ABSTRACT

“Wilful Default” gained attention of Government of India (GoI), Reserve Bank of India (RBI) and credit institutions since 1986 with an objective of enforcing credit discipline. “Wilful defaulters” are those who have the capacity to pay, but yet are delinquent. India is the only country which discerns between a “defaulter” and a “wilful defaulter”. Presently, India is facing a huge challenge with regard to the “stressed assets” which has reached an unacceptable level of more than 12% of the gross advances. These assets have brought sharp dip to the profitability of the credit institutions and eroded their capital base significantly. This study is an initiative to take up an empirical investigation of the suit-filed wilful defaulters’ data (SF_WD) in India.

In this study, Logistic Regression (LR) and Discriminant Analysis (DA) has provided evidence as early warning models that best discriminate Wilfully Defaulted Companies (WDC) with that of the Non-defaulted Companies (NDC). LR is able to classify WDC with an accuracy of 73.1% and NDC with 99.7%. Robustness check carried out with DA provided accuracy of 76.9% for WDC and 98.7% for NDC. The study has investigated empirically utility of nine key financial indicators that could help mitigate credit risk and improve information on the probability of WDs. These variables are statistically significant at 6-1% and have the ability to increase the accuracy of WDs prediction model. They possess high discriminating and predicting power. Result of this prediction model with introduction of three cash flow variables on diversion & siphoning, has contributed positively and substantially increased the performance of the existing financial distress prediction model, for Indian corporates. It establishes the fact that the fund flow variables are better indicators of wilful defaults than the annual static variables. This study has employed a wider, ex-ante approach to detect early stages of WDs with a high degree of reliability. It is able to classify with an accuracy of more than 70% the likelihood of WD in the next 2-3 years. This could avert the high costs associated with identification, declaration and legal recourse undertaken by the credit institutions.

The relevance of this study on wilful defaults at this juncture is very crucial for the credit risk management of the financial institutions in India. The findings of this study would help all the stakeholders in resolution of the stressed assets, lessen the knowledge gap and widen the arena of information in respect of wilful defaults in India.

Key Words: Corporate Defaults, Suit-filed Wilful Defaulters, Credit Risk Management, India, Default prediction, logistic model.