Global Alliance for Banking on Values

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NYENRODE BUSINESS UNIVERSITEIT

THINK BOLDER | THINK VALUES-BASED BANKING

BEST PRACTICES FOR SUSTAINABLE MARKET TRANSFORMATION IN THE BANKING SECTOR

LEADERSHIP,
ENTREPRENEURSHIP,
STEWARDSHIP

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NYENRODE. A REWARD FOR LIFE

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INTRODUCTION

European Union regulation aims to re-orient capital flows, mainstream sustainability in risk management, and foster transparency and long-termism[1]. This agenda, which started with an investor perspective, has built the first foundations for facilitating sustainable investments[2] by requiring all financial market participants to inform investors about the economic, social and governance impact of products and investments.

Corporations and banks assess material physical, transition and litigation risks through various frameworks, including the European Sustainability Reporting Standards, the Corporate Sustainability Reporting Directive and new accounting obligations for climate risk. These actors must describe how they are managing those risks by showing how they are making sure that their business model is ready to operate in a different reality and by providing an assessment of the resilience of their business models in the face of environmental and social developments. Today, the EU Capital Requirements Regulation[3] and the global ISSB IFRS S1 & S2[4] are among the frameworks that either legally or implicitly oblige[5] banks to track actual performance through GHG disclosures.

However, the development of both opportunities and risks in sustainable finance in the European Union has primarily been driven forward through policy and/or regulation. This develop-

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1 The "Sustainable Finance Action Plan" (2017) is a Renewed Sustainable Finance Strategy that includes all stakeholders in the financial system in the EU and aims to phase out harmful economic activities.

2 According to SFDR Article 2 (17), sustainable investments are investments in an economic activity that contributes to an environmental objective or a social objective provided that such investments do not significantly harm any of those objectives and that the investee companies follow good governance practices.

3 *Implementing Technical Standards* for Art 449a CRR specify financed emissions. For more, see https://www.eba.europa.eu/implementing-technical-standards-its-prudential-disclosures-esg-risks-accordance-article-449a-crr.

4 For more on *IFRS S1 General Requirements for Disclosure of Sustainability*-related financial information and IFRS S2 Climate-related disclosure, see https://www.ifrs.org/projects/completed-projects/2023/general-sustainability-related-disclosures/.

5 For example, BCBS's *Advice to Supervisors on Transition Plans Pillar 2*. For more on priority themes, see https://www.bis.org/bcbs/bcbs__work.htm.

ment represents a change from the other sustainable market transformations that the financial sector has experienced. Consider the Partnership for Carbon Accounting Financials (PCAF), an offshoot of a Dutch financial industry initiative to develop a greenhouse emissions (GHG) accounting standard for itself[6] after the 2015 Paris Climate Agreement recognised the financial sector as having an enabling role in the achievement of the most ambitious climate-related goals. The text of the Agreement defined specific targets to be collectively achieved to limit global warming to well below 2°C, and preferably to below 1.5°C, by offsetting carbon emissions by the equivalent amount of carbon reduction elsewhere.

To accelerate the transition to a low carbon future, the Global Alliance for Banking on Values (GABV), a global network organisation of 70 financial institutions in 45 countries, announced the Climate Change Commitment (also called the 3C initiative) in 2019, during its 10-year anniversary celebration in Vancouver. The 3C has been transformative in letter and spirit, mobilising signatories to "assess and disclose the climate impact of their portfolio of loans and investments within a period of three years, and ultimately to ensure that the climate impact of their loans and investments are in line with the Paris Agreement". Along with this initiative, the GABV partnered with the PCAF, first in the Netherlands and then in North America, to become the driving force behind the globalisation of the PCAF Standard. The financial sector has recognised the organisation's critical role in enabling the transition.

The PCAF Standard's evolution from a regional sector initiative to a global institutionalised GHG disclosure obligation inspired the GABV to launch the Values Regulation in Europe (VALoRE) project in 2020, with support from the Open Society Foundations. The aim of VALoRE was to strengthen the capacity of the financial sector in Europe to deliver a just transition to a low carbon, socially inclusive future. It also provided an opportunity to identify the alternatives that values-based banks offer to the market to enable sustainable outcomes.

With the rise of ESG (Environmental, Social and Governance) criteria at traditional banks, it is even more important to be clear on just what can be achieved with ESG screening and what additional impacts can be created with a Triple Bottom Line (TBL) approach to banking, one that is centred on enabling social empowerment, economic prosperity, and environmental regeneration.

This synthesis report presents lessons learned from leading values-based banks in a world with ESG reporting. It seeks to inspire market participants to adopt and reward the sustainable behaviours of values-based banks to eventually create a sector strategy that goes beyond ESG. The report also indicates what the broad adoption of the distinct practices of values-based banks means for changing the rules of the game in the banking industry.
The practices of values-based banks are distinct because 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. To understand how they do this, the practices of the different banks need to be compared to distil their core components. From this analysis, we propose nine distinct practices.

This report has three parts. Part One provides the background to the study and briefly introduces the values-based banking model and ESG. Part Two introduces the Sustainable Market Transformation framework used to inform the collection and analysis of the practices of values-based banks. This part also presents a comparison of these practices and ESG informed practices, which highlights the opportunities for building on these locally proven initiatives for eventual institutionalisation. Part 3 outlines elements to consider when creating a sector strategy. At the end of this report are brief concluding remarks.

6 Simons, L. & Nijhof, A. (2021). *Changing the Game: Sustainable Market Transformation Strategies to understand and tackle the big, complex Sustainability Challenges of our lifetime,* Routledge: London.

CROWD
CONTAINER

PART I
BACKGROUND

The GABV envisions a world in which finance is at the service of people and planet. Achieving this vision requires deep changes in attitudes, incentives, and behaviours. This, in turn, requires a change in the purpose of financial institutions and government regulation.

In 2020, with support from the Open Society Foundations, the GABV launched VALoRE with the aim of strengthening the capacity of the European financial sector to bring about a just transition to a low carbon, socially inclusive future. The workstreams delivered a series of robust best practices intended to inform work on sustainable finance in the European Union. VALoRE workstreams also articulated individual actions around social sustainability for the financial industry, regulators and policymakers, researchers and customers.

VALoRE insisted that the financial industry, including bank managers, investors and public authorities, needed to design and embed effective social impact processes across all their systems, products and services. It called for stricter selection protocols to support financing positive impact and avoid financing harm in the areas where the bank's core business and major activities are currently based.

To make the social impact approach of values-based banks widespread, the GABV called on regulators and policymakers to tackle obstacles to scaling up, including acknowledging the low-risk profile of social impact portfolios in banking rules, limiting the finance of harm, and helping to empower citizens to invest in positive impact. VALoRE encouraged regulators to recognise and support the social role of local and values-based banks, who are by design more resilient and connected to local and global sustainability.

VALoRE examined the work of three GABV members—Banca Etica in Italy, GLS Bank in Germany and MagNet Bank in Hungary—and the viable market alternative that they provide that enables sustainable outcomes. This exercise highlighted that the difference lies in these values-based institutions' holistic and coherent management, which is centred on delivering social empowerment, economic prosperity and environmental regeneration. In other words, sustainability for these institutions is neither a checklist nor an add-on, but rather their purpose.

VALUES-BASED BANKING

Values-based banks operate according to a set of six principles[7]. They have:

1. Economic, social and environmental performance as a 'triple bottom line' at the heart of the business model.
2. A grounding in communities, where they serve the real economy and enable new business models to meet the needs of both.
3. Long-term relationships with clients and a direct understanding of their economic activities and the risks involved.
4. A long-term perspective that is self-sustaining and resilient to outside disruptions.
5. Transparent and inclusive governance.
6. A bank culture which embeds these principles.

7 *Principles of Values-based Banking*. Available at https://www.gabv.org/wp-content/uploads/2022/02/Principles__def.pdf.

The values-based banking model "brings positive financial innovation focused on meeting human needs in the real economy"[8]. In essence, these banks want to use, and enable others to use, money to consciously contribute to a world that flourishes within the nine planetary boundaries and twelve dimensions of the social foundation[9].

According to a 2021 study of the best practices of 30 values-based banks, making positive social change happen requires clarity into what is considered positive impact[10]. It requires coherent implementation and monitoring. A banking model that fails to integrate positive impact in this way is likely to support activities that harm at least someone or something and benefit only a few. Consider the finding of a study that examined the terms agreed in more than 100 public company acquisitions announced during the Covid pandemic. The authors found that although many of these companies espoused ESG criteria, they secured large gains for shareholders and corporate leaders in these acquisitions while neglecting the interests of wider stakeholders[11].

Values-based banks understand that neither markets nor shareholders alone can be relied upon to deliver positive social impact objectives under the current incentive structures and mismatch between benefits and costs. What constitutes positive impact and social sustainability needs to be spelled out if we are to achieve the type of global transformation required to meet the Sustainable Development Goals (SDGs), the United Nations blueprint to deliver a better future by 2030[12].

Values-based banks have financed positive impact for decades, proving that non-extractive finance is possible and viable. They understand the connection between economic stability and human rights, equal opportunities, social inclusion, and access to high-quality services. And they follow a holistic, continuous and comprehensive approach to delivering positive social impact.

It is clear the world urgently needs action that delivers change. We need to change finance to finance change. GABV's practitioner-informed approach is to identify key gaps, collect best practices and identify pathways to maximum impact and transformation. This approach is oriented towards actors capable of driving such changes and those who exert influence upon them, including member banks, partners, regulators and stakeholders in the EU, and EU countries.

ESG AS THE STARTING POINT

An important development is that due to regulatory reforms and related risks, retail, commercial and investment banks focus more on integration of ESG aspects when making decisions about financial products. These regulatory reforms define ESG "as the process of considering actual or expected climate, social and governance factors and their effects on investments when making investment decisions"[13].

While the term ESG is often used in reference to the identification of environmental and social risks, and the corresponding risk management response, at the most fundamental level, it is another dataset. This dataset broadens the set of risks to a bank, its clients,

8 Peter Blom, former Chair of the Board of the Global Alliance for Banking on Values and former CEO of Triodos Bank in UNEP (2015), *Values Based Banking Bringing the Voice of the Citizen into Finance,* Inquiry Working Paper 15/03. Available at https://wedocs.unep.org/bitstream/handle/20.500.11822/9673/-Values_Based_Banking_Bringing_the_Voice_of_the_Citizen_into_Finance-2015Values_Based_Banking_-_Bringing_the_Voice_of_the_Citizen_into_Finance.pdf.pdf?sequence=3&%3BisAllowed=.

9 Raworth, K. (2017), *The Doughnut of Social and Planetary Boundaries.* Available at https://www.kateraworth.com/doughnut/.

10 Kocornik-Mina, A., R. Bastida-Vialcanet and M Eguiguren Huerta (2021). Social Impact of Values-based banking: Best Practises and a Continuity Framework. *Sustainability,* 13(14), 7681. available at: https://www.mdpi.com/2071-1050/13/14/7681.

11 Reported by Moral Money (14 February 2022). Falling out of love with stakeholder capitalism. Financial Times, and also available at Bebchuk, L.A., K. Kastiel and R. Tallarita (2022). Stakeholder Capitalism in the Time of COVID". *ECGI Working Paper Series in Law*. 670/2022. Available at SSRN: https://ssrn.com/abstract=4026803.

12 Sustainable Development Goals available at https://www.un.org/sustainabledevelopment/sustainable-development-goals/.

13 See also, OECD (2021), *ESG Investing and Climate Transition – Market Practices, Issues and Policy Considerations.* Available at: https://www.oecd.org/finance/ESG-investing-and-climate-transition-market-practices-issues-and-policy-considerations.pdf.

and their activities to include environmental, social and governance dimensions. The findings inform the implementation of new policies, procedures, tools, products, services, etc. and are often subject to monitoring and disclosure requirements.

More recently, regulators have been issuing ESG requirements. They often focus on ESG risks (single materiality) and do not consider ESG-related impact (double materiality). There is a risk that this new kind of regulation could absorb considerable resources without necessarily adding value, at least to those banks that are already considering environmental and social impacts in their activities. It is important to engage with regulators early on so that regulatory efforts will prove effective and cost-efficient.
There are challenges for implementation of ESG as well, such as the publication of different approaches, data inconsistencies and the lack of comparability of ESG criteria and rating methodologies. A failure to address these challenges could limit the "pace and scale of the capital allocation needed to achieve tangible progress to support long-term value and a transition to low-carbon economies"[14].
Yet, once implemented, ESG practices are expected to mitigate risks, capture new market opportunities, and align with changing stakeholder expectations. Unfortunately, only with thoughtful implementation might ESG standards contribute to long-term financial stability, resilience, and reputation for banks supporting sustainable development goals. In other words, ESG alone is unlikely to deliver the required sustainability outcomes.

Institutions that adopt ESG need to start thinking more like values-based banks. That is, a bank that has placed ESG at the core of its business model must see educating clients, partners, and authorities about the importance of following ESG principles as part of its mission. The additional effort required for proper implementation highlights how much of the expected transformational role of ESG actually depends on the quality and ambition of the institution.

14 OECD (2021), *ESG Investing and Climate Transition – Market Practices, Issues and Policy Considerations.* Available at: https://www.oecd.org/finance/ESG-investing-and-climate-transition-market-practices-issues-and-policy-considerations.pdf.

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PART II
VALUES-BASED BANKS CAN INFORM A SECTOR STRATEGY

There is an acknowledged and ever-growing tension between the challenges we face and the models and approaches we rely upon to address them. According to the *Manifeste pour la Démocratisation de L'Europe*, a manifesto containing concrete proposals that was launched by Thomas Piketty and other European citizens, Europe must build a new model to ensure the fair and lasting social development of its citizens and move away from vague and theoretical promises[15].

Models that discount the interconnectedness and responsibilities of peoples to their environment and future generations in favour of short-term utility and profit maximisation yield unsustainable outcomes. In the last 30 years alone, the world has gone through eight financial crises, from the Latin American sovereign debt crisis in 1982 to the 2008 global financial crisis. These crises expose extensive misconduct and self-interest and are typically followed by regulatory overhauls and bankruptcies. Absent changes in the rules of the game, the question is not whether there will be another crisis, but when.

SUSTAINABLE MARKET TRANSFORMATION FRAMEWORK

This study applied the Sustainable Market Transformation framework to analyse how the rules of the game are changed in the financial market[16]. In this framework, markets refer to sets of related transactions between different actors in an enabling environment. What these transactions have in common is that they all relate to a specific product, service or value proposition. For example, the market for financial services (general) or the market for financial services in values-based banking (specific). Market transformation adds the time dimension to the concept of markets. Markets are not static phenomena; they develop over time.

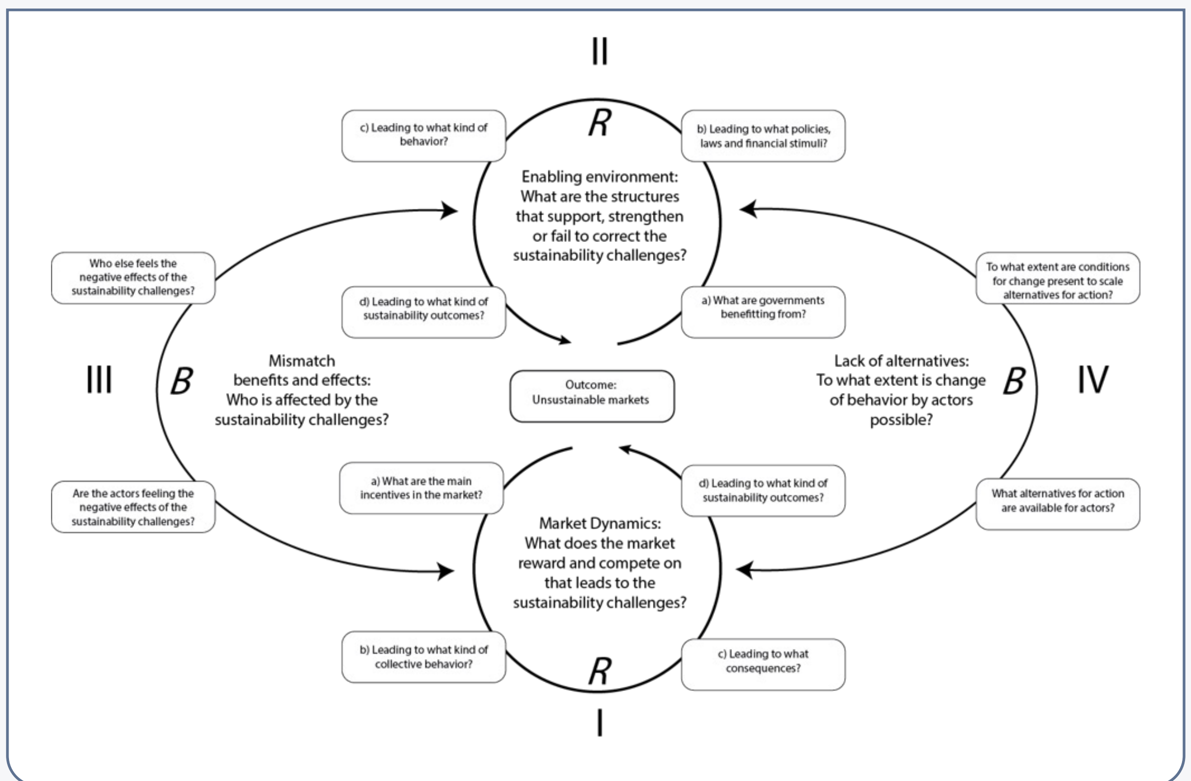
Sustainable Market Transformation refers to the extent that sustainability issues are included in the transactions in a market. A sustainable market transformation refers to a market's elevation to higher levels of sustainability.

According to the Sustainable Market Transformation framework, transformation can be explained by analysing the regulative pressures and the social and professional normative pressures in combination with the economic mechanisms at play. These different pressures are included as system loops that lead to unsustainable outcomes in Figure 1.

15 Original in French: *"L'Europe doit bâtir pour ses citoyens un modèle original de développement social, equitable et durable, et elle ne pourra les en convaincre qu'en sortant des promesses vagues et théoriques."*

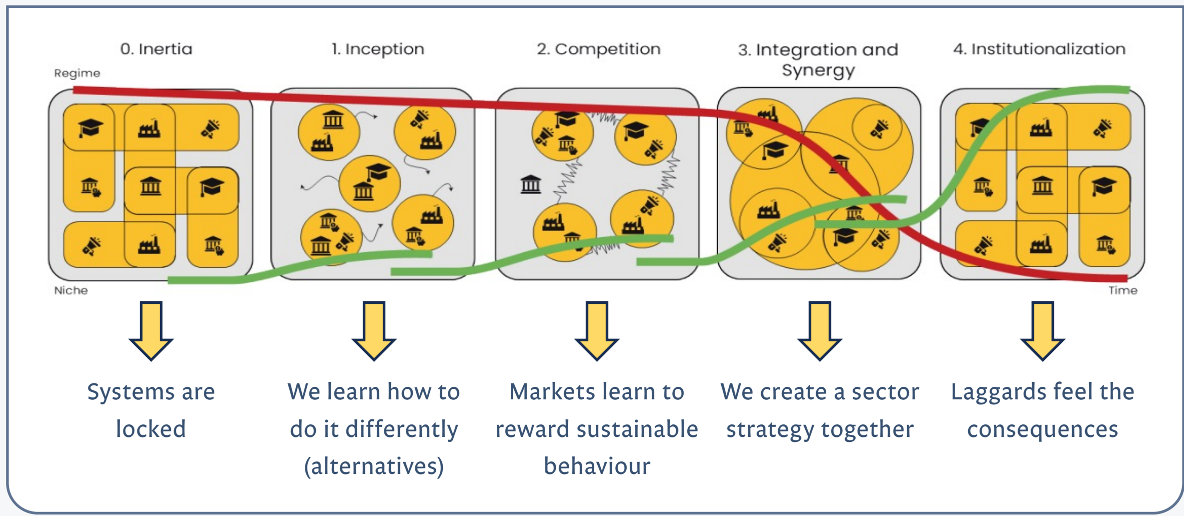
16 Simons, L. & Nijhof, A. (2021). *Changing the Game: Sustainable Market Transformation Strategies to understand and tackle the big, complex Sustainability Challenges of our life time,* Routledge: London.

Figure 1. Effectuated system loops for traditional forms of banking



Each of the system loops is changed in a specific phase of the market transformation process[17]. This implies that fundamental change is made more actionable by breaking it down into five phases, with specific interventions for companies, governments, financial institutions, NGOs and knowledge institutes. Each phase comes together with a specific dynamic so that roles of different actors evolve over time. What was still effective in a previous phase might be an obstacle for more sustainable outcomes in the next phase (see Figure 2).

Figure 2. Sustainable market transformation curve



17 Nijhof, A., Argyrou, A. A., Chevrollier, N., Wins, A. (2022). Sustainable market transformation. A refined framework for analyzing causal loops in transitions to sustainability. *Environmental Innovation and Societal Transitions,* 42, 352-361.

In Figure 2, each phase has an S-curve representing the start of the new behaviour and its rise per phase until a saturation point is reached that marks the end of one phase and the start of the next. It suggests that there are always some actors who prefer the old ways and resist change while others are trying to create a more sustainable future[18]. This process is not sequential (one event followed by the next) but is all happening at the same time. So, at the beginning of each phase, there is a broadly accepted pattern of behaviour (how we used to do things) and there is an undercurrent of new patterns of behaviour. At the end of a phase, the undercurrent has become mainstream, thus creating space for a new undercurrent moving towards the next phase. The duality in these processes makes a battle between forward-looking market actors who want progress and laggards who are still in denial that the problem even exists and are satisfied by doing more of the same predictable[19].

It is not surprising then that the evident change in the mainstream banking sector, particularly at the supranational level with initiatives such as UNEP-FI's Principles of Responsible Banking that seeks to shift incentives towards social well-being and environmental sustainability, is hampered by the quality of implementation. Or that as long as priorities appear to be in competition with human and environmental considerations, the impact of these efforts on the core decision parameters and risk models used by bankers worldwide, as well as by governments and regulators, will remain limited. Without changes to the system that now rewards short-term and accounting driven profit maximisation over outperformance on sustainability impacts, these initiatives are likely to remain narrowly focused. In the end, given the scale and persistence of social, environmental, political, technical and economic challenges, the speed at which the banking system changes is likely to be insufficient without additional efforts.

VALUES-BASED BANKING ALTERNATIVES TO INFORM A SECTOR STRATEGY

We noted earlier that the approach of GABV members is different. It focuses on banking based on values and visions of sustainable, inclusive, diverse futures. Values-based banks go beyond strict exclusion criteria and a sustainable product offering to the intentional use of finance to tackle social inequality and environmental challenges. They help to build resilient, inclusive communities.

The decision making in values-based banks is based on a holistic and intentional approach designed to contribute to positive social and environmental change in society. Instead of screening for ESG risks in their financing activities, GABV members aim for Triple Bottom Line (TBL) financing. This is the additional, transformative and intentional financing GABV banks offer alongside the more traditional financial products offered by all banks. Values-based banks consider sustainability as a value that permeates all aspects of a bank's operations and culture.

Values-based banks have key practices that contribute to positive social and environmental change in their communities. This report identifies several practices and examples of how values-based banks change the rules of the game in the financial market they operate in, based on the case studies of Magnet Bank, GLS Bank and Banca Etica. Some of the identified practices were still emerging at the time of writing and so will require more institutional support to be able to be applied over the entire portfolio. However, this study included a practice in this analysis if it seemed to be a promising and distinct pathway for contributing to positive social and environmental change. Table 1 presents an overview of the key characteristics of the practices of regular banks and how they differ from the practices of values-based banks. The highlighted practices cover aspects of operations, data use and transparency, as well as engagement and outreach.

The banks studied are retail banks that also offer commercial finance. However, the principles identified will also apply to a high degree to other types of banks, such as universal banks and investment banks.

18 Geels, F., Schot, J. (2007). Typology of sociotechnical transition pathways. *Research Policy* 36 (3), 399–417. https://doi.org/10.1016/j.respol.2007.01.003.

19 Holtslag, M., Chevrollier, N., Nijhof, A. (2021). Impact investing and sustainable market transformations: The role of venture capital funds. *Business Ethics, the Environment & Responsibility,* 30 (4). doi:10.1111/beer.12371.

Table 1: Overview of the core features of regular banks and values-based banks in relation to nine distinct practices in a world with ESG

PRACTICE	REGULAR BANKS	VALUES BASED BANKS
1. Scope of screening	ESG risk screening	Impact plus screening
2. Sharing of knowledge	For own use	To inform and empower
3. Intention in decision making	Profit	Positive Impact
4. Reaching out	Creditworthiness	Need for finance
5. Product offerings	Return on investment	Return on relationship
6. Reconnect savers and borrowers	Anonymous / Black box	Give influence to clients
7. Influence transformation	No pro-active influence	Use influence for responsibility
8. Voice alternatives	Follow rules	Advocate for policy reform
9. Nurture synergies	Sustainability as add-on and/or checklist	All aspects of the operation tailored to deliver

Together, these nine distinct practices raise the ambition for the banking sector beyond ESG:

1. **Broaden ESG screening to Impact screening:** Many regular banks only aim to reduce credit risks. From that perspective, ESG becomes a screening exercise to identify and exclude or manage ESG risks. Values-based banks demonstrate the advantages of prioritising purpose for the real economy and the community. While this involves making ESG risks explicit, client assessments and related financing decisions are made in pursuit of positive impact. Therefore, the screening process is not restricted to identifying how environmental, social and governance aspects influence the financial value of a transaction, but also to showing how this financial transaction creates a positive impact on these same aspects. For example, Banca Etica has a well-functioning method that measures the impacts created by their credits.

2. **Ensure knowledge sharing with all stakeholders:** The screening of clients generates a lot of information related to sustainable social, economic, and environmental development. Values-based banks do not treat this information as their own. They aim for radical knowledge sharing so that every stakeholder can use this information. For example, at a customer level, Magnet Bank provides information in the form of an impact scorecard so that clients are aware of what their money is doing. At a business client level, this information can support the preparation of sustainability reports to clients such as those that Banca Etica is piloting. At a sector level, this same information can be used to generate benchmark reports, including ambitious and inspirational organisational processes in relation to sustainability.

3. **Base decisions on intentionality of positive impact:** At regular banks, the entire organisation is dedicated to making profit and might generate social and environmental value almost by accident. Conversely, in values-based banking, an tailor-made organisation applies a holistic and intentional approach to real economy transformation to the entirety of the portfolio. This is called the Triple-Bottom-Line approach to banking. The case study of Magnet Bank illustrates how an organisational culture embedded in values provides the foundation for all their financial and supporting activities. And at GLS Bank the intentional approach to People, Planet and Prosperity is not only enacted by excluding investments they do not want to be associated with, but also by

actively using and evolving finance to do good by measuring how investments respect planetary ceilings and social floors.

4. **Aim to provide finance to socially relevant clients:** Another practice of values-based banks is broadening the interpretation of clients included in financing activities. Typically, the norm is clients who are creditworthy. For values-based banks, the norm is different: they aim to finance societal actors who are contributing to positive change in society. Instead of excluding risky clients, values-based banks aim for the inclusion of socially and environmentally relevant clients by looking at the needs of people and then looking at how finance can support those needs. GLS Bank is aiming to finance clients involved in permaculture, shared living and alternative schools. Magnet Bank functions as a "last resort" for some NGOs and other social organisations who have difficulties in finding financial resources.

5. **Expand product portfolio:** Innovative products are required to be able to also finance clients with lower creditworthiness. Financing for the transformation of the real economy requires continuous innovation, providing products that are needed and finding a way to become profitable in the long-term. To do this, banks need to be working in partnership with others for the longer term. For example, to address systemic biases that favour higher earning occupations over other socially relevant ones, GLS bank invests to support student loans that set interest rates with consideration of structural differences in earnings by occupation. Or for Banca Etica, the unpaid accounts are three times lower than those at regular banks because they invest in the relationship with clients who receive a Relationship Guarantee based on their commitment to their obligations. Magnet Bank offers a "Pay as you like" system for the management of retail accounts because they do not want to exclude anyone from banking with them.

6. **Reconnect deposit owners with impact:** Normally, clients who give their savings to a bank have no idea how this money is invested. Banking is organised like a black box in which money flows in and out and somehow generates a return. However, values-based banks open up the black box around their investments. For example, Magnet Bank gives savings clients a voice in how and where to invest a part of the assets of the bank. And GLS Bank requires every client to sign off that it is okay to disclose what projects are being financed because they aim for 100% transparency by showing on their website where the money is going.

7. **Stimulate loan recipients to transform their practices:** Any transaction with a client is not just financial. Banks always have an influence on the activities of the client due to the conditions linked to the transaction. These conditions can be focused on increasing creditworthiness but can also be used to stimulate clients to become more responsible. The latter is done by values-based banks. For example, GLS Bank supports clients with investment proposals that strengthen their social and environmental practices or by showcasing the effect of different CO_2 prices on the business models of clients. Magnet Bank views its role not as directly creating social impact, but as assisting their clients to create social impact.

8. **Raise the voice of banking for just institutions:** Banks have significant knowledge about the influence of governmental policies on the real economy. They can use this knowledge to advocate for just institutions. For example, through VALoRE, the GABV advocated for progress in a social taxonomy and for the exclusion of gas and nuclear from the green taxonomy of the European Union.

9. **Tailored organisation to deliver positive social and environmental impact and sustainability:** Banks have intentionally pursued synergies across all aspects of their operations. Banca Etica, for example, has developed an Impact Appetite Framework and a Risk Appetite Framework. The Board is responsible for ensuring both frameworks are met. Departmental collaboration is grounded in a joint commitment to impact.

PART III
THE WAY FORWARD

Can these practices result in system change in the financial market? To answer, we must take a closer look at how system change is triggered. One of the key takeaways of systems thinking is: "The problem we see is not the problem we need to solve."[20] The problem we see is a natural outcome of a system. To assess whether system change is happening, we must analyse its deeper levels and determine to what extent collective behaviours in the banking system that generate sustainable outcomes are being stimulated. According to the systems theory of Sustainable Market Transformation described in Part Two, there are four generic system loops that assess what type of collective behaviours are being stimulated (Figure 1 above).

The Market Dynamics system loop (I) addresses the rules of the game in relation to what the market is competing on. For many banks, sustainability is seen as a risk that might influence the value of their assets. This triggers collective behaviours like ESG screening and maybe exclusion of clients that are too risky considering their ESG score. However, the practices of values-based banks show that sustainability can also be seen as an opportunity for long-term investments. By showing that purpose and good financial results go together, the mindset of other banks can change from a perception that Triple-Bottom-Line approach is possible, through showing it is viable, to showing it is desirable because it offers clients value not only in terms of providing credit but also by determining the intentionality of their impacts and enhancing their public reporting processes.

20 Simons, L. & Nijhof, A. (2021). *Changing the Game: Sustainable Market Transformation Strategies to understand and tackle the big, complex Sustainability Challenges of our life time,* Routledge: London.

The Enabling Environment system loop (II) addresses the rules of the game in relation to government policies. Here, the main rule that is challenged is getting rid of finance as a black box. Governmental oversight requires transparency in how financial transactions positively or negatively influence the real economy. Due to the radical transparency practiced by values-based banks, the banking sector will become more transparent and therefore make governmental oversight more effective.

The Consequence system loop (III) addresses the rules of the game in relation to who is enduring the consequences of the current outcomes. This is only influenced to some extent by the practices of values-based banks. Clients who have difficulty in attracting finance from regular banks might suffer the consequences if all banks were only to apply the traditional way of banking. So, this part is changed by how values-based banks operate. However, the consequence loop is also intended to assess whether banks who still operate in the traditional way have started to feel the consequences of their actions and thus more pressure to engage in a Triple-Bottom-line approach. This is not yet the case in the current setup.

This fits with the outcome of the case studies at Magnet Bank, GLS Bank and Banca Etica. These showed that the current market transformation is mainly focusing on a transformation from Phase 1 to Phase 2. Making sure the laggards feel the consequences is part of Phase 4 of Sustainable Market Transformation (see Figure 2 above). So, focused engagement on this system loop may be possible in a few years, but at present, it makes sense to focus on advocating for the adoption of the identified practices. For this, building alliances with other game changers is crucial for leveraging the direct and, in particular, the indirect impacts that values-based banks have. Alliances can shift these practices from a niche market towards the core financial market in a country.

Finally, the Alternative system loop (IV) addresses whether attractive alternatives are available for banks. If there were no values-based banks, it would be taken for granted that the regular way of banking is needed to survive. However, the very existence of the values-based banks proves this assumption to be wrong. Values-based banks have for many years showcased that transparent, sustainable and inclusive banking can also result in good returns on assets. Therefore, the practices of values-based banks challenge the common mindset in banking by showing that alternatives are available. Furthermore, by adopting some or all the practices identified, clear alternatives are provided to how banks can integrate an inclusive way of banking into the core of their business model.

CONCLUDING REMARKS

VALoRE offered an opportunity to identify the alternatives that values-based banks offer to the market, which enable sustainable outcomes. This synthesis report seeks to inspire market participants to reward the sustainable behaviours of values-based banks and create a sector strategy that goes beyond ESG. It highlights practices that together provide a future pathway for the banking industry.

The nine practices derived from the case studies of Magnet Bank, GLS Bank and Banca Etica conducted between 2020 and 2022 can together provide a future pathway for the banking industry.

Furthermore, just like Environmental, Social and Governance criteria, Risk Management is a gradual process that takes time for any organisation to mature in its practice. So is evolving into a values-based bank. Given the challenges posed by ESG, including adopting a new culture, and the additional time and resources (human and financial) needed, it would be best if these resources and efforts were able to deliver a world where finance is at the service of people and the planet from the start. Accordingly, the aim should be to integrate values-based informed practices and not only ESG ones.

These nine practices have a solid foundation at values-based banks because they are embedded in an organisational culture that embraces the key values-based banking principles of the GABV. It is because of that culture that values-based banks can ask different questions and develop the practices highlighted. Although it is known that the link between values and practice can also work the other way around, known as the crowding-in effect[21], by adopting these practices, regular banks can also learn over time to appreciate their value. In turn, this can result in the integration of similar values even though these banks were not created with these in mind.

To promote positive social and environmental change, the rules of the game need to change. This can be done by policy reform by governments, by adoption of the practices of the values-based banks by other banks or by a mix of the two. This last option is most valuable and realistic because the more banks adopt these practices, the more support there will be for policy reform. And, vice versa, the more policy reform is announced that reflects the practices of values-based banking, the more regular banks will be willing to adopt similar best practices and become values-based themselves.

21 Chevrollier, N., Zhang, J., Leeuwen, R., Nijhof, A. (2020). The predictive value of strategic orientation for ESG performance over time. *Corporate Governance: An International Review,* 20 (1), 123-142. doi:10.1108/CG-03-2019-0105.

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