

EFFECT OF CAPITAL STRUCTURE ON COMPANY PERFORMANCE IN SRI LANKA

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Abstract

The objective of all financing decisions is wealth maximization and the immediate way of measuring the quality of any financing decision is to examine the effect of such a decision on the company's performance. Capital structure is a financial tool that helps to determine 'how do firms choose their capital structure?' a firm's capital structure is then the composition or structure of its liabilities. Therefore managers need to take decision very carefully regarding to the capital structure of company. Capital structure is defined as the relation between the debt and equity that is used to finance firm's assets (Moyer 2001, McMenamin 1999). The choice of a capital structure of a firm can equally be viewed from the management and the ownership structure of the company (Du and Dai, 2002). Pindado and Torre (2004) posit that the capital structure of a firm is determined by the incentives and goals of those who are in control of the firm. Capital structure decision is the mix of debt and equity that a company uses to finance its business (Damodaran, 2001).

The objective of this research is that investigates how the capital structure affects the company's performance. The research is focusing on Impact of capital structure listed companies in Colombo Stock Exchange Market according to the variable and the study base on secondary data. The data are collected from published annual reports on individual companies, Colombo Stock Exchange books, Colombo Stock Exchange journals and magazines. The sample for this study is taken from 10 firms. The sample period is 10 years ranging between 2005 and 2015 and it is ensured that each of the firms has data for at least five years during this period under study. The method of data analysis use in this research work is the descriptive, correlation and regression technique. The data is on the key variables: ROI, ROA, debt-equity ratio, long term debt to capital employed ratio, total debt ratio and age. An exercise is carried out in this respect using debt-equity ratio, long term debt to capital employed ratio, total debt and age as Independent variable while using ROI and ROA as Dependent variables. Expecting findings are capital structure is significantly impact on company performance and capital structure measures are negatively related to firm performance.

Key words: Capital Structure; Company Performance; Debt and Equity; Stock Exchange