

TRADE-OFF BETWEEN LIQUIDITY AND PROFITABILITY

A COMPARATIVE ANALYSIS BY INDUSTRIES

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ABSTRACT

Profitability and liquidity are the most prominent issues that finance management of each organization should take studying and thinking about them into account as their most important duties. Profitability is a measure of the amount by which a firm's revenues exceeds its relevant expenses. Liquidity refers to the ability of a firm to meet its short term obligations. Profitability is measured by accounting base measurements Return on assets and liquidity measured on Current Ratio.

Firms with high liquidity may have low risk and then low profitability. Conversely, firm that has low liquidity may face high; Industries are required to maintain a trade-off balance between liquidity and profitability in its day to day operations. However, too much attention on profitability may lead the firm into a pitfall by diluting the liquidity position of the organization. Trade-off level is of major importance to both the internal and external analysts because of its close relationship a business. Hence, the present study is initiated to identify the trade-off between liquidity and profitability of a comparative analysis by industries in Sri Lanka.

This research has focused on what extent does the trade-off level between Profitability and Liquidity vary by industrial types. To identify the significant variation in liquidity and profitability trade off level among manufacturing sector, services sector, and trading sector.

The study covered 25 listed Companies in the Colombo Stock Exchange a period of past four years from 2010 to 2013. All the data were collected from annual reports of each company and data were analysed by using Ratio analysis, descriptive statistics and ANOVA test Analysis.

According to study results, trade-off level between Profitability and Liquidity vary by industrial types. Manufacturing sector trade off level is very high. Service sector and trading sector trade off low level.

Keywords: Liquidity, Profitability, Trade-off.

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