



**FINANCIAL DISTRESS:  
(A STUDY OF COMPANIES THAT ARE CLASSIFIED AS PN4 AT  
BURSA MALAYSIA BERHAD)**

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**APRIL 2006**

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## **ACKNOWLEDGEMENT**

I would like to take this opportunity to express my sincere thanks and gratitude to all of those people who have contributed comments and suggestions in completing this project paper. My deepest appreciation goes:

- ◆ To my advisor for this project paper, Madam Norzaihan Hashim, for her constructive comments, understanding, guidance and courage in completing this project paper.
- ◆ To my second advisor Madam Jennifer Janang for her valuable comments and suggestions.
- ◆ To all of my lecturers who had gave the best out of them in making my study a success.
- ◆ To my colleagues that helped in one way and another in completing this report.
- ◆ To my family for their unconditional love and continuous support in making this project reality.
- ◆ To all my friends for their support and deepest understanding.

Thank You.

## **ABSTRACT**

This project is attempted to study the relationship between leverage ratio and liquidity ratio with the companies' performance of the companies classified as PN4. Net profit margin is used to measure the companies' profitability. The objective is to see the performance of the companies in PN4 categories before and after they are classified as PN4.

This study has been conducted based on the ten out of twenty-one companies classified as PN4 as at 30 December 2005. The ten companies are selected randomly from the sample size. The study will cover the period of five years, that is two years before the companies classified as PN4, the year the companies enter PN4 and two years after the companies classified as PN4. The name and some descriptions of the samples are included under the population and sample size.

In the report finding I will analyze the leverage ratio and liquidity ratio using the descriptive analysis and Pearson Correlation.

## **1.0 INTRODUCTION AND BACKGROUND OF THE STUDY**

Financial distress refers to a situation in which a company's cash flow is insufficient to pay its current obligations. As a result, the company will default on its debt repayment leading to legal action taken by creditors. When the company is in financial distress, it is said to be insolvent. There are two types of insolvency:

- i) Stock-based insolvency occurs when the company's net worth is negative. That is the total debt value is larger than the total asset value.
- ii) Flow-based insolvency occurs when a company's cash flow could not adequately cover its current obligations. The company will not be able to service interest and repay debt when they become due.

In the course of doing business, some companies may succeed while others may fail. Those that succeed enjoy high returns and their share will be highly demanded in the market. However those that failed become history, eventually to be forgotten by investors.

### **1.1 Financial Distress Companies (PN4)**

A company in PN4 is a company that has an inadequate level of financial condition to warrant continued trading and listing on the official list at Bursa Malaysia Berhad. A listed company is classified as a PN4 when it is in any one or more of the following conditions.

- It has incurred a deficit in its adjusted shareholders' equity on a consolidated basis.