CHAPTER 1

INTRODUCTION

1.1 Background of Study

Now days, in the 21st century, it is important to understand about risk management and apply it. This will enable us to know and prepare for any possible conditions that affect financial stability. Especially in this digital era, transaction is taking place very quickly and everyone is competing to survive in the market. Most companies have failed to adapt trough technological developments, because they are too busy developing a brand while their competitors have taken a thousand steps to anticipate new technologies. They should be aware that the market is dynamic, not static. They never able to survive if they have not taking to anticipate it. This is not only about how to adapt but also how to anticipate every condition.

In addition, in the global market found that foreign competitors have competitive products at competitive prices and of course with high-quality technology to compete with domestic companies. The lack of preparation to anticipate the digital market made big companies collapse. This happened in foreign countries, including in the United States. There are at least 12 more retail companies in 2018 filing for bankruptcy (reported by CNBC 12/31).

In Indonesia, there are several foreign retails that have to leave, such as 7-Eleven, Lotus, Body shop, which have to close outlets with various factors. This will be influenced by both internal and external factors. If the company can taking anticipate it by implementing risk management properly, then the risk of bankruptcy can be minimized.

Risk is the culture, process, structures that are directed towards realizing potential opportunities while managing adverse effects (Australian Standard/ New Zealand Standard Number 4360:2004). Starting from identifying, measuring, mitigating risks, developing strategies to evaluating risk management programs. All of these will disclose in risk management report. Because of the demands community about increase in Good Governance, changes in environment and requirements investors and regulator the risk management is needed by companies. There are several benefits of practicing risk management in companies such as; more effective decisions, effectiveness in program implementation-program or activity, effectiveness of allocation and use of resource, high standards in service customer, high standards of accountability, creativity and innovation in practice management, increased capacity, increased moral organization, and transparency.

To know whether the company have implement good risk management or not, is if the company have disclosed risk management information in the annual report for at least one year prior and has risk management committee to solving the risks. From Australian Standard/ New Zealand Standard (2004), there are 8 components of risk management; Internal environment, Objective setting, event identification risk assessment, risk response, control activities, information and communication, and monitoring. Risk management report must follow these components in annual report. To evaluate risk management report, we will make checklist of level of maturity of risk management. The level is risk naive, risk aware, risk defined, and risk managed.

Risk management itself starting in 1995 with published Australian Standard/ New Zealand Standard 4360:1995. Since the founding of risk management, several risk management standard have been developed including the Project Management Institute, the National Institute of the Standard and Technology, and ISO standards (International Organization for Standardization).

Furthermore, in risk management there are some risks that will be manage such as interest rate risk, market risk, credit risk, operational risk, working capital, liquidity risk, foreign exchange, insurance and others. All of these risks might be happen in the company, for example is the company has risk that promised cash flows are not paid. If this risk is high, that something bad might be happen to the company. If there is risk management committee, the problems can identify and risk management committee can ask company to do something before too late. The respond of risk management committee can anticipate problems that might be worst to the company. If there is risk management in the company, the other risks can be reduces and the problems be able to solve by the company. Therefore, the risk management can help to anticipate bankruptcy risk.

Many researchers already research about risk management. Smith and Stulz (1985) were among the first to recognize that transaction costs of bankruptcy can induce public corporations to make use of risk management instruments. More specifically they show that the use of risk management instruments can moderate the volatility of cash flow, which reduces the probability of incurring direct and indirect bankruptcy costs. Froot, Scharfstein, and Stein (1993) discuss other rationales for risk management in addition to the costs of financial distress and managerial incentives: taxes, debt capacity, capital market imperfections, and inefficient investment.

The research will expect to help companies to think that they may have to change their mind to practicing the risk management to avoid bad decision in the future. If the risk management already have good implement, company who used can detect the overcome future problems. The otherwise, if there is company who has implemented the risk management but mismanaging hopefully will repair or upgrade the system for company itself.

There are researchers also study about relationship between risk management and bankruptcy. For reference, Fehle and Tsyplakov (2005) demonstrate that firms that are either far from financial distress or deep in financial distress do not initiate or adjust their risk management instruments. On the other hand, they show that the rest of the firms do initiate and actively adjust their use of risk management instruments. Purnanandam (2007) shows that financially distressed firms (that have high leverage) have higher incentive to engage in hedging activities, but that these incentives disappear when their financial distress becomes severe.

The researcher from University Of South Carolina, Columbia, by Marin (2007) have been research about risk management help prevent bankruptcy in “Can Risk Management Help Prevent Bankruptcy”, and surprisingly the result is the companies that companies that can manage the risk have approximately 96% lower for filling bankruptcy. This means, the companies that use risk management can anticipate the bankruptcy.

Also there is research about theoretical insight of company bankruptcy methodology for forecasting by Mackevičius, Šneidere and Tamulevičienė (2018) from Vilnius University and University of Latvia in the title “Complex Analysis of Company Bankruptcy Forecasting: Theoretical Insight”. The recommendation of this research is six elements of complex analysis of company bankruptcies.

To measuring the bankruptcy risk, there are some statistical models to calculate bankruptcy risk such as Altmant 1 (critical value Z>1.8), Fulmer (critical value H>0), and Springate (critical value S<0.862). With these method can classify the companies into two groups, which is default (unhealthy, unsuccessful), and non-default (healthy, successful). From these two, will examine which are the company who has good risk management have positive impact to bankruptcy risk or not.

1. 2 Problem Statements

From the explanation above, then generally speaking the problems examined are related to measuring the risk of bankruptcy and relate to risk management implement. For more detailed, the research problems will answer basic questions such as the following:

1. How the level of maturity of risk management in Retail Companies listed in IDX?
2. Is company who used to has implement the risk management (have good level of maturity risk management) has non-default detect to bankruptcy risk?

1. 3 Research Objectives

The main objective of this research is to know and understand the risk management purposes to companies according with existing factors. This discussion is considered important given the risk management yet practically use, so many companies have not use measurement properly to anticipate the risk of bankruptcy. It will certainly give rise difficulties in the company then will risk the investors to anticipate any possibilities. Therefore company needs to develop good risk management in order to save their own business. Which means they must has good risk management report and risk management committee to solve any possibility according to risk mitigation.

1. 4 Research Contribution

As for the benefits that can be derived from this research are:

For author:

1. To add insight thinking in terms of particular risk management can reduce the bankruptcy risk.
2. As one of the conditions for the examination Council of the comprehensive S1 Accounting.
3. It is also useful in research add to insights of science, especially the science of risk management as well as examining the experience of experience of researchers in private.

For company:

This research is expecting to deliver the benefits as well as a useful input in the applying risk management in areas of finance, especially in analyzing risk of bankruptcy.

For public sector:

Research result can serve as a reference in the new science of accounting, financial accounting, in particular concerning about risk management, which can be used by some retail companies as well as those who need it.

1.5 Research Limitation

This research will be limited to record risk of bankruptcy from analyze the financial statement and risk management report evaluation of retail companies. The outcome of this research will help the company to know what exactly the risk management guide the company in case of financing and managing. This research will be conducted in Retail Companies listed in IDX.

1. 6 Writing Systematic

This writing systematic contains all the chapter of thesis in details, they are:

CHAPTER I INTRODUCTION

This chapter briefly about background of research itself, problem statement, research objective and research contribution.

CHAPTER II LITERATURE REVIEW

Explain briefly about relevant theory with the problem discuss includes: the definition of risk management, recognize and measurement of bankruptcy risk from any sources.

CHAPTER III RESEARCH METHODOLOGY

Explain about research objective, research object which consist of the location itself, data collection method which consist of content analysis and data processing and analysis.

CHAPTER IV ANALYSIS AND RESULT

This chapter will go to the problem discussion related to the research retail companies in Indonesia and result from the analysis comparing the company that has been practically use risk management and companies who do not. Finally conclude that practically use the risk management is relevant or not to the risk of bankruptcy itself.

CHAPTER V CONCLUSION

Consist of conclusion, limitations, and recommendations of research.