



IMPACT OF CASH MANAGEMENT ON FINANCIAL PERFORMANCE OF THE SRI LANKAN MANUFACTURING COMPANIES

Janaki Samuel Thevaruban¹

¹Senior Lecturer, Department of Finance and Accountancy, Faculty of Business Studies, Vavuniya Campus of the University of Jaffna, Sri Lanka

ABSTRACT

This study is sought to establish the impact of cash management practices on financial performance of Sri Lankan Manufacturing companies. The target population of the study was 39 manufacturing companies in manufacturing sector. A sample of 20 manufacturing companies was selected from the population. The selection of sample was made based on the availability of full data set for the period of five years from 2010/11 to 2014/15. The main objective of the study is to examine the impact of cash management on the financial performance of Sri Lankan manufacturing companies. It has consisted four sub objectives based on the proxies of independent and dependent variables. The independent variable of the study was cash management with the proxies of cash ratio and cash turnover ratio. The dependent variable of the study was financial performance with the proxies of Return on Equity (ROE) and Return on Assets (ROA) main hypotheses of the study was "There is an impact of cash management on the financial performance of the Sri Lankan manufacturing companies". The study used secondary data and the research design used for this study were descriptive statistics such as mean, Standard deviation, Coefficient of variance and Inferential statistics such as correlation and regression analysis by using Statistical Package for Social Science (SPSS) version 23 package. The findings revealed that Cash Ratio has negative impact with Return on Equity. Same as Cash Ratio negative impact with Return on Assets also. Therefore Cash Ratio is having negative impact on Return On Equity and Return On Assets. However Cash Turnover Ratio was insignificant with Return On Equity and Return On Assets. That mean Cash Turnover Ratio did not have any influence on Return On Equity and Return On Assets of the Sri Lankan Manufacturing companies. Therefore the main hypothesis of the study was partially accepted.

KEYWORDS: Cash Management, Cash Ratio, Cash Turnover Ratio, Financial Performance, Return on Equity, Return on Assets



1. INTRODUCTION

Cash Management is essential to every business that designs to meet up with its financial obligations. No business operation is isolative of cash management. Olowe (1998) said that cash is regarded as the most important current asset for the operations of businesses. Cash is the basic input required to keep the business running on continuous basis and it is also ultimate output expected to be realized by selling the services or products manufactured by firm (Pandey, 2004). Cash Management is imperative in every business organization as cash is said to be the life blood of any business. The essence of cash management is to ensure positive cash flow for smooth business operation. According to Ross et.al (2011) said and as stated by Atrill (2003) that efficient cash management involved the determination of the optimal cash to hold by considering the trade-off between the opportunity cost of holding too much cash and trading cost of holding too little. Therefore there is the need for careful planning and monitoring of cash flows overtime as to determine the optimal cash to hold. According to Gitman (2009) it is objectively used to manage and determine the optimal level of cash required for business operation and the investment in marketable securities, which is suitable for the nature of the business operation cycle. The pattern of the cash and operating cycle varies per industry, but in general term, the pattern involves the provision of cash as capital for firm's initial outlay, the procurement of raw material in manufacturing companies and finished goods in marketing companies, distribution of the finished goods obtain immediate cash or create debtors when goods are sold on credit term (Akinbuli, 2009). Furthermore, the process of managing cash has become a major challenge for most of the companies, because of its significant impact on the results of a company (Ekwere, 1993). The success of any business venture is predicted on how the management has planned and controlled its cash flows (Akinsulire, 2003). Effective cash management is the fundamental standing point to ensure that the firm's finances are in strong position. Further the cash management is very vital for production firms whose assets are mostly composed of current assets (Hornead Wachowity 1998). According Raheman and Nasir (2007) said that cash management directly affects liquidity. Efficient Cash management contributes positively to the performance of firms and their survival. Deloof (2003) said that cash management is an important source of competitive advantage of businesses. Therefore the success and failure of a business firm depends on the efficiency of cash management practices.

2. LITERATURE REVIEW

This section reviews various past studies relating to cash management and financial performance aspects to identify the research gap of the study.

Shin and Soonan (1998) examined that, by using a sample of American Manufacturing firms for the period 1974-1995 and found that there is statistically negative relationship between cash conversion cycle and profitability.

Ebben and Johnson (2011) investigated the relationship between cash conversion cycle and levels of liquidity, invested capital and performance in small firms over time. The sample considered for this study was eight hundred and seventy nine small US manufacturing firms. This study highlighted that the significance of cash conversion cycle as productive management tool for small firm's owners.

John (2014) carried out research on effect of cash management on profitability of Nigerian manufacturing companies. Cash conversion cycle considered as the independent variable with the proxies of cash ratio (CR), debt ratio (DR) and sales growth (SG); dependent variable is profitability with the proxies of Return on Assets (ROA) and Return on Equity (ROE). Correlation and regression analysis were carried out. The results revealed a positive and significant relationship between Cash Conversion Cycle (CCC) and ROE, on the other hand non significant negative relationship between cash conversion cycle and ROA.

Festo (2011) examined the cash management and growth of small scale businesses at Ntun gamo market in Uganda. Primary and secondary data considered for this study. The results of this study indicated that cash management is an essential aspect of the business. For the poor cash management practices constrains business operations and some customers who are not satisfied with the services ran away signifying poor performance and hence retardation in the business growth.

Godwin (2013) carried out investigation on cash management on profitability of financial institution ; a case study of Bank of Africa Uganda. Primary data have collected through distributed questionnaires to 60 staff of the bank. The findings of the study revealed that cash management in Bank of Africa affects the profitability levels. Further he found that the bank was adopted several cash management techniques in order to reduce fraud of cash in the bank.

Atton (2012) examined cash management practices by micro and small scale enterprises at Kasona in the central region of Ghana. He found that cash shortage

is a chronic challenge to the firms and cash management is very crucial to the survival and growth of micro and small scale enterprises.

Abiorro (2013) carried out an investigation on the impact of cash management on the performance of manufacturing companies in Nigeria. He found that reductions in both account receivable (measured as days of sales outstanding) and reductions in Inventory (measured as days of inventory outstanding) associate with positive improvements in firm financial performance.

Velnamby and Kajanathan (2013) have analyzed cash position and profitability among listed telecommunication firms in Sri Lanka. They have considered cash position as the independent variable and Profitability considered as dependent variable. Based on the descriptive analysis they found that cash position ratios have the influence or impact on the profitability.

From the above summarized literature reviews there was only few research have done in Sri Lanka. It was evidence that research in the area of cash management has not been done in a more comprehensive approach. Because this study research gap scarcity demonstrated by scarcity of empirical studies on cash management of the manufacturing companies in Sri Lanka to remain competitive emphasis should be made on cash management and financial performance with regards to how their ability to manage financial performance and should be provided to organizational achievement.

3. NEED/IMPORTANCE OF THE STUDY

The importance of this study may have implications for other sector companies in Sri Lanka who are trying to make decisions regarding cash management reform model and further finding of study would help to develop an understanding in the advantages and disadvantages of financial practices and techniques of managing cash management strategies such as policies, practices and techniques of managing cash management components in the Sri Lankan manufacturing companies and globally. A general conceptual framework model will provide basic guidelines for researchers, Accountants and professionals financial managers and policy makers the manufacturing companies' environment of Sri Lanka. Further this study would suggest various cash management techniques to Sri Lankan manufacturing companies can use to measure their performance in terms of cash ratio and cash turnover ratio.

In Sri Lanka manufacturing companies faced challenges of financial performance they may defer their payments to creditors which is a harmful for the

manufacturing companies and co results in several consequences such as worse credit term in future. This will affect their profitability in the long run. Therefore, if this is continued, it will cause the number of problems to not only for Sri Lankan manufacturing companies but also various stakeholders, whom depend so much on cash management. Therefore this research will help Sri Lankan manufacturing companies to solve cash management practices problem in future. Olowe (2008) found that cash management is concerned with the efficient management of cash so as to achieve an optimum level of cash is the firms' working capital. Therefore the study will be helped the Sri Lankan manufacturing companies to maintain suitable level of cash and cash equivalent to keep its manufacturing activities smoothly. Further study would be useful not only to Sri Lankan manufacturing companies, but also to all business firms throughout the country and other developing economy also. This will also help the stakeholders in business to formulate and implement better cash management policies as well as practices that will help than to manage cash better. It will also useful policy makers of the country also.

4. STATEMENT OF THE PROBLEM

In Sri Lanka, manufacturing companies play a major role to the development of the economy. Manufacturing companies in Sri Lanka are still in a developing stage. They need more short-long investments and finance for expansion of their operational activities. Managing the cash is real challenge to financial managers in Sri Lankan manufacturing companies. Further some of the Sri Lankan manufacturing companies obtained cash from inappropriate sources that were created problems of cash and cash equivalent mismatch in investment decisions. This will lead Sri Lankan manufacturing companies facing the problem of cash management and as well as financial performance of Sri Lankan manufacturing companies.

Further, most of the Sri Lankan manufacturing companies operate at a profit level but they still run into more financial problem resulting inadequate capital to provide the cash needed to pay debts and business activities.

The followings research question has been developed.

- How does the cash management impact on financial performance of the Sri Lankan manufacturing companies?

5. OBJECTIVES OF THE STUDY

The main objective of the study is,

- To examine the impact of cash management on the financial performance of the Sri Lankan manufacturing companies.

The sub objectives of the study are,

- To measure the Cash Ratio’s impact on the Return on Equity (ROE) of the Sri Lankan manufacturing companies.
- To identify Cash Turnover ratio’s impact on Return on Assets (ROA) of the Sri Lankan manufacturing companies.
- To study Cash Ratio’s impact on Return on Assets of the Sri Lankan manufacturing companies.
- To examine the Cash Turnover ratio’s impact on Return on Equity (ROE) of the the Sri Lankan manufacturing companies

6.HYPOTHESES

H1- There is an impact of cash management on financial performance of the Sri Lankan manufacturing companies

H1a- Cash Ratio is having a significant impact on the Return on Equity of the Sri Lankan manufacturing companies

H1B- Cash Turnover ratio is having a significant impact on the Return on Assets of the Sri Lankan manufacturing companies

H1C- Cash Ratio is having a significant impact on the Return on Assets of the Sri Lankan manufacturing companies

H1d- Cash Turnover ratio is having a significant impact on the Return on Equity the Sri Lankan manufacturing companies

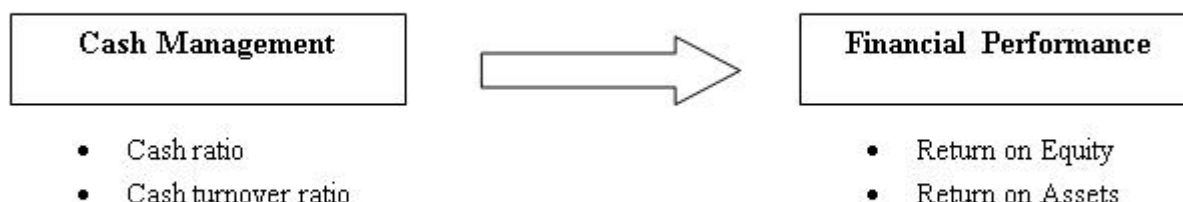
7. METHODOLOGY

This study used secondary data of 20 manufacturing companies out of 39 manufacturing companies listed in the Colombo Stock Exchange for last 5 years. (see appendix 01) Manufacturing companies which have full data for the whole study period 2010/11 to 2014/15 . The sampling method is random sampling method used to collect data and data set also collected from published annual reports of the selected manufacturing companies in the Colombo Stock exchange web site. Researcher has used SPSS version 23 to analysis the data.

8. CONCEPTUAL MODEL

Conceptual framework is a scheme of variables which the study Operationalization in order to achieve the set of objectives. The independent variable of the study is cash management with the proxies of cash ratio and cash turnover ratio. The dependent variable of the study is financial performance with the proxies of Return on Equity and Return on Assets.

FIGURE o1 CONCEPTUAL MODEL



Source: Developed by the researcher

Based on the above conceptual model (Figure 01) researcher has developed two multiple regression model for the analysis purpose

$$ROE = \beta_0 + \beta_1 CR + \beta_2 CTR + e$$

$$ROA = \beta_0 + \beta_1 CR + \beta_2 CTR + e$$

Where,

- ROA= Return on Assets
- ROE=Return on Equity
- CR= Cash ratio
- CTR= Cash turnover ratio
- β_0 = Coefficient of variables
- e= Error term

Table 1 : Operationalization Table

Concepts	Variables	Measures
Cash Management	Cash Ratio	$\frac{\text{Cash + Cash equivalents}}{\text{Total Current Liabilities}}$
	Cash Turnover Ratio	$\frac{\text{Sales Revenue}}{\text{Average cash and cash equivalents}}$
Financial Performance	Return on Equity	$\frac{\text{Net income after tax}}{\text{Total equity}}$
	Return on Assets	$\frac{\text{Net income after tax}}{\text{Average total Assets}}$

Source: Developed by the Researcher

This Operationalization is the most important in the entire research.

9.RESULTS & DISCUSSIONS

Table 1 : Descriptive Statistical Data Analysis for Selected Manufacturing Companies during the Period of 2010/11 to 2014/15

	N	Minimum	Maximum	Mean	Std. Deviation
Cash Ratio	100	.002	5.239	.29476	.848621
Cash Turnover Ratio	100	.370	792.637	9.53468	169.786773
Return on Equity	100	-.399	.677	.11436	.156026
Return on Assets	100	-.242	.409	.06429	.096423
Valid N (List wise)	100				

Source: Calculations are based on annual reports of 20 manufacturing companies

Cash ratio has maximum value of 5.23 and minimum value was 0.002 followed by a mean of 0.29 and its standard deviation was 0.84 from the mean value. Cash turnover ratio shows during the past five years manufacturing companies have minimum cash turnover ratio nearly 0.37 where maximum was near to 792.63 times. In past five years manufacturing companies have earned nearly 9.53 times revenue as their cash in hand and its

standard deviation was 169.78 times. Further the descriptive statistics results depicted the mean value as Return on Equity was 11.4%. The maximum value and minimum values of Return on Equity respectively were 67.7% and 39.9%. That implied Return on Equity was also not perform remarkable position. Its standard deviation 15.6% deviated from mean value. Return on Assets has mean and standard deviation of the manufacturing companies are 6.4% and 9.6% respectively.

Table 1: Model Summary of the Regression Analysis

Model	R	R square	Adjusted R square	Std. error of the estimate
1	.296 ^a	.088	.069	-150567

a. Predictors(constant): Cash, Turn over, Cash ratio

b. Dependent variable: Return on Equity

Source: Calculations are based on annual reports of manufacturing companies

Table 03 illustrates the correlation value is .296. The coefficient of determination of factor which was (R^2) is 0.088 implied 8.8% of the total variance in ROE could be explained by the dependent variables. It means that 8.8% of the cash management practice by other factors. Therefore a Table 03 show the coefficient of determinants is 0.069, of the variation in the ROE is explained by Cash

ratio and Cash turnover ratio of the Sri Lankan manufacturing companies.

Impact on return on equity as well as balance 91.2% Return on Equity is decided by other factors such as micro and macro environmental factors. Therefore, about 6.9% of the variation in ROE is explained by cash ratio and Cash Turnover Ratio.

Table 4: Model Summary of the Regression Analysis

Model	R	R square	Adjusted R square	Std. error of the estimate
1	.287 ^a	.082	.063	.099314

- a. Predictors: (constant) Cash turnover ratio, Cash ratio
- b. Dependent variable: Return on Assets

According to table 04 value of R² is 0.082 is implied that 8.2% of the total variance in ROA could be explained by cash management practice. As well as remaining 91.8% Return on Assets is decided by other factors. The model summary as well as remaining 91.8% Return on Assets is decided by other factors. Table 04

shows the coefficient of determination (Adjusted R square) is 0.063. Therefore about 6.3% of the variations in the Return on Assets are explained by Cash Ratio and Cash Turnover Ratio of the Sri Lankan manufacturing companies.

Table 5: Correlation Analysis

		Cash Ratio	Cash Turnover Ratio	Return on Equity	Return on Assets
Cash Ratio	Pearson correlation	1	-.174	-.246*	-.253*
	Sig. (2 tailed)		.084	.014	.011
	N	100	100	100	100
Cash Turnover Ratio	Pearson correlation		1	-.119	-.090
	Sig. (2 tailed)			.239	.372
	N		100	100	100
Return on Equity	Pearson correlation			1	.885*
	Sig. (2 tailed)				.000
	N			100	100
Return on Assts	Pearson correlation				1
	Sig. (2 tailed)				
	N				100

*Correlation is significant at the 0.05 level

** Correlation is significant at the 0.01 level

According to the analysis the Table 05 shows (-24.6%) negative significant relationship between Cash ratio and Return on Equity. It was significant at the 5% percent. That is when cash ratio is increased; Return on Equity will be decreased. Looks likes this cash ratio negatively (-25.3%) correlated with Return on Assets at the 5% level. This is mean that when the Cash Ratio increased Return on Assets will be decreased. Further Cash turnover is having

insignificant correlation between Return on Equity (11.9%) and Return on Assets (9%). According to the table 05 revealed one of the proxies of independent variables such as Cash ratio shows negatively impact on the financial performance. Especially Return on Equity (ROE) and Return on Assets (ROA) and Cash Turnover ratio are insignificant impact on the financial performance specially Return on Equity and Return on Assets.

Table 6: Coefficient Analysis- Independent Variables (Cash Ratio and Cash Turnover Ratio) and Dependent Variable (Return On Equity)

Model	Unstandardized coefficient		Standardized	t	Sig
	P	Std. error	Beta		
Constant	.143	.019	-	7.690	.000
Cash Ratio	-.051	.018	-.275	-2.794	.006
Cash Turnover Ratio	.000	.000	-.167	-1.693	.094

- a. Dependent Variable: Return on Equity

Model	Unstandardized coefficient		Standardized	t	Sig
	P	Std. error	Beta		
Constant	.081	.012		7.033	.000
Cash Ratio	-.031	.011	-.277	-2.801	.006
Cash Turnover Ratio	-7.856	.000	-.138	-1.401	.165

- a. Dependent Variable: Return on Assets

In Table 06 Cash Turnover ratio was insignificant. It indicates that cash turnover ratio was not impact on financial performance. Further the probability of T test of Cash Turnover ratio was higher than 5%. Since T test of P value was $0.094 > 0.05$ which illustrated that there was insignificant relationship between cash turnover ratio and Return on Equity. The probability of T test of cash turnover ratio was higher than 5%. Since T test of P value was $0.165 > 0.05$ which illustrated that there was insignificant relationship between cash turnover ratio and return on assets.

According to the above model cash ratio was significant at 5%. The probability of T test of Cash Ratio was less than 5%. T test value was $0.006 < 0.05$ which illustrated that there was a negative relationship between Cash Ratio and Return on Equity as well as Return on Assets ($\beta_0 = -0.051, T = -2.794, P = 0.006$). This mean is Cash Ratio increased but at that time financial performance decreased. Further result depicted that there was a negative relationship between Cash Ratio and Return on Equity ($\beta_0 = -0.031, T = -2.801, P = 0.006$) According to the coefficient analysis both ROE and ROA weakly and negatively correlated with Cash Ratio.

TABLE 7: Correlation of CR, CTR, ROE AND ROA

	Pearson correlation	Sig
CR and ROE	-.246	.006
CR and ROA	-.253	.006
CTR and ROE	-.119	.094
CTR and ROA	-.090	.165

Source: Based on SPSS Analysis results

According to the Table 07 there was negative relationship between Cash Ratio and Return on Equity and Return on Assets also. H1a and H1c hypothesis are accepted and have negative significant relationship. However Cash Turnover ratio was insignificant relationship with Return on Equity as well as Return on Assets. Therefore H1b and H1d hypothesis were rejected. Based on sub hypothesis H1 hypotheses can be partially accepted. Therefore researcher finally pointed out that cash management is having partially negative impact on financial performance of the Sri Lankan Manufacturing Companies.

10. FINDINGS

The study revealed that there was a negative significant relationship between Cash Ratio and financial performance of the Sri Lankan manufacturing companies. The findings revealed that Sri Lankan manufacturing companies do not like to hold too much cash for repay the current liabilities. Because Sri Lankan manufacturing companies can use cash and cash equivalents for operation activities such as purchasing materials , salary payment and etc. As well as they can use cash and cash equivalents for investing activities and get interest from it. Therefore in the Sri Lankan manufacturing companies Cash Ratio and Return on Equity and Return on Assets is having negative significant relationship.

This research further showed there was no significant relationship between Cash Turnover ratio and financial performance. Cash turnover ratio explains how many times Sri Lankan manufacturing companies have earned revenue as their cash in hand. If the Sri Lankan

manufacturing companies earn more times revenue as their cash in hand their return will slow down. This revealed that other than cash management revenue of the Sri Lankan manufacturing companies some more factors highly affect to the performance of Sri Lankan manufacturing companies.

11.RECOMMENDATIONS/ SUGGESTIONS

The Sri Lankan Manufacturing companies' finance managers have to keep more focus on cash position at any time. In general, a stable cash position should be maintained by the Sri Lankan manufacturing companies can easily meet its current liabilities with cash or liquid assets it has on hand. Further, better to implement on effective cash management program. Finance manager should always prepare cash budget and cash flow statement for effective cash planning and control. He should also make sure that the cash management process is in compliance with applicable laws, regulations and professional ethical standards, because the financial performance is the major factor in the going concern of business firms. The chief executive officers strive to achieve a reasonable level of financial performance in order to maximize their share holders wealth. Cash conversions cycle measures the lack it takes Sri Lankan Manufacturing Companies investments in raw materials to be realized. The finance managers should be strife to maintain a very low cash conversion cycle. From the sample some of the



Sri Lankan manufacturing companies used for this analysis almost all have too long days. This long a cash conversion cycle may have negative effect on the liquidity of the Sri Lankan manufacturing companies because cash will be tied in raw materials, inventory or accounts receivables. Further finally researcher recommends that on cash management practices, the employment of accounting experts assist the cash management of the Sri Lankan manufacturing companies' financial performance. Therefore these recommendations regarding cash management practices of the Sri Lankan manufacturing companies will help to improve financial performance and as well as increase their operational activities.

12. CONCLUSIONS

Effective cash management is critical to all firms, specially in the developing economy. A firm having a proper set of liquidity management policies and procedures will improve profits, reduce the risk of cooperate failure and significantly improve its opportunity of survival also. This study findings revealed that Sri Lankan manufacturing companies' Cash Ratio and financial performance was having negative significant relationship with each other. In addition to that Cash Turnover Ratio and financial performance do not have any kind of significant relationship with each other. That mean Financial performance of the Sri Lankan manufacturing companies do not determined by Cash Turnover Ratio. Therefore hypothesis H1a and H1c those are cash ratio is having a significant impact on Return on Equity and Return on Assets was accepted. At the mean time H1b and H1d Cash Turnover Ratio is having a significant relationship between Return on Equity and Return on Assets were rejected. Therefore the main hypothesis of the study Cash management is having a significant relationship with financial performance of the Sri Lankan manufacturing companies is partially accepted. Therefore management of Sri Lankan manufacturing companies need to ensure that there are adequate cash management control to ensure all the time there is optimal cash where there are strategies to be in place during minimal cash in hand and surplus cash in hand.

13. LIMITATIONS

There are 39 manufacturing companies listed in the Colombo Stock Exchange but the researcher considered only 20 listed manufacturing companies. And this research also based on the secondary data only. Further the period of study also 2010/11 to 2014/15 only for five years period only.

14. SCOPE FOR FUTURE RESEARCH

The presents study is considered only the listed manufacturing companies in Sri Lanka. But future researchers can investigate the relationship between Cash management and financial performance of the balance 19 different sectors.

Researcher has considered measuring cash management concept only with the proxies of cash ratio and Cash Turnover ratio and to measure the financial performance concept researcher has used only Return on Assets and Return on Equity. Therefore future researchers could be considered more variables and proxies to measure the relationship between cash management and financial performance.

This research conducted in Sri Lanka. Sri Lanka is a developing country. But in future researchers could conduct this research in the developed countries. Further researchers can make the comparison how this cash management is influencing the financial performance of developed and developing countries.

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APPENDIX

01: Sample (Sri Lankan Listed Manufacturing Companies)

No	Listed Manufacturing Companies in CSE	Symbol
01	Abans Electricals	AEP
02	ACL Cables PLC	ACLC
03	ACL Plastics PLC	ACLP
04	Acme Printing and Packaging PLC	ACME
05	Alu Fab PLC	ALUFAB
06	Central Industries PLC	CIP
07	Dipped Products PLC	DPP
08	Kelani Cables PLC	KCP
09	Kelani Tyres PLC	KTP
10	Lanka Aluminium Industries PLC	LAIP
11	Lanka Ceramic PLC	LCP
12	Laxapana Batteries PLC	LBP
13	Piramal Glass Ceylon PLC	LBP
14	Prient Core PLC	PP
15	Richard Pieris and Company PLC	RPCP
16	Royal Ceramic Lanka PLC	RCLP
17	Samson International PLC	SIP
18	Singer Industries Ceylon PLC	SICP
19	Swedeshi Industrial works PLC	SIWP
20	Tokyo Ceyment Company PLC	TCCP