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# The role of Corporate Governance and Corporate Social Responsibility in Business expansion: The Case of Grameen Bank

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## *Abstract*

In the past few years many businesses has suffered some serious setbacks and some banks have even undergone bankruptcy. That's why Corporate Governance (CG) and Corporate Social Responsibility (CSR) have increasingly become very important in the recent years. This thesis investigates the role played by CG and CSR in business expansion. Further it examines what is CG and CSR and how it can bring about growth in a business. For better understanding of the theories we used a case study approach and chose Grameen Bank (GB) a Bangladeshi bank because of its tremendous success and growth over the years even in the middle of the turbulent financial crisis. We wish to find out the role CG and CSR played in this success critically. The expected contributions of this work will be to see the visibility of CG CSR in a bank like GB which has deviated from conventional banking models and how this has influenced its growth.

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## Acronym and Abbreviations

CG	Corporate Governance	BDT	Bangladeshi Taka
CSR	Corporate Social Responsibility	BE	Business Expansion
GB	Grameen Bank		

## ***1. Introduction***

Many businesses have suffered serious setbacks in recent years and some banks have even gone bankrupt as a result of inadequate monitoring of some stakeholders of such businesses. Nowadays, shareholders and other stakeholders are increasingly looking out for increase transparency and accountability (Mallin, 2010) of their businesses in order to ensure that there are prospects for growth and that the business will continue to exist in the foreseeable future, not only in terms of maximizing shareholder's wealth but also taking into consideration the needs of other stakeholders involved with the business (like, consumers, employees, suppliers, government etc) one of the reasons why Corporate Governance and Corporate Social Responsibility have increasingly become very important in the last few years.

The purpose of this study is to examine the role played by CG and CSR in business expansion by looking at how good CG and CSR can be achieved and how it can bring about growth in a business. The thesis is going to take a case study approach and we are going to examine CG and CSR practice in Grameen Bank (GB). We chose this bank because it has recorded tremendous success and growth over the years even in the middle of the turbulent financial crisis, it still stood up unshaken, so we wish to find out the role CG and CSR played in this success critically. The expected contributions of this work will be to see the visibility of CG CSR in a bank like GB which has deviated from conventional banking models and how this has influenced its growth. The thesis will also provide a brief insight on corporate governance and CSR in social businesses in general and this may be of help for future research in this area (the originality of the thesis).

### ***1.1 Research Statement***

Past financial scandals and failures in the financial service sector specially in banks (even those which showed a good profit and a good financial position in their end of year profit and loss accounts and balance sheets), points to the fact that there is more to watch out for as far as transparency and accountability is concerned in banks like areas related to corporate governance and corporate social responsibility (areas which were often overlooked in the past) if this financial failures and scandals are to be reduced or completely avoided and if banks must continue to grow and exist in the foreseeable future.

### *1.2 The purpose of the study:*

Explain what CG and CSR is all about and how it can enhance business expansion in the financial service sector with special reference to Grameen Bank. By bringing out these, the study should also share some light on how conflicts of interests due to poor governance can result to bank failures.

### *1.3 Research Question:*

***“How business expansion is a function of Corporate Governance (CG) and Corporate Social Responsibility (CSR).”***

## ***2. Methodology***

The main purpose of this study is to look at the role played by corporate governance and corporate social responsibility in business expansion. Grameen bank has revolutionized banking by deviating from conventional banking models and being a banker to the poor with a primary objective of alleviating poverty. This part of the study shows the method used to bring out the role corporate governance and CSR has played in the expansion of this bank.

### ***2.1 Research Philosophy***

The primary goal of a research is to develop new knowledge in a particular field. On our way to conduct a research first we need to know about research philosophy as it contains important assumption about how we see the world (Saunders et al., 2009). As Johnson and Clark (2006) cited in Saunders et al. (2009) for us being business and management researchers we should be aware of the philosophical commitments that we make while choosing the research strategy since this has significant impact not only on what we understand but also what we are investigating. Saunders et al. (2009) agreed with Johnson and Clark (2006) by stating that, it is not so important to know whether the conducted research should be philosophically, but it is how well the researchers are able to reflect upon their philosophical choices and defend these choices in relation to the alternatives they could have adopted. In the following part we will motivate which philosophical approach we have adopted and how it helps us in defining our research strategy.

On our way to determine the research strategy for the thesis, first we need to pinpoint our ontological and epistemological orientation. Ontology is defined as a philosophical belief system which deals with the nature of reality (Saunders et al., 2009). Ontology raises questions, the researchers make the assumptions about the way in which the world operates. The ontological position can be described from two aspects Objectivism and Subjectivism (Saunders et al., 2009). Here, *objectivism* is an ontological position that states that social phenomenon and their meanings exists and it is independent to social actors (Bryman & Bell, 2007). Whereas, *subjectivism* also referred as *constructionism, or social constructionism* is the ontological position where the subjectivist view is that, social phenomena are created from perceptions and consequent actions of social actors, also these social phenomena are in a constant state of revision (Saunders et al., 2009). Derived from Easterby-Smith et al. (2002), the concepts of this study are incorporated with stakeholders' perspective which

generates a subjective view of doing business. Moreover, the findings will be generalized through theoretical abstraction; hence we tend to be more on the side of subjectivism and less on the side of objectivism.

To choose the most suitable philosophy for our research first we need to understand epistemology. This issue concerns what should be regarded as acceptable knowledge in a field of study or discipline (Bryman & Bell, 2007). Within this consideration, we have two extreme philosophy, these are *positivism* and *interpretivism*. Here positivism refers to an epistemological position where the researcher takes the stance of a natural scientist and focuses on facts. In this orientation, typically a hypothesis is developed which will be tested and confirmed later on. This type of research is objective in nature (Bryman & Bell, 2007). However, as Saunders et al. (2009) rightly points out, ‘the rich insights into the complex world is lost if such complexity is reduced to mere law-like generalizations’. On the other hand interpretivism is closely related to phenomenology. Here phenomenology refers to the way, in which humans make sense of the whole world around them (Saunders et al., 2009). Interpretivist’s share the view that the social sciences – people and their institutions, are fundamentally different from the objects of natural sciences (Bryman & Bell, 2003). Therefore, the researcher need to grasp the subjective meaning of the social action, which might be overlooked from a purely positivist framework.

In between these two extremes lies research philosophy *realism*. It is another branch of philosophy that assumes a scientific approach similar to positivism (Saunders et al., 2009). There are two types of realism. The first type is direct realism which states that, what you see is what you get; what we experience through our senses portrays the world (Saunders et al., 2009). The second type of realism is critical realism. Critical realism argues that our first experiences that are derived from our senses could be deceptive and there is a need for mental processing after the sensation meets our senses (Saunders et al., 2009). According to Bryman and Bell (2007) critical realism implies two things. First implication is that, the positivists take the view that the researcher conceptualization of reality directly reflects the reality, whereas the realist argues that the researcher’s conceptualization is simple way of knowing that reality. The other implication is that the critical realists are comfortable with theoretical explanation that might not be directly linked to observation.

Concerning our research question, it is clear that a purely positivist or interpretivist approach might not work for this investigation. Therefore, our research philosophy is motivated by

realism at the same time influenced towards a subjective view of reality. Also, Saunders et al. (2009) argues that the critical realism approach is highly relevant in multi-level studies in order to gain good result in a research.

## 2.2 Research Approach

This research as mentioned earlier is going to focus on GB (case study approach). Now we are going to explain how data gotten from the annual reports of GB will be analyzed and how we intend to create a link using this data to explain our case based on theoretical insights.

According to Perry (1998), theory development can either be inductive or deductive. The inductive method involves reasoning from particular cases to general cases while the deductive approach involves reasoning from generalizations to particular cases (Bryman & Bell 2007). This therefore means that where one process ends, the other begins. While induction starts from empirical data, deduction starts from theoretical background knowledge (Bryman & Bell 2007).

John and Lee-Ross (1998) argue that in deduction, the researcher maybe biased in getting information because he goes about his research from theory to empirics, and hence collects empirical data to check if findings comply certain expectations grounded in theory.

A summary of the steps in the deductive method is shown below.



**Figure 1: Steps in deductive Method (Source: *Bryman & Bell, 2007, pg 11*)**

Induction begins where the deductive process ends where the researcher infers the implication of his or her findings for the theory that prompted the whole exercise (Bryman & Bell 2007).

But as Bryman and Bell (2007) puts it, it is useful to think of a relationship between theory and research in terms of induction and deductive strategies. Therefore, to a large extent, deductive and inductive strategies are possibly better thought of as tendencies rather than as a hard-and-fast distinction (Bryman & Bell, 2007).

### 2.3 Qualitative Research Strategy

Bryman and Bell (2007) suggests that the basic distinction between qualitative and quantitative research is that quantitative researchers employ measurement and qualitative researches do not, Ghauri and Gronhaug, (2010) says that the main difference between qualitative is not about the ‘quality’ but of procedure. Furthermore, these research strategies are not just question of quantification, but also a reflection of different perspectives of knowledge and research objective (Ghauri & Gronhaug, 2010). The following table drawn from Newman (1998) gives us an in-depth view of both quantitative and qualitative research style

**Table 1: Quantitative versus Qualitative style**

<b>Quantitative style</b>	<b>Qualitative style</b>
Measure objective facts	Construct social reality, cultural meaning
Focus on variables	Focus on interactive process and events
Reliability is key	Authenticity is key
Value free	Values are present and explicit
Independent of context	Situational constrained
Many cases, subjects	Few cases, subjects
Statistical analysis	Thematic analysis
Researcher is detached	Researcher is involved
<i>Source: Newman W. L (1998) Social Research Methods: Qualitative and quantitative approaches, 3rd edition, Pearson Education, Inc, USA.</i>	

This study is based on, a qualitative research method. Qualitative research method was chosen to get a deep understanding into social science context where behaviors, perceptions, values and attitudes play the main role (Johns & Lee-Ross 1998). Books on qualitative research mainly provide example and cases from the study of society in general and the government sector rather than business. However a connection between the private and governmental sector is clearly visible that has encouraged us to choose qualitative research approach (Gummesson, 1995). We went through the annual reports of GB and tried to establish the growth trend of some key performance indicators (like number of branches, number of customers, credit groups etc). The performance indicators chosen for this research are linked to CG and CSR. We tried to make a big picture out of these indicators by employing descriptive statistical tables and histograms in order to illustrate expansion.

Besides key business phenomenon such as profit, market share, corporate strategy, productivity, total quality management, operations management, financial control systems, balance sheets and so on are rarely mention in qualitative methods (Gummesson, 1995). However a researcher in business sector needs knowledge on these issues to do qualitative research. In the analysis part of the study, we also made use of secondary data still from the annual reports of GB (data we considered to be pertinent in assessing the role of CG and CSR in this bank). The study was designed using deductive approach. We tried to draw a conclusion by examining critically, the findings in the annual reports based on theoretical insights.

Finally, sometimes more than one method of source of data has been used in this study to cross check the finding. This approach is known as triangulation. Triangulation necessarily doesn't always mean that it is a combination of qualitative and quantitative research. Triangulation can also take place within a qualitative research (Bryman & Bell, 2003). The data extracted from the annual reports were quantitative in nature however it was used to cross check the qualitative findings of the paper.

#### *2.4 Choice of case study design:*

Yin (2009) describes a case study as a method allowing intensive research including the holistic and meaningful characteristics of the research object, as for example organizational processes.

“A case study is an empirical inquiry that

- Investigates a contemporary phenomenon within its real-life context, especially when
- The boundaries between phenomenon and context are not clearly evident.” (Yin 2009)

We have examined one case as it represents the critical case in testing a well formulated theory. Furthermore, a single case can be used to determine whether a theory’s propositions are correct or whether some alternative set of explanation might be more relevant (Yin 2009). In a single case study, the concern is the quality of the theoretical reasoning in which the case study researcher is involved and also how the researcher finds out theory out of the findings (Bryman & Bell, 2007). This was the reason for us to choose a single case and explore the scope of new theoretical findings with the help of existing theory.

## *2.5 Data Collection*

Data collection is a hard and complex work while doing case study and it is because of the absence of routine formulas and routinized processes in this type of research (Yin, 2003, p.57). Special skills also are required from researcher to be able to analyze, ask good questions, be tolerant and flexible and be ready to face difficulties while gathering data. Yin (2003) states that even though case study does have some formal plan “the information that may become relevant to a case study is not readily predictable” (p.59).

### *2.5.1 Interview*

Our qualitative research is going to collect primary data from interview. Researchers employ term qualitative interview usually to feature two types of interviews: unstructured and semi-structured. Less structured interview is suitable for qualitative interview (Bryman & Bell, 2003). New questions may arise in a semi structured interview. For our investigation we have conducted a semi structured interview with open ended questions it gave us greater flexibility. This was important to maintain the flow of interview. Furthermore we folled a interview guide that had been enclosed in appendix1.

Depending to the respondent’s location it can be conducted in three ways: via emails, via phone or personal interview (Ghauri & Gronhaug, 2010). As our respondent was is Bangladesh so over phone interview was the better alternative for us also it was cost effective. The interview lasted for 43 minutes. The result of the interview was analyzed through qualitative assessments in this paper.

### *2.5.2 Literature review and Secondary data:*

The great part of our work is related to the secondary data that we collected. We heavily relied on the annual reports of Grameen Bank, articles and journals. For building the theoretical framework of the thesis we heavily relied on relevant articles, journal and book relevant to our research. A strong literature review was done to raise the validity of the research. Furthermore, the data that was been collected helped us to find out the answers to some of the questions that were raised from the literature review.

### *2.6 Analysis of Data:*

The analysis was on secondary data gotten from the annual reports of GB, and we tried to link it to existing literature on CG and CSR in order to have a clearer view of CG practice in GB and how it has contributed to the rapid expansion of GB over the years. We also critically looked at aspects on CG which are related to GB but which are not visible in conventional banks and how these factors have actually brought about growth in GB. Information gotten from our interview also helped us to clarify some issues related to our case.

### *2.7 Validity and Reliability:*

There are certain criteria to judge the quality of a research. To ensure the quality of a research, the researchers often depends on the *validity* and *reliability* measurements of a study. Several tactics are used in this study not only just in the beginning but throughout different phases of the research. In line with this view (Yin, 2003) mentions “design works actually continues beyond the initial design plans” (pg, 35).

**Validity:** Bryman and Bell (2007) states, in business research validity represent the integrity of the conclusions that are formulated from a research. Furthermore, Yin (2003) asserts the use of four tests that are commonly used in different phases of the research by business researchers to ensure the quality of the research and are relevant to case studies. These are explained below in relation to our case.

*Construct Validity:* is the first test and occurs in data collection and composition phase. In this test the researchers need to establish operational measures for the concepts that have been studied. To cover this requirement first, we studied the theories separately that has been used in the paper. Then we developed some relevant common criteria based on which we will test the links between the theories and the collected data. As a tactic *multiple source of evidence*

is used in the data collection. For instance we gone through articles from different sources and collected both primary and secondary data.

*Internal validity:* is the second test that rises in the data analysis phase of the research. It is concerned for causal or explanatory case studies and not for exploratory studies. As our thesis is exploratory in nature we were not so concerned about internal validity of the research. However, we have linked our empirical study on LEGO in relation to our theoretical frame that ensures the internal validity of our research (Bryman & Bell, 2007).

*External validity:* is the third test and is related to research design. It deals with degree to which the findings of the case study can be generalized. It is difficult to ensure external validity in qualitative research, especially for single case study. To deal with this barrier we have supported our study with a strong theoretical base.

*Reliability:* is the last test required in data collection phase. Reliability measures the extent to which data collection techniques or analysis procedures will deliver the same results no matter how many times it is applied (Saunders et al., 2009; Bryman & Bell, 2007; Ghauri & Gronhaug, 2010). The objective of reliability in a case study is to repeat the same study again and check whether findings and conclusions are same (Yin, 2003). Yet, the aim of reliability is not to replicate the same study again but to reduce the errors and biasness in a study.

To ensure that data was reliable, we made sure that all data that was used in this study was gotten from the official published audited financial statements of GB. These accounts according to the various audit reports were prepared in accordance with International Accounting Standards (IAS) and all the audited reports pointed to the fact that accounts presented a true and fair view of GB.

## *2.8 Limitations of the Research:*

The limitations we had in this thesis firstly were that of time. This time limitation coupled with a budget constraint complicated our going to Bangladesh to get one on one interviews with some Board members and employees of GB as we initially planned. But somehow, this limitation increased our critical thinking with special guidance from our supervisor and helped us to investigate thoroughly with the secondary data we had, to carry out the study. However after one long year we finally managed to get the interview of a Branch Manager of Grameen Bank.

### ***3. Conceptual and Theoretical framework***

#### ***3.1 Literature Review***

##### ***3.1.1 Corporate governance and Corporate Social Responsibility (CSR)***

Corporate governance is a relatively new area in the business world which have been of increasing importance over the years and its development has been affected by theories from a number of disciplines like finance, accounting, law, management, economics and organizational behavior (Mallin, 2010). There is no general definition of corporate governance, but rather each institution defines it to suit its objectives. According to Shleifer and Vishny (1997) corporate governance deals with the way suppliers of finance to a corporation assure themselves of getting a return from their investment. Cadbury (2000) on the other hand regards corporate governance to be concerned with holding a balance between economic and social goals and between individual and communal goals. Morrison et al. (2007) gives a more comprehensive definition of corporate governance adopted from the OECD (1999) which regards corporate governance as:

A set of relationships between a company's management, its board, its shareholders and other Stakeholders; Corporate governance also provides the structure through which the objectives of the company are set, and the means of attaining those objectives and monitoring performance are determined. Good corporate governance should provide proper incentives for the board and management to pursue objectives that are in the interests of the company and shareholders and should facilitate effective monitoring, thereby encouraging firms to use resources more efficiently.

Despite the fact that corporate governance is a recent phenomenon in a global context, the theories related to its development are old and are developed from a variety of disciplines (Mallin, 2010) mentioned above. The two theories to be considered in this paper are: the agency theory and the stakeholder theory.

The agency theory according to Mallin (2010) identifies the agency relationship where one party, the principal delegates work to another party, the agent. Applying this theory to corporate governance will mean that good governance should be geared towards maximizing shareholder's wealth. This theory's inclination to corporate governance is very visible in the USA and the UK since their corporate governance is premised on publicly owned

corporations with the shareholders of the business being regarded as the principal and the directors being the agent (Mallin, 2010).

Stakeholder theory on the other hand looks at corporate governance beyond the spectrum of just shareholders and directors, by taking into consideration the importance of other stakeholders –a stakeholder is any person or group of individuals that are affected directly or indirectly by the activities of the company (Mallin, 2010) for example, employees, creditors, suppliers, customers, local communities, environmental groups and government. This theory with respect to corporate governance is widely practiced in civil law countries like France and Germany where employees rights are highly protected (Mallin, 2010). This therefore points to the fact that certain theories are more applicable in certain countries than others. And these differences are either due to the legal, cultural, ownership and other structural differences (Mallin, 2010).

It is very difficult to separate corporate governance from corporate social responsibility (CSR). This is because companies have started developing a good sense of corporate social responsibility by paying attention to their core values that will enable them to create a good lasting relationship with their customers (Enquist & Johnson, 2006). It is impossible to disconnect business from ethics and it is necessary to take all stakeholders into account; and CSR is seen as a sound investment and according to sound investment theory, the stock market reacts to firms' actions and socially responsible behaviors will be rewarded by the market. Hence many businesses are trying as much as possible to adopt the triple bottom line approach to business (that laying business on the foundation of social, environmental and financial aspects not just profit). In triple bottom approach, economic values are related to quality, price and cost (that is, value for money). Secondly, environmental values are linked to ecological protections, improvements and responsibility. Lastly, social values are associated with ethical and community responsibility and benefits (Edvardsson et al., 2006). In the following chapter we will take a deep look on Triple bottom line.

But Yunus (2007) questions the integrity of many businesses who claim to adopt this system by saying that most often it is just a show off and their primary motive is always linked to profit maximization. These were his words regarding this:

*CSR like to talk about the "triple bottom line" of financial, social, and environmental benefits by which companies should be measured, ultimately only one bottom line calls the shots: financial profit. (Yunus, 2007, pg 17).*

Hence Yunus thought and still thinks that when talking about reaching out to the needy, less privileged, poor; social business still remains the ultimate.

### *3.1.2 The triple bottom line*

While Friedman (1970) argues that “there is one and only one social responsibility of business—to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, which is to say, engages in open and free competition without deception or fraud... and on the other hand the state addresses social problems”. His argument was that an executive, by taking money and resources that would otherwise go to owners, employees, and costumers, and allocating them according to the will of the minority, fails to serve the interests of her or his principal. In this way, the executive imposes a tax and spends the proceeds for “social” purposes, which is intolerable, since she or he has neither the skills nor the jurisdiction to do so.

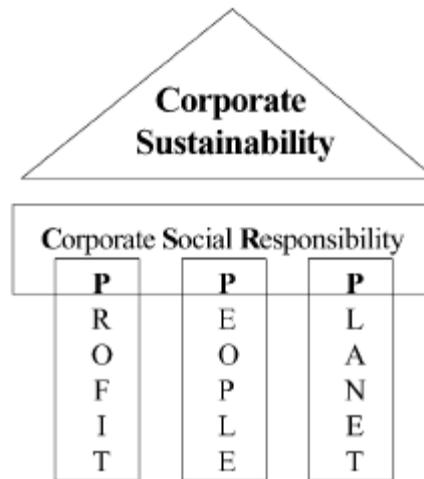
On the other hand, advocates of social responsibility appeal for corporate adoption of the CSR principles. They believe that although the government is mainly responsible for addressing those issues, the contribution of private firms can be substantial.

Elkington (1997) pointed out the need to have a balance of three bottom lines while we run businesses. These three bottom lines are: financial, economic and social bottom lines.

Triple bottom line thinking has become very popular in recent years. Today, Companies are paying attention to their core values and the development of a sense of corporate social responsibility, which can be used in marketing strategies and in customer-retention management (Enquist et al., 2005). Hence, there is more to business now than just the single bottom line where profits are the only objective of running the business and where the primacy of the shareholders cannot be overemphasized. Though there is no conclusive evidence as to whether there is a direct relationship between the practice of CSR (incorporating these three bottom lines) and financial performance of a business, Vogel (2005) argues that there is a business case for CSR for innovative businesses since (according to him) no other researcher has proven otherwise.

(Marrewijk, 2003) looked at the triple bottom line from a people, planet and profit perspective (that is, the three Ps).

This is shown the figure below:



**Figure 2: Corporate Sustainability, CSR and the three P's (Marrewijk, 2003 p. 101)**

The three Ps according to Marrewijk (2003) are not very different from the above mentioned financial, social and environmental bottom line. It points to the fact that, while we do business today and make some profits we must not forget other people, be they employees or the community and we must not degrade the planet for this will compromise the availability of resources for future generations.

While some researchers have frowned at the triple bottom line thinking, advocates of this business philosophy strongly believe it has a lot to offer regarding CSR if it is well put into use. For example Norman and MacDonald (2004) refer to Triple Bottom Line as being nothing but a smokescreen behind which companies can avoid truly effective social and environmental reporting and performance. They further define Triple Bottom Line as:

*“Good old-fashioned Single Bottom Line plus Vague Commitments to Social and Environmental Concerns (Norman & MacDonald, 2004 p. 256) ”.*

For the sake of this study, we will take CSR to be a blend of both the triple bottom line and what Carroll (2003) called total social responsibility which is a sum of:

Economic responsibilities, legal responsibilities, ethical responsibilities and philanthropic responsibilities



**Figure 3: Carroll's pyramid**

Therefore for the sake of the study, CSR will mean the following:

**Economic responsibilities + social responsibilities + environmental responsibilities + legal responsibilities + ethical responsibilities + philanthropic responsibilities**

*Elkington (1997) triple bottom line + Carroll's (2003) total CSR*

The legal and ethical responsibilities will be well understood when we look at corporate governance since the study is aimed primarily to investigate the role of CG and CSR in business expansion.

### *3.1.3 Corporate Governance and Ethics*

If governance is all about setting regulations that will administer a corporation by taking into account the importance of the various stakeholders in managing the corporation, then it is closely related to ethics. As Roberts (2001) drawing from Leviná's phenomenology of ethics stresses that the foundation of ethics lies on the fact that "on the start, the other affects us despite ourselves". This in relation to corporate governance means taking into consideration the effects on other stakeholders before taking a strategic business plan. Ethics involves a discipline that examines good or bad practices within a moral duty (Roberts, 2001). This means that if business is to be considered ethically upright, they should incorporate a good sense of corporate social responsibility incorporating shareholders and other stakeholders rather than just focusing on one group of stakeholders (Enquist & Johnson, 2006). Any other business behavior that do not take this into consideration can be linked to what Roberts (2001) calls the narcissistic tendencies of most business regimes which express not a concern

for others but rather an essential self- preoccupied concern with the aim to be viewed as though they were practicing business ethics.

Therefore, businesses should always take into consideration corporate issues rather than just being geared towards profit maximization; because good corporate governance and social responsibility will lead to business expansion and in the long run lead to more profits and corporate failures like those witnessed in the past may be completely avoided. And for this to happen, at times it means going beyond business models and taking rational choices (Selznick, 1996) just like the case of Grameen Bank where Yunus revolutionized banking by going against banking conventions and models and created a bank for the poor in Bangladesh.

#### *3.1.4 Corporate governance and the ethics of narcissus*

Roberts (2001) carried out a study about the proliferation of talk and writing of business ethics in recent years. In his study, he mentioned that:

*“following Levinas, our ground of ethics lies in our corporeal sensitivity to proximate others...” and that*

*“ Such moral sensibility, however, is readily blunted by a narcissistic preoccupation with self and securing the perception of self in the eyes of powerful others”.*

Roberts (2001) argues that the current proliferation of codes of business ethics and the associated development of new social and environmental metrics to audit and measure such conduct will serve, paradoxically, to inhibit rather than promote the exercise of moral sensibility within the conduct of corporate life.

Roberts (2001) further argued that narcissistic vulnerability is played upon to effect governance of the employee and boss at work. Here, he relied on a Foucaultian account of how the boss as subject is formed through the disciplinary practices of the organizational hierarchy and market. He argued that the financial categories of accounting, and the demands for "shareholder value" that are articulated through them, become the standards in terms of which the self is judged, by both others and the self. As importantly, in competing for the recognition of the value of the self in these terms, the person is individualized such that all relationships—with self, colleagues, and subordinates—come to be seen solely as means or obstacles to securing "success" in the eyes of the market and that such individualization may

involve a terminal moment for ethics for it effects an imaginary closure or encrustation of the self in which the boss comes to believe in the essential independence of the self from others.

### *3.1.5 Shareholder and stakeholder views of Corporate Governance*

As seen above on the two main theories underlying the development of corporate governance; agency and stakeholder theory, agency theory is shareholder oriented and governance is geared toward the maximization of shareholder's wealth without giving attention to other stakeholders, this Selznick (1996) calls ``the primacy of shareholders'' and goes further to point out that this has had a pernicious effect on what we take to be corporate rationality. Hence, nowadays corporate governance from a stakeholder perspective is increasing and many companies around the world are adopting a good sense of corporate social responsibility by looking beyond the borders of the company.

### *3.1.6 Corporate governance and executive remuneration in banks*

According to Hull (2007) banks form just one category of financial institutions. A financial institution is one which performs many functions, but the basic task is to be intermediaries between buyers and sellers of financial services, such as borrowing and lending of funds and the provision of insurance against risks (Hull, 2007). The financial service industry is broadly divided into:

Depository institutions, insurance companies, finance companies, investment banks and securities, firms, pension funds, mutual funds. Just like other business corporations, banks are limited liability companies where there is often a divorce between management and control. They are owned by shareholders and managed and controlled by a Board of Directors. Due to this divorce between ownership and management, there are often conflicts of interest that result in the running of banks between the owners of the banks, and those who run and manage the affairs of the bank, and each stakeholder always wants to maximize his or her own benefit at the expense of other stakeholders. This calls for good corporate governance measures in banks that will minimize the conflicting gap between those who own the business and those who run it and those who are involved in the bank in one way or another (creditors, government, employees, taxpayers- other stakeholders) so as to have a balance between areas of interests and conflicts especially when it comes to risk management in banks.

Lucien and Spamann (2010) says that the compensation structure of bank executives have produced incentives for excessive risk because bank executives expect to share in any gains that might flow to common shareholders, but are insulated from losses that the realization of risks could impose on preferred shareholders, depositors, and taxpayers. They further go to explain that this has given executives incentives to give insufficient weight to the downside of risky strategies. The analysis of banks financing structures and compensation according to Lucien and Spamann (2010), shows that the payoffs of bank executives is most often tied to a highly levered bet on the value of the bank's assets. This is because top executives in banks at times own some common stock in the bank, and because they enjoy limited liability, they often engage in risky ventures which are optimal to their personal advantage but which are very excessive from the social point of view. Excessive risk here means risk that may either increase or decrease the value of a bank's asset but whose expected effect on banks value is negative (Lucien & Spamann, 2010).

Some banks in the past attempted to check excessive risk taking by bank executives by tightening the link between the design of pay arrangements and shareholders' interests. But this alone cannot eliminate excessive risks because common shareholders could benefit from taking risks that are socially excessive. Hence, bank executive are sometimes encouraged by shareholders to take these excessive risk so that they make more profits.

Therefore, the compensation structure of bank executives can cause them to take excessive risk and vice versa and this complicates their objectivity as far as risk management is concerned since most often they usually have their interests to protect. Empirical studies have documented that CEOs who are insulated from shareholder pressure and do not receive high-powered pay are less prone to engage in risk-taking (Lucien & Spamann, 2010).

Now, going back to the agency theory explained above, if we try to establish an agency relationship between the executives of the bank (insiders) and the shareholders we will realize just as (Lucien & Spamann, 2010) puts it that when compensation arrangements are flawed, it is common to look for agency conflicts between insiders and shareholders as source of the problem of excessive risk taking and corporate governance reforms as solution in order to enhance business growth and expansion.

So, going back to the question on whether the Board of Directors is incapable of controlling risk taking, we may be tempted to say, yes if they are not checked because they will always want to maximize their benefits at the expense of other stakeholders and at times even at the

expense of other parties also represented in the board. Therefore regulations should be geared towards preventing top executives in banks from taking risks that is socially excessive, yet privately optimal.

At this juncture, we will like to expand a bit further to see why excessive risk taking is aggravated in big banks especially in the USA. The biggest banks in the USA (as well as in many major world economies) are not stand-alone entities, but subsidiaries of financial conglomerates, known as bank holding companies in the USA. Lucien and Spamann (2010) explains that modern US bank holding companies received a substantial share of their compensation not in common shares, but in options on such shares. This further has more risk incentives than the common shareholders holding companies.

Also, risk monitoring and risk control in banks by the providers of finance plays an important role in risk taking by executives. But it is important to mention here that many deposits in banks are covered under deposit insurance by the government, this reduces the incentive of creditors to monitor risks (moral hazard) and further increases the incentive of bank executives to take excessive risks (adverse selection) which they would not had it been the deposits were not covered. Small creditors too have insufficient funds to monitor risk taking and often prefer to benefit from risk monitoring as free riders. This further explains how complicated it is for the board of directors to keep aside personal gains and engage in risk taking objectively.

From the above we can clearly see that risk taking with aspect to the Board of Directors is more an aspect of ethics than corporate governance, and despite the fact that corporate governance can help to a certain extent to limit risk taking in banks, it cannot completely eliminate excessive risk. Banks therefore call for separate governance regulations because conflicts of interest in corporations outside the financial sector are often between executives and shareholders, where compensation arrangements reward executives for short-term gains. This may have an adverse effect on the long term value of shareholders interest by creating excessive risk down the road. In this case, governance regulation should call for measures aimed at improving internal governance arrangements and preventing deviation of such arrangements from shareholders interests (Lucien & Spamann, 2010).

But in the financial service sector, risks often occur because shareholders have an interest in taking risks than is socially desirable-in turn; shareholders may be served by providing executives with incentives to take such risks. Consequently, conventional corporate

governance measures aiming to align management with shareholders are not an appropriate solution. Hence governance reforms cannot be relied upon to eliminate excessive risk taking because they cannot be expected to eliminate incentives to take risks that would be excessive from a social perspective but not from a shareholder perspective (Lucien & Spamann, 2010).

### *3.1.7 Why Banks different from other corporations*

As mentioned above, they are certain special traits that banks possess which call for separate examination with respect to corporate governance in order to enhance growth and expansion. Specifically, banks are generally more opaque than non-financial firms and governments heavily intervene in the banking industry more frequently (Levine, 2004).

Beginning with opaqueness, this trait points to the fact that there is usually information asymmetry between insiders and outsiders and this makes it very difficult for diffuse equity and debt holders to monitor bank managers (Levine, 2004). Due to conflicts of interest between debt holders and controlling owners of banks, there is always a disagreement between these two parties when it comes to risk taking. Debt holders are very sensitive when it comes to risk taking because they do not enjoy any upside potential from risk taking but do on the downside if the bank cannot service its debts. The opacity of banks makes it very complicated for debt holders to monitor risk in banks.

Still because of high information asymmetry caused by the opaque nature of banks it becomes very difficult to design incentive contracts that align managers' interests with bank equity holders. Furthermore, since managers frequently control the boards of directors that write the incentive contracts, managers of opaque banks can often design compensation packages that allow managers to benefit at the expense of the long-run health of the bank (Levine, 2004).

Levine (2004) also points out that opaqueness also makes it easier for insiders to exploit outside investors and the government. He goes further to explain that in many countries, the domination of large sectors of the economy by relatively few families makes insider abuses more likely, most often at the expense of outside equity investors, depositors, and ultimately taxpayers. He uses this example to demonstrate that:

In the year 2003 La Porta, Lopez-de-Silanes and Zamarripa find high rates of connected lending in Mexico. They find that 20% of total loans go to related parties. These loans benefited from interest rates that were about 415-420 basis points below those to unrelated

parties. Related borrowers also benefited from longer maturities, were significantly less likely to have to post collateral, were 33% less likely to pay back, and the recovery rates on these loans were massively less (78 percent lower) than on loans to unrelated parties. Similarly, Levine (2004) presents evidence that insiders in Russian banks diverted the flow of loans to themselves and then defaulted 71% of the time. This shows the extent to which information asymmetry and opaqueness of banks have significant implications for governance by equity and debt holders.

In addition, competitions between businesses usually make it possible for managers to sit up since they are afraid of a takeover. These usually bring in an element of governance in the business (governance by competition). Levine (2004) says that the opacity of banks can weaken competitive forces that, in other industries, help discipline managers through the threat of takeover as well as through competitive product markets. Product market competition is frequently less intense in banking. Bankers typically form long-run relationships with clients – to ameliorate the informational problems associated with making loans – and these relationships represent barriers to competition. This issue is further compounded by the absence of an efficient securities market.

The second aspect that we are going to examine here that makes banks different from other corporations is government regulation.

Firstly, it is important to mention that government regulation of banks through deposit insurance has a great implication regarding corporate governance in banks. Levine (2004) explains that deposit insurance has three main effects regarding the corporate governance of banks:

- 1) It reduces the incentives of depositors to monitor banks
- 2) It induces banks to rely less on uninsured creditors with incentives to monitor and more on insured depositors with no incentive to exert corporate governance.
- 3) Deposit insurance also strengthens the central banks role as lender of last resort and this have helped produced banks with very low capital asset-ratios relative to other firms. And as this capital falls, this increases the incentives of controlling owners to increase the riskiness of the bank.

Points 1 to 3 above tells us that government regulation through deposit insurance will only go a long way to increase risk taking in banks because this will simply compound the problems of moral hazard and adverse selection as seen above.

Government regulations also stiffen competition in the banking sector. This is because it clearly specifies who should own banks. This is a very big impediment for competitive corporate control as seen above.

Also, concerning the issue of the dominance of some families' ownership of banks, government regulatory restrictions are often ineffective at limiting family dominance of banks, but the regulatory restrictions on purchasing equity actually protect these family controlled banks from takeover and hinder corporate governance (Levine, 2004).

### *3.1.8 Business growth or expansion*

Business expansion can be broadly divided into two categories. The first category is internal expansion in which the business grows and expands by either increasing the size of the production plant or creating new production plants in order to gain economies of scale. The second category of expansion is called external growth or expansion which is gotten through the merging or integration of firms (Perloff, 2008).

For the purpose of this thesis, business growth or expansion will be limited to internal expansion. That is the growth of Grameen Bank internally seen through the increasing number of branches created over the years, increasing number of customers, increasing number of credit groups, elevating profit figures etc.

### *3.1.9 Performance indicators*

Friedman (1970) argued against business responsibilities to other stakeholders and claimed that all businesses were geared toward maximizing shareholder's wealth or profits. Going by this shareholder view of governance profit is the main drive of doing business and should be the only indicator of growth or expansion.

However, we can also look at business beyond the spectrum of just profit and an indication of growth or expansion. Rather look at business from a stakeholder perspective; a way of looking at business that calls for more than just profits.

The unconventionality of Grameen bank makes it look more like a social business. According to Zeller et al. (2003) the social performance of an organization (whether a private-for-profit firm, cooperative or NGO) comprises the relations of the organization with its clients and with other stakeholder groups.

Zeller et al. (2003) also distinguished major dimensions of social performance as follows:

1. Outreach to the Poor and Excluded: Mission and Targeting Strategies: According to them,

*“MFI has generally been developed to reach a population excluded from the classical financial System. MFIs can have the objective of reaching socially excluded populations or the poor, or simply to offer financial services in a region where classical banking systems are absent. The depth of outreach of the MFI can be measured to evaluate its focus on the economically and socially excluded population”*.

(Source: Zeller, Lapenu and Greeley Summary Report, Social Performance Indicators Initiative (SPI) 2003)

2. Adaptation of the services and products to the target clients. Zeller et al. (2003) also argue that, it is not enough to decide to reach a target population. The MFI must learn about the target population and work on the design of its financial services so that they can fit with the needs and the constraints of the clients. “Pro-poor” services are too often standardized. Social performance indicators can analyze the process leading to service definition and the extent to which the MFI knows about its clients ‘needs.

Other indicators include:

3. Improving social and political capital of clients and communities. For the MFI, trust between the MFI and the clients can reduce the transaction costs and improve repayment rates. It thus can foster collective action and reduce free-riding (Meller et al., 2003).

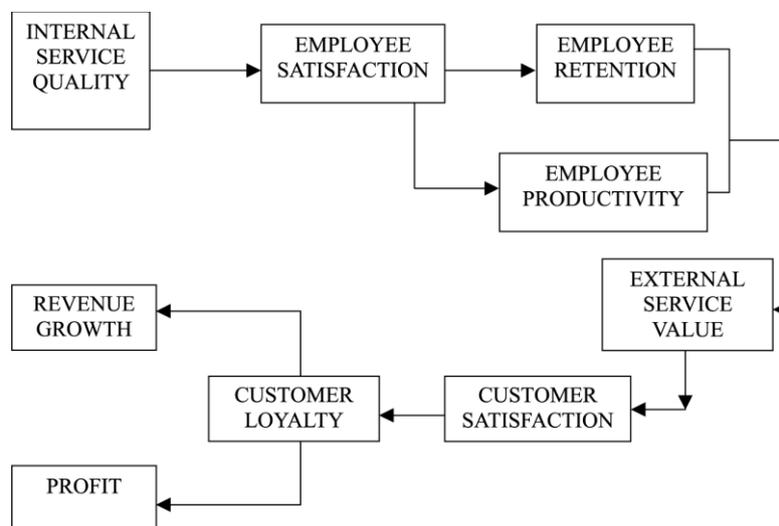
4. Social responsibility of MFI: Meller et al. (2003) also point out that Social awareness is a necessary pre-requisite for socially responsible corporate behavior. Social responsibility requires an adaptation of the MFI corporate culture to their cultural and socio-economic context, an adequate human resource policy, credit guarantees adapted to the local conditions, and balanced relationships between staff and clients (in particular in MFIs where there are elected clients who participate in decision making).

### 3.1.10 Business expansion performance stimulators: The service profit chain

Heskett et al. (1994) explained that one plausible account of the link between an employee's work experiences and financial performance holds that, in the service sector, customer satisfaction is a critical intervening variable and that management theorists call this view of organizational performance the service profit chain.

Zeithaml and Bitner (2003) further explained that the service profit chain model serves as an explanation to how investment in people drives profitability. Heskett et al. (1994) explain that the Service-Profit Chain can be viewed as one which establishes relationships between profitability, customer loyalty, and employee satisfaction, loyalty and productivity.

The figure below shows this model as adapted from Lau (2000)



Source: Adapted from Lau (2000)

**Figure 4: The service profit chain**

The service profit chain model points to the fact that, customer loyalty drives profitability (Heskett et al., 1994).

### *3.2 Overview of Corporate Governance Code of Bangladesh*

Identifying the lack of governance in the corporate sector in Bangladesh and the lack of authenticity in the regulatory body led Bangladesh Enterprise Institute (BEI) to develop the first corporate governance code of Bangladesh (BEI, 2004). BEI is a private sector entity with no statutory or regulatory power. However, the BEI code is the first set of CG guidelines in Bangladesh and contains separate guidelines for private sector as well as the Non Government Organization (NGO) and State Owned Enterprise (SOE) sectors. It was a project funded by the DFID and the Commonwealth Secretariat. The code is consistent in other parts of the world (such as OECD guidelines 1999, and the Combined Code, 2003). Since the BEI CG code (2004) follows the corporate concept of independent directors on the board, separation of the chairman and the CEO and the formulation of audit committees. It is also mentioned that the BEI code was developed in consultation with the OECD code of CG (1999).

The code contains the conduct and principles in the following areas:

- Board Issues
- Role of Shareholders
- Financial Reporting, Auditing and Non-Financial Disclosures
- Sector-Specific Provisions:
  - Financial Institutions
  - State-Owned Enterprises
  - Exhortation to Other Entities, and
- NGO Governance Principles

#### ***Board Issues***

*Structure:* A unitary board of directors is the form of board structure that has been suggested in the code. The guideline emphasizes to enable a majority of board members to be non executive and independent directors. Moreover, it suggests that the position of the chairman and CEO should be fulfilled by different individuals since their functions are necessarily separate. It also explains that a strong independent chairman provides the appropriate counterbalance and check to the power of the managing director/CEO.

*Duties of the Board:* The major duties of the board includes developing a director's job description including roles, rights, responsibilities, required qualifications and agree to a

board code of conduct. Besides, create committees of the board of directors as appropriate. In addition, initiate a board performance review process and also train new directors. Finally based on the above change or modify the Memorandum and Articles of Association.

### ***Disclosure and reporting***

The guideline suggests conveying both internal and external audit to ensure accountability and transparency in reporting. A sample contents of an annual report has been enclosed in the guideline

*Internal audit:* The code suggests forming more than one committee such as audit committee, nomination committee and remuneration committee to ensure credibility. It also prescribes that there should be at least three member and a chairman appointed by the board. The chairman of the board should not be a member of the committee. Moreover, the chairman should be a non executive director with professional qualification with relevant financial experience.

*External auditor:* Code suggests that external auditors should be independent, well-qualified and free of conflicts of interest. Except tax work, the audit firms should not go for non audit services and if they perform any non audit service, both non audit fees should be disclosed to the share holders to ensure transparency. The code provides guidelines to institute a rotation of external auditors.

### ***Shareholders***

The code prescribes to create and distribute a handbook for the share holder. Therefore, they can effectively participate in the AGM and contribute more by reviewing the procedures for nominating directors and nominating of the external auditors to ensure adequate and appropriate opportunities for shareholder.

### ***Financial Institutions:***

The key feature of this provision is to Develop and publish a code of “Best Practice” for customers and corporate social and environmental responsibility. it also suggests to expand the disclosures in the Annual Report and other public documents. It also suggests initiating a risk management review, if it’s not practiced yet.

### ***NGO Governance Principles***

The code contains separate principles for NGOs in Bangladesh. The principles provide a regulatory structure through which the mission and objectives of the NGO are set and performance monitoring is carried out. Underlying the Governance principle is a set of values, which have been identified as being of core importance to any NGO serving the community. These include professionalism, accountability, integrity and responsibility.

## ***4. Empirical study, Analysis and discussion***

### ***4.1 History of Grameen Bank in brief***

Grameen Bank was founded by Muhammad Yunus who was born in 28th June, 1940 in the village of Bathua, in Hathazari, Chittagong. His father was a successful goldsmith who always encouraged his sons to seek higher education. But his biggest influence was his mother, Sufia Khatun, who always helped any poor that knocked on their door. This inspired him to commit himself to the eradication of poverty. In 2006, The Nobel Peace Committee awarded **Muhammad Yunus** and **Grameen Bank** with Nobel Prize for their efforts to create economic and social development.

After the liberation war in 1971 East Pakistan became a new nation - Bangladesh. Yunus was working abroad as an assistant professor. In 1972 he went back to his home country with a vision to build a free and prosperous new nation. He joined the Economics Department at Chittagong University. But his dream turned in to a nightmare. There were natural disasters including floods, droughts, cyclones, and monsoons in the early 1970s. And the whole country was suffering from the vicious destruction from the War of Liberation. And finally the terrible famine in 1974-75, thousands were dying.

In 1974, Professor Muhammad Yunus, professor of Chittagong University, led his students on a field trip to a poor village. They interviewed a woman named Sufiya who made bamboo stools, like many others she relied on the local money lender for the money she need to buy the bamboo for her stools. On a condition that she would sell her stools to the money lender and he will decide the price. Through this unfair arrangement, she was left with a penny profit margin. Yunus with one of his students made a list of the victims of that money lending business. He found, there were 42 victims who borrowed a total amount of 856 taka – at that time this amount was equivalent to 27 USD (Yunus, 2007)

Realizing that there must be something terribly wrong with the economics he was teaching, Yunus took matters into his own hands and gave those twenty seven dollars from his own pocket to free the victims out of the clutches of those money lenders. He found that it was possible with this tiny amount not only to help them survive, but could serve as a good stepping stone toward poverty alleviation (Yunus, 2007).

He found that in conventional banking the rules were strict. And the banks disagreed to give loans to the poor because poor people don't have any credit history and collateral security to

secure loans. The conventional banks only lend money to the people who already had money. Yunus couldn't convince the bankers. So he tried it in a different way. He took the loan himself and lent it to the poor without collateral. And the result was very positive. The poor people paid back their loans, on time and every time.

But Yunus failed to convince the Banks to disburse loan for the poor. Finally he decided to establish a separate bank for the poor people which would give loans without collateral, without requiring a credit history, without any legal instruments. He started it as a project in 1976 and finally in 1983 it was transformed into a formal bank under a special law passed for its creation (Yunus, 2007)

Now, considering Poverty as a denial of human rights, Grameen bank started its journey in 1976 with a view to fight poverty and empowering the women of the most rural portions of Bangladesh. Grameen bank used 'micro credit' system as the tool to fight poverty. The definition of microcredit that was adopted in Microcredit Summit (2-4 February 1997), is: 'Programs extend small loans to very poor people for self-employment projects that generate income, allowing them to care for themselves and their families'. (The Virtual Library on Microcredit). The label of 'microcredit' got into general use for a wide range of small loans including agricultural, cooperative, savings bank and rural credits etc. This has created confusion in policymaking, institution-building, and in designing regulatory framework. Dr. Yunus tried to classify microcredit into different categories; stating, "I think we can come out of this confusion. (I think we could have avoided the confusion, to some extent, if we had called it "micro-capital". That's what it really is. Bengali term that I use for it translates as "micro-capital".)" He is considered as a pioneer to implement micro credit system successfully in large scale business operation. He suggested 10 broad classifications of microcredit. And what Grameen Bank says is that they have developed their own type of microcredit system that they call "Grameen credit". From the statement of, Dr. Yunus, we see "Grameen credit" is distinctive in its feature from the other type of microcredit systems.

Today Grameen Bank gives loans to over seven million poor people, 97 percent of whom are women. With 2,559 branches, it works in 84,691 villages. Total staff is now 23,144. Since opened, the bank has given out loans totaling the equivalent of \$6 billion (U.S.).

The repayment rate is currently 98.6 percent. Grameen Bank routinely makes a profit, just as any well-managed bank should do. Total revenue generated by Grameen Bank in 2008 was Tk 12.00 billion (US \$ 174.61 million). Total expenditure was Tk 10.69 billion (US \$ 155.62

million).Grameen Bank made a profit of Tk 1305.00 million (US \$ 18.99 million) in 2008. Grameen bank has declared 30% cash dividend for the year 2008. This is the highest cash dividend declared by any bank in Bangladesh in 2008.

Financially, it is self-reliant and has been profitable every year of its existence except 1983, 1991, and 1992. And according to Grameen Bank's internal survey, 64 percent of their borrowers who have been with the bank for five years or more have crossed the poverty line (Yunus, 2007). Grameen Bank now has 18 companies in the Grameen network. They are all independent companies, registered under Companies Act of Bangladesh. Since then, Yunus and his bank have won the Nobel Peace Prize and micro-credit has spread as an idea around the world (Yunus, 2007).

Therefore, in a nutshell, development of Grameen is closely linked to what (Roberts, 2001) describes as how the defense or elaboration of the 'self is routinely privileged over proximate responsibility for others and how this has led to the emergence of new forms of visibility-environmental, social, ethical as a supplement to financial visibility.

#### ***Mission, Vision & Objective of Grameen Bank:***

GB does not express any specific mission or vision for their organization. From their organizational values and the operational activities, it seems like they are after one mission mostly, which can be stated as 'Fighting the poverty through business' and some key visions can include social development through poverty elimination, woman empowerment and creation of self employment opportunities.

The Grameen Bank Project (Grameen means "rural" or "village" in Bengali language) came into operation with the following 5 objectives. These are still counted as the key objectives for the organization today.

Extend banking facilities to poor men and women;

Eliminate the exploitation of the poor by money lenders;

Create opportunities for self-employment for the vast multitude of unemployed people in rural Bangladesh;

Bring the disadvantaged, mostly the women from the poorest households, within the fold of an organizational format which they can understand and manage by themselves; and

Reverse the age-old vicious circle of "low income, low saving & low investment", into virtuous circle of "low income, injection of credit, investment, more income, more savings, more investment, more income". (Grameen Bank 2010)

### **16 decisions for borrowers:**

Grameen Bank developed a set of vows for their clients, aiming to generate social, environmental and economic awareness amongst them as an integral part of its service. They put a great deal of emphasize on this and try to make it work. When provided with the loans, the borrowers are requested to collectively take the following sixteen decisions, which many take very seriously and which change their lives. (Grameen Bank 2010)

1. We shall follow and advance the four principles of Grameen Bank – Discipline, Unity, Courage and Hard Work - in all walks of our lives,
2. Prosperity we shall bring to our family
3. We shall not live in dilapidated houses. We shall repair our houses and work towards constructing new houses at the earliest
4. We shall grow vegetables all the year round. We shall eat plenty of them and sell the surplus.
5. During the plantation seasons, we shall plant as many seedlings as possible
6. We shall plan to keep our families small. We shall minimize expenditures. We shall look after our health.
7. We shall educate our children and ensure that we can earn to pay for their education.
8. We shall always keep our children and the environment clean.
9. We shall build and use pit-latrines. We shall drink water from the tube-wells. If it is not available, we shall boil water or use alum.
10. We shall not take any dowry at our sons' wedding; neither shall we give any dowry at our daughters' wedding. We shall keep the centre free from the curse of dowry. We shall not practice child marriage.
11. We shall not inflict any injustice on anyone; neither shall we allow anyone to do so.
12. We shall collectively undertake bigger investments for higher incomes.
13. We shall always be ready to help each other. If anyone is in difficulty, we shall all help him or her.
14. If we come to know of any breach of discipline in any centre, we shall all go there and help restore discipline.

15. We shall introduce physical exercise in all our Centers.

16. We shall take part in all social activities collectively.

### **10 Indicators of poverty elimination:**

According to Grameen Bank, a recent internal survey shows that, 68 per cent families of Grameen borrowers have crossed the poverty line. The remaining families are moving steadily towards the poverty line from below. (Grameen Bank, 2010)

Grameen bank uses the following ten indicators to identify elimination of poverty level of the borrower:

1. The family lives in a house worth at least Tk. 25,000 (twenty five thousand) or a house with a tin roof, and each member of the family is able to sleep on bed instead of on the floor.
2. Family members drink pure water of tube-wells, boiled water or water purified by using alum, arsenic-free, purifying tablets or pitcher filters.
3. All children in the family over six years of age are all going to school or finished primary school.
4. Minimum weekly loan installment of the borrower is Tk. 200 or more.
5. Family uses sanitary latrine.
6. Family members have adequate clothing for everyday use, warm clothing for winter, such as shawls, sweaters, blankets, etc, and mosquito-nets to protect themselves from mosquitoes.
7. Family has sources of additional income, such as vegetable garden, fruit-bearing trees, etc, so that they are able to fall back on these sources of income when they need additional money.
8. The borrower maintains an average annual balance of Tk. 5,000 in her savings accounts.
9. Family experiences no difficulty in having three square meals a day throughout the year, i.e. no member of the family goes hungry any time of the year.
10. Family can take care of the health. If any member of the family falls ill, family can afford to take all necessary steps to seek adequate healthcare.

This analysis will look at how corporate governance is practiced in Grameen bank and we will link this practice with the Code of Corporate Governance of Bangladesh. Since we have

already given a brief background of this code in the literature review, we will proceed with the analysis.

## *4.2 Analyzing Corporate Governance and CSR practice in Grameen Bank*

In this part of the paper we try to link some aspects postulated by the corporate governance code of Bangladesh and see how this is visible in GB. We will also try to link expansion with CG and CSR in GB drawing from our literature review and theoretical framework.

### *4.2.1 Board structure*

Beginning with the Board structure, it is important to note that the Board of Directors is the central entity in a functioning corporate governance system since it is the governing body of any organization. According to the Corporate Governance Code of Bangladesh (2004), the board is accountable to the shareholders and/or stakeholders of the organization. One important feature of the code is that the code encourages boards to become more proactive and effective by training directors in corporate governance and their responsibilities. Moreover the code also states that the board should also ensure a succession plan for senior management and the MD/CEO. The code also suggests that the majority of the board of directors should be independent and non executive. Moreover, it should consist of 7-15 members. Furthermore, separation of MD and Chairman has been proposed. The table below shows the composition of the Board of Grameen Bank with respect to number and disparity in number between executive and nonexecutive directors.

**Table 2: List of Managing Director and Chairman since 2004 to 2008**

<b>Year</b>	<b>Managing Director</b>	<b>Chairman</b>	<b>No of executive Directors</b>	<b>No of non executive Directors</b>	<b>Board size</b>
2008	Prof. Md Yunus	Mr. Tabarak Husain	10	3	13
2007	Prof. Md Yunus	Mr. Tabarak Husain	10	3	13
2006	Prof. Md Yunus	Mr. Tabarak Husain	10	3	13
2005	Prof. Md Yunus	Mr. Tabarak Husain	10	3	13
2004	Prof. Md Yunus	Mr. Tabarak Husain	10	3	13

*Source: Annual report (2004-2008)*

We decided to take a comparison with respect to the above table from 2004 because the code was published in 2004. We found that the board consists of 13 members and is unitary in nature. It consists of 3 non-executive members including an independent chairman. The executive directors are selected through five phase screening from root level (from the interview of Branch Manger). From the table we can clearly see that the chairman of the board and the managing director are two different individuals. Also, there is a fair representation when we look at the different categories of the board members; nine are from the borrowers who also double as the owners of the bank. But concerning the match in number of executive and non executive directors it was not very attractive when we compared it to the laid down principles put forward by the Code of Corporate governance of Bangladesh. This we shall deal more on when looking at a critical view of the practice of corporate governance in Grameen bank in the next part of this paper. From the table above it can be seen that Professor Mohammed Yunus has been the Managing director of the company since the bank was founded in 1973; on the other hand Mr. Mr. Tabarak Husain is acting as chairman since 2003.

#### *4.2.2 The CSR practice in Grameen Bank*

Though Corporate Social Responsibility (CSR) has become a driving force in many service based business, still there is debate about CSR and its role. Friedman questioned whether a business can have any social responsibilities to increase its profit (Friedman 1970); however other authors disagreed. They tried to see it from a broader perspectives rather than a restricted point. Vogel (2005) tried to illustrate it as the market of virtue. He felt that at least no one has proven that CSR has a negative relation with profit. While Carroll (1979) believes that social responsibility of business encompasses the economic, legal, ethical and discretionary expectations that society has of organizations at a given point in time.

According to Yunus (2007, pg 15) CSR takes two basic forms.

One, which might be called "weak CSR," has the credo: *Do no harm to people or the planet (unless that means sacrificing profit)*. Companies that practice weak CSR are supposed to avoid selling defective goods, dumping factory wastes into rivers or landfills, or bribing government officials.

The second form, "strong CSR," says: *Do good for people and the planet (as long as you can do so without sacrificing profit)*. Companies that practice strong CSR actively seek out

opportunities to benefit others as they do business. For example, they may work to develop green products and practices, provide educational opportunities and health plans for their employees, and support initiatives to bring transparency and fairness to government regulation of business. Grameen Bank can be placed close to the second form as it is socially concerned even though to a certain extent, this is still subject to debate as we are going to find out in the critical evaluation.

#### *4.2.3 Grameen Bank and New Institutionalism*

According to Selznick (1996) an organization can be viewed as a "as an institution" when it has a going concern of taking account of relevant stakeholders, attending to long-run interests, being sensitive to the operative structure of authority rather than just regarding business as the voluntary association of shareholders who own the enterprise and are the only members who really count. After the revolution of micro credit Grameen Bank came a long way. Transformation from a project to a bank, improvisation of Grameen Bank I to Grameen II finally results into Social business. It's a business designed to meet a social goal. A social business is a business that pays no dividends. It sells products at prices that make it self-sustaining. The owners of the company can get back the amount they've invested in the company over a period of time, but no profit is paid to investors in the form of dividends. Instead, any profit made stays in the business—to finance expansion, to create new products or services, and to do more good for the world. (Yunus, 2007)

The Flood in 1998 was one of the worst of the history of Bangladesh. In it Thirty million people were driven from their homes, over a thousand people were killed, and two rice crops were badly damaged. One hundred and fifty-four members died in the flood; many more lost family members and the homes, farms, and farm animals of many were washed away. Over half of GB borrowers, and more than 70 percent of GB branches, were affected by the flood. After more than fifteen years of operation, Grameen was ripe for change—and the great flood of 1998 provided the opportunity for a major upgrade of the system. Over the next two years, Grameen staff around the country participated in an extensive process of rethinking the bank's operations, looking for ways to strengthen its economic footing, make its products more relevant to the needs of members, and increase its flexibility in dealing with changing conditions and needs. .So Grameen – II was born. Which was more flexible and responsive system By August 2002, Grameen II had been adopted throughout the country. (Yunus, 2007, pg-64)

**Table 3: From Grameen I to Grameen II: A More Flexible, Responsive System**

<b>Grameen I</b>	<b>Grameen II</b>	<b>Reason for change</b>
No provision to save for pension	Borrower deposits a fixed monthly amount in Grameen pension scheme	To help borrowers build a nest egg for retirement.
Fixed, one-sized-fits-all savings program	Varied savings plans to fit members individual needs	To encourage saving for special needs and long-term economic benefit.
No initiative to collect savings from non members	Active campaigns to collect savings from non members	To enable the bank to self-fund future loans.
Mostly one year loans with fixed installment amounts	Loan duration and installment size may vary	To allow borrowers to tailor loan products to individual needs and changing circumstances.
Common loan ceiling for the entire branch	Individual loan ceilings based on savings and other measurements	To reward and incentivize good borrowing and repayment practices by members.
Family responsible for loan of deceased borrower	Special saving funds ensures that outstanding loans are paid off after death	To alleviate borrowers' fears of leaving debt behind after death.
Borrower becomes defaulter If loan is not repaid in 52 weeks	Borrower becomes defaulter if repayment schedule is not met within six months	To create an early warning signal of potential borrower problems.
Funds for new bank branches borrowed from head office at 12 % interest	New branches are self funding from day -1 using savings from borrowers and non borrowers	To ensure that branches become self-sufficient quickly.

*Source: Muhammad Yunus (2007)*

First successful example of Social business is Grameen Danone, started its journey in 8 November of 2006. This is a family organization of Grameen Bank. Grameen Danone Foods will reduce poverty by creating business and employment opportunities for local people since raw materials including milk needed for production, will be sourced locally. The companies that make up Grameen Danone Foods Ltd. have agreed not to take out any of the profits out of the company. Instead they will invest these for creation of new opportunities for the welfare and development of people. Hence it is called 'social business enterprise (Yunus, 2007).

#### 4.2.4 Expansion of Grameen Bank

From the above we have clearly seen that Grameen Bank is not a conventional bank like other banks which aim primarily at profit maximization; rather its main objective is to alleviate poverty by being a banker to the poor. Going through the annual reports of Grameen bank, we realized that this bank has recorded tremendous success since it was created as an NGO in 1973 till today as a full fledged bank (except in 1983, 1991, 1992, as a result of the famine and natural-flood that hit Bangladesh in this period). This therefore means that had if there was no disaster in these years, Grameen Bank probably would not have made any losses during those years, since ever thereafter, it has been growing and expanding very fast. The table and figure below gives more light with respect to this:

**Table 4: Grameen Bank Historical data series**

<b>Performance Indicator</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>
Cumulative Disbursement (All Loans)	4416.82	5025.61	5954.02	6685.51	7591.32	8741.86
Disbursement During the Year (All Loans)	430.36	608.79	724.96	934.94	905.81	1150.54
Year-end Outstanding Amount	312.96	415.82	471.19	529.53	646.05	791.82
Housing Loan Disbursement During the Year	4.74	2.95	2.01	1.4	2.21	2.43
Number of Houses Built cum	607415	627058	641096	650839	665568	679577
Total Deposits (Balance)	343.52	481.22	633.31	756.61	933.89	1200.49
Deposits of GB Members (Balance)	228.70	306.10	390.48	430.39	508.20	648.68
GB Members' Deposit as % of Total Deposit	67	64	62	57	54	54
Number of Groups	685083	877142	1086744	1168840	1210343	1253160
Number of Members	4059632	5579399	6908704	7411229	7670203	7970616
Percentage of Female Members	96	96	97	97	97	97
Number of Villages covered	48472	59912	74462	80678	83566	83458
Number of Branches	1358	1735	2319	2481	2539	2562
Profit/Loss (For the Year)	7.00	15.21	20.00	1.56	18.99	5.38

*(Amount in Million USD)*

*(Source: Grameen Bank official website)*

The above figures points to the fact that even in the recent economic crunch that hit many banks especially in the USA, Europe and Asia, Grameen Bank still showed some growth; just like Yunus the CEO of GB puts it forward in GB's 2008 annual report:

“... GB has not only succeeded in deflecting the fallouts from the global economic chaos it continued its forward march with renewed vigour and enthusiasm throughout 2008 ...”

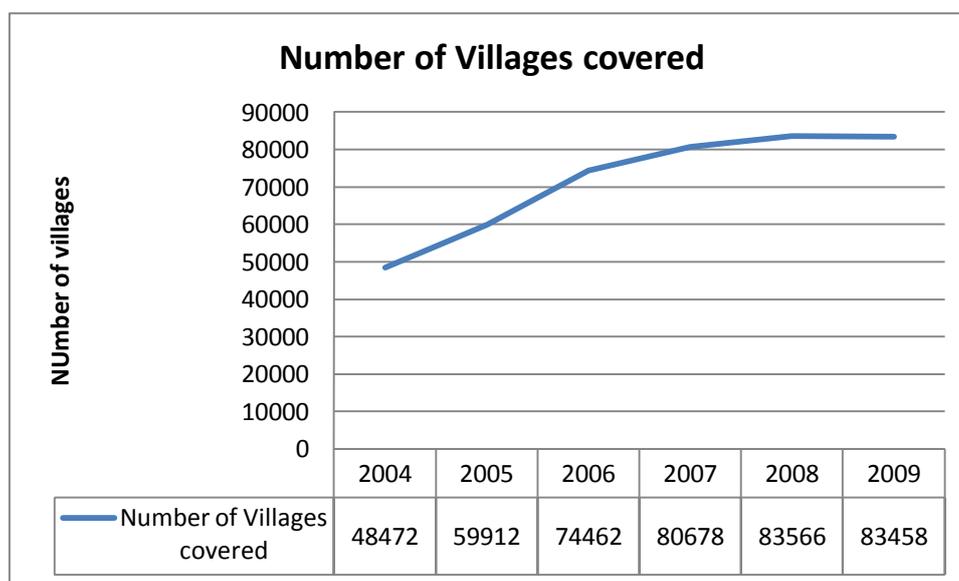
In the upcoming part we have done an in-depth analysis of the above mention performance indicators. We have also tried to assess the indicators to see the business expansion of the company and linked it to different aspects of corporate governance and corporate social responsibility.

The expansion of Grameen bank can also be assessed in terms of the number of villages covered by the bank over the years. The table and figure below shows the upward trend in the number of villages covered by Grameen bank from 2004 to 2009.

**Table 5: Number of villages covered**

Years	2004	2005	2006	2007	2008	2009
Number of Villages covered	48472	59912	74462	80678	83566	83458

(Source: Annual reports of Grameen Bank, 2004 to 2009)



**Figure 5: Number of villages covered (Source: annual reports of GB, 2004 to 2009)**

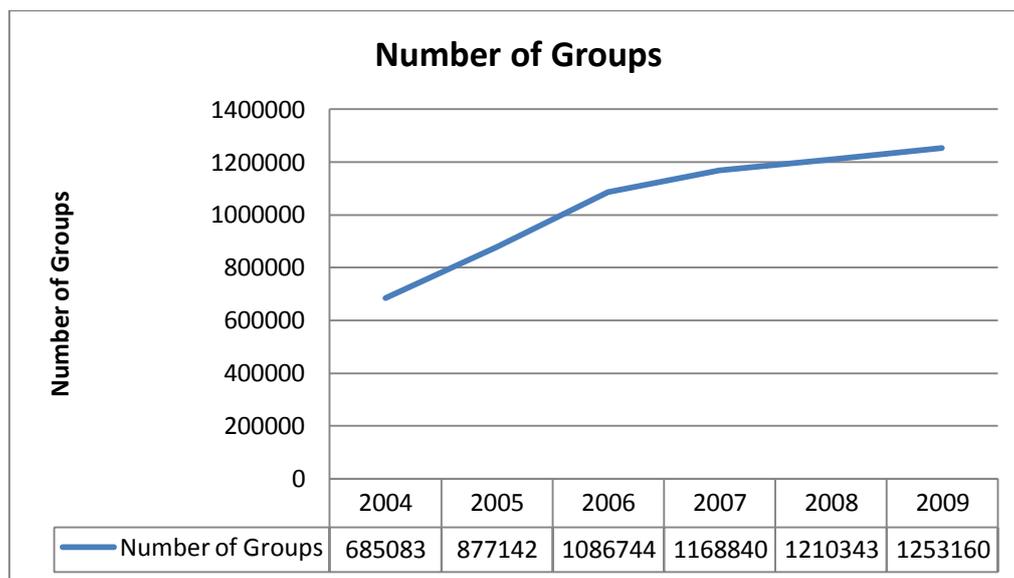
From the table and figure above, we can clearly see that GB showed a continuous improvement from 2004 to 2009 with respect to the number of villages covered by the bank. For example in 2004 the bank covered a total of 48,472 villages while this number moved right up to 83,458 villages in 2009.

Also, to obtain loans from GB customers must belong to a credit group. A group is composed of at least three members. This therefore means that an increase in the number of credit groups signifies an increase in the number of borrowers and vice versa. The table and figure below shows the number of credit groups from 2004 to 2009.

**Table 6: showing the number of credit groups**

Years	2004	2005	2006	2007	2008	2009
Number of credit Groups	685083	877142	1086744	1168840	1210343	1253160

*(Source: Annual reports of Grameen Bank, 2004 to 2009)*



**Figure 6: The number of credit groups (Source: annual reports of GB, 2004 to 2009)**

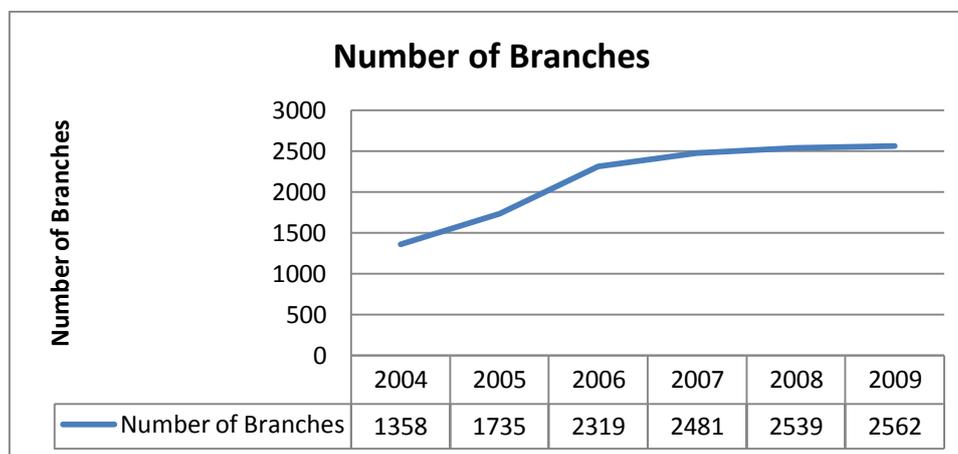
From the table and figure above, we can clearly see that the number of credit groups in GB showed an upward trend from 2004 to 2009; increasing from 685,083 credit groups in 2004 to 1,253,160 credit groups in 2009. This indicates that there was a massive increase in the number of borrowers as the years went by and this is an indicator of growth.

Another key issue that indicates expansion in banks and other financial institutions is the number of branches that the bank or financial institution has. A self-regulatory bank like GB that does not receive funds from donors can only create more branches if it has some reserves from the past ploughed back for expansion purposes. The table and figure in the next page shows the number of branches that GB was operating in from 2004 to 2009.

**Table 7: Number of villages Branches**

Years	2004	2005	2006	2007	2008	2009
Number of Branches	1358	1735	2319	2481	2539	2562

(Source: Annual reports of Grameen Bank, 2004 to 2009)



**Figure 7: The number of branches (Source: annual reports of GB, 2004 to 2009)**

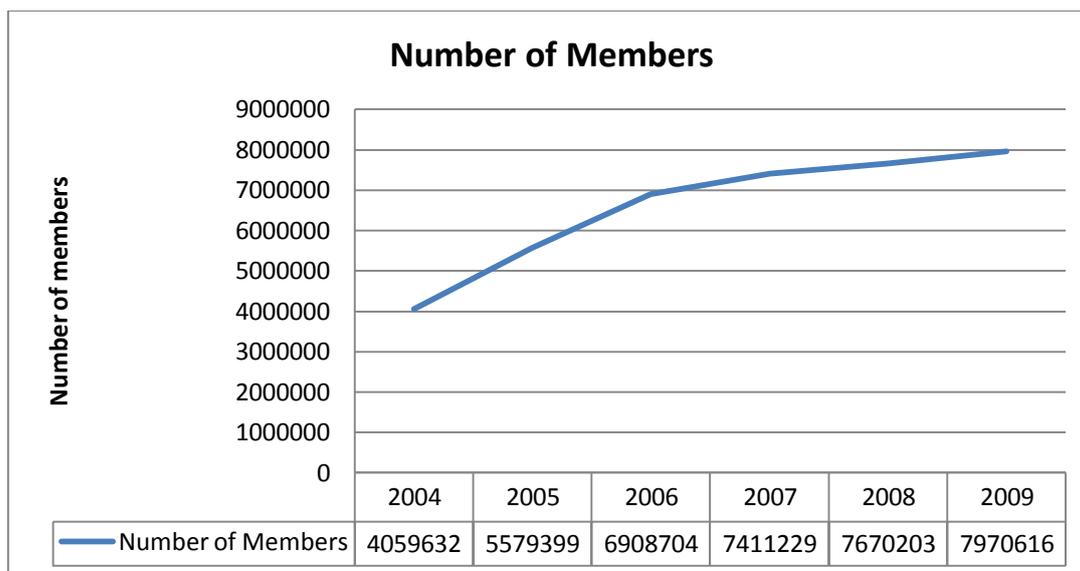
The above table and figure indicates that Grameen bank witnessed an upward trend regarding the number of branches from 2004 to 2009. For example, it had a total of 1358 branches in 2004. From 2004 to 2005 the number of branches increased by 377, giving a total of 1735 branches in 2005. These points to the fact that, based on the figures, averagely a new branch was created every day from 2004 to 2005. In 2009, the total number of branches moved right up to 2562.

Any business that has a high clientele will easily increase in size and expand. Increasing the number of branches in GB without a corresponding increase in the number of member of the bank cannot result to expansion. Rather it will mean that capital is tight down (considering the expenses needed to open a new branch). The table below and figure in the next page gives a picture of the number of Grameen members from 2004 to 2009.

**Table 8: The number of members**

Years	2004	2005	2006	2007	2008	2009
Number of Members	4059632	5579399	6908704	7411229	7670203	7970616

(Source: Annual reports of Grameen Bank, 2004 to 2009)



**Figure 8: The number of members (Source: annual reports of GB; 2004 to 2009)**

The above table and figure still shows an upward trend in the number of members from 4,059,632 members in 2004 up to 7,970,616 members in 2009. This therefore points to the fact that probably, the new branches created as shown in table 3 and figure 3 above was meant to take care of the increasing number of borrowers. This is an indicator of growth.

All the above points to the fact that GB has witnessed tremendous growth and expansion over the year (for purpose of simplicity, we considered the growth trend from 2004 to 2009).

### *4.3. Corporate governance and expansion of GB*

#### *4.3.1 Financial reporting, auditing and financial disclosures*

Firstly, concerning disclosure of financial statements, GB does this well and accounts are actually audited by independent auditors in accordance with to the Code of Corporate Governance for Bangladesh as seen above. But looking at the Code of Corporate Governance for Bangladesh, the duties and responsibilities of external auditors are still subject to providing an opinion as to whether the accounts present a true and fair view of the business. But it is important to note that according to the Financial Services and Markets Act 2000 auditors have an extended responsibility of reporting to external regulators breaches of laws and regulations such as insider trading or breaching of solvency requirements for banks or insurance companies (Morrison, 2007). The following table shows the rotation of auditors of GB from 1999 to 2006.

**Table 9: List of External auditors over the years**

<b>Year of reparation of financial statements to be audited in GB</b>	<b>Auditors of financial statements</b>
1999	HOWLADAR YUNUS & CO, HODA VASI CHOWDHURY & CO, Chattered Accountants
2000	Rahman Rahman Huq, Ahmad & Ahmad, Chattered Accountants
2001	Ahmad & Ahmad, Mahfel Huq & Co, Chattered Accountants
2002	Rahman Rahman HUQ, Mahfel HUQ & Co, Chattered Accountants
2004	Hoda Vasi Chowdhury & Co, Howladar Yunus & Co, Chattered Accountants
2005	Hoda Vasi Chowdhury & Co, S.F Ahmed
2006	Ahmad & Ahmad, S.F Ahmed & Co, Chattered Accountants

*(Source Annual Reports 1999-2006)*

Constant rotation of auditors all things being equal makes borrowers, depositors, the general public and other stakeholders of Grameen bank to be more confident with the information contained in the financial statements presented at the end of the year in the annual report and this makes these financial statements more credible. High credibility of financial statements can go a long way to enhance growth all things being equal.

Also, full disclosure of end of year financial statements (profit and loss accounts, balance sheets, statements of cash flows and statements of changes in equity) reduces the opacity of Grameen bank and narrows down the idea of insiders and outsiders regarding information (information asymmetry).

#### *4.3.2 Credit Monitoring and Credit Assessment*

From the literature review we mentioned that one of the key factors that call for corporate governance in banks is regarding risk. Since banks are financial leverage institutions which earn a return by taking risks, risks control is a key issue when we look at CG in banks. Unlike normal conventional banks, GB bank gives out loans to the poor without collateral security which is almost a direct opposite of what is being held by banking models. This complicates the issue when one tries to link this to risk sensitivity of banks and other businesses as put forward by the Code of Corporate Governance for Bangladesh. At first one may be tempted to believe that GB gives credit only to those who cannot pay back (just like throwing money away), but that's not the case. GB bank's credit risk sensitivity is more linked to ethics than rationality based on confidence and trust. Hence in corporate terms, other banks monitor risk both before giving

credit and after the borrower gets the loan, and before a borrower obtains a loan, he or she must present acceptable collateral security so that in case of any default of payment, the bank seizes the asset that was set aside as collateral. GB on the other hand monitors credit risk before a loan is given to a customer by giving loans only to customers belonging to a credit group as explained above. This means that there is no monitoring of borrowers. But the corporate measure that GB takes to make sure that it does not have excessive loan losses is that it only gives out bigger loans to the same borrower after the previously smaller loan taken by the borrower has been repaid. So far, the repayment rate has been very high. For example it was 98, 82% in 2006, 98, 02% in 2007, and 98, 32% in 2008 (comparative consolidated statement for 2006, 2007, and 2008). This very high rate of timely loan repayment in Grameen bank as a result of its lending policy that safeguards against losses based mostly on ethics and trusts than rationality reduces the mismatch between deposits and loans and hence makes liquidity readily available for future borrowing; and thus enhances the bank's expansion.

**Table 10: Repayment rate over the years**

<b>Year</b>	<b>Repayment Rate</b>
2004	99.05
2005	99.01
2006	98,82
2007	98,02
2008	98,32

*(Source: Comparative Consolidated Statement for the Years 2004 & 2008)*

However, in our interview with the branch manager<sup>1</sup> (our interviewee) we tried find out the implementation if the credit monitoring system that Grameen Bank follows. He said that in reality it is not always possible or maintain the credit risk monitoring method in groups as the competition is too high. Since some other banks are offering micro credit loans. Moreover, the borrowers not always interested to join a group to get loan rather they go for the banks which has flexible credit policy. This points to the fact that it is necessary as part of TRM in GB, this aspect should be looked into. Confidential

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<sup>1</sup> The identity of the branch manager will be kept confidential due to privacy measures.

As seen above, compensation structure of bank executives can cause them to take excessive risk and vice versa and this complicates their objectivity as far as risk management is concerned since most often they usually have their interests to protect. Empirical studies have documented that CEOs who are insulated from shareholder pressure and do not receive high-powered pay are less prone to engage in risk-taking (Lucien & Spamann, 2010). The latter is much similar to what holds in Grameen Bank. In GB top managerial decisions are initiated by the founder of the bank (M. Yunus) who is also the managing director of the bank. The table below shows his salary and allowances for the years 2008 and 2009.

**Table 11: Managing Directors salary and allowances (figures BDT)**

<b>Salary and Allowances</b>	<b>2009</b>	<b>2008</b>
Basic salary	378,000	276,000
Dearness allowances	27,600	27,600
House rent allowances	138,000	138,000
Medical allowances	6,000	6,000
Domestic aid allowance	12,000	12,000
Entertainment	7,080	7,080
Bonus	46,000	46,000
Felicitation allowance	23,000	23,000
<b>Total</b>	<b>637,680</b>	<b>535,680</b>

*(Source: Notes to the Financial Statements 2009)*

From the table we realize that the salary and bonus structure is made up of the following:

Basic salary, Dearness allowances, House rent allowances, Medical allowances, Domestic aid allowance, Entertainment, Bonus, Felicitation allowance. From the above figures we can see that the bonuses and other allowances of the managing director of GB are fixed between 2008 and 2009. The difference in the basic pay is probably brought about by long term expansion. These fixed remuneration packages point to the fact that there is no special motivation in this bank for top management to strive to make extra profits by engaging in excessive risk taking since there is no extra bonus based on profits made. We came to this conclusion because, despite the fact that there was profit disparity between 2007 and 2008, the bonuses remained fixed. This is a very important corporate governance measure in GB unlike other conventional banks whose CEOs have a remuneration scheme designed in such a way that

they are insulated in any downturn of risk but receive a bonus if a risky investment turns out to be profitable. Hence, top management of GB is more interested in growth and expansion rather than on short term bonuses; one of the reasons for the rapid expansion over the years.

#### *4.4 The service profit chain and business ethics*

Roberts (2001) looking at the proliferation of talk and writing regarding business ethics in the corporate world drew upon Levinas's phenomenology of ethics in "Otherwise than Being or Beyond Essence". According to Roberts (2001) to Levinas,

*"The ground of ethics lies not within being- as reason, or thought, or choice- but rather in beyond essence in the way that- from the start, the other affects us despite ourselves"*

This is the kind of stakeholder ethical thinking that Yunus portrayed in GB. The fact that the inspiration behind GB stemmed from the over told story of Yunus' visit to a village and giving a woman some money who was being exploited by money lenders to buy her raw materials and make bamboo baskets...etc (as seen above in the historical part) points to the fact that he was thinking from Levinas' phenomenology of ethics perspective- a business philosophy he further expanded and coined it "social business and banking for the poor".

In our interview with the branch manager we tried to find out some of the criteria being used to recruit employees in GB (2011). He told us that:

*"In addition to professional and educational qualification, it is very important that as an aspiring employee of GB, you possess some emotional qualities of feeling for others and having a great desire to do good even if the reward you get is not big enough financially and that you need to be someone who is contented with what he has and be of good moral character"*

The above simply point to the fact that, the employees of GB share in Yunus' vision of social business- of people working hard for moderate pay and gaining much joy in seeing poor people waking up from poverty.

Now how has this brought about expansion in GB?

Haskett (1994) and Zeithaml and Bitner (2003) explains the service profit chain- how service quality can lead to employee satisfaction, productivity which will then enhance external

service value and make customers to be loyal, thus bringing in more profits and revenue growth.

The profit trend of GB as seen above cannot be overemphasized- the figures are clear and real. Embracing a corporate ethical business philosophy (Levinas phenomenology of ethics) of doing good for good and employing employees who share in this vision, Yunus and his management team succeeded in building an internal service quality and satisfying employees through moderate remuneration and an additional satisfaction founded on the grounds of ethics. Once these employees were satisfied they saw themselves as our interviewee put it:

*“as an employee of GB I see myself not just as an ordinary employee working just for a salary but also as someone involved in a course for change focused towards poverty alleviation”*

This makes the employees to put in their best resulting in high productivity which will intend lead to high external service provision to satisfy the customers.

Now, to complete the link of the service profit chain, we need to carefully consider the aspect of customer loyalty in GB. Customer satisfaction and high quality external service provision does not necessarily mean customer loyalty. Satisfaction can easily lead to loyalty if satisfactory service has a competitive advantage.

From the figures regarding performance indicators above with respect to the number of borrowers in GB, we can see an exponential growth rate in the number of customers over the years. We identified two reasons for customer loyalty in GB namely:

- Reasons related to the explanation from the service profit chain- that high external employee productivity leading to high external service provision and hence customer (borrowers) loyalty and
- The nature of GB customers. This type of loyalty results from the fact that Bangladesh is one of the poorest countries in Asia with a population more than 158 million people. (world fact book, 2011)

Many of these people before the setting up of GB had no credit history and hence could not secure loans from the normal conventional banks which were operating in Bangladesh at that time due to limited collateral security. GB’s policy of lending without collateral security to the poor made the poor to see this as a dawn of a new opportunity. This therefore partly explains the loyalty of GB borrowers.

The table below gives a summary of an integration of Levina’s phenomenology of ethics as postulated by Roberts (2001) and the service profit chain in the context of GB.

**Table 12: The service profit chain and expansion in GB informed by Levina’s phenomenology of ethics**

<b>Service profit chain element</b>	<b>Element realization drawing from Levina’s phenomenology of ethics</b>
Internal service quality	Realized through a foundation of ethics (doing good for good) believing that the others affects us despite ourselves, instilled by Yunus and inspired by the woman making bamboo baskets and also through moderate remuneration
Employee satisfaction	Because they share in the vision (internal quality) and because many of them were unemployed graduates before the coming of grameen bank; so small pay does not really matter. At least is better than no pay at all.
employee retention	Because they are satisfied
Employee productivity	Because of all of the above
External service value	Because of all of the above
Customer satisfaction and loyalty	As a result of high quality external service provision and the nature of borrowers as explained above
Revenue growth and profit	Customer loyalty

#### *4.5 CSR: The triple bottom line philosophy and the expansion of GB*

Drawing from the works of Freeman, Johnson (2006) says that CSR is a sound investment according to sound investment theory, the stock market reacts to firms’ actions and socially responsible behaviors will be rewarded by the market.

Linking CSR to business expansion or making an argument for a business case for CSR is very problematic. CSR can easily result to business expansion when customers are aware of CSR and the importance of incorporating the concept into business. We have seen above how Grameen bank does business from a stakeholder perspective and has made profit over the years though the environment as a stakeholder is mute because Grameen Bank doesn’t maintain any environmental standards. However, *16 decisions* for the borrowers show a weak concern for environment (from the interview with the branch manager). Thus, there is therefore no clear balance of the three bottom lines in Grameen bank.

Regarding publishing CSR or Sustainability Report of Grameen Bank, the response is of our interviewee was that Grameen Bank is not concerned about publishing any CSR report as most of the borrowers are illiterate, thus they are not in a position to analyze the report. In fact many employees of the bank are not aware of concept such as CSR or Triple Bottom line.

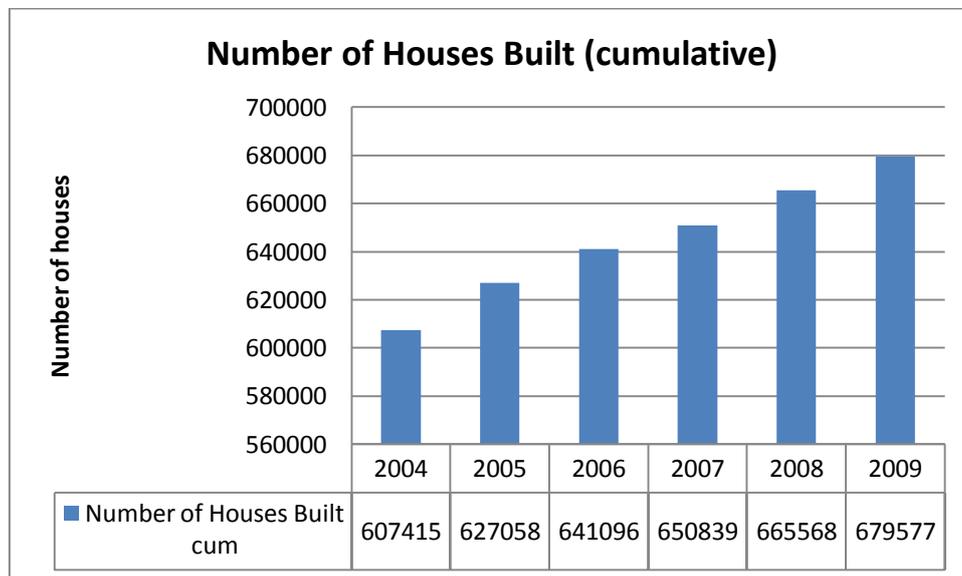
However to clarify some issues regarding CSR practice in GB, we are relying on secondary data. Here we are going to consider two important indicator of CSR in GB linked to social responsibility (the number of houses built and the amounts granted as scholarship to Grameen members).

The table and figure below shows the number of houses built:

**Table 13: Number of Houses Built (Cumulative)**

Years	2004	2005	2006	2007	2008	2009
Number of Houses Built cum	607415	627058	641096	650839	665568	679577

(Source: Annual reports of Grameen Bank, 2004 to 2009)



**Figure 9: The number of houses built (Source: annual reports of GB; 2004 to 2009)**

The above table and figure shows an upward trend in the cumulative number of houses built from 2004 to 2009. In the 2004 the total number of houses built was 607415, the number increased to 679577. Building more houses is one of the key indicators of breaking the cycle

of poverty and also one amongst the sixteen decisions found in the methodology of Grameen Bank.

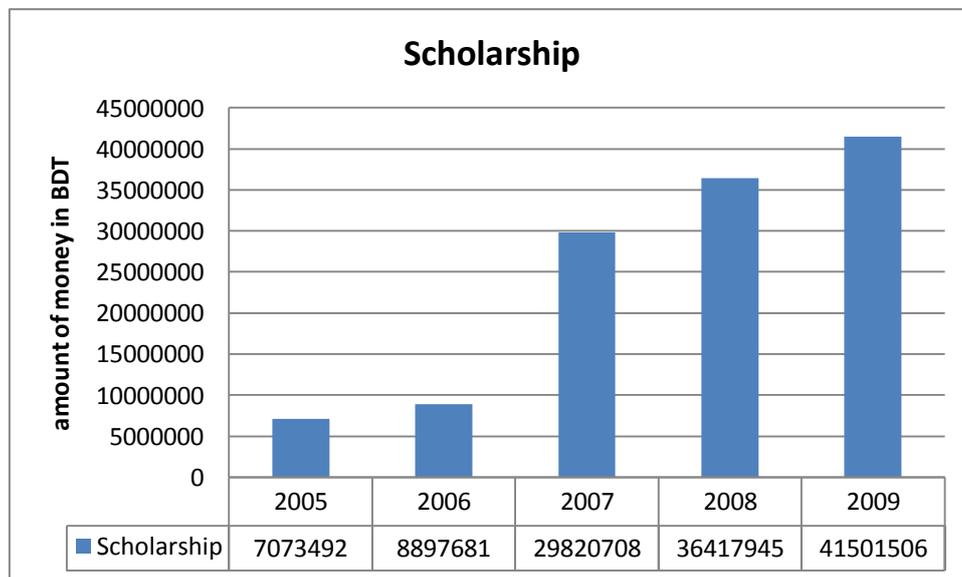
Also, Grameen has in its efforts to incorporate a stakeholder perspective has gladly ceased as obligation to award scholarships to Grameen children as shown in the table and figure below:

**Table 14: Amount of Scholarship given**

Years	2005	2006	2007	2008	2009
<b>Scholarship</b>	7073492	8897681	29820708	36417945	41501506

(Amount in BDT)

(Source: Annual reports of Grameen Bank, 2004 to 2009)



**Figure 10: The number of scholarship (Source: annual reports of GB; 2004 to 2009)**

The above table and the graph illustrate the amount of loan given to the children of the borrowers' form 2005 to 2009. In 2005 a total of 7073492 bdt was given as scholarship to the children of borrowers that were increased up to 41501506 bdt in 2009. However, Grameen Bank provides loans only to its own borrowers and not to borrower of any other micro credit institution. (from the interview of the Branch Manager). Education for children is also considered as one of the sixteen decisions of Grameen Bank. Both housing and education are treated as basic need and are also associated with community responsibility and benefits that can easily be linked to social values one of the pillar of triple bottom line.

If we take a look at the previous graphs we observe an upward trend in the number of members, number of village covered that proofs the expansion of bank. Similarly the number of houses and the total amount of scholarship has an upward trend. It is understandable that

with the expansion, the bank is focusing more on their main objective that is elimination poverty.

Trying to assess the role corporate governance and corporate social responsibility has played to enhance the growth of GB over the years is a bit problematic due to the nature of the bank, since most of the literature reviewed above with respect to corporate governance in banks was much more related to what holds in conventional banks and many assumptions regarding the above were based on conventional banking theory. But still we tried to take a critical view at the practice of corporate governance and CSR in Grameen Bank with special reference to the Code of Corporate Governance for Bangladesh.

## *4.6 Critical Evaluation*

### *4.6.1 Critical Evaluation of Corporate Governance Practice in Grameen Bank from a Global Perspective:*

From all what we have seen above it is obvious that it is a bit difficulty to actually see clearly how corporate governance is being practiced in GB owing to the fact that it does not operate like any other usual bank or business whose primary aim is profit maximization; rather it is a social business. In this part of the paper, we are going to carry out a critical evaluation of the corporate governance practice in GB from a global theoretical perspective.

Firstly, concerning disclosure of financial statements, GB does this well and accounts are actually audited by independent auditors in accordance with to the Code of Corporate Governance for Bangladesh as seen above. But looking at the Code of Corporate Governance for Bangladesh, the duties and responsibilities of external auditors are still subject to the Companies Act of 1985. That is the duty of providing an opinion as to whether the accounts present a true and fair view of the business. But it is important to note that according to the Financial Services and Markets Act 2000 auditors have an extended responsibility of reporting to external regulators breaches of laws and regulations such as insider trading or breaching of solvency requirements for banks or insurance companies (Morrison, 2007).

Also, we realized that despite the fact that GB has publicly disclosed its goals and mission and the nature of its operations in accordance with the Code of Corporate Governance for Bangladesh, there was some contradiction when we looked at the annual report of GB of 2008; GB claims that it is not an NGO because it is a self generating system and does not receive grants from donors but going through the notes to the accounts of 2008 we realized

that not 3.07 indicated that foreign funds were received from foreign donor agencies (IFAD 161 BA, IFAD 239 BA, NORAD, SIDA, Dutch Grant and JBIC) by Grameen Bank under the subsidiary loan agreement with the Government of the Peoples Republic of Bangladesh.

Another area of interest is the board structure. The board structure in particular and the organizational structure in general of any business have a very big role to play when it comes to corporate governance. As at 2008 96% of the deposits of GB were from borrowers who are also the owners of the bank while the remaining 4% is from the government. Looking at the organizational structure of GB from the 2008 annual report, we realized that the bank is headed by a board of directors which is composed of thirteen members. And just as we have seen in the analysis this board consists of three non-executive directors and ten executive directors. This is contrary to the Code of Corporate governance for Bangladesh which stresses that there should be a balance between executive and non executive directors or if needs be non-executive directors should even exceed executive directors to ensure better accountability and transparency.

Another point that really caught our attention was the nature in which GB bank gives out loans which is almost a direct opposite of what is being held by banking models. GB lends to the poor without collateral security. This complicates the issue when one tries to link this to risk sensitivity of banks and other businesses as put forward by the Code of Corporate Governance for Bangladesh. At first glance we saw this as though GB gives credit only to those who cannot pay back (just like throwing money away), just as we mentioned above but finally we realized that GB bank's credit risk sensitivity is more linked to ethics than rationality based on confidence and trust. Hence in corporate terms, other banks monitor risk both before giving credit and after the borrower gets the loan, and before a borrower obtains a loan, he or she must present acceptable collateral security so that in case of any default of payment, the bank seizes the asset that was set aside as collateral. GB on the other hand monitors credit risk before a loan is given to a customer by giving loans only to customers belonging to a credit group as explained above.

We also noticed that the Code of Corporate Governance for Bangladesh just like the Combined Code of UK and the King Report of South Africa is on a ``comply or explain basis'' for all listed companies. GB is a listed company in the Bangladesh stock exchange but going through the annual reports of GB from 1983 to 2008 there was no note that explains

any significant deviations from the Code despite the fact that there were some deviations as seen above.

Concerning CSR, we are already aware that GB is referred to as a social business whose primary aim is not profit maximization but rather it is aimed at ‘‘putting poverty in a museum’’. This points to the fact that GB is stakeholder oriented and its objectives are mostly geared outside beyond the borders of the bank. This can be seen through its scholarship schemes as mentioned above. But there is something paradoxical about this that also caught our attention. GB only provides scholarships to the children of Grameen members. And at the same time, these Grameen members or customers of GB are the owners of GB. This in the wider perspective might still be seen as a business which is owner oriented, and this scholarships can be seen as a marketing strategy to cajole more customers and this too in a way contradicts Yunus’ (the Managing Director and founder of GB) idea of strong and weak Corporate Social responsibility.

#### *4.6.2 Sustainability reporting and environmental protection*

Sebhatu (2011) looked at a case on SPM based on organization’s values and its ability to communicate and implement its strategies through proactive corporate social responsibility and his study suggested that reporting represents a company’s commitment and ability of communication with external stakeholders. Many companies and banks today present a sustainability report as part of their external reporting showing their concern to the environment and other aspects relating to CSR. This aspect is absent in Grameen bank. We tried to find out from our interviewee why Grameen bank does not have any sustainability or CSR report in their annual reports and whether they intend to do that in the near future?

He said that:

*‘‘Environmental concerns are not really a top priority of Grameen bank. We are interested in alleviating poverty by serving as a banker to the poor. Many of our customers who are a major stakeholder of the bank are not even familiar with this. All they are interested in is to get loans, invest them and repay. We therefore do not intend to publish such report in future’’*

The fact that GB do not consider the environment as a very important stakeholder greatly complicates the triple bottom line thinking philosophy in this financial institution that call for a balance between the TBLs.

#### 4.6.3 Corporate governance and the business as a going concern

It is part of governance of banks and other companies that the management of every business should ensure the training of young staff to replace people in top managerial position especially when they go on retirement. Recent developments in GB indicates that Yunus (the brain child of the bank and acting CEO of GB since 1971) needs to go on retirement owing to the fact that he has reached the retirement age according to the laws of the Republic of Bangladesh. Recently, the central bank of Bangladesh has relieved him from his duty mentioning that he has crossed the age of his retirement already and that he is holding the position of MD illegally. However, Yunus has taken this matter to the Supreme Court where his petition was refused. At the same time Yunus said to the media that he will resign through a smooth transition of management leadership from him to the next MD. (The Daily Star, 2011)

The question that comes to mind now is what will happen to GB after Yunus is gone? Has staff been trained adequately to fit into his shoes? These are some of the questions we tried to find out from the branch manager (our interviewee) and this is what he said:

*“Sincerely, I and many others in my position really do not know what will happen to this bank when Yunus is gone. His presence alone and his international recognition has contributed to the success of the bank a great deal. Infact many employees and customers frown at the idea that he should retire now. I don’t think there is anyone who have adequately been trained to fit into his shoes and be trusted by the borrowers like they trusted Yunus”*

If the above statements from the branch manager are true, it means that the proactive element of adequate employee training which part of TRM was neglected in GB. Another element one can draw from the above is that GB’s expansion was also linked to TRUST and CONFIDENCE in Yunus. He was and he is still in the most part considered “an image of truth” by the borrowers.

The fact that Yunus studied in the USA, got a Phd in Economics and went back home to meet a country drowning in poverty with a very high illiterate population made his idea of “a bank for the poor” to be conceived as a divine intervention with Yunus being regarded as the mesire.

## ***5. Summary, Conclusions and Recommendations***

The main aim of this thesis was to look at the role of Corporate Governance and Corporate Social Responsibility in Business Expansion with special reference to Grameen Bank as case study. At the beginning the analysis we tried to give a picture of the success that Grameen Bank has recorded over the years with special reference to the annual report of GB. The profit figures, number of borrowers, number of branches, and number of villages covered and number of houses built showed an upward trend over the years indicating that Grameen Bank has been growing and expanding. The reason why we showed this expansion was to put forward a picture of what we were trying to prove (that is the role corporate governance and corporate social responsibility has played in the expansion of GB), so we thought it was necessary to first of all show quantitatively that GB was expanding before giving the reasons behind this expansion which are linked to CG and CSR.

In the introductory and literature review section of the paper we saw how some banks have failed due to poor corporate governance. The argument that we had in mind was that, of poor governance can lead to bank failure and if failing banks can be resurrected by instituting good corporate governance it therefore means that continuously good corporate governance cannot only stop banks from falling but can go a long way to facilitate expansion; the same with CSR.

From the above analysis we therefore conclude as follows:

Grameen Bank practices corporate governance and CSR to a certain extent. CG practice in Grameen bank is not very similar to what holds in conventional banks due to the nature of GB (social business). CG in GB can be seen through disclosures of financial information, auditing of accounts and constant rotation of auditors, remuneration structure of the managing director designed in such a way that he gets no extra benefit for taking excessive risk by lending to unworthy customers (here we are talking of customers that do not belong to a credit group), and credit risk monitoring by lending money only to customers belonging to a credit group and giving out big loans to the same borrower only when he or she repays the former small loan. Disclosure increases depositor's and other stakeholders' confidence, auditing lends credibility to the financial statements and further increase confidence of depositors and reliability on GB, credit risk monitoring witnessed more as a question of ethics and trust not rationality makes it possible for those without collateral security to obtain loans from Grameen bank and also facilitates repayment since bigger loans are obtained only

on repayment of smaller loans. All these facilitate business growth and expansion. Therefore corporate governance has a role to play in the growth and expansion of GB.

We also saw looked at how we could explain the philosophy behind GB drawing from Leviná's phenomenology of ethics and further took the pendulum to business expansion by seeing how this brought about growth and expansion drawing from the value profit chain.

Concerning CSR, GB shows some degree of CSR as a social business though the environmental bottom line is overlooked. This is seen through the number of scholarships it gives to Grameen children. This has been increasing over the years as shown above. Another area of CSR that is visible in GB is the housing loans it provides to member of the bank as shown above.

We therefore conclude this part by saying that, GB practices corporate governance and CSR and this has contributed to its expansion over the years. Using CG to explain the expansion of GB is more a question of ethics than that of rationality as we have seen above. But the question now is: to what extent has CG and CSR contributed to the expansion of GB? This might be an area of interest in future research.

### *Recommendations*

The critical analytical section of this thesis pointed out some flaws regarding the practice of CG and CSR in GB. It is very true that GB has revolutionized banking in the world and that it is practicing some degree of good CSR in branches of Grameen social network of businesses, but it will be more visible if GB could grant scholarships even to non-Grameen children since they also form part of the social environment. This may go a long way to add more substance to the triple bottom line thinking mentioned above. It is also important that that GB consider the environment as a very important stakeholder. This is because not considering the environment as an important stakeholder may mean that GB can grant loans to customers who want to engage in businesses that are degrading to the planet (though this is subject to investigation).

Another key issue is that of managing GB. It is a good corporate governance measure to see into it that a business remains a going concern and directors and managers make sure and prove to other stakeholders that the business will continue to exist in the fore seeable future. The best way to do this is to undertake adequate training of young staff who will undertake top executive managerial positions in the future to ensure the continuity of the business.

Going through the official website of GB and the various annual reports we realized that this aspect was lacking; and it was more like Yunus, Yunus and Yunus all the time. This sounded more as if GB was a sole trader whose continuity is questionable suppose Yunus falls ill or the inevitable occurs. Therefore, if GB must continue to expand in the years to come, it must provide room for adequate training of young personnel to ensure continuity of the bank.

Hence we can see that since its inception till date, Grameen bank has made itself a force to reckon with and it has almost become a role model for many micro-credit institutions both at home (Bangladesh) and abroad and many countries are looking out for ways to develop their own social businesses due to the impact that this bank has created in the world in terms of poverty alleviation, but we strongly believe that, if the idea of corporate governance and CSR could be treated more seriously in this bank, it may go a long way to take the bank many steps forward and improve on its transparency and this will further facilitate growth and expansion and also clear some doubts to international researchers and media regarding some of its practices.

Another important lesson we learned from this thesis case was the fact that, at times ethics in business can be more important than very rigid governance. This is because from the look of things, confidence and trust contributed more to the success in GB than rigid corporate governance rules which are applicable in conventional banks. The idea of lending without collateral played a very important role on the onset since it gave an opportunity for those who have a business idea and could think and work hard but did not have a banking history and enough collateral security to obtain loans to actually get these loans; loans that they later invested, got them multiplied into bigger sums of money, repaid what they borrowed from GB, took bigger loans and so on. All these escalated the figures in the balance sheet of GB as the years went by.

This is a banking philosophy that gives a new twist to what is held by conventional banks (some of which) have failed despite the fact that they had a proper finesse in banking models and rigid credit monitoring; hence it is an aspect worth emulating by other banks (that is an idea of lending without collateral to the poor but yet monitoring credit).

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## Appendix: Interview guidelines:

We are students of Karlstad University and we are writing our Master's thesis. For the research we have maintained the following guidelines. The original interview has been conducted in Bengali. Here we have translated the questions in to English.

### **Questions enabling an understanding of Grameen Bank:**

1. Would you please tell us your name, position and designation that you hold in Grameen Bank?
2. In which branch are you working and how long are you working there?
3. Would you tell us the mission, vision and objective of Grameen Bank in brief?
4. In what kind of organization did you use to work before you joined Grameen Bank?
5. What kind of banking services do Grameen Bank offer?

### **Questions concerning Business Expansion**

6. What is the main reason behind your rapid expansion?
7. What is the reason behind your high repayment rate?
8. Do you want to change or want to modify your banking method?
9. Do you want to expand the bank more?
10. Did the foreign aid or loan help Grameen Bank to expand?

### **Questions concerning Corporate Governance**

11. How does Grameen Bank select the executive director?
  - Do they have any banking knowledge?
12. Do they rotate the external auditor?
13. Do the borrowers understand the Annual Report and does it influence them in borrowing and paying loans?
14. How do you monitor the credit risk management?
15. What would be the effect on Grameen Bank if Mr. Yunus step down?
16. What kind of transition did Grameen Bank undertook in 1991/92

### **Questions concerning Corporate Social Responsibility**

17. What are the other parties that Grameen bank takes under consideration after borrower?
18. In Europe many companies publish CSR report. Do you have any intention to publish this type of report in future?
19. Do you give scholarship to those whose children whose parents are not borrowers of bank but poor?

20. What is Grameen bank's concern regarding environment?
21. What do you personally think? Will Grameen bank eliminate poverty from Bangladesh?
22. How do you feel working in an organization like Grameen Bank and working for a noble cause?