The Meta-trend Stakeholder Profile

Impacts on the Finance and Banking Industry

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- Stakeholder engagement
- Meta-trend
- Finance
- Banking
- Climate change
- Freshwater access

The primary impact of meta-trends, such as climate change, for the finance industry, translates to investment, underwriting and the role of financing in the sustainability of communities and industries. The assessment of such investment risks and opportunities will depend on the engagement of an evolving profile of stakeholders in information-gathering and planning for the finance and banking industry.

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Meta-trends such as climate change and risks to freshwater access represent a unique kind of problem for the banking and finance industry. Though financiers and other industries may face risks to the physical assets of business such as the building structures or even workforce populations, the primary impact for the finance industry translates to investment, underwriting and the role of financing in the sustainability of communities and industries. The assessment of such investment risks and opportunities will depend on the engagement of an evolving profile of stakeholders in information-gathering and planning for the finance and banking industry.

The finance industry has long considered investors, customers and employees to be typical company stakeholders, but there has been wildly varied progress in broadening this definition and in including assessment of social and environmental meta-trends into banking practices. A number of banks are far ahead of the curve in terms of incorporating sustainability into their stakeholder engagement strategies, often with a particular regard for decreased freshwater access and climate change. For example, Citigroup is one of the founders of the Equator Principles, which are a set of voluntary guidelines that apply to project financing (Equator Principles Financial Institutions 2006: 1). Adopted by more than 40 banks worldwide within the first three years of formulation, these guidelines not only list environmental and social characteristics that make an investment preferable, but establish certain standards of impacts or special locations that make the project ineligible for funds. In order to establish and then follow the Equator Principles, participating banks consult with a variety of new stakeholders, including non-governmental organisations, public-sector and policy-making participants, indigenous populations in sample project areas and environmental groups and agencies. Other banks have taken the initiative to voluntarily reduce their own carbon footprint in response to global climate change or adopt other sustainable behaviours as a result of stakeholder pressure. A number of investment firms have begun to incorporate sustainability and responsible practices into their assessment systems or tracking, including Calvert, Domini Social Investment, Goldman Sachs and the Dow Jones Sustainability Indices (DJSI). These organisations typically develop a list or index of companies that exhibit ‘responsible practices’ in their environmental, social and ethical company behaviours.

Meta-trends, stakeholder engagement and the finance industry

For the finance industry, environmental meta-trends have the potential to broaden the definition of ‘high-risk’ investments and therefore significantly impact the types of projects and businesses a bank is willing to underwrite. Financing a water-intensive project in an area with decreasing access to freshwater is a risky investment that can become even more dangerous in cities or regions plagued by intense political disputes over water rights. Decreased access to freshwater is likely to prompt and increase strict regulatory environments which include more stringent effluent limitations for liquid wastes released into local waterways or difficulty in obtaining and maintaining water discharge permits. Inefficient irrigation practices or polluting fertiliser use for agricultural investments may also represent long-term regulatory or economic concerns and privatisation of water sources can have dramatically negative impacts on the sustainability and survival of whole communities.

Global climate change also fuels a broadening definition of 'high-risk' areas for project, business or building creation. BankTrack[1] estimates that as of 2007, about 20% of global GDP (gross domestic product) is affected by climatic events (Herz and Frijns 2007: 7). The impacts of climate change also cause population migration, which results in major market shifts. Large groups of people living in areas with increasing exposure to storms, floods, droughts and other severe weather may be forced (or may choose) to relocate to milder climates. Defaulting on mortgage loans increase in such locations, where individuals are more likely to have to permanently abandon their homes or other property.

On the opportunities side, financing businesses that use or invent sustainable technologies or processes represent high-yield investment opportunities in light of decreased freshwater access and global climate change. Companies that lower carbon or greenhouse gas emissions also have high ROI (return on investment) potential in that they end up facing fewer long-term regulatory costs and companies that innovate emissions-reducing technologies profit from the emerging market in carbon emissions offsets and exchanges.

The finance industry is in a position to help to create and direct trading systems and other market incentives for emission reduction. After the European Union implemented a system of tradable emission permits, Fortis developed carbon banking services for companies that had to deal with the resulting increase in liability and within the first two years of the programme Fortis gained over 150 carbon banking customers (2006: 24). Deutsche Bank is also participating in the European Carbon Emissions market by developing financial products based on emissions certificates that can be sold by emission-reducing companies or project managers as an extra source of revenue or funding (Hölz and Münch 2006: 12). BankTrack estimates that, by 2020, the global carbon market may be valued as high as US$250 billion (Herz and Frijns 2007: 7).

Banks must also consider potential new concerns of their traditional stakeholders. From a brand image point of view, customers may want to know that their banks, to which they often maintain a high degree of loyalty, are financing sustainable businesses and projects that are good for the Earth and society (Blodget 2007). In the finance industry, environmentally 'green' can go hand in hand with traditional green-coloured monetary profits. Stocks deemed 'sustainable' by Goldman Sachs outperformed Morgan Stanley Capital International World Index by 25% from 2005 to 2007 (Cui 2007). In an age of greater corporate transparency and increased sustainability reporting, customers are showing an increased preference for responsible investments (Herz and Frijns 2007: 7).

Conclusion

In order to effectively address and respond to emerging risks and opportunities, banks must consult with a broader range of stakeholders, including scientists, architects, engineers and urban planners who can help to identify risks and risk-trends affiliated with geographic-specific investments. Entrepreneurs and innovators can help to identify the newest technologies and trends in the sustainability realm, so that banks can better understand the language of growing markets. Feedback of government stakeholders is important in cities that have particularly strong regulatory and/or sustainability policies

1 BankTrack is a network of civil-society organisations and individuals tracking the social and environmental effects of the private financial sector's operations, including the business of commercial banks, investors, insurance companies and pension funds. From www.banktrack.org.

and in areas where limited water supplies are regionally managed. With the striking performance of 'responsible' investments today, the activities of the banking and finance industry can transformation the sustainability of whole industries in a rapidly changing world. The engagement of stakeholders to guide and assess future investments will translate into how well we all adapt to natural resource shortages, market potential in a world where carbon emissions are closely constrained, accommodate populations on the move and find ways to enable businesses to do well by doing good.

References

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