Effect of Capital Structure Towards Profitability on Listed Manufacturing Firms in Colombo Stock Exchange

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ABSTRACT

Introduction - A firm's capital structure emphasizes how firm finances its assets through debt, equity, or a combination of these two ways. The capital structure instruments include the company's long-term debt, common equity & preferred shares.

Design/Methodology/Approach – Published annual reports of listed manufacturing companies used to collect data in the Colombo Stock Exchange (CSE). The study selected 37 manufacturing companies listed in CSE as of 31st December 2019 out of 289 listed companies. The study analysed data through descriptive statistics, regression analysis, the Hausman test and correlation to evaluate the relationship.

Findings – The study found a negative and significant relationship between DTE, LTDTE, SIZE and profitability; the DTA has a positive relationship with profitability. It is not substantial with both ROE and ROA, which revenues the capital structure significantly impacted the profitability of manufacturing firms due to three variables significant with ROE and ROA out of four variables. The study found that long-term debt is not significantly impacting because companies maintain their capital structure with short-term debt and less long-term debt.

Conclusion – The study concluded that a significant relationship between capital structure and profitability, and long-term debt is not a significant factor in the manufacturing sector. Further, it justified that optimum capital structure is a mixer of debt and equity because vital variables represent both equity and debt in the model.

Keywords: *Capital Structure, Financial Performance, Profitability, Equity, Manufacturing Companies.*