

Determinants of Capital Structure: An Analysis of Pre and During Economic Crisis – Evidence from Listed Consumer Services Sector Companies in Sri Lankan Stock Exchange

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Abstract

Introduction: Leverage plays a vital role in optimizing capital structure, and identifying determinants of leverage across varying economic conditions is crucial for strategic financial management. However, limited research focuses on recognizing key determinants of leverage of the consumer service sector in Sri Lanka, creating a gap in understanding its unique leverage dynamics and determinants. To fill this gap, this research endeavor aimed to examine the determinants of financial leverage in consumer service companies in Sri Lanka, with a specific focus on how these determinants behave before and during an economic crisis.

Methodology: This study adopted a quantitative methodology to investigate the impact of firm profitability, size, asset tangibility, and growth on leverage, measured by the long-term debt-to-asset ratio. Data were collected from 15 listed Sri Lankan consumer service corporations, selected by size, covering eleven years from 2014 to 2024. Panel regression analysis was performed to identify the effects of these variables on leverage under different economic conditions.

Findings: Profitability consistently showed a notable adverse effect on leverage, intensifying during downturns as firms prioritized internal financing to mitigate risks. Asset tangibility positively influenced leverage but diminished in relevance during crises. Firm size positively impacted leverage over the years, but larger firms adopted conservative financing strategies during economic uncertainty, mirroring smaller firms. Growth consistently exhibited an adverse effect on leverage, as growing firms avoided excessive debt, favoring financial stability.

Conclusion: In conclusion, this impact slightly weakened during crises due to restricted external financing access. This emphasizes the importance of understanding contextual factors that influence financial decisions during instability. These findings benefit corporate managers and policymakers by enabling more informed strategies for risk management and sustainable finance.

Keywords: Capital Structure, Consumer service companies, Economic Crisis, Leverage