IMPACT OF WORKING CAPITAL MANAGEMENT ON PROFITABILITY: AN EMPIRICAL EVIDENCE FROM LISTED MANUFACTURING COMPANIES IN SRI LANKA

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ABSTRACT

Working capital management (WCM) is an integral part of financial management and management of working capital may have a significant impact on the profitability. This study explores the effect of working capital management on firm profitability in Sri Lanka covering the period of 5 Years from 2011 to 2015, based on a sample drawn from the listed manufacturing companies. The sample comprises of 25 manufacturing companies listed on the Colombo stock exchange (CSE). In order to examine the effects of WCM on the firm profitability, the ROA and ROE were used as measures for profitability. WCM was measured using the number of days of inventory, number of days of receivables and number of days of payables, considering these WCM ratios, jointly cash conversion cycle (CCC) was estimated. Data of the selected firms which are listed in the CSE were obtained from their websites. Pearson's correlation and regression analysis are used in drawing empirical evidence to answer the research questions of the study. The results depict that there is negative association and impact between CCC and profitability, measured by ROE and ROA. Which indicate that, as the cash conversion cycle increases it would tend to reduce the profitability of the company. The results revealed that, CCC is significantly impact on return on asset (p=0.014) at the significant level 0.05. And cash conversion cycle is significantly negative correlated with return on asset (-2.504) at the level 0.05.*

Keywords: *Cash conversion cycle, Colombo stock exchange, Profitability, Working capital management.*

1. INTRODUCTION

Working capital management (WCM) is an integral part of corporate finance. WCM deals with the problems that arise in managing current assets (CA), current liabilities (CL) and the interrelationship that exist between them. Usually working capital gets converted into cash within 12 months (Dong & Su, 2010). Finance managers spend much time on day to day problems that involve in working capital decisions. Inadequate working capital leads the company to bankruptcy. On the other hand too much working capital results in wasting cash and ultimately the decrease in

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