

Analysis of Financial Health through Z score Model: A study of Sun Pharmaceuticals Ltd.

VICKY⁽¹⁾

SUNITA CHAUDHARY⁽²⁾

1. Research Scholar, Department of commerce MDU Rohtak.
2. Research Scholar, Department of Commerce, Banasthali Vidyapith (Rajasthan)

ABSTRACT:

Financial performance of the companies plays a vital role in the growth of the companies. Investors analysis the financial performance of the companies and make a decision regarding investments in the organization. Altman Z score model is a very useful tool to determining the financial performance of the companies. It shows the possibility of companies to conversion in distress companies. The present study seeks to analysis the financial performance of sun pharma and determined the company's position based on Z score model. The main reason behind to select Sun pharma were dramatically changes in the performance of the company since 2014. The study concluded that the company in distress zone and company sholld take neccessary action for rectifies it.

Key words: Z score, bankruptcy, financial health, financial distress.

INTRODUCTION

For the expansion of the business firm required to maintain adequate amounts for operating activities and other activities .The organizations also required using these funds in rational and efficient manner. These funds are used for working capital as well as capital budgeting decisions. In working capital management funds is used for purchasing of raw materials, salaries, wages etc. Whereas for capital budgeting decisions it is required to expand the capacity of the firm, acquisition of the fixed assets etc. Investors are provides the funds to the companies for getting positive return on their investments. But if the investors predict that companies will not provides the future return than they will not invest in the companies .As a results companies are unable to arrange the funds. So management needs to use funds in rational manner. Different stakeholders of the companies are analyzed the financial information and take decisions regarding companies .The analyses show the present as well as future performance of the companies which is useful for analysis the future prospect of the companies .Analysis of financial health companies is a part of financial analysis which shows the bankruptcy probabilities of the organization in near future or not .Bankruptcy refers to a situation which shows that companies not be able to pay its debts on time . As results, it reduced the employment opportunities, revenues, industrial growth etc. So the solvency positions of the company deeply affect the companies directly as well as stakeholders of the companies. If the bankruptcy available future then investors decision regarding their investments and management also take remedial action to reduce it.

REVIEW OF LITERATURE

Gopalkrishnan et al. (2016) explored the financial health of pharmaceutical industries by using Z score model. For the attainment of objective they collected data from eight pharma companies of five years from 2012 to 2016. They applied Z score model for analyzing the financial performance of pharma companies during the study period. They concluded that most of the firm in this sector perform well and some firm not perform well and they required to more attention for strengthen the financial health.

Kumar et al. (2016) explored the financial efficiency and liquidity position of Cipla Ltd. The objective of the study to analyze the trend of working capital of Cipla Ltd. The study used Cipla Ltd as a sample and the time period of the study was 14 years from 2000 to 2013. For attainment of the objectives study used some ratios like current ratio, working capital, operating profit margin etc. used. For analyzing the data panel regression, co-efficient of correlation, were used. The study concluded that liquidity position of Cipla Ltd is quite good and it would positive impact on profitability.

Objectives of the Study

1. To evaluate the financial health of the Sun Pharmaceuticals Ltd. by using Z score Model.
2. To suggest recommendations for future growth and development of the Sun Pharmaceuticals Ltd.

Research Methodology

The study used secondary data to determining the financial performance of Sun pharmaceutical Ltd. The time period of the study were two years from 2016-2018. The study mainly focused on Sun pharma due to unexpected changes since 2014. At present its shows the poor financial performance due to many factors. To determining the financial distress of company researcher applying the Altman Z score model.

The Description of the model as follows:

Model Explanation

$$Z = 1.2X_1 + 1.4X_2 + 3.3X_3 + 0.6X_4 + 1.0X_5$$

Where,

X_1 = Working capital/ total assets.

X_2 = Retained earnings / total assets.

X_3 = EBIT / total assets.

X_4 = Book value of equity / book value of total debts.

X_5 = Net sales divided by total assets

According to the model the following situations are creating:

1. $Z > 2.99$ - Safe Zone.
2. $1.81 > Z > 2.99$ – Grey Zone
3. $Z < 1.81$ – Distress Zone.

Analysis and Interpretation

Table Financial performance of Sun Pharma ltd.

Years	Working Capital	Retained Earnings	EBIT	Book Value of equity	Net Sales	Z Score
2016-17	-0.013	0.368	0.004	0.018	0.234	0.7888
2017-18	-0.015	0.331	0.008	0.016	0.234	0.7514

Above table shows the financial performance of the Sun pharma for the period of two years from 2016 to 2018. The above table implemented the Altman Z score model and find out the financial strengths of the company. The model used five ratios for indication of financial performance of the company. In year 2016-17 the working capital ratio to total assets is negative and in 2017-18 it is also negative. The retained earnings to total assets in both years are very low. EBIT to total assets ratio is also low in both years. Book value of equity to book value of the debt is also low. Net sales to total assets ratio is also low in both years. After using the above ratios in Z score model researcher find the Z score. In both years it is less than 1.81 and it means the company is in the distress Zone. As per the model the company will be not able to pay its debts after two years .So Company is required to focus on their management of various activities.

Conclusion

After the analysis the data of two years by using of Altman Z score model researcher found that the company is in the distress Zone and the company is required to take necessary action to improve the financial performance of the company. The company is also required to analysis the factors which are responsible for this conditions. In brief research conclude that the financial health of the company is very poor and it is belongs to the distress company based on Z score model.

Suggestions for improving the financial health

After concluding the study based on Z score model the research suggest to the company for try to find out the factors which are responsible for that position and after that analysis them . The researcher also suggests analyzing the various financial decisions like merger, acquisition and capital mix etc. The management should take necessary steps to improve the financial performance of the company.

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