The Impact of Credit Risk on Bank Profitability: Evidence from Licensed Commercial Banks in Sri Lanka

D. M. Sumanathilake[1] and S. S. Weligamage[2]
Department of Finance, University of Kelaniya, Sri Lanka[1,2]
infor.dimuthu@gmail.com[1], susima@kln.ac.lk[2]

ABSTRACT

Introduction - Lending is one of the main incomes generating activity in commercial banks. Credit risk occurs in connection with lending. Among the different risks facing by banks risks, credit risk is considered as one of the major determinants of bank profitability because of the number and diversity of stakeholders affected.

Design/Methodology/Approach - The objective of the study is to assess the impact of credit risk on profitability of licensed commercial banks in Sri Lanka for the period 2015 to 2019. Thirteen commercial banks were selected for the study and data was collected through published annual reports and using Eviews Statistic Software was performed Descriptive analysis, Correlation and Regression analysis.

Findings - This study found that non-performing loan (NPL) ratio has a insignificant negative impact on Return on Assets (ROA) ratio, while total loan to total deposit (TLTD) ratio has significant negative impact on Return on Assets (ROA) ratio. Furthermore, non-performing loan (NPL) ratio has significant negative impact on Return on Equity (ROE) ratio, while total loan to total deposit (TLTD) ratio has insignificant negative impact on Return on Equity (ROE) ratio.

Conclusion -Findings of this study contribute to formulate efficient and effective credit risk management control policies for licensed commercial banks in Sri Lanka.

Keywords: *Credit Risk , Bank Profitability, Non-Performing Loan, Return on Assets, Return on Equity*