

**IMPACT OF OPERATING LEVERAGE ON PROFITABILITY
OF LISTED COMPANIES IN THE MANUFACTURING SECTOR
IN SRI LANKA**



By

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A Project Report

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ABSTRACT

Strategic cost structure choices determine how firms divide operating costs between fixed and variable components, and therefore have important implications for financial performance. Using a measure of operating leverage that directly reflects the importance of fixed, current and operating costs in firms' cost structures and in this way, the present study is initiated to find the relationship between operating leverage and profitability.

The study covered twenty five listed companies which were selected from manufacturing sector in Colombo Stock Exchange over the period of four years from 2015 to 2018. Operating leverage was measured by using net operating asset turnover, fixed asset turnover and current asset turnover and profitability was measured by using return on assets. Descriptive analysis, correlation analysis and regression analysis were used in analysis and finding suggests that there is both significant positive relationship and insignificant negative relationship between operating leverage and profitability of selected manufacturing companies in CSE.

The result of this study generally shows that there is a significant impact on operating leverage on profitability of listed companies in the manufacturing sector in the Colombo Stock Exchange. Net operating asset turnover has an insignificant, weak negative relationship between operating leverage while fixed and current asset turnover has a significant positive relationship between operating leverage and profitability of the manufacturing sector in CSE. Finally, it can be concluded that Finally, it was concluded that, operating leverage describe 8.6% of variation of profitability of manufacturing companies and the level of operating leverage and profitability varied according to the ratios which used to measure main variables. However, the findings of this research are based on ratios that used for the study and the nature of the companies.

The finding is more useful to financial managers of companies for taking sound decisions on the proper tradeoff between liquidity and profitability. Researcher conclude that operating leverage is an important determinant of financial policies and why managers give their concentration on operating leverage.

Keywords: *Operating Leverage, profitability, manufacturing firms*

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