CHAPTER I

INTRODUCTION

1.1 Background of Study

Indonesian economy's development has heightened competition between technology companies. The increasing level of competition among businesses requires them to innovate meticulously, improve performance, develop human resources, and create products that give them a competitive edge. Due to the fact that Indonesia's economy is still developing, there is no guarantee that businesses will survive. They are even more likely to be at risk of financial distress or insolvency. If they had made an incorrect prediction about the company's performance, it would have had fatal consequences. Thus, bankruptcy can be detrimental to one's credit score and should be viewed as a situation in which a business or individual is unable to generate sufficient revenue or income to meet or pay financial obligations. This is frequently the result of high fixed costs, a high proportion of illiquid assets, or revenue that is susceptible to financial downturns.

Typically, this condition does not manifest itself in businesses; rather, there are early warning signs that can be identified if financial statements are analyzed more carefully in a particular way. Bankruptcy can occur as a result of both internal and external factors affecting the business. Financial ratios can be used to predict a company's financial distress. A company's financial distress has a significant impact on its investors, which is why additional analysis and study are required to forecast future financial distress. The analysis and study's findings will also have an effect on investors' long-term investment decisions. Numerous financial ratios can be analyzed to determine a company's overall financial health and the likelihood of its continued viability as a viable business. Financial ratios that connect and compare the various numbers on a company's balance sheet or income statement are more meaningful than stand-alone numbers such as total debt or net profit. Financial ratios' overall trend, or whether they are improving over time, is also critical.

Current Ratio is one of the financial ratios that measure the liquidity of a company by dividing current asset to current liabilities. In current ratio, we see the ability of the business to meet short-term obligations, typically those due within a year. It explains to investors and analysts how a business might maximize its current assets in order to pay down current debt and other payables.

Another financial ratio is Gross Profit Margin. The gross profit margin is a financial indicator that analysts use to determine a company's financial health. It is calculated as the amount of money remaining after subtracting the cost of goods sold from product sales (COGS). Gross profit margin, which is occasionally referred to as the gross margin ratio, is often stated as a percentage of sales. The gross profit margin percentage of a business is computed by subtracting the cost of products sold from the net sales (gross revenues minus returns, allowances, and discounts). The gross profit margin is then calculated in percentage terms by dividing this value by net sales. If a company's gross profit margin swings significantly, it may indicate bad management methods and/or substandard products. On the other hand, similar swings may be appropriate when a business makes significant operational changes to its business model, in which case transitory volatility should not be a cause for concern. For instance, if a business decides to automate some supply chain tasks, the initial investment may be substantial, but the cost of goods ultimately drops as a result of the reduced labor expenses associated with automation. Adjustments to product pricing may also have an effect on gross margins. If a corporation sells its items at a premium, it will have a higher gross margin, all other factors being equal. However, this can be a difficult balancing act, as if a corporation sets its prices too high, fewer customers will purchase the goods, resulting in market share loss.

The Altman Z-score is the result of a credit quality test that determines a publicly traded manufacturing company's likelihood of bankruptcy. The Altman Z-score is calculated using five financial ratios extracted from a company's annual 10-K report. It makes use of profitability, leverage, liquidity, solvency, and activity to determine whether a business faces a high or low risk of bankruptcy. Altman's Z-Score has been widely accepted as a reliable tool for assessing a company's financial health. Altman developed a multivariate formula for assessing a company's financial health and forecasting the likelihood of financial distress and bankruptcy. Numerous studies evaluating the effectiveness of Altman's Z-Score have demonstrated that the formula has a reliability of between 80% and 90%. (Altman E., 2000).

Table 1.1 Data of Current Ratio, Gross Profit Margin and Altman Z Score of 2 Technology Sector Companies Listed in IDX Year 2016-2020

Company	Year	Current Ratio (X_1)	Gross Profit Margin (X_2)	Altman Z Score (Y)	Altman Z Score Indictors
PT. Anabatics Technologies Tbk (ATIC)	2016	1.18	14.77	7.98	SAFE
	2017	1.14	15.87	5.74	SAFE
	2018	1.44	15.23	3.09	SAFE
	2019	1.10	15.93	2.40	POTENTIALLY BANKRUPT IN A YEAR
	2020	0.98	15.98	3.43	SAFE
PT. Elang Mahkota Technologies Tbk (EMTK)	2016	5.08	43.43	3.24	SAFE
	2017	5.64	37.37	2.77	NEED ATTENTION
	2018	4.32	31.64	2.68	NEED ATTENTION
	2019	3.20	25.02	2.46	POTENTIALLY BANKRUPT IN A YEAR
	2020	2.56	24.24	4.85	SAFE

Source: prepared by the writer (2021)

Table 1.1 shows the Current Ratio, Gross Profit Margin, and Altman Z Score. The results are calculated using the data given in financial statements and annual reports. . PT. Anabatic Technologies Tbk current ratio decrease gradually through year 2018 until 2020, eventhough having an increased from year 2017 to 2018. In 2017 to 2018, PT. Anabatic Technologies gross profit margin happened to be decreased, but keep increasing from 2018 until 2020. The Altman Z Score of PT. Anabatic Technologies Tbk was keep decreasing from 2017 until 2019, but manouver significantly in 2020.

PT. Elang Mahkota Teknologi Tbk shows their current ratio was gradually decrease through year 2018 until 2020, along with the gross profit margin. The Altman Z Score was decreased from 2016 but increase significantly in year 2020

Thus, this study will determine whether the Current Ratio and Gross Profit Margin have an effect on the company's financial distress. The writers are interested in performing research under the title **"THE IMPACT OF CURRENT RATIO AND GROSS PROFIT MARGIN ON FINANCIAL DISTRESS IN TECHNOLOGY SECTOR COMPANIES LISTED ON THE INDONESIA STOCK EXCHANGE FOR THE PERIOD 2016-2020."**

1.2 Problem Formulation

Based on the background of the study above, the research's problem identification is as follows:

1. Does Current Ratio partially impact Financial Distress in Technology Sector Companies Listed in Indonesia Stock Exchange?
2. Does Gross Profit Margin partially impact Financial Distress in Technology Sector Companies Listed in Indonesia Stock Exchange?
3. Does Current Ratio and Gross Profit Margin simulataneously impact Financial Distress in Technology Sector Companies Listed in Indonesia Stock Exchange?

1.3 Problem Limitation

Due to the time constraints, the writer will limit himself to research whether there is impact of current ratio and gross profit margin towards financial distress. Current Ratio, Gross Profit Margin, and Altman Z Score will be applied to a sample of technology companies listed on the Indonesia Stock Exchange taken by the writer. The calculations will establish whether Current Ratio and Gross Profit Margin impact Financial Distress.

1.4 Objectives of Study

The objectives of this research is to answer the problems that has been formulated, which is:

1. To identify whether Current Ratio partially affect Financial Distress in Technology Sector Companies Listed in Indonesia Stock Exchange.
2. To identify whether Gross Profit Margin partially affect Financial Distress in Technology Sector Companies Listed in Indonesia Stock Exchange.
3. To identify whether Current Ratio and Gross Profit Margin simultaneously affect Financial Distress in Technology Sector Companies Listed in Indonesia Stock Exchange.

1.5 Benefit of Study

The outcomes of this research are likely to give benefit to a wide variety of users.

1.5.1 Theoretical Benefit

- For Writer

  The writer was able to utilize theories and knowledge gained during his undergraduate studies through this research. The writer is able to develop a more complex and comprehensive understanding of the research subject, particularly about Financial Distress

- For Academician

  This research may serve as a resource for future scholars interested in financial analysis and financial distress.

1.5.2 Practical Benefit

- For Firms

  Firms can benefit from this research by increasing their awareness of the importance of the Current Ratio and Gross Profit Margin. Additionally, organizations can obtain additional references and a different perspective for decision-making, particularly in the area of financial health.

- For investors

  This research can provide investors with new information and perspectives when examining firms. Investors are notified of the impact on the firm's financial health when the Current Ratio and Gross Profit Margin are implemented.

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