**Values-Based Banking**

Course outilne

**1. INTRODUCTION AND HISTORY**

* The essence of banking. Why banking is a transformational econòmic activity.
* History of banking in the past 200 years. The eclosion of cooperative, ethical and values-based banking*.*

**The essence of banking**

“Financial systems perform the essential economic function of channeling funds from units who have saved surplus funds to units who have a shortage of funds . The units who have saved can lend funds: they are known as lender-savers. The units with a shortage of funds must borrow funds to finance their spending: they are the borrower-spenders. In direct finance, borrower-spenders borrow funds directly from lenders in the financial markets by selling them securities. In indirect finance, a financial intermediary stands between the lender-savers and the borrower-spenders: the intermediary helps to transfer funds from one to the other. Another important function of a financial system is the monetary function. The introduction of money into the economy enables savers and spenders to separate the act of sale from the act of purchase and allows them to overcome the main problem of barter, which is the ‘double coincidence of wants’ (each of the two parties involved in a transaction has to want simultaneously the good the other party is offering to exchange). From a structural point of view, a financial system can be seen in terms of the entities that compose the system. A financial system comprises financial markets, securities and financial intermediaries. Financial markets  are markets in which funds are moved from people who have an excess of available funds (and lack of investment opportunities) to people who have investment opportunities (and lack of funds).”

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**Activities & multiplier effect of banking in economy**

Within the financial system, borrowing and lending are the two primary activities where there are six essential elements:

1. the ***ultimate lenders***(= surplus economic units) and ***borrowers***(= deficit economic units), i.e. the non-financial economic units that undertake the lending and borrowing process. The ultimate lenders lend to borrowers either directly or indirectly via financial intermediaries, by buying the securities they issue.
2. the ***financial intermediaries***which intermediate the lending and borrowing process. They interpose themselves between the lenders and borrowers, and earn a margin for the benefits of intermediation (including lower risk for the lender). They buy the securities of the borrowers and issue their own to fund these (and thereby become intermediaries).
3. ***financial instruments (or assets),***which are created/issued by the ultimate borrowers and financial intermediaries to satisfy the financial requirements of the various participants. These instruments may be marketable (e.g. treasury bills) or non-marketable (e.g. retirement annuities).
4. the ***creation of money***(= bank deposits) by banks when they satisfy the demand for new bank credit. This is a unique feature of banks. Central banks have the tools to curb money growth.
5. ***financial markets,***i.e. the institutional arrangements and conventions that exist for the issue and trading (dealing) of the financial instruments.
6. ***price discovery,***i.e. the establishment in the financial markets of the price of money, i.e. the ***rates of interest***on debt (and deposit) instruments and the ***prices***of share instruments.

Commercial banks play a key role in modern economy and their activities serve as a multiplier for economic development. Among others we can outline the following ones:

1. **Capital Formation.** Banks play an important role in capital formation, which is essential for the economic development of a country. They mobilize the small savings of the people scattered over a wide area through their network of branches all over the country and make it available for productive purposes.
2. **Creation of Credit.** Banks create credit to provide more funds for development projects. Credit creation leads to increased production, employment, sales, and prices, and thereby, they cause faster economic development.
3. **Channelizing the Funds to Productive Investment.** Capital formation is not the only function of commercial banks. Banks invest the savings mobilized by them for productive purposes. Pooled savings should be distributed to various sectors of the economy to increase the productivity of the nation, developing entire new companies & industries within the economy.
4. **Facilitate international trade.** A large part of trade is done on credit. Banks provide references and guarantees, on behalf of their customers, on the basis of which sellers can supply goods on credit. This is particularly important in international trade when the parties reside in different countries and are very often unknown to one another.
5. **Bank Rate Policy**. Economists believe that by changing the bank rates, changes can be made in a country’s money supply. Federal or state banks in developing countries; the interest rate is to be paid by banks for the deposits accepted by them and the rate of interest to be charged by them on the loans granted by them.
6. **Bank Monetize Debt.** Commercial banks transform the loan to be repaid after a certain period into cash, which can be immediately used for business activities. Manufacturers and wholesale traders cannot increase their sales without selling goods on a credit basis. But credit sales may lead to locking up of capital.
7. **Finance to Government**. The government is acting as the promoter of industries in underdeveloped countries for which finance is needed it. Banks provide long-term credit to the government by investing their funds in Government securities and short-term finance by purchasing Treasury Bills.
8. **Bankers as Employers.** After the nationalization of big banks, the banking industry has grown to a great extent. Bank’s branches are opened in almost all the villages, which leads to the creation of new employment opportunities. Banks are also improving people for occupying various posts in their office.
9. **Professional services.** Banks act as advisers, counsellors and agents of business and indus­trial organisations. They help the development of trade and industry.

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**A brief history of banking**

Banking has evolved a lot from their beginnings in 2000 BC when merchants gave grain loans to farmers and traders carried goods between cities in the areas of Babylonia and Assyria, and even since Adam Smith introduce his “invisible hand” theory in 1776. In 1800’s, the average life span of an American bank was five years, after which most of the banknotes that it issued became worthless, until Alexander Hamilton, the first secretary of the US Treasury, established a national bank that would accept member banknotes at par, thus floating banks through difficult times. This national bank created a uniform national currency and set up a system by which national banks backed their notes by purchasing Treasury securities, thus creating a liquid market; by then some commercial banks already had emerged as a dominant ones, such as JP Morgan which also almost single-handedly halted the Panic of 1907 by quickly persuading all the major players on Wall Street to work towards stability and back a recovery, just as a central bank would do today.

During the Crash of 1929 preceding the Great Depression, banking and brokerage firms were operating with margin requirements of mere ~10%. It meant that the brokerage firms would lend $9 for every $1 an investor had deposited, which led over 9,000 banks to fail between 1930-1933, making clear that new regulation was needed and after WWII governments took a more active role in banking and along with Bretton Woods institutions (IMF and World Bank) lead to regulation and more important, domestic banking finally settled to the point where, with the advent of deposit insurance and widespread mortgage lending, the average citizen could have confidence in the banking system and reasonable access to credit. The modern era had arrived.

Charge cards were invented in the US in the 1950s quickly followed by credit cards; and the ATM deployed by Barclays Bank in London in 1967 but The most significant development in the world of banking in the late 20th and early 21st centuries has been the advent of online banking, which in its earliest forms dates back to the 1980s but really began to take off with the rise of the internet in the mid-1990s. The growing adoption of smartphones and mobile banking further accelerated the trend. While many customers continue to conduct at least some of their business at brick-and-mortar banks, a 2021 J.D. Power survey found that 41% of them have gone digital-only.

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**The eclosion of cooperative, ethical and values-based banking.**

As banking were developing and influencing economy as whole, also complexity and surging needs for common people clients arose and not always in the profitable way commercial Banks wished and this led to a new ways of undestanding bank’s purpose. Cooperative financial institutions originated in Germany in the mid-19th Century as philanthropic self-help institutions designed to encourage workers to join resources and accumulate savings. Hermann Schulze-Delitzsch (1808–83), a politician and judge, founded the first urban credit cooperative in 1850 mainly concerned to promote economic self-sufficiency. A principal purpose of early credit cooperatives was to draw outside funds into communities that needed them, not as charitable donations, but as loans to be repaid which was key to quickly spread the model to other countries in Europe. At the beginning of 20th century the financial cooperative concept spread from Europe to Northe America, where the first financial cooperative (caisse populaire) was established in Canada in 1900 and in 1908 in US and just one year later the first credit union legislation came up, while in 1934 the Federal Credit Union Act was passed.

Nowadays, economic crises have proved social banking and social finance have become important trends among bank customers in Europe, growing at a faster pace than mainstream banks, transforming social banks from niche institutions to large, publicly visible players. Social banks try to invest their money only in endeavours that promote the greater good of society, instead of those which generate private profit just for a few. This means that social banks consider social and economic “sustainability” when making financial decisions, the main difference between mainstream banks and social banks is this: While mainstream banks are in most cases focused solely on the principle of profit maximization, social banking implements the triple principle of profit-people-planet. Social banks care about making a profit, but equally for promoting human and environmental well-being and to do this, social banks have four features that make them unique:

* ***Responsibility*.** Social banks know their customers personally.
* ***Transparency***. Unlike many mainstream banks, social banks know what is done with the money they lend to their customers.
* ***Sustainability.*** While most mainstream banks are focused on creating short term profit, social banks focus more on the long-term effects of money.
* ***Inclusion***. Being accessible and proactively engage diverse input from society

Values-based banking born to serve the unserved, people and communities that are not reached by existing financial networks (the so called ‘bottom of the pyramid’ market) through microcredit, microloans, microinsurance and other financial products and in many cases local small scale institutions are growing, some to become formalised financial institutions in order to meet growing customer need.

In the last 40 years a ‘new’ type of values based banking has developed, known widely as social, ethical, green or alternative banking. These banks have focused on human needs in the real economy. They have played a key role in investing in green and social innovation sectors which other banks have not yet investigated and understood. Triodos and GLS Bank, for example, were pioneers in the analysis, understanding and financing of solar and wind energy. Nowadays they and others are also incubators for many new housing models as well as companies and small entrepreneurs. Once these structures have been deemed to have been de-risked the traditional banks begin to enter the market too.

Integrate and consolidate small/regionals banks and scale up values-based banking through big mainstream banks in order to serve and fulfill more people’s needs in a complex, competitive and demanding environment are the challenges in the years to come.

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**2. THE MODERN CONCEPT OF VALUES-BASED BANKING**

* Description of vàlues-based banking. The Global Alliance of Banking on Values. The GABV today.
* Purpose
* The six principles of values-based banking. A code of conduct but also a transformational paradigma. Intentionality and consciousness as part of the business model.

**Values-based banking & GABV**

**A movement of leading purpose-driven banks, transforming banking for a sustainable future**

Finance plays a pivotal role in shaping our society. Every loan and investment impact our communities, environment, and economic future, for better or worse. Many people depend on access to finance to live up to their full potential and enjoy a decent and dignified life.

Banking and finance, therefore, come with great responsibility. Banks are not simply neutral brokers of money. They are often creators of money. By deciding how to allocate money, banks are important agents of change.

With that in mind, there’s a growing number of pioneers and banking leaders from around the world with a values-driven approach to banking. They have joined forces with a shared mission to put finance at the service of people and the planet.

We call them values-based banks, and they form the Global Alliance for Banking on Values (GABV).

The GABV was founded in 2009 by ten pioneer banks that believed in the need for a fairer financial system. Today, it is a growing membership organisation with presence in more than 40 countries across Africa, Latin America, Asia Pacific, North America and Europe. As today, GABV has 70 members from +40 countries, 16 supporting partners, 80K employees, +200B anual revenue assets and +60M customers impacted from values-based banking alliance.

The Global Alliance for Banking on Values (GABV) is an international network of frontrunner organisations and leaders in the banking industry that use finance to serve people and the planet. Our collective goal is to make the banking system more transparent and support positive economic, social and environmental change.

*Vision*: Finance at the service of people and the planet. Our collective goal is to change the banking system so that it is more transparent, supports economic, social and environmental sustainability, and is composed of a diverse range of banking institutions serving the real economy.

*Mission:* Our purpose is to expand and strengthen the practice of values-based banking, and to lead the way for a financial system that promotes social equity, responds to the climate emergency and delivers true and lasting prosperity and well-being for all.

*Identity:* The Global Alliance for Banking on Values is a movement of innovative leaders and frontrunners in sustainable finance. Integrity, human dignity and the protection of the environment are at the core of their operations. By setting an example, they lead the transformation of banking and finance in their respective communities, countries and regions and expand their reach and impact by supporting others on the way to change*.*

**The six principles of values-based banking**

Since its founding, the GABV banks have been clear that a set of principles were needed to be developed and shared that distinguish in the minds of customers, partners and coworkers why Global Alliance banks are different from other forms of banking. For the majority of banking institutions, the primary or exclusive driver of business decisions is based on the profitability of the services provided, even if the by-products of those decisions do not deliver sustainable economic, environmental or social development. For GABV members, business decisions start by identifying a human need to be met, and then establish how to meet that need in a way that is sustainable from an environmental, social and economic perspective, including sustainable profitability for the bank. This meant that in agreeing to be a member of the Alliance, each bank would live by these 6 principles:

1. **Triple bottom line-** Values-based banks integrate this approach by focusing simultaneously on people, planet and prosperity. Products and services are designed and developed to meet the needs of people and safeguard the environment.
2. **Real Economy-** Values-based banks are grounded in the communities and sectors they serve. They focus on the actual needs of people and businesses in the real economy rather than engaging in the financial economy. In doing so they deliver social, environmental, and financial returns.
3. **Client-centered-** Values-based banks establish strong relationships with their clients and are directly involved in understanding and analysing their economic activities and assisting them to become more values-based themselves.
4. **Long-Term resiliency-** Values-based banks adopt a long-term perspective to make sure they can maintain their operations and be resilient in the face of external disruptions. At the same time, they recognise that no bank, or its clients, is entirely immune to such disruptions.
5. **Transparency-** Values-based banks maintain a high degree of transparency and inclusiveness in governance and reporting. In this context, inclusiveness means an active relationship with a bank’s extended stakeholder community, and not only its shareholders or management.
6. **Culture-** These principles and values are reflected in the leadership practices, corporate culture and the organisation of the bank. Human resources policies and practices support critical reflection and discussion of values and how they translate into everyday decision making. Training and education is not limited to building financial skills, but also fosters an understanding of the bank’s mission, values and business model in the broader social and environmental context of the bank.

**Role of banking: A transformational paradigm**

Even before 2007 financial crisis, an intense and wide-ranging debate about meaning and purpose of banking had arisen. With financial crisis, the critique turned to capitalism itself with media posing questions such as “Crisis in Capitalism?” and “what’s wrong with capitalism?” with the dominant international financial system and business model as main targets of this criticism.

Questions focused in how banks generated their profits and moreover, how they share these benefits with their stakeholders including customers, investors, co-workers (especially senior management) and in general, with wider society. Fortunately, since early this century, many conversations, cross-investments and cooperative initiatives had taken place between several social, environmental and culturally conscious banks throughout the world and while this debate continues without reaching a resolution, this group of banks has for some time been answering many of these challenges by delivering strong, straightforward and sustainable banking services focused on a values-based banking model, caring more about influencing real economy rather than the financial economy as a core element of their business model.

For GABV members, business decisions start by identifying a human need to be met, and then establish how to meet that need in a way that is sustainable from an environmental, social and economic perspective, including sustainable profitability for the bank. These intentionality and consciousness about the leading role and impact they can drive in their community, is a key part of the business model and brand values of the GABV:

* **Intentional-** Values-based Banks are intentional in creating social and environmental impact. It's why they exist and this intentionality guides everything they do.
* **Coherent-** Values-based banks take a holistic and coherent approach to the design of their business model, being aware about potential conflicts and challenges.
* **Contextual-** The values are reflected, intentional and appropriate to bring positive social and environmental impact in a specific context.
* **Transparent**- Values-based banks are accountable at all levels of the business model. Transparency enables outsiders to easily understand how a bank is behaving.
* **Systemic**- Values-based banks work with others to change the banking system itself, so it is better able to serve people and protect the environment.
* **Authentic**- By being intentional in what they do, and integrating values in their business, values-based banks are genuinely authentic.
* **Inclusive**- Values-based banks aim to build an inclusive financial system that responds to the needs of everyone, and not just a few.
* **Ambitious**- Values-based banks aspire to the highest standards and want to be recognised as thought leaders at the forefront of progressive banking.

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**3. PRINCIPLES ONE AND TWO: TRIPLE BOTTOM LINE APPROACH AND REAL ECONOMY**

* Deep meaning of both principles
* The two principles analysed jointly
* Examples of the two principles in action in the Global South. Examples in Western economies.

**What is Triple Bottom Line (TBL)?**

Triple Bottom Line (TBL) focuses on meeting people, planet and prosperity goals as one. Real Economy and Financial Economy Intermediation can be considered Triple Bottom Line (TBL) if it supports individuals or enterprises delivering impact in at least one of the following categories: Social Empowerment (People), Environmental Regeneration (Planet), and/or Economic Resiliency (Prosperity). Examples of TBL intermediation include financing for SMEs to generate employment in an environmentally-friendly manner, that is, with no negative consequences, alternative energy projects, housing for low- or middle-income individuals, and guarantees or letters of credit for SMEs exporting goods and creating employment. Personal financing/ credit cards are generally not TBL, unless both the purpose and outcomes of financing support environmental regeneration, social empowerment and/or economic resiliency that can be verified (e.g. financing education, asset purchase to provide productive income, etc.). Evaluating impact in social and/or economic and/or environmental wellbeing of every intermediation is key to know if is TBL or not, with a positive impact considered as TBL while neutral or negative impact can’t be considered as a TBL intermediation.

***Context matters.***Large scale palm oil production for industrial beauty production is not specifically TBL. Palm oil production for local consumption in a country where it is part of the traditional diet can be TBL (access to food) if the social and environmental risks are managed so that the impact after mitigation is not material. Financing a beauty saloon where the micro-entrepreneur family members work informally is not TBL in North Europe, but it is TBL in South America, where the microbusiness faces barriers to access to finance and informal employment is widespread in the micro-entrepreneur segment. Financing a high standard dental clinic offering dental care may be TBL in a North American town were dental healthcare is scarce, but it may not be TBL in a Central African capital, where the fee restricts accessibility to the elite in practice. A hairdresser franchise may be considered TBL for its contribution to employment in a high unemployment region of Southern Europe, while it may need to demonstrate something additional (e.g. use of organic products) to be considered TBL in a low unemployment region of Northern Europe. Each bank is encouraged to develop a TBL classification system aligned with the GABV guidelines and adapted to its context, to ensure relevance and usefulness for internal management and external recognition.

Key concepts to understand how to evaluate as a TBL:

* **Impact-** Plausible positive contribution to social, economic or environmental wellbeing, improving the conditions from the existing situation in the context .
* **Negative impact-** Risk of significant (i.e. large scale and/or extreme) harm to People, Planet or Prosperity. Harm can be to the borrower, her employees, her clients, the community, and/or the environment, as a borrower activity consequence.
* **Financially excluded-** Population without previous access to formal loans, and/or without credit history, and/or with previous negative credit history.
* **Financially underserved-** Individuals and MSMEs with barriers to access the amount and term of credit needed for their businesses to fully develop their potential within reasonably risk limits, due to limited credit history and guarantees.
* **Additionality-** Contribution to increasing the positive impact for the People, Planet and Prosperity, additional to the typical conditions and practices prevalent in the context, i.e. a given market at a given time.

Additionality implies a constant aspiration to pushing the frontier further: the same activity that brings additional impact today may not continue bringing additional impact in 10 years’ time, if progress is made in the general conditions and standards. The same activity may be of additional impact in one country and not in another country where the normal standards are higher. Given the average energy efficiency level of building in a given context, there is additionality in exceeding the energy efficiency standards of the average new building, and not in an average new building (new buildings are always more energy efficient than old ones, so being in line with the new average is not sufficient).

**TBL’s positive impact areas & additionality**

TBL intermediations must contribute to at least one dimension of social, economic or environmental wellbeing positive impact from the *UNEP Impact radar*. Impact categories of sustainable development are a global reference specific to financial institutions, high-level enough for each bank to develop an aligned, yet context-specific, TBL classification system. Within that dimension of wellbeing, at least one of the areas must be met, the financing contributes to at least one of the areas listed below, and in some areas, prove additionality (i.e. better than the average in the context, marked with an “A” in the list below):

|  |  |  |
| --- | --- | --- |
| **Social Wellbeing** | **Economic Wellbeing** | **Environmental Wellbeing** |
| Food and water(A) | Inclusive, healthy economies | Resource efficiency (A) |
| Housing (A) | Economic convergence | Waste |
| Health and Sanitation |  | Water, air, soil, climate, biodiversity and ecosystems |
| Education |  |
| Employement (A) |
| Energy and mobility (A) |
| Culture and heritage |
| Information, justice, integrity and security of person (A) |

*Source: GABV Scorecard Manual*

**Negative and neutral impact**

Impact is negative if there is significant risk of doing harm to People, Planet and Prosperity, even if the intermediation also shows some positive impact aspects, e.g.: loans to financially excluded low income population that lead to over-indebtedness and debt traps; biogas plants using crops issued of high soilimpoverishing farming techniques. There is a list of activities causin negative impact such as those related with weapons, gambling, fossil fuels, drift net fishing, forced labor and among others which include any activity illegal under host country laws or regulations or international conventions and agreements. Plus, every bank can identify any other activity associated to a risk of doing harm in the specific context.

Neutral impact is intended as the category of activities that do not have a specific positive or negative impact on social, economic or environmental wellbeing, where the bank does not bring specific additionality to what is offered by the majority of market players. Neutral impact includes:

* Activities in line with current standards of respect of People, Planet and Prosperity prevalent in the context (given market at a given time), and without a specific positive impact. Example: mainstream law firms, conventional restaurants, standard residential mortgages.
* Cases where the intermediation contributes to decreasing a material net negative impact. Example: large scale business moving from a polluting technology to a less polluting one also thanks to the financing received; large energy company with oil and gas as main business, but using the financing to invest and increasing the renewable energy share.
* Activities included in the social wellbeing dimension (e.g. food, housing, health, education) and with pricing features specifically targeted to the high-end market or economic elite in the context (as opposed to pricing features accessible for the majority of the population). Example: high-end target market yoga studio.
* Intermediations where the environmental and social standards are in line with the recent regulatory or average standards for new goods and constructions. Example: conventional farming and animal breeding compliant with local regulation; standard modern vehicles with lower emissions than older vehicles; intermediations with associated carbon emissions off-set and paid by the borrower.

**Real Economy (RE)**

Grounded in communities, serving the real economy, and enabling new business models to meet the needs of people. Values-based banks serve the communities in which they work, they meet the financial needs of these geographic and sector-based communities by financing enterprises and individuals in productive and sustainable economies.

Financial intermediation can be considered as Real Economy (as opposed to Financial Economy) if it is directly linked to a Real Economy Asset or Activity. This means that the intermediation is aimed at directly supporting the production of goods and services, as opposed to focusing primarily on buying and selling in the financial markets. As indicated below RE intermediation is no more than one degree away from a real asset or activity.

Examples of RE intermediation include direct financing to manufacturers or service companies, foreign exchange forward contracts for importers or exporters of goods and services, derivative contracts directly related to the activities of enterprises, direct financing to individuals for purchase of asset, among others. Assessment on the usage of intermediation especially for personal financing shall determine the connection to RE activities. Accordingly, debt consolidation, share trading/margin financing, among others, shall not be considered as Real Economy intermediation. Assets held for trading as opposed to maturity as well as secondary market purchases will generally be considered non-RE. This exclusion list may be modified based on experience or following annual checks to ensure previous classifications remain valid. Some examples of RE intermediation can be seen in the following chart:

REAL ECONOMY FINANCIAL ECONOMY

|  |  |
| --- | --- |
| Real Asset/Activity |  - Local medical clínic - Energy-efficient office building - Organic farm - Coal energy plant - Clothing manufacturer - Housing for seniors |

|  |  |
| --- | --- |
| One degree |  - Financing of energy retrofit - Alternative energy equity stake - Financing to food manufacturer - Direct financing leveraged buyout - FX forward contract for clothing - Real-estate fund with direct  exporter investments in property |

|  |  |
| --- | --- |
| Two degrees |  - Shares purchased in secondary - Hedge of client FX positions with market for SRI fund other banks  - Liquidity deposit with other banks - Mortgage backed securities for low - Financing to hedge fund for buyout income housing |

|  |  |
| --- | --- |
| Three degrees |  - Specific maturity tranche of mortgage-backed securities  - Credit default swap |

|  |  |
| --- | --- |
| Four degrees |  - Tranche of a collateralised debt obligation for commercial loans |

*Source: GABV Scorecard Manual*

The importance of real economy in facing challenges has been proved in recent COVID-19 crisis, when despite excess of liquidity pumped from governments through deferral taxes, direct loans, wage subsidies, etc…globally, the intended lending largely failed to materialise, with traditional banks citing an uncertain economic outlook to have tightened lending and in the other hand, quantitive easing and artificial stimulation of price assets, made health crisis in financial markets comparatively short-lived. But even with traditional banks failing in their very first reason to exist (lending), once again, this appears not to be the case for values-based banks. In a survey conducted by the Global Alliance of Banking on Values (GABV) among their member CEOs in the Fall of 2021, more than half of the 52 respondents reported loan growth of more than 5% in the first half of 2021 (and also, they lent 70% of their assets to the real economy on average compared to 40% of the balance sheets of GSIBs between 2011-20201). In terms of deposit growth, more than 70% of respondents observed at least a 5% growth2 and which translates in a better chance to overpass health crisis for communities as whole, estimulating real economy and not only financial economy.

With that in mind and among many other reasons why does placing assets (loans) in real economy matters, we will underline the following three that VSECU, a Values-Based Bank member, mention3:

* **Stability—**By being close to the purchase and the borrower, these lenders can have a much better understanding of the benefits and risks of making a loan. With a greater understanding of the product, the borrower, and the place where it’s happening, they can make loans that work better for the borrower and for the credit union/bank. All of this helps to maintain stability, which is essential to keeping the promise to the membership that credit unions are a safe, secure, and trustworthy place to do your banking.
* **Local Recirculation—**When deposits are lent out into the community for a home, car, or business, [**the money goes back into the local economy**](https://www.vsecu.com/blog/how-credit-unions-keep-your-money-local/) and enables greater vitality in their shared community. Each time a person makes a payment on their loan, the money can go right back out for another person’s needs. The more the money cycles through the local area, the more activity and vitality there is. Activity and vitality are key to making improvements to the quality of life, and who doesn’t like that?!
* **Sustaining and Improving Lives—**Focusing on the real economy is one powerful way values-based credit unions and banks can do that. When a loan helps a young family buy and move into their first home, that improves the quality of their life. When access to credit helps a person get that vehicle to get to work and play, that improves the quality of their life. When a business loan helps a company grow and hire local talent, that improves the quality of life.

**TBL & RE acting together**

Placing loans in productive activities which will pour benefits and circulate money all across the communities as well as contributing to add social, economic and/or environmental wellbeing positive impact beyond current standards are powerful tools which acting together have even more positive impact for those people and communities that needed the most, setting a new standard for financial institutions around the globe to make the things right. Here some examples of these principles in action:

**SDB bank focuses on the real economy to face the crisis in Sri Lanka**

*(full article in* [*https://www.gabv.org/interview/sanasa-development-bank-focuses-on-the-real-economy/*](https://www.gabv.org/interview/sanasa-development-bank-focuses-on-the-real-economy/) *)*

Sri Lanka faces one of the worst economic crises seen in decades. The country has an immense amount of debt, soaring inflation and a lack of necessities such as fuel, grains, and medicine. The International Monetary Fund (IMF) has begun conversations about how best to support the country by working closely on its economic policy.

Despite the current situation, Global Alliance for Banking on Values member [SDB bank](https://www.sdb.lk/en) continues to support disadvantaged clients across the country. At the same time, it has achieved outstanding financial results in 2021, delivering a 9% rise in profits. **Intrigued by how well the bank did in such a challenging situation, we spoke with the bank’s Acting CEO, Niranjan Thangarajah**, to learn more.

SDB bank is a Sri Lankan development bank founded in 1997. The bank provides banking products and services to micro, small and medium-sized enterprises. It has a significant impact on grass-roots economic development by stimulating small and medium enterprises (SMEs) and micro, small and medium enterprises (MSMEs) growth countrywide.

Thangarajah explained how the economic crisis arose. *“If you look at the Sri Lankan economy, it has more of a solvency challenge than a liquidity challenge. When I say solvency, it’s to do with debt. That’s why you will see announcements that the country’s going to restructure its debt. If you go to the origin of the problem, the Sri Lankan economy has been a predominantly import-driven economy. If you look at the development in the past, it was stimulated by debt to make Sri Lanka a tourism and transportation hub. Unfortunately, the debt was not well structured.”* And with COVID-19 hitting their main revenue stream (tourism), Thangarajah had it clear: *“There is a clear solution for the current problem in the country. It is to increase your production base, get people to produce, and get people to add value. As banks and institutions, that’s what we should be investing in and supporting, backing people who are producing today. Once that is done, you’re self-dependent, self-sufficient and the problem is resolved,”*

When asked if having a values-based banking model that focused on the real economy helped the bank survive and thrive in this environment, Thangarajah agrees: *“If you ask me how we did well during these times, and how we intend to do better, it is mainly because of our values-based approach, because we see a big opportunity in the country which has always existed. Values-based banking has helped us because we are adding value. When I say adding value, I mean we are a bank that is close to rural society. We are focused on inclusivity, getting everyone into the banking system. We are also applying digital technology to increase accessibility. I think we have invested a lot on the digital side, as a bank there, which takes digital banking to the masses”.*

**VSECU’s energy savings provide individuals with basics needed to live better lives**

*(full story in* [*https://www.gabv.org/stories-from-gabv/vsecus-energy-savings-provide-individuals-with-basics-needed-to-live-better-lives/*](https://www.gabv.org/stories-from-gabv/vsecus-energy-savings-provide-individuals-with-basics-needed-to-live-better-lives/) *)*

VSECU’s mission is to improve the quality of life for all Vermonters, and to achieve this, it strives to bring people together to empower the possibilities for greater financial, social, and environmental prosperity.

As a triple bottom line financial cooperative, it strives to be an innovator in the credit union industry and sees itself as a part of a larger movement of purpose-driven and values-based businesses that consistently reach above and beyond industry norms.

In response to the growing demand for solar and efficiency financing in the early 2000s, VSECU developed [VGreen](https://www.vsecu.com/personal/green-loans/), a suite of products that are designed to maximize the savings of energy upgrade projects. The program has grown to not only include loan products, but also a money market account, the VGreen MMA, where the deposits are recirculated to fund VGreen loans. VGreen now has a $95M portfolio, and the one-year loss ratio is 0.18%, the lowest of all VSECU’s portfolios.

VSECU membership is open to anyone who lives or works in Vermont. The fact that Vermont is a state with no-to-low population growth has meant that for clean energy businesses to grow and thrive they needed to look beyond their borders. In 2017, the credit union extended its field of membership, forming a common bond partnership with a trade organization, Northeast Sustainable Energy Association (NESEA) and now welcomes NESEA’s members to become VSECU members. This partnership facilitates growth and diversity in the VGreen program that brings many benefits to the entire membership.

VSECU continues to adapt and innovate the VGreen program to the market challenges and technology advances in product development. The credit union funds loans for bicycles, appliances, cold climate heat pumps, solar projects, home battery storage, geothermal heating systems, comprehensive energy projects, electric vehicles and motorcycles, and more. It underwrites energy savings as a utility expense offset and looks to partnerships to provide credit enhancements such as loan loss reserves to increase access to financing more members who face financial challenges. Energy savings can mean healthier, safer, and more durable homes, and more affordable, reliable transportation – the basics needed to live better lives.

The products developed by VSECU include unsecured options, such as the Energy Improvement Loan and the Investment Tax Credit Loan, offering discounted interest rates, long period or lower initial payment. They also offer The Energy Equity Loan that features discounted rates and no-or-low closing cost expense and Green Vehicle loan with 100 and 50 bp discount off Standard auto’s loan for EV’s and other MPG vehicles, respectively. In addition, VSECU also offers an off-grid mortgage for those interested in financing a home that is not connected to traditional electric utilities. In 2021, they piloted the EnergyFirst Mortgage through a Department of Energy (DOE) grant-sponsored partnership, these projects received a DOE Home Energy Score, pre- and post-project completion, and an energy savings guarantee. While the pilot program is complete, the credit union is evaluating the results and exploring ways to build the product into our regular mortgage product offerings.

VSECU has a wide range of partnerships with clean energy vendors and installers, which are offered VGreen vendor program to offer local customer-centered financing options and installers loan with discounted financing rates as part of a whole customer-focused clean energy adoption experience. VSECU also partners with Efficiency Vermont, the primary efficiency utility in Vermont, to offer the Home Energy Loan, subsidized financing for qualifying home energy upgrades with interest rates as low as 0%.

As VSECU looks to consider ways to grow and diversify green lending, it will continue to collaborate with its current partners, listen to consumers and businesses, and form new mission-aligned partnerships to provide financing solutions that adapt to the clean energy market.

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**4. PRINCIPLES THREE AND FOUR: LONG TERM RELATIONSHIP WITH CLIENTS AND LONG TERM SELF-SUSTAINING AND RESILIENCY**

* Deep meaning of both principles
* The two principles analysed jointly
* Examples of the two principles in action in the Global South. Examples in Western economies.

**WHAT DOES LONG TERM RELATIONSHIP WITH CLIENTS MEAN?**

Values-based banks establish strong relationships with their clients and are directly involved in understanding and analysing their economic activities and assisting them to become more values-based themselves. It means a direct understanding of their economic activities and risks involved. Proper risk analysis is used at product origination so that indirect risk management tools are neither adopted as a substitute for fundamental analysis nor traded for their own sake.

Values-based banking is also concerned with a different understanding of the use of money and means that financial activity needs to have human dignity at its core. This is why the six principles cannot be fully understood without the contribution of long-term relationships with clients. From the GABV perspective, there is substantial consideration for the clients, who are, indeed, treated as if they were actually bankers themselves, and, by banking on values, they are empowered financially to regenerate the economy. From the perspective of long-term relationships with clients, radical transparency is essential. A bank that is respectful with clients has to be explicit with them about the way the bank is using the clients’ money, so that depositors will always have the chance of withdrawing their money if the bank is using it in a way that is not in accordance with the clients’ values. The bank follows a mission and a purpose and designs its asset allocation policies based on these, but the bank cannot assume that all citizens will buy in to their approach, which is why transparency is so important. A long-term relationship with clients also has to be understood from an integrated perspective and is also framed by real economy and triple bottom line principles. A bank that has human dignity at its core looks for a different understanding of the relationship with clients, both depositors and borrowers: transparency applies to both. Long-term relationships also apply to both but especially to borrowers, since a deep understanding of the needs, aspirations and risks involved in the borrowers’ activities is of paramount importance in making the final asset allocation decision and assessing to what extent the activity of the client fits with RE and TBL principles. It is also a way of showing respect for shareholders and, especially, depositors of the bank.

The current perception of the financial system, including banking is that the system as such is selfish, driven by short-term profit maximization and subverted by greedy managers. In 2013 a study by Jaroslav Belas of the Tomas Bata University in Zlin looked at the impact of the financial crisis on business ethics in the Slovak banking sector19. Although banks in Slovakia have their own ethical code in which they undertake to offer only services that meet customer needs (Slovenska bankova asociacia, 2007), a 2012 survey by Deloitte found strong and growing dissatisfaction amongst Slovak consumers. Employment uncertainty amongst Slovak bank workers was translating into deteriorating even cynical customer service. A wider, international study by EY in the same year across 35 countries found that 56% of bank customers believe banks do not recognise their real needs and do not adjust their products to meet these needs. A study in May 2015 by the University of Notre Dame on behalf of law firm, Labaton Sucharow, found that despite the very public campaign by the US Government to root out bad behaviour in finance, it remains a problem in need of attention on both sides of the Atlantic. William Dudley of the New York Federal Reserve remarked that the degree of risk taking reflects the prevailing incentives in the industry. Nearly a third of those questioned in the study ‘believe compensation structures or bonus plans in place at their company could incentivise employees to compromise ethics or violate the law’. The report’s authors also noted that ‘respondents from the UK are either more willing to commit a crime they could get way with or are more frank about it’. Few admitted to being willing to blow the whistle and a number reported that they now had employment terms that prohibited them from reporting illegal or unethical behaviour.

This shows the necessity of offering adapted products and services with a policy that defines how the bank will offer suitable products and services through appropriate channels, including designing products, services and channels and monitoring their suitability. Example of good practice: A clear and comprehensive product development policy is in place to define how to develop new products/services and improve existing ones. It should be based on extensive market research, client feedback and needs assessments. The bank has a list of collateral assets or goods that cannot be seized. The list is based on local norms and includes items that would create severe hardship or total loss of income earning ability for the client. Also, includes avoid predatory lending, or any aggressive sales technique and to respect clients' right to refuse products. The bank must have a mechanism of rigorous and regular monitoring of front line staff and third-party sales techniques (e.g., agents, insurance companies or money transfer companies) to impede aggressive sales. When raised, 'red flags' trigger corrective measures and also the bank's incentive/ bonus structure does not promote aggressive sales. Example of good practices about this:

* Non-performing loans and productivity levels are monitored and raise red flags to require additional investigation if they exceed internal thresholds.
* The incentive systems value portfolio quality at least as highly as other factors, such as client growth. Targets are aligned with context so that they are achievable.
* The weight of the incentive scheme over the over the monthly salary should not be more than 50/60%

Banks found they could earn more from money than from providing services for the real economy. Fees replaced interest income as the core component of revenue. This trend is exacerbated when unprecedented levels of liquidity are injected into the system by central banks. In addition, the regulatory focus has been on holding higher levels of capital for interest income related assets. The ‘income to capital’ ratio is higher for non-interest income and this will be an influencer of bank behaviour when capital is scarce or costly. In a basic bank fee income can be less risky than lending. We also acknowledge that interest income may be problematic if it is connected with high, unsustainable levels of debt whether personal, corporate or public. Nonetheless the trend towards greater fee income reflects a more complex financial system, which is precisely the opposite than what is necessary to create stronger relationships with clients, banking needs to lend more, not less and it seems traditional mainstream banks have been gotten it wrong.

Know your customer, what do they do, their motivations, needs and handling of risk is fundamental when we talk about truly long-term relationships with clients in banking, because is not about making money out of money, is about adding value to the community through SME’s and individuals who circulate benefits in real economy in the long run and at the same time, making better businesses for its own prosperity by this healthy working principle.

**LONG-TERM SELF-SUSTAINING AND RESILIENCY**

Long-term, self-sustaining and resilient, means that values-based banks adopt a long-term perspective to make sure they can maintain their operations and be resilient in the face of external disruptions. This principle can be seen as a pre-requisite for everything else. We are talking about finance, more specifically banking, which is a heavily regulated industry all over the world. In this context, values-based banks must be very aware of the need to be resilient and financially and operationally very solid to be able to cope with expected and unexpected external disruptions. This is a question of long-term survival since many companies that fail because of external disruptions do so because they did not have the right long-term approach to operations and did not focus sufficiently on preventing risks and analysing the market and the potential business opportunities correctly. Being resilient, solvent and sufficiently profitable is a sine qua non for all banks to be able to cope with external disruptions, but it is especially relevant for values-based banks since they aspire to become role models for the financial industry.

The GABV seeks to finance change and change finance. By financing people and communities who are not served, they contribute to positive change in society. At the same time the GABV takes initiatives to change the financial system as we know it with a view to ensuring that banking is a healthy force for the advancement of society and the protection of our planet. The collective goal is to change the banking system so that it is more transparent, supports economic, social and environmental sustainability and is composed of a diverse range of banking institutions serving the real economy. Banking and finance, therefore, bear great responsibility: banks are not simply neutral brokers of money; they are often creators of money. By deciding how to allocate money, banks are important agents of change.

VBB’s was not affected by the financial crisis in the same way as mainstream financial institutions in part because they had invested in long-term customer relationships and had not become dependent on the wholesale money markets. They are part of a values based rather than market oriented economy. The values based banks’ way of doing business is perceived as responsible and sustainable and as a support for society. Even during the recent health crisis, VBB have shown better results and resiliency than those traditional mainstream banks as the newest version of the annual researching, “Real Economy-Real Returns” show, with quite interesting findings that help us to understand the differences between VBB’s and Global Systematically Important Banks or GSIBs (aka most important traditional mainstream banks). We selected a just a few metrics as a snapshot to see the differences between them (*full metrics comparison and report in* [*https://www.gabv.org/resources-research/real-economy-real-returns-2021/*](https://www.gabv.org/resources-research/real-economy-real-returns-2021/)):

|  |  |  |  |
| --- | --- | --- | --- |
|  | 2020 | 2015 | 2010 |
| Real Economy | VBB | GSIB’s | VBB | GSIB’s | VBB | GSIB’s |
| Loans/Assets | 68.8% | 40.1% | 73.8% | 41.6% | 73.3% | 40.0% |
| Deposits/Assets | 79.9% | 54.9% | 78.2% | 52.5% | 76.6% | 47.4% |

|  |  |  |
| --- | --- | --- |
|  | 5y (2016-2020) | 10y (2011-2020) |
| Financial returns & volatility | VBB | GSIB’s | VBB | GSIB’s |
| Return on Assets | 0.68% | 0.57% | 0.68% | 0.59% |
| Return on Equity | 8.4% | 7.4% | 8.4% | 7.9% |

|  |  |  |
| --- | --- | --- |
|  | 5y (2016-2020) | 10y (2011-2020) |
| CAGR’s | VBB | GSIB’s | VBB | GSIB’s |
| Loans | 9.0% | 2.5% | 10.9% | 3.5% |
| Deposits | 9.5% | 4.4% | 10.7% | 4.5% |
| Assets | 9.4% | 4.1% | 10.1% | 3.1% |
| Equity | 11.0% | 2.4% | 12.6% | 4.2% |
| Total Income | 7.1% | -0.3% | 9.6% | 0.05% |

*Source: Real Economy, Real returns 2021*

As a group, the difference between VBBs and GSIBs is clear. The level of lending is on average 30% higher for VBBs than for GSIBs and it remains core to VBB’s activity, with 69% of their balance sheets devoted to lending compared to 40% for GSIBs in 2020. The ROA for the VBBs is, on average, slightly higher when compared to the GSIBs, even with a greater hit from pandemic than GSIB’s and relative to Returns on Equity (ROE), VBBs have superior performance over both time periods analysed. On balance, it appears that banking focused on meeting societal needs can provide acceptable returns to investors in bank equity instruments. Finally, when it comes to growth, we realised marked differences between the two groups in Loans, Deposits, Assets, Equity and Total Income. One element driving higher growth for VBBs is their relatively small scale. Another is that VBBs with a strong and long-term client focus tend to have higher client loyalty and lower client attrition. In addition, in some markets, clients are consciously choosing to move banking activities to VBBs. Further research on the sources of growth for both groups could be informative.

For sure VBB’s are not immune to struggle and also face a lot of challenges because bank failures occur all across the spectrum of banking. Of the 353 bank failures in the USA between 2008 and 2011, 85% were small community banks. Credit unions were not immune either. In the UK over 50 have closed since 2002. The Dunfermline Building Society was the largest building society in Scotland, but became insolvent after taking on too many risky assets, losing money in its own IT business and buying sub-prime mortgage securities. It became a test case in the UK for new bank legislation allowing the regulator to ‘takeover’ the building society and sell the good assets, which were taken over by the Nationwide Building Society and ShoreBank’s failure was caused by a mix of economic, governance and political issues like many other banks it had too little capital in the face of an unexpectedly deep recession, just to name a pair of cases to show why long-term, self-sustaining and resilient are key to face a complex environment full of potential risks and disruptions.

**Long-term principles acting together**

It is clear that values based banking is a viable model, yet many remain unconvinced that that it can work beyond a relatively small scale niche, and can serve the broad needs of populations and business. However such thinking fails to recognise that the current financial system already marginalises and excludes many in the world. And this is why these principles are so important, because they bring growth and self-sustaining through the most important asset a bank can have: its clients. To be sustainable values based banks have to broaden their reach and diversify their portfolio by reaching across to stakeholders of the market-oriented economy and win them over to a values based economy.

**Client-centered: Uganda’s Centenary bank case**

*(full article in* [*https://www.gabv.org/values-in-practice/intentional-centenary-bank/*](https://www.gabv.org/values-in-practice/intentional-centenary-bank/) *)*

Centenary bank started in 1985 with a clear mission, *“To provide appropriate financial services, especially microfinance, to all the people, particularly in rural areas, in a sustainable manner and in accordance with the law”.*Over the years, Centenary Bank has opened dozens of branches across the country, including automated tellers, and has provided financial classes, savings group structures and offered free accounts. They have done everything to lower the threshold to access, and they continue to do so.

In alignment with its mission, Centenary Bank decided to partner with International Grameen Foundation to help the bank roll out and scale financial services to the existing and new customers via mobile. While they tried to expand as far as possible into rural areas, they found that actually going to a bank could still be a barrier for new and existing clients. Considering the extended use of mobile phones in the country, the Bank has been offering mobile service to its clients as long as one has access to a telecom network.

Moreover, since the rollout, growth in other key business areas was realized: congestion in the banking halls was reduced, bank revenues have grown significantly over the years and deposits continue to grow as more and more rural clients gain access. To ensure all customer access to a mobile network, Centenary Bank worked with the Uganda Communication Commission to provide the codes necessary for each transaction, as well as various telecoms who provide support in terms of networks.

Centenary Bank’s mission is at the heart of their business and is reflected in everything they do – from products and services to how they make decisions, approach risk, and decide whom to collaborate with. By integrating their intention in all levels of the institution, they ensure that even through changing market conditions, their commitment to their customers never changes, only their approach.

*Another relevant case: Caja Arequipa (*[*https://www.gabv.org/values-in-practice/authentic-caja-arequipa/*](https://www.gabv.org/values-in-practice/authentic-caja-arequipa/)*)*

**Self-sustaining and facing challenges: The Banca Etica case.**

*(full article in* [*https://www.gabv.org/values-in-practice/coherent-banca-etica/*](https://www.gabv.org/values-in-practice/coherent-banca-etica/) *)*

When Banca Etica opened its first branch office in 1999, it did so knowing it was the first banking institution to operate exclusively in sustainable and alternative finance in Italy. Since its foundation in 1999, Banca Etica has been working to reach a legislative acknowledgement of the value of ethical finance. It has proven through financial success that it’s possible to simultaneously consider social and environmental evaluation of the loans alongside risk and return. They go hand-in-hand. Unfortunately, while there is a great deal of change in the banking industry, the more broadly accepted approach with respect to social and environmental impact is not coherent. It is not seen as mutually beneficial and in fact, oftentimes, sustainable activities are often financed alongside harmful activities.

The call for legislative acknowledgement of the value of ethical finance meant that the broadly accepted approach in the banking industry was being challenged. At the end of 2016, the Italian Parliament passed a law that recognised and promoted ethical finance. It was the first law of its kind approved in Europe and a major success for Banca Etica.

Currently, Banca Etica manages about 3 billion euros of savings and has kept its commitment to its people – clients and shareholders – by increasing credit to people and social enterprises, even during the crisis years. Its unwavering consistency and coherency in its pressure on lawmakers, its banking activities, and its full transparency have led to an increase in deposits, the share of capital and growing confidence of Italian investors in ethical finance.

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**5. PRINCIPLES FIVE AND SIX: TRANSPARENT AND INCLUSIVE GOVERNANCE AND ALL OF THESE PRINCIPLES EMBEDDED IN THE CULTURE OF THE FINANCIAL INSTITUTION**

* Deep meaning of both principles. The relevance of governance and culture in a transformational business model.
* The two principles analysed jointly
* Examples of the two principles in action in the Global South. Examples in Western economies.

**WHAT IS TRANSPARENT AND INCLUSIVE GOVERNANCE?**

Transparency is being honest with your stalkeholders about what you do and how you do it. Values-based banks maintain a high degree of transparency in governance and reporting. In this context, inclusiveness means an active relationship with a bank’s extended stakeholder community and not only its shareholders or management; they actively engage with the broader stakeholder community, taking their views into account in strategic decision making. A diverse stakeholder group is reflected in the composition of a values-based bank’s board and its co-workers. Communication is transparent, clear and easy to understand, making the bank accessible for all.

Transparent and inclusive governance is referring to a hygiene factor in all human activities that aspire to the highest ethical standards. Being transparent does not automatically mean that you operate in an ethical way, but it is very unusual that a company is operating ethically if it does not show high standards of transparency. The same happens with inclusive governance; it is usually a precondition for operating with high ethical standards. As we see in long-term client relationships principle, transparency is key to build meaning relationships with clients and that can’t be reached without a strong, diverse and inclusive corporate governance which understands the importance of coping with stalkeholder’s needs.

As was stated in their Berlin declaration in 2013 (entitled “Transforming the Financial System for Stability and a Focus on People”), transparency is a required fundamental principle to pursue GABV’s goal for a paradigma shift in finance, in how banks operate and making the financial system more people-oriented and stable and what stakeholders, including banks, regulators and governments, had to do to make this happen. Clients and depositors of banks need and deserve transparency on how the bank uses their client’s money and how their business model works. Only through transparency can trust be restored and people understand the financial system and how it can serve them. All banks must provide full transparency on their business models and use of client funds using common standards to be determined by independent experts such as the Global Reporting Initiative.

Throughout our survey with people, and reviews of the practices of values based banks the most mentioned value is transparency – knowing where your money is going and what it is doing. Transparency is about revealing understandable and unbiased information. The financial system and money are just a means towards meeting human needs. In the words of French social bank La Nef: “we simply want to make a bridge between savers and borrowers” but to do so there must be informed and responsible customer choice. Although financial reports of many of the big banks are as long as 500 pages the amount of understandable and unbiased information is arguably low and the number of pages may be off putting to anyone other than a bank analyst, certainly to the customer who may want to learn more about what is happening in the institution. Some banks present more usable data and case studies as evidence of their social and environmental impact. It also allows customers, actual or potential to assess more effectively the risks associated with a bank or product alongside a straight comparison of interest rates. Transparency also enables independent research to be conducted.

GABV believes that transparency is the most important driver of change in finance, as it is crucial to informing customer choice. Transparency also relates to how a bank is run. Despite the rhetoric and exhortations to higher standards, too little attention is paid by regulators or policy makers as to how banks or the infrastructure such as the payments systems are run and where responsibility and accountability lie. Given the pivotal role that banks and the financial system play in fuelling or constraining economic activity, greater diversity and transparency in the selection process of the composition of boards of banks and regulators can help change the culture and rebuild trust.

Diversity and inclusion are fundamental for a good governance. Diverse challenges and stakeholders demand diverse solutions. Only by accepting such diversity is banking and the financial system able to serve the needs of all actors. The diversity of stakeholders; rich and poor, urban and rural, young and old, local and international needs to be reflected and represented in governance. Global financial conglomerates, focused only on shareholder value, will not provide the diversity and closeness to the real economy that is needed. Smaller banks, embedded in the communities they serve and with a clear vision about serving the real economy and addressing issues of social inclusiveness have an important role to play. These banks provide both a sustainable source of innovation and unique access to financial products. Inclusive governance serving this diversity will provide a more resilient financial system avoiding the risks of concentration that can hold governments hostage.

If we take humanity as a central point of the financial system then all human beings are born stakeholders and as such all stakeholders should have the right of fair access to the financial system as well as access to air, water, soil or any other common good. And as such, everyone is to a certain extent affected by developments in the financial system. However, often citizens, as well as politicians and journalists build opinions on seemingly very flimsy understanding of the financial system. This is not a surprise as the system is complex and lacks transparency at all levels. Most of us do not know where our money goes and do not understand the processes behind it.

**ALL PRINCIPLES EMBEDDED IN THE CULTURE OF THE FINANCIAL INSTITUTION**

All these GABV’s principles which we have been exploring so far, will be poured into a last one principle where everything matches and is adopted as a whole values-based banking culture. These principles and values are reflected in the leadership practices, corporate culture and the organisation of the bank. Recognizing that the process of embedding these values requires deliberate effort, these banks develop human resources policies that reflect their values-based approach (including innovative incentive and evaluation systems for staff) in which training and education is not limited to building financial skills, but also fosters an understanding of the bank’s mission, values and business model in the broader social and environmental context of the bank (stakeholder-oriented practices). Leadership enables strong staff participation. These banks also have specific reporting frameworks to demonstrate their financial and non-financial impact such as the GABV Scorecard which is an scorecard developed by GABV and its membres  that sets the bar for sustainable and social banking. The GABV Scorecard structures and captures the vision, strategy and practice of values-based banks. The approach provides a snapshot of where an organisation is in its journey and may flag what next steps are needed to move the institution further along in the Banking on Values movement. The GABV Scorecard can be used by any banking institution and is based on the principles of values-based banking. Also, to spread the values-based culture, GABV has created The GABV Leadership Academy, a transformative learning experience for bankers in values-based institutions. It is intended to develop leaders who can step into their full potential and deepen their impact in their respective organisations. This programme, “Leading in Times of Disruption”, provides leaders in values-based banks with tools to lead and innovate during periods of disruption and high complexity while growing strong roots and common ground for everyone involved in the value-based banking.

At the centre of values are cultural values because the other business values depend on the culture of the banking organization, and the way of working on daily financial services offered to customers. Though the GABV principles can easily be understood by looking at each one of them individually, the real interpretation of values-based banking, the key to its regenerative strength and its differential purpose when you compare it to mainstream finance, can only be fully apprehended when you look at the principles as they really are: six interdependent pillars that support the architecture of values-based banking. Being a values-based bank means having sufficient and demonstrated achievements in each of the six principles, but it also means doing this in a coherent way, in the light of the widely shared understanding that values-based banks have a compelling mission to regenerate the economic system through finance: this is the “why”, the reason why they exist as banks. From this perspective, all the principles are intertwined and have to be seen and analysed in this way. Achieving the other principles is not possible if one does not have a set of policies and values in action that is coherent, that empowers co-workers and that is applied in every decision making process at all levels in the institution, and recognized by stakeholders, paving the way for the achievement of the goals in a way that respects the other principles.

**EXAMPLES OF TRANSPARENT AND INCLUSIVE GOVERNANCE**

*Transparent governance*

Sunrise Banks is a family owned, nationally chartered community bank. It is governed through an advisory board and board of directors comprised of local business owners, community representatives, and local ownership. It is certified as a Community Development Financial Institution (CDFI) and is also certified as B Corp; a certification granted to organizations that demonstrate a commitment to transparent corporate governance, solid environmental stewardship, and positive community impact. Sunrise Banks originate small business, commercial real estate, and community facility loans in the urban core of Minneapolis and Saint Paul. Over 60% of Sunrise’s loans are originated in low income communities.

*Diverse governance.*

Assinboine Credit Union is a socially responsible financial cooperative. It was formed in 1943 by Winnipeg Electric Company employees in Canada. It has a set of rules describing a desired board composition in which diversity plays an instrumental role. Skills and other competencies such as understanding of Assiniboine’s mission and triple bottom line commitment are only part of the mix. Diverse representation of members and the communities they serve complete the requirements. An annual gap analysis is undertaken to check whether gender, age, ethnic or cultural diversity is maintained with regard to those the credit union serves.

*Inclusive governance and Inclusive banking*

GLS Bank has 3 positions on the supervisory board for employee representatives. The bank also invites all clients to participate in the discussion and feedback process. This is not only evidenced by having a very active and open social media presence but also by inviting all members to the annual meetings and actively asking for their feedback. Banca Etica invites its co-operative members to assess borrowers and in such a way engage them in decision-making.

**Transparent: Beneficial State Bank “Move Your Money” divest/invest initiative.**

*(full article* [*https://www.gabv.org/values-in-practice/transparent-beneficial-state-bank/*](https://www.gabv.org/values-in-practice/transparent-beneficial-state-bank/)*)*

In September 2016, a report was published listing the banks financing the Dakota Access Pipeline (DAPL), the underground oil pipeline under construction in the mid-western United States. The report’s release woke people up to the connection between their deposit dollars and the pipeline’s financing and suddenly, people understood more deeply the power of their deposits. Although the divestment movements spurred the first step of action to take their money out of banks financing the pipeline, information was lacking for better alternatives.

In response, Beneficial State Bank, located in the United States, created a “Move Your Money” outreach campaign to help depositors find socially responsible alternatives to the big banks. This bold advocacy earned media attention, new customers, and new social media followers. As visibility grew, the team created and distributed a [toolkit](http://bit.ly/moveyourmoneynow) to partners, allies, and any individual looking to align their money with their values. The toolkit is not only an instructional on the “how to’s” of moving one’s money, but it also gives information on how to identify a values-based bank, using the GABV Principles as a guide.

The “Move Your Money” campaign was an effort to change the current financial paradigm by urging people to ask critical questions of their banks: How does your bank treat the communities and people it serves, the employees it hires, and the planet upon which we all depend? By positioning banking as the most powerful form of crowdfunding, Beneficial State Bank showed people that everyone can make an individual change and imagine a world that aligns with their values of inclusivity, equity, and justice.

**Inclusive: Visión Banco and its “constructing dreams” program.**

*(full article* [*https://www.gabv.org/values-in-practice/inclusive-vision-banco/*](https://www.gabv.org/values-in-practice/inclusive-vision-banco/)*)*

In 2010, Paraguay had a shortage of 1,000,000 homes. As a result, access to finance for housing and the ability to make home improvements was out of reach for many. That same year and in response to the housing deficit, Visión Banco, a values-based bank in Paraguay, launched a long-term financing product to improve the housing conditions of low-income micro-entrepreneurs. They partnered with Habitat for Humanity – an international non-profit that provides affordable, high-quality housing solutions for low-income people. Together, they created a product for long-term finance for low-income housing.

The initial stages were challenging, considering the segment of the population they were targeting already had difficulties gaining access to credit. It required Visión Banco not only to develop a product but also to complement it with financial education and partnering with key stakeholders in order to succeed: Habitat for Humanity helped to consolidate the process, and the Inter-American Development Bank (IDB) approved a partial-credit guarantee, an essential component in expanding the Bank’s loan offering. In doing so, Visión Banco broke a nationwide paradigm that the state was the only one responsible for housing.

Over 1,500 homes were built or improved using the “constructing dreams” product launched by Visión Banco. Following the success of the product, the state has encouraged more access to housing by allocating more funds toward long-term financing.

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*Alliance for sustainable futures, Jaap Boostra & Marcos Eguiguren, Edgar Ewar Publishing, 2023*

**6. THE PRINCIPLES OF VALUES-BASED BANKING COMPARED WITH UNEP FI PRINCIPLES FOR RESPONSIBLE BANKING**

* The UNEP FI PRBs, history, detail and meaning.
* The PRBs compared with the VBB Principles. Excellence of the current business model and performance in the VBB principles vs facilitating the transition for mainstream Banks in the PRBs.

**UNEP FI PBR’s HISTORY**

The [United Nations Conference on the Human Environment](http://www.unep.org/Documents/Default.asp?DocumentID=97) (Stockholm, 1972), established the [United Nations Environment Programme](http://www.unep.org/) (UNEP) as the environmental conscience of the [United Nations](http://www.un.org/) (UN) system. The concept of the UNEP Finance Initiative was launched in 1991 when a small group of commercial banks, including Deutsche Bank, HSBC Holdings, Natwest, Royal Bank of Canada, and Westpac, joined forces with UNEP to catalyse the banking industry’s awareness of the environmental agenda. In May 1992, in the run up to the Rio Summit that year, the UNEP Statement by Banks on the Environment and Sustainable Development was launched in New York, and the Banking Initiative was formed.

This Initiative, which operated under the auspices of the United Nations Environment Programme, engaged a broad range of financial institutions, including commercial banks, investment banks, venture capitalists, asset managers, and multi-lateral development banks and agencies – in a constructive dialogue about the nexus between economic development, environmental protection, and sustainable development. The Initiative promoted the integration of environmental considerations into all aspects of the financial sector’s operations and services. A secondary objective of the initiative was to foster private sector investment in environmentally sound technologies and services.

In 1997 the Insurance Industry Initiative (III) was formed, engaging insurers and reinsurers and this same year, the UNEP Statement by Banks on the Environment and Sustainable Development was redrafted, in order to broaden its appeal to the wider financial services sector. At this stage, the Banking Initiative was renamed the Financial Institutions Initiative (FII).

From 1999 the two groups of banks and insurers began to work together on issues of mutual interest, and in 2003, the two groups merged to form the UNEP Finance Initiative. Then, in 2012, UNEP FI and a group of insurance companies took the first steps in anchoring sustainability at the heart of their business strategies when they developed the Principles for Sustainable Insurance, the first global framework for the insurance industry to address environmental, social and governance risks and opportunities. The development of the Principles led to the largest collaborative initiative between the UN and the insurance industry—the PSI Initiative. Over 200 organisations worldwide have adopted the four Principles for Sustainable Insurance, including insurers representing more than 25% of world premium volume and USD 14 trillion in assets under management.

In 2019, a coalition of 132 banks convened by UNEP FI developed the first global sustainability framework for the banking industry when they launched the Principles for Responsible Banking. The six guiding principles help signatory banks ensure their strategy and practice align with the vision society has set out for its future in the Sustainable Development Goals and the Paris Climate Agreement and bring purpose, vision and ambition to sustainable finance. Signatories commit to embedding the principles across all business areas, at the strategic, portfolio and transactional levels. With the development of principles for the insurance and banking industry in addition to the Principles for Responsible Investment, sustainability blueprints now exist for all sectors of the finance industry.

To fast-track financial institutions’ action on decarbonising the global economy, UNEP FI has convened coalitions of actors from across the financial sector – investors, banks, and re/insurers. 2019 saw the launch of the [UN-convened Net-Zero Asset Owner Alliance](https://www.unepfi.org/net-zero-alliance/) in partnership with the PRI; in April 2021 UNEP FI launched the [Net-Zero Banking Alliance](http://www.unepfi.org/net-zero-banking), and the [Net-Zero Insurance Alliance](https://www.unepfi.org/about/about-us/history/unepfi.org/net-zero-insurance) was born in July 2021. The member-led alliances unite financial institutions who have committed to achieving net-zero GHG emissions in their portfolios by 2050, in line with the Paris Agreement; the members collaborate in working groups to jointly develop tools and guidance.

As 2022, UNEP FI has 349 members from banking industry all around the world.

**UNEP FI PRINCIPLES FOR RESPONSIBLE BANKING**

The Principles for Responsible Banking are a unique framework for ensuring that signatory banks’ strategy and practice align with the vision society has set out for its future in the Sustainable Development Goals and the Paris Climate Agreement.

The framework consists of 6 Principles designed to bring purpose, vision and ambition to sustainable finance. They were created in 2019 through a partnership between founding banks and the United Nations. Signatory banks commit to embedding these 6 principles across all business areas, at the strategic, portfolio and transactional levels:

* ***Principle 1: Allignment****-* We will align our business strategy to be consistent with and contribute to individuals’ needs and society’s goals, as expressed in the Sustainable Development Goals, the Paris Climate Agreement and relevant national and regional frameworks.
* ***Principle 2: Impact and target setting****-* We will continuously increase our positive impacts while reducing the negative impacts on, and managing the risks to, people and environment resulting from our activities, products and services. To this end, we will set and publish targets where we can have the most significant impacts.
* ***Principle 3: Clients and customers****-* We will work responsibly with our clients and our customers to encourage sustainable practices and enable economic activities that create shared prosperity for current and future generations.
* ***Principle 4: Stakeholders****-* We will proactively and responsibly consult, engage and partner with relevant stakeholders to achieve society’s goals.
* ***Principle 5: Governance and culture****-* We will implement our commitment to these Principles through effective governance and a culture of responsible banking.
* ***Principle 6: Transparency and accountability-***We will periodically review our individual and collective implementation of these Principles and be transparent about and accountable for our positive and negative impacts and our contribution to society’s goals.

3-step process guides signatories through implementing their commitment:

1. [**Impact Analysis:**](https://www.unepfi.org/banking/bankingprinciples/resources-for-implementation/impact-analysis/)identifying the most significant impacts of products and services on the societies, economies and environments that the bank operates in.
2. [**Target Setting:**](https://www.unepfi.org/banking/bankingprinciples/resources-for-implementation/target-setting/)setting and achieving measurable targets in a banks’ areas of most significant impact.
3. [**Reporting:**](https://www.unepfi.org/banking/bankingprinciples/resources-for-implementation/reporting/)publicly report on progress on implementing the Principles, being transparent about impacts and contributions.

Through the principles, banks are convened by the United Nations to collectively produce cutting-edge guidance and pioneering tools on key areas of sustainable finance, learn best-practice from their peers, scientists and industry experts, and benefit from individual feedback and collective reviews as they progress on their sustainability journey.

**UNEP FI PRB’S AND GABV’S VBB PERFORMANCE**

**Transition of mainstream banks to PBR’s principles**

The coalition of PRB signatories has grown to represent 40% of the global banking system by assets. Signatories provided information regarding their progress addressing key impact areas (Environmental, Social and Internal Changes) according to their fulfilment of three key steps:

1. Analysis of their current impact on people and planet.
2. Based on this analysis, prioritisation and setting of targets where they have the most significant impact. This is followed by implementing actions to meet targets.
3. Publicly reporting on progress, and, by year four, having this reporting verified by a third-party.

Signatory banks must implement these steps within their first four years of joining the principles. This report is the first collective baseline review, marking 1.5 years of the principles’ initial 4-year timeline. This report captures banks progress up to March 2021. Signatories will be in their first or second year of reporting depending on when they joined the principles.

Although most of the banks have identified sustainability as a strategic priority to their organization, started analyze impact, some of them already set targets to measure progress and impact of implementing these principles and get early signs of impact in real economy, there is a long way to see a real change, mainly due to the nature of the process which started with a self-impact evaluation that can differ a lot among organizations in both, progress and accuracy of the evaluation, as stated in its first PRB’s Collective Progress Report: many banks are navigating the complex process of analysing their impact in line with the PRB requirements. However, the progress made by PRB signatories differs widely. Good examples of implementation are emerging from a small number of advanced banks. These can be used as practical examples for peers on their own implementation journey1.

Signatories must accelerate their commitments to address key challenges, notably:

* *Improve the availability and quality of data.* Many banks lack the ability to track and measure progress due to the limited availability and quality of internal and external data. They must therefore work together and with stakeholders to increase the availability of shared knowledge sources and agree on approaches where data is not available, such as using national averages or appropriate proxies. Banks must also improve corporate disclosure and management of available data in order to address this challenge.
* *Strengthen impact analysis.* Banks need to gain technical knowledge and expertise to deepen their understanding of how to review the impacts, both positive and negative, of their activities, products, and services across their portfolios.
* *Increase action on further critical sustainability issues.* Some sustainability themes that have been identified by science and the international community as critical are underrepresented. For example, currently only 15% of banks identified biodiversity as an area of significant impact, and 23% identified human rights as significant, despite research and stakeholders indicating both are important risks and impacts to be addressed by the sector.
* *Sufficiently link all targets to the outcomes of impact analyses.* Targets should be in line with banks’ PRB commitments and encompass the activities financed by the organisation. Too many banks are setting targets linked to internal, operational activities such as head office electricity consumption rather than portfolios. Additionally, some of the existing targets do not show compelling links to identified significant impacts, or fulfil the commitment of setting specific, measurable, achievable, relevant and timebound (SMART) targets.

*Independent review of progress*

The CSAB’s independent review of the Collective Progress Report is based on the collective perspectives of the 12 CSAB members as well as the 46 stakeholders that these members consulted with across all major regions and sustainability areas. The CSAB welcomes the work that PRB and many of its member banks have done to identify activities and progress to date. However, as noted throughout the independent view, CSAB members encourage a more holistic focus (including on key issues such as human rights, equality, and biodiversity), comprehensive goal setting, and demonstrated execution against these goals by the following PRB Collective Progress Report, with indications of meaningful progress from member institutions in the interim.

Banks may take steps towards sustainability through individual projects or programmes but ultimately significant change depends on strong institutional commitment to sustainability which is then integrated through sustainability roles throughout the organisation. It should not be overlooked that banks are big employers and need to rethink how to implement value-orientation amongst their employees. Today, many banks have a Corporate Social Responsibility department, internal ethical policies or codes of conduct. Yet this does not exclude them from irresponsible behaviour despite such efforts. Looking at the sustainability reports of many mainstream banks that highlights their community commitment and environmental footprint improvements it would be hard to imagine that these same banks finance (in greater or lesser extent) activities/companies opposed to those commitments, such as deforestation, polluting energy, forced labor, etc... Arguably, the culture of sustainability does not penetrate throughout the whole organisation, especially in big mainstream banks with a long and deep history about making profits at the main reason to exist .

**VBB’s applying principles and performance**

On the other hand, there are values based banks which put meeting human needs at the very core of their business. Values based banks are proof that it is possible to apply values holistically and profitably throughout a bank

As we saw before, VBB’s have proved to get better results than GSIB’s during health crisis, in a normalized basis and in a long and mid-term. For sure, as already discuss too, they are not immune to external disruptions and face several challenges to their very own existence, it is very reliable to underline the effort and results through all this journey, being an example for other banks (and especially mainstream banks) that there is a way to do a better banking for all while you make profits for the long run in the process. And also, we can say that VBB’s already had a background of doing the things right, putting client needs in the centre of their business strategy, that made easier for them to follow, interiorize in their organizational culture and put in practice GABV’s principles in a faster and seamless way in order to get better results than those big mainstream banks trying to understand and adopting PRB’s principles.

VBB’s practice banking with a holistic focus on the real economy to deliver clear societal benefits (environmental regeneration, economic prosperity and social empowerment). They have consistently shown that serving the real economy leads to better and more stable financial returns than those shown by the largest banks in the world. These VBBs, members of the GABV, operate in numerous markets and serve diverse needs. They use distinct business models to address the very real banking needs, especially access to credit, of enterprises and individuals within their communities.

Real economy, refers to economic activities that generate goods and services as opposed to a financial economy that is concerned exclusively with activities in the financial markets.  Financial intermediation can be classified as a real economy if it is directly linked to a real economy asset or activity. This means that intermediation is aimed at directly supporting the production of goods and services instead of focusing primarily on buying and selling in the financial markets. Real economy intermediation is no more than one degree away from a real asset or activity.

The strength of values-based banks lies in their commitment to serve their clients and communities. In a changing world, these purpose-driven banks continue to excel in this important work. They remain coherent with their purpose and in their comprehensive response to the immediate challenges arising from the global health pandemic and the global challenges of climate change, biodiversity and ecosystem degradation and social inequality.

Values-based banks continue to demonstrate steady financial returns and growth with a strong focus on the real economy, built on solid capital positions. These entities support the intermediation of money to individuals and enterprises that deliver positive economic, social and environmental impact. They operate in numerous markets, serving diverse needs, using different business models. And they are united by a set of common guidelines, the Principles of Values-based Banking.

The business case for values-based banking is compelling. It has contributed to the rise in visibility and relevance of sustainable finance globally and could indicate that the sector has reached a tipping point. Yet, despite the growing realisation of the limits of banking driven by only profit, it is still to emerge as a dominant force in the banking sector. Inertia and the power of the status quo, including existing personal incentive structures, piecemeal or fragmented ESG integration, and a lack of courage and innovation by banking executives and shareholders, remain barriers to the pursuit of deep-seated, systemic change.

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**7. CONCLUSIONS**

* Values-based banking as a superior conscious business model approach and ethical excellence within the financial industry.

It is undeniable that Values-Based Banking is the very top peak to achieve in terms of what financial institutions have to do banking in order to face arising challenges in the world and becoming agents of positive change for the people and planet. It is demonstrated VBB’s superior performance and resiliency versus GSIB’s, but concerns about scalization of applying these principles to big mainstream banks are valid ones. Having a realistic early approach prioritizing possible things to comply over ideal ones with a clear path to transit from this first possible compliance stage to a full VBB’s compliance, is key to sum up mainstream banks to this model in a successful manner. This is not an easy task to do, high resistance from a very tight sector as banking is, with a lot of incentives and rewards to remain in the same old profit-at-any-cost driven model is a huge wall to bring down with the associated risk of being too rigid becoming it in a frustrating and impossible task to comply and follow or being too loose and not to serve to its purpose to change banking for good and just becoming in another *“greenwashing”* practice as it has happened with many other past and current initiatives.

Through initiatives and institutions like the GABV and VBB’s respectively, is how financial system as a whole can recover credibitlity with stakeholders (a.k.a everyone) and back to the roots of their very first “*raison d'être*”: to serve society by connecting borrowers and lenders and doing it in a sustainable way for this same society (by meeting the highest people and planet standards). Mainstream banks have gone the wrong way, making money out the money at any cost with high consequences for humanity and the world, which can’t take them any longer. The world needs and asks for a better financial system that would be part of the solutions, not part of the problems and fortunately, Values-Based Banks have shown there is a way for a better banking: client-centered, environmentally friendly and economically viable at the same time. A widespread adoption of the principles and a continuing model perfection in guidelines and reporting according to complexity in both, world and financial system challenges, are key for successful in the future.

This titanic challenge also requires our support as banking clients, demanding better services and higher standards to our banks and as people, citizens of the world, backing better practices for all wellbeing and turning against those which do the opposite. Our power of voice together is huge and nowadays there are a lot of communication channels to express it and contribute in an active way to make our world a better and fairer place to live in for everybody.