

## INCOME DIVERSIFICATION AND PERFORMANCE OF COMMERCIAL BANKS IN SRI LANKA

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### Abstract

The general objective of this study is to investigate the impact of income source diversification on the bank performance of Sri Lankan listed commercial banks. This study covers Sri Lankan commercial banks during the sample period of 2012-2021. Ten licensed commercial banks were selected based on the highest market capitalization. The study was done using quantitative research methods with a deductive approach, and the secondary data was gathered from the annual reports of each bank. The performance measures return on equity and return on assets while income diversification is measured by the diversification index. Additionally, four control variables (bank size, financial leverage, growth rate and lending strategy) were used. Panel data regression is used as the main analytical tool as the data set contain cross sections and the time series nature of the data. Based on the findings of the research there is a positive relationship between bank income diversification and bank performance even though the degree of diversification is not at the peak within the Sri Lankan context. The study revealed that bank income sources are diversified significantly in the Sri Lankan banking industry and that both interest and non-interest activities significantly impact positively on bank performance. In contrast, bank growth in the number of branches significantly negatively impacts bank performance. According to the findings of this study, it can be concluded that there is a significant positive impact of income diversification and bank performance in Sri Lanka (Both Return on Assets and Return on Equity).

**Key words:** *Bank Performance, Income Diversification, Return on Assets, Return on Equity, Sri Lankan Banking Sector, Interest Income, Non-interest Income*