ABSTRACT. This research paper primarily focuses on the impact of financial leverage on investment decisions of firms and it is an attempt to look at the impact of financial leverage on investment levels using firm-level panel data in Sri Lanka. The researcher expects to contribute to the existing literature by bringing evidence from a panel data set, which comprises 20 firms, all listed on the Colombo Stock Exchange sampled over a 10-year period (i.e., from 2000-2009). In addition, the researcher distinguishes between two types of firms, namely: (i) high-augmentation firms; and (ii) low-augmentation firms. The results reveal a significant negative relationship between leverage and investment. More interestingly, while the researcher found a negative relationship between leverage and investment for low augmentation firms, our econometric results reveal an insignificant relationship between the two variables for high augmentation firms.

Key words: Financial Leverage, Investment, Trading Companies.

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