

## **Relationship between Income Source Diversification and Financial Performance of Commercial Banks in Sri Lanka**

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### **Abstract**

Profitability of commercial banks highly depends on the net interest income generating activities. Due to the profitability and stiff competition, banks have changed their income sources, by diversifying into non-interest income generating activities. The objective of the study is to investigate the impact of income source diversification on financial performance of commercial banks in Sri Lanka.

The study used secondary data of 15 commercial banks covering the period of 2008-2017. Diversification Index used as diversification indicator while Return on Assets (ROA) and Return on Equity (ROE) used as performance indicators. There are some control variables like asset size, growth rate, equity ratio and loan ratio added to the model to ensure that there is no any affect for the relationship between bank income diversification and bank performance from those variables. Descriptive statistics, correlation and regression analysis have used as analytical tools of the study. Results revealed that there is a positive relationship between income diversification and bank performance despite the fact that degree of diversification being not in the peak within Sri Lankan context. Additionally asset size, loan ratio and asset growth variables are not significant variables to the both ROA and ROE models and equity ratio variable shows a significant negative relationship with bank performance in both models.

**Keywords:** Interest income, Non-interest income, Income diversification, Financial performance