SOCIAL FINANCE AND SOCIAL BANKING – A PATH TOWARDS A MORE SUSTAINABLE FUTURE[1]

PETAR MITIĆ[2] and SLOBODAN RAKIĆ[3]

Abstract: *Introducing products and services in finances and banking with a prominent social component is one of the ways international community responds to modern challenges. The aim of this chapter is to make systematization and provide insight into the financial products and services that are designed to improve social environment. Main categories of the classification proposed by the authors are: Retail and Microentrepreneruship, Corporate and Investment Banking, Asset Management and Insurance. Even though many of these products and services are still in an experimental phase, a growing need for social finance and banking is evident. Additionally, the influence of public opinion on the financial institutions contributes to their adaptation. Overall, a clear trend of growth of this type of products and services is apparent. Future research and professional discussions are particularly important in order to support further development of the concepts of social finance and social banking.*

Key Words: *social finance, social banking, development, social environment, sustainable development, corporate social responsibility.*

1. Introductory Notes: From Millennium Development Goals to Sustainable Development Goals

In order for the international community to adequately respond to modern challenges, such as accelerated growth of ecological problems, poverty, terrorism, migration, polarization of the world's wealth, economic crisis and rapid technological and social development [Munitlak Ivanovic-Mitic, 2016], several global conferences have been organized with the aim to gather international community around common goals and to establish certain standards of sustainable development. These conferences emerged in response to the initiatives of various international organizations such as United Nations (UN), World Bank (WB), International Monetary Fund (IMF), etc. The first such conference, entitled *United Nations Conference*

---

[1] This paper is a part of research projects numbers III47009 (*European integrations and social and economic changes in Serbian economy on the way to the EU*) and OI179015 (*Challenges and prospects of structural changes in Serbia: Strategic directions for economic development and harmonization with EU requirements*), financed by the Ministry of Education, Science and Technological Development of the Republic of Serbia.

[2] Research Assistant, Institute of Economic Sciences, Belgrade, petar.mitic@ien.bg.ac.rs.

[3] Assistant Professor, Educons University, Faculty of Business Economics, e-mail: rakic@educons.edu.rs; This paper is partially based on chapter 3.2. from the Ph.D. thesis by Slobodan Rakic entitled „Examination of the effects of Corporate Social Responsibility on the Profitability of the Banks in the European Union".

on Environment and Development (UNCED) was held in Rio de Janeiro in 1992, where 178 countries and several thousand NGO representatives took part[4]. After Rio in 1992, the next conference of such magnitude was held in Johannesburg in 2002, entitled *World Conference on Sustainable Development* from which a Declaration on sustainable development emerged.

Meanwhile, as a parallel process, in September 2000 in New York City, world leaders from 189 countries held the *Millennium Summit* where they ratified the *United Nations Millennium Declaration* and established eight Millennium Development Goals (MDGs). These goals represented the first organized world response to growing concerns about health, education, economic development, environment, and inequality. A review process of MDGs was done at the World Summit in September 2005, also in New York City.

Next major conference was *The United Nations Conference on Sustainable Development* in Rio de Janeiro in 2012, which is also known as Rio +20. All of the 192 members of the UN participated in this conference. The main objectives were how to build a *Green Economy* in order to achieve a sustainable development while improving international coordination actions through construction of the institutional frameworks. It is also important to mention a conference on sustainable development which was held in New York in September 2015. There, a plan named *Transforming our world: the 2030 Agenda for Sustainable Development* was adopted. This conference is of great importance for sustainable development because 17 global Sustainable Development Goals (SDGs) were adopted. "The *Goals and targets will stimulate action* over the *next fifteen years in* areas of *critical importance for humanity* and the *planet*" [United Nations, 2015, p.5].

When discussing efficiency and effectiveness of implementing these goals, it is important to emphasize that the predecessors of the SDGs were MDGs. If the original and current objectives of achieving a sustainable development are compared, it can be concluded that the new goals of sustainable development are more ambitious and have a broader spectrum compared to the MDGs. What remains the same is the fact that none is legally binding. Countries that adopted SDGs have agreed to make their own frameworks for the implementation and monitoring of these objectives, but this does not represent a guarantee for the full implementation. According to some viewpoints, SDGs are seen as an overly ambitious attempt to create a set of universal goals. Critics stated that "today's development goals are full of good intentions, but we all know where they lead" [The Economist, 2015]. This raises the question of participation of the private sector and local stakeholders, because the UN has no mechanism to involve other stakeholders except Member States. Newly formed SDGs are viewed as a system within which an interdependent network of targets exists. This is the first time that the goals and targets are interconnected both horizontally and

[4] Before the conference in Rio in 1992, there was a conference held in Stockholm in 1972 but it reffered specifically to environmental protection, while the conference in Rio was the first one where the concept of Sustasinable Development was mentioned.

vertically. The key problem is implementation of targets, because some are more complicated than others and it will require a high degree of political will to implement them [Le Blanc, 2015].

From the perspective of social finance and banking, it is of utmost importance to implement SDGs in international policies and activities. Eventhough there is no clear mention of social finance or social banking directly linking it with SDGs, there is a clear indirect connection through Goal 1 of SDGs which states "End poverty in all its forms everywhere" [UN Statistics Division, 2016, p.2] and especially Target 1.4. from Goal 1. which clearly mentiones microfinance as one of the most important parts of social finance and banking [UN Statistics Division, 2016, p.2]. All in all, the goal of social finance and banking is to help tackle poverty, empower and provide access to financial products and services to vulnerable social groups.

2. The Introduction of Social Features in Finance and Banking

In parallel with the process of introducing environmental aspects to financial sector, a tendency to "humanize" the existing financial products and services emerges [Rakic *et al.*, 2014]. There is a need to adjust the financial operations to the principles of sustainability, which contain a wide range of qualitative indicators related to social environment. According to Roy-Sapre (2016) "several studies have argued that access to financial instruments, such as banking services and investment options, lead to a better quality of life, especially for the poor and disadvantaged". Be that as it may, a clear difference should be made between developed and developing countries. The main goal of social finance and banking in developing countries is to help population get out of poverty, while developed countries have a more subtle goal to help their population achieve a higher level of social development, and thus products and services that are offered in those two groups of countries are slightly different. According to the European Federation of Ethical and Alternative Banks (FEBEA), there are five key factors that separate traditional banks from those that incorporate social protection in their business. With certain modifications made by the authors, these factors can be represented as [FEBEA, 2012]:

1. The impact of banks on the social environment
2. Origin of money
3. Destination of money
4. Criteria and values for the use of money
5. Socially Responsible Management

The first factor is the bank's business policy which defines its role in the social environment. If the bank incorporates protection of the social environment it needs to focus its policies and practices on directing more resources to projects that are environmentally and socially responsible. The second factor implies that if a bank has a relationship with the social environment, it will not accept money coming from socially and environmentally damaging activities, such as all forms of criminal activities [Radovic et al., 2013], severe environmental pollutants, commercial organizations that do not respect workers' rights and have unethical attitude towards individuals and society as a whole. According to the third factor – destination of money, banks should invest in such activities that promote employment, sustainability, protection of the environment, social inclusion of vulnerable groups, etc. Furthermore, banks have developed systems not only for the assessment of the quantitative, but qualitative business activities as well. Criteria and values for the use of money must be created with regard to social and environmental principles. The concept of a socially responsible management is the fifth factor, which refers to the way the bank's management formulates and implements effective business strategies and policies. Transparency has to be a fundamental value of the bank, which is not always the case with traditional banks.

3. The Financial Products and Services Aimed at Improving the Social Environment

The current theory views institutions, products and services that have non-traditional forms of financial services as "specialized". Practice shows that their

Figure 1: The financial products and services aimed at improving the social environment

Source: Authors

growth rates have been above those of traditional institutions, "especially in the area of microcrediting since the early 2000s when the business was booming" [Postelnicu - Hermes, 2016]. The authors underwent the work of categorizing financial products and services intended for improving social environment (Figure 1).

Some of these products and services are not in widespread use yet. It will take time until they are settled in everyday business practice. But what is noticeable is that there is a growing need for them globaly and the influence of public opinion changes the attitude of financial institutions to adapt, change and improve their offers. Also, these products and services do not focus solely on profit as a prerequisite for loan granting or other services, but also assess the nature of the service itself, use value, ethical relationship and other social criteria.

3.1. Retail Banking and Microentrepreneruship

Microfinance can be classified into five main groups of financial products: Microcredit, Microsavings, Microinsurance, Microleasing and Microtransfers. These products are characterized by low administrative and transaction costs, flexible criteria, low interest rates, short repayment terms, etc. They are mainly intended for vulnerable population in poor countries [Microfinance, 2010]. The creator of this concept is Muhammad Yunus, who won the Nobel Prize in 2006. These products and services are either offered by specialized banks or micro-credit organizations. Majority of the deposits are received from western developed countries' major financial organizations, private donors and humanitarian organizations that specialize in fundraising. These deposits are then invested trought microcredit organizations in developing countries (e.g. *Oikos Bank* of Denmark). It is also possible for financial institutions to establish a trust fund to invest in microcredit organizations or to establsh their own organization for investing in this type of products and services (e.g. *Triodos Bank* - Microfinance Fund).

After developing the first microcredit banks that are considered socially responsible (e.g. *Charity Bank, Triodos Bank* and *AIB bank*), their business policies began to adapt and take socially responsible deposits under specific terms. When talking about socially responsible savings and loans, most of these products actually relate to the provision of a guarantee to depositors on the method of use of deposited funds. They have a guarantee that the placement of the funds will be in activities that ensure a positive stance towards social environment. For example, *Triodos Bank* takes into account environmental protection and accordingly places deposits received. A large number of banks, such as *Charity Bank* and *GLS Bank*, offer a specially designed type of savings which are subsequently invested in social protection projects: if the customers agree to a lower interest rate, then the difference in the interest rate, from lower to standard, is invested in these projects. Additionally, the tax policy on this kind of savings can be more favorable but this depends solely on the tax policy of the state where the bank operates. "In the UK, the savings that were intended to further the placement of the sustainable loans were tax-exempt" [Charity Bank, 2016].

A large number of retail loans relate to mortgage loans that are designed for the poor. Savings and credit organizations in the UK (e.g. *Leeds Building Society Bank*, *Necastle Building Society*) offer an extremely wide range of mortgage services, including those for the poor citizens. Sustainable banks offer their customers investment opportunities in individual securities or various funds that invest in social protection projects (e.g. *Triodos Microfinance Fund* and *Triodos Ethical Stocks & Shares ISA).* It should be noted that there are different credit and debit cards that operate on the principle of spending portions of costs for cards maintenance on humanitarian organizations or projects (e.g. *Charity credit card* from *Co-operative Bank)* supports organizations such as *Amnesty International, Oxfam, Save the Children* etc.

3.2. Corporate and Investment Banking

Commercial banks are designing special payment systems, savings and current accounts and other forms of banking operations for organizations which run socially responsible businesses. For example, *MagNet bank* waives costs of a montly maintenance fee for account management if the client requests it. There is no obligation of payment, but an option of payment for that service. The bank's goal in the future is to charge clients the actual account usage, rather than fixed amount, so that it can represent a real value of account usage and not hidden costs[5] for clients. Furthermore, the bank is arguing that responsible payment and option for its clients will help bank cover real costs of account management and not force the bank to cover costs of account management from revenues collected under a different legal title [Magnet Bank, 2016].

Next in line is Impact Investing which uses for-profit investment to address social and environmental problems. Typifying this approach is the Global Impact Investment Network (GIIN), a non-profit organization dedicated to promoting a more effective impact investing around the world [GIIN, 2017]. GIIN seeks to promote the infrastructure, activities, education, and research that facilitate more effective impact investing. The ultimate aim is a coherent, well-developed marketplace for the impact investing industry, creating along the way "social investment banks" and "social enterprise clubs" [John, 2010].

When investment banking is concerned, social responsibility can play an important role in attracting funds for the investments. An investment bank of this type pays particular attention to the attitude of companies towards the social environment when offering their services. The investment sector of *Triodos bank* has had a number of successful projects that are shown in Table 1, within which it helped various organizations raise significant funds for socially responsible projects.

[5] Usually, neutral banking operations, such is account management fee, are paid in fixed amount regardless of service usage. That is why it is arguable that some clients whose account usage is low partially cover costs of the clients whose account usage is high.

Table 1: Examples of securities issuance for socially responsible projects

Institution	Type of Activity	Amount	Description
Thera Trust	Bond issue	£2,000,000	Bond offer to retail investors for a national charity that provides support to people with a learning disability.
Glasgow Together	Bond issue	£2,000,000	Bond offer to investors for a social enterprise that employs ex-offenders to build and renovate properties.
Aspire Gloucestershire	Social Impact Bond	£310,000	Private placement to investors for a payment-by-results programme which aims to tackle youth homelessness.
Ebsi	Loan and Equity	£350,000	Private placement that supports commissioners develop SIB which aim to improve the lives of disadvantaged children.
GLL	Bond issue	£5,000,000	Bond issue for charitable social enterprise in the health and leisure sector.
Bristol Together	Bond issue	£1,600,000	Private placement for social enterprise supporting major programme of job creation for ex-offenders.

Source: [Triodos Bank, 2016] Table is compiled by the authors.

When it comes to commercial loans to support socially responsible projects, they are given to organizations whose main activity is closely related to social responsibility. Table 2 presents a classification of socially responsible projects that are most frequently seen in practice. Given these types of projects are relatively new, it is often a standard that their return is guaranteed by some public institution or private donor. However, there is an upward trend in their profitability especially in the penitentiary system, health system, education and employment.

Next to commercial loans for companies, the same loans can be given to entrepreneurs with their start-ups or socially responsible small businesses. It is important to mention that "social enterprises in the financial sector—e.g. community development finance institutions (CDFIs) and credit unions—provide financial services and support to clients excluded from access to mainstream financial services; and, some CDFIs make it a condition for business lending that a client has been unable to obtain a commercial bank loan“ [Haugh-Talwar, 2016].

Table 2: Types of socially responsible loans

Type of loan	Purpose of the loan
Education	• Improvement of education system • Assistance to vulnerable social groups to obtain quality education
Crime rate and public safety and security	• Reduction of the crime rate due to preventive action • Reducing the rate of recidivist • Education and training of inmates
Social Housing	• Reducing the number of homeless people • Improvement of living conditions
Healthcare	• Improving public health • Preventive actions • Reducing the use of harmful substances
Sport activities and youth	• The construction of sports centres and promotion of sports • Sports event organization
Art and Culture	• The construction and renovation of art and cultural institutions • Promoting culture and art through organization of different events and manifestations
Local and Municipal Affairs	• Improvement of public utility services such as public transport, parks and other content • Improvement of public administration
Employment	• Employment of people with disabilities or people with mental illnesses

Source: Authors

3.3. Asset Management

“In only three or four years, ecological bonds exploded from insignificant market niche to impressive growth component of major international porftolios and many other types of significant investors” [Malovic, 2015]. Similarly, just a few years later, Social Impact Bonds (SIB) has been introduced. SIBs are public-private partnership securities that finance social programmes which are based on their financial performance. “They present a new method of financing social outcomes via private investment. It is envisaged that the SIB will be used to raise capital for social projects in the way bonds are used for investment projects" [Fox-Alberston, 2011]. The primary goal of these bonds is for the state to obtain additional private funding sources in order to improve or develop various social programs, but to keep profitability margins to make them attractive. By their structure, these bonds are standard forms of bonds and differ only by object of financing. There can be different types of social programmes, in which in the early stages re-socialization of former inmates can be seen as the main objective, also resolving the issue of the homeless and care for community and children.

The first SIB was issued in the UK in 2010 and called *Peterborough Social Impact Bond*. It aimed to assist the reintegration of former prisoners into society in order to prevent a recurrence of the criminal activity. In total, the bond raised $5 million for the project for a period of 5 years, with different foundations as investors. Another important project of bond issuance was carried out in the UK, with the aim of helping over 16,000 homeless young people to find a place to live, work and to be trained. Investors in these bonds were specialized socially responsible finance funds and investors [Social Finance, 2016]. After Great Britain, which was the first to issue this type of bonds in 2010, three years later, the USA, Germany, the Netherlands and Australia issued their bonds with similar characteristics for different types of social programmes. They were followed by Belgium, Canada, Portugal, Israel, Finland, Switzerland by 2015 and Sweden in 2016 [Social Finance, 2016, p.11].

The business policy of social impact investment funds is not primarily profit-oriented, but rather focused on the influence on social environment, which puts profit on second place, or at least in the place of equal importance as the social impact of the investment. An example for one of the most influential social impact investment funds is the *Global Health Investment Fund* pursuing a business policy of assisting the financing of the development of new drugs, vaccines, diagnostic tools, and other disease-fighting interventions that burden low and middle-income countries. The Fund operates on the quick solution principle, seeking different investment opportunities for cures that can be developed within a two or three year framework and invest in projects that do not exceed 10 million USD per project [GHIF, 2016].

3.4. Insurance

Insurance companies have a significant role in the implementation of the system of corporate social responsibility, and in particular their impact is more significant when they assume the role of institutional investors. Insurance companies also play an important role in the development of new products and services in the field of environmental protection, not only in social protection.

Looking at the life insurance market which has a relatively high concentration degree [Munitlak Ivanovic et al., 2013], there is a number of new forms of life insurance tied to social responsibility. One of the examples is the insurance of cyclists by *ETA* insurance company, which helps cyclists in the event of unforeseen cicrumstances. There is also a noticeable trend of socially responsible insurance companies improving the existing forms of insurance, such as insurance of those who are over 50 years of age or insurance of persons who have incurable diseases or in case they get any of them.

Insurance of non-profit and humanitarian organizations is increasingly gaining importance due to a strong growth in this sector over the past two decades. As an example, we can mention *Naturesave,* the insurance company which has developed a special group of insurance products and services called *Charity & Non-Profit Insurance,* intended for humanitarian and non-profit organizations with standardized insurance services such as "insurance of premises, assets, revenue, employers and public liability, as well as specific charity event insurance" etc. *Naturesave* is provoding competitive premiums and flexible options, only for charity and non-profit organizations and they are ready to meet specific requirements those organizations might have with regard to their core activity [Naturesave Insurance, 2017].

Specific forms of insurance represent less significant forms of insurance that do not have a large market share. As an example of specific forms of insurance there can be identified a growing trend of insurance of pets with already established various options for preimums with a wide range of various insurance coverages [Co-op Insurance, 2017].

4. Conclusion

Social responsibility in financial sector is an emerging trend which will find its place in mainstream finance. As it is already mentioned, there are two main directions of social finance. One is in poor and developing countries, where microfinance is gaining ground, and the other is in developed countries where the awareness of the public is forcing companies and other economic stakeholders to include social responsibility in their investments and business strategies.

Considering all abovementioned, certain characteristics can be identified for the majority of products and services that are considered socially responsible, which are:

- Transparent cost structure without predatory and high default interest rates
- Flexible approach towards clients in case of non-performing loans
- Offering loans to socially responsible projects and organizations
- Blacklisting loans considered bad for the social environment
- Flexible credit scoring and less bureaucracy
- Respecting ethical and moral codes
- The policy of low tax rates

Systematization has been made that provides an insight into the financial products and services that are designed to improve social environment. Main categories of the systematization are: Retail and Microentrepreneruship, Corporate and Investment Banking, Asset Management and Insurance. This systematization of social finance is intended to shed light on this field and put into context different actions undertaken by various financial institutions, international organizations, nongovernment sector and other parties in developing better social environment through financial sector.

References

Aldohni, A.K., 2016. Is Ethical Finance the Answer to the Ills of the UK Financial Market? A Post-Crisis Analysis. Journal of Business Ethics, pp.1-14. doi:10.1007/s10551-016-3269-5.

Charity Bank, 2016. www.charitybank.org. [Online] Available at: https://charitybank.org/ethical-savings/ethical-isa#key-benefits [Accessed 19 July 2016].

Co-op Insurance, 2017. www.co-opinsurance.co.uk. [Online] Available at: http://www.co-opinsurance.co.uk/petinsurance [Accessed 25 March 2017].

FEBEA, 2012. http://www.ethicalbankingeurope.com/. [Online] Available at: http://www.ethicalbankingeurope.com/sites/default/files/library_files/definition_ethical_bank-en.pdf [Accessed 15 June 2016].

Fox, C.-Alberston, K., 2011. Payment by results and social impact bonds in the criminal justice sector: New challenges for the concept of evidence-based policy? Criminology & Criminal Justice, 11(5), pp.395-413. 10.1177/1748895811415580.

GHIF, 2016. www.ghif.com. [Online] Available at: http://www.ghif.com/ [Accessed 10 July 2016].

GIIN, 2017. www.thegiin.org. [Online] Available at: https://thegiin.org/about/ [Accessed 27 March 2017].

Haugh, M.H.-Talwar, A., 2016. Linking Social Entrepreneurship and Social Change: The Mediating Role of Empowerment. Journal of Business Ethics, 133(4), pp.643-58. doi:10.1007/s10551-014-2449-4.

John, J.F., 2010. Social finance: commerce and community in developing countries. International Journal of Social Economics, 37(6), pp.415-28. doi: 10.1108/03068291011042300.

Le Blanc, D., 2015. Towards Integration at Last? The Sustainable Development Goals as a Network of Targets. Sustainable Development, 23(3), pp.176–87.

Magnet Bank, 2016. Pay as much as you like for retail account management. [Online] Magnet Bank Available at: https://www.netbank.hu/en/corporate#!en/about-the-community-bank/pay-as-much-as-you-like-for-retail-account-management [Accessed 19 July 2016].

Malovic, M., 2015. The Role and Prospects of Eco-Bonds in International Finance. Ecologica, 22(80), pp.756-59.

Microfinance, 2010. http://www.microfinanceinfo.com/. [Online] Available at: http://www.microfinanceinfo.com/microfinance-products/ [Accessed 18 July 2016].

Munitlak Ivanovic, O.-Mitic, P., 2016. Razvoj i teorijske postavke koncepta rezilijentnosti. In Pravci strukturnih promena u procesu pristupanja Evropskoj uniji. Belgrade: Institut ekonomskih nauka. pp.67-80.
Munitlak Ivanovic, O., Raspopovic, N., Mitic, P.-Rakic., 2013. Analysis of Life Insurance Premium in Regard to Net Income as an Influencing Factor - the Case of the Republic of Serbia. Industrija, 41(4), pp.23-38.
Naturesave Insurance, 2017. www.naturesave.co.uk. [Online] Available at: http://www.naturesave.co.uk/charity-insurance/ [Accessed 27 March 2017].
Postelnicu, L.-Hermes, N., 2016. Microfinance Performance and Social Capital: A Cross-Country Analysis. Journal of Business Ethics, pp.1-19. doi:10.1007/s10551-016-3326-0.
Radovic, V., Mitic, P.-Raspopovic, N., 2013. Implementation concept of "Business crisis and continuity management" - a great challenge in the recovery process of Serbian Economy. In Management of Corporate Security, New Approaches and Future Challenges. Ljubljana, Slovenia: Institute for Corporative Security Studies. pp.115-28.
Rakic, S., Mitic, P.-Anđelic, G., 2014. Social and Environmental Management Systems in Banking Sector. Plovdiv, 2014. University of Agribusiness and Rural Development.
Roy, P.-Sapre, A., 2016. Does Social Embedding Influence Banking Habits? A Case of India. Journal of Emerging Market Finance, 15(2), pp.169 - 190. doi.10.1177/0972652716645892.
Social Finance, 2016. Social Impact Bonds. London: Social Finance. http://www.socialfinance.org.uk/wp-content/uploads/2016/07/SIBs-Early-Years_Social-Finance_2016_Final-003.pdf.
The Economist, 2015. The 169 commandments. The Economicst.
Trinks, P.J.-Scholtens, B., 2017. The Opportunity Cost of Negative Screening in Socially Responsible Investing. Journal of Business Ethics, 140(2), pp.193-208. doi:10.1007/s10551-015-2684-3.
Triodos Bank, 2016. www.triodos.co.uk. [Online] Available at: https://www.triodos.co.uk/en/business/corporate-finance/track-record/charities-and-social-enterprises/ [Accessed 19 July 2016].
UN Statistics Division, 2016. Report of the Inter-Agency and Expert Group on Sustainable Development Goal Indicators. New York: United Nations United Nations.
United Nations, 2015. Transforming Our World: The 2030 Agenda for Sustainable Development. United Nations.