

Determinants of Capital Adequacy Ratio of Commercial Banks in Sri Lanka

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Abstract

A resilient banking groundwork plays a foremost part in supporting economic activity and backed to the overall growth of the country. Capital adequacy ratio is a vibrant measure of protection and soundness for banks and depository institutions because it functions as a buffer or cushion for absorbing losses. It is an essential requirement for financial institutions to maintain adequate level of capital and every financial organization must keep balance between capital and available risk in its assets in order to assure its stability. Thus, it has turn into one of the critical benchmarks for Banks. This study is an attempt to empirically examine the factors influencing the capital adequacy ratio (CAR) and to identify the impact of such factors on Capital adequacy Ratio of licensed commercial banks in Sri Lanka. Going with an investigation on this matter would provide assistance to certain parties when they making decisions. This study used multiple regression analysis for panel data of eight licensed commercial banks out of a population of Twenty-five banks in Sri Lanka for a 9 year essential requirement for financial institutions to maintain adequate level of capital and every financial organization must keep balance between capital and available risk in its assets in order to assure its stability. Thus, it has turn into one of the critical benchmarks for Banks. Profitability has a moderate positive relationship with the identified firm-specific variables. The results revealed that Bank size; Deposits, Liquidity and Profitability are negatively correlated with Capital Adequacy Ratio while Loans are positively correlated with Capital Adequacy Ratio.

Keywords: *Sri Lankan, Banking sector, Capital Adequacy Ratio, Deposits, Panel data.*