CHAPTER I

INTRODUCTION

1.1 Background of Study

A company in carrying out its operations of course will experience an unstable financial situation which can be caused by the decision making of shareholders or the influence of external factors such as politics and state conditions. The ever-changing economic conditions affect the performance of both small and large companies. Also, business developments in this era of globalization make competition in the business world increasingly tight. Businesspeople are required to be more creative, innovative, and expand the scope of business. With intense competition, companies must strengthen their management to survive in their industry. Company management should be able to anticipate the changes of economic conditions that can affect companies financial.

Companies should be able to compete against the intense competition. If the company does not have the readiness and ability to compete, it will result in a decrease in the company's activities and the company will not be able to survive. This makes the company's financial condition is unhealthy which illustrates the occurrence of financial distress. Financial distress problems can have a major impact on the company such as the loss of trust from the stakeholders. Continuing financial distress conditions can lead a company to bankruptcy. The bankruptcy of a company can harms many parties such as investors who will lose their capital invested in that company and creditors who have lent capital but cannot get repayment from the company.

All companies can experience financial distress so this problem is an important issue that must be watch out because financial distress is an early sign of a company's bankruptcy. The lightest level of financial distress starts from the company's financial difficulties in short-term which usually only temporary and not so severe. However, if there is no immediate action from the company, this condition will get worse and the company can be liquidated, which is the most severe level of financial distress. Company management can supervise the company's financial condition to minimize the occurrence of bankruptcy by analysing financial statements (Ramadhani and Lukviarman, 2009). The financial statements issued by the company contain information such as financial position, the performance of company, and changes in the company's financial position which can be converted into useful information in decision making. This can be done by conducting a financial distress analysis in the form of financial ratios (Nirmalasari, 2018). Beside financial ratios, there are several other methods that can be used to predict financial distress such as cash flow analysis, the Z-score method introduced by Altman, or through corporate governance evaluation.

There are several financial ratios used in this research that affect financial distress which are Debt to Assets Ratio, Return on Assets Ratio, and Total Assets Turnover Ratio. Debt to Assets Ratio is a ratio that tells the percentage of a company’s total assets that were financed by using debt, it also indicates the company’s financial leverage. By using this ratio, analysts can compare the financial leverage of each other company in the same industry and shows how stable a company is. The higher the ratio, the degree of leverage is also higher, and it will make the risk also higher to invest in that company because as it has more risk of missing debt payments. This ratio measures the company's ability to guarantee its debts with a number of assets it owns (Wardiyah, 2016).

Return on Assets is a ratio that measures the ability of company in earning profits by using their assets. It is an indicator to manager, investor, and analyzer of how profitable the company in relation to its total assets or how efficient the management utilize its assets which made higher ROA is being preferred. Higher return on assets means that the better the company in utilizing their assets to generate net income.

Total Assets Turnover is one of the activity ratios. Total Assets Turnover is used to measure the ability of company to generate sales revenue with the assets owned by the company. The higher total assets turnover, the faster the asset turnover occurs which shows that the company have a better performance in utilizing their assets to generate sales revenue. This ratio indicates the amount of sales that can be generated from each rupiah embedded in the company's total assets.

One of the high-risk sectors is property and real estate. Property and real estate companies are usually chosen as one of the business instruments for investors because they are an alternative for long-term investment. The property and real estate sectors are considered to have an important role in contributing to economic growth and is believed that it can become a benchmark for economic growth. This industrial sector is difficult to predict because it is the sector that is most vulnerable to interest rate fluctuation, inflation, and exchange rates that affect people's purchasing power. The inconsistent changes of these industry do not close the possibility that property and real estate companies are experiencing financial distress.

Table 1.1 Data of Debt to Assets Ratio, Return on Assets, Total Assets Turnover and Financial Distress (Altman Z-Score) of Property and Real Estate Companies Listed on Indonesia Stock Exchange for the period 2018-2021

Companies	Year	Debt to Assets	Return on Assets	Total Assets Turnover	Financial Distress (Altman Z-Score)
PT Natura City Developments Tbk (CITY)	2018	0.162	0.095	0.287	9.818
	2019	0.122	0.034	0.132	11.742
	2020	0.084	0.068	0.157	15.591
	2021	0.081	0.001	0.082	15.737
PT Jaya Real Property Tbk (JRPT)	2018	0.365	0.100	0.233	4.493
	2019	0.337	0.093	0.223	4.789
	2020	0.314	0.088	0.193	5.265
	2021	0.306	0.067	0.187	4.879

Source: Prepared by writer (2023)

Table above shows an effect between Debt to Assets Ratio (DAR), Return on Assets (ROA), and Total Assets Turnover (TATO) during 2018-2021. From 2019 to 2020, the DAR of PT Jaya Real Property Tbk decrease which makes the Altman Z-Score increase. However, in 2021, the decrease of DAR makes the Altman Z-Score to decrease. The decrease of Altman Z-Score is not following the existing theory, which states that the decrease of debt to assets ratio will make the Altman Z-Score increase as the possibility of experiencing financial distress is lower.

Moreover, during 2018 to 2019, PT Natura City Developments Tbk had a decrease in ROA and TATO which cause the Altman Z-Score to increase significantly. While during 2020 to 2021, the decrease in ROA and TATO didn’t cause the Altman Z-Score to increase but decrease. These differences will be the reason of this research conducted, which is to find what factors that have significant effect on financial distress.

Lots of research have been conducted before regarding the effect of financial ratios on financial distress and there are inconsistent results. Some of the previous research resulted in Debt to Assets Ratio, Return on Assets, and Total Assets Turnover have significant effect on financial distress while some have the opposite results. Inconsistent results from previous research make the writer interested in conducting a re-examination of the effect of Debt to Assets Ratio, Return on Assets, and Total Assets Turnover on Financial Distress in different companies and different periods.

Based on the background that have been explained above and there are inconsistent results from the previous research regarding the dependent variables that have been chosen in this research, the writer decides to do research with the title **“The Effect of Debt to Asset Ratio, Return on Asset and Total Asset**

Turnover on Financial Distress in Property and Real Estate Industry Listed on the Indonesia Stock Exchange."

1.2 Problem Limitation

There are several problem limitations set by the writer to limit the scope of this research which are:

1. The research object that chosen by the writer for this research is property and real estate companies listed on Indonesia Stock Exchange.
2. The dependent variable chosen by the writer for this research is Financial Distress which will be measured by using Altman Z-score.
3. The independent variable chosen by the writer for this research is Debt to Assets Ratio, Return on Assets, and Total Assets Turnover.
4. The period of data for this research is limited from 2018 to 2021.

1.3 Problem Formulation

Based on the background that has been written above, the problem formulation are as follows:

1. Does Debt to Assets Ratio have significant effect on Financial Distress in Property and Real Estate companies listed on Indonesia Stock Exchanges for year 2018-2021 partially?
2. Does Return on Assets have significant effect on Financial Distress in Property and Real Estate companies listed on Indonesia Stock Exchanges for year 2018-2021 partially?

3. Does Total Assets Turnover have significant effect on Financial Distress in Property and Real Estate companies listed on Indonesia Stock Exchanges for year 2018-2021 partially?
4. Does Debt to Assets Ratio, Return on Assets and Total Assets Turnover has significant effect on Financial Distress in Property and Real estate companies listed on Indonesia Stock Exchanges for year 2018-2021 simultaneously?

1.4 Objective of the Research

Based on the stated problem formulation, this research objective are as follows:

1. To find out whether Debt to Assets Ratio has a significant effect on financial distress in Property and Real Estate Companies listed on Indonesia Stock Exchange for 2018-2021 partially.
2. To find out whether Return on Assets has a significant effect on financial distress in Property and Real Estate Companies listed on Indonesia Stock Exchange for 2018-2021 partially.
3. To find out whether Total Assets Turnover has a significant effect on financial distress in Property and Real Estate Companies listed on Indonesia Stock Exchange for year 2018-2021 partially.
4. To find out whether Debt to Assets Ratio, Return on Assets and Total Assets Turnover have significant effect on Financial Distress in Property and Real Estate Companies listed on Indonesia Stock Exchanges for year 2018-2021 simultaneously.

1.5 Benefit of the Research

This research is expected to give both theoretical and practical benefit to the readers.

1.5.1 Theoretical Benefit

This research is expected that it can be a source of reference and literature for further research. This research is also expected to provide knowledge to the readers about financial distress and financial ratios that can affect the occurrence of financial distress in companies.

1.5.2 Practical Benefit

1. For investors

   Provide information to investors about the condition of the company whether it is experiencing financial distress and become an insight for investors when making investment decisions.

2. For company

   This study uses data provided directly by the company so that it is a form of real analysis of the company's condition that has been adapted to the theoretical basis, so this can be used as a benchmark in considering the actions to be taken by the company.