Sustainable Business Practices in Banking Sector

Dr. Mukta Mani*

Abstract

The sustainable business practices include incorporating principles of sustainability into each of its business decisions, supplying environment friendly products or services and committing to environmental principles in its business operations. The objective of the study is to examine the role of banking sector in developing the sustainable business practices. The study has been carried out through detailed review of literature and analysis of various research reports on Sustainable business practices. It is found that the Indian banks have realised the need of adopting sustainable business practices, however, they are far behind from their foreign counterparts. The banks need to mainstream sustainability into its core business practices by integrating it into strategy formulation. The banks also need to follow the environmental trends and changes in regulatory framework to assess the possible implications of these changes on their borrowers' overall financial position. They have to develop new products such as ethical funds or loans specifically designed for environmental businesses to capture new market opportunities associated with sustainability. And lastly, the Sustainability Reporting is the key requirement for giving a thrust to the sustainability efforts of the government.

Keywords: Banking, Sustainable Business Practices, Sustainability Reporting

Introduction

The word 'Sustainability' has different meaning to different people. The most popular definition is from the Brundtland Commission Report from United Nations World Commission on Environment and Development –WCED, (1987), which states that sustainable development is "Development that meets the needs of the present without compromising the ability of future generations to meet their own needs." Sustainable business practices are the ways of minimizing negative impact of business on the global or local environment, community, society, or economy. The sustainable business practices include incorporating principles of sustainability into each of its business decisions, supplying environment friendly products or services and committing to environmental principles in its business operations. The 'Triple Bottom Line' (TBL), a term coined by Elkington (1997), implies that corporations should focus "not just on the economic value they add, but also on the environmental and social value they add-and destroy". Lots of efforts are being made by the state and central governments to promote sustainable business practices in the business organisations. Many researchers have focused and studied sustainable business practices in the corporate sector. However, banking sector has not been examined much on this issue. Banking sector is the backbone of economy. Commercial banks play a very significant role in the development and growth of economy. In India, banks are highly regulated by the central banking system. Although the banking sector was opened up for private sector and foreign banks during liberalisation, still the public sector banks have the major market share. Thus, the role of public sector banks in the economy can't be ignored. Public sector banks like State Bank of India and Punjab National Bank have a very large network of branches and through their branches they reach to every corner of the country. We can develop a mechanism of promoting sustainable business practices through banking system and use their branch network for dissemination of these practices to every corner of the country. The objective of this study is to examine the role of banking sector in developing the sustainable business practices.

Dr. Mukta Mani*
Department of Humanities and Social Sciences, Jaypee Institute of Information Technology, Noida

Literature Review

Wise and Ali (2009) in their study on corporate governance and corporate social responsibility in commercial banks of Bangladesh, through analysis of the annual reports of these banks, found that the corporate social responsibility disclosures by the banks focus on initiatives undertaken to support two critical sectors within Bangladesh's economy: agriculture and the SME sector. Sharma, Nishi (2011) made an attempt to analyse CSR practices and CSR reporting in India with special reference to banking sector and concluded that banking sector in India is showing interest in integrating sustainability into their business models but its CSR reporting practices are far away from satisfaction. Ventura and Vieira (2007) made a study to understand the dynamics of institutionalizing corporate social responsibility in the field of Banking Organizations in Brazil and found that from being an isolated marginal action, CSR in the past ten years is now a structured action in banking organizations. Narwal (2007) made a study to highlight the CSR initiatives taken by the Indian Banking Industry. The findings suggest that banks have an objective view-point about CSR activities. They are concentrating mainly on education, balanced growth (different strata of society), health, environmental marketing and customer satisfaction as their core CSR activities. Moreover, there are studies focused on development of scales or instrument for measuring the sustainable business activities of the firms. Walter F. Abbott and R. Joseph Monsen (1979) developed a corporate social involvement disclosure scale, based on the analysis of annual reports of the Fortune 500 companies. They have used six areas under analysis as: environment, products, equal opportunities, personnel, community involvement, and other disclosures. Ullman (1985), Addock and Graves (1997) used the Kinder Lydenberg Domini (KLD) rating system, where each company in the S & P 500 is rated on eight attributes namely; employee relation, product, community relation, environment, treatment of women and minorities, nuclear power and military contracts. Zappi (2007) used three attributes employees, customers and environment, for measuring the CSR in Italian banking industry. Sharma, Nishi (2011) has given a list of core thrust areas for reporting CSR activities by the Indian banks as: children welfare, community welfare, education, environment, healthcare, poverty eradication, rural development, vocational training, women's empowerment, and protection to girl child and employment. The rating of the CSR activities of Indian banking sector has also been done by Karmayog, an NGO. As per the report of the Karmayog, (out of 36 banks surveyed, two third banks couldn't even secure a rating of 3 at a scale of 0 to 5) while, only one bank could attain level 5. Bihari et al. (2011), in his research article on the social responsibility of banking sector, concluded that the role of banks in controlling the environmental damage is extremely important. As per relatively indirect nature of their environmental and social impacts, banks need to examine the effects of their lending and investment decisions. Various studies on Green Banking and Sustainable Development concluded that Indian banks need to be made fully aware of the environmental and social guidelines to which banks worldwide are agreeing to. As far as green banking is concerned, Indian banks are far behind their counterparts from developed countries. If Indian banks desire to enter global markets, it is important that they recognize their environmental and social responsibilities. Similar findings have been observed by Khawaspatil and More (2013) in their research article on green banking. They found that in-spite of a lot of opportunity in green banking and RBI notifications, Indian banks are far behind in implementation of green banking. Global Reporting Initiative (GRI), report on 'Sustainability Reporting, Practices and Trends in India 2012', reveals that around 80 companies in key sectors of India, namely, metals and mining, oil and gas and construction sectors are leading adopters of sustainability reporting practices in India. But unfortunately, the financial services sector is still to take on reporting on a large scale. From the above discussion it may be inferred that the commercial banks are fairly involved in CSR initiatives and activities. However, the whole hearted initiatives for development of sustainable business practices are still lacking. There is a need to promote the sustainable business practices through increased initiatives in this direction.

Sustainable Business Practices

This section focuses on the role of commercial banks in sustainable development. The integration of sustainability into the banking sector has taken two key directions. Firstly, to inculcate the sense of environmental and social responsibility in the core banking operations and secondly, to integrate the sustainability into banks' core business environmental and social considerations into product design, policies and strategies. For example, the integration of environmental criteria into lending and investment strategy, and the development of new products that provides environmental businesses with easier access to capital. The sustainable business practices may be divided in the following heads:

(i) Strategic Imperative

It is imperative for the banking sector to mainstream sustainability into its core business practices. Until now, sustainability has been taken as a 'good-to-do' practice. However, in the last few years, global reporting agencies started scrutinizing Indian organisations on the sustainability parameters. Organizations like BankTrack have actively scrutinized Indian banks and are openly calling out potentially environmentally harmful investment decisions under their 'dodgy deals' section. Thus sustainable business practices don't remain good-to-do activities anymore, and they are ready to take driver's seat in framing the business strategies for organisations. There are certain roadblocks in the way of integration of sustainability practices with strategic decisions. The companies lack proper assistance and information for this integration. Some companies take assistance from foreign experts. Moreover, companies find it difficult to justify investments in sustainability initiatives, as the returns are not immediate. Indian companies can learn from their foreign counterparts that have established sustainability taskforces consisting of members from different departments throughout the organisation.

(ii) Lending and Borrowing

Banks face financial risk while granting loans to business. To assess the risk, banks rely on the financial statements of the borrower. Under the current financial reporting system, the environmental liabilities of the borrower remain unreported and thus enhance the risk of lenders. If the borrower is involved in the projects or business which is causing contamination in the environment, the borrower may end up spending extra money on the cleanup of site or may have to pay heavy penalties. Such unforeseen liabilities may impair their ability to service their bank loans. The contamination might also reduce the value of the collateral. Thus prudent lenders must follow the environmental trends and changes in regulatory framework to assess the possible implications of these changes on their clients' overall financial position.

(iii) Products and Operations

The awareness towards environmental and health issues have increased in the last few decades. Many researches are being conducted in this direction. Influenced by these trends, some banks have begun looking closely into their own environmental and social performance. In many cases this effort has resulted in adoption of energy and resource efficiency programs within the institutions themselves. Several international banks have recently adopted innovative and proactive strategies to capture the opportunities associated with sustainability. They have developed new products such as ethical funds or loans specifically designed for environmental businesses to capture new market opportunities associated with sustainability. Operational efficiency through green practices makes an immediate effect on the finances of the organizations. Many international organisations have set their targets for reduction in Green House Gas (GHG) emissions, which directly converts into energy efficiency. It is assumed that a 5% energy efficiency contribute more than USD 10 million in cost savings annually. The most popular ways of increasing energy efficiency are energy efficient buildings.

(iv) Sustainability Reporting

Sustainability reporting is a way for businesses to communicate the impact they have made on their social and physical environment. Government of India has taken many initiatives in the direction of promoting businesses to integrate CSR into their core business operations. The National Voluntary Guidelines on the Social, Environmental and Economic Responsibilities of Business (NVGs) released by 2011 highlight the need to integrate sustainability into core business practices. National

Stock Exchange (NSE) started India's Standard & Poor's (S&P) ESG India Index in 2008. This is the first index of companies in India that measures and ranks 50 NSE listed companies on the basis of performance of the companies on environmental, social and corporate governance (ESG) areas. The Bombay Stock Exchange (BSE) has designed GREENEX, a green index, to assess energy efficiency performance of companies. For the success of indicators like GREENEX and ESG Index, it is mandatory to have quality data available regarding the sustainability practices of businesses. Thus, sustainability reporting is the key requirement for giving a thrust to the sustainability efforts of the government.

(v) Policy Initiatives

India has become world's eleventh largest economy in terms of nominal Gross Domestic Product (GDP). The economic growth in last few decades has brought with it the pressure to raise social and environmental standards. The government has framed many policies and given directives to ensure compliance to the environmental protection norms. The Securities and Exchange Board of India (SEBI) mandated from November 2011, that the 100 largest listed entities must submit Business Responsibility Reports, as a part of their annual reports. This happened after the release of National Voluntary Guidelines on Social, Environmental and Economic Responsibilities of Business in July 2011 by the Ministry of Corporate Affairs, Government of India. The other recent initiatives include the Sustainable Development and Corporate Social Responsibility Guidelines for Central Public Sector Undertakings. The major policy and legislative initiatives are listed below-

1. Environment Impact Assessment (EIA) notified by Ministry of Environment and Forest, for 32 sectors in 1994.
2. In year 2000, SEBI specified principles of Corporate Governance as listing requirement under clause 49.
3. Release of Charter on Corporate Responsibility for Environment Protection by MDEF in 2003.
4. In 2006, Revised EIA notified to include 7 more sectors taking it to 39.
5. Release of National Action Plan on Climate Change (CC) by Prime Minister's Council on CC in June 2008.
6. Release of Voluntary Corporate Social Responsibility Guidelines by Ministry of Corporate Affairs in December 2008.
7. Guidelines on Corporate Social Responsibility for Central Public Sector Enterprises released by Department of Public Enterprises in April 2010.
8. Release of National Voluntary Guidelines on Social, Environmental and Economic Responsibilities of Business by Ministry of Corporate Affairs in July 2011.
9. In November 2011, SEBI Board decided to mandate submission of Business Responsibility Report by top 100 listed companies as per NVG.
10. New Companies Bill tabled in Parliament for discussion in December 2011.

Conclusion

Banks have been assigned a special role in the economic development of the country and the Reserve Bank of India has prescribed that certain percentage of bank lending should be allocated to development sector called the "Priority Sector". The Indian banks have begun to realise their role as multipliers for responsible and sustainable business. The banks have increasingly started to integrate evaluation on sustainability as one of the key inputs to their decision on financing and valuation of projects. Globally, the banking and financial services sector has been setting trends in sustainability reporting and accounts for the largest number of companies from an individual sector that report under sustainability parameters. Since banking companies are the major source of capital for companies, they can exercise a great influence over their clients and investing companies. The clients, in turn, may have a chain of companies and suppliers that are controlled or significantly dependent on them. Thus a higher participation by the banking sector could revolutionize the landscape of sustainable business practices in India.

References

1. Addock, S.A., and Graves, S.B. (1997), "The Corporate Social Performance-Financial Performance Link", *Strategic Management Journal*, 18 (4), 303-319.
2. Bihari, Suresh Chandra and Pradhan, Sudeepta (2011), "CSR and Performance: The Story of Banks in India", *Journal of Transational Management*, 16 (1), 20-35.
3. Elkington, John (1997), *Cannibals with Forks: The Triple Bottom Line of Twenty-First Century Business*, Capstone, Oxford.
4. S.G. Khawaspatil and R.P. More (2013), "Green Banking in India", *Golden Research Thoughts*, 2 (7), 1-4, ISSN:-2231-5063.
5. Narwal, Mahabir. (2007), "CSR Initiatives of Indian Banking Industry", *Social Responsibility Journal*, 3 (4), 49-60.
6. Sharma, Nishi. (2011), "CSR Practices and CSR Reporting In Indian Banking Sector", *International Journal of Advanced Economic and Business Management*, 1 (2), 58-66.
7. Ullmann, A. A. (1985), "Data in Search of a Theory: A Critical Examination of the Relationships among Social Performance, Social Disclosure, and Economic Performance of U.S. Firms", *Academic of Management Review*, 10 (3), 540–557.
8. Ventura, E.C.F. and Vieira, M.M.F. (2007), "Social Responsibility as a Displacement of Capitalism: Evidences from Banks in Brazil", *Electronic Journal of Business Ethics and Organisational Studies*, 12 (1), 35-47.
9. Walter F. Abbott and R. Joseph Monsen (1979), "On the Measurement of Corporate Social Responsibility: Self-Reported Disclosures as a Method of Measuring Corporate Social Involvement", *The Academy of Management Journal*, 22 (3), September, 501-515.
10. Wise V. and Ali M. M. (2009), "Corporate Governance and Corporate Social Responsibility in Bangladesh with Special Reference to Commercial Banks" AIUB BUS Econ Working Paper Series No 2009.05.
11. *World Commission on Environment and Development (1987), Our Common Future, Oxford, Oxford University Press, ISBN 019282080X.*
12. Zappi, Gianna (2007), "Corporate Responsibility in the Italian Banking Industry: Creating Value through Listening to Stakeholders", *Corporate Governance,* 7 (4), 471-475.