

## CHANGES ON CAPITAL STRUCTURE OF THE FIRMS ON THE OCCASION CRISIS AND SITUATION OF TOURISM COMPANIES TRADED ON ISE

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*The capital structures of the enterprises and the factors that affect these structures have been dealt with extensively in literature. The experimental studies of Modigliani-Miller conducted within the context of developed countries' economic and institutional structures showed that capital structure does not affect the enterprise value. On the other hand, other studies revealed that the changes in the market affected the enterprises' finance structure and their finance preferences. In this study, the factors that determine the structure of the tourism enterprises are studied in an environment where market deficiencies abound. The study also looks at the changes that are caused by these factors especially during the crisis of during crisis period of 1998 – 2006.*

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**Keyword:** *Financial structure, ratios, crisis, tourism enterprises*

JEL Classification: *L83, M1, O1, G010, G300, G320*

### INTRODUCTION

Capital structure of the firms and determination of the factors affecting those structures have been discussed and tackled in the literature and empirical studies. However, it is known that, capital structures change during the periods before and after the crises. Firms revise their capital structures according to their debt and risk positions and change their decisions depending on this.

Furthermore, it is known that partnership structures of the firms affect the investment decisions and preferences; some decisions are guided by not all the partners but by the ones with higher shares. Also the preferences of the top management become more important.

In this study, the factors affecting financial structures of the tourism companies during market failures have been investigated, and the changes in the effects of the factors are discussed and tried to be determined for the certain periods of the crisis between 1998-2006

## **THE OBJECTIVE AND THE CONTENT OF THE STUDY**

In this study first it is aimed to identify the course of the financial structure of the companies traded on ISE (The Istanbul Stock Exchange) by years. In this context, financial ratios are calculated using the data of 12 months balance sheets and income statements of the companies in question between the years of 1998-2006.

Financial ratios have been analyzed in three groups as liquidity ratios, financial structure ratios and profitability ratios in the study.

In the study, figures from the published balance sheets and income statements of the companies, whose shares are traded on The Istanbul Stock Exchange (ISE), for the years of 1998-2006 have been used. The data set used is formed using two systems for the periods of 1998-2003 and 2004-2006 due to the amendments of the balance sheet items. Also the number of the companies analyzed differs by the periods mentioned.

In this study, the factors determining the financial structure of the Turkish firms during market failures have been studied by the analysis of panel data method performed on 8 tourism companies traded on ISE. Also the changes on the effects of the factors in question are tried to be determined in respect of certain crisis periods.

## **CAPITAL STRUCTURE IN THE LITERATURE**

Capital structure of the firms and the factors affecting those structures have been discussed extensively in the literature. Theoretical works have brought three main classes of models to test: The trade-off, the agency, and the pecking order hypotheses. Since the capital structure irrelevance proposition of Modigliani & Miller (Modigliani; Miller, 1958), hundreds of papers have focused on financial policy. But the subsequent studies presented that the changes coming about in the market had affected the financial structure and preferences of the enterprises (Carpenter, 1993).

Few studies focus on international samples to test capital structure models. They are two noticeable exceptions (Rajan & Zingales, 1995; Booth & Aivazian & Demirgüç & Kunt & Maksimovic, 2001). Rajan & Zingales find similar levels of leverage across the G7 countries, thus refuting the idea that firms in bank-oriented countries are more leveraged than those in market-oriented ones (Rajan & Zingales, 1995). They also find that the determinants of capital structure that have been reported for the U.S. (size, growth, profitability, and importance of tangible assets) are important in other countries as well. However, new technologies and innovation that is also profitable to the tourism firm in a competitive market, must increase the value of the whole tourism product (Korres, 2008).

They explored the determinants of the financial structure by analyzing the financial decisions of the public enterprises in big industrial countries (Rajan, 1995). Rajan and Zingales concluded that there are similar behaviors in the companies of United Nations and other countries. Lelond, found that the liabilities of the Joint Stock Company and optimal leverage power for the company risk were obviously related (Lelond, 1994).

Effects of financial crisis are reflected primarily on working capital and cause alterations in the composition and sudden increases in the need of this capital. Indeed Fazzari and Petersen, who examined the composition of working capital investments during the recession years of 1975 and 1982 put forward that the working capital investments was three times more flexible than fixed capital investments (Fazzari & Petersen, 1993).

Also, Lelond explained that bonds, cases of dividend substitution, repurchases of debt and bad debts displayed different behaviors depending on the level of investments. A model examine the interaction between company adjustment and repeating capital costs and investment activity and financial decisions of a company in a model (Monuer & Triontis, 1994). Monuer and Triontis found that high levels of production that increase the debt capacity, financial flexibility and the effect of debt financing on the company investment and company decisions was economically unimportant for the firm in order to perform some phases.

One other study found that marketing via the Internet has larger advantages than other means. it reduces the costs of divulgation and publicity activities; it eases the brochures and pamphlets update; it eases and turns its procedure more economical comparing (Rocha & Victor, 2010).

## **FINANCIAL DIMENSION OF THE ESTABLISHMENT IN GENERAL AND FEATURES**

Common economic fluctuations are the most important risk element other than internal and sectoral factors. External shocks and monetary and fiscal policies of the governments, tax adjustments, transfer payments and other factors boost the economy or causes economic downturn. All those factors affect the firms, consumers and investors change their decisions, especially the breakdown of the economic boost affects the firms negatively (Pinche, 1990).

In terms of partnership structure of the Turkish companies, the big partners are generally Latin American companies. Also, since the companies are relatively young, compared to the companies of many of the countries, mostly the founder himself or second generation founders are in the administration. As a result, generally big partners that do not want to lose control make the decisions in the firms. Fear to lose control coupled with underdevelopment of the financial markets make the companies prefer internal sources for business finance.

Structural financial problems of Turkish establishments may be listed as follows:

- Currency crises are transferred to the firms via financial markets. During crisis periods, the increase in local value of the fixed liabilities in foreign currency and interest rates of the credits affect the balance sheets negatively.
- Receivables, stock, working capital and assets turnovers are slow in general, as an efficiency measure in resource usage. Decreasing turnovers both increase the need for resource and affect the profitability negatively.
- Establishments see increase in profits in increasing the profit margins, in other words in increasing the prices, rather than efficiency and effectiveness in resource usage. However, external financing becomes costly increase in prices leads to slowing down the turnovers and restricting the increase in sales. It is ignored that as long as it is possible to increase the turnovers by lower profit margins, it is possible to increase the profitability.
- Establishments may aim to have more profit using incentives. It is possible to increase the accounting profit by incentives, but economic profitability of the firms will be low.

- Another structural problem of the establishments in our country is the existence of an effective common group in business management. As a limited number of partners hold most of the capital, they determine the decisions.

As the firms traded at ISE consistently by the year 2000 is examined, it is seen that stocks have been acquired by some certain entities. However, the gathered data led us to the conclusion that the majority of the hotels use traditional cost accounting systems(Pavlatos;Paggios,2007). A single partner controls more than 50% of the business capital in 45% of the 243 establishments in ISE (Sak; Ersel, 1995).

## **THE DATA SET AND THE VARIABLES USED IN THE STUDY**

The general approach applied in empirical studies about the capital structure of the companies has been how capital structure (the relation between debt and owner's equity) of the firm is affected from different a priori affecting factors. In regression equations a leverage statement takes place as a dependent variable. Generally, some common factors are handled as explanatory variables. In our study too, the effects of some of the factors that we have been used on the capital structure and a brief explanation about their calculation methods is presented.

In order to understand whether the financial performance of an establishment is good and compare the measured performance with the rivals, reference values called benchmarks are needed. Usually ratios are used rather than absolute financial indicators as reference values. Ratios relate two absolute financial indicators, in other words are indicators that compare financial figures.

Information about how the data were collected, calculations were made and comparisons needed for the financial performance analysis is presented below. Financial tables and reports which consist of exact data that is used for the calculations of ratio analysis is also given.

Indebtedness, profitability, economic size and financial structure have been used as variables in the study. Assessment of the effective factors is handled in two different ways. First one is by comparing the value of stocks and sector averages using stock exchange prices and second one is by presenting the change in financial structure of the firms during crisis periods by means of some ratios exploiting financial table figures of the firms in the sector. Therefore the ratios have been used are; liquidity ratios (current, liquidity, cash ratio), financial structure ratios (Financial Liabilities/Assets Ratio, Financial Liabilities/Total Liabilities Ratio, Short- Trade Payables /Assets Ratio, Owner's Equity/Total

Liabilities Ratio, Leverage Ratio), profitability ratios (Profitability of Owner's Equity, Net Profit Margin, Gross Profit Margin, Operational Profitability).

The statistical assessments showed that;

- A low positive correlation was observed between ISE price-earnings ratio and tourism sector price-earnings ratio. However the correlation was higher in 2004-2006 period than 2000-2003 period. In other words, tourism sector was not affected much during crisis period in terms of securities market.
- A low positive correlation was found between the securities market of developing countries and tourism companies included in the study.
- If we look at the relationship between the figures used in the analysis by in terms of ratios, a low relationship was present between the ratios; however, the relationship a high between liquidity ratio and cash ratio was high.

## **RESULTS OF THE STUDY**

### **Analysis of the Sector Using Stock Exchange and Global Market Values**

Economic value added is used for determining the firm value beginning from the 1980s. Although in some studies, it was found that there was no relationship between the economic added value, market value of the firm and stock prices (Fernandez 2001; Bernstein (1998), in some studies, the relationship between the economic added value, market value of the firm and stock prices was high (Teleranta, 1998; Dodd and Chen, 1996). There are studies conducted in Turkey examining the relationship between economic value added, net profit and stock prices (Gürbüz and Erzincan, 2004).

The table 1 shows the stock exchange data of 8 firms including hospitality and transportation companies traded on the stock exchange market.

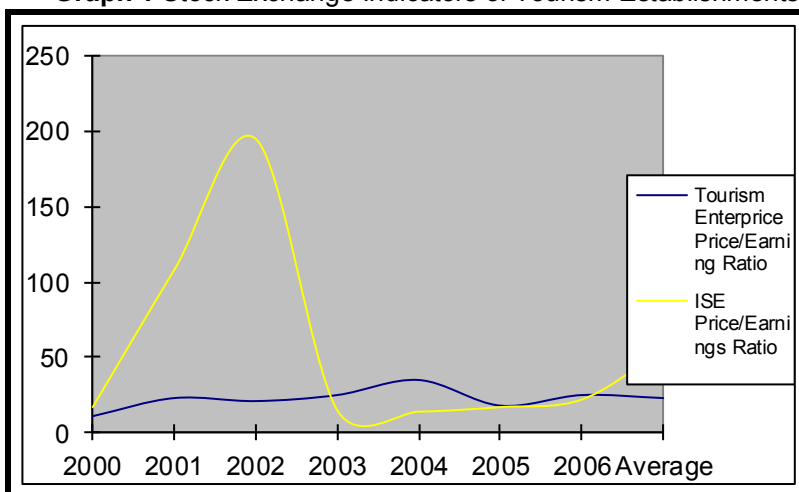
According to the market indicators presented above, price/earnings ratio of tourism enterprises has been generally close to the price/earnings ratio based on ISE 100 Index for research period. Even according to ISE 100 index, it increased in very high ratios in two years period after 2001 crisis: 108% for 2001 and 195% for 2002.

**Table 1** Stock Exchange Indicators of Tourism Companies

Ratios	2000	2001	2002	2003	2004	2005	2006	Average
Tourism Comp. Price/ /Earnings Ratio	11	23	21	25	35	18	25	23
ISE price/Earnings ratio	17	108	195	15	14	17	22	55

*(Calculations are based on the financial tables of the tourism companies traded on ISE.)*

**Graph 1** Stock Exchange Indicators of Tourism Establishments



No increase was found in tourism sector parallel to this. In other words, tourism sector was not affected from the increase in other sectors. However, it should be noted that the weight of tourism companies in ISE 100 index was very low (only 11% in 2002) and the stocks of tourism companies were traded poorly, which shows that the demand of investors for the sector is low.

2001 crisis created a deep uncertainty environment. The existence of an increase in all stock markets after the crisis period shows that there

was a global recovery. However, the global setbacks in the two years prior to the 2001 crisis were partially signals of a crisis.

### Analysis of the Sector Using the Ratios

In order to explain the change in the financial structure of the tourism companies during the crisis periods, some ratios from the financial table figures were used. The ratios used were; liquidity ratios (current, liquidity, cash ratio), financial structure ratios (Financial Liabilities/Assets Ratio, Financial Liabilities/ Total Liabilities Ratio, Short-term Trade Payables /Assets Ratio, Owner's Equity/Total Liabilities Ratio, Leverage Ratio), profitability ratios (Profitability of Owner's Equity, net profit margin, gross profit margin, operational profitability).

Before analyzing the tourism sector in Turkey, some ratios of developing countries and European Countries are presented below in order to put forward the level of the changes in the global arena.

**Table 2** Average Financial Structure and Profitability ratios of selected Countries (2006)

Ratios	Developing Countries (%)	Europe (%)
Total Liabilities /Total Assets Ratio	47.12	74.93
Owner's Equity/Total Asses Ratio	52.88	25.07
Total Liabilities / Owner's Equity Ratio	89.10	298.83
Net Profit/ Owner's Equity Ratio	14.76	18.36
Net Profit/ Total Assets Ratio	7.81	4.60

<http://pages.stern.nyu.edu/~adamodar/>

If we look at the 2006 averages of the selected countries, it can be seen that tourism sector averages are close to the averages of those countries.

In a study based on the average values of the period 1995-2005 depending on the data from sectoral balance sheets of CBRT, concerning the financial structure of some companies grouped in several criteria, it was found that companies used short term sources in financing and owner's equity and commercial debt was dominant in financing sources.

It is seen that a significant progress has been made in liquidity ratios after 2002, such that average of current ratio reached to 2.10, while it was 2.0 in 1998.

Especially in 2001-2003 period, credit usage decreased to the levels below previous years. While in 2002 45% of total assets was financed through borrowing, in 2006 total assets financed through borrowing decreased to 43%, of which 46% were financial credits.

**Table 4** Financial Structure and Profitability of the Companies:  
 1998-2006

	1998	1999	2000	2001	2002	2003	2004	2005	2006
<b>LIQUIDITY RATOS</b>									
Current Ratio	2.00	1.80	1.58	1.65	1.63	1.80	2.10	2.00	2.10
Liquidity Ratio	1.20	1.15	1.13	1.25	1.35	1.25	1.40	1.60	1.55
Cash Ratio	0.45	0.62	0.56	0.42	0.38	0.34	0.32	0.56	0.53
<b>FINANCIAL STRUCTURE RATIOS</b>									
Long Term Liabilities /Assets Ratio	0.10	0.13	0.17	0.15	0.19	0.22	0.25	0.19	0.20
Financial Liabilities /Assets Ratio	0.23	0.22	0.18	0.25	0.28	0.22	0.24	0.20	0.23
Financial Liabilities /Total Liabilities Ratio	0.45	0.56	0.52	0.67	0.63	0.58	0.68	0.64	0.58
Short Term Trade Payables /Assets Ratio	0.11	0.14	0.12	0.11	0.12	0.13	0.16	0.15	0.18
Short Term Trade Payables/ Total Liabilities Ratio	0.22	0.26	0.21	0.25	0.23	0.24	0.28	0.26	0.25
Owner's Equity/Assets Ratio	0.38	0.46	0.49	0.38	0.48	0.46	0.53	0.56	0.52
Leverage Ratio	0.65	0.56	0.54	0.52	0.51	0.58	0.67	0.63	0.66
<b>ASSETS PROFITABILIT Y</b>									
Return on Equity	0.18	0.23	0.11	0.26	-0.10	-0.26	0.17	0.18	0.17
Net Profit Margin	0.32	0.23	- 0.08	- 0.02	- 0.15	0.12	0.15	0.22	0.15
Gross Profit Margin	0.38	0.35	0.20	0.12	0.22	0.36	0.18	0.34	0.25
Operating Profit	0.12	0.08	0.01	0.07	0.10	0.12	0.13	0.18	0.12

After the general setback in profitability ratios in 1999-2003 period, a recovery period is seen as the assets profitability rose to 4% in 2006 from -12% in 2001 and return on equity reached to 17% in 2006, from -10% in 2002 with a big take off. On the other hand, the inexistence of a significant recovery in operating profitability may be explained by the income of the tourism companies being in foreign currency while the costs accrued in TL after 2003. It may be said that in this period depreciation of foreign currencies against TL may also be a reason. Another point emphasized frequently, especially recently within the framework of financial liabilities of the companies has been the amount of the liabilities in foreign currency.

In the period of post 2001 crisis, it is seen that the ratio of long term, short term and financial liabilities to assets increased. The assets of those firms grew faster than their liabilities. In other words, liabilities increased or short term liabilities decreased.

It is seen that in the period 1998-2006, short term trade payables/total assets ratio increased again to the level of 18% due to the effects of Asian crisis and following 2000 and 2001 economic crisis. Anyhow, in last three years the weight of short term liabilities in company finance decreased compared with the previous period and the ratio of it in total assets is accrued around 12%.

If the consolidated balance sheets formed from six months financial tables of the 172 industrial companies traded on ISE during 2000 and 2001 crisis of Turkey are analyzed, it will be seen that while the establishments have turned over the money they used 1.51 times in 2000, in the year 2001 they turned it over 1.37 times. The situation is the same for tourism sector.

Foreign exchange position rate is used to analyze the foreign currency risks of the companies based on assets and liabilities in foreign currency. Foreign Currency Position Rate may be calculated as  $(\text{Assets in Foreign Currency} - \text{Liabilities in Foreign Currency}) / \text{Assets Total}$ . According to the analysis depending on this, foreign currency position rate of tourism sector in the year 2000 was -2%. This ratio is considerably more than the other sectors. For instance, it is - 24% in construction sector.

While the liquid assets of the sector increased 15% in real values during the period of 2001 crisis, their share in circulating assets increased from 15.6% to 17.3%.

Net working capital of the establishments shows an increase comparing with the previous year. Also no significant change took place during 2001 crisis period. This can not be commented as the

establishments in tourism sector were not affected, because the share of circulating assets was low while the share of short term liabilities was high, which had always been risky for the sector. All the improvements in the net working capital are crucial because they show the ability and capacity of the firm to pay all its short term debts.

- The firms increased the risk more by taking out new loans in order to compensate the problems in the assets and liabilities of their balance sheets and to improve the financial structure by increasing the profit ratios via focusing on traditional activities and to solve the problems in liquid debts. The changes observed and the precautions are summarized below; The scarcity of the working capital leads to cuts on the growth budgets (like postponement of the repair and maintenance programs, delaying the modernization and expansion activities) and decrease the performance and productivity in the end.
- Current ratios are generally high during crisis periods. This stems from the firms not being able to collect their receivables.
- Bris, in his study on 3617 establishments of 17 countries including Turkey between 1985-2000, found that the current ratio, which has been the most important parameter to measure the financial vulnerability of a firm, decreased to 1.33 from 1.38 over three years before the crisis Bris and Others (2001). This suggests the existence of a gap in the net working capital of the firms before the financial crisis.
- During the crisis periods the amount of overdrafts, which were used the most widely by the Turkish firms as a credit type, decreased. On the other hand, the cost of credits became higher by the reason of flexible interest rates.
- It is seen that firms avoid postdated checks during 1998 and 2001 crisis and a high amount of decrease of 30% -40% is recorded in the volume of checks.
- Profitability ratios of tourism firms were lower than the other industrial and service sectors. The yield from owner's equity should be emphasized. Each of those criteria of profitability was another criterion of the operational success of the firm.

- The tendency of mergers and takeovers of companies increased after 1980. This is also seen in tourism sector even in low figures.

## RESULT

After 1980s, financial yield of the firms was greater than the yield from real sector. This encourages the firms to invest on non-productive assets. At the same time, an increase was observed in the number of financial companies. Besides, the share of tourism sector in the whole economy has increased.

The increase of the activities of financial companies also increased globally forced all the financial and non-financial companies invest in financial assets. This transforms the potential crisis to global level. Turkey was the country most affected during the global crises. This is observed obviously in the crisis of 1998, 2001 and subsequent crises.

One of the reasons that the firms in Turkey are more vulnerable during crisis periods was the inadequacy of capital stock equity and carrying on the activities mainly by short term debts. Even in big establishments, average owner's equity ratio is 30% of the total assets.

The tendency of investment during the expansion periods before the crisis, leads the firms to external financing in order to adjust the lack of capital due to the scarcity of retained profits.

The periods before and after the crisis has been significant to understand the changes in capital structure during the crisis periods. It was found that capital structure has been on the behalf of credits and credits have been mostly commercial credits and borrowings during pre-crisis periods. During crisis and post-crisis periods the cost of borrowing increased and the terms become shorter. This as well puts the firms in a difficult position.

The incomes being mostly in foreign currency decreases the foreign currency risk to some extent in tourism sector. However, the foreign currency position has been -2% during the period in question. Despite the low risk in foreign currency position, incomes in local currency have been decreased and on the other hand costs have increased due to the appreciation of local currency against foreign currency. This also decreased the profitability of the firms.

During crisis periods, current ratio of the firms increases, collection of the receivables are delayed, accordingly borrowing increases. This increases the liability ratio in financial structure.

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## ENDNOTES

### Areas of study Destinations Tourism Companies

Company Names	
Altinyunus Çeşme	
Marmaris Martı	
Çelebi Havayolları	
Favori Dinlenme Tesisleri	
Marmaris altinyunus	
Net turizm	
Petrokent turizm	
Tek-art turizm	

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