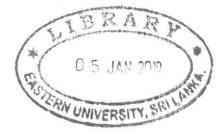
COMPARATIVE ANALYSIS OF CHARACTERISTICS OF NON-PERFORMING LOANS BETWEEN STATE BANKS AND PRIVATE BANKS IN SRILANKA



NIYARAKETIYE GEDARA AVISHKA UMMADI THATHSARANI DIKKUMBURA (EU/IS/2012/COM/102) (COM 1602)

By



A Project Report

submitted to the faculty of Commerce and Management, Eastern University, Sri Lanka as a partial fulfillment of the requirement of the Degree of Bachelor of Commerce Honours in specialization in Accounting and Finance [BCOM Hons (Acc & Fin)] Specialization in Accounting and Finance

> Department of Commerce Faculty of Commerce and Management Eastern University, Sri Lanka

> > 2018

ABSTRACT

Banking sector plays a major role in any country. Therefore, the changes occur in banking sector directly affect to the fiscal and financial policies of the country.it is widely accepted that the quantity or percentage of Non-performing loans or amount of arrears on loan is often associated with bank failures and financial crises. NPLs create problems for the banking sector's balance sheet and also create a negative impact in the income statement as a result of provisioning for loan losses. In the worst scenario, a high level of NPLs in banking system poses a systematic risk, inviting a panic run on deposits and sharply limiting financial intermediation and subsequently investment and growth.

Non-performing loans are a critical factor for every bank and should focus on more as it has saviour consequences. Many researches have done on factors affecting to NPL and those studies have come up with different conclusions. Hence, this is still open area for further studies. This study focuses on comparison of Non-Performing Loans Between State Banks and Private Banks in Sri Lanka. Sample of the study is ten licenced commercial banks in Sri Lanka and data collected for the period of ten years.

Non-performing loans characteristics measured by the interest rates, size of the loans, Repayment Period of loans, Credit Terms and the collateral security used by the banks. The univariate analysis Findings revealed there is a significant difference in the characteristics of non-performing loans between state banks and private banks.

Keywords : Non-performing loans, Commercial Banks

TABLE OF CONTENT

| Acknowledgement | I |
|------------------|-----|
| Abstract | II |
| Abbreviations | III |
| Table of content | IV |
| List of tables | |
| List of figures | IX |

1.CHAPTER ONE : INTRODUCTION

| 1.1 Background of the study | 1 |
|-------------------------------|----|
| 1.2 Problem statement | 4 |
| 1.3 Research questions | .4 |
| 1.4 Objectives of the Study | .5 |
| 1.5 Significance of the study | .5 |
| 1.6 Scope of the study | .6 |
| 1.7 Chapter Summary | .7 |

2.CHAPTER TWO: LITERATURE REVIEW

| 2.1 Introduction | 8 |
|---|----|
| 2.2 Sri Lankan Banking Industry | 8 |
| 2.3 Bank Ownership | 10 |
| 2.4 Theoretical Literature | 11 |
| 2.5 Empirical Literature | 12 |
| 2.5.1 Non-performing loans | 12 |
| 2.5.2 Reasons of loans being Non-performing loan | 14 |
| 2.5.3 The effects of Non-Performing loans on Economy | 15 |
| 2.5.4 Economic factors affecting non-performing loans | 15 |
| 2.5.5 Loan related factors affecting non-performing loans | 16 |
| 2.5.6 Loan Repayment | 19 |

| 2.5.7 Loan repayment performance | 19 |
|---|----|
| 2.5.8 Bank specific factors | 20 |
| 2.5.9 Relationship between NPLs and bank's specific factors | 23 |
| 2.6 Chapter Summary | 26 |

3.CAHAPTER THREE: CONCEPTUALIZATION AND OPERATIONALIZATION

| 27 |
|----|
| 27 |
| 27 |
| |
| 29 |
| 29 |
| |
| |
| |
| 31 |
| 32 |
| |

4.CHAPTER FOUR: METHODOLOGY

| 4.1 Introduction | .33 |
|---|-----|
| 4.2. Study Setting, Study Design and Method of Survey | .33 |
| 4.3 Population and sample | .34 |
| 4.4 Method of data collection | .35 |
| 4.5 Methods of data presentation | .35 |
| 4.6 Method of data analysis | .35 |
| 4.7 Univariate Analysis | .35 |
| 4.7.1 Mean | .35 |
| 4.7.2 Standard deviation | .36 |
| 4.8 Chapter Summary | .36 |

HAPTER FIVE: DATA PRESENTATION AND ANALYSIS

| Introduction |
|---|
| Interest rate differences of NPLs between state banks and private banks37 |
| 5.2.1 Average level of interest rates of the NPLs in the state banks |
| 5.2.2 Average level of interest rates of the NPLs in the private banks |
| 5.2.3 Trend of interest rates of both state and private banks |
| .3 Loan size differences of NPLs between state banks and private banks |
| 5.3.1 loan size of the NPLs in the state banks |
| 5.3.2 loan size of the Non-performing loans in the private banks |
| 5.4 Differences in Repayment period of NPLs46 |
| 5.4.1 Repayment period of the NPLs in the state banks |
| 5.4.2 Repayment period of the NPLs in the private banks |
| 5.5 Differences in credit terms of NPLs48 |
| 5.5.1 Credit terms of NPLs in the state banks |
| 5.5.2 Credit terms of NPLs in the private banks |
| 5.6 Differences in collateral security of NPLs51 |
| 5.6.1 Collateral security of the NPLs in the state banks |
| 5.6.2 Collateral security of the NPLs in the private banks |
| 5.6.3 Graphical representation of Collateral Security of NPLs53 |
| 5.8 Chapter summary |

6.CHAPTER SIX : DISCUSSION

| 6.1 Introduction | .54 |
|---|-----|
| 6.2 Discussion on Interest rates of non-performing loans | .54 |
| 6.3 Discussion on loan size of non-performing loans | .55 |
| 6.4 Discussion on repayment period of non-performing loans | .56 |
| 6.5 Discussion on Credit terms of Non-performing loans | .56 |
| 6.6 Discussion on Collateral Security of Non-performing Loans | .57 |
| 6.7 Chapter summary | .57 |