

FINANCIAL SITUATION OF PN17 COMPANIES LISTED IN THE MALAYSIAN  
STOCK EXCHANGE

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## DEDICATION

To my beloved mother, father, and my dear siblings, friends, who are always supportive when is needed, without their understanding I would not be able to complete my dissertation.



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May God bless all of us!

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## ABSTRACT

A Practice Note 17 (PN17) Company is a listed company in the Malaysian Stock Exchange that is financially distressed or does not have a core business or has failed to meet minimum capital or equity (Less than 25% of the paid up capital). Financial ratio analysis method can be used to detect the failure of this company. As of 9th August 2010, there are still thirty four companies listed on Malaysian Stock Exchange classified under PN17 List. These companies have entered into PN 17 list in accordance with existing standards. There are also investors who do not know the status of these listed companies. A real and full attention has not been given yet for these companies. Analytical studies and scientific researches are almost still lacking on PN17 Companies listed in the Malaysian Stock Exchange. The aims of this research work is to examine the differences between the financial liquidity ratios (Current, Quick, Cash Ratio) and Altman's Z-score in determining the financial failure of companies, that is using financial ratios and Altman Z Score to examine whether there is different between PN17 companies and Non-PN17 listed in the Malaysian Stock Exchange. It also aimed to determine whether are all the PN17 Companies listed in the Malaysian Stock Exchange financial failure companies, to explore and report the financial situation of companies listed on Malaysian Stock Exchange. The available data collected from the library of Malaysian Stock Exchange covering the period from 2003 to 2009 were used in the analysis. This study answered the research questions formulated. Financial Liquidity ratios and Altman Z-score can be used to detect financial distress of companies, and it is important to compare ratios with the industry average or with a competitor in the same sector. Not all the PN17 Companies are financial failure Companies, It was found that there are financial difficulties companies still listed among the Non-PN17 list. Companies should emphasize on the issue of accounting disclosure.

## ABSTRAK

Syarikat Nota Amalan 17 (PN17) adalah sebuah syarikat berhad di Bursa Saham Malaysia yang telah mengalami masalah kewangan atau tidak mempunyai perniagaan teras atau telah gagal untuk memenuhi keperluan modal minimum atau ekuiti (kurang daripada 25% daripada modal berbayar). Kaedah analisis nisbah kewangan boleh digunakan untuk mengesan kegagalan syarikat ini. Setakat Ogos 9hb, 2010, masih terdapat tiga-puluh penerbit tersenarai syarikat PN17 pada pasaran Bursa Saham Malaysia. Syarikat-syarikat ini telah dimasukkan ke dalam senarai PN 17 mengikut piawaian yang sedia ada. Terdapat juga pelabur yang tidak tahu status syarikat-syarikat tersenarai. Perhatian yang sebenar dan penuh masih tidak diberi lagi untuk syarikat-syarikat ini. Kajian secara analitikal dan penyelidikan saintifik masih kekurangan pada Syarikat-syarikat PN17 Syarikat yang tersenaraikan di pasaran Bursa Saham Malaysia. Tujuan kerja penyelidikan ini adalah untuk mengkaji samada terdapat perbezaan antara nisbah-nisbah kecairan kewangan (nisbah kewangan semasa, pantas dan tunai) dan Skor Z Altman dalam menentukan kegagalan kewangan sesebuah syarikat, iaitu, menggunakan nisbah kewangan ini dan Skor Z Altman untuk menentukan sama ada terdapat perbezaan status kewangan diantara Syarikat PN17 dan Bukan-PN17 tersenarai di Bursa Saham Malaysia. Ia juga bertujuan untuk menentukan sama ada kesemua Syarikat PN17 yang tersenarai di pasaran Bursa Saham Malaysia adakah Syarikat gagal kewangan, untuk meneroka dan melaporkan keadaan kewangan sesebuah syarikat yang tersenaraikan di Bursa Saham Malaysia. Data-data tersedia ada di perpustakaan Bursa Malaysia telah dikumpulkan dari tempoh 2003-2009 untuk dianalisis. Kajian ini telah menjawab soalan-soalan penyelidikan yang telah digubal. Nisbah kecairan kewangan dan Skor Z Altman boleh digunakan untuk mengesan masalah kewangan syarikat, dan ini adalah penting untuk membandingkan kadar dengan purata industri atau dibandingkan dengan pesaing dalam sektor yang sama. Tidak semua Syarikat PN17 adalah syarikat yang kegagalan kewangan. Dapatan kajian juga menunjukkan bahawa terdapat beberapa Syarikat yang mempunyai masalah kewangan tersenarai diantara Syarikat Bukan-PN17. Syarikat harus memberi penekanan tentang isu pendedahan perakaunan.

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**LIST OF ABBREVIATIONS**

KLSE	-	Kuala Lumpur Stock Exchange
N/A	-	Data Not Available
Delisted	-	Company Delisted from the Stock Exchange
SPSS	-	Statistical Package for Social Sciences
-T1	-	One year Prior to Classification as PN17 Company
-T2	-	Two years Prior to Classification as PN17 Company
-T3	-	Three years Prior to Classification as PN17 Company
+T1	-	The First year after the Classification as PN17 Company
+T2	-	Two years after the Classification as PN17 Company
+T3	-	Three years after the Classification as PN17 Company



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## CHAPTER 1

### INTRODUCTION

#### 1.0 Introduction

This chapter provides an overview of this research work, problem statement, scope, objective, significance, and its potential contributions. The research questions and organizations of this thesis are also presented while definitions of key terms used in this study are explained.

#### 1.1 Background of the Study

The Malaysian central bank was established in 1959. It plays a key role in the financial sectors in the infrastructure development of Malaysia's economy. Securities Commission in Malaysia was established in 1993 for promoting the development of Malaysian securities' market in accordance to the Malaysian Securities Law 1993 (Sanaa, 2009).

The Malaysian Stock Exchange takes a very strict view of breaches to the Malaysian Stock Exchange Rules and Malaysian Stock Exchange Listing

Requirements; as these breaches have the potential to undermine investor's rights and protection.

Undertake enforcement proceedings and actions in relation to identify contravention of the Malaysian Stock Exchange Rules and Malaysian Stock Exchange Listing Requirements and initiate legal action where necessary, to give effect to the enforcement decisions and actions. It also administers and process claims in respect of the Compensation and Fidelity Funds maintained by Malaysian Stock Exchange. Strict enforcement for contravention of the Malaysian Stock Exchange Rules and Malaysian Stock Exchange Listing Requirements are done through enforcement actions seeking to deter future breaches, educate the market, influence change, and enhance corporate governance.

The Malaysian Stock Exchange Listing Requirements and Malaysian Stock Exchange Rules empower Malaysian Stock Exchange to take enforcement actions for breaches of the Malaysian Stock Exchange Listing Requirements and Malaysian Stock Exchange Rules. The persons who are subject to these enforcement actions are applicants, listed issuers, management companies, trustees, directors, Participating Organizations, Trading Participants, Clearing Participants, Participants of Exchange Trading Platform, Registered Persons, Authorized Depository Agents, Authorized Direct Members and any such person to whom the Malaysian Stock Exchange Listing Requirements and Malaysian Stock Exchange Rules are directed.

Each year, Malaysian Stock Exchange makes enquiries and investigates potential rule breaches and depending on the conduct involved, the facts and circumstances, will trigger a variety of responses for the breaches / non-compliances including referrals of potential and significant contravention of the Capital Markets & Services Act 2007 to Securities Commission. Enforcement actions or sanctions by Malaysian Stock Exchange are merely one of the tools available to Malaysian Stock Exchange to address the breaches of the Malaysian Stock Exchange Listing Requirements and Bursa Malaysia Rules. A listed issuer must, in accordance with these Requirements, disclose to the public all material information necessary for informed investing and take reasonable steps to ensure that all who invest in its securities enjoy equal access to such information, a listed issuer must ensure that no disclosure of material information is made on an individual or selective basis to

analysts, shareholders, journalists or other persons unless such information has previously been fully disclosed and disseminated to the public.

According to the Malaysian Stock Exchange Listing Requirements and Malaysian Stock Exchange Rules, a listed company that is financially distressed or does not have a core business or has failed to meet minimum capital or equity and companies' shareholders' funds are (less than 25% of their total paid-up capital) will be classified as PN17 Company. This Company is required to submit to Malaysian Stock Exchange their plan on how to regularize or face possible delisting. These Companies that triggered any of the criteria pursuant to Practice Note 17 of the Main Market Listing Requirements of Malaysian Stock Exchange are said to be reprimanded. Under these circumstances and in accordance with the Bursa Securities decision, the companies will be removed from the official list of Bursa Securities, after the imposition of suspension, and delisting procedures against the companies if it failed to be regularized ([www.klse.com](http://www.klse.com), retrieved on 7<sup>th</sup> February, 2010).

Malaysia Securities Berhad Market has frequently reprimanded companies for breaching of Listing Requirements of Malaysian Stock Exchange. This has resulted in increasing calls on objectivity and uncovering the risks in the Malaysian financial markets because an early uncovering of weakness in the markets enables an immediate intervention. Consequently these avoid the crises in the financial system (Michael, 2007; Hoon, 2002).

Hasabullah et al., (2009) has provided insight that financial analysis of data using ratio analysis can be used as an early alerting method for financial failure among companies listed in the stock exchange. Financial analysis is a tool that helps management to make decisions and plans and control them. During the last century, a number of events in the international economy greatly affected the performance of countries on the international economic environment, chronic crises of stock markets. The financial markets in Southeast Asia in 1997, has witnessed a major breakdown in both Hong Kong and Indonesia. The crisis erupted in Philippines, Thailand, South Korea and Malaysia, led to the spread of infection in these Asian countries unexpectedly for the failure of companies and the political instability as well. The Malaysian experience was a great example for others in improving their performance in the market (Hoon, 2002).



The use of financial analysis has increased in the recent decades due to the increase in both industrial and commercial projects and the competitiveness among them, establishing standards and criteria of the sectors of such markets to monitor and assist in establishing the decision. Globalization is an era, which is considered as a revolution of information, which has triggered the need to analyze and treat huge numbers of the data (Mohammed, 1997). The advancement is another important factor led to the necessity of providing investors with the many needed financial criteria, such as Technology, Economics, Management and accounting. All these represented an accelerating issue for the giant, limited, and multi-nationality companies to appear (Ali, 2008). A financial statement was shown by Altman and Beaver to be sufficient information for a highly discriminate function for large businesses (Robert, O. 1971).

One of the major purposes of the financial analysis is studying the financial failure. Specifically, the insurance field, where projects need bank loans for limiting and avoiding bankruptcy risks (Edward, I. 1968). Moreover, purposes of the financial analysis it is to predict the processes that produce the financial failure to activate many reasons and factors over long periods of time up to the case of inability to pay obligations and access to new commitments, loss of balance financial and operating cash. The result is that the company is experiencing financial hardship and the inability to pay their existing obligations in a timely manner and indicators, and that is why they suffer from such problems (Hayali, 2004).

There are cases where classical inspection is not able to detect issues and deviations in financial management reporting. However, through the use of financial analysis methods, such deviations can be tracked in greater details. Financial analysis is also used in evaluation works for obtaining concise and realistic financial and accounting reporting. Problem arises pursuant to hiding of important information by those who prepare financial reporting and the lack of commitment by many companies and facilities to disclose the accounting detected are reported for regulating to adhere to laws and rules in line with the recommendations and principles of the International Accounting Standards Committee. Therefore, an important functions of the financial analyst is to show the true picture of the facility by ensuring accounting and financial reports are reflected professionally (Ali, 2008; Hayali, 2004).

Researchers' attention began to focus on analyzing the financial conditions of companies in the sixties in the United States with the encouragement of the American Institute of Certified Public Accountants, and the Securities and Exchange auditor's role in early warning of the incidence of corporate bankruptcy. Beaver was the first researcher to complete a study in this area in 1966. He built a model which is known as complex financial ratios. Later, Researchers from Britain, Canada, and the United States have done similar studies in this field, where Altman is considered the most common model among them (Mohammed, 1997).

The financial ratios serve financial analyst in the evaluation of corporate performance in the areas of profitability, liquidity and solvency, as well as the efficiency of management in the design and implementation of funding policies and investment (Mohammed, 1997).

## 1.2 Problem Statement

The Star, a local newspaper highlighted among others the negative views expressed on PN17 Companies especially by the auditors on the payment-failure of loans and the main benefits, companies' shareholders' funds are less than 25% of their total paid-up capital (Kok, 2010). There are Companies that were classified under the PN 17 list as early as year 2005 that failed to resolve their financial problems. Among such Companies are also those that were warned for the lack of disclosure of data or to reconsider their regularization plans. Companies' that continued unable to regularize had also led to their delisting from the listing under the Malaysian Stock Exchange ([www.klse.com](http://www.klse.com), retrieved on 17th May, 2010). Also as of 9th August 2010, there are still thirty four companies listed on Malaysian Stock Exchange classified under PN17 (Practice Note 17) List and these companies has entered into PN 17 list in accordance with existing standards ([www.klse.com](http://www.klse.com), accessed on 11th August, 2010).

Despite the recent strong stock market rally and performance, some investors may still doubt the financial health of some listed companies, and the investors are very concerned about whether to cut losses or hope in the healing of these shares for

stocks they owned that were classified as under the companies PN17 category. Some investors are also unaware that they are those holding shares in companies that have been classified under PN17. In some cases, investors do not know about written off notices of these companies (Kok, 2010).

There are many questions, worries, and comments on PN17 future. However, a real and full attention has not been given yet for these companies. Analytical studies and scientific researchers are almost still lacking on PN17 Malaysian Companies listed in the Malaysian Stock Exchange.

### 1.3 Research Questions

To provide better insights into the areas that enable to better deal with financial analysis, the following research questions are formulated to guide this study:

- (i) Is there a difference between the financial liquidity ratios i.e. Current Ratio, Quick Ratio, Cash Ratio and Altman Z-score 1968 in determining the financial situation of the PN17 Companies listed in Malaysian Stock Exchange?
- (ii) Is there a difference in determining the financial situation between PN17 failure Companies and Non PN17 Companies listed in Malaysian Stock Exchange using financial liquidity ratios and Altman Z Score 1968?
- (iii) Are all the fifty two PN17 Companies listed in Malaysian Stock Exchange financial failure Companies?
- (iv) Is there any financial distress companies that are listed in the non PN17 list of companies listed in the Malaysian Stock Exchange listing facing financial failure?

#### 1.4 Objectives of the Research

To achieve the purpose of this study, the main research objectives are:

- (i) To examine the differences between the financial liquidity ratios, (Current, Quick, Cash Ratio), and Altman's Z score 1968 in determining the financial situation of PN17 companies.
- (ii) Using financial liquidity ratios and Altman Z-score 1968 to determine whether there is difference in the financial situation between PN17 and Non-PN17 companies.
- (iii) To determine whether all the PN17 Companies listed in Malaysian Stock Exchange are financial failure Companies.
- (iv) To determine the situation of financial performance of companies that are listed in the Non-PN17 list of companies listed on Malaysian Stock Exchange.

#### 1.5 Scope of Study

The scope of this study is as follows:

- (i) This study is based on data of all the fifty two PN17 Companies, and other fifty-two non-PN17 Companies which were selected from different sectors listed on Malaysian Stock Exchange.
- (ii) Financial Analysis Ratios including Cash Ratio, Current Ratio, and Quick Ratio, based on comparing to the industry average, and Altman Z Score 1968 were used to determine and explore the situation of financial performance of the Companies studied.

(iii) The PN17 Companies data used in the analysis works were based on the financial information of the respective companies, 3 years prior to classify as PN17 list and 3 years thereafter, data collected from 2003 until 2009. For the Non-PN17 Companies the analysis works of the financial results were based on the last five years financial results of these Companies, from 2005 until 2009.

## 1.6 Significance of the Study

The importance of the study can be summarized as following: -

(i) This study will contribute to bridge the lack of studies which explore the financial accounting in Malaysian context.

(ii) This study attempts to provide a new horizon for further research on financial accounting.

(iii) This study is among other studies using Altman's model 1968 and financial ratios to determine financial hardship of Companies. It's also among other studies especially on the PN17 Companies listed on the Malaysian Stock Exchange.

(iv) This study will be able to further provide insight on financial situation of PN17 Companies' position to strengthen the confidence of shareholder and investor in making better informed investment decision.

## 1.7 Research Organization

This thesis comprises of five chapters as follows:

Chapter one provides an overview of this research work, problem statement, scope, objective, significance, and its potential contributions. The research questions

and organization of this thesis, definitions of key terms used in this study are explained.

Chapter two provides the Literature Review of existing literature related to this study. The review undertaken is to provide an overview of the gaps of literature of this study and how this current work will contribute to the research.

In Chapter three, the methodology used in this study is explained. The topics covers include research design and, sampling design, research hypotheses, measurements, descriptive statistics and the method of data analysis.

Chapter four features on data analysis and findings, data collection and data analysis, results are presented.

Finally in Chapter five, it covers the discussion, conclusion and recommendations of this research works.

## 1.8 Definitions

The main terms used in this study are defined below:

**Bursa Malaysia Securities Berhad Market:** is the Malaysian Stock Exchange regulated and supervised by the Malaysian Securities Commission under the Malaysia Securities Act 1993.

**PN17 Company:** Company that triggered any of the criteria pursuant to Practice Note 17 of the Main Market Listing Requirements of Malaysian Stock Exchange are said to be reprimanded under the PN17 list as financial distress companies.

**Non-PN17 Company:** Companies traded normally in the official Bursa Malaysia Securities Berhad or the Malaysian stock exchange market.

**Business Failure:** means the company ceased operations following its inability to make a profit or to bring in enough revenue to cover its expenses.

**Insolvency:** means the inability of a company to pay off its debts, or pay debts as they fall due.

**Industrial Average:** is a value-weighted average of ratios of companies traded on the Malaysian Stock Exchange.

**A ratio:** is a figure or percentage representing the comparison (Robert, 1971).

**Liquidity:** is financial metrics that is used to determine a company's ability to pay off its short-terms debts obligations, or measures that help to ascertain a firm's ability to pay operating expenses.

**Current Ratio:** is a financial liquidity indicator that measures whether or not a firm has enough resources to pay its debts over the next 12 months, and it compares a firm's current assets to its current liabilities.

**Quick Ratio:** is a financial liquidity indicator that further refines the current ratio by measuring the amount of the most liquid current assets there are to cover current liabilities, and a sign of company's financial strength or weakness.

**Cash Ratio:** is an indicator of a company's liquidity that refines both the current ratio and the quick ratio by measuring the amount of cash, cash equivalents or invested funds there are in current assets to cover current liabilities.

**Altman Z-score:** is a linear combination of five common business ratios, the coefficients were estimated by identifying a set of firms which had declared bankruptcy and then collecting a sample of firms which had survived, with matching by industry (Wikipedia, the free encyclopedia).

## 1.9 Summary

This Chapter has provided an overview of this research work, problem statement, scope, objective, significance, and its potential contributions. The research questions and organization of this thesis, definitions of key terms used in this study are explained.

There is still lack of research works which uses financial ratios, that is current, quick and cash ratios and Altman's Z score to investigate companies listed in the Bursa Malaysia Securities Berhad Market and this is especially so for the PN 17 Companies. All the PN 17 Companies and selected other Companies listed in this Securities are used in the current research work.



PTTA UTHM  
PERPUSTAKAAN TUNKU TUN AMINAH



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