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*Sustainability Unwrapped* a conversational podcast about responsibility, ethics, inequalities, climate change, and other challenges of our times. Where science meets practise to think about a world and how to make our society more sustainable one podcast at a time.

Today we are talking about sustainability and ethics in the banking sector. My name is Emilia Vahamaa, and I am an associate professor in finance at Hanken. I get to discuss this interesting topic together with assistant professor Nebojsa Dimic, from the University of Vaasa, and Mika Leskinen, chief investment officer and head of ESG at FIM and S-Bank. Welcome, Nebojsa and Mika.

Thank you.

Thank you.

In my opinion, ethics is an interesting topic to discuss since most people have different views on ethics and also different attitudes towards it. And the topic is very much relevant for the banking industry for two reasons. First, banking is largely based on trust. And then second, banks can also steer other secretors by their financing decisions, so what kind of businesses to finance and what types to avoid, basically.

But in general, ethics and sustainability in the banking industry have gained a lot of attention after the financial crisis of 2008-2009. And the crisis was largely due to inadequate regulation and excessive risk taking. And since the crisis, the need for mechanisms to address these problems have been highlighted.

But today, I wanted to focus on a few very timely and interesting topics within this area of sustainability and ethics in the banking sector. There hasn't really been much guidelines in this area previously. But last year, United Nations launched Principles for Responsible Banking, and these principles provide a framework for sustainable banking system. And United Nations also claims that these principles help the industry to demonstrate how they make a positive contribution to society.

So what do you think, Nebojsa and Mika? Can such guidelines be really useful in practise?

Well, if I may start--

Yes.

I have experience on United Nations Principles for Responsible Investing, and those principles have had a great effort or effect on investing part of banking. So at least that gives some idea, hope that those principles you, Emilia, mentioned might have some effects as well in the future.

If I may add-- sorry. I don't know if I interrupted, but I find all of these initiatives by the United Nations and these global organisations quite useful in the world of sustainability and ethics. These principles of responsible banking that Emilia has mentioned are tightly connected to Sustainable Development Goals, our SDGs, which is probably one of the biggest initiatives by United Nations so far, as well as Paris Climate Agreement, which is another maybe second biggest initiative out there.

So those two huge initiatives are proven to make-- they made a difference and positive impact. So I hope that the Principles of Responsible Banking will follow that trend as well and help banks in order to carry their activities with the consideration of ESG impacts in those activities. So, as Emilia said, banks need to focus on their internal daily operations and how to integrate ESG into internal daily operations, basically how they manage their physical branches, locations, human capital, and so forth, as well as their external interactions with clients and basically what type of projects that will fund.

So considering these ESG impacts will be very good for them, and this initiative such as Principles of Responsible Banking is going to, in my view, make a difference.

Yes, I have high hopes as well, so let's see. Of course, always these types of initiatives can be used as kind of polishing the view of your company and not really making changes. But I hope and I think that these principles are actually so wide and covering that it's rather difficult, I would claim, at least, to try and fulfil all the criteria just in order to polish your public view.

And I also think that, for example, when we're talking about climate change and financing, investing to protect from climate change, it's very important to understand the difference between investing and financing because normally when we talk about investing and do investing, we operate in the market, and we don't actually finance, in many cases and anybody. So someone actually said [INAUDIBLE] when we were talking about the EU regulation, yes, it would be good if they would regulate also those parties that do financing, actually, not just doing stock market investing.

Sure.

So in that way or in that sense, it's these kind of new principles that cover wider aspect of investing,

i.e., financing would be welcome.

I agree. Well, then Nebojsa, you already brought up this Paris Climate Agreement. If we continue with that, so yeah, banks, for example, they can make a difference by not financing businesses that are fossil fuel heavy and focusing on promoting green energy instead. And so on. Can we really see the impact of these attempts in practise, and do they make a difference? What do you think?

Well, I'm a guy who is very enthusiastic about this whole sustainability world, so I usually see all of these agreements as something very positive, and then I see something good coming out of it.

Yeah.

I think this, in case of Paris Agreement, of course, I guess everybody knows that the United States is the country that opt out of the agreement with the Trump administration, which I think was a big hit to this whole attempt to stop this global warming. But as far as I understood, even though on the federal level, the United States is not pursuing these goals, on local levels, on the state level, it's happening. So people are realising that global warming and climate change is something that is happening, and they need to act in order to stop it.

So if Trump's administration doesn't want to go with it, they made a lot of effort on a smaller scale, on a state level, and companies are doing the effort as well and rest of the world at the same time. So I think these-- I just find these initiatives great thing. Of course they're not perfect, and it's difficult to put the whole world together in any of these initiatives because you have certain countries that are really advanced in terms of fighting the climate change or they take these environmental topics very seriously, such as whole Scandinavian region where we live over here.

But then at the same time, we have all these emerging markets that are-- not all of them, but many of them really don't take this issue seriously. So it's difficult to find agreement on a global level, but these are just great things to great attempts. And I think that they are working quite well. They're not perfect, but that's the best we can do right now.

Of course, I hope that everybody would jump on board and then take this even more seriously. But the agreement itself, I find it really good. All right, Mika has something to add.

Yeah, how about you, Mika? In practise, do you see this in your work?

I think yeah, although we know that the US policy hasn't been too supportive during the past few years. But let's see. Maybe in a few weeks' time there will be hopefully a different tone. But still there

are plenty of multinational US companies that have been active and leading the field, same as comparing between federal and states in USA. So there is a lot of things happening, although the top level hasn't been into it too much or maybe at all.

So in that sense, I am also quite optimistic that there are a lot of things happening all this time, although the regulation wouldn't especially need there to be action in some part of the world. And when it comes to Asia, I think in general, also there is a lot of things happening. China is the biggest investor in solar and wind farms, for example, or wind industry in the world. And they have stated new goals.

Most probably, those goals, if they actually confirm them, which seems to be the case, will be the most ambitious in the world just suddenly out of pushes, so to say. And also the environmental problems are so concrete in many parts of Asia, so it might be also easier to get this mentality through there. And there is support from people. And as long as people's income is rising so that their only problem or question for today is not where to get money to feed family that day, there are new kind of things that are of interest. And obviously environment, the environment they are living in, is one of those.

Sure. Well then, in addition to having an impact on the climate, banks can, of course, also promote other types of goals. Now, for example, if we take Goldman Sachs that have announced that they will not arrange any initial public offerings for companies with all-male boards. So this is, of course, clearly done in order to promote gender equality. What's your take on these types of actions?

Well, if I start, I think those are good, and they are good examples of the one who's got the money can say the rules.

Yes.

As long as you don't end up being the only one in the world doing that. In that case, it would probably not work completely because you would be out of the business. But obviously the idea is that someone has to start the trend, and others will follow, and then the improvement takes place. The not financing coal-based business is a good example. I think every day-- now we read every day big international banks coming out that say we won't be financing coal-based business from 2030 or 2040 onward.

And so and I think today really showed two of those announcements. So there, the big part of the businesses is moving in the same direction. And I cannot see any reason why that would be the case

in some other issues as well.

Sure. How about you, Nebojsa? Do you see a problem with these types of ways to guide other companies' strategies, or is that fine?

Well, a lot of times I would like to remind people that ESG stands for Environmental Social Governance. So a lot of people tend to think of this whole sustainability world as the climate change issue or global warming issue, as they feel that, OK, this is something we need to-- this would be the biggest problem that we need to solve right now in the world.

But ESG, there is social. There is governance issues. So it's great that there is initiatives toward some other areas, not just environment. Of course environment is a hot topic, and most of the people find environment as something that needs to be worked on the most. But yeah, this kind of stuff, such as gender equality, it's also included in the United Nations Sustainable Development Goals. And this is something that really needs to be taken care of.

And I think lately that there has been some progress in this area, but not nearly as enough as we need to make progress in here. So it's great. I find these thinkings really, really good. And again, this is a big challenge, because if I go back to this Western world versus some sort of emerging countries, some other parts of the world, you have some areas of the world right now that it's deep in a culture that women shouldn't be going to school or get education. Women should not work or drive a car or get a driving licence and so forth.

And it's some parts of the world, that's just how they've been living for so long. And this is something that I guess is-- it's a big issue to change the whole culture in these areas. But we must not forget that, for example, we had slavery in the United States as a part of the culture for a very long time, and it changed. We have a lot of areas in the world where LGBT population didn't have any rights, but now they do. So I think this is also something that can change and will change. In some areas, it's going to be a bigger challenge than in others, and it will take more time.

But these issues needs to be discussed openly, and all this bad statistics related to these needs to be brought up and discussed. And that's the way to make it better. And then I think it's possible, and these initiatives are great, and we need to all think of those also.

Yeah, but also back to my beginning on the point. It's not just environmental issues we talk about here. It's others as well, and quite a lot of them.

Yeah, sure. And related to gender equality, of course, we have, as you mentioned, big differences

between countries. And some countries have quotas, and we have EU recommendations, and then there are some stock market rules or regulations so that in order to list in a specific stock exchange, you might have to fulfil some criteria. And then this type of an initiative by a company that arranges initial public offerings. So this is an interesting way to steer as well. What were you saying, Mika?

Yeah, although it's true that climate change has taken the airtime, I would say 98% of the airtime, I tend to think that without climate change, the other shop checks wouldn't have got even this much attention than they are getting now. Because the climate change has lifted the whole concept of responsible or sustainable investing to high level that, although percentage-wise the other issues don't get too much, but in absolute terms, they do get quite nice attention as well.

And especially now, when the processes regarding climate change and investing have matured. They are not ready, but in many organisations they are in place. Now there is more time also to shift to see other issues as well. So climate change has had a big effect on other issues' attention as well.

Sure, and then we have research papers showing that often changes come together. So, for example, if we focus on independence, so at the same time we might improve gender equality. It's as if we have to replace some board members, so we might just as well fix a few other issues at the same time and so on. So I suppose this is [AUDIO OUT] that as well. All change or all attention, maybe, is positive in that sense.

Well then, I wanted to bring up also money laundering briefly since those problems have also gained a lot of attention recently. So banks are required to know their customers and the origin of the customer's funds. So how big a problem is this money laundering for the banking industry in practise, and then how can we control for that?

Well, that's a big question, and--

It's a heavy one.

No, I kind of work in a factory where we do investing. And I don't face clients as such too often.

Yeah.

Different people are working in the client space. But obviously the regulation, all regulation, and maybe especially the regulation related to money laundering and know your customer principles have had a big effect on the staffing in banks. I think even in Scandinavia, probably thousands of people have been hired to work in this area. So it has had an effect, and it's caused a lot of work in

the organisations. And it's very finely defined what you need to do at what stage of any process.

So I think banks do take the issue absolutely seriously, and no one wants to get involved with that issue in a negative way. That's for sure.

Yes, I agree. It's definitely-- it costs a lot of money in terms of lost business and lost--

Yeah, it costs everything.

--reputation if you end up with that publicity.

Yeah.

It's interesting, related to money laundering, that we had huge cases of HSBC, for example, and Mexican cartels' connection where this money from this money was being laundered from them, and even connection with some terrorist organisations and such a huge, huge cases. And then we fast forward to a few years from now and we have Danske Bank, for example, again happening and then Swedbank in Sweden.

So I was really disappointed learning about Danske Bank a few years ago, and I really didn't expect something like that can happen so close to us. But it was their Estonian branch, and a lot of money came from Russia from unknown sources and being laundering. It was one of the biggest cases in history in terms of how much money went through there.

And the Danske has such a big reputation, and this incident could have put the whole bank down. So you would think that it's impossible that this much money would go through to be laundered by such a big organisation. But it happened. But I agree that I think authorities are taking this very seriously and know nowadays it's getting harder and harder to do these kind of activities.

And I hope that we will not have such big cases in the future regarding to money laundering. Because I think banks are really-- these banks that went through these incidents got affected a lot, and then now these other banks don't want to be on the same boat anymore, so they're trying to do the best they can to stop it.

And actually we discuss in the classes I teach what should banks do in order to avoid this in the future, what kind of monitoring transparency system they should introduce. And of course we don't solve these issues because it's difficult to solve the money laundering in a classroom. But quite a lot of interesting suggestions come up where we come up with them and discuss them. And I hope that

such a big cases are not going to happen in the future.

Yeah, and it's a good reminder that governance does matter.

Exactly.

In the end, it's a governance issue.

Indeed. Well then, how about the hot topic of the present moment, so the pandemic? Do you see some kind of an effect by that in the banking industry in ethics and sustainability? Is it so that all the attention now globally goes to the pandemic and at the same time businesses can do whatever? Or are these related in any way?

No, at least I cannot see it that way. For example, in my daily work, thinking I'm doing this is just one additional issue that's probably going to be present a few years. And it hasn't slowed our interest in climate change or things related to climate change basically at all. Also probably this will leave some new thinking on risk consideration side of investing. But this will be just one topic among others.

Although not denying at the moment it's the topic. But it won't change too much in the long run, I think.

Yes, and something we have discussed earlier about Principles of Responsible Investing, and actually Mika has said that in 2020 there is quite a huge increase in signatories of the United Nations PRI, and it's quite the big surprise that-- or maybe not a surprise. Maybe people just understand that these issues are very important, and regardless of the COVID crisis and spotlight that COVID has taken, we can see that people still care about these environmental, social, or governance issues.

So they are still signing these principles. And the encouraging thing was that in some other parts of the world besides Europe, there's been increase in signatory since 2020.

So the same things are basically happening despite the pandemic, or the same type of development. So, yes, sure, more things maybe happen online than before, but, yeah, hopefully the direction is still the same.

Yeah, I think in banking the trend has been, as we know, for not going into the branches anymore. So this is nothing new in banking now. [INAUDIBLE] the employees don't go to the branches anymore. We work at home. [LAUGHS]

Same everywhere, I suppose--



Yes.

--in all kinds of businesses. Well, how about, then, do you have any topics that you wanted to bring up?

I was thinking about a little bit how banks would benefit from doing sustainable jobs--

Yeah.

--or what this sustainable banking brings to banks. And I checked some studies and a little bit of academic research of that. And basically the big one-- I don't know if you would agree-- is that the reputation. So, as we just talked about, these cases of, for example, money laundering in Danske Bank, the reputational hit is huge in these kind of cases.

If you have a money laundering case, or if you're not treating your employees well, it's going to hurt you. So banks need to keep up with their business to avoid these kind of reputational hits, as well as in investor confidence. And Mika probably has something more to say, like how do investors feel when they see that there is a problem in certain organisation or a company or a bank, so they don't want to do business with them.

So this reputation of benefits and this investor confidence is something that would help banks if they perform sustainable banking. I don't know if you have some others that, what do you think, why banks would benefit from doing sustainable business.

Yeah, I think soon, you cannot make a difference by doing more and more sustainable things. You'll make a difference if you don't do, i.e., just stay in the business you need to do those things. And this is so heavily competed area that you don't get an advantage of getting more fees or similar if you're doing sustainable things. You need to price the loan or whatever competitively anyway. You cannot properly demand a premium, even if your product is more sustainable.

Obviously there must be people who are ready to pay more for being sustainable, but there are plenty of people who won't be paying a premium for sustainable things. So in that sense, I think you cannot think that [INAUDIBLE] kind of increase fees because this is a sustainable product or so, because everybody's doing it sooner or later, and there is great competition.

Yeah, so it's maybe more of that negative downside--

Exactly.

--as opposed to-- yeah, so you don't want to be the bank that gets caught related to interest rate manipulations or whatever we've now seen in the past. So, yes, you may get record fines from the authorities, but on top of that, it's that reputational hit--

Yes.

--that is the big deal there. Yes, the discussion has been really interesting, and I think that it's time to start to wrap it up at this point. So where do you see the future in this area? Or where are we heading? Is the future a good one?

I think we are keeping the track, i.e., the direction is clear, and it will only get-- the transition will only get faster going forward. So, yeah, I don't expect any major new kind of revolutionary ideas. We know we need to be more sustainable in every action we take. And whether it's working-related decisions or your free-time-related decisions, the only way is towards more sustainable action.

Do you think that in the future, the playing field will be more even globally so that countries will be closer to one another? Or do we still-- even if we have improvements all over the globe, basically, do we still have big differences left in the future as well?

Well, there will always be differences based on local issues or local cultural things, maybe. But when it comes to climate change, I think things will be harmonising over time. And legislation such as is coming out in European Union will, sooner or later-- hopefully sooner-- happen in other places as well, with some local differences, obviously. But the big picture is getting harmonised.

How about Nebojsa? Do you have any take on this?

I definitely agree with Mika here. It's evident that the ESG issues are here, are present, and they're part of the business practises, no matter if we talk about banks or any other industry. These issues are important. And companies are trying to incorporate these in their activities and their business practises.

So of course it is necessary. The banks take part of this as well, and it's natural that now we have initiatives for the banks as we had for some governments or certain companies or industries. So it's important that banks come onboard and they are on board. And in the future, I think this whole area will just grow stronger.

I don't see this, as Mikhail said, any major changes that will happen in the future, except that these

issues will become more important, and there will be more initiatives and a bigger push by the banks to achieve this sustainable banking. Because there is no other way. If banks want to keep their customers, if they want to keep the best employees, they just need to get on board of sustainable banking.

I don't see that it's possible, and especially in the future that it will be possible to completely avoid these issues and still be successful. So I think this will continue. Because if we want to make this world a better place, we have to push from the different angles. So banks are going to do their share. I'm sure of that.

Yes, and I completely agree. And I also think that [AUDIO OUT] other companies via banks, so via who gets funding. So that is a very effective way. So you can require or ask for all kinds of changes just as this Goldman Sachs policy to not take initial public offerings further which don't have women on company's boards and so on. So these types of things that would take a lot of effort from the legislators are rather simple, then, if you put it that way so that the bank requires something in order for you to get funding or to get service from them.

And I also think, if I can add, banks are enormously powerful. Some of these big banks are bigger than some small countries around the world. So the decisions the banks make can make a huge impact. So stuff they do can really make a difference. So that's why I think that it's really important and it's really good to have banks on board in the sustainability world, and then they keep on doing even better job in the future.

Because we had these cases of money laundering that we talked earlier. And there is lots of discussions about, for example, bankers' bonuses that they pay, the environments in banks' trading floor and someone investment bank, how aggressive and greedy and risk-loving they are. I mean, I'm talking now 20 years in the past, 10 years in the past. I'm sure now the situation is changing for better.

So I think the way banks act can make a huge, huge impact. So this is why this topic is very important and timely. And I see good things happening in the future.

Yes, and in general, it does seem that the banks are interested in the area themselves as well. And now just that I checked, it was 185 banks who have signed these Principles for Responsible Banking by the United Nations and so on. So it's not irrelevant in that sense.

Many are interested, and it is a high priority to them. And hopefully our future graduates as well that we are now educating at these universities will be knowledgeable and will make a difference on their

behalf as well. Yes, Mika.

Yeah, I would also like to remind that banks and other institutions can also do a lot of things without signing some [INAUDIBLE].

Sure, definitely.

So first of all, signing something, it doesn't necessarily mean you are doing a lot of things. But one can do a lot of things even without signing. There might be some rational reasons not to sign some principal.

Yeah, of course, all these agreements are not for institutions in all sizes and--

Yes.

--in all types of-- yeah. It's not always doable, but, yeah, definitely it just shows that there is interest and that banks are willing to commit to these types of efforts.

I thank you both for this interesting discussion. Thank you for joining this session, and let's wait and see what happens, what the future brings in this area. It's an interesting area to follow. Thank you.

Yep, thank you.

Thank you very much for the invitation.

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