

PREDICTING CORPORATE FINANCIAL DISTRESS IN KENYA:

A survey of the non-financial institutions listed in Nairobi Security
Exchange

JEDIDAH MWITI



A Thesis Submitted in Partial Fulfillment for the award of Masters of
Science in Finance and Investment Degree of Kenya Methodist University.

June, 2013

ABSTRACT

The Altman Z-score is a linear combination of accounting ratios, weighted by coefficients, used to predict corporate financial distress. The economic consequence of corporate failure is enormous especially for the stakeholders of public-held companies. Prior to a corporate failure, a firm's financial status is frequently in distress. Consequently, a method of determining corporate financial distress is clearly a matter of considerable interest to investors, creditors, employees and other stakeholders. This study assessed whether Edward Altman's revised financial distress prediction model of 1993 can be useful in predicting business failure in Kenya. The population of this study was composed of non-financial institutions listed in the Nairobi Securities exchange 2006 to 2011. Eight firms were selected for the study: four firms that continue to be listed and four firms that were delisted in Nairobi securities exchange. The source of Secondary data was obtained from financial reports of those listed and delisted companies at the Nairobi Securities Exchange and the Capital Markets Authority. It adopted a descriptive research design with financial data being gathered from the financial statements of non-financial firms listed in the Nairobi Securities Exchange. Data was analyzed using multiple linear regression method. This is a statistical technique for estimating the relationships among variables. More specifically, regression analysis helps one understand how the typical value of the dependent variable changes when any one of the independent variables is varied, while the other independent variables are held. Multiple linear regression was used for forecasting and prediction and also in determining which among the independent variables are related to the dependent variable and to explore the forms of these relationships. Liquidity and leverage were found to have no significant influence in determining corporate financial distress. Growth and profitability, on the other hand, had a significant influence. The Altman Z score model (a multivariate approach) was found to be a significant distress prediction model. This study evaluated the applicability of the Altman's revised model of 1993 in the prediction of the financial distress in Kenya, more specifically in non-financial institutions. This study will particularly be important for the emerging market investors.