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DIFFERENTIATING BETWEEN SINCERE AND INSINCERE CORPORATE SOCIAL RESPONSIBILITY (CSR): EVIDENCE FROM THE GERMAN BANKING INDUSTRY

1. INTRODUCTION

Firms have fully understood the benefits of accommodating their communication strategy to the increasing demands of society as regards business ethics and corporate responsibility. The space they devote to these issues in their annual reports is bigger and bigger, and their discourse is not only about pious intentions but also about implementation. Similarly, scholars try to apprehend this reality with an ever wider range of concepts: social responsibility, social responsiveness, corporate citizenship, etc. The problem is that this mutual sophistication makes it increasingly difficult to differentiate between firms that are sincerely engaged in Corporate Social Responsibility (CSR) and those that use this concept as a mere window-dressing for marketing purposes.

Within this context, this paper will show how to discern the difference between them in the case of the banking industry. Taking the concrete case of Germany,

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four different types of banks will be analyzed: the three traditional groups used by the German Central bank (Commercial, Cooperative and Savings Banks) and a new type of bank which emerged in the 1980s: ethical banks. For each of these four types of financial institution, the main objective is to see if there is a difference between, on the one hand, what the banks *say* they do (through analysis of CSR policies in their annual reports) and, on the other hand, what the banks actually *do* (through analysis of their financial statements).

The results will lead us to conclude that a sincere commitment to CSR involves a substantial change in the business model. Is that necessarily the future of ethical approaches to business? Should it be the same for all types of firms? A debate will be opened. In the meanwhile, an analysis of the banking industry shows that only a few institutions are ready to take a step forward in this direction.

The aftermath of the subprime mortgage crisis has accelerated the pre-existing process of an ethical approach in the banking industry. Today, all banks claim to be socially, environmentally and economically committed to the philosophy of sustainable development and sustainable finance. Nevertheless, the present paper will show that, beyond outward similarities, there are two major types of banking approaches, each reflecting a distinct business model. On the one hand, there is a number of banks whose ethical/social approach is mainly based on *what they say*. This is mainly the case of commercial banks (i.e. shareholder-based banks), which usually demonstrate outstanding CRS reporting but are not ready to change in depth their traditional business model. On the other hand, there are banks whose ethical/social approach is based on *what they do.* This can be illustrated by a new and still fairly unknown type of bank which emerged in the mid-1980s: the so-called ethical bank. They publish modest CRS reports but as an analysis of their financial information shows that, in their banking practice, they go far beyond other banks in the objective of socially responsible finance.

The present paper will thus explore new methods on how to differentiate between sincere and insincere commitment with CSR. It is organized as follows: after these few introductory words, the following section will set up the theoretical framework. Section three will then explain the methodology used. Section four will analyze the main features of mainstream banking. Finally, section five will show the contours of alternative banking and its consequences.

2. THE THEORETICAL FRAMEWORK

Social demand for ethics vis-à-vis corporations is not new. Industrial accidents like those of Chernobyl and Bhopal, or simply the everyday pollution created by manufacturing plants on our doorsteps, have laid the foundations of growing

community awareness as regards environmental issues. Similarly, accounting scandals such as those of Enron or WorldCom, have stirred the demand for corporate responsibility beyond the financial sphere. The resulting pressure of public opinion has forced firms to reconsider their role in society. Today firms cannot be envisaged any more as a passive spectator of what happens around them, but rather as an active social actor. Consequently, we are witnessing major changes not only in the managers' way of thinking but also in the theoretical framework that describes the relationship between firms and society.

The status of corporations in society is shaped by one fundamental question: do they exist only to create wealth for shareholders? Or does good corporate governance demand that a firm's board of directors also consider the interests of other stakeholders (ultimately society at large)? In this regard, it is interesting to note that at the beginning of the modern industrial era scholars did not see any seeming contradiction between individual (firms') wealth and collective (social) welfare. Adam Smith in particular made it utterly clear that, through the "invisible hand", individual profit seeking will invariably lead to the most efficient allocation of resources and, therefore, it will result in the greatest utility for the whole society (Smith, I, 7).

With the passage of time, the fact that the marketplace conditions described by Adam Smith rarely matched reality made this apparent convergence of interests collapse. Accordingly, the role and nature of the corporation as regards society opposed two different views: shareholder primacy theorists on the one hand, and social welfare theorists on the other. Proponents of the first school, best endorsed by Milton Friedman's famous article "The Social Responsibility of Business is to Increase its Profits" (1970), contend that the primary purpose of a company is to maximize shareholder wealth. Any other activity diverting from that focal goal would be considered a waste of resources and would weaken the competitive power of the company. Even if any stockholder can personally use his dividends to support any social cause he may choose, at the corporate level the firm has no competence to handle social problems related to the general public. This latter task is not the responsibility of business organizations, but of governments.

Conversely, supporters of social welfare theory advocate for a broader notion of corporate responsibility. Public opinion, which ultimately makes the law, can view corporations as economic institutions acting not only in a given marketplace, but also in a specified society. Consequently, firms have the right to make profits but also the obligation to provide certain social services. Shareholder wealth maximization might thus be tempered by some kind of moral commitment to social expectations. Howard Bowen's (1953) landmark book was probably the first to abridge these ideas into the specific concept of corporate social responsibility (CSR). Archie Carroll (1979; 1991) systemized further the notion of CSR by suggesting that the corporation's responsibility to maximize financial return to shareholders is just

a "bottom line". The overall picture of his pyramidal model expanded the firm's obligations towards the legal, ethical and philanthropic spheres. Finally, Edward Freeman's (1984) influential book deserves particular mention here because it helped to personalize the so far vague notion of social responsibilities. It was through the new term "stakeholder" that he delineated the specific groups that should be considered by the firm in its CSR orientation.

With the evolving process of globalization and the absence of a supranational governmental body with the authority to monitor the activity of transnational companies, attention was shifted from social responsibility to social responsiveness. This latter concept implied not only the condition of having assumed an obligation, but in compliance with ever growing expectations of the community, it also emphasized an action-oriented dimension of concrete implementation. Firms were thus confronted by the problem of determining to what extent this new focus on corporate social performance (CSP) would affect their financial results. A big debate was then opened around two main questions: Is CSP indeed related to corporate financial performance (CFP)? If so, what is the direction and the underlying mechanism that explain this relationship?

Despite the enormous bulk of surveys on this subject over the last 40 years, the empirical evidence put forward still remains inconclusive. A growing number of studies support the hypothesis of a positive CSP-CFP link (Schreck, 2011; Callan and Thomas, 2009; Peters and Mullen, 2009; Rettab et al., 2008; Orlitzky et al., 2003). They contend that companies firmly committed to being socially responsive are generally rewarded with better financial results. Reputation always being an important mediator in the relationship (Neville et al., 2005), it would seem that CSR and stakeholder satisfaction are "good for business". On the contrary, other scholars claim that CSP and CFP are negatively related (Garcia-Castro et al., 2009; Makni et al., 2008; Laan et al., 2007; Lopez et al., 2007). Most of them consider that a company engaged in CSP activities necessarily incurs additional costs that dilute its primary purpose, which is to maximize profits. So, according to this view, CSR "distracts" from business. There is even a third hypothesis, endorsed by some other authors (Soana, 2011; Magnolis et al., 2007; Aupperle et al., 1985; Abbott and Monsen, 1979; Alexander and Buchholz, 1978), for whom there is not a significant correlation between CSP and CSF.

There is thus considerable incertitude concerning the CSP-CSF relationship. It should be noted that the whole issue is affected by various methodological problems. For instance, there is little agreement among researchers as regards the definition and measurement of the two main variables at stake (CSP and CFP). This fact, in turn, raises questions of data reliability and comparability across studies (Margolis et al., 2007). And yet, there is a clear tendency in modern literature to consider that engaging in CSR activities can reduce costs and risk to a firm, thus enhancing its reputation and legitimacy and, ultimately, creating new competitive

synergies. One could even say that, after several decades of social activism, CSR has become a strongly institutionalized feature in mature economies (Brammer et al., 2012). The idea that corporations should engage in some form of responsible behavior has become a legitimate social expectation. This fact is illustrated by the diffusion of CSR departments within companies, the spread of stock market indices related to sustainability, the proliferation of social ratings and environmental standards, etc.

Interestingly, this prevalence of a CSR perspective in the current business environment has strongly attenuated the age-old opposition between shareholder primacy advocates and social welfare theorists, initially conveyed by authors such as Adolph Berle (1931) and Merrick Dodd (1932). Time passing, a subtle modification in the notion of what really constitutes shareholder wealth has led many contemporary scholars to believe that one can keep profit seeking as the primary goal of the firm while doing so in a socially responsible manner (Parkinson and Kelly, 2001). Michael Jensen (2001), for example, suggests that the ancient conflict between shareholder value and social responsibility can now be finally reconciled through what he calls "enlightened value maximization". This concept incorporates the basic tenets of stakeholder theory but specifies that long-term value maximization must be the firm's sole objective. Therefore, in this new enlightened form, social and environmental responsibilities are considered as legitimate means to the end of shareholder benefits. Somehow, the message is that companies must engage with Dodd's theory of social welfare in order to truly achieve Berle's concept of profit maximization. Eventually, this reconciliation of previously opposing perspectives is not without recalling the harmonious vision of society proposed by Adam Smith.

The problem is that this enlightened conception of CSR offers little practical guidance for managers' decisions where a tradeoff between competing stakeholder interests are to be made, especially in a medium or short-term horizon. From the Principal-Agent theory perspective (Jensen and Meckling, 1976; Eisenhardt, 1989), modern corporations are seen as a set of contracting relationships among individuals who have conflicting objectives. Managers, for example, might potentially seek to maximize their own utility at the expense of shareholders' interests, all of which does not necessarily enhance the company's long-term value. Likewise, we shall see in the following sections that even if the culture of "short-term profit at any cost" is now unanimously banished from the business vocabulary, there is still much "green-washing" in the actual business practice. Conceiving CSR in its enlightened form as a way to reconcile firms and society might seem at a glance a good idea, but it does not exclude "window dressing". Consequently, the traditional (not "enlightened") shareholder perspective is not as outdated as some would like us to believe. Friedman himself noted, on an interview reported by Joel Bakan, that this insincere CSR can be fully justified:

> "The executive who treats social and environmental values as means to maximize shareholders' wealth – not as ends in themselves – commits no wrong. It's like »putting a good-looking girl in front of an automobile to sell an automobile«, he told me. »That's not in order to sell pulchritude. That's in order to sell cars«." (Bakan, 2004, p. 34)

3. METHODOLOGY

Before going through the analysis, it first seems appropriate to clarify the methodology. In this regard, it has already been said that the main objective of this paper is to study how the banking industry conceives their business activities according to two different approaches. Each of these banking patterns is determined by taking into consideration two different types of variables, which in turn are measured by examining the different nature of their corresponding sources:

- *What they say.* – The banks' CSR discourse will be apprehended on the basis of their social and environmental reporting. Their promises at that level will then be compared with their practices for implementation. As a guiding tool, we have summarized the banks' CSR policies in Table 1, which is largely based on the method used by Bert Scholtens (2009). Despite its limitations, already pointed out by the author himself, this methodological framework has at least the advantage of being easy to apply to the different banks and hence gives us a common ground for assessing their CSR policy at a glance from a comparative perspective.
- *What they do.* – Beyond the narrative analysis of CSR policies, the reality of how banks are committed to sustainable finance is ultimately reflected in their financials. Three different types of documents will be analyzed: the balance sheet, the income statement, and the off-balance sheet.

The present study will be focused on the particular case of Germany. Several reasons justify this choice. First of all, Germany is a country with a fairly diversified banking industry. Unlike other European countries, there is one ethical bank in Germany: the GLS Gemeinschaftsbank, founded in 1992 with headquarters in Bochum. It should also be noted that Germany is one of the few countries where a sizeable group of savings banks with a distinct business model have been preserved (Ayadi et al., 2009). In a previous article (Relano and Paulet, 2012), ethical banking had already been compared with commercial and cooperative banks, but savings banks had then been ignored. Particular attention will thus be given here to this group in the comparative analysis with ethical banks. Finally, the present article will explore new methodological devices. Choosing again the same country is thus a way of testing the explanatory power of the methodology itself.

The study of the German banking industry will be conducted at two different levels. On the one hand, the whole sample of German banks displayed in its different categories will initially be considered for comparative analysis. On the other hand, and as a means of putting a concrete "face" on each of the above-mentioned categories, a study of some concrete financial institutions will be proposed. Let it be recalled, for example, that the GSL Bank is the only existent representative of ethical banks in Germany. To carry out some comparisons with specific individual institutions of the other baking categories seemed then the most appropriate in certain cases. Both levels (general and individual) are in fact complementary and mutually reinforcing as regards the main hypothesis and the final conclusions.

4. MAINSTREAM BANKS: CSR AS A MARKETING DEVICE

To say that banks really care about sustainable development has now become commonplace (Jeucken, 2001). They all claim to be the most virtuous institutions as far as the environment and society are concerned (Saeed, 2004). Plenty of initiatives are indeed addressed to these matters. In terms of the environment, for instance, many banks would put forward their commitment to reducing their consumption of electricity by using energy efficient bulbs or their efforts in recycling paper from photocopies. Active employee travel policies with respect to commuting or with fair gender/race representation in the institution are not exceptional any more (Giddings et al., 2002). Nevertheless, all these actions just concern the direct impact of banks on the planet and society. Most of them are fairly easy to implement and are not very expensive, giving moreover an instantaneous "green image". But they are not the most important to take into consideration. Far more critical, though less visible, is the indirect impact of banks through the clients and projects they finance. Notice that, without intermediary financial institutions like banks, the Three Gorges Dam on China's Yangtze River, or the Baku-Tbilisi-Ceyhan oil pipeline, linking the Caspian Sea to the Mediterranean, would never have been possible. When civil society realized this, pressure for recognition of environmental and social responsibility largely shifted from the heavy industry to the banking sector. The so-called Collevecchio Declaration (2003), a global coalition endorsed by more than 200 organizations to promote sustainable finance in the banking sector, is in that sense an outstanding example.

The response of the banking industry to this challenge did not take long to come. In June 2003, ten of the world's largest banks launched the so-called Equator Principles, which is a set of environmental and social benchmarks for managing environmental and social risk related to project financing. Another important tool used by banks for complying with the demand of social and environmental accountability, but which now falls within the investment domain, is Socially

Responsible Investment (SRI). The idea is not new. It had emerged in the US by the end of the 1920s, but its exponential development has coincided with the recent success of concepts such as business ethics and socially responsible finance (Loiselet, 2000). So, in a similar manner as firms have been trying to comply with the goals of sustainable development through the concept of CSR since the 1990s, banks have been attempting to fulfill this very same demand since the 2000s by means of different devices adapted to the financial domain. Some of the most important ones are listed in the first column of Table 1.

Table 1. CSR performance of different types of banks (2011)

	Deutsche Bank	Volksbank Baden Baden	Landesbank Baden-Würtenmberg	GLS Bank
1. Sustainability report	1	1	1	1
2. ICC Business Charter on Sustainable Dev.	0	0	0	0
3. UNEP Finance Initiative	1	0	1	1
4. Equator Principles	0	1	0	0
5. Global Compact	1	0	0	1
6. “Who Cares Wins” report	1	0	0	0
7. Certified environmental management	0	1	1	1
8. Certified environmental management	1	0	1	0
9. Environmental policy	1	1	1	1
10. Supply chain management	1	0	1	0
11. Quantitative environmental targets	1	0	1	0
12. Transparency of environ. performance	1	1	1	1
13. Environ. risk management in loans	1	1	1	1
14. Exclusion of specific sectors	1	1	1	1
15. World Bank guidelines	1	0	1	1
16. OECD guidelines	1	0	1	0

	Deutsche Bank	Volksbank Baden Baden	Landesbank Baden-Würtenmberg	GLS Bank
17. Socially responsible investing (SRI)	1	1	1	1
18. Socially responsible saving	0	1	0	1
19. Sustainable financing	1	1	1	1
20. Microcredit	1	0	0	0
21. Environmental advisory services	1	0	1	1
22. Climate products	0	0	1	1
23. Other sustainability products	1	0	1	1
24. Sponsoring (NGOs, community,…)	1	1	0	0
25. Community involvement	1	1	0	0
26. Training on SD to employees	1	1	1	1
27. Diversity and opportunities	1	1	1	1
28. Feedback from employees	0	1	0	1
29. Business ethics principles	1	1	1	1
Total	**23**	**16**	**21**	**19**

Source: annual reports of banks

If we check to what extent the different types of banks apply these elements, simply by giving them a "digital" score (0 or 1) according to their compliance or not with the issue under consideration, it appears very clearly that Deutsche Bank is the most virtuous institution in terms of responsible finance, with a total of 23 points (see tab. 1). Contrary to popular belief, Table 1 also shows that cooperative banks are not always the champions of CSR. Finally, it is worth noting that Deutsche Bank publishes annually a specific CSR report of more than 100 pages and a separate web site is devoted to their corporate responsibility, whereas the *Nachhaltigkeitsbilanz* of the GSL Bank is just a two-pages-chapter of its corporate report. More generally speaking, commercial banks are normally very good in communicating about CSR. The problem is that this ostentatious proclamation of good intentions on sustainability is often used for "greenwashing" purposes. In many cases there is a gap between what the banks say and what they actually do in their in their day-to-day practice.

It is indeed fairly easy for a bank to announce its commitment to responsible finance as a primary goal of their overall strategy. It suffices to issue a certain number of ethical funds, to devote some money to social patronage, to promote a number of internal environmentally-friendly attitudes, to pronounce adherence to international principles which do not compromise the core of the business, and finally to publish an annual extra-financial report in which all these initiatives are highlighted. But one thing is to "look green" and another quite different to "be really green". A pioneering critical study entitled *Shaping the Future of Sustainable Finance* (Durbin et al., 2006), gives clear evidence that the above-mentioned initiatives are no guarantee of sincere commitment. After reviewing the environmental and social policies adopted by 39 key banks from around the world, their conclusions are not very promising. It seems that banks are adopting an environmental rhetoric with little commitment to changing their performance. With few exceptions, bank practices are lagging significantly behind relevant international standards.

The critical point is implementation. Writing in an isolated office about CSR policies is far easier than putting it into every-day practice. In that sense, a considerable number of commercial banks seem not to realize the contradiction existing between their CSR policies and some of their investing and financing decisions around the world. Three examples will illustrate this point for the case of Deutsche Bank (Van Gelder and Denie, 2007, pp. 116–137). The first concerns the production of cluster munitions. Due to the indiscriminate targeting of this explosive device, civilians account for 98% of the victims and thus represent a direct contravention of international humanitarian law. Despite this, Deutsche Bank has repeatedly given credit facilities to various producers of this weapon, like Textron or Rheinmetall. Likewise, Deutsche Bank has contributed to financing the controversial mining techniques of the American company Freeport McMoran, which are devastating extraordinary diverse ecosystems and unique endemic species in New Guinea. Finally, it is not anodyne to note that Deutsche Bank was the only Western bank to hold the accounts for the Central Bank of Turkmenistan during the period of Saparmurat Niyazov, a notorious dictator and leader of an oppressive regime violating the human rights of its citizens. And yet, the German institution has never clarified how this financial support for Niyazov's Turkmenistan fits with its voluntary human rights commitments under the UN Global Compact.

There is thus an obvious gap between the theoretical intentions on sustainability, as expressed in the CSR reports, and the practical consequences of certain financial activities. The main reason explaining this inadequacy is that commercial banks have tried to satisfy the customer's simultaneous demand for profitability and ethics. Unfortunately, this is just not possible, at least in the short term. So those banks which are not ready to renounce the dogma of maximization of profits can only be engaged in the idea of sustainable finance in a rather superficial

manner. This is so far the most common attitude amongst commercial banks. Obviously, most of them offer their clients the possibility of investing in a wide range of ethical funds and do have a number of credit lines especially devoted to environmental or social issues. But their general strategy has not changed. In their mind, the development of these new products must nonetheless serve the main invariable objective: more shareholder benefits. In fact, since the idea of greening the environment is now in fashion, commercial banks have used this tendency to win new clients and to cover a new demand, and thus make still more profit.

A simple way of checking if the CSR policies of a given bank are really integrated in the day-to-day operations is to examine the coherence of "good intentions" with banking practice as reflected in their financial statements. So moving from theory to practice, we will first analyze the balance sheet, the income statement and the off-balance sheet of the entire sample of German banks. Table 2 summarizes this information. The asset side of the balance sheet shows the following parameters: interbank operations, loans, financial participations and reserves. All figures reflect the percentage of each parameter to total assets. On the liabilities side, the following items are considered: interbank operations, deposits, financial transactions and equity. The figures are also calculated in terms of percentage to total liabilities.

Table 2. Financials Structure of various types of banks (in %, 2011)

	Assets				**Liability**				**Off-BS**
	Interbank	**Loans**	**Financial**	**Reserves**	**Interbank**	**Deposits**	**Financial**	**Equity**	
Germany									
Commercial	29	37	28	8	24	30	41	5	Assets x 5
Cooperative	24	49	22	5	30	30	34	6	Assets x 4
Savings	20	65	12	3	14	64	14	8	= Assets

Source: Deutsche Bundesbank 2011.

Focusing initially on the category of commercial banks, the first thing to notice is that the difference between client transactions on the assets side (loans) and on the liabilities side (deposits) is negative. This means that there is a deficit of resources due to a dominance of credit granting activities. This is fairly characteristic of commercial banks. A similar reasoning actually applies to the category of cooperative banks. The case of saving banks is somewhat different, namely because the difference between deposits and loans is quite the reverse. This

means that, when compared with their universal and cooperatives peers, savings banks are more focused on collecting deposits.

Another element worth examining is the level of financial transactions. As Table 2 shows, this item is considerably high in the case of commercial banks, both in the assets and liabilities sides. This fact clearly illustrates that raising capital from global financial markets is the core activity for this type of financial institution. Once again, cooperative banks do not seem very different in this regard, showing percentages slightly lower than commercial banks. Only savings banks, with percentages under 15%, seem somewhat at variance. This means that rather than focusing in the speculative operations of artificial secondary financial markets, the main activity of savings banks is concentrated on the traditional business of banks: savings collection and credit distribution. So much in line with their historical mission, savings banks are the champions of German retail banking.

The evidence which can be grasped from the column devoted to the off-balance sheet is very much in line with the previous argumentation. As can be seen in Table 2, the value attained by this item represents five times the value of the total assets in the case of commercial banks and four times in the case of cooperative banks. Nothing similar is observed in the off-balance sheet of savings banks. Since their financial transactions are more reduced and their core business is still locally oriented, it is not surprising to attest that their off-balance sheet does not exceed the value of the total assets.

All these facts seem to draw a panorama of the German banking industry where commercial and cooperative banks show a similar – though not exactly the same – business practice. Only savings banks are somewhat at variance from this mainstream model. The next section will show that this picture is incomplete and not entirely accurate. There is still another type of bank to be considered, ethical banks, whose CSR policies and banking practice still differ more radically from the mainstream business model.

5. ETHICAL BANKS: SINCERE CSR AS A *RAISON D'ÊTRE*

This section will demonstrate that ethical banks can be considered as a real alternative to the business model of conventional banks. They actually play the role that cooperative banks do not play anymore. Schulze's and Raiffeisen's original initiatives came to light because the existing institutions of their period failed to meet a segment of the population's needs and aspirations. Similarly, ethical banks were created in the mid- 1980s in response to a particular market niche so far unfulfilled: people who wanted to give real sense to their money and did not believe any more the good intentions generally conveyed by traditional banks in their CSR policies which are not followed by facts.

Without going into full details as regards their precise characterization (Relano, 2008; De Clerck, 2009), it is worth noting that the main difference of ethical banks is not based on the size of their CSR report. Since, as already seen, to obtain the appearance of a "green bank" is quite simple and not necessarily very expensive, ethical banks are not interested anymore in declarative paper policies. Table 1 shows that, in this regard, ethical banks are less performing than commercial banks. This is because they make little effort in communicating how virtuous they are in terms of social/environmental sustainability. Beyond the CSR rhetoric, ethical banks prefer to focus on the real impact of their banking activities.

The major divide of ethical and mainstream banks comes from a simple paradoxical fact: it is just impossible, at least in the short term, to satisfy the customers' simultaneous demand of increasing financial returns on the one hand, and greater ethical, social and environmental involvement on the other. In the face of such a conflicting dilemma, commercial banks have clearly taken up a stance in favour of profit maximization. Owing to the process of semi-demutualization and mimetic isomorphism, cooperative banks are increasingly making similar kinds of choices (Redler, 1994; DiMaggio and Powell, 1983; Cf. Palomo and Carrasco, 2001). Let us take, for example, the case of Dutch Rabobank, the most important cooperative banking group in Europe. Despite being a signatory of the Equator Principles and the general tenet of their CSR discourse, this bank is actively involved in the financing of the Singaporean company Wilmar International, whose activities in the palm oil business are clearing tropical forests and destroying endangered species like the orangutan (Van Gelder, 2007). More recently, US and European regulators have fined Rabobank over $1 billion for "inappropriate conduct" in a scam to manipulate the London Interbank Offered Rate (Libor). It is easy to say, afterwards, that such behavior is entirely contrary to one of their core values: integrity.

Beyond the pious words of moral declarations, ethical banks are the only financial institution to put profits at the service of ethics not just in theory but also in practice. They believe that profitability should not only be measured in terms of financial performance. Social and environmental returns should also be taken into consideration. In other words, ethical banks integrate ethics within their whole financial project. They are thus ready to accept the idea of working with narrower profit margins if this is compensated by further social or environmental added value. It would not be surprising, for instance, that they accept working with lower levels of financial collateral or higher monitoring costs if the project they finance is worth it in social or environmental terms. For ethical banks, this leading principle can be summarized in one single maxim: less profit, more sense.

In more precise terms, one of the most outstanding facts that make ethical banks different from other banking institutions is that they usually refuse to participate in the speculative operations of the financial market. Consequently, ethical banks

avoid investing in complex financial instruments that promise high profits but also imply greater risk. They consider that this economic logic is responsible for many international crises, social inequalities, ecological problems, etc. Ethical banks can occasionally hold financial products until maturity to cover potential liquidity needs, but unlike their traditional counterparts, their participation in the stock market is generally insignificant and confined to long-term and non-speculative operations.

As a result, ethical banks concentrate their activities on retail banking. In this regard, ethical banks privilege the social, ethical or environmental dimension of the projects they finance. So, unlike traditional banks, whose lending policies are normally based on a single bottom line screening (assessing exclusively the financial performance), ethical banks usually put in place a triple bottom analysis (environmental, social and financial performance). Particular attention is thus given to projects in areas such as social and ecological housing, organic farming, renewable energies, small and medium-size companies, etc. In these domains, ethical banks are ready to take higher risks and accept funding certain projects which have been previously refused by traditional banks. More generally speaking, ethical banks encourage solidarity between depositors and borrowers to enable loans at reduced interest rates for projects which are worthy in social, ethical or environmental terms. Eventual problems of imperfect or asymmetric information are counterbalanced by the general policy of focusing their activities at the local or regional level. It is because they know very well the region, the projects and the people they finance that social banks are ready to take higher risks. Very much like the original cooperative movement in the 19th century, this is entirely consistent with their community involvement.

All these characteristics shape a distinct business model, which is ultimately reflected in the structure of their financial statements. Table 3 shows the results of applying our analytical grid to the case of GLS Bank. If we make a comparison with the other two banks, one may immediately notice that, like cooperative banks, the balance between the client transactions on the liabilities side (86%) and the assets side (76%) is positive. This means that there is a dominance of savings activities. As far as the financial transactions are concerned, one can easily observe the existence of extremely low percentages (the exact figures are 0.57% on the asset side and 0.06% on the liabilities side). This fact indicates that, unlike other financial institutions, the participation of GLS bank in the global financial market is negligible.

Most importantly, Table 3 shows that GLS Bank does not conduct its business in the same manner as others banks do. If a final piece of evidence were necessary, it suffices to note that the value of the off-balance sheet in the case of GLS Bank bears no comparison to that of Deutsche Bank. The total amount of financial products contracted by GLS Bank to hedge the institution against different kinds

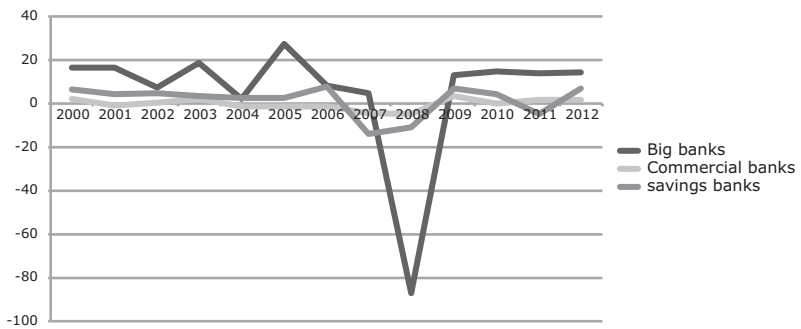
of risks just represents 13% of their total assets, whereas it is more than 500% in the case of Deutsche Bank (and it was still much higher before the subprime crisis). Big universal banks like Deutsche Bank are thus very dependent on the income resulting from their trading activities. In this regard, graph 1 show how the financial part of the operating income in case of the top five German banks (*Großbanken*) varies a great deal through time depending of the overall macroeconomic situation. Quite the opposite, the negligible participation of ethical banks in trading activities makes this type of institution very stable through time, whatever the global financial context (Paulet and Relano, 2011).

Table 3. Balance Sheet Structure: Deutsche Bank and GLS Bank (2011)

	Assets				Liability				Net income/ net interest income	Off-BS
	Interbank	Loans	Financial	Reserves	Interbank	Deposits	Financial	Equity		
Deutsche Bank	10	17	61	12	16	27	47	8	62	Assets x 5
Landesbank Baden Wûrtemberg	17	32	31	20	20	40	31	9	12	= Assets
GLS	24	76	1	8	7	86	0	7	80	13% Assets

Source: Own calculations, Annual reports of banks.

Figure 1. Net result from trading portfolio as a percentage of operating income



Source: Deutsche Bundesbank.

Leaving aside big commercial banks, the comparison of ethical banks with savings banks deserves particular attention. As already mentioned, both types of institutions are local and retail oriented. Unlike traditional commercial banks, both are also governed by a broader objective function than being merely profit or shareholder-value driven. Moreover, one can easily convey that both are inclusive financial institutions, savings banks focusing mostly in the dimension of financial exclusion and ethical banks in the sense of environmental and social criteria. And yet savings banks and ethical banks are not at all the same type of financial institution. The main difference is that the business model of savings banks still includes a significant part of operations in the financial market. In Germany, this kind of activity is carried out by Deka Bank, which on behalf of the whole savings bank group operates at a national level as a provider of investing products. Graph 1 illustrates this situation very well. The income of savings banks originating from trading activities is not comparable with that of big universal banks, but it is still noteworthy. Let it also be mentioned that the off-balance sheet of savings banks (attaining the same size of their total assets) is not as important as that of other types of banks, but it is still quite substantial, especially if compared with that of ethical banks (see tab. 2 and 3). Finally, it is perhaps not anodyne to state that the savings banks group has been indirectly affected – through the *Landesbanken* – by the financial turmoil associated with the subprime crisis.

Nothing of all this is to be seen in the case of ethical banks. Note that savings banks are indeed different from their cooperative and commercial peers, but still work within the same business model. They just represent variations within the same paradigm. Only ethical banks are really at variance in all respects. Since what really matters is not how banks use and distribute their profits, but rather how they earn their money, ethical banks represent an alternative distinct model to mainstream banking.

6. CONCLUSION

Ethical banks, commercial banks, cooperative banks and savings banks are all regulated by the same authorities. They all have to abide by the same rules and to compete in the same marketplace, but they are not essentially the same kind of financial institution. When looking at their sustainable development reports or their CSR communication, one might indeed be confused as to who is more deeply and sincerely committed to the perspective of responsible finance. But as the evidence of the financials shows, only ethical banks really "do" what they "say". This is because their business model is substantially different.

The performance of ethical banks shows that sincere commitment to CSR makes business sense. This does not imply, however, that all financial institutions should

be ethical. In fact, non-sincere CSR commitment also makes full business sense to other segments of banks. In any event, financial pluralism is reinforced and, as textbooks in finance regularly state, the more diversified a banking industry is in terms of size, ownership, and business structure, the smaller is the systemic risk. There is thus a case for maintaining the pioneering business model of ethical banks, even if, ultimately, it is up to customers to decide the sense they want to give to their money.

Abstract

This paper analyses the difference in the CSR commitment between different types of banks, based on the German example. It compares the three traditional groups (Commercial, Cooperative and Savings Banks) and a new type of bank which emerged in the 1980s: ethical banks. For each of these four types of financial institution, the main objective is to see if there is a difference between what the banks declare (through analysis of CSR policies in their annual reports) and what the banks actually do (through analysis of their financial statements). The conclusion is that a sincere commitment to CSR involves a substantial change in the banks business model. An analysis of the banking industry shows that only a few institutions are ready to take a step forward in this direction.

Key words: Ethical banks, CSR in banking

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