A Literature Review of Net Profit Margin

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ABSTRACT

Net profit margin is one indicator of the company’s financial performance. Net profit margin on cruise industries, for example, exhibit consistently robust growth trends for the leading cruise players, over 2016–2019, contrary to most commercial shipping market segments that experienced abrupt and persistent revenue declines since the outbreak of 2008 global financial crisis, cruise shipping has seen a robust resistance and relatively rapid recovery. Spurred by the growing importance of institutional investors, capital markets in emerging economies experience rapid growth. Specifically, equities ownership in emerging capital markets have tripled since the early 1990s. Another factor attracting equities investment involves institutional investors who offer potential for increased monitoring in the invested firms. The objective of this research is to determine the factors associated with net profit margin. I presented a literature study using systematic literature review of relevant publications and as a result of this process, 18 articles are included and then examined the bibliographical references to check the validity of the inquiry and to avoid any potential omissions. I identify several variables that affect and affected by net profit margin.

Introduction

A firm’s performance depends on efficient management of economic resources and performance is usually a function of firm-specific economic factors and macroeconomic factors, in other words, an efficient allocation, management and manipulation of these factors is required to enhance profitability (Maity et al., 2019). Spurred by the growing importance of institutional investors, capital markets in emerging economies experience rapid growth (Tee, 2019). Specifically, equities ownership in emerging capital markets have tripled since the early 1990s (Khorana et al., 2005). Another factor attracting equities investment involves institutional investors who offer potential for increased monitoring in the invested firms (Aggarwal et al., 2011).

Net profit margin on cruise industries exhibit consistently robust growth trends for the leading cruise players, over 2016–2019, contrary to most commercial shipping market segments that experienced abrupt and persistent revenue declines since the
outbreak of 2008 global financial crisis, cruise shipping has seen a robust resistance and relatively rapid recovery (Syriopoulos et al., 2020). In 2019, Carnival recorded cruise revenue at $20.8 billion (+10.3%, 2019/2018), similarly, Royal Caribbean also gained robust revenues at $10.9 billion (+15.3%, 2019/2018), and Norwegian Cruise Line, on the other hand, saw comparatively modest revenue growth at $6.5 billion (+6.6%, 2019/2018) (Syriopoulos et al., 2020).

Literature Review

Jensen et al. (2020) evaluated transformational leadership drawing upon media sources which were content analysed to create individual CEO profiles, and these profiles were then given to a panel of three judges who rated the CEOs on their transformational leadership style, and finally the results showed significant associations between intellectual stimulation and inspirational motivation respectively, and different financial performance indicators. Jensen et al. (2020) observed a tendency of positive relationships between individualized consideration and firm performance and these findings remained significant after controlling for company baseline performance, firm size, CEO tenure, and company location, finally the findings largely support the positive role of CEO transformational leadership in shaping firm performance.

Rastogi et al. (2020) identify the trend in the financial performance of the Indian and US based renewable energy companies by utilizing k-means cluster of machine learning algorithm, furthermore, the trends that emerged from the cluster analysis are studied alongside the major events that took place both internal and external to the firm and the government regulations and changes in tariff policies have emerged to be the common factors in determining the firm’s future. For the developed economy such as the US, an announcement by a global governing body or a spat between two countries over terms of trade can seriously affect the performance of concerned companies, hence, it is concluded that the tariff rates and policies for renewable energy companies need to be framed in a manner to encourage the firms to increase their investments towards the clean energy production (Rastogi et al., 2020).

Srinivasan (2020) found that affected firms are more likely to make acquisitions following tariff reductions and found some evidence that the acquisitions made in response to tariff decreases are associated with better firm profitability ratios in the following year, indicating that firms respond to increased competition by making
acquisitions to improve their operational efficiency. Cross-sectional tests show that this association is more pronounced for single segment firms, capital intensive firms, firms with higher profit margins, and firms with better growth opportunities, which suggests that this association is stronger for firms that are affected by increased competition to a greater extent, and firms that stand to gain more from acquisitions when faced with increased competition, and moreover, the positive relation between acquisition likelihood and tariff cuts is more pronounced for financially unconstrained firms, and during times of high capital liquidity, which implies that it is easier for firms with greater access to capital to respond to increases in foreign competition by making acquisitions (Srinivasan, 2020).

Nanda & Panda (2019) found large scale of heterogeneity among the firms under different quantiles of profitability; export earnings, firm size, asset turnover and volatility of exchange rate are the decisive determinants of financial performance across all quantiles and also found that quantile regression approach is a better method than panel OLS models in the presence of highly heterogeneous and non-normal distributions. Financing assets by current debt is negatively impacting return on assets and return on capital employed of firms from lower quantile whereas profitability is positively impacted if they are financed by long term debt, and debt financing of assets does not make any sense for firms with high quantile of profitability (Nanda & Panda, 2019). Michaelides et al. (2019) investigates how CEOs' salaries are affected by firm-level determinants, e.g. firm size, returns on assets, returns on equity, capital expenditure, market concentration, Tobin's Q etc, as well as by the individual characteristics of each CEO, e.g. CEOs age, gender, and based on the findings, the market concentration index in the US energy sector has a negative and statistically significant impact on CEO salary for all firms that operate in either a highly monopolistic or a purely competitive environment.

Maity et al. (2019) present that firm specific (e.g. size of firm; age of firm; fixed asset turnover) and macroeconomic variables (e.g. GDP; inflation; export intensity) made a significant impact on profitability of this industry and the findings of the study should assist managers as well as policy makers to frame sustainable policies of this mature industry. Gropp et al. (2020) found that with guarantees in place unproductive firms receive larger loans, invest more, and maintain higher rates of sales and wage growth, moreover, firms produce less productively. Firms also survive longer in banks’ portfolios and those that enter guaranteed banks’ portfolios are less profitable and productive, and finally, fewer economy-wide firm exits observed and bankruptcy filings in the presence of guarantees (Gropp et al., 2020).
Mason (2018) argues for greater focus of entrepreneurship research, education, and investment in knowledge-based services (KBS) and presents initial research exploring unique differences, challenges, and opportunities for new venture development in KBS. Karimi & Barati (2016) present fifty-eight efficient companies with a performance value of 1, and fourteen companies became inefficient with the efficiency size was less than 1; therefore, reference units were also introduced to the managers for efficiency of inefficient companies. Grashuis (2018) presents per the results, variability in the financial performance of US farmer cooperatives is for the most part associated with the operating profit margin, which confirms prior findings of cost inefficiency in the empirical literature, therefore, US farmer cooperatives may improve financial performance by emphasizing sales and operating costs.

Brahma et al. (2018) found that post-merger operating performance is negative and significant across all the five accounting indicators matched by size, and market to book ratio suggesting that utility mergers underperform in the long term, and the findings suggest that gains accruing to utilities involved in acquisitions are short term in nature. Bougatef & Korbi (2018) present the existence of two common determinants of intermediation margins in Islamic and conventional banking systems, and the degree of diversification permits banks to operate with lower margins and exploit the revenue from non-traditional activities to compensate the decrease in intermediation margin, and finally the degree of risk aversion is among the principal factors responsible for the increase of bank margins.

Bougatef & Korbi (2018) reveal that net profit margins of Islamic banks may be explained for the most part by risk aversion, inefficiency, diversification and economic conditions, and with regard to conventional banks, their margins depend positively on market concentration and risk aversion and negatively on specialization, diversification, inefficiency and liquidity. Bansal et al. (2018) reveal that interest expended interest earned (IEIE) and credit deposit ratio (CRDR) reduced the profitability of private banks in India. IEIE, CRDR and quick ratio (QR) reduced the profitability of public banks in India, while cash deposit ratio (CDR) and Advances to Loan Funds (ALF) increased the effectiveness of public banks, and under the total banks IEIE, CRDR reduced the profitability, on the other side, CDR, ALF and Total Debt to Owners Fund (TDOF) increased the profitability of total banks in India, and finally under the dependency of ROA, CRDR and TDOF reduced the return of private banks in India, while CDR, ALF and QR enhanced the profitability of private banks (Bansal et al., 2018).
Agrawal et al. (2018) found a significant interaction exists between the recruiter gender and profit margin variables in effect on days that it takes to fill an open position, and at lower job position profit margins, female recruiters were found to outperform their male counterparts, conversely, at higher job position profit margins, male recruiters appear to outperform female recruiters. Hyun (2017) investigates the effect of the 1997 Korean financial crisis on the trade credit behavior of Korean small and medium sized enterprises (SMEs) using a unique panel data set for the period 1994 to 1999 and uncover new evidence supporting the substitution and redistribution hypotheses, which contradicts earlier studies, specifically, the results show that liquid SMEs provided more trade credit to their client firms during the credit contraction, while financially constrained SMEs received more trade credit from their suppliers, further, evidence found that SMEs in financially distressed regions relied more on trade credit than their counterparts in financially healthier regions.

Chung et al. (2017) present that as China increases its size of economy, state-owned financial institutions, resource-focus firms (e.g. mining and petroleum) firms also rapidly increased its overall size, although the number is still small, privately owned Chinese global firms (e.g. Lenovo, Huawei, Zhejiang Geely Holding Group, Ping An Insurance) also are now listed as Global Fortune 500 firms, in contrast, Japanese firms that lost their global market positions steadily disappeared from Global Fortune 500 firms, and representative firms include Daiei, Mitsubishi Motor Company, and NEC. Gupta et al. (2017) found that firms operating in more competitive industries experienced significantly larger wealth declines upon revelation of the news of governance failure (backdating of stock option grants), and interpret the findings to suggest that the quality of corporate governance is less critical for firms operating in more competitive product markets since product market competition acts as an implicit substitute for the performance discipline imposed by high quality of corporate governance.

García-Sánchez et al. (2017) suggest that the presence of financial experts on audit committees is useful to reduce insolvency risk, supporting the monitoring advantage hypothesis of financial expertise, this relationship is stronger when banking sector regulation is weaker and also in banks with stronger policies against unethical practices, and these findings suggest that financial expertise substitutes regulation and complements ethical policies in reducing insolvency risk. Chan & Abdul-Aziz (2017) present that the investigation on the operating strategies of property development companies indicates that a number of common strategies adopted were; (i) to keep the leverage ratio low by raising equity to purchase development
land, (ii) to reduce the amount of interest paid by refinancing bank loans with lower interest bonds, commercial paper, or medium terms notes, (iii) to engage in joint ventures with landowners or government agencies, (iv) to focus on high growth areas of the Klang Valley and the Iskandar Region, (v) to offer high-end or luxury residential units with an attractive concept, (vi) to vertically integrate the development business, and finally (vii) to diversify into other non-related areas of business as a hedge against property development risks.

Ali & Konrad (2017) provide full support for the hypothesis that a gender-diverse top management team is positively associated with diversity and equality management (DEM systems), and the results provide partial support for the following hypotheses: DEM systems are positively associated with performance and this relationship is moderated by lower through middle management gender diversity; and DEM systems mediate the relationship between top management team gender diversity and performance. Sun et al. (2017) reveal that capital adequacy, management quality, and diversification determinants significantly explain the margins of both types of banks, Islamic and conventional banks, and also found evidence suggesting market quality matters, and finally this is an expected result since both banks operate, despite their inherent institutional differences, in a competitive environment to meet the core demands for funds, which are the same, for traditional lending and borrowing activities. Azeem Qureshi & Yousaf (2014) demonstrates that for the firms operating in Pakistan, having its own peculiar macroeconomic anomalies, pervasive credit risk, poor corporate governance, and inefficient legal and regulatory framework; leverage is the dominant factor in explaining total variation in profitability and adversely affecting it. Size, liquidity, market share and age have a positive impact on profitability in all models, except domestic sectors where size and liquidity have significant negative and insignificant positive relationship, respectively, and it finds an insignificant relationship of capital intensity and growth with the profitability (Azeem Qureshi & Yousaf, 2014).

Method

This research use a literature study (Artha & Jufri, 2021; Khairi et al., 2021; Snyder, 2019) and included 18 articles as a result.

Result and Discussion

The results are presented in table 1 below:
| Author(s)                | Variable(s)                                      | Result(s)                                                                 |
|-------------------------|--------------------------------------------------|---------------------------------------------------------------------------|
| Wang & Wu (2020)        | IPO underpricing                                 | NPM has no significant effect on IPO underpricing                         |
| Sofronas et al. (2020)  | Tobin’s Q                                        | NPM has positive significant effect on Tobin’s Q                           |
| Chaudhry et al. (2020)  | Audit Committee Chair (ACC) experiential expertise (ACCEE); ACC financial expertise (ACCFE); ACC monitoring expertise (ACCME); Nomination Committee Chair (NCC) human resource expertise (NCCHRE); NCC monitoring expertise (NCCME); NCC experiential expertise (NCCEE); firm size; firm value | ACCEE, NCCHRE, NCCME, firm size has no significant effects on NPM; ACCFE, ACCME, NCCEE, firm size have positive significant effects on NPM; board size has negative significant effect on NPM |
| Bourke et al. (2020)    | asset light strategies                           | asset light strategies has no significant effect on NPM                   |
| Alakent et al. (2020)   | corporate social responsibility (CSR)            | NPM has negative significant effect on CSR                                 |
| Weidman et al. (2019)   | return on equity (ROE)                           | NPM has positive                                                          |
| Authors            | Variables                          | Findings                                                                 |
|-------------------|------------------------------------|--------------------------------------------------------------------------|
| X. Wang et al. (2019) | account receivable, account payable | NPM has negative significant effects on account receivable and account payable |
| Tee (2019)        | total institutional investor (TII); local institutional investor (LII); foreign institutional investor (FII); shareholding by mutual funds, endowment, and government controlled funds (PRII) | TII, LII, PRII have positive significant effects on NPM; FII has negative significant effect on NPM |
| Sekhon & Kathuria (2020) | CSR                               | CSR has no significant effect on NPM                                      |
| Rahman et al. (2020) | advertising efficiency, advertising intensity | advertising efficiency has positive significant effect on NPM; advertising intensity has no significant effect on NPM |
| Mimouni et al. (2019) | sukuk                             | sukuk has negative significant effect on NPM                             |
| Hayat et al. (2020) | environmental performance          | NPM has positive significant effect on environmental performance          |
| Aydı̇n et al. (2020) | debt ratio, liquidity ratio, available seat kilometer, employee number, fleet size | debt ratio, liquidity ratio, available seat kilometer, have negative significant effects on NPM; employee number, fleet size have no |
The results above show the variables that associates with net profit margin (NPM). The results show there are no outside and macroeconomic variables that associate with NPM. Contrary with Ren et al. (2021) who revealed that covid-19 as macroeconomic variable affect NPM and Mucharreira et al. (2019) who revealed that tourism affect NPM in hotel industry.

### Conclusion

The results of the research show the variables that associates with net profit margin (NPM). This research contributes to the identification of variables that affect and affected by NPM. The limitation of this study is the variables above are inside variables. Future research should investigate about macroeconomic variables that associate with NPM.

| Study                          | Variable            | Relationship                      | Notes |
|--------------------------------|---------------------|-----------------------------------|-------|
| Zhou et al. (2019)             | research and development investment | NPM has negative significant effect on research and development investment |       |
| Killingsworth & Mehany (2018)  | gross profit        | NPM has positive significant effect on gross profit |       |
| Fu (2018)                      | fuel intensity      | fuel intensity has negative significant effect on NPM |       |
| Przychodzen & Przychodzen (2018) | sustainable innovations | NPM has positive significant effect on sustainable innovations |       |
| Nanda & Panda (2018)           | net exports         | net exports has positive significant effect on NPM |       |
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