The Effect of Operating Cash Flows, Sales Growth, and Operating Capacity in Predicting Financial Distress

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Abstract:
Purpose: This study was conducted to obtain empirical evidence and to discuss the effect of operating cash flow, sales growth, and operating capacity in predicting financial distress in all manufacturing companies listed on the Indonesia Stock Exchange in 2017-2019.
Method: This study is based on an associative quantitative approach and is assisted by the Statistical Package for the Social Sciences (SPSS) program.
Findings: The results show that operating cash flow had a negative effect on financial distress, and sales growth also had a negative effect on financial distress, while operating capacity had a positive effect on financial distress.
Practical Implication: This article can be used as a consideration for companies in terms of prevention so that companies avoid financial distress. In addition, users of financial statements can be used as a consideration before making an investment decision so that they can find out indications of financial distress in a company.
Significance of the study: The results of this study can provide useful contributions and information for company management to determine the effect of operating cash flow, sales growth, and operating capacity in predicting financial distress so that companies can take policies to take corrective or preventive action.

Keywords: Operating Cash Flow; Sales Growth; Operating Capacity; Financial Distress.

I. INTRODUCTION

1.1 Research Background

Financial statement analysis is a tool to obtain information relating to the company's financial performance and can be used to project the company's financial aspects in the future. However, in reality, companies that have operated for a certain period of time are forced to dissolve or be liquidated due to financial difficulties that have led to bankruptcy. An analysis of the symptoms of bankruptcy must be carried out in order to anticipate future bankruptcies. There are many ways to measure or indicate the financial wellness of a business (Swalih et al., 2021). Predicting financial distress with designing appropriate indices and models can make companies aware of the occurrence of financial distress (Vosoughi et al., 2016). This model can help potential investors and creditors to invest so they don't get caught up in these financial difficulties. Some of the bankruptcy detection tools that can be used are the Altman Z-score model (1968), the Springate model (1978), the Zmijewski model (1983) and the Grover model created through the assessment and redesign of the Altman model (Evi& Maria, 2013).

Financial distress is a stage of decline in a company's financial condition that occurs before bankruptcy or liquidation (Fahmi, 2013). Generally, companies that experience financial distress have a tendency to go bankrupt. Bankruptcy analysis is important to do with the consideration that the bankruptcy of a publicly traded company will harm many parties (Murni, 2018). Continuity of business and company failure (financial distress), if compared, are like two opposing sides of a coin. Companies that are considered to be financially sound are not necessarily really good and their business continuity can be guaranteed, it could be declared bankrupt a year later.

Imam (2012: 143) defines financial distress as a condition in which the company's finances are in an unhealthy state, or a crisis that occurs before bankruptcy. Financial distress can be divided into two types, namely economic failure and financial failure (Ardina, 2013). Economic failure can occur due to the company's failure to cover the company's operating costs. Meanwhile, financial failure can be caused by two things. The first cause is technical insolvency, a situation where the company fails to pay its obligations due but its assets are greater than the total debt it owns. The second cause is bankruptcy, a situation where the company is no longer able to fulfill its obligations to debtors because the company experiences insufficient or insufficient funds to continue its business so that the company's economic objectives cannot be achieved. Financial distress is a very important problem for companies to pay attention to, because if the company is really experiencing financial distress, the company will be at risk of going bankrupt.

Financial distress can occur due to influence from within the company itself (internally) and from outside the company (externally). Damodaran (2001) states, the factors causing financial distress from within the company are more micro, namely cash flow difficulties, the amount of debt, and losses in the company's operational activities for several years. If the company is able to cover or overcome these
Based on these factors in predicting financial distress, this study selects operating cash flow, sales growth, and operating capacity as variables in predicting financial distress. Apart from the problem of previous research which did not show consistent results, the reason for conducting research related to financial distress is that Indonesia is very prone to financial distress in several national companies. Companies that have the potential to experience bankruptcy with the emergence of financial distress, according to researchers, are very interesting to study because it is a threat that can be experienced by all companies regardless of the type or size of the company and it can happen at any time. Every company should be vigilant for the odds of financial distress as it doesn't matter what the company's sector is or how big the bank is; they have a chance to experience financial distress (Dharmawan et al., 2020). The difference between this study and the previous research is by adding the operating cash flow variable as a variable that can predict the occurrence of financial distress, because in the previous research it was more dominant to use the cash flow variable, whereas in this study it was more specialized in operating cash flow.

1.2 Research Problem

A phenomenon that has recently occurred in Indonesia is that exports have dropped further and the prices of export commodities have also fallen on world commodity markets (Sindonews, 2017). Several companies were delisted from the Indonesia Stock Exchange (IDX) until 2019 as many as 38 companies. The following are companies that were delisted from the Indonesia Stock Exchange (IDX) from 2011 to 2019 which are presented in Table 1.

<table>
<thead>
<tr>
<th>No.</th>
<th>Year</th>
<th>Delisting</th>
<th>Sector</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>2011</td>
<td>5</td>
<td>3 service, 2 manufacture</td>
</tr>
<tr>
<td>2</td>
<td>2012</td>
<td>4</td>
<td>2 service, 2 manufacture</td>
</tr>
<tr>
<td>3</td>
<td>2013</td>
<td>7</td>
<td>4 service, 2 manufacture, 1 mining</td>
</tr>
<tr>
<td>4</td>
<td>2014</td>
<td>1</td>
<td>1 service</td>
</tr>
<tr>
<td>5</td>
<td>2015</td>
<td>3</td>
<td>1 service, 2 manufacture</td>
</tr>
<tr>
<td>6</td>
<td>2017</td>
<td>8</td>
<td>5 service, 1 manufacture, 2 mining</td>
</tr>
<tr>
<td>7</td>
<td>2018</td>
<td>4</td>
<td>1 service, 3 manufacture</td>
</tr>
<tr>
<td>8</td>
<td>2019</td>
<td>6</td>
<td>4 service, 1 manufacture, 1 mining</td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td>38</td>
<td></td>
</tr>
</tbody>
</table>

Source: Indonesia Stock Exchange, 2020

One of the companies delisted from the Indonesia Stock Exchange (IDX) in 2018 was PT Dwi Aneka Jaya KemasindoTbk (DAJK). PT Dwi Aneka Jaya KemasindoTbk was issued from the Indonesia Stock Exchange (IDX) through share delisting. DAJK's financial performance is indeed unhealthy, it is known that it has debts from several banks (www.cnbcindonesia.com), (insight.kontan.co.id), and (economy.okezone.com). Indonesia's economic growth has also decreased from the previous year (www.kompas.com), (detikfinance.com), and (www.kompas.com). PT Krakatau Steel Tbk (KRAS) experienced losses for 7 consecutive years, accumulated debts, issues of mass layoffs, and the resignation of commissioners. PT SolusiBangunan Indonesia (SMCB) experienced losses from 2016 and has built-in debt. Bankruptcy cases and postponement of debt payment obligations (PKUP) have increased, this has shaken the national economy. In addition, reports from the international debt rating agency Moody's Investor Service reveal that companies in Indonesia are at risk of defaulting on debt. The manufacturing companies that were most frequently requested against PKPU were textile companies, garment companies, steel companies, and plastic companies.
The rate of global economic growth is weakening. The slowdown in economic growth was caused by weakening trade and manufacturing activity, trade tensions, as well as developing countries experiencing market pressure and many countries experiencing recession. The company is expected to generate maximum profit while maintaining the going concern assumption (Santoso and Wedari, 2007). With this principle, the entity is considered capable of maintaining the business in the long term and will not be liquidated in the short term. However, in practice, companies often cannot maintain this going concern assumption due to financial difficulties. The prediction of financial distress companies plays an important role for managing organizations (Norfian et al., 2018).

II. LITERATURE REVIEW AND HYPOTHESES

2.1 Literature Review

The concept of agency theory according to Jensen and Meckling (1976) is a contract in which one or more people (principal) order another person (agent) to perform a service on behalf of the principal and authorize the agent to make the best decisions for the principal. Jensen and Meckling (1976) state that the problems are: (1) Moral hazard, which is a problem that arises if the agent does not carry out the things agreed upon in the work contract. (2) Adverse selection, which is a condition in which the principal cannot understand whether a decision made by the agent is correct based on the information he has obtained or it occurs as a negligence of duty. The relationship between agency theory and the variables in this study is that investment decisions and corporate strategy innovation are in the hands of the agent, so that the agent is required to run the company well in order to increase the company's growth. Apart from that the agent is given the authority to manage the company, this means that the agent is responsible for operations within the company. Therefore, agents are required to be able to maximize the use of company assets for operational activities in order to increase sales.

2.2. Hypotheses

2.2.1 Effect of operating cash flows on financial distress

Operating activities are activities related to profit, operating activities also include cash inflows and net cash outflows from operating activities such as investing in inventories, obtaining credit from suppliers, and providing loans to customers. The cash flow statement is of special importance to the solvency of firms, which is useful information for lenders (Dung & Anh, 2020). Cash flow from investment and finance activities has a more limited role in predicting financial difficulties than operating cash flow (Dung & Cong, 2020). The relationship between agency theory and cash flows from operating activities is an agency theory that deals with agency conflicts or conflicts of interest between agents and actors where shareholders and management have different interests. Management is required to be able to make policies that can balance the interests of shareholders and the interests of the company's growth, such as considering various factors including how much profit a company earns, sufficient cash flow to continue operating the company. Therefore, a good agency relationship is needed so asymmetry information does not occur.

Research conducted by Amelia and Wahidahwati (2017) shows that cash flow has an effect on financial distress. The results of this study are supported by research by Ulfii et al., (2017) and Radiansyah (2013) which show that operating cash flow has a negative effect on financial distress. Companies that have high operating cash flow means that they have sources of funds to carry out their operating activities. If the operating cash flow generated by the company has increased, the less likely the company will experience financial distress, and vice versa if the company's operating cash flow has decreased continuously without being overcome, the company can experience financial distress (Amarilla et al, 2017). Based on this description, the hypothesis proposed in this study is:

H1: Operating cash flow has a negative effect on financial distress

2.2.2 The effect of sales growth on financial distress

Sales growth or sales growth ratio is a ratio that is used to predict a company's growth in the future, this ratio also reflects the successful application of investments made by the company in the past period which can be used as a prediction regarding the company's growth in the coming period (Simanjuntak et al, 2017). Agency theory explains that investment decisions and corporate strategy innovation are in the hands of agents, so agents are required to run the company well in order to increase the company's growth. High sales growth can increase company revenue from sales that occur during a certain period at the company. Firms having high sales growth tend to invest funds in business expansion rather (Tahir, 2016).

The results of research conducted by Ni Luh and Ni Ketut (2015) show that sales growth has an effect on financial distress. This is supported by the research of Utami (2015) and Widhiari and Merkusiwati (2015) which state that the sales growth ratio has a negative effect on financial distress. The sales growth ratio in this study is proxied by sales growth. Companies that have a high growth rate tend not to experience failure so that the company is able to increase sales (Wulan & Dharma, 2017). High sales growth will cause higher profits so that the financial condition becomes quite stable and reduces the possibility of the company experiencing financial distress. Meanwhile, if the sales growth has decreased which cannot be overcome by the company, this can result in financial distress because the sales that have decreased from the previous period can affect the company's assets, profits and debt. (Wiwin and Dani, 2017). Based on this description, the hypothesis proposed in this study:

H2: Sales growth has a negative effect on financial distress

2.2.3 The effect of operating capacity on financial distress

Operating capacity or activity ratio is a ratio which is also known as the efficiency ratio which is used to assess whether a company is effective or not in using assets to
generate sales, so that it will create the accuracy of a company's operational performance (Atika, 2012). Financial distress is a significant factor in the asset pricing model (Kakinuma et al., 2020). Agency theory explains that agents are given the authority to manage the company, this means that agents are responsible for operations within the company. Therefore, agents are required to be able to maximize the use of company assets for operational activities in order to increase sales. The higher the total asset turnover, the more effective the company's total assets are in generating sales. If the actors in company management activities cannot maximize the use of company assets, the company's sales cannot be maximized, so that the possibility of a company experiencing financial distress will be even greater.

Research conducted by ChristonSimanjuntak (2017: 06) shows that operating capacity has a significant negative effect on financial distress. This is supported by research by Agustini and Wirawati (2019), Widhiari and Merkusiwati (2015), and Antikasari (2017) which show that the activity ratio has a negative effect on financial distress. The results of research conducted by indicate that the activity ratio has a negative effect on financial distress conditions. This proves that the higher the operating capacity value, the less likely the company will experience financial distress. The operating capacity ratio in this study is proxied by total asset turnover (TATO). If TATO produces a high value, the asset turnover is faster so that it generates profit and the use of all assets in generating sales is more optimal. With a high TATO value, it can also mean that the same number of assets can increase sales volume so that the company is less likely to experience financial distress, and vice versa (Widhiari and Merkusiwati, 2015). Based on this description, the hypothesis proposed in this study is:

H1: Operating capacity has a negative effect on financial distress

III. RESEARCH METHODS

3.1 Research design
This study uses an associative quantitative approach. The method used to obtain data in this study is non-participant observation. In this study, the research location was determined in all of manufacturing companies listed on the Indonesia Stock Exchange 2017-2019 which were downloaded through the official IDX website, www.idx.co.id.

3.2 Data collection methods
Data were collected from secondary sources. Secondary data in this study are financial reports obtained from all manufacturing sector companies listed on the Indonesia Stock Exchange (BEI). This data was obtained from the official IDX website, www.idx.co.id, during 2017-2019.

3.3 Population and sampling methods
The population used in this study are all of manufacturing companies listed on the Indonesia Stock Exchange 2017-2019. In this study, sampling using a time series approach and determining the number of samples using purposive sampling method. The criteria used for sample selection can be seen in Table 2 below:

<table>
<thead>
<tr>
<th>No</th>
<th>Criteria</th>
<th>Criteria</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>The company is not listed in the manufacturing sector on the Indonesia Stock Exchange consecutively during the 2017-2019 period</td>
<td>(3)</td>
</tr>
<tr>
<td>2</td>
<td>Manufacturing companies that do not have audited financial statements for the 2017-2019 period</td>
<td>(37)</td>
</tr>
<tr>
<td>3</td>
<td>Companies that were delisted from participation in the Indonesia Stock Exchange during the 2017-2019 period</td>
<td>(2)</td>
</tr>
<tr>
<td>4</td>
<td>Manufacturing companies that carry out mergers and acquisitions during the 2017-2019 period</td>
<td>(2)</td>
</tr>
<tr>
<td>5</td>
<td>Manufacturing companies that experienced losses during the 2017-2019 period</td>
<td>(31)</td>
</tr>
<tr>
<td></td>
<td>The number of companies that meet the sample criteria</td>
<td>84</td>
</tr>
<tr>
<td></td>
<td>Number of observations during 2017-2019</td>
<td>252</td>
</tr>
</tbody>
</table>

Source: www.idx.co.id, 2020

3.4 Operational Definition of Variables
The operational definition of a variable is a definition that explains how variables are measured and calculated (Chandrarin, 2017: 88). The operational definition of each variable will be explained as follows:
Overall, the sales growth on absolute residuals. The test- 
bounding error in al-
chws that there are no autocorrelation-

3.5 Data analysis methods
This study uses multiple linear regression analysis. 
Y = α + β1 X1 + β2 X2 + β3 X3 + e ..........................(1)
Information
Y : Financial Distress 
X1 : Operating Cash Flow
X2 : Sales Growth
X3 : Operating Capacity
A : constanta
β1,β2,β3 : Multiple Regression Coef.

Prior to multiple linear regression analysis, descriptive
statistical analysis and classical assumption were first
performed. All research hypotheses were tested using
multiple linear regression analysis with the help of the SPSS
23 for windows program.

IV. RESULT AND DISCUSSION

4.1 Descriptive Statistics Results

Table 4: Descriptive Statistics Test Results

<table>
<thead>
<tr>
<th>Variable</th>
<th>Indicator</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial Distress</td>
<td>Altman Z-Score Model</td>
</tr>
<tr>
<td></td>
<td>Z = 1.2Z1 + 1.4Z2 + 3.3Z3 + 0.6Z4 + 1.0Z5</td>
</tr>
<tr>
<td>Operating Cash Flow</td>
<td>Operating Cash Flow = Operating Cash Flow / Current Liabilities</td>
</tr>
<tr>
<td>Sales Growth</td>
<td>Sales Growth = (Sales_t - Sales_{t-1}) / Sales_{t-1}</td>
</tr>
<tr>
<td>Operating Capacity</td>
<td>TATO = Net sales / Total Asset</td>
</tr>
</tbody>
</table>

Table 3: Variable Operational Definitions

<table>
<thead>
<tr>
<th>Variable</th>
<th>Indicator</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial Distress</td>
<td>Altool Z-Score Model</td>
</tr>
<tr>
<td></td>
<td>Z = 1.2Z1 + 1.4Z2 + 3.3Z3 + 0.6Z4 + 1.0Z5</td>
</tr>
</tbody>
</table>

The number of observations on manufacturing
companies on the Indonesia Stock Exchange during 2017–
2019 in this study was 84 data. The financial distress
variable has an average value of 2.270939. In the operating
cash flow variable, the minimum value is -0.5051 owned by
PT HartadinataAbadiTbk., While the maximum value of
2.0051 is owned by PT Hanjaya Mandala SampoernaTbk.
Overall, the operating cash flow variable has an average
value of 0.400639. In the sales growth variable, the
minimum value is -0.1229 owned by PT Star Petrochem
Tbk., While the maximum value of 3.1212 is owned by PT
Budi Starch & Sweetener Tbk. Overall, the sales growth
variable has an average value of 0.140821. In the operating
capacity variable, a minimum value of 0.1786 is obtained
which is owned by PT Star Petrochem Tbk., While the
maximum value of 5.1789 is owned by PT AlakasIndustrindoTbk. Overall the operating capacity
variable has an average value of 1.095563.

4.2 Classical Assumptions Tests
Classical assumptions tests aim to determine the
feasibility of the regression model used in research (Ghozali,
2016: 103). The classical assumptions tests used in this
research are normality test, multicollinearity test,
autocorrelation test, and heteroscedasticity test.

a) Normality test, this study uses the Kolmogorov-Smirnov
test to detect whether the normality test is fulfilled or not
provided that the significance level is greater than or
equal to 0.05 then it is normally distributed. Based on the
test results, the Asymp.Sig. (2-tailed) value was 0.086,
so it can be concluded that it is normally distributed.
b) Multicollinearity test, multicollinearity can be seen from
the tolerance value and Variant Inflation Factor (VIF),
name if the tolerance value is more than 10 percent and
the Variant Inflation Factor (VIF) value is less than 10,
it means that there are no symptoms of multicollinearity.
The test results show that the independent variable in
this study has a tolerance value above 10% and VIF for each
independent variable is less than 10, therefore the model
free from multicollinearity symptoms and is suitable to
be used to predict.
c) Autocorrelation test, aims to test whether in the linear
regression model there is a correlation between
confounding error in period t with confounding error in
period t-1 (previous). To detect the presence or absence
of autocorrelation can be used with the Durbin Watson
test (D-W). The test results show that the Durbin-Watson
value in this study is 0.640. This value is between -2 and
+2. This shows that there are no autocorrelation
symptoms in this regression model.
d) Heteroscedasticity test, in this study to detect the
presence or absence of heteroscedasticity can be done by
performing the Glejser Test, namely by regressing the
independent variables on absolute residuals. The test
results show that the significance value of each variable
in the regression model is greater than 0.05, so it can be
concluded that the regression model in this study is free
from heteroscedasticity symptoms and the research
Based on the table above, the regression equation formed is as follows:

\[ \text{FD} = 0.059 - 0.091 \text{AKO} - 0.177 \text{SG} + 0.586 \text{OC} + e \]

From the regression equation formed, the results can be interpreted as follows: A constant value of 0.059 means that if the operating cash flow, sales growth, and operating capacity variables are considered constant (value 0), the value of financial distress will increase by 0.059. Based on Table 5.7, it can be seen that the value produced by F count is 18.181 with a significance level of 0.000 smaller than \( \alpha = 0.05 \). Thus, this research model is suitable to be used to prove the hypotheses formed. The adjusted R2 value in this study is 0.380, which means that 38 percent of the dependent variable financial distress can be explained by operating cash flow, sales growth, and operating capacity, while the remaining 62 percent is influenced by other variables not included in this research model.

### 4.3 Results of multiple linear regression analysis

#### 4.3.1 The Effect of Operating Cash Flow on Financial Distress

Based on the test results using multiple linear regression, it shows that the operating cash flow variable has a regression coefficient value of -0.091 with a significance level of 0.039 which is smaller than the significant value of 0.05, so it can be concluded that operating cash flow has a negative effect on financial distress. This shows that the higher the level of operating cash flow owned by the company, the lower the tendency for the company to experience financial distress. Thus it can be stated that the first hypothesis (H1) in this study is accepted.

Companies that have high operating cash flow means that they have sources of funds to carry out their operating activities. The ability to generate cash flow from operations is essential to healthy finances, no company can survive in the long run without generating cash from operations. Therefore, if the company has a good amount of cash flow, creditors will have confidence that the company is capable of performing its obligations and the company will avoid financial distress. Vice versa, if the company's operating cash flow has decreased continuously without being overcome, the company can experience financial distress (Amarilla et al, 2017). The results of this study are supported by research by Amelia and Wahidahwati (2017), Ulfi et al., (2017) and Radiansyah (2013) which show that operating cash flow has a negative effect on financial distress.

#### 4.3.2 The Effect of Sales Growth on Financial Distress

Based on the test results using multiple linear regression, it shows that the sales growth variable has a regression coefficient value of -0.177 with a significance level of 0.007, which is smaller than the significant value of 0.05, so it can be concluded that sales growth has a negative effect on financial distress. This shows that the higher the level of sales growth a company has, the lower the company's tendency to experience financial distress. Thus it can be stated that the second hypothesis (H2) in this study is accepted.

The higher the sales growth rate of a company, the company is successful in executing its strategy in terms of marketing and product sales, this means that the greater the profit the company will get from these sales. This reflects that the company's financial condition is stable enough to reduce the possibility of the company experiencing financial distress. Meanwhile, if the sales growth has decreased which cannot be overcome by the company, this can result in financial distress because the sales that have decreased from the previous period can affect the company's assets, profits and debt. (Wiwin and Dani, 2017). The results of this study are supported by research by Lubis and Patria (2019), Widhiari and Merkusivati (2015), Yudiawati and Indriani (2016), Setyowati and Sari (2019), and Uddin et al. (2020), which state that the sales growth ratio has a negative effect on financial distress.

![Table 5: Results of Multiple Linear Regression Analysis](image)

**Table 5: Results of Multiple Linear Regression Analysis**

<table>
<thead>
<tr>
<th>Variabel</th>
<th>Unstandardized</th>
<th>Coefficient</th>
<th>Standardized Coefficient</th>
<th>t-stat</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
<td>Beta</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Constant</td>
<td>0.059</td>
<td>0.088</td>
<td>0.672</td>
<td>0.503</td>
<td></td>
</tr>
<tr>
<td>X1</td>
<td>-0.091</td>
<td>0.044</td>
<td>-2.096</td>
<td>0.039</td>
<td></td>
</tr>
<tr>
<td>X2</td>
<td>-0.177</td>
<td>0.065</td>
<td>-2.747</td>
<td>0.007</td>
<td></td>
</tr>
<tr>
<td>X3</td>
<td>0.586</td>
<td>0.087</td>
<td>6.705</td>
<td>0.000</td>
<td></td>
</tr>
<tr>
<td>R Square</td>
<td></td>
<td>0.402</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Adjusted R Square</td>
<td>0.380</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>F hitung</td>
<td>18,181</td>
<td>0.000</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Source:** Processed from primary data, 2020
4.3.3 Effect of Operating Capacity on Financial Distress

Based on the test results using multiple linear regression, it shows that the operating capacity variable has a regression coefficient value of 0.586 with a significance level of 0.000 smaller than the significant value of 0.05, so it can be concluded that operating capacity has a positive effect on financial distress. This shows that the higher the level of operating capacity a company has, the higher the company's tendency to experience financial distress. Thus, it can be stated that the third hypothesis (H3) in this study is rejected.

A company with a high operating capacity shows that the company has a faster asset turnover so that it generates profits and the use of all assets in generating sales is more optimal. This condition provides an opening for controlling shareholders to practice expropriation, or to use control rights or control rights to maximize the welfare of themselves or certain groups by distributing wealth from other parties (Claessens et al., 1999). So it can be concluded that if the value of operating capacity is high, the potential for expectation will be even greater and will result in a higher possibility of financial distress. The results of this study are supported by research by Kusanti (2015), Hadi (2014), and Alvina (2019) which state that operating capacity has a positive effect on financial distress.

V. CONCLUSION AND SUGGESTION

5.1 Conclusion

The findings of this study indicate that operating cash flow has a negative effect on financial distress. This means that the higher the level of operating cash flow owned by the company, the lower the tendency for the company to experience financial distress. If the company has a high amount of cash flow, creditors will have confidence that the company is capable of performing its obligations and the company will avoid financial distress.

Sales growth has a negative effect on financial distress. This means that the higher the level of sales growth owned by the company, the lower the company's tendency to experience financial distress. This is because high sales growth will lead to higher profits so that the financial condition becomes stable enough and reduces the possibility of the company experiencing financial distress.

Operating capacity has a positive effect on financial distress. This means that the higher the level of operating capacity owned by the company, the higher the company's tendency to experience financial distress. This is because if the operating capacity value is high, the potential for the controlling shareholder to make expectations is greater and will result in a higher possibility of financial distress.

5.2 Suggestion

Companies should pay more attention to financial reports, especially on operating cash flow ratios, sales growth, and operating capacity which are proven to have an influence on financial distress and it is hoped that this research can be used to take preventive measures so that companies avoid financial distress. For the company, especially the management, it is hoped that it can manage the company well by using its assets for operations effectively and efficiently so that the company is able to optimize its sales and the profits earned will continue to increase. Thus the occurrence of financial distress can be avoided by a company.

Users of financial statements should pay more attention to disclosure of information in the company's financial statements so that they can find indications of financial distress in a company. Before making investment decisions, potential investors and creditors also need to consider fundamental aspects such as the company's financial ratios.

Future research is expected to add observation periods and not only examine financial distress in manufacturing companies, but can expand the sample of companies. The Adjusted R2 value of 0.380 shows that 38% of financial distress is influenced by operating cash flow variables, sales growth and operating capacity, while 62% is influenced by other variables not presented in this research model. This is an opportunity for further researchers to develop research related to other factors that affect financial distress.

REFERENCES


Tehran Stock Exchange