# ASSESSMENT OF THE FINANCIAL CONDITION OF ENTERPRISES THE CASE OF BUSINESS ENTERPRISES OF UZBEKISTAN

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## ABSTRACT

*The amount of enterprises, which are undergoing bankruptcy, is increasing around the world. Therefore, the problem of financial condition and bankruptcy risk assessment of companies are quite topical. By comparing actual indicators and standard values, the financial condition of companies can be evaluated. Bankruptcy prediction is important to the various stakeholders of the company as well as the society on the whole. The purpose of the research is to study financial condition and the suitability of major bankruptcy prediction model by applying them to companies in Uzbekistan. The research shall analyze the financial statements and market data of the companies by using Enyi's model of relative solvency.*

**KEY WORDS:** *bankruptcy risk, Enyi's relative solvency model, financial condition, liquidity*

## INTRODUCTION
### Analysis of the problem

In recent years, the financial stability of enterprises has become an important task and issue for enterprise managers and financial analysts. In a market economy, the crisis of enterprises is one of the most common. In the context of financial and economic instability in the activities of enterprises, they encourage property owners and investors to make important decisions on the situation. Otherwise, businesses will gradually face a crisis. The most important issue in the activities of enterprises in a free economy is the assessment of business efficiency, as well as the analysis of their financial condition. Accurate assessment of the financial condition of enterprises is also an important factor in ensuring macro-level stability. This can only be known by analyzing the activities of enterprises on the basis of formally prepared and published financial statements. Therefore, the constant detection and monitoring of the risk of bankruptcy of enterprises is a decisive factor not only for the future activities of these enterprises, but also for the economy of this country.

According to our research, the assessment of the financial condition is important for Uzbek businesses and organizations, as businesses in Uzbekistan play a special role in creating jobs and stimulating economic growth. In this regard, the need for analysis of financial transactions in determining the financial condition, solvency and financial stability of each enterprise is growing not only in Uzbekistan but also around the world.

According to Stat.uz (2020), the share of business and entrepreneurship in GDP in Uzbekistan was 53.9%. This shows that the role of organizations engaged in business activities in the country is high. Thousands of new business enterprises start operating in Uzbekistan every year. However, at the same time, the number of enterprises that are going bankrupt and ceased their operations due to deteriorating financial situation is growing significantly (Picture 1). This indicates that in most of business organizations in Uzbekistan financial management are not well organized and there are shortcomings in the process of early detection and assessment of financial condition and the implementation of the necessary measures.
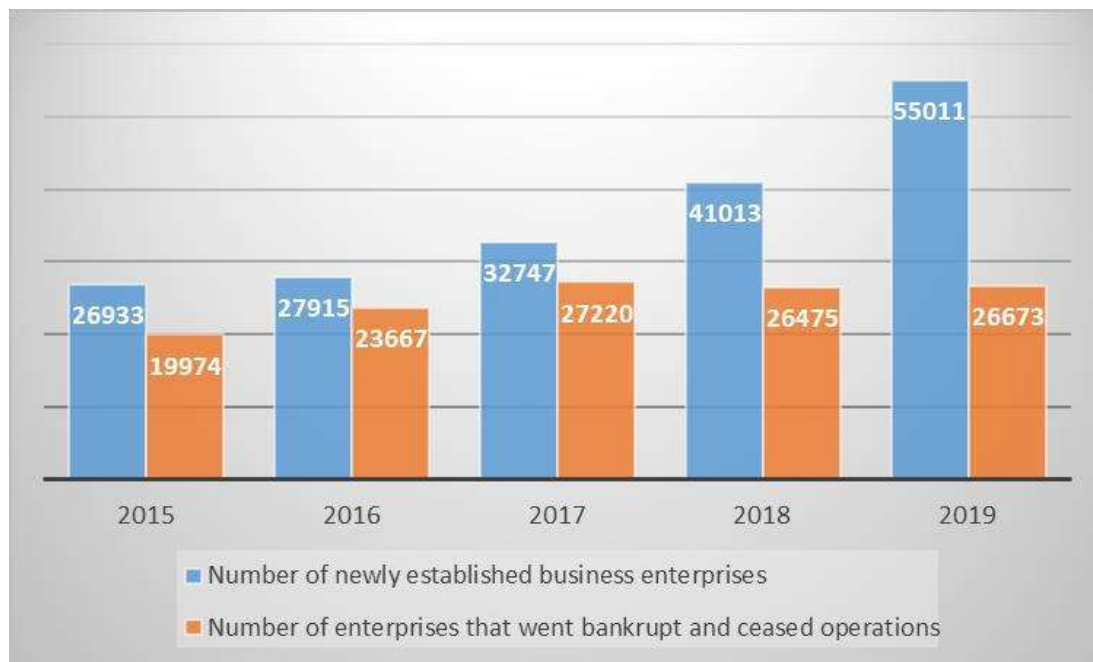
**Picture 1. Dynamics of newly established and closed business enterprises in Uzbekistan in 2015-2019**

*Source: www.stat.uz*

## LITERATURE REVIEW

In the words of Enyi (2005), business is as strong as a non-heavy capital base, as dynamic and vital as liquidity and management decisions, such as working capital. One of the major challenges facing the management of many corporations over the last decade is to ensure financial stability and avoid bankruptcy. According to Enyi, Patrick Enyi (2010), the bankruptcy of General Motors, Lehman Brothers and Woolworths, the crisis of small and medium business survival in developed and emerging economies are the consequences of this misguided or inefficient business performance analysis. According to Lyon (2010), the main question that has plagued business leaders over the past few years is how to better support the business, achieve financial stability, and avoid bankruptcy. The solution to this problem can be solved through the need to effectively organize the methods and mechanisms of preliminary assessment of the financial condition of enterprises Lyon (2010).

Analysis of the financial condition of enterprises has become a major topic after some financial crises. In the past, many studies have been conducted on the financial condition of organizations and the effectiveness of bankruptcy analysis. There have been many attempts to find the best prediction model, but few have been successful. Harlan Platt and Marjorie Platt (2008) studied the financial problems of firms on three different continents. They compared and analyzed the paths and key factors leading to financial difficulties in all three geographic regions. Their research has shown that lending practices, financial management skills, and failure to predict the financial condition of firms have led companies to suspend operations. A review of statistical and theoretical financial concentration forecasting models has been proposed by Scott (1981), but it is very limited in terms of scope and can be considered obsolete in the current context. Narendar V. Rao et. al (2013) in his paper investigated the financial health of industry companies in India based on Z-score analysis. It reveals that Indian industry enterprises have been financial healthy. Al-Rawi, Kiani and Vedd (2018) used the Altman Z-score analysis to predict a firm's insolvency. They have remarked that the firm has increased its debt and migth be facing bankruptcy in the near future. Mizan, Amin, and Rahman (2011) conducted a study for the prediction of financial condition of the business companies in Bangladesh. Their study reveals some valuable findings like, two firms have been found financially sound having no bankruptcy possibility in the near future and other companies have been found to be unsatisfactory and they have a significant likelihood of facing financial crisis in the near future.

## METHODOLOGY

There are many models to analyze and predict the financial condition and firm's bankruptcy risk. Being presented in 2005, Enyi's relative solvency model is new, but famous and effective. It is different from models both in terms of mathematical expression and approach to the identifying financial condition of the enterprises. In this research we analyze and assess the financial condition of the selected state business enterprises by exploiting Enyi's relative solvency model.

**A CASE STUDY**
**Analysis and Results**

**According to Enyi,** the model provides a solvency test which depends on the firm's ability to recover costs and make profit. There are two basic indicators of the model: **OBEP** (operational break-even point) and **RSR** (relative solvency ratio). The initial step of model is begun with calculating the mark-up ratio (**MUR**), which indicates the ability of a company management to recover the costs and maximize the profit.

$$MUR = PBT/TOC$$

where **PBT** – profit before tax, **TOC** – total operating cost.

The second step is calculation of break-even point (**OBEP**). At OBEP, the firm has achieved enough contribution from operations to cover all the attributable costs, a point beyond which profits may be noted.

$$OBEP = (1+MUR)/2*MUR$$

Next step is the measuring the required volume of working capital (working capital required, **WCR**) which is central to operation of the company to sustain operational break even.

$$WCR = TOC*OBEP$$

One of the most important indicator is relative solvency ratio (**RSR**). RSR measures the liquidity of a company.

$$RSR = AWC/WCR$$

Here, **AWC** is available working capital which is the difference between current assets and current liabilities of a company.

## ANALYSIS AND RESULTS

**Table 1. The necessary financial indicators of "Kvarts" and "UzKimyosanoat" Joint-stock business companies in 2019, (all financial indicators are measured in USD)**

| Companies | PBT | TOC | CA | CL |
|---|---|---|---|---|
| "Kvarts" JSC | 36700709 | 23821288 | 96474396 | 11479267 |
| "Uzkimyosanoat" JSC | 12730780 | 13344380 | 18363152 | 13901750 |

*Source: www.openinfo.uz*

Collecting necessary data from balance sheet and income statement of these enterprises we can calculate financial condtion level by using Enyi's model.

**Table 2. Necessary indicators of selected companies**

| Companies | MUR | OBEP | WCR | AWC | RSR |
|---|---|---|---|---|---|
| "Kvarts" JSC | 1.54 | 0.824 | 196228741.3 | 84995129 | 4.33 |
| "Uzkimyosanoat" JSC | 0,95 | 1,02 | 13665967,2 | 4461402 | 0,33 |

*Source: Author's calculations from using the data*

**In Enyi's model, scale of RSR has exact criterion of financial distress level. Companies with 0.01 – 0.25 RSR are insolvent or high probability of bankruptcy. RSR coefficient between 0.26 and 0.99 is classified as a company with poor financial condition. 1 and above in RSR indicates the absolute financial health.**

Using the calculated data in Table 2, we can conclude all information that which is given in Table 3:

**Table 3. Financial condition status of selected business companies**

| Companies | RSR | Financial condition level | Probability of bankruptcy |
|---|---|---|---|
| "Kvarts" JSC | 4.33 | Healthy | Very low |
| "Uzkimyosanoat" JSC | 0.33 | Poor financial condition | Middle |

After calculation process results suggests that financial condition level and bankruptcy risk of selected companies in Uzbekistan are different. Enyi's relative solvency ratio shows us that "Kvarts" JSC has a very good financial condition. It doesn't have any problem with financial default and liquidity problem nowadays. However, "UzKimyosanoat" JSC has experienced that it has problem with financial management and liquidity. That's why the company may face difficulties to meet their obligations in time and in terms of its financial problems.

## CONCLUSION RECOMMENDATIONS

Analysis and assessment of financial condition and financial crises management plays a great role in business companies and financial development. The fundamental financial health of a business firm is the main concern for the stakeholders. On the basis of the financial soundness, they take a decision regarding their possible involvement with a particular firm. In this regard, the Enyi's relative solvency model is one of the best measurements that can shape the decision of the stakeholders.

"Uzkimyosanoat" company needs to increase its working capital and limit its permanent costs. This means that the company's balance shows that the proportion of fixed assets are considerable high, so that more proportion of the profits of the company is paid to its internal cost.(for example: for depreciation charges). Therefore, the enterprise should reduce the number of its fixed assets (or should use new technology) and increase the amount of working capital.

In general, to reduce the likelihood of bankruptcy risk:

▫ Increase the share of working capital in the total assets and make them from their own resources

▫ The corporation should hold an optimal ratio between borrowing and equity resources.

▫ The companies should control the receivable and payables accounts to ensure an optimal balance during the financial year.

Overall, the findings of the research can be useful for the managers to take financial decision, the stockholders to choose investment options and others whose their interest in the concern business companies of the country.

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