

LEVERAGE ON PROFITABILITY

Dr.D Anjaneyulu¹, Shyam Prasad Rao H²

¹Asst Prof, Dept of MBA, Santhiram Engineering College, Nandyal, India.

²Student of MBA, Santhiram Engineering College, Nandyal, India.

ABSTRACT

This research investigates the influence of leverage on the profitability of firms, with a particular focus on how financial leverage—defined as the use of debt in a company's capital structure—affects profitability metrics such as Return on Assets (ROA) and Return on Equity (ROE). Leverage is a double-edged sword: while it can enhance returns by allowing firms to invest more than their equity alone would permit, it also increases financial risk and the likelihood of insolvency during downturns. This study analyzes the relationship between leverage and profitability using financial data from firms across multiple sectors. Quantitative methods, including ratio analysis and regression modeling, are employed to assess whether an optimal level of leverage exists that maximizes profitability while maintaining financial stability. The study also explores the influence of firm size, industry type, and market conditions on this relationship. The findings reveal that moderate levels of leverage can boost profitability, but excessive reliance on debt adversely affects financial performance. This research offers valuable insights for corporate managers, investors, and policymakers seeking to make informed decisions regarding capital structure and financial planning.

Keywords: Leverage, Profitability, Financial Performance, Return on Assets (ROA), Return on Equity (ROE), Capital Structure, Debt Ratio, Financial Risk, Regression Analysis, Corporate Finance.

1. INTRODUCTION

Leverage is a fundamental concept in corporate finance, referring to the use of borrowed capital (debt) to finance the company's operations and investments. The primary goal of leveraging is to amplify the potential returns on equity, allowing a business to generate higher profits without necessarily increasing its own capital. By using debt, companies can access additional resources to fund expansion, new projects, or other capital-intensive activities that have the potential to generate returns greater than the cost of borrowing. However, this comes with the risk of higher financial obligations, as interest payments and the repayment of principal can strain a company's cash flow if not managed effectively.

In the case of ACC Cements, a leading player in the cement industry, leverage plays a pivotal role in enhancing profitability. The cement industry is inherently capital-intensive, requiring substantial investment in infrastructure, plants, and machinery. By utilizing financial leverage, ACC Cements can undertake large-scale projects and expand its capacity without needing to rely solely on equity financing, thus preserving its ownership structure. The company strategically uses debt to finance its operations, which, when managed prudently, can lead to a significant increase in return on equity (ROE), benefiting shareholders.

2. RESEARCH METHODOLOGY

The primary source of data will be ACC Cements' publicly available financial statements. These reports provide detailed insights into the company's financial position, performance, and cash flow dynamics. Secondary data, such as industry reports, relevant academic journals, and financial databases, may also be used to supplement the primary data and provide a broader context for comparison with industry benchmarks and competitors.

ANALYTICAL TOOLS AND TECHNIQUES:

1) Ratio Analysis: Ratio analysis will be one of the core techniques used to assess the relationship between leverage and profitability. Key financial ratios will be calculated to measure leverage, profitability, and financial health. These ratios will include:

- a) Debt-to-Equity Ratio
- b) Interest Coverage Ratio
- c) Debt Ratio
- d) Return on Equity (ROE)
- e) Return on Assets (ROA)

2) Trend Analysis

3) Key areas of focus will include:

- a) Leverage trends: Analyzing the year-on-year changes in debt levels and capital structure adjustments.
- b) Profitability trends: Observing how key profitability metrics like net profit margin, operating profit margin.
- c) Impact of external factors: Identifying any significant events, such as shifts in interest rates or changes in the cement

industry, that may have influenced the relationship between leverage and profitability.

3. DATA ANALYSIS

ROI:

The term investment may refer to total assets (or) net assets. The funds employed in net assets is known as capital employed.

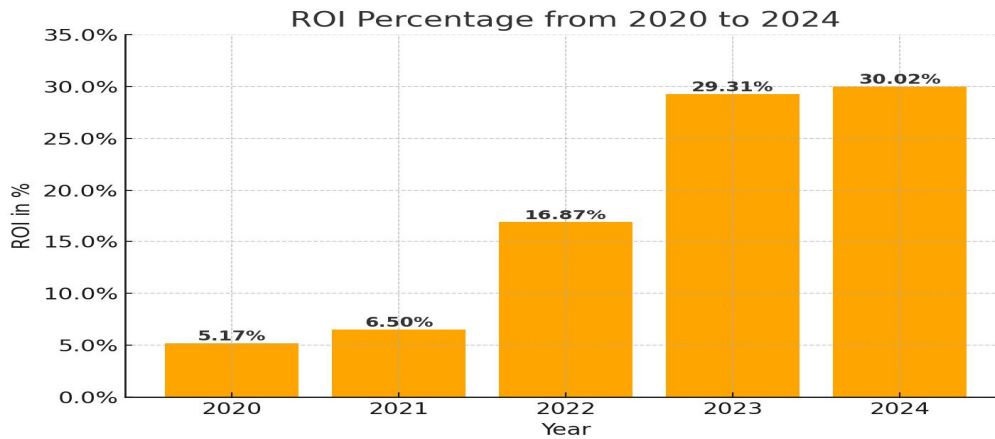
$$\text{Return on investment} = \text{EBIT} / \text{Capital employed} * 100$$

4.1: TABLE return on investment of zuari cement ltd

Year	Operating profit after Tax Rs. In lakhs	Capital Employed Rs. In lakhs	Poi in %
2020	3343.81	64698.07	5.17
2021	4206.66	64698.07	6.50
2022	10913.23	64698.07	16.87
2023	18963.61	64698.07	29.31
2024	19424.53	64698.07	30.02

SOURCE: ANNUAL REPORTS OF ZUARI COMPANY.

4.1: CHART



Interpretation:

From the above table 4.1 it is evident that ROI is fluctuating in the study from 2020 to 2024. From the year 2024 the ROI is increasing. It is low in the year 2020 and it is high in the year 2024.

PROFIT MARGIN:

It is relative to sales it is gross profit margin. The profit margin reflects the efficiency with which management producers each of the product.

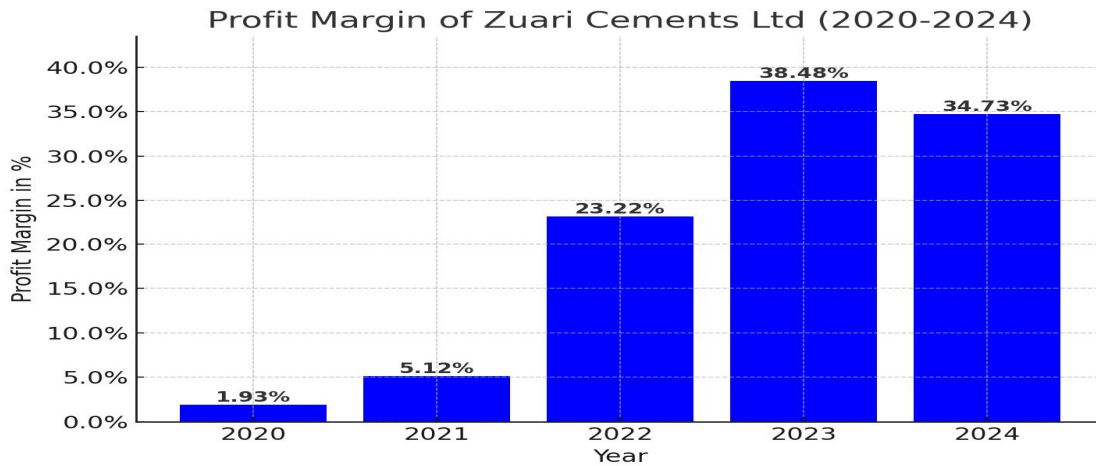
$$\text{Profit margin} = \text{net profit} / \text{net sales} * 100$$

4.2: TABLE profit margin of zuari cements Ltd

-Year	Net profit Rs in lakhs	Net sales Rs in lakhs	Profit margin in %
2020	559.35	29021.15	1.93
2021	1669.06	32605.16	5.12
2022	9217.49	39689.62	23.22
2023	16928.32	43996.40	38.48
2024	18293.13	52667.30	34.73

Source: Annual report of zuari cement ltd

4.2: CHART



Interpretation:

From the above table 4.1.2 it is clear that the profit margin is fluctuated in them study from 2020 to 2024. It was high in the year 2023 and it was in the year 2022 and it was low in the year 2020.

CALCULATION OF ASSET TURNOVER RATIO:

Asset turnover ratio = Net sales/Total Assets *100

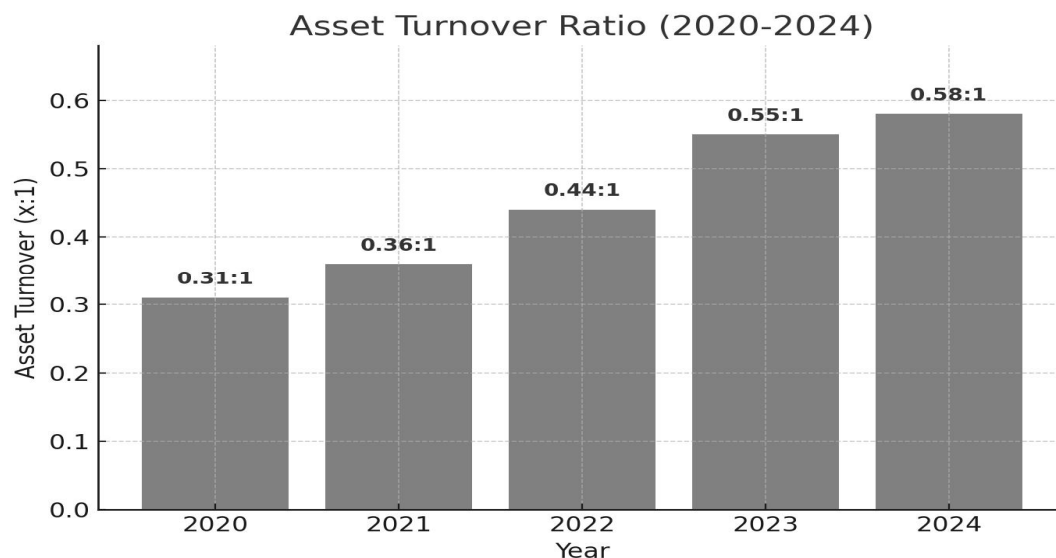
4.3: TABLE

Asset turnover ratio of zuari cement ltd

YEARS	NET SALES Rs. In Lakhs	NET ASSETS Rs.In Lakhs	ASSET TURNOVER ain %
2020	29021.35	92787.09	0.31:1
2021	32882.65	91896.51	0.36:1
2022	39689.62	89896.69	0.44:1
2023	44396.4	81253.47	0.55:1
2024	52667.30	89896.69	0.58:1

Source: Annual report of zuari cement ltd

4.3: CHART



Interpretation:

From the above table 4.3 it is evident that the asset turnover ratio is 0.31 in the year 2020. It is increasing from the period 2022. It was high in the year 2024 and it was low in the year 2020.

4. CONCLUSION

The study of leverage on profitability reveals that financial leverage plays a significant role in shaping a firm's financial performance. When used strategically, leverage can enhance profitability by increasing returns on equity and enabling firms to pursue growth opportunities beyond their internal financing capacity. However, excessive reliance on debt increases financial risk, leading to reduced profitability and greater vulnerability during economic downturns. The findings emphasize the importance of maintaining an optimal capital structure—one that balances the benefits of debt financing with the risks it introduces. Managers must carefully assess their firm's financial condition, industry dynamics, and market environment before making leverage-related decisions. Ultimately, a well-managed leverage strategy contributes positively to long-term profitability and financial stability, supporting sustainable business growth.

5. REFERENCES

- [1] **I.M PANDEY** “FINANCIAL MANAGEMENT” 9TH Edition New Delhi, Vikas Publication.
- [2] **S.N MAHESWARI & S.K MAHESWARI** “FINANCIAL MANAGEMENT” 4th edition sultan chand &sons, New Delhi.
- [3] **M.Y.KHAN&JAIN** “FINANCIAL MANAGEMENT”, 2ND edition, Tata McGraw Hill Publishers New Delhi.
- [4] **PRASANNA CHANDRA**, “FINANCIAL MANAGEMENT”, 3rd edition Tata McGraw Hill Publishers New Delhi.