Impact of Fundamentals on Share Price of Financial Firms in a Country Depressed by Economic Crisis

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Abstract

This study examined the influence of company fundamentals on the share prices of licensed commercial banks and finance companies of Sri Lanka; a country experienced a severe economic crisis since 2019. The data window comprised listed ten commercial banks and twenty-three finance companies for a period of seven years from 2014. Thus, the study elaborates the reaction of stock prices to the company's fundamentals under general economic conditions i.e., before experiencing the economic crisis. The Fixed Effect model with cluster-adjusted standard error was applied to deal with heteroscedasticity, autocorrelation, and cross-sectional dependence. The results of the overall analysis show that firm size and the Debt-to-Equity ratio have a significant influence on share prices in the banking and finance sector. Firm size has a positive impact, indicating that larger firms are perceived as less risky and more attractive to investors. Conversely, the Debt-to-Equity ratio exhibits a significant negative effect, reflecting the adverse impact of high financial leverage on share value. In contrast, Earnings-per-Share, Dividend Payout Ratio, Net Asset Value-per-Share, Firm Growth, Non-Performing Loan Ratio, and Return on Equity display an insignificant positive impact on share price. Additionally, Return on Assets, Capital Adequacy Ratio, Public Holding, and Firm Age show an insignificant negative effect, implying that these factors have not been primary considerations for investors in this sector. For the banking sector, Net Asset Value-per-Share and Return on Equity were found to have a significant positive impact on share price. In contrast, Return on Assets and Public Holding exhibited a significant negative relationship with share price. With regard to the finance sector, the Debt-to-Equity ratio showed a strong negative association with share prices. This study confirms that share prices are influenced by certain fundamentals like the Debt-to-Equity ratio, Firm Size, Return on Assets, Return on Equity, and Public Holding. The results emphasize how imperfections in the market and investor behavior have to be considered to understand the dynamics of share prices in the banking and financial sector of Sri Lanka, with reference to the economic factors.

Keywords: Company fundamentals, licensed commercial banks, licensed finance companies, share prices

Introduction

The efficiency of capital markets is crucial to the economic development of a country. The CSE provides the avenue for trading equity securities in Sri Lanka. Licensed commercial banks and finance companies also play a key role in the stabilization and development of a broader

economy. The determinants of share prices in the secondary market have long been a subject of interest for investors, academics, and policymakers. In particular, understanding the determinants of the share prices is important for making wise investment decisions.

This study focuses on examining how fundamental variables influence the share prices of the banks and finance companies listed on the Colombo Stock Exchange in Sri Lanka. It adopts a panel data approach to evaluate the relationship between firm-specific fundamentals and market prices, focusing on the period from 2014 to 2020. The findings are expected to contribute to the existing literature and provide insights into more informed investment decisions in Sri Lanka's financial sector.

Increasing firm value or maximizing shareholder wealth is the primary objective of any business organization. Firm value is often associated with share prices. Stock prices are determined in the secondary stock exchange, and high prices increase the firm's value. Share prices of a firm are affected by various factors and are mainly divided into company fundamentals (micro) and macro factors (external). This study, conducted on licensed banks and finance companies listed on the Colombo Stock Exchange, examined the impact of company fundamentals and selected control variables on determining the share price. The Colombo Stock Exchange, a significant player in the financial market, plays a crucial role in this research.

Investors use published financial data and other information that is relevant to the future growth of a company to make their investment and divestment decisions. Financial ratios are more common among investors, and they analyze financial data in terms of profitability, leverage, liquidity, and activity level to make investment decisions. Therefore, financial ratios affect a company's share price and act as key determinants of the share price of the company. The share price of the company is not only affected by the company's financial or internal information. External factors and investor sentiment also play a major role when investors make investment decisions.

Research Problem

Capital markets act as a bridge between investors and enterprises in need of capital, facilitating the efficient allocation of funds toward productive investments that drive economic growth. The Colombo Stock Exchange (CSE) acts as the epicenter of Sri Lanka's capital markets, where securities are traded, including the shares of publicly listed finance companies and banks. These licensed banks and financial institutions represent a major segment within the CSE. In Sri Lanka's dynamic economic climate, the main factors influencing the share price variations of listed banking and finance companies are not well understood, despite their crucial role in the economy. This study addresses this knowledge gap by investigating the empirical relationships between key financial fundamentals and stock prices of listed banking and finance institutions on the CSE.

The relationship between the company's fundamentals and the valuation of its equity has great practical relevance to investors in making informed decisions. Financial indicators such as profitability, efficiency, leverage, and asset quality indicate about the financial health and earning capabilities of listed institutions (Herath & Gunaratne, 2011). In the Sri Lankan literature, we observe some empirical studies which have established a causal relation between companies' fundamentals and their stock market performance of non-financial firms (Kengatharan & Dimon Ford, 2020), diversified financial firms (Jayarangi & Buddhika, 2025), and finance companies (Pandigamage & Ranaweera, 2023). Amongst Pandigamage &

Ranaweera (2023) have considered only finance companies with some financial performance measures. However, such extensive study is missing in the literature which covered both commercial banks and finance companies in a comparative study considering their financial performance, asset quality, and capital adequacy.

This research is based on data obtained from CSE, covering the company fundamentals in the banking and finance sector from 2014 to 2020. During this period, the sector experienced significant volatility, particularly in terms of asset quality and profitability. As illustrated by data from the Central Bank of Sri Lanka and the charts below, both banking and finance companies are subject to notable fluctuations in key financial indicators.
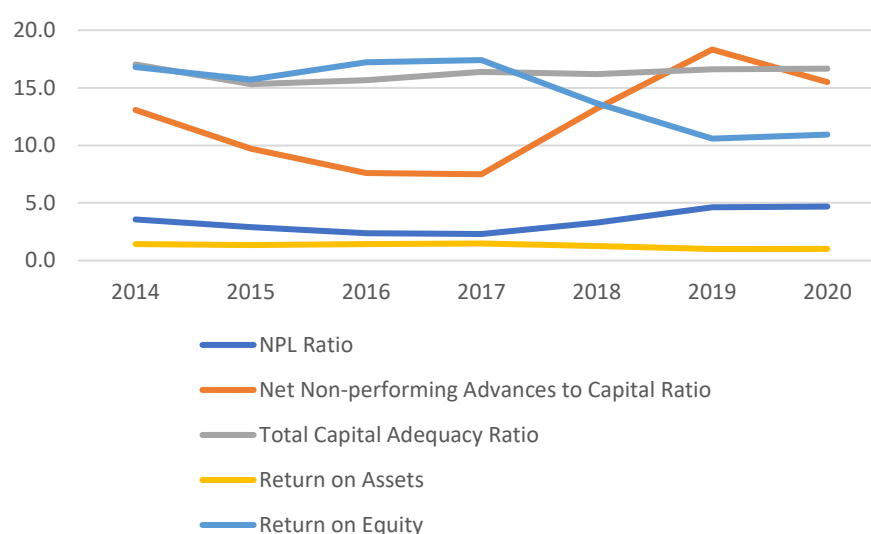

Figure 1: Key Financial Indicators – Licensed Banks (2014–2020)

As illustrated in Figure 1, the banking sector experienced a notable increase in the NPL ratio between 2017 and 2020, along with a decline in return on equity and return on assets, reflecting stress on earnings. Compared to banks, the finance companies showed even more pronounced fluctuations in their performance metrics (Figure 2). ROE saw sharp volatility, and the NPL Ratio rose significantly from 2017 onward, peaking by 2020. The weaker asset quality and profitability in finance companies highlight the sector's higher exposure to credit risk and economic fluctuations.

The higher NPL ratio of the sector indicated increased credit risk, which embodied a challenging position for maintaining asset quality. Further, the country's credit rating was downgraded by Fitch, which worsened the country's debt sustainability and overall economic outlook. All these factors affect the financial health of the banking and finance industry. All these factors affect the financial health of the banking and finance industry. Further, significant challenges came from regulatory changes, as CBSL is the monitoring body of the sector, and the capital adequacy requirement was increased to a considerable level. Concurrently, fluctuating returns on assets and equity and impaired asset quality significantly affected the company's fundamentals.
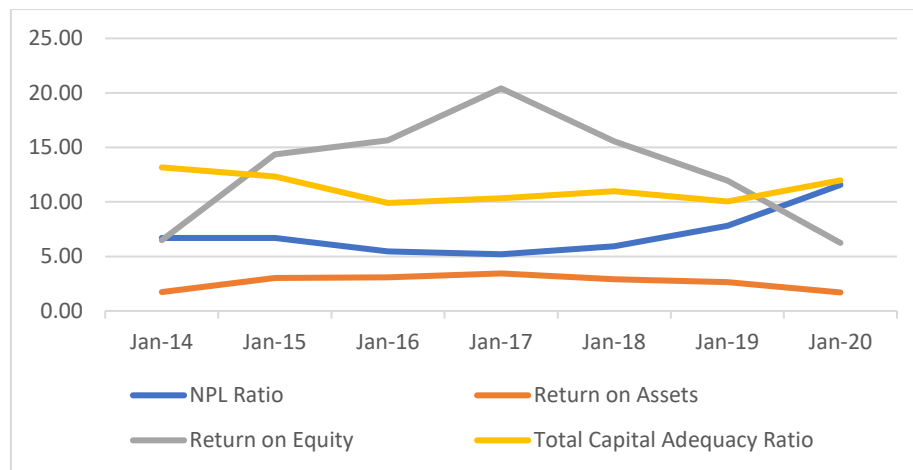
Figure 2: Key Financial Indicators – Licensed Finance Companies (2014–2020)

It is normally accepted that a banking share is traded above the book value, and to further understand how company fundamentals translate into investor sentiment and market pricing, a comparison between Book Value (BV) and Market Value (MV) was conducted for selected companies. Table 1 summarizes this comparison.

Table 1: Book Value vs. Market Value (2020)

Company Name	Book Value (Rs)	Market Value (Rs.)
Sampath Bank	292.00	162.40
Commercial Bank	130.83	095.00
Haton National Bank	290.78	172.00
LOLC Finance	005.96	002.20
LB Finance	167.20	120.50
Central Finance	200.86	081.00

Source: Annual Reports (2020)

The data clearly show that all selected companies are trading below their book value, a strong signal of market undervaluation or diminished investor confidence. This could be attributed to macroeconomic challenges such as the country's credit rating downgrade by Fitch, rising credit risk, and tighter regulatory capital requirements imposed by CBSL

Research Questions

The main question guiding this research is to what extent do company fundamentals affect share prices of licensed banks and finance companies in Sri Lanka?. To offer a comprehensive insight into this central question, the research will further delve into the following sub-questions.

- Are a firm's fundamentals associated with the market price of shares of banking and finance companies?
- Do the firm's fundamentals affect the market price of shares of banking and finance companies?
- Does the impact of a firm's fundamentals on the market price of shares vary with the sector (banking and finance)?

Significance of Study

This research aims to provide a substantial scholarly contribution by examining the relationship between company fundamentals and share prices of licensed banks and finance companies listed on the Colombo Stock Exchange in Sri Lanka. It aims to develop a comprehensive theoretical framework that can guide future research in the Sri Lankan financial market. This framework has the potential to act as a major consideration in equities research, providing a systematic approach for evaluating the impact of firm fundamentals on stock prices. Moreover, theoretical insights from this study may also have an important role in understanding the distinct characteristics and behaviors that financial markets exhibit in emerging economies.

On the practical level, this research provides strong framework for stakeholders, including investors, legislators, and company representatives in Sri Lanka. The financial market in Sri Lanka is currently experiencing change due to legislative modifications and economic fluctuations. To promote a stable and transparent market environment, it is imperative to utilize data-driven insights (Basu, 1983). This study can potentially give investors significant rewards through its insights. Acquiring a comprehensive understanding of the influence of the various company fundamentals on share prices would provide investors with the necessary expertise required to make informed judgments. With such understanding, they can capitalize on investment opportunities that stand a good chance of proving profitable and, at the same time, minimize potential losses. The intended audience of this communication comprises individuals involved in formulating and implementing policies impacting the finance sector. The possible impact of policymakers using the findings of this research is the facilitation of policymaking that promotes equity and effectiveness within the market environment. Organizations can develop strategic methods to increase the key elements of company fundamentals that have a significant impact in the Sri Lankan market by understanding these factors. Consequently, this can empower companies to secure investments and develop long-term, sustainable expansion.

Literature Review

This section carries an in-depth analysis of theoretical underpinnings and empirical evidence on the fundamental determinants of the stock market performance of firms. Accordingly, a critical analysis is undertaken to assess the methodologies and findings of key studies to establish gaps and inconsistencies that this research will address.

Theoretical Foundation

When establishing the effect of companies' fundamentals on stock market performance, it requires combining stock valuation with risk and return and some behavioral aspects of investors. The Dividend Discount Model (DDM) pioneered by Rosa & Mukhibad (2022), argues that the value of shares based on the expected future dividend stream discounted at the required rate of return as perceived by marginal investors. Current fundamentals like earnings, assets, financing costs, and investment needs determine a company's ability to generate future dividend flows. Higher expected future dividends increase valuation, while a higher discount rate required by investors reduces present value (Yuniningsih et al., 2019). DDM establishes a direct conceptual linkage between profitability, growth, payout-related fundamentals, and share prices. However, empirically, DDM performs poorly in explaining stock price movements since dividends account for less than half the variation (Tripathi, 2009). Investors also gain through capital gains. DDM offers a sound theoretical framework for how fundamentals affect intrinsic value through future dividends. Sri Lankan researchers have used DDM approaches to value listed firms, with modifications like adding expected capital gains to dividends in estimated cash flows (Ozlen, 2010). DDM models provide straightforward

valuation frameworks that are amenable to sensitivity analysis concerning financial variables. However, empirical limitations necessitate complementing DDM logic with insights from other pricing theories.

As per the DDM, dividends and their growth as fundamentals could determine the intrinsic value of shares, which, in turn, could fluctuate share prices. The extent to which the said share price reaction could be subject to the level of market efficiency. The Efficient Market Hypothesis (EMH), originally proposed by (Malkiel & Fama, 1970), contends that in an efficient market, share prices fully reflect all available information at all times. The weak form of EMH claims that past price data is incorporated in current prices. The semi-strong form posits that share prices adjust rapidly to publicly released information like earnings announcements and dividend policy changes. The strong form argues that even non-public information is reflected in prices (Malkiel & Fama, 1970). The logic underlying EMH is that competition among rational, profit-seeking investors analyzing fundamentals will cause share prices to incorporate new information quickly and converge toward intrinsic value (Malkiel & Fama, 1970). Fundamentals like earnings, assets, growth rates, and payouts determine expected future cash flows and, hence, intrinsic value as per discounted dividend valuation models. In efficient markets, deviations between prices and intrinsic value get arbitraged away.

However, critics argue that perfect efficiency is unrealistic due to frictions like trading costs, limits to arbitrage, information asymmetry, and investor irrationality (Maharaja & Saravanakumar, 2014). Further, empirical evidence shows that share prices respond swiftly to events like earnings releases, indicating that semi-strong efficiency holds reasonably well (Asquith & Mullins, Jr., 1983). Overall, EMH provides the basic economic logic for how company fundamentals get impounded into share prices through trading by informed investors. In the Sri Lankan context, academics view the Colombo Stock Exchange as reasonably efficient in the semi-strong form, with prices reflecting public information on fundamentals fairly rapidly (Adaramola, Abere, & Ogiamien, 2023). However, some studies have identified overreaction, suggesting limited weak-form efficiency (Samarakoon, 1996). Overall, EMH suggests company financials have a significant role in shaping the share valuations of listed Sri Lankan firms.

Depending on the level of market efficiency, investors would be differently affected by systematic risk, which would ultimately enhance return expectations of investors. This risk-return relationship is underlined by the Capital Asset Pricing Model (CAPM) which contends that share returns investors require and prices are determined by the stock's systematic risk relative to the broader market portfolio (Sharpe, 1964). Systematic risk is measured by the stock's beta, reflecting sensitivity to macroeconomic conditions affecting the market as a whole (Malkiel & Fama, 1970). CAPM posits that higher beta stocks will offer higher expected returns to compensate for their more significant non-diversifiable risks but will have lower current prices. Fundamentals can influence a stock's systematic risk exposure and required risk premium. The model assumes perfect capital markets and that investors only hold efficient portfolios comprising the market portfolio.

However, empirically, CAPM underperforms multi-factor models in explaining returns (Malkiel & Fama, 1970). Its assumptions of no trading costs, unlimited share divisibility, and universally efficient portfolios are unrealistic. However, the conceptual logic regarding the risk-return trade-off remains influential in asset pricing theory. Overall, CAPM suggests that company fundamentals that impact perceived systematic risk factor loadings may affect share

valuations. Financial leverage, volatility, and growth orientation influence systematic risk. However, the pricing model itself has limitations in its predictive power.

Compared to the above theories, Dimitrov & Jain (2008) propose Arbitrage Pricing Theory (APT) as an alternative factor model counting multiple factors which could determine return behavior of stocks. APT posits that share returns are driven by multiple macroeconomic factors beyond market risk, as in CAPM. Fundamentals determine a stock's sensitivity to pervasive economy-wide influences like inflation, industrial production, term structure of interest rates, etc. (Collins & Kothari, 1989). Exposures to macroeconomic factors are captured through factor loadings in the APT model. It suggests fundamentals affect share prices through both systematic and firm-specific channels. APT performs better empirically than single-factor CAPM (Blume, 1980). However, APT does not identify the relevant priced risk factors for a market, relying instead on statistical approaches.

For the Sri Lankan stock market, academics have used APT frameworks to assess systematic risk arising from macroeconomic volatility (Ball & Brown, 1968). Overall, APT provides a robust conceptual mechanism for how fundamentals drive share prices through multifactor exposures. However, a lack of guidance on relevant risk factors for a specific market reduces out-of-sample predictive ability (Basu, 1983).

Challenging EMH, behavioral finance theories also argue that share prices deviate from intrinsic values due to cognitive biases and limits to arbitrage (De Luca, 2017). Prospect Theory suggests investors are risk-averse in the domain of gains but risk-seeking over losses, causing overreaction and underreaction to the updates (Hatta & Dwiyanto, 2012). Biases like confirmation, anchoring, and availability heuristics also create mispricing. Limits to arbitrage allow anomalies to persist Umar et al (2021). In Sri Lanka, academics have found evidence of overreaction to earnings news and underreaction to broker recommendation changes, consistent with behavioral models (Samarakoon, 2004). However, whether mispricing can be systematically exploited remains contentious due to noise trader risk (Kuswardani & Johan, 2022).

Overall, behavioral finance theories complement the logic of informationally efficient markets, explaining temporary anomalies in the context of fundamentals. However, empirical research suggests that market efficiency prevails over long-term horizons (Turnip, 2022). Integrating behavioral perspectives provides insights into potential distortions from investor irrationality affecting short-term share returns. In conclusion, conceptual pricing models provide logically coherent frameworks for analyzing links between company fundamentals and share valuations through expectations of cash flows and required investor returns. Empirical evidence suggests no single model thoroughly explains share price behavior. An integrative multi-theory approach combining efficient market, risk pricing, and behavioral perspectives is needed to develop a comprehensive understanding of how fundamentals drive prices of listed companies in Sri Lanka's capital markets.

Empirical Evidence

Financial theory elaborates a strong link between company fundamentals and equity valuation (Maharaja & Saravanakumar, 2014; Purwanto & Safira, 2020; Putra & Wuryani, 2021). Fundamentals determine investors' expectations about future cash flows and, therefore, share prices. Empirical evidence abounds on the impact of company financial metrics represented by EPS, ROE, ROA, and DPS on the performance of share prices in global stock markets. This section summarizes findings from empirical studies focused on both developed and emerging

economies and highlights evidence emanating from the Sri Lankan setting. Financial performance is one of the significant determinants of firm value. Return on Equity, Return on Assets, and Earnings per Share were employed in this research to evaluate the impact of firm performance on share price. According to Werastuti (2014), firm performance is usually embodied in shareholder value. Putri and Suwitho (2015) establish that financial performance positively and significantly impacts firm value. This aligns with Hidayah (2014), who found that improved financial performance leads to higher firm value.

Earnings per share (EPS) helps investors find stocks that could give them a higher return, as they can compare the EPS of different entities. Empirical evidence shows that most individual investment decisions are based on the EPS. The price-earnings ratio (P/E ratio) is also based on the firm's market price per share and EPS. It is also a standard tool among investors for making comparisons between firms in similar industries to decide which firm's share is overvalued or undervalued. It helps to make wise investment decisions based on the company's ability to make money (Kaizoji & Miyano, 2019).

ROA measures the profitability derived from the total assets of the company, while ROE reflects the returns that accrue to the shareholders from their equity investment in the firm. Empirical studies have shown a strong positive association between ROA and share prices after considerations for leverage, implying that higher earning potential as reflected in ROA is rewarded through higher valuations (Kaizoji & Miyano, 2019; Musa, 2020; Tarczynski et al., 2020). Studies in emerging markets have found that higher ROE significantly and positively impacts share prices. Al-Malkawi et al. (2018) provided evidence of a strongly significant relationship between ROE and stock prices for Nepali banks over 2008–2012, as investors reward higher profitability relative to equity.

Funding policy, investment policy, and dividend policy are the functions of financial management. Funding policy involves determining the best sources of capital, hence determining the capital structure, cost of capital, and financial risk. These factors affect the firm's performance and, finally, the firm's value. The debt-to-equity ratio shows the capital structure of the firm. According to Sutrisno (2016), a firm's capital structure has a positive and significant impact on the firm's value, indicating that more debt in the capital structure increases the firm's value. Inversely, Graham and Harvey (2001) underline that stock prices fall in firms with overly aggressive leverage.

The dividend policy of a firm documents the distribution of its earnings as dividends to shareholders and how much will be retained for reinvestment for future growth. The dividend payout ratio of a firm is a mirror of a firm's dividend policy. The impact of the dividend payout ratio on the share price of banking and finance companies is also studied in this thesis. The empirical evidence suggests that there is no consensus among researchers on the impact of dividend policy on firms. According to Raza et al. (2018), a review of existing literature found three different approaches or schools regarding the impact of dividend policy on the share price. The first school of thought is that a rise in dividend payout will increase the firm's value (share price). The second school of thought holds that an increase in dividend payout will reduce the firm's value (share price), and the third supports that firm value or share price is not affected by dividend policy.

Firm growth is a good indication of firm performance and sustainability. Firm growth is measured by growth in the lending portfolio in the context of this research. By analyzing firm growth in terms of portfolio growth, this paper tries to understand the influence of firm growth

on the firm's value of banks and finance companies. Empirical evidence indicates that growth in loan portfolios increases the firm's value due to the expectation of higher future cash flows. Firm growth also improves investor confidence, positively impacting the share price. According to Sugianto et al. (2022), firm growth does not affect the share price based on the research conducted in Indonesia involving the banking sector. In contrast, Serrasqueiro (2009), concluded that firm growth, as measured by sales growth, has a positive impact on firm value. Credit quality is critical in sustaining industry growth, financial performance, and investor confidence. CBSL's industry data reveals that the sector's credit quality was deteriorating during the period under investigation in this study. It is a significant risk to industry. The non-performing loan ratio is used to evaluate the credit quality of the banking and finance firms. Credit risk can increase owing to failure to pay loan installments on due dates by clients. If we refer to the available literature on the impact of non-performing loans on firm value, Sugianto et al. (2022), states that banking NPL significantly impacts a firm's value.

Customer deposits can be identified as the primary source of financing in the banking and finance sector. Therefore, maintaining a strong capital base against lending and other risky assets is crucial for the sector's progress while preserving stakeholder confidence. Capital Adequacy Ratio/CAR is a major fundamental financial ratio, reflecting the strength and stability of banks and financial institutions. It is the ratio of a bank's capital to its risk-weighted assets. CBSL prescribes minimum thresholds for CAR to ensure stability in the banking system and safeguard depositors. Since the stability and performance of banks are highly sensitive to financial markets, CAR may shape investor perception and, thereby, the share prices of banks and other financial institutions. According to Sugianto et al. (2022), the capital adequacy ratios do not have an impact on the value of banking firms.

The Net Asset Value (NAV) represents the net equity per share where the value of a company's assets is minus liabilities, divided by the number of outstanding shares. This is an essential financial ratio since it approximates each share's intrinsic value and provides a precise measure of the firm's financial health and assets carried out. Changes in the market value of. various bank assets, such as investments, loans, and other monetary instruments, can impact changes in NAV per share. As a key determinant of investor sentiment, NAV per share might shape market perceptions that drive stock prices. A higher NAVPS generally indicates a more financially stable company, which can positively influence share prices (Trueman, 1986; Ohlson, 1995). However, NAVPS alone may not fully capture the market's perception of a company's future growth prospects, which are also crucial for share valuation.

As per the extant evidence, several micro and macro factors influence the share prices of listed companies in Sri Lanka. At the company level, financial performance metrics are considered amongst the most salient determinants of equity valuation and pricing of Sri Lankan firms (Kengatharan & Ford, 2021). Fundamentals such as earnings per share, return on equity, and return on assets provide link into a company's profitability, operational efficiency, and financial health. EPS signals earnings potential and calculates the share of net profit attributable to each outstanding share ROE measures how effectively shareholder capital is used to generate returns. Meanwhile, ROA shows how effectively a company's assets are utilized to produce profits. These metrics directly impact investor perceptions of a company's attractiveness and prospects, reflected in share valuations. Besides fundamentals, share prices fluctuate in response to prevailing economic conditions, stock market dynamics, regulatory changes, and investor risk appetite (Nisa & Nishat, 2011). For instance, more substantial GDP growth and corporate earnings tend to lift market confidence and increase share prices.

Methodology

This section elaborates on the methodology adopted to study the influence of company fundamentals on the share price of financial firms in Sri Lanka. Thus, the section explains sample design, data collection techniques, and the proposed econometric models.

Population and Sample

The research covers a well-defined population of all licensed banks and finance companies listed on the Main Board of the Colombo Stock Exchange (CSE) over a seven-year period from 2014 to 2020. According to the most recent data available, CSE data saw a total of ten licensed commercial banks and thirty-four licensed financial companies listed on the main board. This is noteworthy because this underlines the significant presence of finance companies and the banking sector within the broader market landscape. At the same time, finance companies and the banking sector accounted for 4% of the total market capitalization as of the same period, signaling latent growth potential and, subsequently, their dynamic role in shaping the action of the market (CSE, 2023). Thus, the industry is very interesting for a detailed analysis, in particular for research on how company fundamentals impact share prices.

The sample consists of ten listed commercial banks and twenty-three finance companies. They were selected based on information availability and the existence of the companies during the period under consideration. A selective non-probability sampling method was employed to identify the most relevant finance companies for this study. This approach was chosen because it focuses on cases rich in information directly pertinent to the research objectives. Accordingly, the sample excluded some finance companies based on certain criteria: listing after the year 2020, suspension of operations by the Central Bank, missing data for intended variables, and data access issues following the amalgamation of some finance companies.

Variable Definitions and Measurements

In the context of this research, the variables were meticulously defined and operationalized to ensure clarity and precision in the analysis. Share price is the dependent variable of the study, and the independent variables are company fundamentals, which include earnings per share, dividend payout, net asset value per share, return on assets, return on equity, firm growth, debt-to-equity ratio, non-performing loan ratio, and capital adequacy ratio. Accordingly, the independent variables reflect company performance, profitability, and financial position. These selected firm-specific variables are freely accessible to everyone, which satisfies the basic criteria of the Efficient Market Hypothesis, where market efficiency depends on the extent to which information is available. Supporting the Dividend Discount Model, we selected the dividend payout ratio, arguing that dividend payments and their growth potential determine the value of stock, thereby affecting investors' sentiment. As per signaling theory, increases in profitability and earnings signal positive prospects, thereby increasing share prices (Brigham & Houston, 2007). We selected these profitability measures because they may benchmark the expected rate of return for investors in the Capital Asset Pricing Model. According to trade-off theory, higher debt levels beyond the optimal point can negatively affect share prices (Brigham & Houston, 2007). Control variables comprise firm size, public holding, and firm age, which may potentially influence share price. Firm size and firm age could determine ways of maximizing the shareholder's wealth. Mature and large firms may tend to distribute regular dividends as well as higher-growing dividends compared to young and small firms. Such dividend payments support share valuation in the Dividend Discount Model. The equity stake held by the public is another control variable, which aligns with the Efficient Market Hypothesis. Increased public holding and access to the same set of information by the public

are supposed to enhance market liquidity, resulting in market efficiency. Measures of these variables are presented in Table 2.

Table 2: Measurements of Variables

Variable	Measure
Dependent Variable	
Share Price	The market price of a share
Independent Variables	
Earnings per share	Net income is scaled by average outstanding shares
Dividend-payout	Dividend per share is scaled by earning per share
Net assets value per share	Net assets is scaled by average outstanding shares
Return on assets	Profit after tax is scaled by average total assets
Return on equity	Net income is scaled by average shareholders' equity
Firm growth	(Loan portfolio Y_1 – Loan portfolio Y_0)/ Loan portfolio Y_0
Debt to equity	Debt is scaled by equity
Non-performing loan ratio	Non-performing loans is scaled by total loans
Capital adequacy ratio	(Tier 1 capital + Tier 2 capital)/ Risk-weighted assets
Control Variables	
Public holding	Shares held by public investors, excluding insiders and promoters
Firm age	Log of number of years since incorporation
Firm size	Log of total assets

Data Collection

Secondary data were collected by extracting information from the annual reports of the sample companies. The annual reports were obtained by accessing the official websites of the respective companies, as well as the website of the CSE. The financial statement data were extracted and organized in a panel data format for the period spanning 2014 to 2020. The necessary ratios were computed thereon.

Data analysis methods

A group of statistical techniques were utilized to analyze the panel data, ensuring a comprehensive understanding of the relationships between the share price and fundamentals variables of the study. Accordingly, a descriptive analysis was undertaken to explore nature and distribution of the data. To address the first research question, Pearson's correlation analysis was undertaken to examine the possible relationships among variables. Panel regression analysis was implemented to introduce different model specifications in order to address the second and third research questions of the study. The general panel regression model employed is as follows:

$$\ln(\text{price}) = \beta_0 + \beta_1 \text{EPS}_{it} + \beta_2 \text{DPR}_{it} + \beta_3 \text{NAVPS}_{it} + \beta_4 \text{ROA}_{it} + \beta_5 \text{ROE}_{it} + \beta_6 \text{GROWTH}_{it} + \beta_7 \text{DE}_{it} + \beta_8 \text{NPL}_{it} + \beta_9 \text{CAR}_{it} + \beta_{10} \text{PH}_{it} + \beta_{11} \ln(\text{Age})_{it} + \beta_{12} \ln(\text{Size})_{it} + \text{year dummy} + \text{sector dummy} + u_{it}$$

Findings and Discussion

This section covers the research outcomes and key takeaways based on data analysis. Such outcomes are primarily generated through descriptive and correlation analyses. Regression analysis is used to test the hypotheses.

Descriptive Analysis

Table 3 presents the descriptive statistics of the company fundamentals and share price.

Table 3: Descriptive Analysis

Variables	Obs.	Mean	S.D.	Minimum	Maximum
Earnings per share	231	16.170	32.020	-23.970	224.000
Dividend Payout Ratio	231	0.181	0.213	0.000	1.774
Net Assets Value per Share	231	159.540	459.850	-1.100	2960.000
Return on Assets	231	0.015	0.028	-0.161	0.108
Return on Equity	231	0.110	0.197	-1.707	0.526
Firm Growth	231	0.192	0.343	-0.387	3.337
Debt to Equity	231	6.776	4.353	-29.324	19.366
NPL Ratio	231	0.059	0.046	0.009	0.343
Capital Adequacy Ratio	231	0.166	0.132	-0.068	1.488
Public Holding	231	0.342	0.254	0.001	0.998
Firm Age	231	32.000	16.000	5.000	64.000
Firm Size	231	151295.50	262565.90	1022.00	1408941.00
Share Price	231	139.950	413.720	0.600	2580.300

The average earnings per share is Rs.16.17 for the period considered, with a considerable deviation from the mean. On average, the dividend payout ratio of the banking and finance sector is 18.13%, with a significant deviation from its mean. Some companies did not declare dividends during the period under consideration, while others paid higher dividends, resulting in an exceptionally high dividend payout ratio. Net asset value (NAV) per share deviates significantly among the companies, with an average of Rs.159.54 per share and a wide range of values from negative to as high as Rs. 2,960. This is expected, as the size of the Bank of Sri Lanka is larger than that of the finance companies. On average, the return on assets (ROA) for the banking and finance sector is 1.457%, with a range from negative returns to a maximum of 10.77%. Banking and finance companies have maintained a moderate 10.95% return on equity during this period. The return on equity (ROE) shows a variance of 19.68%, ranging from negative returns to an exceptionally high 52.55%. The average firm growth rate, measured by companies' loan portfolio growth, is 19.16% and can be considered a significant achievement for the industry.

However, there is substantial variation, ranging from negative growth to exceptionally high growth of over 300% in some companies. The average debt-to-equity ratio is 6.7 times in the industry, with a wide range of values from negative ratios to very high leverage. On average, non-performing loans of banking and finance sector is 5.87% during the period. The variance across the companies is 4.41%, with 0.89% and 34.27% as the minimum and maximum NPL ratios, respectively. Banking and finance companies should maintain the minimum capital adequacy ratio given by the Central Bank of Sri Lanka, the regulator of banking and finance companies. Accordingly, the average capital adequacy ratio of the sector is 16.61%, with a variance of 13.19%

Companies that hold a negative capital base report a negative capital adequacy ratio. On average, the public holds 34.23% of these companies' shares during the period under consideration. However, notably, the public holding of some companies is 99.77%, with a variance of 25.36%,

representing a minimum holding of 0.14%. Interestingly, the average firm age in the industry is 32 years, with considerable variability between relatively young and well-established firms. Firm size was measured by the total lending portfolio. Accordingly, the average firm size is Rs. 151,296 million, with a wide range of sizes from relatively small to very large companies. Share price is the independent variable of this study. The mean share price is Rs.139.95, with Rs. 413.72 representing substantial variability, ranging from a very low to a relatively high share price.

Correlation Analysis

The primary objective of this study is to examine the relationship between selected company fundamentals and the share price of banking and finance companies listed on the CSE. Accordingly, correlation analysis was performed, and the results of the Pearson correlation coefficient between independent and dependent variables are summarized in Table 4.

Table 4: Correlation Analysis

	1	2	3	4	5	6	7	8	9	10	11	12	13
EPS	1.000												
DPR	0.062	1.000											
NAVPS	0.866	-0.032	1.000										
ROA	0.181	0.248	0.038	1.000									
ROE	0.146	0.195	-0.004	0.641	1.000								
GROWTH	0.056	-0.026	-0.026	0.243	0.197	1.000							
DE	-0.029	-0.002	-0.100	-0.017	0.395	-0.001	1.000						
NPL	-0.132	-0.285	-0.009	-0.470	-0.426	-0.176	-0.106	1.000					
CAR	-0.005	-0.007	-0.005	-0.117	-0.039	-0.066	-0.412	0.019	1.000				
PH	0.041	0.417	-0.049	0.027	0.052	-0.057	0.272	-0.245	-0.128	1.000			
AGE	0.415	0.145	0.343	-0.026	0.046	-0.090	-0.062	-0.031	0.113	0.286	1.000		
Size	0.093	0.354	0.008	0.034	0.118	-0.051	0.260	-0.249	-0.166	0.723	0.234	1.000	
Share Price	0.837	-0.025	0.974	0.043	0.007	0.020	-0.101	-0.021	0.007	-0.086	0.319	0.012	1.000

Based on the correlation coefficients, earnings per share (EPS) and net asset value per share (NAVPS) indicate a strong positive relationship with the share price of banking and finance companies. Although there appears to be a positive relationship between share price and return on assets, return on equity, firm growth, capital adequacy ratio, and firm size, such a relationship is not strong. The negative relationship between share price and dividend payout ratio, debt-to-equity ratio, and non-performing loan (NPL) ratio is insignificant. Most interestingly, a negative relationship is observed for the dividend payout ratio, although it is expected to increase the share price upon dividend declaration. Considering net asset value per share (NAVPS) and earnings per share (EPS), the correlation coefficient is 0.866, indicating strong multicollinearity. A similar relationship can be observed between public holding and firm size. Further, there is moderate multicollinearity between return on equity and return on assets.

Regression Analysis

Regression analysis employed different regression models, including pooled regression, random-effects models, fixed-effects models, and clustered standard errors. Table 5 summarizes the results of pooled regression, fixed-effects (FE), random-effects (RE), and clustered regression models. In the following sections, each model is discussed in line with the research objectives.

Table 5: Regression Analysis

	Dependent Variable: Log (Price)			
	(1)	(2)	(3)	(4)
Earnings per share	0.0149***	0.00001	0.00003	0.00003
	(0.004)	(0.001)	(0.001)	(0.001)
Dividend Payout Ratio	0.957***	0.0893	0.077	0.077
	(0.343)	(0.183)	(0.174)	(0.123)
Net Assets Value per Share	0.0007***	0.0008***	0.0002	0.0002
	(0.000)	(0.000)	(0.000)	(0.000)
Return on Assets	-1.983	-1.868	-1.322	-1.322
	(3.427)	(1.652)	(1.575)	(1.591)
Return on Equity	0.329	0.143	0.112	0.112
	(0.533)	(0.241)	(0.227)	(0.349)
Firm Growth	0.340*	0.105	0.060	0.060
	(0.188)	(0.080)	(0.075)	(0.082)
Debt to Equity	0.001	-0.026***	-0.026***	-0.026*
	(0.020)	(0.010)	(0.009)	(0.014)
NPL Ratio	-5.387***	0.821	1.868*	1.869
	(1.648)	(1.083)	(1.042)	(1.829)
Capital Adequacy Ratio	0.085	0.094	-0.007	-0.007
	(0.605)	(0.318)	(0.301)	(0.227)
Public Holding	0.423	-0.010	-0.031	-0.031
	(0.372)	(0.381)	(0.379)	(0.679)
Firm Age	0.792***	0.596**	-0.558	-0.558
	(0.117)	(0.233)	(0.379)	(0.818)
Firm size	0.090	0.222***	0.224**	0.224**
	(0.061)	(0.081)	(0.090)	(0.100)
Year (dummy)	-	yes	yes	yes
Sector (dummy)	-	yes	yes	yes
Pooled	yes	no	no	no
Random-effect	no	yes	no	no
Fixed-effect	no	no	yes	no
Clustered S.E.	no	no	no	yes
R-squared	0.670	0.196	0.247	0.247
Prob > F	0.0000	0.0000	0.0000	0.0000
Groups	-	33	33	33
Observations	231	231	231	231

Note: Standard errors are given in parentheses. ***, **, and * Statistical significances based on a t-statistic at the 1%, 5%, and 10% levels, respectively.

The pooled regression model does not capture the firm-wise variation of data. It nearly accounts for 67% variability of share price by firms' fundamentals in the banking and finance sector. RE models suggest that there is a significant positive relationship between share price and NAVPS, firm age, and firm size. Also, debt-to-equity ratio has a strong negative relationship with share prices. Accordingly, higher NAVPS is associated with a higher share price, while older and larger firms in the industry experience a positive impact on their share price. A strong negative relationship indicates that investor sentiment for highly leveraged firms negatively affects the share price. However, the RE model does not suggest that earnings per share, dividend payout ratio, firm growth, and NPL ratio are major determinants of the share price of banking and finance companies, even though those variables were significant under the pooled data analysis. Firm size and debt-to-equity ratio were insignificant under the pooled method, but they show a strong relationship with share price under the RE model.

Further, results of the RE model analysis suggest that approximately 19.58% of the price variability of individual banking and finance companies over time is accounted for by company fundamentals. Considering the R-squared values, firm-specific factors account for 59.34% of the variability in share price among the companies selected in this study. This means the independent variables explain 59.34% of the variability in share price among the companies. The "Chi-square (χ2) statistic" generated by the model is 84.77, and it assesses the overall significance of the regression model. Considering its lower p-value, the overall model is statistically significant.

Notably, the FE model suggests that only the debt-to-equity ratio and firm size strongly impact the share price of banking and finance companies. The debt-to-equity ratio maintains a negative relationship, similar to the RE model. Firm size indicates a positive relationship; a similarly strong relationship was revealed under the RE model. Conversely, there is a negative relationship between share price and firm age, even though other models indicate a strong positive relationship. However, that negative relationship is not statistically significant. Net asset value per share (NAVPS) was a major determinant of share price under both the pooled and RE models. The observed positive relationship is not significant under the FE model. All other variables, including EPS, DPR, NAVPS, ROA, ROE, firm growth, NPL ratio, public holding, and firm age, are statistically insignificant in explaining their relationship with share price. The overall R-squared value stands at 0.0038, which indicates that the study's variables have very low explanatory power over share price. However, the overall FE model is statistically significant, indicating that variables collectively and significantly affect the share price.

Hausman Test

In the previous section, the results were separately discussed for pooled, RE, and FE models. In order to select the most appropriate model, the Hausman test is implemented to choose either the RE model or the FE model. The Hausman test evaluates the key assumptions of both models and determines whether individual-specific factors affect the independent variables. If the test result shows that individual-specific factors are correlated with the independent variable, the FE model is appropriate. If the test results indicate the opposite, the RE model is selected for the data analysis.

To decide the appropriate regression analysis method for achieving the objectives of this research, the Hausman test was carried out based on the FE and RE analyses discussed in the prior section. The null hypothesis (H0) revealed that the random-effects model was appropriate, while the alternative hypothesis (H1) proposed the fixed-effects model. The generated p-value

(0.0842) is greater than 0.05, and the random-effects model is therefore considered the most appropriate. Hence, the random effects model effectively explains changes in share prices based on firms' fundamentals. Accordingly, NAVPS and debt-to-equity are statistically significant in explaining variations in share prices. Nevertheless, the FE model also appears statistically significant at the 10% level, capturing firm-wise variation in the data effectively. Accordingly, the debt-to-equity ratio and the non-performing loan ratio are identified as statistically significant fundamentals.

Discussion of Results

The empirical finding reveals a positive relationship aligned with the theoreticalexplanations that higher earnings of companies attract investors, leading to an increase in the market price of shares. However, earnings per share is not a significant determinant of the market price of shares of banking and finance companies, as evidenced by its low significance level. However, according to Menike and Prabath (2014), earnings per share have a significant positive impact on the market price of shares, based on a study involving 100 companies listed on the CSE that retrieved financial data from 2008 to 2012. According to Islam et al. (2014), share prices of companies do not always move in line with growth in earnings per share, and it was further noted that share price increases or decreases depend on micro- and macroeconomic factors. This finding aligns with the outcome of the analysis, and deteriorating macroeconomic factors in the Sri Lankan context may have a greater impact on investor sentiment. Further, studies conducted by Sukhija (2016) revealed that earnings per share is insignificant in determining the market price of shares of banking and finance companies.

The positive relationship revealed by this research finding shows that a higher dividend payout ratio could be perceived positively by investors in their investment decisions. However, lower statistical significance suggests that the impact of the dividend payoutratio does not influence the market price of shares alone. Investors interested in banking and finance may prefer long-term company growth over short-term gains. This can be one reason for this weak relationship. However, previous studies have also indicated mixed relationships between the dividend payout ratio and share price. According to Sukhija (2016), the dividend payout ratio shows an insignificant positive relationship with the market price of banking and finance companies, which aligns with the observation. However, the same research revealed that the dividend per share strongly impacts the market price of the share, suggesting investors are more concerned about the dividend yield than the dividend payout ratio. However, Sondakh (2019) revealed that the dividend payout ratio negatively and significantly affects firm value, based on a study of financial service sector industries listed on the Indonesian stock market.

Net asset value per share (NAVPS) indicates the book value of an equity share based on the net assets reported in the company's balance sheet. Theoretically, a higher NAVPS should increase theshare price. This relationship is evident in the empirical study's results, but its impact on the market price of equity shares is insignificant. However,NAVPS is highly used when determining whether the share price is over or undervalued, especially in the banking and finance sector. This weak relationship was confirmed by Menike and Prabath (2014). However, a strong positive relationship was confirmed by Malkawi, Alshiab, and Pillai (2018), and Sarifudeen (2016), leading to mixed conclusions regarding the impact on the market price of shares.

Return on Assets and Return on Equity are reasonable measures of the financial performance of companies. Higher ratios give investors a positive sentiment regarding the earning capacity and efficiency of the company's asset utilization, generating higher returns on investments.

Conversely, ROA shows a negative relationship with the market price of shares of banking and finance companies. Regarding ROE, the model revealed a positive relationship, aligning with the theoretical explanation. However, in terms of significance, neither variable significantly affects the market price of shares. This negative relationship between ROA and share price confirms that further research should be done by including other macro and microeconomic factors in the model. The study conducted by Nazar (2020) on material sector companies in Sri Lanka revealed an insignificant negative relationship with ROA, consistent with the results of the current study. According to Bintara et al. (2019), return on assets positively affects stock price. Based on the survey conducted on the Indonesian manufacturing companies, Tahu (2017) found that stock prices strongly respond positively to ROE, although the findings in this study indicate a weak positive relationship.

Another variable is firm growth, which is measured by the increase in the companies' credit portfolios over the years. The positive relationship aligns with the theoretical explanation, as investors are willing to invest in growing companies for higher financial returns. The weak relationship indicates that firm growth alone is not a decisive factor in investment decision-making during the period under consideration. This suggests that economic conditions between 2014 and 2020 or market perceptions had a greater influence on the market price of shares. If we consider the results of other research, Fajaria and Isnalita (2018) revealed that firm value increases when companies maintain higher growth and profitability. However, according to Sukhija (2016), firm growth is negatively correlated with the share price.

The banking and finance companies mainly borrow and provide lending as their core business. This is primarily recognized as a transfer of funds from excess holders to needy people. However, customer deposits are the primary source of funds for banking and finance companies. However, customer deposit was not considered for the debt-to-equity ratio. Based on empirical findings, the significant negative relationship confirms that higher leverage increases financial risk, negatively impacting the share price. That indicates that investors are highly concerned about the higher leverage of banking and finance companies when making investment decisions. Samarkoon (1997) however shows that leverage is not related to the average return of the equity. Further studies by Fajaria & Isnalita (2018) reveal that leverage causes lower firm value. However, based on the study of Tahu (2017), although leverage negatively affectsfirm value, the impact is insignificant.

The asset quality of banking and finance companies deteriorated during the research period as measured by the non-performing loan ratio. This significantly impacts on the firm's profitability, as it leads to higher provisions for bad debts and write-offs. Conversely, regression results revealed a positive relationship betweenthe NPL ratio and the market prices of shares of banking and finance companies. However, this positive relationship is not statistically significant. This relationship was further analyzed separately for banking and finance companies using the Fixed Effects model with clustered standard errors. The results indicated that the NPL ratio negatively affects the market price of banking shares (coefficient: -0.9485) and positively affects the share price of finance companies (coefficient: 1.8119). However, the relationship is not statistically significant, as the p-values exceed the 0.05 significance level 0.727 for the banking sector and 0.380 for the finance sector.

The relationship between share price and non-performing loans holds utmost importance in financial analysis. Indeed, the regression analysis indicates a weak positive correlation between the share price and the NPL ratio. Thus, this finding is inconsistent with the prevailing beliefs regarding the effects of asset quality and profitability on share prices. Ordinarily, a high NPL

ratio indicates poor asset quality and elevated credit risk, which should adversely affect a firm's profitability and share price (Sharpe, 1964).

A key indicator of banking and finance companies is the NPL ratio, which defines their financial health. It shows the level of non-performing credit, defined as the number of credit facilities assessed as non-performing and in arrears against the total number of credit facilities. These measures signify higher levels of risk and poor quality of assets and negatively influence the share price of the enterprise since they affect the confidence of other investors (Samarakoon, 1996). This fact is covered in the literature; for instance, Beaver et al. (1980) made significant attempts at explaining this by proposing that high levels of NPL ratios may depress share prices. However, the regression results of this study show a positive relationship between share price and NPL ratio, although it was not statistically significant. This finding contradicts the previous theoretical evidence that has postulated a negative relationship between share price and NPL ratio. A weak and counter-intuitive correlation might be that other factors affecting share prices weaken the direct link between NPL ratios. As such, it could also point to the fact that other investors might have expected high levels of NPLs and, thus, factored in the high valuations, or there could be sector- or market-related issues. The results are dissimilar from the existing literature, which observed a strong effect of NPL ratios on share prices, for example, Perera and Morawakage (2016).

The significance of capital adequacy enhances the general findings on the stock prices of banking and finance firms, as exemplified by the coefficient value of minus, a numerical figure of approximately -0.0067, which indicates a negative flow. Nonetheless, the results suggest a poor relationship, whereby the p-value is high at 0. 977. The CAR is calculated as a percentage of total risk-weight assets and represents the ratio of Tier I and Tier II capital deposited within a specific bank (Blume, 1980). Regulators set a minimum CAR that shows a bank's ability to cope with losses when facing a distress situation. Higher CAR means that a bank can easily meet its obligations and recover for any losses it is likely to incur; thus, it should support financial stability and investor confidence (Beaver et al., 1980).

However, according to the results of this study, the increase in CAR might not have a powerful impact on the future share price. One explanation could be that even though a high CAR is good for stability, it may also mean that the banks have more capital than necessary, which could mean lower returns for shareholders to the extended meaning of this over-capitalization (Barberis & Thaler, 2002). These two things present a trade-off and might result in a neutral or negative attitude toward the fluctuation of share prices by investors. Specifically, prior literature examined by Perera and Morawaka. (2016), observed research findings that CAR substantially influenced share price. The lingering difference depicted in the current study entails that other factors might have ensued, affecting the correlation between CAR and share prices in the current market environment. This underscores the factors that make using financial metrics difficult and clarifies that the same metrics can produce different results regarding investor reactions and market forces.

In overall, regardless of the sector, a positive market reaction is observed for earnings per share, net asset value per share, and dividend per share while it is negative for debt-to-equity ratio and NPL ratio. Typically, stability of financial firms is measured by asset quality, capital adequacy, liquidity, and profitability. In response to shareholders' wealth maximization, stock prices positively react to earnings per share and net asset value for share, but such reaction is silent for traditional profitability measures such as ROA and ROE. As a measurement of asset quality, non-performing loan ratio is negatively related to stock prices, and representing capital

adequacy, debt to equity ratio also shows a negative influence. Mature firms as well as large firms seem to be generating higher stock returns than their respective counterparts. Mostly identical results are reported in the sector-wise comparison, but the response is overlooking for the banking sector where especially, market reaction is positive for the return generated for the shareholders' wealth.

Robustness Analysis

Sector-wise Analysis

In this section, we analyze the banking and finance sectors separately to check the robustness of our overall findings. Analysis of robustness is one of those decisive stages of empirical research that helps build confidence that our conclusions are valid not only under certain conditions but also across different scenarios. We will examine the stability and reliability of the relationships identified between company fundamentals and share prices by comparing the results from the overall analysis with the sector-specific analyses.

This robustness check has been conducted to compare overall findings with the findings of individual sectors to examine the impact of the sector on the market price of shares. The results are summarized in Table 6. Accordingly, banking and finance sectors show different patterns among the firm-specific variables with their share prices. A comparison of the overall analysis with the sector-specific ones indicates that variables including NAVPS, ROA, and ROE show impacts unique to sectors, especially the banking sector.

Table 6: Regression Analysis (Sector-wise) - Clustered Standard Errors

	Dependent Variable: Log (Price)		
	Banking and Finance	Banking	Finance
Earnings per share	0.000	-0.001	-0.0007
	(0.001)	(0.005)	(0.001)
Dividend Payout Ratio	0.077	-0.052	0.072
	(0.123)	(0.153)	(0.352)
Net Assets Value per Share	0.000	0.006 ***	0.000
	(0.000)	(0.001)	(0.000)
Return on Assets	-1.322	-19.18 **	-0.920
	(1.591)	(7.530)	(1.784)
Return on Equity	0.112	3.164 ***	0.187
	(0.349)	(0.841)	(0.368)
Firm Growth	0.060	0.163	0.053
	(0.082)	(0.174)	(0.088)
Debt to Equity	-0.026*	-0.001	-0.029*
	(0.014)	(0.024)	(0.016)
NPL Ratio	1.869	-0.948	1.811
	(1.829)	(2.629)	(2.021)
Capital Adequacy Ratio	-0.007	0.294	-0.005
	(0.227)	(1.052)	(0.322)
Public Holding	-0.031	-0.503 **	0.416

	(0.679)	(0.193)	(1.575)
Firm Age	-0.558	0.640	-0.360
	(0.818)	(0.599)	(1.111)
Firm size	0.224**	-0.449	0.240**
	(0.100)	(0.286)	(0.116)
Year (dummy)	yes	yes	yes
Sector (dummy)	yes	yes	yes
R-squared	0.247	0.864	0.212
Prob > F	0.0000	0.0000	0.0000
Groups	33	10	23
Observations	231	70	161

Standard errors are given in parentheses. ***, **, and * Statistical significances based on a t-statistic at the 1%, 5%, and 10% respectively.

Interaction Effects

In this section, interaction effects are analyzed using fixed-effects regression with standard errors adjusted for clusters. This will establish whether the interaction amongst the key variables is strong enough to impact the dependent variable, the share price, and check for consistency in the association for various scenarios. Table 7 reports the results of the fixed-effect regression model adjusted for cluster standard errors. The test results, such as coefficients, standard errors, and p-values for each interaction, indicate the statistical significance of the relationship with the share prices of the banking and finance sector.

Table 7: Multiple Regressions (Interactions)

Dependent Variable: Log (Price)				
Interaction	Coefficient	Standard Error	t-Statistic	P-Value
EPS * AGE	-0.048	0.012	-3.930	0.000
EPS * SIZE	0.003	0.001	2.320	0.027
AGE * ROE	-1.182	0.446	-2.650	0.012
ROA * NPL	-49.970	10.020	-4.990	0.000
PH * CAR	-6.804	3.260	-2.090	0.045
SIZE * ROE	0.508	0.196	2.590	0.014
SIZE * NPL	-1.898	0.597	-3.180	0.003
CAR * NPL	12.692	3.628	3.500	0.001
DE * NPL	-0.512	0.190	-2.680	0.011

Results establish how other firm-specific characteristics moderate the relationships between the key financial metrics and share prices. The interaction between Firm Age and EPS negatively affects share prices at a statistically significant level, indicating that as firms age, the positive effect of EPS on share prices lessens. This shows that the more aged a firm gets with higher earnings per share, the less likely these earnings will translate into higher share prices than younger firms. The above relationship can be realistic due to slower firm growth, shifting investor expectations towards younger firms, mature firms' focus on dividend payout and stable earnings, increased competition, regulatory constraints on diversifications, and the stage of the firm's life cycle, etc. Further, the country's economic status could impact this interaction effect.

The interaction effect between EPS and firm size has a positive and statistically significant influence on share prices. This suggests that investors view the earnings of larger firms more favorably, likely due to their established market presence, financial stability, and perceived lower risk. As a result, higher investor confidence and sentiment reflect positively on the share price.

The interaction effect between AGE and ROE has a negative and statistically significant influence on share price. In our previous analysis, age as an independent variable had a negative impact on share price & it was not statistically significant. However, that negative impact becomes more substantial/more significant as ROE increases in matured companies. This suggests that an increase in ROE does not mitigate the negative effect of age on the share price. Even that negative impact becomes more prominent.

The interaction between ROA and NPL significantly impacts share price. This suggests that high non-performing loans supersede any positive impact of strong ROA, leading to a negative effect on the share price of banking and finance companies. The interaction effect of public holding and capital adequacy ratio has a statistically significant negative impact on the share price. That indicates that the share price tends to decrease when the interaction between two variables increases. In other words, firms with higher public holding and capital adequacy ratios might experience a negative impact on the share price.

The interaction between size and return on equity has a statistically significant positive impact on the share price. The positive interactions between the two variables align with investor behavior and financial theory. The moderating effect of firm size and non-performing loan ratio on the share price is statistically significant and negative. Share Prices of larger firms with higher NPL ratios tend to decrease. This is a realistic relationship, as the rising NPL may harm the stability of the larger firms.

There is a statistically positive relationship between share price and the interaction effect of capital adequacy ratio and NPL. It appears that the impact of rising NPL is mitigated by a firm's higher capital buffer. The statistically strong negative relationship indicates that as debt to equity and non-performing ratio rise, the share price of those companies decreases due to higher leverage and bad credit quality.

Conclusions

This study aims to investigate the factors that affect the market price of shares of Banking and Finance companies listed on the CSE. The following conclusions can be reached regarding the main objectives of the study based on the data analysis.

EPS positively affects share price; however, the analysis revealed that EPS does not significantly influence share prices. This establishes that EPS has a less comparative impact than other factors on the share prices of the banking and finance companies listed on the CSE, which the research findings on similar studies also support. The impact on the banking and finance sectors separately is negative and insignificant. The analysis establishes a weak positive relationship between DPR and share prices, suggesting that dividend payouts are not a major factor considered by investors for investment decisions in this sector. In contrast, a weaker negative relationship for the banking sector shares was observed.

Although a positive relationship was observed for Net assets value per share, it was not strong. While NAVPS can sometimes be used to assess whether shares are overvalued or undervalued,

it appears to have a minimal influence on share prices at the sector level or within finance sector. In contrast, a strong positive relationship between share price and NAVPS was observed in the banking sector. The results showed a negative relationship between ROA and share prices, indicating that an increase in ROA is not associated with a higher share price in this industry. In the banking sector, this negative relationship was stronger and had a significant impact on share prices. During the period under review, banks had maintained ROA levels below 2%, which heavily influenced the performance of their shares. ROE showed a moderate positive relationship with share prices, although the effect was statistically insignificant. This finding suggests that ROE does not play a significant role in determining share prices overall. However, in the banking sector, the positive relationship between ROE and share prices was notably stronger.

The analysis revealed a weak positive relationship between firm growth and share prices, indicating that firm growth does not significantly influence share prices. Similar results were observed across all sectors individually. The debt-to-equity ratio had a significant negative effect on share prices, suggesting that higher financial leverage increases risk and leads to lower share prices. However, in the banking sector, this negative relationship was relatively weak.

While the NPL ratio showed a positive relationship with share prices, the relationship was statistically insignificant. This suggests that the slight increase in share prices associated with higher NPL ratios is not meaningful. Typically, higher NPL ratios indicate lower asset quality, which negatively impacts share prices. In contrast, the relationship between the NPL ratio and share prices in the banking sector was negative, although weak. CAR had a negative, though insignificant, effect on share prices, indicating that it does not significantly influence share prices in this sector. In contrast, a weak positive relationship between CAR and share prices was observed in the banking sector compared to the overall sector and the finance sector.

The empirical analysis presented in this paper contributes to understanding the banking and finance markets by establishing that most of the hypothesized relationships between the firm-specific factors and share prices are insignificant. This could be due to some market imperfections, weak investor sentiment toward the sector, and some overall economic factors in the Sri Lankan market during the study period. A high debt-to-equity ratio indicates that a company is heavily financed by debt, which can be perceived as risky by investors. This perception often leads to a decrease in share prices, as investors may fear potential insolvency or financial instability. Therefore, companies strive to maintain a balanced debt-to-equity ratio to ensure financial health and investor confidence. On the other hand, firm size appeared to affect share price positively and again demonstrated the role of market perception and the firm's stability in investment decisions.

In terms of the remainder of the traditional measures, employing EPS, ROA, and DPR to analyze the predicted impacts through the model, the research reinforces that significant environmental complexities within the banking and financial markets are drivers of the share price. These findings can help formulate propositions for further studies and help investors and policymakers who aim to comprehend and predict the share prices within this sector.

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