Determinants of Non-performing Loans in Non-banking Financial Institutions: Evidence from Sri Lanka

N. Ekanayake[1], I. Hansani[2], D.Kuruwita[3] and G. Chamodi[4]
[1,2,3,4]*Dept. of Finance, University of Colombo, Sri Lanka*
nishanie@dfn.cmb.ac.lk

Abstract

This study investigates the factors affecting non-performing loans (NPLs) of non-bank financial institutions (NBFIs) in Sri Lanka by analyzing ten licensed finance and specialized leasing companies. The study employed a quantitative approach using secondary data from corporate reports of the selected NBFIs from 2011 to 2020. The study sample consists of five licensed finance companies and five specialized leasing companies, which claim for 65 percent of the NBFIs industry. The dependent variable under investigation is non-performing loans, while independent variables include macroeconomic and institutional-specific factors. The study used four proxies to measure institutional-specific factors; size of the company, return on assets, capital adequacy, and efficiency. Considered macro-economic factors are GDP, inflation, and interest rates. The impact of macroeconomic and institutional-specific factors on non-performing loans was observed through a multiple regression model under the ordinary least square method using EViews statistical software. The model results revealed that NPLs have a significant negative relationship with return on assets, GDP, and inflation and a significant positive relationship with the economy's interest rates. Further, it was found that capital adequacy, efficiency, and size factors do not have a significant relationship with NPLs. The findings highlighted the need for better credit risk mitigation practices in the non-banking sector to improve the financial system's stability.

Keywords: *licensed finance companies, non-bank financial institutions, non-performing loans, specialized leasing companies*

ISSN 2806-514X