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**PREDICTION OF FINANCIAL DISTRESS USING FINANCIAL PARAMETERS AND ALTMAN Z SCORE WITH
SPECIAL REFERENCE TO THE CASE OF SUZLON ENERGY LTD.**

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ABSTRACT

Financial Distress is a situation where, if any company is unable to pay off its short-term and long-term Liabilities. The main aim of the research undertaken is to find out whether company is in Financial Distress using 5 years' data for the company Suzlon Energy Ltd. Data collected on various financial parameters from the year 2014 till 2018. The method used is a case study method with specific company only. The current study used financial performance indicators viz Net Sales, Total Assets, Retained Earnings, Working Capital etc. The Altman Z score is used for analyzing the data and interpret the financial distress of the company. Financial statement analysis and various financial ratios are used for analysis. The research is based on secondary data and data is mainly collected from Bombay Stock Exchange website and annual reports published. The purpose for considering Suzlon Energy Ltd. for this research is due to its lot many news related to its high debt and NPAs. The findings suggest that the financial distress can be predicted from financial performance as well leads to pledging of shares by promoter.

KEYWORDS

Altman Z Score, BSE, Suzlon Energy Ltd., financial distress, promoters pledging.

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INTRODUCTION

Financial distress is a term in financial management which indicates a condition where company is unable to pay its creditors and lenders. The condition of financial distress is more likely when business is highly leveraged. Financial distress is more common just before a business declares bankruptcy. If the level of distress is high, the firm may be forced into immediate liquidation.

Financial distress usually refers to situation where the cash inflows of the firm are not sufficient to meet daily operational expenses. Often the financial distress comes with its own costs such as fees paid to lawyers and costs of extra interest paid for late payments. Financial distress is often a long term process and has an impact on capital structure, investment policies and performance of many firms even after the emergence of debt restructuring. Firms diversify their priority structure relative to its pre distress composition.

Financial distress is an individual, business or company's inability to generate enough revenue when there is too much debt. Predicting financial distress remains a significant area of focus for researchers due to its vital importance for the firms and stakeholders including investors, lenders and others. Financial Distress is a situation where, if any company is unable to pay off its short-term and long-term Liabilities.

ABOUT SUZLON ENERGY LTD.

Suzlon is world's leading renewable energy solutions provider offering a 360 – degree total solutions package to its customers that covers the entire spectrum of wind energy projects. Its revolutionizing and redefining the way sustainable energy sources are harnessed across the world. Present in 18 countries across Asia, Australia, Europe, Africa and America.

Suzlon is powering a greener tomorrow with its strong competencies in renewable energy systems. Suzlon Energy Ltd. is a wind turbine supplier based in Pune, India. It was formerly ranked by MAKE as the world's fifth largest wind turbine supplier. In 2014 the company dropped out of the Global top ten rankings due to extensive losses and inability to repay debts.

REVIEW OF LITERATURE

In the opinion of Baldwin and Mason (1983) "When a firms business deteriorates to the point where it cannot meet its financial obligations, the firm is said to have entered the state of financial distress"¹

As per H.Platt and M.Platt (2006) "Financial distress and bankruptcy are different. Financial distress is something that happens to companies as a consequence of operating decisions or external forces while bankruptcy is something that companies choose to do to protect their assets from creditors"²

In the opinion of Zaki, Bah and Rao "Financial distress differs from bankruptcy as it refers to a period when a borrower is unable to meet a payment obligation to lenders whereas, bankruptcy is an official declaration of a firm's financial state in which it may cease business activities or reorganize. When financial distress remains unresolved, it may lead to bankruptcy, but the at outcome is not a certainty"³

According to Platt H. and Platt M "Financial distress is defined as the late stage of organizational decline that precedes bankruptcy"⁴

As per research by Almwajeh "Bankruptcy prediction models or financial distress prediction models even though are widely popular their use in hospitals is limited"⁵

NEED/IMPORTANCE OF THE STUDY

The term financial distress or failure of companies is becoming a growing problem all over world. Financial distress is a situation when companies are unable to pay the debt and not able to pay their liabilities. So the question arises is predication of the companies likely to go bankrupt or in distress possible? Financial Distress is a situation where, if any company is unable to pay off its short-term and long-term Liabilities. Financial distress is a term in corporate finance used to indicate a condition when promises to creditors of a company are broken or honored with difficulty. If financial distress cannot be relieved, it can lead to bankruptcy. Financial distress is associated with costs to the company.

The financial distress of company has multifold impact. Many stakeholders stake at stake. Employees, Investors, Vendors all get affected by such situation. Financial distress prediction is very important from the point of risk management perspectives. If this prediction is possible it will be really good help even for the banks. Many banks are loaded with huge NPAs due to bankruptcy of the companies. Can this likelihood of the company getting bankrupt be predicted? The researcher has undertaken the research to know this possibility of prediction.

STATEMENT OF THE PROBLEM

Financial distress prediction has become significant due to its importance to the firms and all the stakeholders including investors, lenders etc. The continuance of financial distress for long term may lead to closure of firm. Early prediction of distress can prove to be warning for long term effects. Prediction of early financial can help avoid bankruptcy.

OBJECTIVES

The researcher has undertaken the research with following objectives:

1. To understand the conceptual background of financial distress.
2. To predict the Financial Distress using Altman’s Z Score
3. To suggest strategies for risk minimization.

RESEARCH METHODOLOGY

The research carried out is based on secondary data collected from various sources as research papers, news articles. The yearly annual reports and website of the company are the main sources of data. The method used is a **case study method** with specific company viz **Suzlon Energy Ltd.** For the undertaken research the Altman’s Z score model was used for knowing if the company is in distress or not.

Altman Z Score model for predicting bankruptcy

$$Z = 0.012X_1 + 0.014X_2 + 0.033X_3 + 0.006X_4 + 0.999X_5$$

X₁, X₂, X₃, X₄ are in percentage points.

X₁ = working capital / total assets

X₂ = retained earnings / total assets

X₃ = earnings before interest and taxes / total assets

X₄ = market value of equity / total liabilities

X₅ = sales / total assets

Interpretation of Z Value

Z > 2.99 Safe Zone

1.81 < Z < 2.99 Grey Zone

Z < 1.81 “Distress” Zone

TABLE 1

Independent Variable	Measurement	Dependent Variable	Measurement
Financial Distress	Altman Z Score	Financial Performance	Financial Ratios

RESULTS & DISCUSSION

TABLE 2

Name of Company	Financial Year	A=EBIT/Total Assets	B=Net Sales /Total Assets	C=Market Value of Equity / Total Liabilities	D=Working Capital / Total Assets	E = Retained Earnings / Total Assets	Z Value	Interpretation 1	Interpretation 2
Suzlon Energy Ltd	2017-18	0.01	0.48	0.32	0.25	0.06	0.84	Likelihood of bankruptcy is very high	Company is in DISTRESS
	2016-17	0.04	0.65	0.78	0.21	0.00	1.52	Likelihood of bankruptcy is very high	Company is in DISTRESS
	2015-16	0.18	0.53	1.71	0.17	0.03	2.32	Likely to go bankrupt within 2 years	CAUTION ZONE
	2014-15	0.08	0.14	0.56	0.31	0.15	0.89	Likelihood of bankruptcy is very high	Company is in DISTRESS
	2013-14	0.01	0.16	0.27	0.03	0.12	0.48	Likelihood of bankruptcy is very high	Company is in DISTRESS

The above table shows that the using financial ratios and Altman Z score value it is possible to predict if the company is in Financial Distress. If the Z score is monitored for regular frequency the likelihood of bankruptcy can well in advance predicted and can be avoided.

FINDINGS

Based on the values of Altman z Score it’s possible to predict whether the company has likelihood to go bankrupt and in turn have financial distress. Before investing or lending money to any company if this type of analysis can be done it will surely help the stakeholders to minimize their risk.

The major factors which are the reasons for the financial distress of the companies are the insufficient accounting practices, unrealistic budgeting and pricing, cash flow, poor debt management, low sales and high expenses.

RECOMMENDATIONS/SUGGESTIONS

If high debt or liabilities are the cause of financial distress, the company can undergo restructuring its debt. If any operational issues are the reason for the distress, the company can negotiate a payment holiday to its creditors and improve the operations to be able to clear the debt.

CONCLUSIONS

If financial distress cannot be relieved, it can lead to bankruptcy. Analyzing financial distress and taking adequate measures to avoid bankruptcy are crucial for the success of the organization. Financial distress can be predicted using Altman Z score and this prediction will help all the stakeholders to minimize the risks involved.

SCOPE FOR FURTHER RESEARCH

The undertaken research is a **case study** method based on data collected for specific company viz. **Suzlon Energy Ltd**. The data considered for undertaken research is for 5 years only. Further research can be done with some other company or it can have done with comparative analysis of many companies. Sector wise companies can be considered for study in future.

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Academically yours

Sd/-

Co-ordinator

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