Effects of Profitability, Liquidity, Leverage, and the Pandemic on Financial Distress

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ABSTRACT

This research was conducted in order to produce empirical evidence on the effect of profitability, liquidity, leverage, and the COVID-19 pandemic on financial distress. The research was conducted referring to the object of research in the form of companies in the cyclical consumer sector that have been listed on the Indonesia Stock Exchange from 2018 to 2020. The sample used in this study amounted to 35 companies with predetermined sample criteria. The analytical method in this study uses multiple linear regression analysis with the use of the SPSS version 25 application. In this study it was found that profitability and pandemics had an effect on financial distress. Other variables in the form of liquidity and leverage have no effect on the company's financial distress. It is hoped that the results of the research can be useful for interested parties to find out things that can have an effect on financial distress.

Keywords: Financial Distress, Ratio, and Covid-19

INTRODUCTION

The pandemic period has had a tremendous impact on the paralysis of the domestic and foreign economy, thus posing the threat of recession to depression in many countries (Junaedi & Salistia, 2020). According to the Badan Pusat Statistik (2020), the contraction of economic growth of up to 5.32% that occurred for two consecutive quarters could also have an effect. BI and the Indonesian Minister of Finance share the view that Indonesia's economic future is bleak until early 2021 with a decline in growth until August 2020 of -6.13% (Mulyani, 2020). The economic crisis in 2020 caused Indonesia and even other developed countries to experience difficulties in their industrial sectors (Junaedi dedi & salistia Faisal, 2020). In the article (Runis et al., 2021), it is explained that a decrease in performance can cause the company to experience financial distress so that management is needed that has the ability to keep the company running and avoid financial distress.

In the article (Murni, 2018), financial distress is characterized by a company's financial crisis. In another article (Waqas & Md-Rus, 2018) states that before going bankrupt, the company will experience financial distress which is marked by losses by the company in several years. According to (Fadillillah, 2019), financial distress can be predicted which can be done by analyzing the
company's financial statements that contain financial information for interested parties. In the article (Maretha Rissi & Amelia Herman, 2021) defines a company's financial distress condition as marked by negative net income in its two-year operational period.

According to article of (Sudana, 2012), the ability to earn a profit by utilizing sources such as company sales, capital, or assets measured by comparison is called profitability. Profitability provides information related to success or failure in company operations as an effort to achieve goals (Anis Mafiroh, 2016). Profitability is used to provide information on efficiency and the effectiveness of the company's operating results in a certain period (Sudana, 2012). According to (Fadlillah, 2019), profitability information is to determine the effectiveness and efficiency of generating profit from the use of assets. Companies that make poor profits and tend to experience financial deficits are called financial distress (Putri & Aminah, 2019). According to (Agustini & Wirawati, 2019) for investors, the company's net profit is useful as a reference in distributing dividends. Investors will not get dividends if the company's willingness to make profits is small or suffers losses. This condition is feared to cause the company to go bankrupt. If the company experiences continuous losses because it does not generate profits or profits, the company's performance must be improved so that there is no ongoing financial distress (Fadlillah, 2019). Some articles (Agustini & Wirawati, 2019; Dirman, 2020; Fadlillah, 2019; Hafsi, Nanda Ayu; Setiawanta, 2021; Mahaningrum & Merkusiwati, 2020; Runis et al., 2021; Saputra, 2022) prove that profitability has an effect on financial distress. However, the high profit of the company cannot guarantee that the company will avoid financial distress because high profits can come from high receivables as well, such as research conducted by Anis Mafiroh (2016), has different results and shows that profitability has no effect on financial distress conditions.

According to (Hanafi, & Halim, 2012) liquidity is the ability to pay current debt by looking at current assets to short-term debt ratio. Maintaining company liquidity is a form of agent responsibility to the principal as a shareholder in order to pay off short-term debt on time (Agustini & Wirawati, 2019). According to (Putri & Aminah, 2019), the liquidity ratio is current assets divided by current liabilities. According to agency theory, debt decisions are controlled by agents. (Fadlillah, 2019) states that a high liquidity ratio with current assets can guarantee the company can pay its current debt, so that the liquidity ratio will affect financial distress. Financial distress research conducted by (Fadlillah, 2019; Hafsi, Nanda Ayu; Setiawanta, 2021; Runis et al., 2021; Syuhada et al., 2020) uses the independent variable liquidity examining property companies which proves that the liquidity ratio affects the prediction of financial distress. However, in current assets there are receivables that are difficult to change in paying current debt, thus proving that liquidity has no effect on financial distress (Agustini & Wirawati, 2019; Anis Mafiroh, 2016; Dirman, 2020; Mahaningrum & Merkusiwati, 2020; Maysarah et al., 2022; Murni, 2018).

According to (Anis Mafiroh, 2016) there are several companies that overcome financial distress problems by adding loans and some of them carry out mergers or business combinations. A ratio that needed to determine the amount of debt on assets or on equity so that the chance of default on obligations to the company will be measurable is called leverage (Mahaningrum & Merkusiwati, 2020). According to (Agustini & Wirawati, 2019), The high value of the company's leverage ratio will also be followed by high obligations to be paid by the company. From (Pradana, 2020), states that high loans can cause companies to pay interest on loans so that it can increase the chance of companies experiencing financial distress. In using the independent variable leverage, some of the articles (Agustini & Wirawati, 2019; Mahaningrum & Merkusiwati, 2020; Pradana, 2020; Runis et al., 2021) state that leverage has no significant effect on the company's financial distress. On the other hand, companies with high debt but followed by high assets can indicate that the company is able to pay its obligations with its assets so that leverage does not affect financial distress Dirman (2020) and Murni (2018).
Before this research was conducted, there was a pandemic that caused all industrial sectors to experience a decline in performance (DAD et al., 2020). In the article (Murni, 2018), financial distress conditions are marked by a decline in the performance and financial crisis of companies. During the pandemic there is a policy of social activity in the community that can cause a decrease in the level of the economy in Indonesia (Hafsari, Nanda Ayu; Setiawanta, 2021). Economic growth has decreased considerably compared to 2019 (Saputra, 2022). The impact of this affects the company, consumers prefer to postpone or cut needs that are not priorities such as secondary needs (Maysaroh et al., 2022). The pandemic causes a gradual decline in income so that creditors or investors have increased vigilance in financing the company because they consider management to be incapable of carrying out their duties and ultimately, the company is experiencing financial distress conditions (Hafsari, Nanda Ayu; Setiawanta, 2021).

Company size was chosen as a control variable because company size can provide an overview of the state of stability and strength of the company in facing bankruptcy (Dirman, 2020). The large size of the company makes it easy to get access to funding for business development and attract creditors and investors (Putri & Aminah, 2019). Small company sizes will be faced, such as resource difficulties, limited integrity, and funding difficulties (Aghnitama et al., 2021). Company size can also have a direct effect on financial difficulties. This is similar to the article (Agustini & Wirawati, 2019), which gives the result that company size can have a negative effect on financial distress because the greater the total asset value, the greater the ability of company to pay off its obligations.

The results of previous studies were inconsistent. Due to the inconsistency of previous research, the researcher wants to conduct research on the effect of profitability, liquidity, and leverage on financial distress. On the other hand, researchers are also interested in conducting a study on financial distress in which the pandemic period is one of the causes of financial distress and company size is a control variable. There has been no previous research that uses the control variable in the form of firm size to study the effect of profitability, liquidity, leverage, and pandemic, which has the potential to have an effect on financial distress, so this research is interesting to do. The cyclical consumer sector companies for the 2018-2020 period were selected in this study as research objects.

METHODS

The method used in this study is quantitative with the object of research namely the annual reports of cyclical consumer sector companies that have been listed on the Indonesia Stock Exchange (www.idx.co.id) during the 2018-2020 period. The total population was 121 companies before purposive sampling was carried out. Companies must include several sample criteria before research. There were 8 companies that did not submit periodic financial reports on the Indonesia Stock Exchange during the 2018-2020 period. There are 79 companies that have not experienced negative losses or profits for 2 consecutive years or more on the Indonesia Stock Exchange during the 2018-2020 period. Until finally, the final number of sample companies that can be studied is 35 companies.

Data analysis In this study using multiple regression analysis. The analysis was carried out on the SPSS version 25 application. Multiple regression analysis was used to perform predictive analysis on the dependent variable with two or more independent variables (Sugiyono, 2021). Multiple regression analysis was carried out by performing the F test and T test. The F test has a function to test the effect of the independent variables together on the dependent variable through certain criteria, but the F test cannot test the effect partially. (Widarjono, 2015). The T test has a function to partially test the effect of the independent variable on the dependent variable (Savitri, C., 2021).
RESULTS AND DISCUSSION

Multiple regression analysis
In this study, a test was conducted on profitability, liquidity, leverage, and pandemic on financial distress with firm size as the control variable. This research was conducted with a model such as the following:

![Diagram showing Multiple regression analysis model]

F Test
The results of data processing using multiple linear regression through SPSS version 25, one of which obtained the F test results as shown in the following table:

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>df</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regression</td>
<td>23792,750</td>
<td>5</td>
<td>17,043</td>
<td>0,000</td>
</tr>
<tr>
<td>Residual</td>
<td>27642,312</td>
<td>99</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>51435,061</td>
<td>104</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Data Processed 2022
Based on the results of the F test, the F value is 17.043 which has a significance value of 0. In the distribution table for the F value with a probability of 0.05 by determining the formula based on the number of samples and variables, the resulting value is 2.46. The value of 2.46 is smaller than 17.043 and the significance value is less than 0.05, so it can be said that all independent variables together can have an effect on the dependent variable.

T Uji test
In addition to producing the F test, multiple linear regression also produces a T test as shown in the following table:

<table>
<thead>
<tr>
<th>Model</th>
<th>B</th>
<th>Std. Error</th>
<th>t</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>(Constant)</td>
<td>13,038</td>
<td>9,654</td>
<td>1,351</td>
<td>.180</td>
</tr>
<tr>
<td>ROA</td>
<td>14,598</td>
<td>1,649</td>
<td>8,850</td>
<td>.000</td>
</tr>
<tr>
<td>CR</td>
<td>.768</td>
<td>1,044</td>
<td>.735</td>
<td>.464</td>
</tr>
<tr>
<td>DER</td>
<td>-.049</td>
<td>.144</td>
<td>-.337</td>
<td>.737</td>
</tr>
</tbody>
</table>
Pandemi 4.987 3.588 6.390 .016
SIZE -.452 .377 -1.200 .233

Source: Data Processed 2022

Through the T test, the formula for multiple regression equations can be formed as follows:

$$FD = 13.038 + 14.598PR + 0.768LI - 0.049LE + 4.987P - 0.452SIZE + e$$

The equation above has a regression coefficient of profitability variable (X1) of 14.598, which means that any increase in profitability will have an impact on financial distress. Liquidity (X2) has a regression coefficient of 0.768, which means that any increase in liquidity will affect financial distress. Leverage (X3) produces a regression coefficient of -0.049, which means that any decrease in leverage will have an impact on financial distress. Pandemic (X4) produces a regression coefficient with a value of 4.987, which means that every decline in the pandemic can have an impact on financial distress. Size has a regression coefficient of -0.452, which means that each decrease in size affects financial distress. Each increase and decrease of the independent variable can affect financial distress.

Results And Discussion

Through the t-test conducted, the t-count for profitability (X1) is 8.850 with a significance value of 0. The resulting significance value is not greater than 0.05 which indicates that profitability has a significant effect on financial distress. Through the t-table, the number 1.660 is generated through a formula based on the number of samples and the number of variables. After a comparison between t-table and t-count has the result that the t-count of profitability is not smaller than t-table (8.850>1.660). H1 is supported that profitability has an influence on financial distress conditions. This happens because a high profitability ratio can be a sign that the company can utilize its assets effectively to generate profit. The high profitability that has been obtained by the company, the higher the financial distress that will be faced by the company.

The t-test performed shows tcount for liquidity (X2) of 0.735 with a significance value of 0.464. The resulting significance value is not less than 0.05 which indicates that liquidity has no significant effect on financial distress. Through the t-table, the number 1.660 is generated through a formula based on the number of samples and variables. Comparison between t-table and t-count yields t-count of liquidity not bigger than t-table (0.735 < 1.660). H2 does not support that liquidity does not affect the company's financial distress. This happens because the liquidity ratio used is the current ratio for non-long-term predictions, because financial distress requires a long-term predictor. This research is in line with research conducted by Agustini & Wirawati (2019), Dirman (2020), Mahaningrum & Merkusiwati (2020), Runis et al. (2021), Saputra (2022) which states that financial distress can be affected by profitabilitas.

Through the t-test performed, the t-count value on leverage (X3) is -0.337 with a significance value of 0.737. The resulting significance is not smaller than 0.05 which results show that leverage does not have a significant effect on financial distress. Through the t-table, the number 1.660 is generated through a formula based on samples and variables. The comparison between t-table and t-count results that the t-count leverage is not less than t-table (-0.337>-1.660). H3 is not supported that leverage has no effect on the company's financial distress. This happens because leverage, which has a proxy with the debt to equity ratio, is not an accurate predictor. The results of this study are supported by research by Dirman (2020) and Murni (2018) which states that financial distress can’t be affected by leverage, but contradict the research of Agustini & Wirawati (2019), Mahaningrum & Merkusiwati (2020), Pradana (2020), and Runis et al. (2021).
The t-test carried out obtained the results of a pandemic t-count (X4) of 6.390 and had a significance value of 0.016. The resulting significance value is not greater than 0.05, providing evidence that the pandemic can have a significant effect on financial distress. Through t-table, the number 1.660 is generated through a formula based on samples and variables. The comparison between t-table and t-count has the result that the t-table is greater than the pandemic t-count (6.390>1.660). This proves that H4 is supported, namely that a pandemic can have an impact on the company's financial distress. This happened due to government policies that had an impact on the economic slowdown and decreased buying interest.

The t-test carried out obtained the results of a size significance value of 0.233. The resulting significance value is not greater than 0.05, providing evidence that the pandemic can not have a significant effect on financial distress. This proves that size of the company does not have a significant effect on financial distress. This occurs because the Natural logarithm of the company's total assets added in this study cannot suppress the errors that exist and may arise in this study. Company size can describe how much assets owned by the company. However, the size of the company still cannot prevent the company from financial distress (Yuda Pratiwi & Sudiyatno, 2022).

CONCLUSION

Through this research it was found that liquidity and leverage do not have an impact on financial distress. Profitability and pandemic have an influence on financial distress. In the financial statements there is a profitability ratio that is used to measure the effectiveness of management as an agent in its operations. Profitability is the basis for the company's assessment of its performance by referring to the return of funds that have been invested. The effectiveness of the use of poor assets can increase operating costs and cause companies to experience difficulties in carrying out their operations. Companies that are unable to carry out their operations can result in financial distress. The existence of the influence of profitability on financial distress can provide an overview for the principal in giving trust to his funds in the company so that the principal can manage the funds invested. The pandemic period in this study led to the implementation of a policy of limiting social activities that caused instability in various corporate sectors. Specifically, restrictions on social activities during the pandemic caused people to experience a decrease in income and even lose their income. This causes the company to experience a decrease in revenue from sales which is the main support in its operational activities so that the conditions experienced can cause financial distress to the company. There are still many shortcomings in this study, such the use of operational definitions of variables in a pandemic is not good. The test carried out in this study was only a simple test without differentiating the financial statements during testing, and in this study, it was only conducted in consumer cyclical sector companies. Suggestions in this study are be able to examine companies other than the consumer cyclical sector, better use of operational definition of the pandemic variable, and further research will be carried out by conducting different tests before and after the pandemic.

REFERENCES

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