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**Article**

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# Alternative finance and sustainable development

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## **Abstract:**

**Aim:** The aim of this article is to evaluate alternative finance for the implementation of the basic assumptions and goals of sustainable development.

**Design / Research methods:** Using the comparative analysis the most frequent mentioned forms of alternative finance have been assessed. The analysis took into account both the assumptions and the basic goals of sustainable development.

**Conclusions / findings:** The conducted analysis show that despite many features that indicate the inclusion of alternative finance in philosophy of sustainable development, the implementation of the basic assumptions and goals are arbitrary. Many of the alternative forms do almost realized nothing.

**Originality / value of the article:** An juxtaposition of sources of financing with the concept of sustainable development is usually carried out when analyzing the funding opportunities for relevant initiatives. However, in this case, the assessment is concentrating on the sources of financing and implementation by them of the adopted sustainability assumptions and goals.

*Key words: alternative finance, sustainable development.*

JEL: G23, G24, G30, G32, O30.

## **1. Introduction**

The financial crisis of 2008 exposed the weakness of the traditional banking system and financial markets. In response to growing problems, governments and regulators in many countries have introduced additional restrictions that significantly hinder access to capital. This situation particularly affected the SME sector and newly emerging enterprises. These entities, therefore, began looking for other alternative financing methods. Taking into account the fact that the SME sector makes a significant contribution to the economic development of all countries

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(e.g. in Poland it generates about 50% of GDP), and growth as such cannot be achieved without innovation, the actions restricting access to capital were not only a serious blow to the economic operators themselves, but also translated into a slowdown observed for a very long time.

By adopting a Declaration of Action for Sustainable Development in Rio de Janeiro, the signatory countries have committed themselves to respecting the principles and achieving the objectives set. Hence, the question arises whether the financial crisis and the resulting lack of access to capital and the above declarations go hand in hand and whether the resulting alternatives are the answer to the emerging problems.

The aim of this article is to evaluate alternative sources of finance for the implementation of the basic assumptions and goals of sustainable development.

The article is divided into three sections. The first of them discusses the basic concepts of sustainable development. Particular attention has been paid to the assumptions and goals adopted by many countries within the framework of this concept. The second section deals with alternative finances, the origins of their growing popularity and their basic forms. The final section analyzes and evaluates the implementation of sustainable development policies by individual forms of alternative finance. The most important conclusions flowing from the analysis are contained in the summary which also offers further indication of research opportunities.

## **2. Sustainable development – basic concepts, objectives and directions of action**

Sustainable development has been defined in many ways, but the most common and frequently quoted definition is from “Our Common Future” – “Sustainable development is development that meets the needs of the present without compromising the ability of future generations to meet their own needs.”

The concept of sustainable development is associated primarily with the United Nations Conference on Environment and Development organized in Rio de Janeiro in 1992 (the so-called Earth Summit). At the meeting, government representatives

from 170 countries, including Poland, declared their support for the idea of environmentally sensitive economic development. During the Conference, as well as later, a number of different types of treaties were signed, which have been put into effect with greater or lesser success. Unfortunately, the implementation of the idea of sustainable development met with very sharp criticism. This is a normative concept of conscious and active shaping of social relations and human-environment relations. It requires, therefore, a difficult axiological understanding that is contrary to the ruling, ubiquitous liberal democracy. So if most ethical values are subordinated to economic values, and not vice versa, the realization of sustainable development will remain only a utopia.

This concept has enormous scientific and research potential, especially from an interdisciplinary perspective. It offers the opportunity to compile and combine the perspectives of different academic disciplines, such as linking ecology, ethics, economics, research, sociology and many other disciplines. In addition, research on sustainable development provides the basis for formulating recommendations for social policy, identifying ways to improve the quality of life and the state of the environment (Rokicka, Woźniak 2016).

Sustainable development assumes that economic growth is supposed to lead to greater social cohesion (including reduce social stratification, equalize opportunities, counteract marginalization and discrimination) and improving the quality of the environment through limiting the harmful impact of production and consumption on the state of the environment, the protection of natural resources (Kuraszko 2009).

Sustainable development refers to the social and economic development of an enterprise, which enables the implementation of the strategy and the attainment of its objectives without interfering with its future realization (Witek-Crabb 2005). Therefore, the development of an enterprise should be carried out in such a way that it does not interfere with the future development potential, also on the basis of building a competitive advantage.

Implementing such a development requires not only the knowledge of internal procedures and capabilities but also a very detailed knowledge of the conditions and environment in which it operates. Mutual relationships and ways of interacting are of great importance here. It is quite common for managers to seek solutions that

should reconcile conflicting interests of different parties. Hence, it is necessary to harmonize economic objectives with social and environmental objectives.

Looking at sustainability research, it is noteworthy that some authors interchangeably use the terms *sustainability* and *business responsibility* (Laszlo 2008). This is in some way justified, because sustainable development involves the use and conservation of natural resources and the orientation of technology and institutions in order to achieve and sustain the fulfillment of the human needs of present and future generations. This understanding, which preserves soil, water resources, plants and genetic resources of animals, does not degrade the environment and uses technologies, is economically viable and socially acceptable (Kuciński 2009).

Regardless of whether these concepts are considered the same or not, they certainly have common assumptions. Their focus is on external effects and distribution problems related to the economic activity of enterprises.

Key elements of sustainable development, according to the Brundtland Report (Brundtland 1987), were:

- Recovery of economic growth
- Changing the quality of economic growth
- Satisfying basic needs such as jobs, food, water, access to sanitation, health care
- Ensuring a sustainable level of production
- Protecting and improving the natural resource base
- Technology reorientation and risk management
- Merging the environment and economy in the decision-making process
- Reorientation of international economic relations.

In 2015 the Goals for Sustainable Development were established, which were included in the UN's Development Agenda 2030. They contain 17 basic objectives: No poverty, Zero Hunger, Good health and well – being, Quality education, Gender equality, Clean water and sanitation, Affordable and clean energy, Decent work and economic growth, Industry, innovation and infrastructure, Reduced inequalities, Sustainable cities and communities, Responsible consumption and production,

Climate action, Life below water, Life on land, Peace, justice and strong institutions, Partnership for the goals.

### 3. Alternative finance

Alternative Finance (AF) is an innovative segment of financial market, aimed at providing consumer loans, startup financing, providing capital to the SME sector through the use of new technologies – online platforms and social networking sites (Waszkiewicz 2016). In the broader context, alternative finance serves to stimulate economies and to fund charity or socially important actions (Wardrop et al. 2015).

The new segment operates outside the traditional banking and capital markets (Baeck et al. 2014), so it is a part of *shadow banking*, defined by the Financial Stability Board (FSB 2011) and European Commission in the Green Book (EC 2012). Also Goldman Sachs (Nash, Beardsley 2015) speaks similarly about alternative finance.

The most frequently mentioned forms of alternative finance include: P2P Consumer Lending, P2P Business Lending, Donation Crowdfunding, Reward Crowdfunding, Equity Crowdfunding, Invoice Trading, Debt – Based Securities, Community Share/Microfinance, Pension – led Funding. Among the most popular, however, are mainly P2P loan platforms and crowdfunding platforms.

The P2P lending platforms are divided into two groups according to the type of “customers” that use these solutions: P2P consumer lending and P2P business. The first group offers access to loans given and taken by individuals. The interest rate is determined in the auction, i.e. the appropriate statement of the borrower's offer with the offer of the lender. Hence, the rate is generally lower than the market rate of credit and credit lines, but at the same time higher than the market offering of deposit instruments, taking into account the corresponding period of time. The second group refers to operations where the borrower has an economic entity, while the lender may be represented by other entities and individuals (Baeck et al. 2014).

The first P2P platform was launched in the UK in 2005, but the idea quickly spread around the world. However, the cradle of this form of alternative finance

remains the UK, as it is the place where most of these loans are offered. According to the NESTA research (Baeck et al. 2014) in 2014 £749m has been lent in P2P business lending and £547m in P2P customer lending.

Crowdfunding is the use of the internet community and networks to raise capital for a variety of ideas. It is a typical collection of money (smaller or larger amounts) through the internet for the purpose one chooses. Due to the way of payment to the donors, we distinguish four types of crowdfunding (Motylska-Kuźma 2016):

- donation – projects are non-profit, usually associated with charity, so for the money paid the donor does not receive anything in return;
- reward – in return for donations, donors receive rewards, but their nature is very often dependent on the amount of payment. The prize could be the prototypes of products, tickets for an event organized, etc.
- lending – this kind of crowdfunding is very similar to business P2P lending, so these forms are often identified with each other. However, P2P is supposed to transfer financial surpluses from lenders to borrowers and it is not necessarily a specific purpose here. In the case of lending crowdfunding, the purpose must be specifically defined;
- equity – investors acquire shares in companies, later using dividends, distributions of profit or redemptions at initial prices.

Invoice trading is the purchase by investors of the sales invoices with discount, using ICT (Wardrop et al. 2015). So it can be said that it is some sort of factoring, although not institutionalized. It is increasingly called microfactoring.

Microfinance refers to loans granted to a very specific group of SMEs, namely those who are in financial trouble or for some reason are excluded from the traditional banking system. Community shares, however, are the transfer of certain amounts to charity (Wardrop et al. 2015).

In case of debt-based securities, the borrower receives the funds for the indicated purpose and, in return, issues an unsecured debt instrument for a specified period of time (Waszkiewicz 2016). This is similar to the issue of bonds, but because it is outside the traditional banking system, the instrument received is not only not secured, but very often the legal capacity of its debt collection is very limited.

Pension-led funding is the financing of the SME sector from the funds accrued from the pension funds of the project promoter. Intellectual property serves frequently as security, and the method itself is developed only in the UK (Wardrop et al. 2015).

The market for alternative finance can boast a very dynamic development. According to the NESTA research (Baeck et al. 2014), between 2012 and 2014, in the UK alone, the following growth rates were recorded:

- Equity crowdfunding – 410%
- P2P business lending – 250%
- Rewards crowdfunding – 206%
- Invoice trading – 174%
- Debt – based securities – 117%
- P2P consumer lending – 108%
- Community shares – 95%
- Donation crowdfunding – 77%
- Pension – led funding – 5%.

#### **4. Alternative finance and sustainable development**

Table 1 below provides a comparative analysis of all forms of alternative finance and assesses the level of achievement of the assumptions and the goals of sustainable development. Each of the alternative finance forms listed in Chapter 3 was rated 1 to 3, where 1 means that no objective or assumption was covered by the form of financing analyzed, 3 – full implementation. Ratings are given subjectively, based on the definitions and descriptions in Chapter 3. Because all the assumptions and objectives of sustainable development are considered equivalent, no weights which are responsible for the priority were introduced into the analysis. The sum of the rates received reflects the degree of coherence of a given form of financing with the ideas of sustainable development.



**Table 1. Assessment of alternative finance**

Rule/Goal of sustainable development	P2P consumer lending	P2P business lending	Donation crowdfunding	Reward crowdfunding	Equity crowdfunding	Invoice trading	Debt – based securities	Community shares	Pension – led funding	Average
The Rules:										
Recovery of economic growth	2	3	1	2	3	3	3	2	2	<b>2.33</b>
Changing the quality of economic growth	2	3	1	2	3	2	3	1	1	<b>2.00</b>
Satisfying basic needs	1	3	2	2	3	3	3	2	1	<b>2.00</b>
Ensuring a sustainable level of production	1	2	1	2	3	2	2	2	2	<b>1.89</b>
Protecting and improving the natural resource base	1	2	2	2	2	2	2	2	2	<b>1.89</b>
Technology reorientation and risk management	1	2	1	3	3	2	3	2	2	<b>2.11</b>
Merging the environment and economy in the decision-making process	1	2	2	2	2	2	2	2	2	<b>1.89</b>

**Table 1. Cont.**

Rule/Goal of sustainable development	P2P consumer lending	P2P business lending	Donation crowdfunding	Reward crowd-funding	Equity crowd-funding	Invoice trading	Debt – based securities	Community shares	Pension – led funding	Average
Reorientation of international economic relations	1	1	1	1	1	1	1	1	1	<b>1.00</b>
The goals:										
No poverty	2	2	2	2	2	2	2	2	2	<b>2.00</b>
Zero hunger	2	1	2	1	1	1	1	2	1	<b>1.33</b>
Good health and well-being	1	1	2	2	1	1	1	1	1	<b>1.22</b>
Quality education	1	1	1	1	1	1	1	1	1	<b>1.00</b>
Gender equality	3	3	3	3	3	3	3	3	3	<b>3.00</b>
Clean water and sanitation	1	1	2	1	1	1	1	1	1	<b>1.11</b>
Affordable and clean energy	1	1	1	1	1	1	1	1	1	<b>1.00</b>
Decent work and economic growth	2	3	2	3	3	3	3	3	3	<b>2.78</b>
Industry, innovation and infrastructure	2	3	2	3	3	3	3	3	3	<b>2.78</b>
Reduced inequalities	3	3	2	2	2	2	2	2	2	<b>2.22</b>
Sustainable cities and communities	2	2	2	2	2	2	2	2	2	<b>2.00</b>

**Table 1. Cont.**

Rule/Goal of sustainable development	P2P consumer lending	P2P business lending	Donation crowdfunding	Reward crowdfunding	Equity crowdfunding	Invoice trading	Debt – based securities	Community shares	Pension – led funding	Average
Responsible consumption and production	2	3	2	3	3	3	3	3	3	<b>2.78</b>
Climate action	1	1	1	1	1	1	1	1	1	<b>1.00</b>
Life below water	1	1	1	1	1	1	1	1	1	<b>1.00</b>
Life on land	1	1	1	1	1	1	1	1	1	<b>1.00</b>
Peace, justice and strong institutions	1	1	1	1	1	1	1	1	1	<b>1.00</b>
Partnerships for the goals	1	1	1	1	1	1	1	1	1	<b>1.00</b>
<b>Total:</b>	<b>27</b>	<b>29</b>	<b>28</b>	<b>29</b>	<b>28</b>	<b>28</b>	<b>28</b>	<b>29</b>	<b>28</b>	
<b>Percentage [%]:</b>	<b>36.0</b>	<b>38.7</b>	<b>37.3</b>	<b>38.7</b>	<b>37.3</b>	<b>37.3</b>	<b>37.3</b>	<b>38.7</b>	<b>37.3</b>	

Source: author's own assessment

As can be seen in Table 1, the principle of economic growth is best implemented, and among the goals – “gender equality”, “decent work and economic growth”, “industry, innovation and infrastructure” and “responsible consumption and production”. The “reorientation of international economic relations” was completely omitted. Alternative financing is indeed transnational, as most platforms work for people not necessarily associated with a given country. On the other hand, however, this is not a sufficient argument to consider them to be capable of affecting the economic relations between individual countries. Some sustainability targets have also been omitted. Firstly, alternative finance does not meet the goal “quality education”. Some of the analyzed forms of funding may be sources of capital needed to meet the goals of improving the quality of education. However, the financing model alone does not meet the above objective. Another unrealized goal is “affordable and clean energy”. As in the case of quality of education, projects

funded through obtained capital may involve renewable energy sources, but the source of financing alone does not contribute to this objective. A similar situation also applies to goals such as “climate action”, “life below water”, “life on land”, “peace, justice and strong institutions” and “partnership for the goals”.

However, by observing the summary estimates of all the alternative forms of financing analyzed, it can be seen that they do not differ significantly. In fact, some of the assumptions or goals are pursued by selected models better and others worse. However, on average, these ratings remain on a very similar level. It is between 27 and 29 points, i.e. on average 37.6% of the maximum number of points.

It is worth noting that the sum of all points can be between 25 and 75. The lowest value is a situation in which a given form of financing does not pursue any of the assumptions and goals of sustainable development (receives a rating 1 everywhere). The highest value – all objectives and assumptions are fully implemented. When comparing this theoretical framework with the results obtained, it could be concluded that alternative financing is unlikely to support the objectives of sustainability and its assumptions, although it would seem at first glance that they favor a responsible business and fight against inequalities that are one of the fundamental concepts associated with sustainable development.

### 5. Summary

It should be noted that the market of alternative finance is no longer just a response to the crisis, but an increasingly rapidly growing segment of the modern financial market. And while this is still a market niche compared to European credit assets, the AF market has a huge potential for growth.

Alternative finance is mainly used to finance the SME sector, including innovative solutions, charitable donations or microfinance. It has limited procedures, transaction transparency, control capabilities, and high quality customer service. The primary benefit is either reduced cost or favorable interest rates as well as satisfying individual social needs.

However, from the point of view of implementing the principles and objectives of sustainable development, alternative finance does not seem to respond directly to the much needed changes. Brief evaluation of the different forms of funding can lead to erroneous conclusions that they especially fight with social differences, stimulate “healthy” growth because they promote socially acceptable activities. A more detailed analysis demonstrates, however, that the first impression is wrong. It is true that alternative finance certainly contributes to the realization of many projects that are more or less in line with the assumptions and goals of sustainable development, but the funding models themselves do not serve them.

The above analysis has several limitations. First, the assessment is subjective. This means that it is not based on credible research, but on subjective judgment of the author, made on the basis of definitions and descriptions of the forms of alternative funding and the principles and goals of sustainable development. Nevertheless, it points to some interesting insights that may be the basis for further research.

Secondly, the evaluation included only the concept of the funding model itself. As mentioned above, adding to the analysis the characteristics of the projects being implemented could in greater detail determine whether alternative finance contributes to achieving the principles and goals of sustainable development or not. It should not only evaluate the projects themselves, but to examine their scope and nature of their impact on the environment and society.

In conclusion, consumer awareness and ubiquitous technology have led to the creation of a certain sensitivity on the part of enterprises towards aspects of social responsibility that have a direct impact on sustainability. Alternative finance has a role to play here, which will be appreciated both by donors and by capital recipients.

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