.50	11,470,206,683.88	15,973,040,452.32	18,960,101,898.12
Retained earning	(7,675,849,033.72)	(303,097,499.22)	11,167,109,184.66	27,140,149,636.99	46,100,251,535.11
Paid in capital (+)	23,336,194,531.00	113,945,681,167.00	172,812,648,351.00	180,815,320,490.00	115,184,835,274.00

The cost of internal forecast result is that, since the company wanted to lower its short term debt intake by 2% per year and did not feel inclined to take long term debt, the shareholders need to chip in around an average of 121 billion rupiah per year. While chipping in they have to continue taking short term debts, albeit more lower. Not only that but the forecast also raises the assets that was around 199 Billion rupiah in 2018 to 900 Billion by the end of 2023F.

The external forecast is based on the potential demand in the market and based on the average ratios that the benchmarks have. The reason the benchmarks are being followed here are because benchmarks are what a company should aim for. They are the examples that should be followed as much of them are usually a public company. In Indonesia if you are a public company then it can be considered as an example to strive for. If an industry average of a company is 5% and your company is below that, then to improve your financial conditions you can set that as your target. The target for this forecast is the sales to increase 4.9% per year based on CAGR calculation of Indonesia export demand from 2011-2015 (BPS, 2016). While for the GPM is 12.8%, for OPM is 2.8%, EBTM is 2.8%, and ROA is 1.7%. These targets are from the average of the industry consisting of ratios from CPRO, DSFI, SKBM. The result yielded great results that managed to fulfil the requirement to be considered as improving the financial health of PT G.

External	2019F	2020F	2021F	2022F	2023F
Revenue	252,121,408,913.23	264,318,498,848.06	277,112,800,948.30	290,533,556,809.50	304,611,439,797.92
Gross Profit	32,229,291,601.59	33,788,475,210.37	35,424,001,899.70	37,139,609,693.69	38,939,219,643.21
Operating Profit	7,061,307,728.37	7,402,918,564.96	7,761,255,862.41	8,137,138,606.73	8,531,425,884.33
Net Profit	3,312,989,349.08	3,397,385,451.73	3,494,951,074.41	3,600,260,664.37	3,713,637,775.96
Retained earning	(9,098,873,104.29)	(5,701,487,652.56)	(2,206,536,578.15)	1,393,724,086.22	5,107,361,862.17
Long term Debt(+)	44,863,791,952.79	434,516,073.21	633,207,408.16	735,537,094.82	841,032,556.15

The NPM becomes positives and the retained earning became positive by 2022F. Most of the targets are able to rise in a steadier amount. The cost to sustain this forecast is taking on a long term debt of 44 billion rupiah in 2019F and adding around 661 million rupiah the year after. They also needs to take some short term debt but it is considerably lower which is 56 billion rupiah compared to their original 130 billion rupiah. The reason why there is a change in capital structure was due to referencing the competitors common size of long term debt as an example. Due to the change in the capital structure, according to the matching principle of finance, short-term assets should be financed with short-term liabilities and long-term assets should be financed with long-term liabilities (Guin, 2011) , PT.G fixed assets will also increases.

Between the two results, even though the external yielded lower results, the target that is likely to be achieved is the external target forecasting. The main reason is due to the owner inability to chip in an average of 121 Billion rupiah from 2019F to 2023F when interviewed for validation and the preferences of taking on long term debt rather than paid in capital. There are other reasons for this such as the amount of asset needed to support internal forecasting results, and the efficiency of internal forecasting is very low. Form the ridiculous amount of asset they are only able to generate ¼ sales of the assets needed, which is very unnecesasary. As the time difference between each target is only a year apart.

CONCLUSION AND RECOMMENDATIONS

In conclusion, PT. G current financial condition is not generally health. Compared to its peers the profitability level are much lower and should be improved. To improve their financial health, PT. G must target their financial performance with these targets: increase sales of 4,9%, GPM is 12.8%, for OPM is 2.8%, EBTM is 2.8%, and ROA is 1.7% for the 5 years period. To achieve this they must maintain their COGS on the level of 87% , taking a long term debt so to decrease the short term debt they need, and to invest in fixed assets with buying newer machines , equipment, and renovating their building.

For the recommendation, PT.G needs to do financial analysis often so they can analyse and have concrete evaluations for their performance. They also need to improve their competitor research so they do not lose in competition. Furthermore, they should implement forecasting in general to make plans set targets, and anticipate future situations.

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