

Study of Credit Risk and Liquidity Risk of Banks and its Impact on Profitability: Case Study on Bank of Ceylon

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The quality of the financial system has an important role in a country's economic stability. During the 1980's and 1990's when the financial and banking crises become worldwide, new risk management banking techniques emerged in order to manage the different types of risks. The risks those are most applicable to banks are credit risk, market risk, foreign rate risk, liquidity risk and insolvency risk. The issues of risk management in the banking sector have greater impact not only on the banks' profitability but also on the economic growth. The main objective of this research is to study the impact of credit risk and liquidity risk on Bank of Ceylon's profitability. Data was gathered from the banking sector, particularly, Bank of Ceylon. Purposive sampling method was used for sampling secondary data from 1994 to 2015.

Data were analysed by using (SPSS). Risk management was considered as the independent variable with the proxies of credit risk and liquidity risk. Profitability was considered as dependent variables with the proxies of profitability margin, ROE and ROA. Analysis was carried out using correlation and regression analysis. The hypothesis is, there is a relationship between risk and profitability of the bank. According to correlation analysis the correlation between credit risk and profitability margin, ROA and ROE are respectively 0.370, 0.310 and 0.163. Results reveal positive relationships between credit risk and profitability, Correlation between liquidity risk and PM, ROA and ROE are respectively -0.218, -0.038 and 0.173. According to model summary R square is 0.059. It shows that nearly 6% of the profitability is determined by credit risk and liquidity risk of Bank of Ceylon. The significant value between independent variables and dependent variable is 0.151 and 0.560 respectively, which is greater than 0.05 and the hypothesis is rejected. This indicates that there is no relationship between credit risk and liquidity risk with

profitability of Bank of Ceylon. Therefore, the Bank of Ceylon has controlled their credit and liquidity risk during the period of 1994- 2015

Key words: *Credit risk, Liquidity risk, Profitability.*