International Research Journal of Advanced Engineering and Science
ISSN (Online): 2455-9024

How Does Corporate Social Responsibility Affect Financial Stability? - A Study of Sri Lankan Licensed Commercial Banks

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Abstract**—** *This research study aims to identify the influence of Corporate Social Responsibility on Financial Stability. This study embodies only eight licensed Sri Lankan commercial banks due to the minimization of missing data. The study used secondary data from the CSE's database, which was compiled from yearly financial reports of licensed commercial banks. The analysed Corporate Social Responsibility indicator includes a natural log of the amount spent on Corporate Social Responsibility activities. In contrast, the financial stability indicator embraces the Z-score, which is adopted with literature support. Pooled Ordinary Panel least squares regression analysis has been employed for the study to investigate How Corporate Social Responsibility affect Financial Stability. According to the findings of the study, the attribute of Corporate Social Responsibility, which is the natural log of the amount spent on CSR activities, has a significant and positive impact on Financial Stability. The major finding of the research ultimately reveals that Corporate Social Responsibility significantly influences the Financial Stability of licensed commercial banks in Sri Lanka in a positive way. Based on the findings, the researcher suggests that banks should indulge in Corporate Social Responsibility activities and commit more funds to corporate donations in order to strengthen their the Financial Stability.*

Keywords**—** *Corporate Social Responsibility, Financial Stability, Licensed Commercial Banks.*

I. Introduction

Corporate Social Responsibility has been a famous research area in the focus of academicians over many decades. Masulis and Reza (2015) illustrates Corporate Social Responsibility as a corporate charitable contribution and also as an important form of discretionary corporate expenditures. The World Business Council for Sustainable development (1999) defines "Corporate Social Responsibility (CSR) as the continuing commitment by business to behave ethically and contribute to economic development while improving the quality of life of the workforce and their families as well as of the local community and society at large". CSR also serves as the strategy to cope with the dynamic environment and it makes the good business sense in the context of social investment. (Ness, 1992). This depicts that CSR is a strategy used by firms as a corporate expenditure which also drives towards the economic development by contributing to the society.

The long literature from the concept of CSR examined the association between CSR and Financial Performance vastly in various sectors in consistent with the stakeholder theory (Freeman, 1984). Numerous research studies from the foreign countries found the positive association between CSR and Financial Performance. (e.g. Kaur & Singh, 2020; Ikram et al., 2019; Zhou et al., 2015; Chen & Wang, 2011; Fu & Shen, 2015; Ofori et al., 2014; Uadiale & Fagbemi, 2012). Even though it is said that Sri Lankan companies are still in infant level while analyzing CSR (Kengatharan et al., 2020) some researchers from Sri Lanka also found that CSR and Financial Performance are related in a positive way. (e.g. Jayasinghe, 2020; Gamhewage et al., 2018).; Wijesinghe & Senaratne, 2011; Nimsith et al., 2017). Researcher observed that the concept CSR is continuously repeating with CSR disclosure practices and its association with financial performance. Thus, the findings of (Alharthi, 2017) depicts that there is a strong correlation between financial performance and financial stability while profits increase the stability and reduce the risk of bankruptcy. This gave the prompt to researcher to take financial stability as an independent variable.

Financial Stability deprives the major concern from government of the countries and researchers at the macro economical level but recently academicians have made into the reality that stable financial firms are mandatory while concerning the Financial Stability of a country. (Ramzan et al., 2021). So, analyzing Financial Stability of firms in financial sector of a country leads to get the comprehensive picture of Financial Stability of an economy. Considering Sri Lanka, the banking sector dominated the financial sector accounting for 72.5 percent of total assets as at end 2020. (Central Bank Annual Report, 2020)

A sound banking sector is a major determinant of economic growth. (Zeqiraj et al., 2020). Even though this recent finding emphasis on the importance of banking sector to the economic growth of the Southeast European countries, this was also proved by many scholars (e.g., King & Levine, 1993; Rajan & Zingales, 1998; Ferreira, 2008; Abusharbeh, 2017) before. Thus, the banking sector has been becoming the most important sector in all over the countries in the world. No exceptionally in Sri Lanka, Kumari, (2017) also supported in her studies that the economic development is affected by the growth of banking sector in Sri Lanka. Therefore, analyzing the financial stability of the banking sector in the research studies is quite vital for the economic development of the country.

There are few very recent researches in foreign context have analyzed the impact of CSR on Financial stability and even they have found out the CSR has a significant impact on Financial stability in a positive way. (e.g. Cooper et al., 2019; Ramzan et al., 2021). Cooper et al. (2019) further concluded that CSR is a barometer for banks that act in a way consistent with promoting a stable and sound financial sector. Ramzan et al. (2021) also strongly brought their conclusion as banks that invest more in CSR initiatives strengthen their client relationships, hence reducing their financial risk and enhancing their Financial Stability.

Justifications of CSR and Financial Stability can be found in many. Theoretically, it is consistent with the stakeholder theory (Freeman, 1984). Empirically. Ramzan et al. (2021) justified that CSR can lead to long-term financial sector stability because many firms participate in CSR activities after knowing that firms which engaged in CSR got much longer life times than other firms which didn't do so. Cooper et al. (2019) pointed out that a strong CSR encourages managers to act in a manner that is consistent with the goals of Financial Stability. Chollet and Sandwidi (2018) clearly stated in their findings that CSR factors seem to mitigate the risk so management should be more committed to CSR to reduce firm risks. This finding can lead to a fact that reduced risk drives into a financially stable condition. Karagiorgos (2010) analysed CSR and found out a positive and significant relationship between CSR and stock returns and suggested to adopt CSR strategy to get the positive evaluation from the market and its stakeholders. Researcher can depict from this finding that higher stock value and positive evaluation from market and stakeholders would be leading to a stable position.

Further in Sri Lanka, Jeewanthi et al. (2019) found that CSR appears to be a market-based performance driver as investment in CSR can attract more investors and address competition in the market. This finding also supports to the impact of CSR on Financial Stability as through the increased market performance there will be mitigation in risk and this can lead to the Stability of the firm.

Thus, researcher observes that CSR and Financial Stability both leads to the economic development and also CSR would have the significant impact on Financial Stability in a positive way. Further analyzing the impact of CSR on Financial Stability of banking sector would be even beneficial so as to take prompt actions to strengthening the financial sector as well as the economy as a whole.

As such, the research question has been arisen as "How does CSR impact on Financial Stability?" while extensive studies have focused on CSR and Financial Performance (e.g. Kaur & Singh, 2020; Ikram et al., 2019; Zhou et al., 2015; Chen & Wang, 2011; Fu & Shen, 2015; Ofori et al., 2014; Uadiale & Fagbemi, 2012) only a few research studies have been conducted in the context of CSR and Financial Stability (E.g. Cooper et al., 2019; Ramzan et al., 2021). In Sri Lankan context, even though most of the research studies have been examined CSR and Financial Performance (e.g. Jayasinghe, 2020; Gamhewage et al., 2018; Wijesinghe & Senaratne, 2011; Nimsith et al., 2017; Kengatharan et al., 2020; Abeysinghe & Basnayake, 2015; Lakshitha & Perera, 2016).

None of the research studies focused on CSR and Financial Stability of banking sector. Further, most of the researchers examined CSR as a CSR activities disclosure. (e.g. Kengatharan et al., 2020; Jayasinghe, 2020; Gamhewage et al., 2018; Wijesinghe & Senaratne, 2011). The research studies which analyzed CSR as the corporate donations or the amount spending on CSR are scant (e.g. Nimsith et al., 2017). Therefore, the empirical research gap is found. Further, the No studies which analyze the impact of CSR on Financial Stability of the Licensed Commercial Banks have found in Sri Lanka. Thus, the contextual gap is also established here.

Thus, the current study attempts to fill the gap in the literature by investigating the effect of Corporate Social Responsibility on Financial Stability of the Sri Lankan Licensed Commercial Banks using annual reports from CSE website. This research article is structured as follows: Section 2 provides a review of the empirical studies that examine the impact of CSR on financial Stability of licensed Commercial Banks in Sri Lanka; Section 3 depicts the Methodology; Section 4 focuses on the findings and their interpretation; and Section 5 concludes the study and provides suggestions.

II. Literature Review and Hypotheses

In consistent with the stakeholder theory (Freeman, 1984) numerous studies concluded the findings with significant and positive association between CSR and Financial Performance in various sectors from the foreign countries (E.g. Kaur & Singh, 2020; Ikram et al., 2019; Zhou et al., 2015; Chen & Wang, 2011; Fu & Shen, 2015; Ofori et al., 2014; Uadiale & Fagbemi, 2012). In Sri Lankan context, there are also some researchers who found out that CSR and Financial Performance are related in a positive way. (E.g. Jayasinghe, 2020; Gamhewage et al., 2018; Wijesinghe & Senaratne, 2011; Nimsith et al., 2017). Not surprisingly, only a few numbers of researchers found out significant and negative impact of CSR on the Financial Performance from foreign countries (e.g. Rutledge et al., 2014). But in Sri Lankan context, it is weird that most of the research studies found out significant and negative association between CSR and Financial Performance. (e.g. Kengatharan et al., 2020; Abeysinghe & Basnayake, 2015; Lakshitha & Perera, 2016). They even argued for the negative relationship that most of the firms they didn't even start to practice CSR activities and also haven't yet revealed in the annual report (Kengatharan et al., 2020). It is also consistent with the findings of (Wijesinghe, 2012) that there is a significant discrepancy between the expected and actual amount of CSR disclosures concerning economic, environmental, and social aspects.

Besides, most of the research studies expressed there is no any association with CSR and Financial Performance from foreign countries (e.g. Ho et al., 2019; Aras et al., 2010; Zhang et al., 2019; Esteban-Sanchez et al., 2017; Szegedi et al., 2020). They even justified it as CSR is perhaps not sufficiently related with firm financial and economic performance in developing countries yet. (Aras et al., 2010) and also licensed banks may have suffered through the uncertain economic situations (Szegedi et al., 2020). The findings of (Alharthi, 2017) depicts that there is a strong correlation between financial performance and financial stability while profits increase the stability and reduce the risk of bankruptcy. So, researcher is induced to analyze CSR with financial Stability.

There are few very recent researches in foreign context have analyzed the impact of CSR on Financial stability and even they have found out the CSR has a significant impact on Financial stability in a positive way. (e.g. Cooper et al., 2019; Ramzan et al., 2021). Cooper et al. (2019) further concluded that CSR is a barometer for banks that act in a way consistent with promoting a stable and sound financial sector. Ramzan et al. (2021) also strongly brought their conclusion as banks that invest more in CSR initiatives strengthen their client relationships, hence reducing their financial risk and enhancing their Financial Stability. But in Sri Lankan context, there are no any researches found in the concept of CSR and Financial Stability in the banking sector.

Further, most of the researchers examined CSR as a CSR activities disclosure in foreign countries. (e.g. Ho et al., 2019; Aras et al., 2010; Zhang et al., 2019; Esteban-Sanchez et al., 2017; Szegedi et al., 2020). Most of the studies in Sri Lankan context also analyzed CSR as a CSR activities disclosure (e.g. Kengatharan et al., 2020; Jayasinghe, 2020; Gamhewage et al., 2018; Wijesinghe & Senaratne, 2011). On contrary, a few recent studies form countries only examined CSR on the basis of amount spent on CSR activities or corporate donations. (e.g. Ramzan et al., 2021; Zhou et al., 2015). The Sri Lankan studies, which analyzed CSR as the corporate donations or the amount spending on CSR are scant. (e.g. Nimsith et al., 2017). The literature review indicates that the majority of studies have concentrated on European, African, and other Asian countries, with only a few studies focusing on Sri Lanka.

In consistent with the stakeholder theory (Freeman, 1984), numerous studies concluded the findings with significant and positive association between CSR and Financial Performance in various sectors from the foreign countries (e.g. Kaur & Singh, 2020; Ikram et al., 2019; Zhou et al., 2015; Chen & Wang, 2011; Fu & Shen, 2015; Ofori et al., 2014; Uadiale & Fagbemi, 2012). In addition, the majority of research predict a favorable, significant influence of CSR on the Financial Stability of banks. (e.g. Cooper et al., 2019; Ramzan et al., 2021). The following hypothesis can be developed based on the supporting literature:

Hypothesis 1: There is a positive significant impact of Corporate Social Responsibility on Financial Stability of Licensed Commercial banks in Sri Lanka.

III. METHODOLOGY

Overall research design adopted for the study is explained as follows: Positivism research philosophy, deductive research approach, explanatory research design, archival and documentary research strategy and mono method quantitative study as the research choice are followed by the researcher.

The scope of this study is limited to Sri Lanka's eight licensed commercial banks. The population of interest for this study consists (initially) of the 24 Licensed Commercial Banks as reported by the Central Bank on September 30, 2021. In selecting the population, the potential of missing data was minimized by removing the banks that were unsuitable for the duration of the investigation. Eight licensed Commercial Banks remained in the population after the eliminations. This has done with the suggestion of (Kengatharan et al., 2020) said that future research can obtain more reliable results by analyzing CSR using samples of organizations with a long history of CSR practice. The other basis of the selection of eight licensed commercial banks is they are practicing and revealing the CSR activities in numerical terms clearly in their annual reports over a decade.

The study employs the statistical tool Pooled Ordinary Panel Least Squares Regression analysis to test the study hypotheses. Pooled Ordinary Panel least squares regression analysis will be performed to investigate the impact of Corporate Social Responsibility on the Financial Stability for a decade over the period of 2011-2020. It is supported by the techniques used in the research study of (Ramzan et al., 2021). Data analysis is carried out with the aid of the software package Eviews, which is used to analyze the data.

TABLE 01: Variables used in the study

Variable name	Proxy	Measures	Symbols
Financial Stability	Z-Score	((ROA + Equity) / Assets)) / Standard Deviation (ROA)	FS
Age	Number of operating years		Age
Size	The natural log of Total Assets		Size
Corporate Social Responsibility	The natural log of the actual amount spent on CSR activities		CP

Source-Developed by the researcher with the support of literature

Z-Score is used as a measure of Financial Stability in the study and it is been using as a measure in numerous studies (E.g. Ramzan et al., 2021; Gupta & Kashiramka, 2020; Abdelbadie & Salama, 2019; Ozili, 2018; Madi, 2016; Diaconu & Oanea, 2014)

Natural log of the corporate donation or the amount spending on CSR is employed as the indicator of Corporate Social Responsibility of Banks. It is used as the measurement of CSR in recent studies. (e.g. Ramzan et al., 2021; Nimsith et al., 2017; Zhou et al., 2015). Researcher took this initiative because the previous researchers in Sri Lanka examined CSR as a CSR activities disclosure and got negative relationship suggested that future research should be conducted to quantify the investment in CSR. (Lakshitha & Perera, 2016). Thus, researcher observed the repetitive method of measuring CSR as a CSR activities disclosure through various dimensions in Sri Lanka in most of the studies and also some studies found the negative association of CSR with Financial Performance in Sri Lanka. (e.g. Kengatharan et al., 2020; Abeysinghe & Basnayake, 2015; Lakshitha & Perera, 2016). Though they argued, this is quite against to the stakeholder theory (Freeman, 1984). Thus, Natural log of the corporate donation or the amount spending on CSR is employed in this study as the measurement of Corporate Social Responsibility of Banks would be leading to quantify the CSR practices and expecting to get accurate results.

International Research Journal of Advanced Engineering and Science
ISSN (Online): 2455-9024

Age and size are selected as the control variables in this study. These are the common important control variables used in most of the studies. (e.g. Ramzan et al., 2021; Kaur & Singh, 2020; Zhang et al., 2019; Dissanayake & Xydias-Lobo, 2016; Wijesinghe & Senaratne, 2011; Gamhewage et al., 2018). While analyzing the Financial Stability, these both will play the prominent role.

The impact of Corporate Social Responsibility on Financial Stability in this study tested with the following Model 1:

$FS_{it}= a_0+ \beta 1 \log CSR_{it} + \beta 4\ Age_{it} + \beta 5\ Size_{it} +\mu_{it}$

IV. FINDINGS AND DISCUSSIONS

4.1 Descriptive Analysis

TABLE 02: Descriptive Statistics

	Min	Max	Mean	Std. Deviation
CSR	0	22.32	15.25	3.68
Age	2	100	42.4	28.06
Size	23.39	28.72	26.54	1.28
FS	-0.88	6.9	3.39	1.98

Source- Generated by Researcher with the help of E-views

According to the statistics it can be observed that the minimum natural log of amount spent on CSR is 0 while maximum is 22.32. But the mean of natural log of amount spent on CSR with 15.25 indicates that overall the banks in Sri Lanka are allocating more amount of fund to CSR practices. This is quite higher than the Pakistan's banks as 15.13 is their maximum value. (Ramzan et al., 2021). Age has a mean of 42.4 and varies from 2 – 100; Size has a mean of 26.4 and varies from 23.39 – 28.72; Financial Stability has a mean of 3.39 and fall in the range within -0.88 - 6.9.

4.2 Regression Analysis

TABLE 03. Model summary

Model	R^2	Adjusted R^2	F-Statistics
1	0.394	0.370	16.499

TABLE 04. Result of regression analysis (Dependent variable = FS)

Independent variable	B	Std. Error	T	Sig.
(Constant)	-10.39	5.642	-1.84	0.000
CSR	0.095	0.061	1.55	0.042
Age	0.017	0.010	1.70	0.031
Size	0.436	0.232	1.87	0.000

Source- Generated by Researcher with the help of E-views

Table 03 shows the model summary.

$R^2 = 0.394$

Adjusted $R^2 = 0.370$

In this model R^2 indicates that 39.4% of the Financial Stability can be explained by the differences in the Independent variable (Corporate Social Responsibility). The remaining 60.6% of the Financial Stability is attributed to other factors. Here the value of an adjusted R^2 is 0.370, slightly less than the value of 0.394. The F-statistics and significance level shows that Model 01 generates statistically significant outcomes.

Table 04 presents the result of coefficient measure of Financial Stability (FS). This indicates that Corporate Social Responsibility has the significant impact on Financial Stability at 5% Significance level. β value for Corporate Social Responsibility is 0.095. This explains that one unit increase in Financial Stability will result a positive impact on Financial Stability with 0.095 units. The analysis states indicator of Corporate Social Responsibility has the significant and positive impact on Financial Stability. Size which is used as the control variable in this study shows the significant positive impact on Financial Stability at 1% Significance level while Age reflects the positive impact and significance at the 5% level.

4.4 Test of Hypothesis

Hypothesis of this study as follows:

Hypothesis 1: There is a positive significant impact of Corporate Social Responsibility on Financial Stability of Licensed Commercial banks in Sri Lanka.

From the analysis of Regression, in the model R^2 indicates that 39.4% of the Financial Stability can be explained by the differences in the Independent variable (Corporate Social Responsibility). Further, the result of coefficient measure of Financial Stability indicates that Corporate Social Responsibility has the significant positive impact on at 1% Significance level.

Therefore, H1 is accepted.

This conclusion complies with the research studies of Cooper et al., 2019; Ramzan et al., 2021 and also this proves the stakeholder theory (Freeman, 1984). This finding can also relate with the research studies which got positive association between CSR and Financial Performance. (e.g. Kaur & Singh, 2020; Ikram et al., 2019; Zhou et al., 2015; Chen & Wang, 2011; Fu & Shen, 2015; Ofori et al., 2014; Uadiale & Fagbemi, 2012; Jayasinghe, 2020; Gamhewage et al., 2018).; Wijesinghe & Senaratne, 2011; Nimsith et al., 2017).

V. CONCLUSION AND RECOMMENDATIONS

5.1 Conclusion

The purpose of this study was to examine the significant impact of Corporate Social Responsibility on Financial Stability of Sri Lankan licensed Commercial banks for the period of 2011- 2020. With the use of descriptive and Pooled Ordinary Panel least squares regression analysis the study's intended objectives have been successfully attained. Licensed Commercial banks in Sri Lanka have strengthened their Corporate Responsibility activities over these ten years. They are allocating more amount of money as corporate donations year by year. It can be concluded as Corporate Social Responsibility has significant positive impact on Financial Stability of commercial banks in Sri Lanka.

Further, CSR is quantified in terms of the amount spent for Corporate Responsibility activities in this study. Since this study resulted in the significant and positive impact on Financial Stability of licensed Commercial banks in Sri Lanka, it can be generalized that allocating funds to Corporate Social Responsibility activities can be strengthen the Financial Stability of the banks. CSR is a strategy used by firms as the social investment to survive in the market besides, it drives towards the economic development. Thus, the study gives valuable foresights to the banks in Sri Lanka where the banks play major role in economic development. Further, the concept CSR is continuously repeating with CSR disclosure practices and its association with financial performance. So, the study

G. Jathurika, "How Does Corporate Social Responsibility Affect Financial Stability? - A Study of Sri Lankan Licensed Commercial Banks," *International Research Journal of Advanced Engineering and Science*, Volume 7, Issue 4, pp. 241-246, 2022.

contributes to the research area of CSR to quantify CSR as the extension of previous literature.

5.2 Recommendations

This study reflects that the licensed commercial banks in Sri Lanka have been improving their Corporate Responsibility activities over the last decade. The generalized finding in this study which is "allocating funds to Corporate Responsibility activities can increase the Financial Stability" would be beneficial to the top management of the banks to rethink in the allocation of more funds to CSR activities to survive as Financially Stable in the market. The study proposes that the corporate management of developing banks should consider the decision of allocating funds as corporate donations in order to indulge more Corporate Social Responsibility activities to make an improvement in the Financial Stability by reducing risk. This can even ensure their long-term survival in the market. Further, the government of Sri Lanka also can implement some regulations in context with the allocation of corporate donations as a proportionate to the total assets of the firms.

5.3 Limitations of the study

Due to the possibility of missing data, just eight licensed Commercial Banks remained in the population, hence the study's sample size is insufficient. Further, the study is confined to only in secondary data, it would be better if future studies focus on both primary and secondary data for the analysis.

5.4 Directions for future research

In the future studies it would be better to cover all the banks in Sri Lanka while focusing on both primary and secondary data for the analysis. The comparison research studies between Sri Lanka and other countries would also be effective and beneficial to explore into new strategies used by other countries for the CSR practices. Besides, Corporate Social Responsibility can be analyzed with other prominent variables such as financial inclusion, Firm value and also Dividend policy in future other than repetitive Financial Performance.

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