EXPLORING THE FINANCIAL IMPACT OF SUSTAINABILITY INITIATIVES IN EMERGING ECONOMIES: EVIDENCE FROM THE SRI LANKAN BANKING SECTOR

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ABSTRACT

The growing emphasis on sustainability in the financial sector has heightened interest in examining its impact on banks' financial performance. Despite its importance, the relationship between sustainability practices and financial outcomes remains underexplored, with existing studies yielding inconclusive results. This research investigates the effect of sustainability initiatives on the financial performance of commercial banks, with a particular focus on the Sri Lankan banking sector. Specifically, it evaluates the influence of economic, environmental, and social sustainability initiatives on two key performance indicators: Return on Equity (ROE) and Return on Assets (ROA). Adopting a quantitative methodology, the study draws on secondary data extracted from the annual reports and sustainability disclosures of the six Systemically Important Banks (SIBs) in Sri Lanka for the period 2019–2023. Sustainability initiatives were measured by assessing the extent to which banks complied with sustainability guidelines outlined in the Global Reporting Initiative (GRI), classified under economic, environmental, and social dimensions. To analyze the relationship between sustainability initiatives and financial performance, the study employed descriptive statistics, correlation analysis, and multiple regression analysis. The findings reveal that economic and social sustainability initiatives have a significant impact on banks' financial performance. In contrast, environmental initiatives, despite their increasing prominence in the financial sector, show no significant relationship with financial outcomes. These results suggest that while economic and social dimensions of sustainability may directly contribute to financial performance, the benefits of environmental initiatives may be less immediate or more difficult to quantify in the short term. Overall, the study highlights the importance of integrating sustainability initiatives into banking strategies, while also emphasizing the need for further research to clarify the mechanisms through which these practices influence financial outcomes. The lack of significant findings regarding environmental initiatives, in particular, underscores the necessity for deeper investigation into contextual and institutional factors that may moderate the relationship between sustainability and performance in the Sri Lankan banking sector.

Keywords: Sustainability, Financial Performance, Economic Initiatives, Environmental Initiatives, Social Initiative

1. INTRODUCTION

1.1 Background of the Study

The banking sector plays a pivotal role in driving economic growth and development while simultaneously facing increasing pressure to address environmental, social, and governance (ESG) considerations (Onuselogu & Shahzad, 2023). Against the backdrop of global sustainability challenges and heightened stakeholder expectations, the integration of sustainability initiatives within the banking industry has emerged as a critical area of inquiry. This research aims to explore the impact of sustainability initiatives on banks' financial performance, delving into the multifaceted relationship between sustainability practices and financial outcomes.

In recent years, sustainability initiatives have gained prominence in businesses across different industries where banking sector is pivotal in addressing environmental, social, and governance [ESG] factors within their traditional business framework (Onuselogu & Shahzad, 2023). Sustainability initiatives encompass a wide range of practices aimed at minimizing negative environmental impacts, promoting social responsibility, and fostering good governance within organizations (Bătae et al. 2021). According to the World Business Council for Sustainable Development [WBCSD], sustainability initiatives involve integrating environmental, social, and economic considerations into business operations and decision-making processes (WBCSD, 2020).

Companies that prioritize sustainability can differentiate themselves in the marketplace, attract environmentally and socially conscious consumers, and build stronger relationships with investors, employees, and other stakeholders (Adu et al., 2024). This holistic approach of integrating environmental, social and economic systems has spotlight the significance of organizations operating in an environmentally responsible, socially fair, and economically sustainable manner.

Thus, in recent years' banks have adopted many sustainability initiatives to ensure the integration of ESG factors into their banking operation such as promoting green financing methods such as green bonds, green loans, impact investing, adopting eco-friendly practices like paper less banks and engaging in Corporate Social Responsibility (CSR) works (Onuselogu & Shahzad, 2023). While adopting sustainable practices contribute to the achievement of global sustainability goals, such as those outlined in the United Nations Sustainable Development Goals [SDGs) including poverty alleviation, gender equality, clean energy access, and responsible consumption and production, there is a growing interest in exploring how these sustainable initiatives influence the performance of banks in different perspectives.

When considering the Sri Lanka context, The Central Bank of Sri Lanka (CBSL) has progressively advanced the sustainability agenda within the domestic financial sector through regulatory and institutional initiatives. Since joining the Sustainable Banking and Finance Network (SBFN) in 2016, CBSL has introduced the Roadmap for

Sustainable Finance (2019), the Sri Lanka Green Finance Taxonomy (2022), and mandatory sustainability reporting requirements for both banks and non-bank financial institutions. Its accession to the International Platform on Sustainable Finance (IPSF) in 2023 further underscores Sri Lanka's commitment to global ESG standards. These measures reflect a structured effort to integrate environmental and social considerations into financial regulation, despite the broader economic and institutional challenges inherent in an emerging market context.

1.2 Research Problem

The contemporary banking sector faces increasing pressure to adopt sustainability initiatives due to rising environmental and social consciousness among stakeholders. However, it has identified as a risk managing tool of environmental and social risks that would affect negatively on the banks 'financial performance (Buallay et al., 2021). Thus, the growing body of literature has emphasized the strategic importance of integrating ESG factors in to the business model of banks in terms of intensifying its financial performance and ensuring the resilience and competitiveness in the evolving global market (Bătae et al., 2021). Despite the growing attention on sustainability initiatives in the banking sector, the impact of such initiatives like environmental, social and economic initiative on the banks' financial performance remain under-explored (Chen et al.2022; Tulcanaza-Prieto et al. 2020). Even though the banks have highly adopted different sustainable initiatives like green bonds, green loans, paperless banking models, sustainable investment products, CSR activities (Onuselogu & Shahzad, 2023), it is still unclear how these activities influence the financial and non-financial outcomes. Thus, there is a critical need for further research to elucidate the specific impacts of sustainability initiatives on banks' financial performance, providing clearer guidance for banks aiming to enhance their sustainability efforts and achieve better financial and non-financial outcomes. Hence, this study aims to address this gap by examining the significance of various sustainability initiatives on banks' performance.

The research seeks to determine whether there is a significant impact of overall sustainability initiatives on banks' performance, building on existing evidence that suggests a positive relationship between sustainability practices and corporate financial performance

Thus, the study will first explore how sustainable economic initiatives such as green financing, responsible lending practices, cost management and efficiency would impact on the banks' financial performance.

Second, study will explore the significance of environmental engagement, which includes banks' efforts to reduce their carbon footprint and support environmentally friendly projects, and its correlation with improved risk management and operational efficiency leading to better performance of the banks (Chen et al.2022).

Lastly, this research will investigate the impact of social engagement, which involves banks' participation in community development and social responsibility initiatives, on banks' financial performance. Social engagement can enhance customer loyalty and brand reputation, potentially leading to better financial outcomes (Tulcanaza-Prieto et al. 2020).

By addressing these questions, this study aims to provide a comprehensive understanding of how different aspects of sustainability initiatives contribute to banks' financial performance, thereby offering valuable insights for both academic research and practical implementation in the banking sector. Accordingly, the objectives of the study are as follows;

1.3 Research Objective

To explore the significant impact of sustainability initiatives on banks' financial performance.

1.3.1. Sub Objectives:

To explore whether there is a significant impact of economic sustainable initiatives on banks' financial performance.

To explore whether there is a significant impact of environmentally sustainable initiatives on banks' financial performance.

To explore whether there is a significant impact of social sustainable initiatives on banks' financial performance.

In an era where ESG factors becoming integral in the financial sector, the study findings will be significant to many stakeholders as it bridges the knowledge gap surrounding the relationship and the impact of sustainable initiatives with the banks' financial performance. Thus, by exploring how the sustainable initiative contribute towards the banks' financial performance in terms of financial success, risk management and stakeholder satisfaction, the study findings would provide valuable insight to banks, policymakers, academic researchers and other stakeholders.

The research findings would assist banks to understand how sustainable initiative like green financing, social responsibility would influence the banks' financial and non-financial performance metrics. That would enable the banks to optimize their resource allocation, cost minimization, customer satisfaction by focusing on most influential sustainable initiatives. The policymakers can shape up the regulatory frameworks and can launch incentive programs to encourage sustainability initiatives in the financial sector to drive towards economic sustainability. The academic researchers can obtain new insight on sustainability initiatives on banks' financial performance and can apply in future studies to compare the effectiveness of different sustainability initiatives across industries or regions. Further, stakeholders including investors, customers and community would obtain the insight on how the sustainable practices enhance the long-term values of the banking sector and encourage them toward more sustainable investing and ethical banking choices.

Eventually the research will empower the banking sector towards integrating sustainable initiatives to the traditional business model that would in turn contributes to the global sustainability agenda.

2. LITERATURE REVIEW

The sustainable initiative in the banking sector such environmental and social and economic initiatives in order to align with the ESG principles with the banking operations has been believed to influence the financial and non-financial performance of the banks. The literature suggests that there is a growing attention towards sustainability not just as an ethical obligation but also as a strategic driver of the organizations towards long-term inclusive growth and competitiveness Friede et al, 2015.

2.1 Sustainability Initiatives

Sustainability has emerged as a critical paradigm in contemporary business practice, encompassing the integration of environmental, social, and governance (ESG) considerations into organizational strategies and operations. The concept of sustainability in the banking sector involves adopting practices that not only enhance financial performance but also contribute positively to the environment and society. This multidimensional approach is driven by growing recognition of the long-term benefits of sustainable practices, including risk mitigation, cost savings, and enhanced reputation. Numerous studies have highlighted the financial advantages of sustainability, demonstrating that companies with robust ESG profiles often outperform their peers in the long run (Onuselogu & Shahzad, 2023). For banks, sustainability initiatives can take various forms, such as green banking practices, which involve the provision of financial products and services that promote environmental stewardship, and social engagement activities that support community development and social well-being.

2.2 Theoretical Review

The conceptual foundation on how sustainable initiatives could influence the banks' financial performance has been built with the use of several theories which explain the relationship between sustainability and financial performance in the banking sector.

Triple Bottom Line (TBL) theory suggests that sustainability initiatives operate on the principle of the triple bottom line, which evaluates business performance based on three dimensions: people, planet, and profit. By addressing environmental concerns such as climate change, resource depletion, and pollution, sustainability initiatives aim to minimize adverse impacts on the planet while promoting long-term environmental stewardship. Socially, these initiatives seek to uphold human rights, labor standards, and community well-being, fostering inclusive growth and social equity. According to this theory, organizations should measure success based on their social, environmental, and economic impacts.

The theory of Resource Based-View (RBV) has been discussed in many empirical studies as a managerial framework to control the strategic resources of an organization (Freeman et al., 2021). In the context of sustainability, it suggests the non-visible resources like brand reputation, information for being eco-friendly or socially responsible can bring a positive influence towards the bank's performance (Khan et al., 2021).

The stakeholder theory suggests as the businesses including banks are accountable to its stakeholders, such as customers, employees, communities and the environment (Kivits et al., 2021). Thus, adopting sustainable initiatives by banks in terms of environmental and social sustainability can develop a stronger relationship with their stakeholders which in turn leads to a long-term profitability (Freeman et al., 2021).

Thus, as per the existing theories to the current research context, the researcher has identified sustainability initiatives under three major areas: environmental, social and economic

2.3. Empirical Review

Sustainability has become an emerging research area with the gaining attention around the world on considering ESG factors to the business operation. Studies have explored the sustainability effort across different industrial sectors where banking sector is one of the key focuses. Several studies have explored on how different sustainability initiatives have affected on the financial performance in the banking sector.

2.3.1 Economic Initiatives and Banks Financial Performance:

Empirical studies suggest that economic sustainability initiatives such as enhancing operational efficiency, minimizing costs, and managing financial risks can contribute to improved financial performance. Nobanee and Ellili (2017) examined the impact of economic, environmental, and social sustainability reporting on the financial performance of banks in the UAE, concluding that responsible practices like sustainable lending and capital adequacy management support long-term financial stability. Similarly, Al-Tuwaijri et al., (2004) emphasized that such initiatives help mitigate risks such as default and non-performing loans, thereby enhancing overall bank performance.

2.3.2. Environmental Initiatives and Banks' Financial Performance:

Environmental sustainability initiatives such as green banking practices, offering green loans and mortgages, and reducing carbon emissions have been linked to improved environmental and financial outcomes. Chen et al. (2022) found that green project financing positively affects banks' environmental performance. Bătae et al. (2021), in a European context, highlighted that environmental initiatives like emission reduction attract environmentally conscious customers and help mitigate environmental risks, leading to positive financial outcomes. Nizam et al. (2019) also demonstrated that enhanced environmental performance translates into improved financial performance. In a global study, Adu et al. (2024) concluded that climate-related banking initiatives significantly enhance financial performance, particularly when supported by strong corporate governance mechanisms.

2.3.3. Social Initiative and Banks' Financial Performance:

Social sustainability initiatives including ethical business practices, community engagement, and financial inclusion are recognized for building customer loyalty, reputation, and retention, all of which drive financial performance. Esteban-Sánchez et al. (2017) found that strong community relations are positively perceived by investors, thereby boosting corporate financial performance. Tulcanaza-Prieto et al. (2020) reported that Corporate Social Responsibility (CSR) enhances brand reputation and contributes to positive earnings surprises. However, not all findings are conclusive; Soana (2011) argued that there is no statistically significant relationship between social sustainability and financial performance.

2.4. Sustainability Initiatives Reporting

Sustainability reporting has become a critical component of corporate governance in the banking sector, enhancing transparency, accountability, and stakeholder engagement. Through sustainability disclosures, banks align their operations with global ESG goals and communicate non-financial risks and opportunities. Globally, frameworks such as the EU’s Non-Financial Reporting Directive and the Global Reporting Initiative (GRI) have standardized sustainability reporting practices (Global Reporting Initiative, 2020). In Sri Lanka, although banks have made notable progress in sustainability reporting, there remains room for improvement compared to global best practices. Effective sustainability reporting not only attracts socially responsible investors but also enhances risk management, operational efficiency, and reputational capital contributing to long-term financial success. This study uses a sustainability index based on the latest GRI 2020 guidelines to assess banks’ reporting on economic, environmental, and social initiatives, providing a comprehensive measure suited to the Sri Lankan context.

2.5. ***Financial Performance of Banks***

Financial performance is a fundamental indicator of a company’s profitability, stability, and investor appeal (Supriyadi, 2021). In the banking sector, financial performance is typically evaluated using financial statements and ratio analysis, with Return on Equity (ROE) and Return on Assets (ROA) serving as key metrics. ROE measures the effectiveness of using shareholders’ equity to generate profits, while ROA assesses the efficiency of asset utilization.

Sustainability practices have been increasingly linked to financial performance. Nobanee and Ellili (2017) noted that sustainable banks often enjoy reduced operational costs and stronger stakeholder relationships. Benvenuto et al. (2023) further asserted that companies with effective sustainability reporting tend to experience increased investor confidence and improved stock performance. As ESG concerns grow globally, sustainability reporting is becoming vital for attracting responsible investors and ensuring long-term financial viability.

The empirical studies discussed above reveal that the economic, environmental and social sustainable initiatives drive the banks towards higher banking performance from many perspectives. The adoption of economic sustainability initiatives by the banks support to mitigate and manage the risk while ensuring its long-term financial stability and profitability. The environmental sustainability initiatives promote the banks and let it attract eco-friendly customers. The social sustainable initiatives enhance the brand reputation and customer loyalty and attract more ethical investors towards the banks. However, the area of study is still emerging and the available findings are not substantial enough to come into a clear-cut understanding on the impact of these economic, environment and social sustainable practices on banks financial performance.

Existing studies in the Sri Lankan context have primarily examined isolated aspects of sustainability in banking, such as the relationship between green banking and bank performance (Dewasiri et al., 2024) or the influence of corporate social responsibility on commercial banks (Abeysinghe & Basnayake 2015). However, there is a notable absence of research that comprehensively investigates the impact of sustainability across its three dimensions environmental, economic, and social on the financial performance of banks. This gap in the literature underscores the need for a more holistic analysis. Accordingly, the present study seeks to address this gap by examining how economic, environmental, and social sustainability initiatives collectively influence the financial performance of banks in Sri Lanka.

3. METHODOLOGY

The paradigm of this research is positivism which holds the assumptions that that reality is observable, measurable, and quantifiable. Because this paradigm makes it possible to test hypotheses and develop conclusions using actual data and statistical techniques, it is well-suited for analyzing the relationship between sustainability initiatives and banks' financial performance The deductive approach will be used for this study because it builds on well-established concepts about sustainability and financial performance, as described in the literature review. The study then aims to evaluate these theories in the context of the Sri Lankan banking sector, giving a well-structured approach from theory to empirical investigation. Further, this study employs a quantitative research methodology as it allows for systematic variable measurement, statistical analysis, and the development of numerical data that can be used to examine the relationship between the independent and dependent variables of the study. The use of secondary data, such as financial reports and bank sustainability disclosures, is consistent with this technique and assures that the study's findings are supported by empirical evidence.

The population for this study consists of all licensed commercial banks (LCBs) operating in Sri Lanka. At the time of the study, the country has 26 licensed commercial banks (CBSL,2023). These banks play an important role in the financial system and contribute significantly to Sri Lankan economic stability. The study focuses on understanding how sustainability measures affect the performance and financial stability of these banks, by generalizing the findings obtained by the sample of the study.

Adopting the purposive sampling method, a selected group of six licensed commercial banks is chosen as the sample out of the total population of 26 commercial banks. These banks have the largest asset base and considered as the most significant banks in the Sri Lankan financial industry thereby designated as Systemically Important Banks [SIBs]. These SIBs are included in the sample because of their sustainability policies and financial results are typical of the Sri Lankan banking industry.

The conceptualization process of the study focuses on understanding how sustainability initiatives, specifically economic, environmental, and social initiatives, affect bank financial performance. The study uses these three independent factors, which are quantified using specific indices, to assess their impact on the dependent variable, "Banks Financial Performance".

3.1 Independent Variables

3.1.1 Economic Initiatives:

Economic initiatives are strategies and initiatives that contribute to overall economic sustainability. Economic initiatives are measured using an Economic Index. This index is determined through an analysis of the number of economic guidelines fulfilled by the bank to the Global Reporting Initiative (GRI) criteria. The calculation involves dividing the number of fulfilled economic guidelines by the entire number of economic guidelines that should be fulfilled, according to the GRI framework (Eranga & Wijesinghe, 2021). This index offers a standardized measure of a bank's commitment to economic sustainability**.**

3.1.2. Environmental Initiatives:

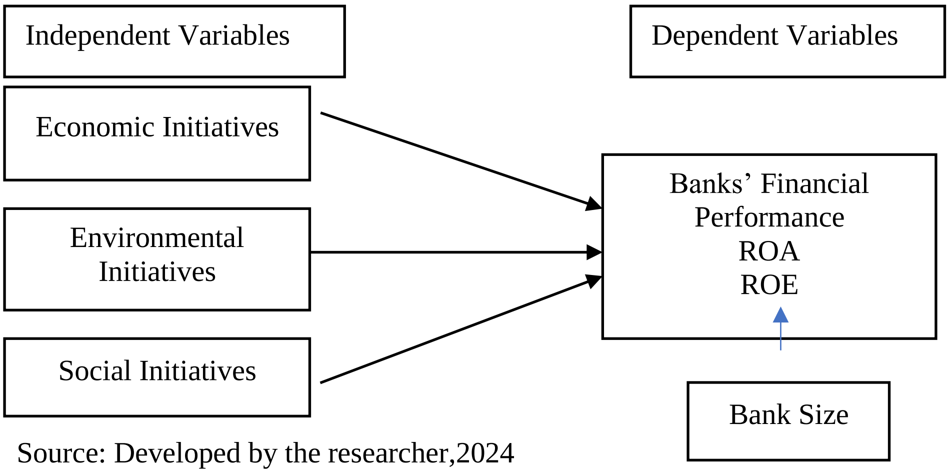
Environmental initiatives are efforts undertaken to minimize their environmental impact and promote environmental stewardship. These activities could include energy-efficient operations, reducing greenhouse gas emissions, and funding projects that promote renewable energy. The Environmental Index was developed to evaluate a bank's environmental initiatives. This index is produced similarly to the economic Index, by dividing the number of environmental guidelines fulfilled by the total amount of applicable environmental criteria, as defined in GRI standards (Eranga & Wijesinghe, 2021).

3.1.3. Social Initiatives:

Social initiatives are efforts to favorably impact society, such as community development projects, financial inclusion, fair work standards, and support for social causes. The Social Index is used to evaluate social efforts. This index is produced through an analysis of the number of social standards fulfilled by the bank to the total number stated by the GRI (Eranga & Wijesinghe, 2021).

3.2 Dependent Variable

The dependent variable in this study "Banks Financial Performance" is measured in terms of financial results, such as profitability, efficiency, and financial strength. The primary measures to indicate banks' financial performance are Return on Equity (ROE) and Return on Assets (ROA). ROA represents a firm's profitability with its total assets (Kabajeh et al., 2012). ROE is a measure of the profitability of a business in relation to its equity (Kabajeh et al,2012). These ratios are extensively used as a comparative measure because they are very much dependent on the industry under consideration. Based on these variables the researcher developed the conceptual framework below;



Source: Developed by the researcher,2024

Figure 1: Conceptual Framework

Based on the conceptual framework following hypothesis are developed;

H1: There is a significant impact of economic initiatives on banks' financial performance

H2: There is a significant impact of environmental initiatives on banks' financial performance

H3: There is a significant impact of social initiatives on banks' financial performance

Data for the study is gathered from the annual reports of Sri Lanka's six Systemically Important Banks (SIBs) over five years from 2018 to 2023. The annual reports, which were accessed through the banks' official websites, include detailed disclosures on economic [EI], environmental [ENI], and social initiatives [SI] as well as financial statements required for calculating performance metrics such as return on equity (ROE) and return on assets (ROA). The economic index, environmental index, and social index were derived using the Global Reporting Initiative (GRI) standards and served as independent variables in the analysis. Accordingly, the two regression models developed to test the banks' financial performance are as follows

ROA= a + b1EI+ b2EnI+ b3SI+ei---(1)

ROE = a + b1EI+ b2EnI+ b3SI+ei---(2)

4. FINDINGS

The findings of the study encompass with a correlation analysis followed by a panel data regression analysis which was tested for two separate models ROA and ROE after satisfying the necessary assumptions related to panel data regression.

In this study, the researcher tested the correlation between the three independent variables and two dependent variables separately, with the Firm Size (Control Variables). Table 1 illustrates the correlation coefficient of ROE (dependent variable 1) with independent variables (EI, ENI, SI) and Control variable (Bank size).

Table 01: Correlation Analysis -ROE

	ROE	EI	ENI	SI	BNKS
ROE	1.0000				
EI	-0.2343	1.0000			
	0.2128				
ENI	-0.4242	0.5908	1.0000		
	0.0195	0.0006			
SI	-0.2381	0.7111	0.6800	1.0000	
	0.2051	0.0000	0.0000		
BNKS	0.6015	-0.0015	-0.4077	-0.3158	1.0000
	0.0004	0.9937	0.0253	0.0891	

Source: Developed by the researcher,2024

The results of the correlation coefficient depict that Economic Initiatives and the Bank Size have a significant moderate correlation with the ROE. The other two independent variables showing an insignificant relationship with the ROE highlights the necessity of further investigating the reasons for these finding.

When analyzing the correlation of independent variables with the dependent variable ROA [Table 2] it reflects that Economic initiatives and Social initiatives indicate a significant relationship with the ROA at 0.05 significance level. However, it is noteworthy that these two variables express a negative correlation with ROA interpreting that when commercial banks focus more on the Economic and Social initiatives aiming sustainability it will have a moderate negative impact on the returns of the commercial banks. Therefore, researcher suggest to further investigate these finding by comparing a comprehensive comparison with the similar empirical studies.

Table 02: Correlation Analysis -ROA

	ROA	EI	ENI	SI	BNKS
ROA	1.0000				
EI	-0.6196	1.0000			
	0.0003				
ENI	-0.3400	0.5908	1.0000		
	0.0660	0.0006			

SI	-0.6391	0.7111	0.6800	1.0000	
	0.0001	0.0000	0.0000		
BNKS	0.0375	-0.0015	-0.4077	-0.3158	1.0000
	0.8442	0.9937	0.0253	0.0891	

Source: Developed by the researcher,2024

4.1 Regression Analysis

The study employs a panel data regression model in order to investigate the relationships between the sustainable initiatives and Banks' financial performance by assessing the multiple entries across the time period of 2019 to 2023. Prior obtaining the output of the regression model necessary diagnostic tests were conducted to confirm the models' validity and reliability. Accordingly, study focuses on testing four main assumptions: multicollinearity, heteroscedasticity, autocorrelation, and cross-sectional dependencies.

The test results ensured that the variables are free from multicollinearity issues as there were no correlation coefficient which exceeds 0.8. confirming that there is no multicollinearity between the independent variables. Further, the Wald test result was used to identify heteroscedasticity. The p-value of Wald test was greater than 0.05 rejecting the alternative hypothesis which explains that there is no heteroscedasticity issue in the model for ROA & ROE. To test the autocorrelation which explains the temporal connection between a given variable and its lagged version, Wooldridge test was adopted. The results of the test reported F value with a probability value less than 0.05 rejecting the alternative hypothesis. Therefore, it was evident that no serial correlation is observed in both ROA and ROE models. Finally, the cross-sectional dependencies were tested to validate that residuals are not correlated across the banks data. The results of the Pesaran's test of cross-sectional independence confirmed that the residuals are not correlated as the P value obtained was greater than 0.05 thereby rejecting the alternative hypothesis.

Based on the Human test results for both ROA and ROE models, Fixed effect model was selected as appropriate to conduct the regression analysis. The results rejected the null hypothesis as the p-value (Prob>Chi2) was lower than 5%. Alternative hypothesis indicates that random effects would be inconsistent and efficient therefore the fixed effect model was suggested. Accordingly, table 3 provides the results of the ROE model as follows;

Table 3: Regression Analysis - ROE

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-35.21414	4.347099	-8.100607	0.0000
LOG(EI)	-0.364955	0.112215	-3.252287	0.0014
LOG(ENI)	-0.186025	0.129172	-1.440131	0.1520
LOG(SI)	0.371695	0.144547	2.571440	0.0111

LOG(BS)	10.77903	1.435613	7.508317	0.0000
R-squared	0.353027			
Adjusted R-squared	0.335179			
F-statistic	19.78014			
Prob(F-statistic)	0.000000			

Source: Developed by the researcher,2024

The findings reveal that two independent variables specifically, economic initiatives and social initiatives have a significant relationship with the return on equity of commercial banks while the variable environmental initiatives have an insignificant relationship with ROE. Further the control variable, bank size also appears to have a significant relationship with the bank's performance indicated through ROE. Nevertheless, it is also observed that both economic and social initiatives have negative coefficients, indicating that when a greater number of sustainability initiatives are introduced it tends to affect negatively on the net income of commercial banks. Table 4 presents the relationship of sustainability initiatives with the banks' financial performance measure by the Return on Assets as follows;

Table 4: Regression Analysis - ROE

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-5.575396	2.868045	-1.943971	0.0538
LOG(EI)	-0.157562	0.074035	-2.128210	0.0350
LOG(ENI)	0.063398	0.085223	0.743911	0.4581
LOG(SI)	-0.406756	0.095367	-4.265181	0.0000
LOG(BS)	0.175202	0.947161	0.184976	0.8535
R-squared	0.352980			
Adjusted R-squared	0.335131			
F-statistic	19.77606			
Prob(F-statistic)	0.000000			

Source: Developed by the researcher,2024

The results of the ROA model further corroborate the findings of the ROE model, indicating a significant negative relationship between economic and social initiatives and banks' financial performance. In a related study, Buallay et al. (2021), using a sample of 882 banks across 80 countries, reported a negative impact of ESG scores on all performance indicators, regardless of bank type or geographic location. These findings highlight the need for further investigation into the relationship between ESG initiatives and financial performance, as they appear to contradict much of the existing empirical literature (Eranga & Wijesinghe, 2021).

In both models' F-Statistics have a p-value of 0.000 highlighting that the overall models are significant. Therefore, it can be concluded that the independent variables significantly explain the variance in the dependent variables, ROE and ROA.

4.2 Hypothesis Testing and Discussion

This study focuses on measuring the impact of Sustainable initiatives on banks' financial performance. To examine the relationship, the researcher formulated three hypotheses and the decisions of the hypothesis can be depicted as follows;

Table 5: Hypotheses Testing

Hypothesis	Result	Decision
Hypothesis 1: There is a significant impact of economic initiatives on banks' performance.	Significant	Accepted
Hypothesis 2: There is a significant impact of environmental initiatives on banks' performance.	Insignificant	Rejected
Hypothesis 3: There is a significant impact of social initiatives on banks' performance.	Significant	Accepted

Source: Developed by the researcher,2024

The findings revealed that Economic Initiatives have a significant impact on banks' financial performance both measured in terms of ROE and ROA. This outcome directly addresses Research Objective 1; which aims to investigate the impact of economic initiatives on the performance of banks in Sri Lanka. However, this finding is contradictory with the study done by prior studies which revealed that economic and environmental initiatives have an insignificant impact on both Return on Assets (ROA) and Return on Equity (ROE), and ultimately on overall banks' financial performance in Sri Lanka's banking sector.

The regression results indicate that Environmental Initiatives have an insignificant impact on banks' financial performance. This finding directly contributes to Research Objective 2; which aims to investigate the impact of Environmental Initiatives on the Performance of Banks in Sri Lanka. Similarly, prior studies discovered that there is no significant impact of environmental initiatives of sustainability on banks' financial performance measured in terms of profitability, liquidity and operations. The findings suggest that adherence to sustainability standards does not necessarily translate into improved financial metrics for bank.

The analysis shows that Social Initiatives have a significant impact on banks' financial performance based on the regression results. This aligns with Research Objective 3; which aims to investigate the impact of Social Initiatives on the Performance of Banks in Sri Lanka. The finding appears to be dissimilar with the study conducted by some prior studies which found that there is no significant impact of social initiatives on banks' financial performance.

5. CONCLUSION AND RECOMMENDATIONS

Overall, this study discovered that aspects of sustainability initiatives (Economic, and Social initiatives) have a statistically significant impact on the banks' financial performance of Sri Lankan banking sector. This finding emerges as a significant contribution to this domain as most of the empirical studies have reveled contradictory findings confirming that sustainability initiatives have insignificant relationship with financial performance measure, indicating no effect on Return on Equity (ROE) or Return on Assets (De Silva,2019). However, in Sri Lankan context although the sustainability initiatives are prevalent, their direct impact on financial performance remains still inconclusive. (De Silva,2019; Weerarathna et al., 2021)

Further the findings emphasized the necessity to further analyse the outcome of obtaining negative coefficients for Economic and Social initiatives yet they found to be significant. While studies such as weerarathna et al., (2021) have come across weaker insignificant relationship of sustainability reporting and listed companies' performance, it can be argued that specifically for banks the initial investment in economic initiatives such as green technologies and practices can lead to short-term financial strain, impacting overall banks' financial performance.

These investments can lead to increased operational costs, which may negatively affect banks' profitability in the short run. The need to comply with sustainability regulations and standards can also impose additional costs on banks, potentially leading to a negative impact on their financial performance. While sustainability initiatives are crucial for long-term environmental goals, their immediate impact on banks' financial performance in Sri Lanka thereby can be negative or insignificant. The balance between investing in sustainability and maintaining financial health remains a challenge for banks, necessitating further research to understand the long-term implications of these initiatives on performance.

Finally, it can be concluded that although the integration of sustainability appears to be beneficial, further empirical studies are needed to establish a definitive link between these initiatives and financial outcomes in the banking sector of Sri Lanka.

5.1 Recommendations

Reviewing the findings of this study, the following recommendations can be suggested in terms of improving the performance of banks.

Since the environmental initiative does not have a significant effect and economic and social initiatives found to be negatively impact on ROE and ROA, the banks should prioritize integrating these sustainability initiatives with into their core business strategies. This might involve developing sustainable financial instruments, such as green bonds or sustainable investment funds, that can offer both economic returns and long-term sustainability advantages. The study's findings indicate that existing sustainability initiatives may not be engaging strongly with stakeholders, such as customers and investors. Banks should invest in awareness campaigns and actively involve stakeholders by exhibiting the long-term benefits and impact of sustainability measures. This can assist develop stronger reputation, increase client loyalty, and eventually improve financial performance.

Although social activities were proven to have a negative impact, their potential long- term usefulness should not be underestimated. Banks could improve their social responsibility programs by prioritizing activities that directly benefit local communities, such as financial literacy programs or inclusive banking services for marginalized populations. Addressing important social issues can help banks build reputations and gain a competitive advantage, potentially leading to better financial outcomes in the future.

Further Banks should consider technical solutions, such as digital platforms, to help with sustainability activities. This could include automating procedures to reduce paper waste, enhancing energy efficiency with smart technologies, or providing digital financial services that encourage environmental sustainability. Technology adoption can increase operational effectiveness and attract an expanding customer base.

5.2 Implications of the Study

This study contributes to the existing literature on the nexus between sustainability and financial performance, specifically in the banking industry. The study raises concern about the idea that sustainability initiatives result in positive financial outcomes, indicating that their impact may vary concerning both the environment and how well they are incorporated within the organization. It also provides significant insights for Sri Lankan banking professionals and policymakers directing their attention to the important fact that they should not rely merely on sustainability initiatives to improve short-term financial performance, instead focus on comprising such initiatives towards an expanded business strategy for creating long-term value. This may lead banks to modify their approach to sustainability and bring their efforts towards activities that meet stakeholder needs as well as organizational objectives. Banks can also use this information to improve their sustainability initiative disclosures and engagement with regulators, investors, and consumers, resulting in a more systematic approach to sustainability.

5.3 Limitations and Future Research Directions

The analysis is limited to evaluating the impact of sustainability initiatives on immediate financial outcomes, specifically Return on Equity (ROE) and Return on Assets (ROA). Future research should focus on the long-term effects of sustainability initiatives, as the benefits of such measures tend to evolve over time. Additionally, other financial indicators, such as shareholder value and customer retention, can be taken into consideration for a more comprehensive analysis.

Moreover, this study did not account for the qualitative dimensions of sustainability initiatives, such as employee engagement or organizational culture. This gap can be addressed in future research by adopting a mixed-methods approach, which would enable the assessment of both quantitative and qualitative impacts of sustainability practices within the banking sector.

Finally, the study's scope is restricted to six Systemically Important Banks (SIBs) out of 26 licensed commercial banks (LCBs) in Sri Lanka, which may limit the generalizability of the findings. To overcome this limitation, future research could expand the sample size to include a larger number of LCBs, thereby providing a more comprehensive understanding of the effects of sustainability initiatives. Additionally, extending the study period could offer valuable comparative insights into the long-term impact of such initiatives.

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