THE IMPACT OF CAPITAL STRUCTURE ON PROFITABILITY OF BANKS IN SRI LANKA

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Abstract

The concept of capital structure means the way a firm finances its assets by the use of a mix of debt and equity. Capital structure decision is the important one, because the profitability of an enterprise is directly affected by such decision. In the financing decision the manager is concerned with determining the best financing mix or capital structure for his firm. According to Buser (1981), the capital structure decision of a bank is similar to that of a non-financial firm.

The objective of this study is to examine the impact of capital structure on profitability of five banks in Sri Lanka from 2010 to 2014, to find an optimal capital structure that would be associated with the best performance and to suggest the banks in the way to increase profitability through adapting a better strategic framework of capital structure.. All data for this research will be collected by secondary data through financial statements.

Based on the findings of the study, there are a few key points that can be used to conclude this study. It is very important that the total debt is the determining factor of profitability in the Banking Industry of Sri Lanka. The outcomes of the study may guide banks, loan-creditors and policy planners to formulate better policy decisions as far as the capital structure is concerned. Further, the study reinforces and refines the body of knowledge relating to capital structure and profitability in Sri Lankan Banks. **Key words:** Capital structure, Profitability, Total debt