European Journal of Business and Management www.iiste.org
ISSN 2222-1905 (Paper) ISSN 2222-2839 (Online)
Vol.8, No.13, 2016

The Role of External and Internal Factors in the Accuracy of Predicting Financial Distress

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Abstract
The purpose of this paper is to predict financial distress explored how the proposed by experts. As we know that the Financial Distress is an early predictor in assessing the financial performance of the company, for this prediction in need of external and internal analysis of the company.
The methodology of this research is the study of literature and secondary data. This paper is expected to provide a comprehensive picture of the company's financial performance through the prediction of financial distress that has been widely used some previous researchers.
The results of this study will be a contribution to the development of literature and provide a comparison of the application of financial distress prediction model that has been done so create a model of financial distress research using external and internal analysis. The results of this study will also provide an explanation that there has been no study of financial distress by using external and internal factors simultaneously and integrated.
Keywords: *financial, distress, performance, company, external, internal factors*

1. Introduction

Financial distress is a condition in which the company faced financial difficulties Financial distress problems occur when the company can not meet its obligations, especially in terms of debt payments (Ross, et al, 1999). Financial distress is the stage of the financial downturn that occurred prior to the bankruptcy or liquidation. If this is not resolved soon will have a major impact on companies such as loss of confidence of stakeholders, and even the company will undergo bankruptcy (Plat and Plat., 2002). So important to analyze the condition of a company is in a healthy state or experiencing financial difficulties (financial distress), so a lot of research done to analyze observing and researching about the company's financial performance Analysis of the financial statements can be one tool to predict financial distress (Rayenda, 2007). Through the financial statements of financial ratios can predict whether or not the financial distress. Many factors led to the bankruptcy of the company, in principle, can be classified into 2 (two), namely internal and external factors. Internal factors are the causes that arise from the company include financial and non-financial factors. The reasons for the details concerning the financial field, namely; a) the existence of debt is too large so as to provide a heavy burden for the company remains; b) the existence of short-term liabilities that are too big in the assets lancer; c) the slow collection of accounts receivable or the number of bad-debt. ; d) errors in dividend policy; e) insufficient funds shrinkage. While the Non Financial is; a) There is an error on the founders, among others, the error in the selection of the company's position, the error in the determination of the resulting product, the error in the determination of the company; b) The organizational structure of the company is not good; c) errors in the selection of corporate leaders .; d) the existence of managerial incompetence, namely errors in menerapan operational policies, excessive expansion.

External factors are factors that are beyond the control of the company and outside the company, among others, the intense competition, reduced demand for the products produced, the lower the price changes in the macro economy as well as inflation, SBI interest rate and balance of payments.

The existence of the shareholders and the management role is essential in determining the profits that will be obtained. This means that every manufacturing company is required to be able to cope with the situation so that it can perform management functions with good management in order to be ahead of the competition (Noegler, 2006), A manager must competence in taking decisions and should carefully consider the nature and cost of of the source of funds that will be selected, since each source of these funds have different financial consequences. Meanwhile, when the company decided to obtain additional funds on activities, necessary preliminary analysis whether the company is in good health or in financial distress, the companies need to analyze internal and external.

Dun & Brodsteet (1991) describes the factors that cause business failure in the form of financial factors, factors of experience, negligence, disaster and fraud, corporate governance and macroeconomic factors.

Platt and Platt (2002), states that when a decline in the financial condition continuously, the company is experiencing financial distress is a condition prior to the bankruptcy, which means the failure of a business, According to Brigham and Daves (2003), financial difficulties occur over a series of errors, decision-making less precise and weaknesses interconnected to contribute directly or indirectly to the management and supervision of a lack of effort the company's financial condition resulting in less use in accordance with what is needed.

According Wruck (1990) when operating cash flows are not sufficient to meet its current liabilities such as accounts payable or interest costs, the company in financial difficulty or in financial distress call. Financial distress can occur from the difficulties of liquidation (short-term), which is the lightest financial distress to the declaration of bankruptcy, which is the most severe financial distress (Brahmin, 2007). To minimize the occurrence of bankruptcy of the company, management must monitor the financial condition and financial statement analysis (Ramadhani and Lukviamrman, 2009). Financial statement analysis is an important tool to obtain information about the company's financial condition. Financial analysis has two main tools that can be used are: analysis of the ratio (ratio analysis) and analysis of cash flow (cash flow analysis) (Palepu and Healy, 2008: 5-1) The second is an analytical tool used by management to menanalisis company's financial condition, if the financial condition of decreased financial management should be careful because these conditions can lead to financial distress.

Much research has been done in analyzing the influence of financial factors which often also called the fundamentals of the financial distress, some studies use financial ratios to predict financial distress of a company include Altman (1968) with Multiple Diskriminant Analysis, Altman et al, (1977) using financial ratios such as earnings before interest and taxes / total assets, market value of equity / book value of debt, retained earnings / total assets, working capital / total assets, sales / total assets (Altman et al, 1995). So even Zavgren (1983), using financial ratios well in predicting financial distress company, the ratio used in the form of Average inventories / net sales, Average recievable / average inventories, Long-term debt / (total assets - short-term debt, net sales / (fixed assets + working capital, Operational earnings / (total assets - Short-term debt, Quick assets / current debts, Quick assets / total assets (Zavgren, 1985). Deakin (1972) using Cash / current debts, Cash / sales, cash / total assets Cash flow / total debts, Current assets / current debts, Current assets / sales, Current assets / total assets, net income / total assets, Quick assets / current debts, Quick assets / sales, Quick assets / total assets, Working capital / total assets, Working Cpital / Sales, Total Debt / Total assetss (Deakin 1977). While Oldson (1980), using financial ratios such Change in income / sum of the absolute value of net income for two years, Current debts / current assets, Log (total assets, / GNP price index level Net income / total assets, Owners' equity, positive or negative, Positive or negative earnings, Working capital / total assets, total debt / total assets (Zahra Poorzamani1, Azita Jahanshad 2013) in line with researchers - peneliti the Brahmins (2007), Alifiah, et al (2012), Almilia and Kritijadi (2003), and Platt and Platt (2002), also using a variable in predicting the company's financial ratios.

Although the analysis of the usual symptoms of bankruptcy by using financial ratio analysis, but some researchers tried to analyze the use of the study on reputation management, actually study this theory is the upper echelon theory put forward by Hamrick and Moson (1984) that the characteristics possessed by top management (Top Management Team) has a direct influence on the performance of the company as a whole, the characteristics in the form of reputation management intent owned by top management. This theory is supported by D'Aveni (1990), that the reputation management has influence in bringing the company out of crisis, management has a good reputation will have a good financial planning strategy anyway. Reputation manjemen peak is social capital owned by manajamen peak with a certificate of expertise in a particular field, the background of which are owned and activities of managers in a particular field (board membership). Hamrick and mason (1984) mengatkan that social capital dimikili by top management can affect creditors in the event of negotiations on corporate debt or influence investors in making investment decisions.

Andrade and Kaplan (1977) and Asquith et al, (1994) also agree about the lack of conversation manager manages the company will affect the ability of managers to manage the accuracy of the financial strategy and choice of profitable investment projects (under-investment problem). Kor (2003) also states that the reputation management has positive influence on financial performance. A lot of support for this esellon Upper tori like Juan and Lee (2011) Kuersten and linden (2011), Ongen et al, (2011) stated that they affect the company's reputation management. Research management and company reputation is built on a variety of characteristics ranging from social responsibility, human resource practices are good and honest financial reporting so as to create a healthy company (Becchetti et al., 2007; Desai et al., 2006; Chum, 2005 ; Chalmers and Godfrey, 2004; Cox et al., 2004, Herrington, 2003; Weaver et al., 1999; Fambrun and Shanley, 1990; Bhagat and Black, 2002) examined the link between the ability of managers to manage risk with corporate governance proksinya is reputation management, they found that the audit committee, and directors who have the education and knowledge related to financial management is able to hedge better than those who did not have the education and knowledge in the field of financial management. While other studies have different opinions about the upper echelon theory before, namely research and Sumiyana Aini (2008), Gatot Nazir Ahmad (2014) in his research found that manajmen reputation is measured with an educational background as well as directors and komisasris background and work experience has a negative relationship with financial distress.

Assessment morbidly regardless reputation management with pengeloalaan peneilaian against the company itself, with a reputation for good management will affect the company's financial management which will affect also the value of the company as a whole, this is in accordance with the opinion of Niksokelainen and Weight (2007) states that the reputation good management reflects the corporate governance (Coporate Governance) are good also.

Agency theory (Jensen and Meckling (1976) is due to the asymmetry of information that resulted in a gap between managers and owners of companies that allow moral hazard, so there will be a cost agency, the condition that caused the company to choose external sources (debt and shares) (Myers and Majluf, 1984) Asimerti information occurs because the management has more information than the shareholders. As such, the management may think that the stock price is currently overvalued (too expensive) so that management will issue new shares at a price that is more expensive than it should be. Then between debt holders and shareholders. The shareholders will control the manager through the bonding mechanism and controlling debt holders while controlling shareholder with a legal bond called ovenant.

From the point of view of the theory of accounting, earnings management is determined by the motivation of corporate managers. Different motivations will produce a different amount of earnings management, such as between a manager who also serves as shareholders and managers are not as shareholders. This is in accordance with the system of management of the company in two criteria: (1) the company is led by the manager and the owner (owner-manager) (2) The company is led by managers and non-owners (non-owner-manager).

Two criteria will influence policy and decision-making to the accounting method on ownership by management tends to affect earnings management action (Boediono, 2005), but the management of the company also affect the value of the company. In cooperate governance (GCG) is a set of processes, customs, policies, rules, and institutions that affect the direction, management, and control of a company or corporation. corporate governance also includes the relationships among stakeholders (stakeholders) involved and destination management companies. The main parties in the governance of the company are the shareholders, management, and board of directors. Other stakeholders including employees, suppliers, customers, banks and other creditors, regulators, the environment, and the wider community.

Corporate governance is a subject that has many aspects. One of the main topics in corporate governance is a matter of accountability and responsibility mandate, in particular the implementation of guidelines and mechanisms to ensure good behavior and protect the interests of shareholders.

The problem arises because the corporate Governace the separation between ownership and control of the company. Corporate governance is needed to reduce the agency problem between owners and managers (Macey and O'Hara, 2003).

In agency theory to explain (Jensen and Meckling (1976) that the management will make a decision to increase the size of the company through investment in order for them to enjoy the compensation based on the amount of assets they manage, meaning that management will make business decisions that benefit their position because they are in possession of information which is more than owners. This condition according to which said Eisenhardt, 1989) that there are three basic assumptions of human nature in order to explain the agency theory, namely: (1) humans are generally selfish, (2) humans have limited thinking about the future perception, and (3) humans always avoid risks (Eisenhardt, 1989). Based on the assumption that human nature as human managers will most likely act on opportunistic nature, namely prioritizing personal interests (Harris, 2004).

The power to manage the company derived from ownership and the owner should be able to run its power in accordance with the value of their investments (Sukamulja, 2004), managerial ownership and institutional ownership are two main corporate governance mechanisms that help control agency problems. Because often Controlling shareholder and management control decisions are taken, the greater the proportion of ownership in the company management, the management tends to be more active in the interests of shareholders in particular is himself. The number of large managerial stock ownership should have a higher performance, because the agency cost reduced. Stiglitz, 1985; Shleiffer and Vishny, 1986 saying that cooperate to improve governance is to have one or more large shareholders and Vishny, 1998 found that there is a big influence of managerial ownership on firm performance.

Based on the research results Emrinaldi (2007), that with the increase in managerial ownership it will be able to encourage lower potential financial difficulties. In line with the opinion of Hanifa, Purwanto (2013), also conducted research whose results stating the results of descriptive statistics indicate that the average institutional ownership in distressed financial firms are smaller than the average non-financial institutional ownership in distressed firms.

Besides the internal factors mentioned above, there are external factors that influence the occurrence of financial distress, namely macroeconomic factors. Many companies are experiencing performance degradation caused by macroeconomic conditions. Subrime subprime crisis (2008), the US led to rising tinggkat SBI rate which increased deposits, which in turn results in a high interest rate credit, so investing in a company be decreased. Domestic investment decreased resulting in increased reliance on domestic business overseas investors, which means that an increase in the current flow of dollars into the country. The decline of the rupiah against the US dollar will lead to inflation, rising inflation is a relatively negative signal for investors, high inflation caused a decline in the profitability of a company that will reduce the distribution of dividends and causing public confidence to invest will be reduced, this will have an impact on funding activities of the company which will eventually happen lambant financial distress and ended in bankruptcy company

Research on the impact of macro-economic changes in the company carried out by Nam et al, (2008) compared the accuracy of prediction of bankruptcy in companies listed on the Korea Stock Exchange in the event of a crisis of 2008. Finding that the macro-economic variables showed superior performance showing signs of financial distress.

Foster (1986), lays out four things that encourage ratio analysis, namely: (1) control the magnitude of the effect of the differences between companies or between time, (2) makes the data more statistical tools to meet the assumptions used, (3) investigating related theories with financial ratios, and (4) examine the empirical relationship between financial ratios and estimates or predictions yariabel- certain variables (financial distress).

Based on the theory and the gap of the above phenomenon, this study examines the related financial distress isue manufacturing company in Indonesia, which is a fundamental influence on the profitability of financial distress, the influence of the educational background of directors and commissioners (EDU), pengalman work toward financial distress, the effect of magnitude Ownership to financial distrenss and Inflation Effect on financial distress.

The first research issue is a fundamental influence on the financial distress
Many studies have been conducted to analyze the influence of financial factors which often also called the fundamental factors, some studies use financial ratios to predict financial distress of a company include Altman (1968) in his research shows that the financial ratios can be made use of for predict the failure or bankruptcy of a company with bankruptcy prediction accuracy rate of 94% and 95% correct in his research, and Platt and Platt (2002), also using a variable in predicting the company's financial ratios.

The second issue in this study is the use of internal non-financial assessment form upper echelon theory with the study of reputation management by measuring the educational background of Directors (Pend) and background work experience Directors (PENGL).

The third issue in this research is to do a study of corporate governance through the Effect of Managerial Ownership on the prediction of financial distress. There are important structures in corporate governance including Parker et al (2005) says that the replacement of the company's leadership, ownership by the managerial and pihal internal or external (blockholder) must have a minimum of 5% of outstanding shares. Morck et al. (1988) find evidence that Tobin's Q (enterprise value) increases and then decreases in line with the increase in managerial ownership.

Issues to four in this study is how the external factors as causes of financial distress. Bernhart and Rosenstein 1998 expressed an external mechanism such as the market can control the company in addressing the company's performance. Francis & Desai (2005) agreed that the life cycle of the company, financial performance degradation may occur due to internal and external factors and Sheuppe (2005) added decline in financial performance are often called by financial distress can be experienced by various companies besarmaupun small. Research conducted by Bhattachacharjee and Jie Han (2010) results that the macro-economic variables have an impact on financial ditress.

Of the many types of research described there are 3 things that have been researched in isolation, the first study of financial internal financial distress both research financial and non-financial internal distress third external analysis in the form of macro-economic shocks in the form of inflation. However, no studies using internal and external factors the company simultaneously in predicting financial distress a company.

2. Review of Provious Works

In a study of financial distress of many researchers use analyzer of different financial ratios such as Altman (1968) by Altman et al MDA model (1977) using financial ratios such as earnings before interest and taxes / total assets, market value of equity / book value of debt, retained earnings / total assets, working capital / total assets, sales / total assets (Altman et al, 1995). So even Zavgren (1983), using financial ratios well in predicting financial distress company that uses the form Average ratio of inventories / net sales, Average recievable / average inventories, Long-term debt / (total assets - short-term debt, net sales / (fixed assets working capital, Operational earnings / (total assets - Short-term debt, Quick assets / current debts, Quick assets / total assets (Zavgren, 1985).

Deakin (1972) using Cash / current debts, Cash / sales, cash / total assets, cash flow / total debts, Current assets / current debts, Current assets / sales, Current assets / total assets, net income / total assets, Quick assets / current debts, Quick assets / sales, Quick assets / total assets, Working capital / total assets, Working Cpital / Sales, Total Debt / Total assetss (Deakin 1977). While Oldson (1980), using financial ratios such Change in income / sum of the absolute value of net income for two years, Current debts / current assets, Log (total assets, / GNP price index level Net income / total assets, Owners' positive or negative equity, Positive or negative earnings, Working capital / total assets, total debt / total assets (Zahra Poorzamani1, Azita Jahanshad 2013; brahmins (2007).

According to Foster (1994) there are two types of approaches that can be used, namely: univariate models of distress prediction that uses two key assumptions in the model's prediction, namely:

a) the difference between the variable distribution of entities in financial distress and non distress.
b) different variables that can be developed for the purpose of financial distress prediction.

Another approach is multivariate models of distress prediction that uses the dependent variable in the form of groups such as the bankrupt and non-bankrupt group or the possibility of bankruptcy. Usually this approach using financial ratios for the test.

A growing issue in this approach include the variables that should be included in the prediction model and the model that should be used. Analysis of financial difficulties greatly aid in the decision to take a stand against companies that are experiencing financial difficulties, so a lot of research trying to develop an early warning system of financial distress by using the ratio-ratio in the financial statements. The use of ratio-financial ratio to distinguish companies that are categorized as healthy and unhealthy has been going on since 1930, Aksoy and Ugurlu (2006) concluded that Winakor and Smith (1935); Ramser and foster (193); Merwin (1942) and Hickman (1958) conducted studies that lead to the conclusion that corporate bankruptcies have different financial ratios significantly compared with existing enterprise operates. Other major initiators associated with bankruptcy research firm (financial distress) is Beaver (1996) which presents the approach of a single variable (univariate) from discriminant analysis which was later expanded to approach multiple variables (multivariate). Furthermore, Altman (1968), which uses multi-discriminant analysis (MDA) to classify financial ratios and financial difficulties develop forecasting models. Altman's model is used in penelitiaan Deakin (1972) Blum (1974), Altman (1973), Altman and Loris (1972), Altman and McGogh (1974), Libby (1975), Haldeman and Narayanan (1977). Gordon Springate in 1978, For nearly two decades, discriminant analysis has become the main method in predicting financial distress / bankruptcy of the company, until late 1980s emerged the use of new methods in the prediction that the logarithmic regression began to emphasize its use for prediction of financial distress or bankruptcy .

Ohlson (1980) used logic models (multiple logistic regression) to build a model to predict the probability of bankruptcy in bankruptcy. Ohlson in research claims that his research is a very important discovery model. This important discovery was shown from research models that take into account the viewpoint of the financial statements when a company issues to the public. It aims to control whether the company went bankrupt before or after the date of issuance of the financial statements. Ohlson claimed that previous models do not explicitly consider the problem of time the financial statements. This model uses the data cross action financial ratio, the logit model because this ignores the dynamic character of the financial ratios. Logit model belongs to the class of static models. Static model is a class of models that require all companies that fail within a certain period of the same process. Where in the logit analysis, determination of distress and non-distress company uses only one year of observation company or also called as a single period models. This model is supported by Elliot and Kennedy (1988), Kennedy (1992), Lecte (1999), Louviere et al (2000).

2.1. Fundamentals of Corporate Finance in the form of Financial Ratios

Ross, et al. (2006: 78) states that in order to compare the performance of companies of different sizes is to calculate and compare the financial ratio, which is calculated from the relationship of a company's financial information and are used for comparison purposes. Calculating Financial Ratios is one source of information to obtain a picture of the financial condition of the company.

Financial Fundamentals is an indicator of the performance of the Vendor which tcermin besarn financial ratio, the performance of the company's fundamental financial analysis can help in identifying the strengths and weaknesses of corporate finance (White and Sond, 2003)

Definition of "Ratio" is a tool that is expressed in Arithmetical terms that can be used to explain the relationship between the two kinds of financial data, One way to analyze the relationships of the various items in the financial statements. Results and analysis is the basis to be able to Interpret financial condition and results of operations of the company.

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2.3. Upper Echelon

Upper Echelon Theory is a theory that considers the concept of top management as the primary decision maker strategij within the organization (Hambrick and Mason, 1984). Decisions taken top managers will have an immediate impact on organizational outcomes, because its what top managers do and how they do will affect organizational outcomes ((Finkelstein and Hambrick, 1996) The main basis of this reasoning is the executive experience, values and personality greatly affect their interpretation of the situation at hand and influence their choice. The lack of conversation manager manages the company has the same role with the decline in the com pany's fundamentals preformance this leads to financial distress, in line with the research Cor (2003) states that the effect on performance management reputation keunagan and reputation management company that better reflects good corporate governance as well (Nikoskelainen and Wright (2007).

Reputation management is one of reputation management proxy lately become a center of attention of inves tors, stock market analysts and regurator. Reputation management in view of the many root management is an important asset to the company as proposed by Batchelor (1999), Bromley (1993), Broulillard (1983), Caminiti (1992), Fomrun (1996), Hail (1992), Holmes (1995) , Sobol, et.al (1992), Weigelt and Camerer (1988). In research Gatot Nazir Ahmad (2014) also expressed the opinion of Bromley (1993), Fombrun and Tranley (1990), Brouillard (1983) Sobol et al, (1992).

2.4. Corporate Governance

The problem arises because the corporate Governace the separation between ownership and control of the company. This separation is based on agency theory that in this case the management tends to increase personal gain rather than the company's goals. In addition to having good financial performance the company is also expected to have good governance.

In agency theory to explain (Jensen and Meckling (1976) that the management will make a decision to increase the size of the company through investment in order for them to enjoy the compensation based on the amount of assets they manage, meaning that management will make business decisions that benefit their position because they are in charge of a number of shares.

Wahyudi and Pawestri (2006) explains that managerial ownership that align the interests of management and shareholders will benefit directly from the decisions taken and suffer losses as a consequence of making the wrong decision. The statement states that the greater the proportion of ownership in the company management, the management tends to be more active in the interests of shareholders in particular is himself. The number of large managerial stock ownership should have a higher performance, because the agency cost reduced. So that the problem will disappear keagenen assumed if a manager is also as an owner. (Jansen and Meckling, 1976) In this study management ownership is measured by proxy Diyah and Erman (2009) in accordance with the percentage of stockholders' proportionate share of the management who actively participate in the decision-making companies (directors and commissioners)

2.5. Macro Condition

As causes of financial distress is also the external factors of the company, Many economic downturn caused the company macro conditions, when the economy in Ameriks krisisi States in 2008 due to rising subprime mortgage interest rates SBI impact on the increase in deposits, which in turn result in high interest rate credit, so investing in the economy declined. Domestic investment decreased resulting in increased reliance on domestic business overseas investors, which means that an increase in the current flow of dollars into the country. The decline of the rupiah against the US dollar will lead to inflation, rising inflation is a relatively negative signal for investors, high inflation caused a decline in the profitability of a company that will lower the dividend resulting public trust to invest will be reduced, this will have an impact on funding lambant corporate activities will eventually happen Financial Distress ended in bankruptcy

3. Conclusion

Based on the analysis of previous studies, and analyzes the literature that has been discussed, the analysis of financial distress by using internal factors and external companies will help the analysis, and scientists to increase the input of theory and based on the phenomenon that occurs in the economy, making many companies who experience financial distress, so many studies done using a variety of variables that the results can be used as input for the company and as a contribution to the theory and practitioners, as well as information for investors to invest their money as capital in the company if the company healthy and able to provide the expected returns or not. Besides, with the study of government can oversee a business, in order to take action to protect the economy, industry, workers and society in general.

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