

## **CORPORATE SOCIAL RESPONSIBILITY – ONE OF PREREQUISITES FOR SUSTAINABLE DEVELOPMENT IN THE BANKING SECTOR**

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**Abstract.** The sustainable development of entrepreneurship is influenced by an organisation's image, the loyalty of its clients and employees and its financial performance. To ensure it, nowadays an increasing number of organisations integrate the corporate social responsibility approach in their operation. The banking sector's performance was considerably influenced by the 2008 financial and economic crisis that caused a decrease in the trust of clients. Therefore, the banks were forced to integrate social responsibility principles in their operation, implementing sustainable and socially responsibility financial policies. The research aim is to examine Latvia's banking sector's experience in corporate social responsibility that is necessary for sustainable development. A case study conducted showed that the banks implemented their corporate social responsibility through four areas: the environment, their employees, the economy and the general public. The banks focused their corporate social responsibility activities on the environment and the public, as Latvia's legal documents stipulated strict requirements for enterprises in respect to environmental protection as well as the implementation of the activities by the banks allowed them to reduce their costs. However, their corporate social responsibility programmes oriented towards raising the public's wellbeing contributed to the loyalty of their clients and employees, which was an essential prerequisite for the sustainable development of the banks. As regards employees, Latvia's legal documents regulate the relationship between the employer and the employee, yet the banks assumed extra responsibilities, introducing a motivation system for their employees in order to attract highly qualified and motivated employees. The sustainable development of banks is directly associated with their profits. In recent years, Latvia's banking sector grew fast and reported stable financial performance; in 2015, the banking sector's profit reached EUR 416 million and it paid in taxes EUR 141.5 million, thereby economically contributing to the country's development.

**Key words:** corporate social responsibility, sustainability, banking sector, case study.

**JEL code:** M14, I31, L26, E58

### **Introduction**

The National Development Plan of Latvia for 2014–2020 declares that sustainable development could be achieved in Latvia only if every its citizen feels responsible for future generations. Enterprises have to operate in a responsible way towards the public and the environment, as only an excellent environment for entrepreneurship can stimulate the development of enterprises and contribute to their competitiveness (Birim B., 2016; Grigore G., 2009; Galbreath J., 2009; De Roeck K., Marique G. et al., 2014) and sustainability. Even though corporate social responsibility (CSR) is not obligatory and it is not strictly stipulated in legal documents, CSR is an important functional component of any successful business (Akdogan A.A., Arslan A. et al., 2016; Gras-Gil E., Manzano M.P. et al., 2016).

Nowadays, an increasing number of organisations, scientists and practitioners in the world get interested in CSR matters. The

importance of CSR has been recognised by the financial and banking sector, thereby implementing sustainable and socially responsible financial policies. However, even though CSR emerged already at the end of the 19<sup>th</sup> century, the term CSR has been known in Latvia since relatively recently and still is not defined in the legal documents. Nevertheless, in Latvia the basic principles of social responsibility result from the Constitution of the Republic of Latvia, international legal documents and strategic policy documents.

CSR is researched based on the findings made by H.R. Bowen (1953); K. Davis (1960); S.P. Sethi (1975); A.B. Carroll (1999); M. Castelo and L. Lima (2006); J. Galbreath (2009); C.W. Bauman and J.L. Skitka (2012); K. De Roeck et al. (2014); A.A. Akdogan et al. (2016) and other scientists who believe that enterprises are able to make more profit and long-term achievements if operating only within CSR practices. However, the scientific literature presents also opposite

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opinions on the introduction of CSR practices in entrepreneurship, pointing out that CSR is a useless waste of financial resources and it is not a function of private business. CSR only moves enterprises away from their key function, i.e. profit-making (Friedman M., 1970). One can conclude that there is scientific discussion on the role of CSR in promoting the sustainable development of enterprises (Jones K. & Bartlett J.L., 2009; McElhane K., 2009).

The research has put forward a **hypothesis** – corporate social responsibility is a prerequisite for sustainable development in the banking sector. The research **aim** is to examine Latvia's banking sector's experience in corporate social responsibility that is necessary for sustainable development.

To achieve the aim, the following specific research **tasks** were set:

- 1) to examine the theoretical aspects of corporate social responsibility;
- 2) to analyse the banking sector's experience in corporate social responsibility practice in Latvia.

A number of **research methods** were employed to achieve the aim and perform the tasks. The monographic and descriptive methods were used to theoretically discuss and interpret the research results based on scientific findings and theories on CSR; statistical analysis – descriptive statistics and time series analysis – were applied to analyse the banking sector's financial performance. A case study was used to analyse CSR in the banking sector in Latvia and to examine CSR activities in the aspect of four key CSR areas: the environment, employees, the public and the economy.

### **1. Theoretical aspects of corporate social responsibility**

The first definitions of the term corporate social responsibility (CSR) date back to the 1950s (Bowen H.R., 1953), even though the very first manifestations of CSR were known even earlier. Today, the term CSR becomes increasingly

urgent in entrepreneurship and research; however, if analysing the scientific literature, one can find that there is no single approach to defining the term (Gudkova T.V., 2014; Matten D. & Moon J., 2004).

The European Commission defines CSR as one of the factors influencing the image of any organisation. An enterprise integrates social and environmental problems in its business operations in cooperation with its shareholders based on the principle of voluntary participation (European Commission, 2001).

Based on the findings available in the scientific literature, one can conclude that in a narrow sense, CSR means timely paid wages to employees, all taxes paid, compliance with legal acts on environmental protection and work safety rules and health care programmes for the employees (Castelo M. & Lima L., 2006). However, in a broader sense, CSR involves a voluntarily contribution of an enterprise to social development in the social, economic (Davis K., 2008) and environmental spheres (Litovchenko S.E. & Korsakova M.I., 2003), which is often unrelated to the enterprise's primary economic activity and exceeds the minimum standards set by the legislation and the social norms accepted in society (Bessanova I.S. & Nikolajeva I.V., 2014). One can say that CSR means an enterprise both fulfils its social obligations set by the legislation and voluntarily assumes extra social costs, taking into account not only the provisions of the laws but also ethical and moral considerations.

One can conclude that in a broader sense, CSR involves four interrelated areas: the environment, the economy, the public and employees (Table 1).

CSR practices in relation to employees mainly involve work safety, training, qualification development seminars, growth opportunities at the enterprise and regularly paid and fair wages, which allows the enterprise to reduce its employee turnover, contribute to the loyalty of its

employees and attract the best specialists (Kim H.R., Lee M. et al., 2010; Panagopoulos N.G., Rapp A.A. et al., 2015; Mueller K., Spiess S.O. et al., 2012; Bauman C.W., Skitka L.J., 2012).

Table 1

**Distinctive features of a corporate socially responsible enterprise**

Area	Characteristics	Author
Employees	Observance of human rights, regularly paid wages, employer-paid health and social insurance.	Birim B., 2016; Kim H.R., Lee M. et al., 2010; Panagopoulos N.G., Rapp A.A. et al., 2015; Mueller K., Spiess S.O. et al., 2012; Bauman C.W., Skitka L.J., 2012
Economy	Fair payment of taxes, creation of jobs, contribution to employment	Carroll A.B., 1999
Society	Sponsoring activities, support for various projects, grant programmes	Davis K., 1960; Bowen H.R., 1953, McGuire M.C., 1963
Environment	Activities to reduce negative impacts on the environment	Van Marrewijk M., 2003

*Source: authors' construction based on Birim B., 2016; Kim H.R., Lee M. et al., 2010; Panagopoulos N.G., Rapp A.A. et al., 2015; Mueller K., Spiess S.O. et al., 2012; Bauman C.W. & Skitka L.J., 2012; Bowen H.R., 1953; Davis K., 1960; McGuire M.C., 1963; Friedman, 1970; Carroll A.B., 1999; Van Marrewijk M., 2003.*

In the economic aspect, the key CSR priorities involve reducing the probability of crises (by means of a risk management strategy), paying taxes and fees to the government, ensuring social and economic stability and eliminating the "grey economy". Observing these principles contributes to attracting investor capital (Holme C., 2010) as well as receiving tax relief.

Enterprises also donate to charity, sponsor activities and financially support social welfare, safety and stability programmes at regional and national levels. The mentioned activities are aimed at supporting social projects in such fields as culture, sports and education.

In entrepreneurship, environmental responsibility is also considered to be a voluntary initiative that exceeds the standards set by the

provisions of laws being in force in the field of environmental protection. A lot of enterprises start actively implementing technological activities aimed at saving energy, water and other resources (Global Corporate Sustainability..., 2013).

One can conclude that even though there are diverse definitions of CSR, the key purpose of CSR is to achieve sustainable social development, which is understood as meeting the needs of the current generation without harming the ability of future generations to meet their needs. In the result, CSR becomes a new business philosophy, according to which enterprises focus on the achievement of public goods and the maintenance of environmental stability in their activity. This means that the purpose of an enterprise is not only profit-making but also contribution to the society (Asaul A.N., 2009), which results in increase in productivity, client loyalty and reputation and in sustainable development (McElhaney K., 2009; Pivato S., Misani N. et al., 2008; Sakarya S., Bodur M. et al., 2012).

**2. Corporate social responsibility in the banking sector in Latvia**

The banking sector in Latvia started implementing CSR activities quite late. The financial crisis in the end of 2008 caused a decrease in the trust of consumers in the banking sector. For this reason, the banks were forced to integrate social responsibility principles in their operation, including developing socially responsible financial products and making socially responsible attitudes to their employees and the public.

An examination of CSR in the banking sector was based on a case study, for which four banks were selected: Swedbank, Rietumu Banka, SEB Banka and ABLV Bank, which, according to data of the Association of Latvian Commercial Banks were the most profitable banks in Latvia in 2015. The examination of CSR was also based on four

areas: employees, the environment, the economy and the public.

**Employees.** In relation to employees, Latvia's legal documents have set high standards for work safety, working conditions, and the ethics of businesses and individuals in entrepreneurship practices. In Latvia, the relationship between the employer and the employee is regulated by the Labour Law (in force since 1 June 2002) and the Labour Protection Law (in force since 1 January 2002).

All the banks selected for the case study observed labour rights as well as organised extra activities for the purpose of raising the wellbeing of their employees, including various corporative and training activities to enhance the quality of the employees. ABLV Bank and SEB Banka placed a special focus on employee motivation (ABLV Bank covers their employees' life insurance with savings and also covers 5 % of their health insurance, while SEB Banka pays bonuses and gives extra benefits to long-term employees etc.).

SEB Banka actively participates in social projects and shares its experience, thus gaining recognition among the public and in the banking sector. In 2015, Global Finance magazine recognised SEB Banka as the best bank in Latvia, and it was ranked eighth in the top 101 most valuable enterprises. Based on a study by CV Online Latvia, the bank was also awarded as the second best employer in the financial sector. In 2015, the Ministry of Welfare granted SEB Banka the status of family-friendly company. This status is granted to enterprises that implement family-friendly policies in relation to both their clients and employees, providing services and an appropriate work environment.

**Environment.** The banking sector's performance in the field of environmental protection is regulated by the legal acts that stipulate the standards for waste management, water resource protection, emissions harmful to the environment and overall environmental

protection (the Environmental Protection Law, in force since 29 November 2006; the law "On Pollution", in force since 1 July 2001; the Waste Management Law, effective since 8 November 2010 and other laws). However, the banks implement extra environmental activities in order to lower their operational costs.

ABLV Bank, for example, implements optimum electricity and thermal energy consumption practices at its office building ("Smart Building"), practically avoiding any losses of the resources; the building is equipped with water taps with sensors, which allows reducing water consumption as well as the bank has a virtual data storage system and exploits work stations that reduce the consumption of paper, the number of pieces of equipment and the amount of wire.

Rietumu Banka participates in the Earth Hour campaign, focusing on climate change in the world and efficient resource use – the bank uses energy-saving office equipment and various digital solutions instead of printed documents. However, when choosing suppliers and cooperation partners, the bank assesses their economic activity impacts on the environment.

SEB Banka too focuses on the environmental aspect through introducing an electronic bill processing system, paper recycling bins, environment-friendly heating systems at its branch offices; besides, 45 % of the bank's automobile fleet has been replaced with environment-friendlier automobiles.

Swedbank cooperates with its clients and other stakeholders in respect to environmental protection issues, seeks to reduce and avoid environmental pollution, reduces electricity consumption at its offices and exploits the most electricity-efficient office equipment.

**Economy.** According to the Association of Latvian Commercial Banks, in 2015 the banks operating in Latvia paid in taxes (except the immovable property tax) EUR 141.5 million. The tax revenue consists of two components: the

individual income tax paid by employees and state mandatory social insurance contributions paid by employers.

ABLV Bank, which employs 690 employees, annually pays labour taxes totalling almost EUR 20 thou. per employee. Rietumu Banka employs a larger number of employees, approximately 800. The bank annually pays taxes amounting to EUR 13 thou. per employee. However, Swedbank, which employs about 2000 individuals, annually pays taxes totalling almost EUR 9 thou. per employee. SEB Banka annually pays a similar amount of taxes per employee – slightly more than EUR 9 thou. SEB Banka's personnel totals 1050 employees.

The mentioned facts are supported by the banking sector's profit performance (Table 2).

Table 2

**Case study on the profit performance of selected banks in Latvia in 2013-2015, mln EUR**

Bank	2013	2014	2015	2015/ 2013, %
Swedbank	112.85	115.89	130.64	+15.7
SEB Banka	23.75	24.67	31.43	+32.3
Rietumu Banka	55.09	53.62	74.25	+34.8
ABLV Bank	44.42	66.22	69.04	+55.4

*Source: authors' calculations based on ABLV Bank, Rietumu Banka, SEB bank and Swedbank data*

In 2015, Swedbank made a profit of EUR 130.64 million, which was 15.7 % more than in 2013. It was followed by Rietumu Banka whose profit totalled EUR 74.25 million, which was 34.8 % more than two years ago, and ABLV Bank whose income was EUR 69.04 million, which was 55.4 % more than in 2013. Overall, Latvia's banking sector performed well in 2015, making a total profit of EUR 415.9 million.

The economic performance of the banks is demonstrated by the number of their clients, which varied in the period of analysis (Table 3).

**Case study on the number of clients of selected banks in Latvia in 2013-2015**

Bank	2013	2014	2015	2015/ 2013, %
Swedbank	944068	948044	954095	+1.1
SEB Banka	485513	485150	470842	-3.0
Rietumu Banka	27169	485150	28717	+5.7
ABLV Bank	26966	26341	25531	-5.3

*Source: authors' calculations based on ABLV Bank, Rietumu Banka, SEB Banka and Swedbank data*

The commercial banks still try to enter new markets and increase the number of their clients or retain the number of their current clients. This situation was influenced by the 2008 financial crisis, which is considered by many researchers to be one of the main causes that reduced the number of bank clients. For this reason, the banking sector more actively introduced a CSR strategy aimed at improving the banks' reputation. It was also influenced by stricter requirements set by the Bank of Latvia and stronger control over the banks by the Financial and Capital Market Commission due to the legalisation of funds acquired in a criminal way, which contributed to a decrease in the number of non-resident clients. Servicing non-residents is one of the key operations, for example, for ABLV Bank and Rietumu Banka.

Totally, the number of bank clients in Latvia reached 2.3 million at the end of 2015. Despite the overall negative trend, Swedbank and Rietumu Banka increased the numbers of their clients, compared with 2013. Swedbank had the largest number of clients, which accounted for more than 42 % of the total bank clients in this sector at the end of 2015. The number of clients plays an important role in the sustainable development of a bank, as it affects the bank's revenues and therefore profit.

**Public.** ABLV Bank supports various events that are important for the public (concerts, guest performances, exhibitions). In 2006, the bank established the ABLV Charitable Foundation, which focused on four areas: "Children and the

Family", "Contemporary Art", "Education" and "Urban Environment". Since its establishment, the Foundation has supported 270 projects, granting funds totalling more than EUR 2.5 million. For charity and socially important projects in 2015, the ABLV group's enterprises granted funds amounting to more than EUR one million. Along with such projects as help for children with hearing impairment and children from poor families, support for contemporary art and the formation of a modern urban environment in Riga, ABLV Bank donated funds to a number of embassies of the Republic of Latvia, thereby helping the government hold the 18<sup>th</sup> November Holiday and popularising the state beyond its borders.

Rietumu Banka too supports cultural events – festivals and exhibitions – as well as founded a charitable foundation in 2007.

Swedbank actively takes part in social projects and charitable foundations that are based on Swedbank's values and priorities in four key areas for support: financial education, education development, sports and society. The bank has introduced a grant programme "Atsperiens" (Take-off) (for the expansion of small and medium enterprises, as well as for motivating the residents who have left the country to return to Riga and start up their own business). The bank cooperates with Latvia's universities, assists them in enhancing their technological resources for studies as well as cooperates with the charitable portal [ziedot.lv](http://ziedot.lv).

SEB Banka actively supports projects oriented towards the growth of future generations. The support strategy and the investment mission of SEB Banka are "The Future is Formed Today". The bank prefers developing projects that lay strong and stable foundations for entrepreneurship growth, contributes to the living conditions of children and youth, promotes education and builds up bank clients' knowledge. By supporting various programmes and projects, SEB Banka assists entrepreneurs not only in

getting finances but also in acquiring knowledge, which could help contribute to the society's wellbeing in the future.

SEB Banka persistently supports social organisations that are engaged in tackling problems important for the public. The bank supports Mentor Latvija – an organisation that helps youth start an independent life and acquire the necessary practical knowledge for it. The Association SOS Children's Villages Latvia, which takes care about children so that they can spend their childhood in families, and the public association "Dzivesprieks" (Joy of Living), which helps youth who have a tough beginning of their life due to various reasons and provides an opportunity for the youth to become normal members of the society. The bank actively shares its knowledge, for example, through annually engaging its employees of all levels in the "Shadow Day". During the Financial Literacy Week, the bank's experts deliver lectures and hold seminars, educating youth and building up their money use skills. In cooperation with the Vitols Foundation, the University of Latvia Fund, the Latvian Academy of Arts, the Riga Stradins University Fund and the association "Dzivesprieks", annually 25 students are paid scholarships. To contribute to sustainable education, the bank cooperates with the Sustainability Centre of the Stockholm School of Economics in Riga in order to strengthen the sustainability of Latvia's business environment and to contribute to the understanding of entrepreneurs about the positive business effects of socially responsible actions. Strong and developed culture is the basis for a sustainable society. Already since 2007 the bank has been the largest sponsor for the chamber orchestra Sinfonietta Riga and the Latvian Contemporary Art Festival held in Cesis.

Since 2001, SEB Banka has been the key sponsor for the annual mountain bicycle marathon SEB MTB. Through supporting sports, including the Latvian Tennis Union, the key focus

is placed on popularising healthy lifestyles, especially among children and youth. In forming a sustainable environment, a large role is played by the involvement of the public; therefore SEB Banka regularly involves its bank clients and employees in social activities. In addition, SEB Banka held charitable dinners in the last three years; during the dinners funds were raised for some charitable organisation. The culture of donation and compassion is also promoted through associating the SEB MTB with the Association SOS Children's Villages Latvia – the participants have an opportunity to get familiarised with the SOS children's villages when registering for the bicycle marathon.

In 2015, taking part in the international campaign Client Day, SEB Banka encouraged its clients to use internet banking and payment cards for making daily payments; the bank donated four cents for charity from every transaction made during that day. For four years already, instead of ordinary presents for Christmas, SEB Banka has given charitable presents – symbolic keepsakes created in cooperation with some charitable organisation – to its clients, thus requesting the clients to support the organisation. For several years now, SEB Banka has donated funds to some organisation, which met the SEB group's support strategy guidelines, instead of giving its largest clients presents at important social events, thus encouraging the others to do the same.

Implementing CSR activities, one can identify a number of advantages for the sustainable development of banks.

First, a bank's profit and its growth pace increase (Gras-Gil E., Manzano M.P. et al., 2016). This is shown by Swedbank's performance – including financial performance, e.g. its capital adequacy and liquidity ratios exceeded many times the minimum ratios set by the legislation. As of 31 December 2015, its capital adequacy ratio was 39.28 % (the minimum ratio was set at 8 %), while its liquidity ratio stood at 54.24 %

(the minimum ratio was set at 30 %). The profits of the banks examined also tended to increase. Scientists emphasise that CSR actions are oriented towards long-term gains rather than fast profit-making (Choi B.B., Lee D. et al., 2013; Gras-Gil E., Manzano M.P. et al., 2016).

Second, by introducing CSR, it is possible to reduce costs (Baron R.M. & Kenny D.A., 2001), including operational costs; for example, if the amount of waste is reduced or if the waste is recycled, the efficiency of consumption of electricity rises. Rietumu Banka uses various digital solutions instead of printing documents; consequently, the consumption of paper declines as well as its office costs are reduced. However, the managements of the banks face problems to calculate their potential gains or losses, as the results depend on the engagement of their employees and clients in this process, which is difficult to predict.

Third, the reputation of a bank (Grigore G., 2009; Orlitzky M., Schmidt F.L. et al., 2003) that helps develop and enter new markets and attract and retain employees improves, as individuals prefer working for enterprises whose values match their own ones (Ghadi M.Y., Ferdinando M. et al., 2015). The number of claims from the regulatory institutions, which are the Bank of Latvia and the Financial and Capital market Commission, decreases as well.

Fourth, sales might increase, as the loyalty of clients rises. Clients wish to know whether products or services are produced in a responsible way towards the environment and other social aspects. A few clients are even ready to pay more for "responsible" products. Therefore, the quality of products or services is enhanced through implementing CSR programmes, which has been proved by a study on corporate reputation in the banking sector in Latvia, which is annually conducted by the research company TNS in association with the Association of Latvian Commercial Banks (Korporatīvas reputācijas pētījums..., 2014).

Overall, by means of their economic activity, the banks develop Latvia's export potential and pay a significant amount of taxes to the government, thereby considerably contributing to the stability of Latvia's economy in future. Each of the selected banks believes it is the duty to support projects oriented towards the growth of future generations, thereby fostering the sustainable development of the bank.

### Conclusions, proposals, recommendations

- 1) Corporate social responsibility becomes increasingly popular in entrepreneurship and research; however, no single understanding and definition of this term exists yet. In a broad sense, the term corporate social responsibility relates to four key areas: employees, the economy, the public and the environment.
- 2) The case study revealed that the most extensive activities regarding corporate social responsibility were implemented in respect to the environment and the public. This may be explained by the fact that Latvia's legislation has set strict requirements for enterprises concerning environmental protection. However, the banks' corporate social responsibility programmes oriented towards raising the wellbeing of the public involve extra costs, which increases the loyalty of both their clients and employees to the banks.
- 3) Latvia's legislation strictly regulates the relationship between the employer and the

employee, yet the banks assume extra responsibilities in respect to their employees, holding corporate and training activities and introducing a motivation system that involves, for example, level 3 pension schemes or life insurance with savings. In such ways the banks try to attract highly qualified and motivated employees.

- 4) The sustainable development of banks is strongly associated with their profits. In recent years, the banking sector in Latvia grew fast and reported stable financial performance; in 2015, the banking sector's profit reached EUR 416 million. In 2015, the greatest profit was reported by Swedbank; its profit totalled EUR 130 million, which accounted for 29 % of the total profit of the sector. This means that the larger profit a bank makes, the greater opportunities for the bank to implement corporate social responsibility programmes.

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