

Social Responsibility and Banking – An Oxymoron?

by John Varley



As a Christian, John Varley defends the function of banks in bringing wealth and stability in commerce, and goes on to explore the contentious issues of investment banking, social values and bankers' bonuses.

John Varley began his lecture by saying that he saw getting the right balance between social responsibility and commercial success as fundamental to running a sustainable business. He views this as a long-standing issue with its origins in the historical controversy surrounding the charging of interest. The suspicion of usury has created a climate where banks need to earn their customers' trust against the weight of innate mistrust – a situation exacerbated by the recent crisis.

Perspectives on the crisis

Before turning to his main theme, Varley offered some perspectives on the crisis. He acknowledged that its causes are complex, but 'there are four things of substance on which most people agree':

(i) Whilst not the sole protagonists, banks played a material role in the confluence of factors that led to the crisis, and got many things wrong. As the CEO of a big bank, he expressed sorrow and regret for the errors made by the banking sector.

(ii) Without decisive, determined and significant action to restore confidence by

global authorities, including the UK government, the banking system would probably have collapsed. Even those banks who did not take capital from governments clearly benefited from these actions.

(iii) It must never happen again. So some fundamental things have to change, and already are changing, in the banking industry.

(iv) There is an important and difficult trade-off to be engineered between improving the stability of the financial system and stimulating and supporting economic growth – both with the aim of recreating confidence.

He asserted, however, that despite the pain of the crisis, the world is much better placed today than it was 20 years ago. Even if the recession turns into a depression, the net growth in global GDP from 1980 to 2010 would still amount to 120%, or 2.7% per year over this 30 year period – a real per capita increase of nearly 40%. That growth lifted millions of people around the world out of poverty.

This is a summary of the CABE Hugh Kay lecture, given by John Varley, Group Chief Executive, Barclays PLC, on Tuesday, 3 November 2009 at St Martin's-in-the Fields, London



▶▶ **The role of banks in society: their social utility**

Varley defended what he calls a broad-based bank, one that provides many different services within the same brand.

First: banks provide the backbone of the modern economy by maintaining reliable and efficient payments systems.



'Wave and pay' technology

of banks. Historically this was through cash and cheques. More recently, Barclays have been innovators in introducing new and efficient methods such as plastic cards, cash points and 'wave and pay' technology. A safe payments system is fundamental to the functioning of household finances and national economies.

The second activity banks provide is "safe storage". Whether in current accounts or via deposits or interest-earning savings accounts, banks offer customers a safe place to store their money in the knowledge that they can retrieve it as and when they wish. Significantly, wealth generation in a country accelerates once most of its population have a bank account. Economies need entrepreneurs to grow; entrepreneurs need investment; investment comes from savings; bank accounts help people.

Third, safe storage unleashes what Einstein called the most powerful force in nature: compound interest. By converting savings into loans, banks undertake maturity transformation. This is their most critical activity in the process of economic development, but it is also the most risky. In transforming maturities, banks take liquidity risks and credit risks, both of which entail delicate judgement.

These functions are important to both commercial and corporate clients. Taken together, they represent the principal activities undertaken by traditional retail and commercial banks – what some call 'boring banking'. Beyond these, there are:

(i) Asset management - products that provide potential for better returns than traditional bank savings, typically through an investor taking principal risk. These provide a means to help reduce the long-term burden of public welfare provision.

(ii) Investment banking – an activity that has recently been described in terms of gambling or 'casino' banking.

Investment banking

In defending this activity, Varley pointed out that Barclays Capital, its investment arm, includes among its clients many governments and leading companies. These are clients that represent the real economy, driving investment, jobs and economic growth. An investment bank has an advisory role (working with clients to design solutions to meet their financial needs), an executive role (helping clients put in place whatever solution has been designed – this can include book-running, underwriting, purchasing securities and hedging exposures) and a trading role (which depends on the existence of efficient secondary markets through which equity and debt securities are traded, and which clients can readily access).

There is a strong, positive and causal relationship between the depth of capital markets and national wealth. Accessible and affordable finance, and well-managed risks, allow companies to take more risk in their efforts to grow, leading to faster economic growth and more job creation. Varley expects that in the future Europe and Asia will follow the 'advanced' example of the USA in meeting the majority of the financing needs of governments and companies through the capital markets. Barclays' analysis is that global economic growth of 4% per annum (what the world needs to create employment





Quaker values

Samuel Gurney and Joseph John Gurney, one of the founding families of Barclays Bank

adherence to rules. Varley cited Pope Benedict, Rowan Williams, Lord Myners and Paul Tucker, who have all expressed strong views to this effect. The public is looking for 'evidence of a change in the industry's values and ethics. Customers need to see the industry's soul.'

Varley had recently received a letter from a Reverend Collingwood about the history of one of the founding families of Barclays, expressing his hope, in these turbulent times, that the bank's behaviour would be influenced by the traditional Quaker values of prudence, plain dealing, philanthropy and probity. Barclays still believes in these values, but perhaps needs to be more explicit about their importance. In particular, they need to take to heart the significance of 'prudence' in their assessment and management of risk. Banks should not be cavalier about risk on the presumption that public funds will bail them out because they are too big to fail.

Varley then turned to the role of financial compensation for bankers. He thought the international agreement on reforms to the structure of remuneration that were announced by the G20 in September a good step forward. The British banks have committed to implementing those, as well as the new FSA Code on Remuneration. Barclays have been working on reforming their internal remuneration practices, recognising and understanding the desire of authorities to ensure that they protect and enhance capital ratios.

'This is, though, difficult territory. That's because we must find a way of accomplishing that without damaging the interests of our shareholders. All parts of banking are increasingly global... So we rely on global talent pools as well. Talent is highly mobile. If we fail to pay, or are constrained from paying, competitive rates, then that talent will move to another employer, whether in the banking industry or otherwise.' Varley said he had an important task as CEO to get these judgements right: 'our objective is to pay the minimum compensation consistent with competitiveness'.

▶▶ and relieve poverty) requires global capital markets to grow at twice that rate – 8%. 'I cannot think of a better way to demonstrate the social utility of investment banks.' Broadly based banks with capital markets have the capabilities to help solve all the world's major problems.

Social values and banking: how banks should behave

With these crucial roles that banks perform go significant responsibilities. These responsibilities are both direct and indirect; at their heart lies the obligation to engender progress.

The direct responsibilities require banks to lend responsibly, to 'store' reliably, to transmit quickly and securely, to offer advice impartially, and to take careful account of the needs and risk tolerances of our customers. The indirect ones oblige banks to use the fruits of their work constructively. So with the profit it generates, a socially responsible bank should invest for the future, support appropriate risk-taking by its customers, run capital ratios that create confidence, pay dividends to its shareholders, and pay due tax to the revenue authorities.

Banks' responsibility now is to engage fully in discussing and implementing changes on how banking operates, the objective being to ensure that the recent crisis never happens again. To rebuild trust, banks need to connect with the public on a different level, accepting the need for moral reform which goes beyond



John Varley was appointed as Group Chief Executive in September 2004, prior to which he had been Group Deputy Chief Executive from January 2004, and Group Finance Director from 2000 until the end of 2003. He was Chief Executive of Retail Financial Services from 1998 to 2000 and Chairman of the Asset Management Division from 1995 to 1998. He is a non-executive director of the pharmaceuticals company AstraZeneca PLC., Chairman of Business Action on Homelessness, President of the Employers' Forum on Disability, President of the UK Drug Policy Commission and a member of the International Advisory Panel of the Monetary Authority of Singapore. He is married and a father to two children.



Clerk with cash in hand

It is the helping of their customers that brings a sparkle to their eyes.

Restoring trust through community development and investment

Most bank employees, Varley claimed, are not motivated by earnings per share or share price. They are motivated by a desire to help – a very Christian value. It is the helping of their customers that brings a sparkle to their eyes.

He saw no conflict between doing business in an ethical and responsible way, and making money. ‘We make our biggest contribution to society by being good at what we do.’ Because Barclays is successful, it creates employment in over 50 countries, employing nearly 145,000 people; it pays large amounts of tax, which builds a lot of schools, hospitals and roads; and it can pay dividends to its shareholders - mostly the pension funds which look after the long-term savings of millions in retirement.

The point is that successful companies need to use their success to improve the lives of those who are touched by them. Most companies think of this as ‘corporate social responsibility’; Barclays calls it ‘sustainability’, which is about achieving the broader needs of all the bank’s stakeholders. These stakeholders are increasingly interested in ethical, environmental and social issues, as well as business conduct.

Barclays is a ‘relationship bank’. Relationships are typically rooted in local communities, where customers live and work. As examples of positive community involvement by Barclays Varley mentioned:

- Financial inclusion - which is about creating access to banking services for people not always well served by the industry; Barclaycard Horizons, a programme to help indebted single parents; an initiative in London to extend basic banking facilities to the homeless.
- In Africa, providing accessible, affordable and understandable banking products and services, and helping local economies to develop.
- Sponsoring the Premier League in the UK; building a global programme called ‘Barclays Spaces for Sports’, which brings sustainable sports sites and projects to disadvantaged communities; distributing over 2,600 coaching packs and giving more than 500,000 individuals, mostly children, the opportunity to benefit from them.

Conclusion

Varley concluded by insisting that the generation of profit is not satanic, but the pursuit of profit must not come at the expense of society. A bank needs to screen activity for its ‘contribution to society’. ‘We have an obligation to behave as a responsible employer; as a responsible lender; and as a responsible investor.’ He wants his staff to be proud of the fact that they work for Barclays. But they’ll only do that with a smile, and with confidence, if they think that their employer behaves responsibly, and is playing its part in building a better society.

He ended with these words:

‘Is it possible for a man to hold at once the office of chief executive of a bank, and the prospect of going to heaven? I hope the answer is yes. That particular right of passage, of course, is conditional on many things beyond our professional lives. But it is at least conditional on me getting right the balance between social responsibility and banking.’ ■