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The Impact of the Determinants of Financial Soundness on Firm Performance: Evidence from Listed Finance Companies in Sri Lanka

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Abstract

Introduction: The success and sustainability of finance companies that play a crucial role in the economic development and stability of Sri Lanka rely heavily on their financial soundness, which is measured through indicators such as capital adequacy, asset quality, profitability, and liquidity. However, there is a research gap in understanding the specific impact of financial soundness on LFC's performance within the context of Sri Lanka.

Methodology: This study examines the impact of financial soundness indicators on finance company's ROE and ROA. Study adopts a quantitative research design, utilizing secondary data and panel regression methods. The sample size includes 09 finance companies over a 10-year period (2013-2022) to ensure adequate representation and diversity.

Findings: Higher capital adequacy positively influences ROA but not ROE. Effective NPL management consistently boosts both ROA and ROE. Liquidity has no significant impact, while higher profitability consistently improves both ROE and ROA in listed finance companies in Sri Lanka.

Conclusion: The insights contribute to understanding the crucial dynamics between financial soundness and performance in the Sri Lankan finance sector, offering valuable implications for policymakers and industry stakeholders.

Keywords: Financial Soundness, Capital Adequacy, Asset Quality, Liquidity, Profitability