The Impact of Liquidity Risk on the Financial Performance of Banks and Finance companies in Sri Lanka

Perera, H.G.S.[1] and Perera, K.H.[2]

[1]gayashadiperera1118@gmail.com; [2]hasinip@kln.ac.lk

Abstract

The banking and finance companies play a significant role in intermediation among depositors and borrowers. These enhance the flows of funds by lending cash to borrower, while providing liquidity to savers. Therefore, liquidity is very critical phenomenon for smooth operation of banking and finance sector business. This study aims to investigate the relationship between liquidity risk and financial performance of banking and finance companies in Sri Lanka. This study employed a sample of 12 commercial banks, 3 specialized banks and 15 finance companies. Independent variables include deposit to total assets ratio, cash reserve to total assets ratio, NPL ratio and liquidity gap while dependent variables include ROA, ROE and net profit margin. Data are retrieved from the balance sheets, income statements and notes of banks and finance companies during the period 2011 to 2019. This study employs multiple regressions to investigate the relationship between liquidity risk and financial performance of banking and finance companies. The study would be useful in developing credit operating procedures in respect of assets management that have impact on stability of banks and finance companies. This study is also useful all other sectors' companies to assets management in accurate way. Economic factors contributing to liquidity risk are not covered in this paper and future research can be conducted by incorporating the economic factors affecting the liquidity risk.

Keywords: Liquidity Risk, Financial Performance, Banks & Finance Companies, Sri Lanka