INDIAN INSTITUTE OF MANAGEMENT KOZHIKODE

Case Study

IIMK/CS/214/FIN/2023/11

March 2023

Fresh n Fresh Mart Limited: Predicting Corporate Default

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Fresh n Fresh Mart Limited: Predicting Corporate Default

by Sudershan Kuntluru and Rachappa Shette

Fresh n Fresh Mart Limited (FFM Ltd):

Mr Kandarp Bhai, a passionate business person, is the chairperson of FFM Ltd. He always believes in simple living high thinking. He started a Fresh n Fresh provisional store in year 2003 near Vastrapur Lake, Ahmedabad, catering to the needs of local residents. The business was doing good. But, personally, he was not contented with the progress. He was working on to scale up the business to offer fresh and variety of household items across the various locations in India at the best affordable prices. He renamed the business as 'Fresh n Fresh Mart Limited (FFM Ltd)' in year 2013 and started operations in a big way across the various cities in India. Both greenfield and brownfield strategies adopted to accelerate the progress.

By the year 2019, the total assets in balance sheet stands at 4,633 crores with a total revenue of Rs 5,416 crores. The net profit for the year 2019 is reported as Rs 145 cores. As on March 31, 2019 (2018) the market capitalization was Rs 1,492 (Rs 1,224) crores. See the Exhibit-1 for condensed financial statements of FFM Ltd. For the chairperson, the drive for further growth is on and continuously interacts with all the stakeholders. The leadership team is called for a meeting to discuss the future plans. In this process, the financial health of the company might get impacted.

You, as an intern at RARE credit rating organization, asked to track the retail industry. Your reporting manager at RARE, having some internal information, asked you to predict corporate default that is evaluate the chances of 'FFM Ltd.' going bankrupt in near future. While thinking on this, you quickly recall one of the model called "Altman's Z-score" discussed by your professor in Financial Reporting & Analysis class. See Appendix-1 presents the summary of your class notes. You learned that the Z - score can be computed using the excel sheet.

Questions:

1. You are required to compute select liquidity, efficiency, profitability and solvency ratios and comment on the financial health of FFM Ltd.
2. You are required to compute the Altman's Z-score for FFM Ltd. for both the years from the financial statements given in Exhibit-1.
3. Explain the merits and demerits of Altman Z-score for effective decision-making.
4. As a CEO of FFM Ltd, what are the steps do you take to improve the existing financial health of the company.

Exhibit-1: Financial Statements of Fresh n Fresh Mart Limited

Balance Sheet

			(Rs in crore)
	Note	31.03.2019	31.03.2018
Assets			
Non-Current Assets			
PPE		1,223	892
Capital WIP		157	290
Intangible assets		5	8
Financial assets		382	252
other non-current assets		102	77
Total Non-Current Assets		*1,869*	*1,519*
Current Assets			
Inventories		1,976	1,452
Accounts receivables		195	162
Other current assets		592	358
Total current assets		*2,763*	*1,972*
Total		**4,632**	**3,491**
Equity and Liabilities			
Equity share capital		39	38
Other equity		1,608	1,356
Total equity		*1,647*	1,394
Non-current liabilities		*667*	*587*
Current liabilities			
Trade payable		1,669	1,293
Other current liabilities		649	217
Total current liabilities		*2,318*	*1,510*
Total		**4,632**	**3,491**

Source: Annual Report of the company

Profit & Loss Statement *(Rs in crores)*

	Note	31.03.2019	31.03.2018
Revenue			
Income from operations		5,377	4,219
other income		39	33
Total Revenue		*5,416*	*4,252*
Expenses			
manufacturing cost		3,459	2,651
employee costs		297	243
finance costs		104	95
Depre. & amortisation expense		197	149
other expenses		1,160	959
Total Expenses		*5,217*	*4,097*
Profit Before Tax		*199*	*155*
tax expenses		54	45
Profit for the year		**145**	**110**

Source: Annual Report of the company

Appendix 1: Z-score model computation:

The below equation is proposed to predict the chances of corporate default or possibility of becoming bankruptcy or non-bankruptcy company.

Altman Z - score = 1.2 I + 1.4 II + 3.3 III + 0.6 IV + 1.0 V

Where:

I = WC/TA
II = RP/TA
III = PBIT/TA
IV = MVE/TL
V = Sales/TA

Where: WC= working capital; TA=total assets; RP=reinvested profits; PBIT=profit before interest and taxes; MVE=market value of equity; TL=total liabilities

The Z - score findings interpreted for chances of bankruptcy are

1.80 & below	Most likely
1.81 - 2.7	High
2.8 - 2.9	Possible
3.0 & above	Unlikely

Reference:

1. https://doi.org/10.2307/2978933

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