

Effect of Leverage on Financial Performance

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A B S T R A C T

Financial Leverage is most crucial and significant when making financial decisions for a firm. Literature provides conflicting opinions about the optimal debt-equity mix. Furthermore, most researchers have taken the same indicators to measure financial performance. Financial leverage is a significant point when making decisions. Therefore, this study was conducted using a quantitative approach to examine the impact of financial leverage on financial performance in companies listed on the Colombo Stock Exchange. Fifty listed companies were selected as the sample. The data was collected using published annual reports for the ten years from 2011 to 2020. The debt to asset ratio and debt to equity ratio were used for measuring the financial leverage. Tobin's Q and Price-Earnings ratio were used as indicators of financial performance. Moreover, firm growth, liquidity, and tangibility were used as control variables. Data were analyzed using multiple regression analysis. The results suggest that high leverage negatively affects financial performance. Using only secondary data and excluding the banking sector are limitations of the study.

Keywords: Colombo Stock Exchange (CSE), Financial Leverage, Tobin's Q (TQ), Price Earnings Ratio (PER)

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