ISSN 2319-345X
Vol. 5, No. 2, April 2016

IJMRBS

International Journal of Management Research and Business Strategy

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Int. J. Mgmt Res. & Bus. Strat. 2016

International Journal of Management Research and Business Strategy

ISSN 2319-345X www.ijmrbs.com
Vol. 5, No. 2, April 2016

ROLE OF INDIAN BANKING SYSTEM TOWARDS SUSTAINABLE DEVELOPMENT OF THE SOCIETY: A CONCEPTUAL ANALYSIS

V Ravikumar[1] and S Chandrakumarmangalam[2]

*Corresponding Author: **V Ravikumar** ✉ vravi02mba@gmail.com

Banks play a crucial role in promoting sustainable development, the industry got off to a late start in acknowledging sustainability as an item on its agenda. In the 1990s, however, it started to play a more active role in sustainable development. The major shift happened when bankers realized poor environmental performance on the part of their clients represented a threat to their business success. This paper emphasizes the concept of sustainability in Indian banking sector and suggest the options to improve sustainable banking in Indian scenario.

Keywords: Sustainable banking, CDM, Carbon credit, Green lending

INTRODUCTION

Sustainable Banking is a philosophy that underpins everything about banking, a value system that says a bank's commercial activities must not only benefit its staff and shareholders, but also its customers and the wider economy, while at the same time preventing, or at least minimizing, any undue effects on society and the natural environment. It also requires banks, where appropriate, to be proactive and take steps to improve society and the environment. Banks can play an influential role in encouraging the shift to a low-carbon society – providing access to capital and measuring risk of investments. Considering environmental and social factors in those investment decisions can have a significant role in shifting the global economy toward sustainable business practices.

The best way for a bank to develop commercially is to look at the big picture and act in a way that benefits consumers, the economy, society and the environment. Banks are part of complex human, social and environmental ecosystems, so it is in their own self-interests to keep those ecosystems going. Sustainable banking is where self-interest and altruism meet. They are not mutually exclusive concepts. The surest way for bankers to promote their own interests is, paradoxical though it may seem to some, to act in the best interests of customers andothers.

Sustainable banking has many labels: Corporate Social Responsibility (CSR), Corporate Responsibility (CR), corporate citizenship, Environmental and Social Governance (ESG) and

[1] Assistant Professor and Head, Department of Management Studies, MPNMJ Engineering College, Chennimalai, Erode - 638 112, Tamil Nadu, India.

[2] Associate Professor and Head, Department of Management Studies, Anna University Regional Centre, Coimbatore – 641047, Tamil Nadu, India

other variants. Whatever it is called, it is not easy to implement. The right balance has to be struck. Abank must not lose focus of its commercial activities in pursuit of worthy causes. There is also a danger of acting in a seemingly hypocritical way: If a bank's commercial sponsorship department – for sound business reasons – backs a Formula 1 team, or its project finance division provides loans for a dam that will flood virgin forests, those departments must be able to answer hostile questions about how supporting a carbon-intensive sport or financing a habitat-destroying project is compatible with the bank's environmental policies. There may be valid answers to such questions, but they must be carefully thought out and rehearsed.

There have been several paradigm shifts in the understanding of the concept of economic development (Meier, 2005; Todaro and Smith, 2011). In the early days of development economics following the end of the Second World War, development was seen as being concomitant with economic growth, and Gross Domestic Product and per capita income were the tools of measurement of a nation's level of development. Several Less Developed Countries (LDCs) passionately followed the path of industrialization and modernization in the hope of achieving higher levels of economic growth and development. But disillusionment quickly set in, as these countries continued to be plagued by widespread poverty and its associated miseries.

In the late 1960s, Dudley Seers engineered the first paradigm shift in the understanding of economic development when he interpreted the term to mean a reduction in poverty, inequality and unemployment. By the end of the 20th century, Nobel Laureate Amartya Sen (1999) was defining development as reducing deprivation or broadening choice. Sen's concept of deprivation represents a multidimensional view of poverty that includes hunger, illiteracy, illness and poor health, powerlessness, insecurity, humiliation, and a lack of access to basic infrastructure. In the three decades between these two interpretations of development, there emerged the equally important concept of sustainable development, i.e., "development that meets the needs of the present without compromising the ability of future generations to meet their own needs" (World Commission on Environment and Development, 1987).

Sustainability in Banking takes two forms

- The adoption of environmental and social responsibility in a bank's routine operations through environmental initiatives (e.g., recycling programs, reduction in the use of paper, improvements in energy efficiency and so on) and socially responsible initiatives (e.g., financial inclusion efforts, support for community events, etc.)
- The integration of sustainability into a bank's core businesses through the incorporation of environmental and social considerations in to the bank's strategy and product design. Examples include the incorporation of environmental criteria into a bank's lending and investment strategy and the development of green financial products.

The potential effect of banks switching to more environmentally friendly practices (i.e., less paper use, less electrical use, solar power, greater energy efficiency, etc.) is definitely large. However when compared with many other sectors of the economy, banks do not generate the same burden of energy and water use, nor are they responsible for large-scale emissions and pollution. Banking is, in fact, seen as a relatively environmentally friendly industry.

However it is the second aspect – customers' activities – that is far more significant. By making sustainability an essential part of its business strategy, risk management and decision-making processes, a bank can support environmentally responsible projects, innovative technologies and sustainable enterprises, which in turn, can make a substantial contribution towards the goal of sustainable development. Presently most banks follow single bottom line analysis while making decisions regarding loans and investments, i.e., they consider only the financial performance of borrowers. Sustainability will imply performing a triple bottom line analysis, i.e., an analysis that takes into account environmental, and social, along with the traditional financial performance.

Indian Scenario

Banks in India have taken up the challenge of socially responsible finance, providing no-frill accounts, participating in priority sector lending, linking up with Self-Help Groups for lending to weaker sections, etc., but are yet to address the issue of environmentally responsible banking. At present the sole focus of banks in this direction is to meet minimum compliance standards. No bank in India is a signatory to Equator Principles (EPs); in fact awareness of these principles among bankers is very poor (Biswas, 2011). No bank has an environment cell or an environment policy, nor do environmental factors find a place in banks' risk management systems.

Mor (2008) highlights the dilemma faced by banks in the country: currently no bank is a signatory to the EPs and all the banks are on an equal footing. If one bank were to become a signatory, it would have to incorporate and implement additional risk management techniques, it might have to ask some large borrowers to rework investment proposals to take care of environmental factors, some projects and borrowers might even have to be rejected for non-compliance. In other words, the implementing bank would find itself on an unlevel playing field. The fear that EP early adopters would risk losing business keeps all banks from adopting these vital principles. But if the environment is not factored into project appraisal and investment decisions, banks face very strong, very real risks of project suspension or closure, resulting in losses for the bank almost certainly in the long run and quite possibly in the immediate future as well.

There are a few instances of banks taking up environmental or green projects (The Climate Group, 2010) some of which are briefly outlined here. Domestic banks such as State Bank of India, Punjab National Bank, IDBI Bank and ICICI Bank have begun to fund renewable energy projects. Foreign banks such as Standard Chartered and ABN Amro are also focused on renewable energy financing. State Bank of India owns wind farms for generation of green power to partly substitute consumption of thermal power by its offices in Tamil Nadu, Maharashtra and Gujarat. Bank of Baroda has launched a scheme for financing SMEs for acquisition of equipments, services and adopting measures for enhancement of energy efficiency/conservation of energy. SBI has entered into a MOU with a consortium of leading Clean Development Mechanism (CDM) consultants to provide finance to implement CDM projects, advisory services as well as value added products in the area of carbon credit finance (such as securitization of carbon credit receivables, carbon credit delivery guarantees and escrow mechanism for carbon credits) (*Business Standard*, 2007).

SBI also has a new Green Home Loan scheme to support environmentally-friendly residential projects. The scheme offers concessions such as 5% concession in margins, 0.25% concession in interest rate, and zero processing fee for projects rated by the Indian Green Building Council (IGBC). IndusInd Bank has initiated its Green Office Project under which it has installed solar powered ATMs in different cities; these will result in energy saving as well as reduced CO_2 emissions. ICICI Bank has been assisting various organizations to undertake clean energy and environmentally sustainable projects/initiatives. It has provided financial assistance to projects that specifically promote energy efficiency, renewable energy, biomass co-generation, biomass gasification, waste heat recovery, etc. The bank has been funding projects that contribute to mitigation of GHG emissions and financing clean technologies. Yes Bank's portfolio has projects in the areas of alternative energy and clean technologies as well as investments in the South Asia Clean Energy Fund and the Tatva Investment Program.

Opportunities for Banks in India

There is no dearth of opportunities for banks wishing to incorporate environmental factors into their operations. Some very basic steps that banks can take are listed below. While these seem minor, their merit lies in ease of acceptance and implementation, and introduction of the necessary culture in banks. This will allow banks to take the first step down the path of sustainable finance.

1. Sustainability reporting: A sustainability report documents the institution's sustainability efforts and includes disclosures of its performance across economic, environmental and social parameters. Such reporting would showcase a financial institution's adherence to voluntary global standards such as the Equator Principles and help to attract investments from new avenues such as socially responsible investors, who only invest in projects that are conscious of the environments and the hazards it faces. Presently only two banks in India are engaged in non-financial reporting, whereas globally, there are close to 300 financial institutions reporting on sustainability performance (Kalia, 2011). Once an institution makes a commitment to sustainability reporting, it would automatically adopt sustainability measures so as to improve its report. An extreme example is that of Triodos Bank, which provides its depositors with an annual list of all the loans the bank has made, allowing savers to see exactly how their money isused.
2. Retail banking measures: Promotion of electronic banking – use of internet banking, mobile banking, ATM operations, ECS facility, electronic remittance, fund transfers, and so on. All these would help reduce the use of paper and obviate the need for travel. More importantly these facilities offer win-win opportunities for all stakeholders – customers save time and money (bank charges for fund transfers are significantly lower than charges for traditional demand drafts or clearing charges for cheques); the bank front office faces less pressure and staff can be productively and profitably deployed elsewhere; society as a whole gains on account of less travel, less emissions and less

paper use. These may appear to be insignificant measures, but given the huge volume of transactions (many of them small in size) they would multiply into significant savings on all fronts. Banks could actively promote these facilities among their retail customers through awareness sessions, basic training, etc. More importantly, banks could ensure that corporate and institutional customers begin to include these modes of banking and fund transfer as part of their dealings with existing and prospective shareholders/debt- holders. For e.g. ECS could no longer be optional, but be made compulsory for payment of dividend/interest; first-time applications could be accompanied not by cheque/DD, but by an RTGS/NEFT transfer. The opportunities exist – they need to be explored and thoroughly exploited.

3. Efficiency in resource use: Banks' use of resources such as water, energy and paper offer great scope for contribution to environment management. Some areas of promise include: Management of emissions by measures such as tele-/video conferencing, green commuting and other approaches to reducing business travel; encouraging carpooling among employees, providing a common staff vehicle for commuting could also be thought of, particularly in cities and towns where traffic congestion is a major issue. Energy consumption reduction strategies such as optimal use of daylight, energy efficient equipment, use of CFL lights, timely and proper maintenance of equipment, etc. Banks could also seriously consider the use of solar energy for office lighting, operation of ATMs and so on .IT operations are responsible for alarge part of banks' energy use and rationalization measures could be fruitfully undertaken. Water consumption reduction and recycling programmes; while recycling may not be feasible at smaller branches and offices, corporate offices and Very Large Branches could seriously consider the possibility. Rainwater harvesting is another low-cost option with huge potential for resource conservation and cost-saving. Reduced paper use and green printing measures such as use of recycled/chlorine-free paper, double-sided printing, etc. Waste management through recycling, especially of paper, and appropriate disposal of e-waste, plastic,etc.

4. Green Lending: At the retail level, banks could promote green housing and energy- efficient homes through differential pricing of home loans and mortgages. In the case of MSMEs, banks would have to go the extra mile to encourage small enterprises to adopt environmentally healthy practices, since these entities lack the knowledge, the expertise and the resources to do so themselves. The biggest impact, however, will come in the case of corporate customers and project finance. Corporate customers have the resources to absorb the extra cost arising out of compliance with environmental norms. Banks can well stand firm on lending to these customers only on condition ofcompliance.

5. Green Investments: A part of a bank's investments could be in Sustainable Development Funds in India such as ABN Amro Sustainable Development Fund, BNP Paribas Sustainable Development Fund, Fortis Sustainable Development Fund, all launched in 2007. All these are funds where the portfolio comprises equity and equity-

related securities of Socially Responsible Companies focusing on sustainable development.

6. Carbon Credit Business: A variety of new financial markets have emerged in recent years, offering businesses key incentives (besides taxes and other punitive measures) to slow down overall emissions growth and possibly, global warming itself. A key feature of these markets is emissions trading, or cap-and-trade schemes, which allow companies to buy or sell 'credits' that collectively bind all participating companies to an overall emissions limit. While markets operate for specific pollutants such as GHGs and acid rain, by far the biggest emissions market is or carbon. Trading in Certified Emission Reductions (CERs), commonly known as carbon credits, presents sizeable business opportunities. Indian banks can involve themselves in this business, herein theycanprovide all the services in the area of CDMs and carbon credits including services of identification and funding of CDM projects, advisory services for registration of CDM projects and commercialization of carbon credits under different structures to meet the requirements of its customers, acting as an intermediary for buying carbon credits on behalf of end-users or carbon funds, financing against CERs and CERs receivables, and other related banking services. India has huge potential for carbon credit business, and Indian banks can set up dedicated carbon credit cells to capture a major share of this carbon credit business, thereby shoring up their fee-based income, while simultaneously contributing to environment protection and improvement. Banks like SBI and IDBI Bank have already made a beginning and other banks can follow suit.

These are only some of the opportunities that banks can tap. While some can be implemented without delay and yield profit in the immediate future, some have a longer time horizon.

CONCLUSION

India today has the opportunity to grow in a manner that moderates the costs of environmental degradation, and this, in turn, presents a vast range of opportunities for India's financial sector. Banks not only need to make direct investments in sustainable development, they also need to leverage their indirect control over investment and management decisions to influence business into fulfilling broader social and environmental goals. There is a plethora of opportunities in the area of environmentally responsible finance, which banks can profitably exploit. Indian banks have a mammoth task ahead of them. But they have no choice in the matter: sustainable finance is the future and more so for Indian banks desirous of becoming globalplayers.

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International Journal of Management Research and Business Strategy

Hyderabad, INDIA. Ph: +91-09441351700, 09059645577

E-mail: editorijmrbs@gmail.com or editor@ijmrbs.com

Website: www.ijmrbs.com

ISSN 2319-345X

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