

THE IMPACT OF CREDIT RISK MANAGEMENT ON THE PERFORMANCE OF BANKING SECTOR Malith

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Abstract

Credit risk management in banks has become more important not only because of the financial crisis that the industry is experiencing currently, but also a crucial concept which determines banks' survival, growth and profitability. The aim of this study is to investigate the impact of credit risk management on the performance of the banking sector in Sri Lanka. Financial reports of seven commercial banking firms were used to analyze for seven years (2005 – 2011). The panel regression model was employed for the estimation of the model. In the model, Return on Equity (ROE) and Return on Asset (ROA) were used as the performance indicators while Non-Performing Loans (NPL) and Capital Adequacy Ratio (CAR) as credit risk management indicators. The findings revealed that credit risk management has a significant impact on the profitability of commercial banks' in Sri Lanka.

Banks today are the largest financial institutions around the world, with branches and subsidiaries throughout everyone's life. Commercial banks are facing risks when they are operating. Credit risk is one of the most significant risks that banks face, considering that granting credit is one of the main sources of income in banks. The management of the risk related to that credit affects the profitability of the banks. The aim of the research is to provide stakeholders with accurate information regarding the credit risk management of the banking sector with its impact on profitability.

Key words: Performance, Credit Risk Management, Profitability, Non-Performing Loan, Capital Adequacy Ratio.