Impact of board structure on Credit risk: A study of financial companies listed in Colombo Stock Exchange in Sri Lanka

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Abstract

Impact of corporate governance on the bank credit risks has been researched over the years and their findings are inconclusive. If the governance systems put into practice are not functioning properly, problems will arise. Therefore, corporate governance issues have been a growing area of management research. Good corporate governance practices are regarded as an important in reducing credit risk. The purpose of the present study is to investigate impact of board structure on credit risk of banks listed in Colombo Stock Exchange. A sample of 13 companies was selected from those which were listed in Colombo Stock Exchange during year 2011 to 2015. Board size, board independence and meeting frequency were considered as independent variables, whereas, non-performing loan ratio was considered as dependent variable and the control variables were financial leverage and firm size. A regression model was developed to establish the relationship between board structure and credit risk. The results reveal that board size and board independence have a negative effect on non-performing loan. Meeting frequency, firm size and financial leverage do not have any significant impact on the non-performing loan ratio. Accordingly, enhancement of board size and board independence helps financial firms to minimize the credit risk. Therefore, banks should appoint board with appropriate size and suitable members to ensure the board independence in order to mitigate the credit risk. .

***Keywords**: Credit risk, board independence, board size, corporate governance, meeting frequency.*