

# Liquidity and Capital Structure: The Case of Sri Lanka

Athambawa Jahfer<sup>1</sup> and Sumudu Inoshika Madurasinghe<sup>2</sup>

<sup>1</sup> Senior Lecturer, Department of Accountancy and Finance, Faculty of Management and Commerce, South Eastern University of Sri Lanka

<sup>2</sup> Assistant Lecturer, Department of Accountancy and Finance, Faculty of Management and Commerce, South Eastern University of Sri Lanka

## Abstract

This research tries to contribute to corporate finance through the study of the relationship between capital structure and liquidity of manufacturing firms in Sri Lanka. The previous studies indicate an inconsistent relationship between liquidity and capital structure. The aim of the research is to investigate the association between capital structure and liquidity of listed manufacturing sectors in Sri Lanka. Data were gathered from annual reports 37 manufacturing companies listed in the Colombo stock exchange during 2009 to 2016. The relationship between capital structure and liquidity was analysed using panel data fixed effect models. The results show that all liquidity ratios namely: Current, Cash and Quick are significantly negatively associated with capital structure and Liquidity Ratio is also insignificantly negatively associated with capital structure. Therefore, we could conclude that there a negative relationship between liquidity and capital structure among the manufacturing companies in Sri Lanka. Further, it was found that size of the firms is significantly negatively associated with capital structure and Profit and Non-Debt Tax Shield are significantly positively associated with capital structure. There is no any significant relationship between tangibility and capital structure.

**Keywords:** - Capital structure, Liquidity, Profit, Tangibility, Size, Non-Debt Tax Shield