SUSTAINABLE DEVELOPMENT AND CSR IN THE FINANCIAL SECTOR

MOLDOVAN (GAVRIL) IOANA ANDRADA

PH.D. LECTURER, THE BUCHAREST UNIVERSITY OF ECONOMIC STUDIES
e-mail: ioanaa.gavril@gmail.com

Abstract

The recent financial crisis has reignited discussions on corporate social responsibility (CSR), mainly on social responsibility of financial companies. The problems that have arisen during the crisis stressed the fact that the financial system has not effectively fulfill the role of financing the real economy, undermining sustainable economic development. The article analyzes the links between sustainable development and corporate social responsibility and presents a normative approach of corporate social responsibility in the financial sector. Through the functions they perform, financial companies can help promote economic growth, increase employment, improve living standards of people, and even contribute to the environmental protection, so that they can have a notable contribution to the promotion of sustainable development when they act effectively. The paper outlines several measures, which, if applied by financial companies, would transform them in promoters of sustainable development.

Keywords: financial institutions, financial crisis, social responsibility, sustainability, sustainable development

JEL Classification: G20, G01, O10

1. Introduction

Social responsibility in general, and corporate social responsibility (CSR) of financial institutions in particular have become highly debated topics in the aftermath of the global financial crisis that burst in 2008, as the crisis has arisen due to the irresponsible behavior of the financial companies.

The global financial crisis of 2008 has put into light the deficiencies of the financial system. It has failed to accomplish its main role, which is efficiently financing the real economy, and it became a mean in itself, a way of achieving rapid and consistent gains respectively. The crisis in the financial sector has rapidly turned into a severe economic crisis, which affected millions of people, by lowering their standard of living or even making them face poverty.

The irresponsibility of the financial companies is hardly assessed in good times, as its effects are not always easily seen or felt, but rather subtle. However, its effects can be more severe than those induced by social irresponsibility of manufacturing companies, for example. This is due to the nature of their activity and to the multitude of interdependences existing between each other and also between them and the companies in the real economy.

CSR is likely to discourage informal economy. The decision to work or not in the shadow economy depends primarily on the official status of the economy, and in the event of a recession people are tempted to compensate the loss of income by engaging in the informal economy (Davidescu, 2014). Socially responsible companies should discourage informal work, as this causes negative effects on society.

The crisis has lead to a paradigm shift regarding financial markets, so that they are not perceived any longer as self-adjusting and self-correcting entities. Moreover, the crisis has brought to the World’s attention the fact that between the financial sector and the real economy there had been a break. For example, in some years before the crisis, the global stock market capitalization, which represents a share of the total value of the global financial market, has exceeded the global GDP (Figure 1). The development of the financial system has been artificial, and it has not fulfilled effectively the role of financing, but rather paved a move away from the objectives of sustainable development. Therefore, authorities and financial corporations should work together so that such disturbances will be avoided in the future and moreover, they should direct their activities towards the sustainable development of the financial system, economy and society.

Given the fact that they control and redirect great amounts of money, financial companies are called upon to promote sustainable development, as they can encourage economic growth, social welfare and also the protection of the environment.

This paper consists of three sections. The first one analyzes the links between corporate social responsibility and sustainable development, the second section highlights the role of financial institutions within the economy, and the third one points out the social responsibilities of financial corporations.
2. Corporate Social Responsibility and Sustainable Development

The literature provides a wide range of approaches for corporate social responsibility (CSR), sustainable development (SD) and the links between them. None of the terms has a generally accepted definition.

For CSR, some of these definitions focus on the notion of sustainable development, while others refer to economic, legal, ethical and discretionary responsibilities of corporations, or to increasing the welfare of the society.

The most popular definition of CSR is the one submitted by Carroll: “The social responsibility of business encompasses the economic, legal, ethical and discretionary expectations that a society has of organizations at a given point in time” (Carroll, 2008). The economic responsibility of a corporation is for it to be efficient, profitable and viable, the legal responsibility refers to obeying the laws and regulations, the ethical responsibility encompasses ethical norms that are not codified into law, while the discretionary responsibility refers to social activities and roles above the economic, legal and ethical responsibilities, such as philanthropy.

The World Business Council for Sustainable Development (WBCSD) defines corporate social responsibility as “the continuing commitment by business to behave ethically and contribute to economic development while improving the quality of life of the workforce and their families as well as of the local community and society at large”, while the European Commission’s definition states that CSR “refers to companies taking responsibility for their impact on society”.

Regarding SD, the most popular definition is the one submitted by The World Commission in Environment and Development in the report “Our Common Future”, also known as the “Bruntland Report”: “Sustainable development is a development that meets the needs of the present without compromising the ability of future generations to meet their future needs. It contains within it two key concepts: the concept of needs, in particular the essential needs of the world’s poor, to which overriding priority should be given; and the idea of limitations imposed by the state of technology and social organization of the environments ability to meet present and future needs” (Ebner and Baumgartner, 2006).

Several authors regard SD and CSR as synonyms (van der Woerd and van der Brink, 2004; Muller, 2006), which means that CSR should consider the three dimensions of social, environmental and economic issues.

Others consider that SD is a broad basis for CSR, due to its three pillar (social, economic and ecological) dimension, and SD at corporate level is seen as CSR (DesJardins, 1998; van Marrewijk, 2003; Zwetsloot, 2003). Therefore, SD is the responsibility of governments, international organisations and individuals, while CSR is focused on a corporate level, so that corporations meet the needs of their stakeholders while protecting the environment (Ebner and Baumgartner, 2006).

According to Valor (2005), social performance is given attention on each of the three markets where corporate act: product market, labour market and capital market. CSR on product market refers to ethical purchasing and sourcing, fair trade, ethical consumerism, socially responsible advertising and marketing techniques, and implementing quality management procedures. On the labour market, CSR policies may be implemented through compliance of human rights standards, good working conditions, development of high standards regarding human resource management, opposition to child labour and oppressive regimes. On capital market CSR refers to socially
3. Functions of Financial Companies

The main role of financial companies is taking money from those agents who make savings and putting them at the disposal of those who need it. Therefore, they intermediate the financing of the economy and in this process one of the main stakeholders in the society itself, as most of the money the financial companies hold, invest or lend come from the society. Given that, their social responsibilities should be a very important element in their policies.

Overall, financial companies fulfill several functions:

- Collect and mobilize savings;
- Allocate funds for investments, through credit or IPOs on the capital market;
- Provide liquidity when needed by reconciling the preferences of borrowers and savers;
- Provide capital accumulation through a mechanism for pooling funds for the purchase of shares in some large companies that otherwise would be inaccessible to small investors;
- Enable the transfer of funds between countries or geographical regions;
- Provide methods for clearing and settlement, thus facilitating the exchange of securities, goods, services and other assets;
- Provide methods for managing uncertainty and controlling risk by offering a wide range of financial instruments for portfolio diversification;
- Offer information about financial assets’ prices, helping economic agents in making investment decisions;
- Provide methods for managing asymmetric information problems by exercising corporate control and monitoring managers of debtors; they also ensure that borrowers make the repayments;
- Select projects by screening and funding viable projects only; They may also contribute to protecting the environment and reducing pollution by financing only the friendly to environment projects;
- Monitor funds by controlling the debtors and ensuring that funds are used as agreed.

Through all these functions that they perform, financial institutions may foster economic growth and generate employment, improve the standard of living, contribute to the environment protection, so that they may have a great contribution to sustainable development when acting properly and effective. Financial corporations should also integrate in their policies social responsibilities above their economic and legal responsibilities.

As financial intermediation is an activity with great impact on society, it should be strictly regulated and supervised, so regulating and supervising authorities also have a great role in promoting corporate social responsibility within the financial system.

However, the recent financial crisis has shown that neither the financial companies nor the regulators or supervisors have acted responsibly. There were a numbers of issues, mainly moral hazard problems, which prevented the authorities from stopping the financial companies’ irresponsible or unethical actions.

4. Social Responsibilities of Financial Companies: a normative approach

Until the end of the 20th century, the social responsibilities of corporations were rather optional and limited to donations or philanthropy. However, in the last decade of the 20th century this situation started to change, so that nowadays, especially in Europe, CSR becomes a practice of business, and moreover, it is increasingly changing from being a voluntary practice to being mandatory by law.

A social responsible financial company should implement a CSR policy that consists, in addition to the classical requirements of CSR, of:

- Allocating the financial resources in a responsible manner, which means investing in or lending to socially responsible activities only.
- Complying with the laws and regulations in force. This means they should make efforts towards achieving a management policy that allows them to be profitable while complying with the rules. Also, they should allocate resources in order to obey the rules, and not for evading them.
- Maintaining confidence in the financial system by providing security guarantees to their depositors in order to protect them (Zeegers, 2000);
- Using the money received as deposits responsibly;
- Lowering their intermediation margins, so that the financial resources are effectively used. It is very important for small economic agents to be able to finance their businesses at low, non-abusive costs.
• Paying attention at the demand of underserved economic agents, in order to adapt their products so that the firms or the population may satisfy their needs easily and at low costs, so that all groups in society have access to their products (Decker, 2008).
• Operating transparently and educating their clients by explaining all the details about the complex financial products they sell. A low percent of the population has the necessary financial education in order to completely understand the characteristics and the implications of financial products. Banks, for example, take advantage of this situation and lend their clients at higher costs than they expect initially, as they do not mention clear information about the wide range of commissions a borrower has to pay.
• Contributing to the environment protection by refusing lending to or investing in polluting industries (Zeegers, 2000; Douglas et. al., 2004);
• Promoting their financial products ethically, with great transparency and no hidden purposes. Moreover, their internal management policy should also be ethical. Cases like those huge bonuses given to managers responsible for the crisis in 2008 should never have happened.
• Concerning about society’s needs by allocation of money in order to satisfy them.
• Getting to know the customers (Decker, 2008), which is expected to reduce the information asymmetry problem inherent in lending (Hodgson, 2002 and Ogrizek, 2002).
• Fighting money laundering and preventing tax evasion (Douglas et. al., 2004).
• Promoting social cohesion (Decker, 2008).

5. Conclusions

Financial companies and the financial system as a whole, should contribute to the welfare of the society by improving its capacity of saving and investing, and should not jeopardize the development of the economy, as recently happened during the financial crisis.

Also, since they control great amounts of money, the financial companies are expected to play an important role in the decrease of poverty and the reduction of social and economic exclusion. Moreover, they are expected that, by their actions, to contribute indirectly to the reduction of pollution and the protection of the environment. In other words, the financial companies should act in the direction of sustainable development.

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7. References

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