Credit Risk on Performance: Evidence from Commercial Banks in Sri Lanka

Sandakelumsiri, P.W.M.[1] and Abeyawardhana, D.K.Y.[2]

[1]mudithasandakelumsiri@gmail.com; [2]dilyapa@kln.ac.lk

Abstract

Credit risk is one of the most common causes of bank failures. Generally, Credit risk is the possibility of a loss resulting from a borrower's failure to repay a loan or meet contractual obligations. This study therefore sought to provide a response to the question: what is the effect of credit risk on the financial performance of commercial banks in Sri Lanka? Aim of this study is to investigate the effect of credit risk on banks performance. Data collected over the six-year period from 2014 to 2019 from the published annual reports of the selected banks and the CBSL reports. The CAMEL model is used as an indicator of bank credit risk and financial efficiency is measured using ROE. Pearson correlation analysis and a multiple regression model were the basis of the data analysis approach. This research paves the way for new data on the relationship between credit risk and the financial performance of Sri Lankan banks to be discovered. The required guidelines for various parties to mitigate credit risk issues in order to make adjustments and optimal investment decisions formulate policies and enforce them.

Keywords: Credit Risk, Financial Performance, CAMEL