



Innovative Finance Inclusion

ETHICAL BANKING: A CASE OF IMPACT INVESTING

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Abstract

Ethical Banking is an original and scalable approach to impact investing in the banking sector. Launched in 2000 by the largest co-operative bank in South Tyrol, it provides an operational procedure to align the ESG impact objectives of depositors with the bank's lending activities, while also allowing (if desired by the bank) a discount on the interest rate charged to borrowers. By bridging the gap between ethically-conscious depositors and the funding needs to support sustainable initiatives, Ethical Banking's model channels funds effectively into six key impact themes, including bolstering fair trade initiatives in underprivileged regions of the world. This requires full transparency on the effective borrowers and the empowerment of depositors in their active role.

Ethical Banking is an example that can be replicated by other banks that wish to prioritize certain sustainable sectors within their loan portfolios and, at the same time, intercept those clients who want to play an active role towards sustainable transition. In this way, the goals and actions for sustainable development on a global scale can be accelerated, channeling more financial resources towards sustainable activities, taking them away from those that are being discontinued.

Keywords:

ESG, Ethical Banking, Sustainable Banking, Italy, Responsible Depositors, Fair Trade.



1 The Organization

Ethical Banking is an umbrella brand launched by the largest cooperative bank operating in South Tyrol of Italy. It represents an original and scalable approach of impact investing in banking activities, offering insights into the implementation of evolving ESG standards within the global financial market landscape.

Launched in the year 2000, Ethical Banking is headquartered at the Raiffeisen bank in Bozen and operates in close collaboration with an extensive network of within-region and nationwide partner banks. Since its inception, Ethical Banking has undergone steady development in terms of its operational scope, network of partners, funding collection and project disbursement. At present, its network comprises 23 partner¹ banks within the local region and four additional national partners² in Italy. The institution’s success lies in its ability to bridge the gap between the demand for impact investing through retail banking activities, driven by ethically-conscious and ecologically-minded depositors, and the financial needs of sustainable business or initiatives.

1.1 A financial product to bridge demand and supply

From a technical point of view, Ethical Banking is based on a retail funding instrument already available at the partner bank, either physical or online (e.g. savings book, term current account, time deposit, certificate of deposit), with the addition of a clause committing the bank to use the funds collected on specific sectors (sustainable in itself) or sustainable projects chosen by the depositor. In addition, the partner bank accepts to disclose the beneficiaries of the 'ethical banking loans', through the internet, thus creating an explicit link between the individual depositor and the borrower.

1.2 Commercial opportunities on the lending rate

In contrast to the typical objective of maximizing the bank’s profits, Ethical Banking prioritizes the provision of supportive interest loans for sustainable initiatives. The favourable credit rates offered by Ethical Banking are made possible due to the slimer profit margin expected by the operating bank (i.e. “impact first” approach) and a lowered yield rate on deposits, as per the preferences of the depositors, shifted to a lower loan rate charged on

¹ See Appendix

² namely EmilBanca in Bologna, Cassa Padana in Leno (Brescia), Cassa Rurale di Trento, and BCC Filottrano (Marche)



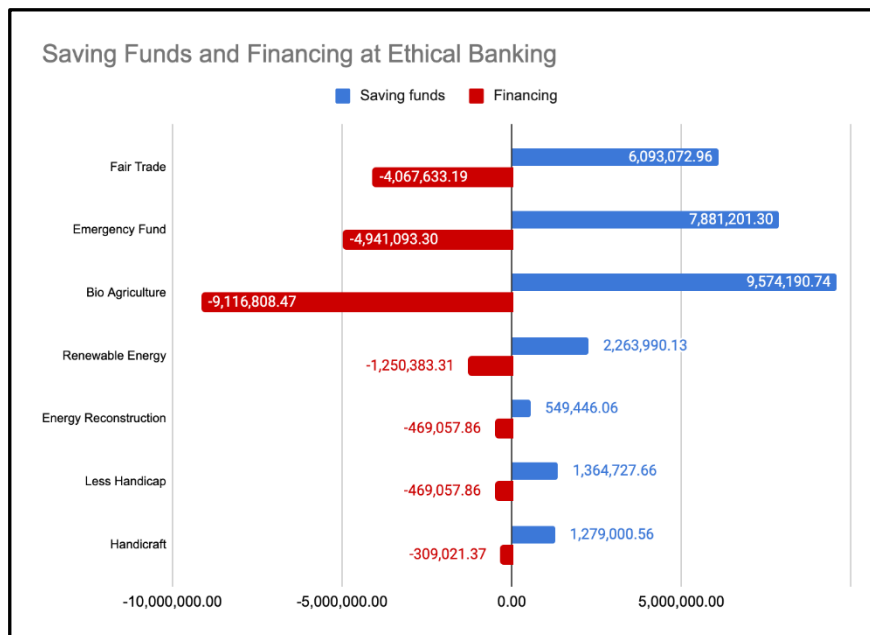


borrowers. This distinctive feature of allowing the bank’s depositors to shape interest rates highlights Ethical Banking’s commitment to advancing societal welfare and promoting the realization of sustainable development goals, rather than a pure profit generation.

2 Specific Area of Interest

At the core of Ethical Banking’s operational philosophy lies a commitment to the principle of solidarity, by setting links among people. Throughout their business, a cooperative bank is dedicated to facilitating flows of deposits into investment on citizens' initiatives, empowering the beneficiaries of funded projects to attain long-term self-help benefits. Simultaneously, the financial products offered by Ethical Banking enable savings capital to support sustainability goals and good causes, ensuring that the returns on investments attained by their individual clients extend beyond mere financial interests.

Depositors can choose to channel their capital into six diverse areas³: (1) Fair Trade, (2) Less Handicap⁴, (3) Organic agriculture, (4) Renewable Energy Production, (5) Energy Efficiency, and (6) Handicraft. The chart below illustrates a quick snapshot of capital flows achieved at Ethical Banking as of 31st December 2022.



Savings that are not yet allocated in target impact areas, are deposited in the Raiffeisen bank in Bozen.

³ Emergency funds for farmers are excluded.

⁴ It works with social associations improving the mobility and quality of life of individuals with disabilities.



2.1 Fair Trade

Notably, the area of Fair Trade stands among the main pillars of work at Ethical Banking, benefiting a great number of farmers and manufacturers in the Global South. Due to limited access to finance in developing countries of Africa, Latin America and Asia, there remains a significant need among farmers and workers in these regions in acquiring fair credits prior to every farming and manufacturing season. As of 31st December 2022, in the Fair Trade area solely, Ethical Banking has collected nearly 6.1 million Euros of funding from depositors and offered credits to the associations in the southern parts of the world at the interest rate of 1.120% in the first quarter of 2023.

In working closely with partners and direct beneficiaries, Ethical Banking guarantees the voice, the ownership and the working conditions of local farmers and workers in developing countries, strictly complied with the Fair Trade standards of the institution. Most importantly, in this area of Fair Trade initiatives, Ethical Banking facilitates the collaboration with the like-minded distribution network (i.e. Altromercato) whose physical stores and online shop are available all over the world. Through this strategic cooperation, the cooperative bank has financed over 70 agricultural and manufacturing projects in the Global South countries and guaranteed the Fair Trade products of funded projects the access to market and end-users.

3 Concluding Remarks

The two key features of this financial product are:

- 1) The deposit owners' right to select the funding areas and projects.
- 2) The bank's unwavering commitment to transparency

As the primary source of any banking investment activity, conscious depositors, or ethical investors, hold the power and the opportunity to selectively allocate their resources to fund sustainable projects according to their preferences. From a strategic point of view, a bank without ethical banking instruments exposes itself to the risk of loss of customers or direct deposits (on this basis, the 'stop the money pipeline' movement or similar in specific countries)⁵; on the other hand, it exposes itself to the risk of 'greenwashing' if it offers

⁵ <https://stopthemoneypipeline.com>



ethically oriented deposits products, but without the possibility of monitoring. Hence, the second necessary characteristic is:

As far as the commitment to transparency is concerned, Ethical Banking’s approach is founded on two pillars: i) quality in information and ii) reporting standards. The first objective is pursued by giving customers free access to the details of their finalized deposit, such as the location of the customer, its business and how the credit was used. The bank’s homepage serves as a gateway of information, regularly updated. In addition, a dedicated Youtube channel features short films documenting “real people” beyond “pure customers” (i.e. from quantitative to qualitative information) of Ethical Banking, fostering media exposure and public awareness.

Second, Ethical Banking assures transparency in its standards. The selection of benefited projects adheres rigorously to their environmental, social and ethical standards (national, European or international standards), and applied consistently. The institution also establishes mechanisms for periodic check-ups and control, safeguarding the best possible outcomes of funded projects.

In essence, Ethical Banking in its capacity as a cooperative bank plays a pivotal role in facilitating the efficient allocation of funds toward sustainable initiatives, thereby contributing to the promotion of impact investing practices and the advancement of sustainable development goals.

Actually, 'ethical banking' is an impact investing approach that can also be replicated by other ethical and sustainable banks that are not (yet) members of the network – or even any commercial bank. In this way, the goals and actions for sustainable development on a global scale can be accelerated, channeling more financial resources towards sustainable activities, taking them away from those that are being discontinued.





Appendix

3.1 Appendix1: List of partner banks in South Tyrol region, Italy

- 1 Raiffeisen bank Algund
- 2 Raiffeisen bank Bruneck
- 3 Raiffeisen bank Deutschnofen-Aldein
- 4 Raiffeisen bank Eisacktal
- 5 Raiffeisen bank Freienfeld
- 6 Raiffeisen bank Gröden
- 7 Raiffeisen bank Kastelruth - St.Ulrich
- 8 Raiffeisen bank Lana
- 9 Raiffeisen bank Latsch
- 10 Raiffeisen bank Meran
- 11 Raiffeisen bank Naturns
- 12 Raiffeisen bank Niederdorf
- 13 Raiffeisen bank Obervinschgau
- 14 Raiffeisen bank Passeier
- 15 Raiffeisen bank Prad-Taufers
- 16 Raiffeisen bank Salurn
- 17 Raiffeisen bank Schlern-Rosengarten
- 18 Raiffeisen bank Tauferer-Ahrntal
- 19 Raiffeisen bank Terlan
- 20 Raiffeisenkasse Überetsch
- 21 Raiffeisen bank Val Badia
- 22 Raiffeisen bank Welsberg-Gsies-Taisten
- 23 Raiffeisen bank Wipptal



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