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INTEGRATING ESG FACTORS INTO BANKING MANAGEMENT STRATEGIES

The specifics of modern banking business in Ukraine necessitate the incorporation of approaches to the consideration of environmental, social and governance risks into the bank management strategy, which is aimed at strengthening the overall level of financial stability of the banking system of Ukraine.

The paper considers the importance and prospects of integrating ESG factors into the banking management strategy. An important advantage of the considered components is the creation of competitive advantages for banks. This allows them not only to meet regulatory requirements, withstand external risks, retain customers, expand their market presence, increase the level of social responsibility of the banking business, form partnerships with international financial institutions and organizations and the goals set by, inter alia, the Paris Climate Agreement and the UN Sustainable Development Goals.

Integration of ESG factors helps to increase customer confidence, attract international investment, and ensure compliance with global requirements and long-term development.

Keywords: banking activities, risks, environmental factors, social factors, management factors, management strategies.

JEL classification: E52, G21

ІНТЕГРАЦІЯ ESG-ФАКТОРІВ У СТРАТЕГІЇ УПРАВЛІННЯ БАНКІВСЬКОЮ ДІЯЛЬНІСТЮ

Специфіка ведення сучасного банківського бізнесу України зумовлює врахування підходів та чинників, спрямованих посилити загальний рівень фінансової стабільності банківської системи України.

В роботі розглянуто значущість та перспективи інтеграції ESG-факторів у стратегії управління банківською діяльністю. Важливою перевагою розглянутих складових перевагою є створення конкурентних переваг банків. ESG-фактори, які формують новий підхід до ведення банківської діяльності, охоплюють три основні складові: екологічну, соціальну та управлінську. Їх інтеграція дозволяє банкам адаптуватися до сучасних викликів і сприяти стійкому розвитку економіки.

Екологічна складова (E) фокусується на питаннях захисту довкілля та адаптації до змін клімату. Банки активно інвестують у «зелені» проєкти, такі як розвиток відновлюваної енергетики, підтримують впровадження енергоефективних технологій та розробляють спеціальні фінансові продукти («зелені» кредити).

Соціальна складова (S) акцентує увагу на відповідальності банків перед суспільством. Інституції зосереджуються на створенні умов для фінансової інклюзії, забезпечуючи доступність банківських продуктів і послуг для малозабезпечених верств населення, людей із сільської місцевості та вразливих груп.

Управлінська складова (G) орієнтована на підвищення рівня прозорості та етичності банківських операцій. Банки впроваджують політику відкритості через публікацію фінансових звітів відповідно до міжнародних стандартів, забезпечують підзвітність клієнтам і акціонерам. Однією з ключових ініціатив є боротьба з корупцією, яка реалізується через впровадження антикорупційних політик та внутрішніх механізмів контролю.

Це дає змогу не лише відповідати регуляторним вимогам, протистояти зовнішнім ризикам, утримувати клієнтів, розширювати свою присутність на ринку, підвищувати рівень соціальної відповідальності банківського бізнесу, формувати партнерства з міжнародними фінансовими установами та організаціями. Інтеграція ESG-факторів дозволяє підвищити довіру клієнтів, залучити міжнародні інвестиції та забезпечити відповідність глобальним вимогам та розвиток у довгостроковій перспективі.

Keywords: банківська діяльність, ризики, екологічні фактори, соціальні фактори, управлінські фактори, стратегії управління.

Statement of the problem. Strengthening Ukraine's banking sector and developing its capital markets will be an integral part of postwar reconstruction and development. Very large amounts of domestic and external funds will need to be mobilized. This funding should be rapidly deployed to ensure overall financial and banking stability, which is significantly influenced by, among other things, ESG factors (E-environmental, S-social, G-governance). The financial potential and ability of banks to cope with them will ensure the continuity of business processes and adaptation to the ever-changing external and internal development conditions. Formation and implementation of the components of the post-war development strategies of the banking system with due regard to ESG factors can ensure balanced development of the banking institution, financing of environmental and social initiatives, as well as adequate response to changes in society, economy, and regulatory environment.

Analysis of recent research and publications. The mainstreaming of environmental and social development goals was initiated back in 2012 by the International Finance Corporation (IFC) with the development of the Sustainable Development Concept in terms of Performance Standards for environmental and social sustainability [1], aimed at identifying business risks and their consequences, as well as recommendations for their elimination (including stakeholder engagement and client disclosure obligations). In 2012, the United Nations adopted the UN 2030 Agenda for Sustainable Development [2]. In 2020, the European Parliament's Regulation on the establishment of a framework for the promotion of sustainable investment continued to shape the system of regulations on sustainable development risk management [3]. In 2021, European banking authority presented Report on management and supervision of ESG risks for credit institutions and investment firms [4], which provided common definitions of ESG risks, mechanisms, processes and strategies for banks and investment firms (institutions) to identify, assess and manage them, as well as recommendations on how ESG risks should be included in supervisory review and assessment by competent authorities. These regulations became the basis used by the National Bank of Ukraine to develop a document called "Policy on the Development of Sustainable Finance for the period up to 2025" [5], which defined that the policy goals are: to promote sustainable economic development of Ukraine; to promote environmental awareness and social responsibility in the financial sector of Ukraine; to promote compliance in the activities of financial institutions regulated by the National Bank of Ukraine with environmental goals, principles of sustainable economic activity and the principle of energy efficiency as a priority, defined in accordance with the European Green Pact; to promote the development of a closed-loop economy in Ukraine as a crucial factor in achieving climate change mitigation.

In 2022, the International Audit and Consulting Corporation (KPMG) devoted a substantial study "ESG Risks in the Banking Sector" to this issue [6], which addresses ESG factors and sustainability issues in the banking sector and identifies ways to integrate these aspects into the risk

management system and process.

The preliminary completion of the legislative range of regulations was the addition by the Committee of Sponsoring Organizations (COSO) and the World Business Council for Sustainable Development (WBCSD) to the universal guidance on managing risks that have a direct impact on the sustainable development of any organization, with a section on the impact of the institution's activities on the environment, social sphere and corporate governance [7, 8].

It should be noted that the issue of integrating ESG factors into banking management strategies has not been sufficiently researched in terms of forming an appropriate theoretical framework. Characterization of the practice and experience of applying ESG components as a basis for managing sustainability risks in banks is provided in the scientific works of Ukrainian scientists: Bortnikov G., Lyubich O. [9], Vovchenko O.V. [10], Zhytar M. [11], Petrenko V.S., Borovik L.V., Karnaushenko A.S. [12], Soloviy I.P., Panchyshyn Y.V. [13], Shulga N. and Omelenchuk V. [14].

The presented scientific papers systematize environmental, social and governance risks, confirm the importance of ESG approaches in the activities of banks, are quite systematic and comprehensive, but there are still a number of problems that require further research and development, in particular, in terms of justifying the need to consider them as new standards for conducting banking business with subsequent adaptation and integration into banking management strategies.

The objectives of the article are to study the significance and benefits of modern ESG trends in the activities of banks, to determine the consequences of their integration into banking activities, to analyze the benefits of analyzing their impact on financial stability and profitability, and to justify their necessity for the development of the modern banking system of Ukraine.

Summary of the main results of the study. The current banking business environment determines the key role of the ESG concept in shaping banks' business strategies. This allows not only to define the responsibility of banks to society and the environment, but also to directly influence their financial performance. Integration of ESG factors into the banks' business model strategy ensures long-term stability and competitiveness, and helps to avoid numerous risks.

The environmental component (E) focuses on reducing the negative impact of banks' and clients' activities on the environment. For example, banks finance renewable energy projects, refuse to support environmentally harmful industries, and introduce green lending policies.

In the social sphere (S), banks are actively working to create an inclusive environment, support human rights, and improve working conditions.

The governance component (G) involves transparency in decision-making, adherence to ethical standards, and the fight against corruption.

For banking, the integration of ESG factors is an important risk management tool. For example, investments in environmentally hazardous industries or cooperation with

socially irresponsible companies can lead to reputational and financial losses. On the other hand, banks that actively develop ESG activities gain competitive advantages, strengthen customer confidence and attract investors focused on sustainable development.

In the context of global financial and economic instability, banks face the need to adapt to new challenges, including climate change, social inequality, and increased regulatory requirements. For example, international standards, such as the UN Sustainable Development Goals, the Basel Accords and the European Union's initiatives, require active implementation of ESG standards in banking.

In Ukraine, the integration of ESG factors is becoming increasingly important for a number of reasons. First, it is an opportunity to attract international investment, as global investors are increasingly focused on sustainable financial practices. Secondly, adaptation to ESG standards helps to strengthen the competitiveness of Ukrainian banks in the international market. In addition, adherence to ESG principles allows banks to meet the expectations of society in terms of social responsibility and support for environmental initiatives.

Growing customer interest in green financial products also increases the relevance of integrating ESG factors. For example, environmental deposits or loans for energy efficiency projects are becoming increasingly popular among Ukrainian consumers. This opens up new opportunities for

banks to expand their product portfolios and strengthen customer relationships.

Thus, the integration of ESG factors into banking management strategies is not only a response to current challenges, but also a strategic necessity to ensure the sustainability, competitiveness, and reputation of banks as socially responsible financial institutions [10].

In partnership with the International Finance Corporation (IFC), the NBU is actively working to develop new standards for sustainable finance. The goal of this cooperation is to integrate environmental, social, and governance principles into the day-to-day operations of Ukrainian financial institutions. This process is part of the large-scale Sustainable Finance Development Project in Ukraine, which started in 2021 with the signing of the Cooperation Agreement on 04/16/2021. [15].

The regulatory landscape of the Ukrainian financial sector is undergoing significant changes. According to the updated NBU Policy until 2025 [5], starting in 2023, banks, and starting this year, non-bank financial institutions, will have to take into account environmental and social factors in their operations. This means that risk management becomes more comprehensive and responsible.

To understand the importance of implementing sustainable development goals as a priority in the management of banking activities, let's take a closer look at the components of ESG factors (Table 1).

Table 1

The essence of ESG factors and examples of their manifestation in banking activities

| Component | Characteristics | Examples of presentation |
|-----------------------------|---|---|
| Environmental component (E) | Includes issues related to climate change, resource use, waste management, carbon reduction and support for environmentally friendly technologies | - investments in green projects such as renewable energy; - financing energy efficiency initiatives; - introduction of green loans or bonds. |
| Social component (S) | Covers issues of human rights, social responsibility, gender equality, working conditions and community engagement | - development of financial inclusion programs; - support of local communities; - ensuring accessibility of banking products for vulnerable groups. |
| Governance component (G) | It deals with transparency, accountability, anti-corruption, ethical standards and corporate governance. | - ensuring openness of information for customers and shareholders; - implementation of anti-corruption policies; - responsibility for decision-making in crisis situations. |

Source: summarized by the author

ESG factors that form a new approach to banking include three main components: environmental, social and governance. Their integration allows banks to adapt to modern challenges and contribute to the sustainable development of the economy.

The environmental component (E) focuses on environmental protection and adaptation to climate change. Banks are actively investing in green projects, such as renewable energy development, supporting the introduction of energy-efficient technologies, and developing special financial products, including green loans. These measures help to reduce the carbon footprint and support environmentally responsible business.

The social pillar (S) emphasizes banks' responsibility to society. Institutions focus on creating conditions for financial inclusion by making banking products and services accessible to low-income populations, people from rural

areas, and vulnerable groups. Banks also support local communities by participating in social initiatives, financing infrastructure projects, and developing special programs. At the same time, they promote gender equality, ensure proper working conditions and encourage interaction with various social groups.

The governance component (G) is focused on increasing the level of transparency and ethics of banking operations. Banks implement an openness policy by publishing financial statements in accordance with international standards and ensuring accountability to customers and shareholders. One of the key initiatives is the fight against corruption, which is implemented through the introduction of anti-corruption policies and internal control mechanisms. Particular attention is paid to effective corporate governance and the development of risk management strategies that allow banks to remain resilient even in crisis

conditions [9].

Thus, ESG factors play an important role in banking activities by integrating the principles of environmental responsibility, social justice and good governance. They not only improve the reputation of banks but also form the basis for long-term economic development and financial stability in Ukraine.

The importance of ESG factors for banking in Ukraine is summarized in Fig. 1.

Summarizing the above in Fig. 1, it should be noted that

the integration of ESG factors into banking activities in Ukraine plays a key role in ensuring its adaptation to the modern requirements of society and the global financial space. One of the main benefits of such integration is strengthening the reputation of banking institutions and increasing customer confidence. Attention to the environmental, social and governance aspects of operations demonstrates banks' responsibility to society, which strengthens customer loyalty, attracts new service consumers and creates a positive image in the market.

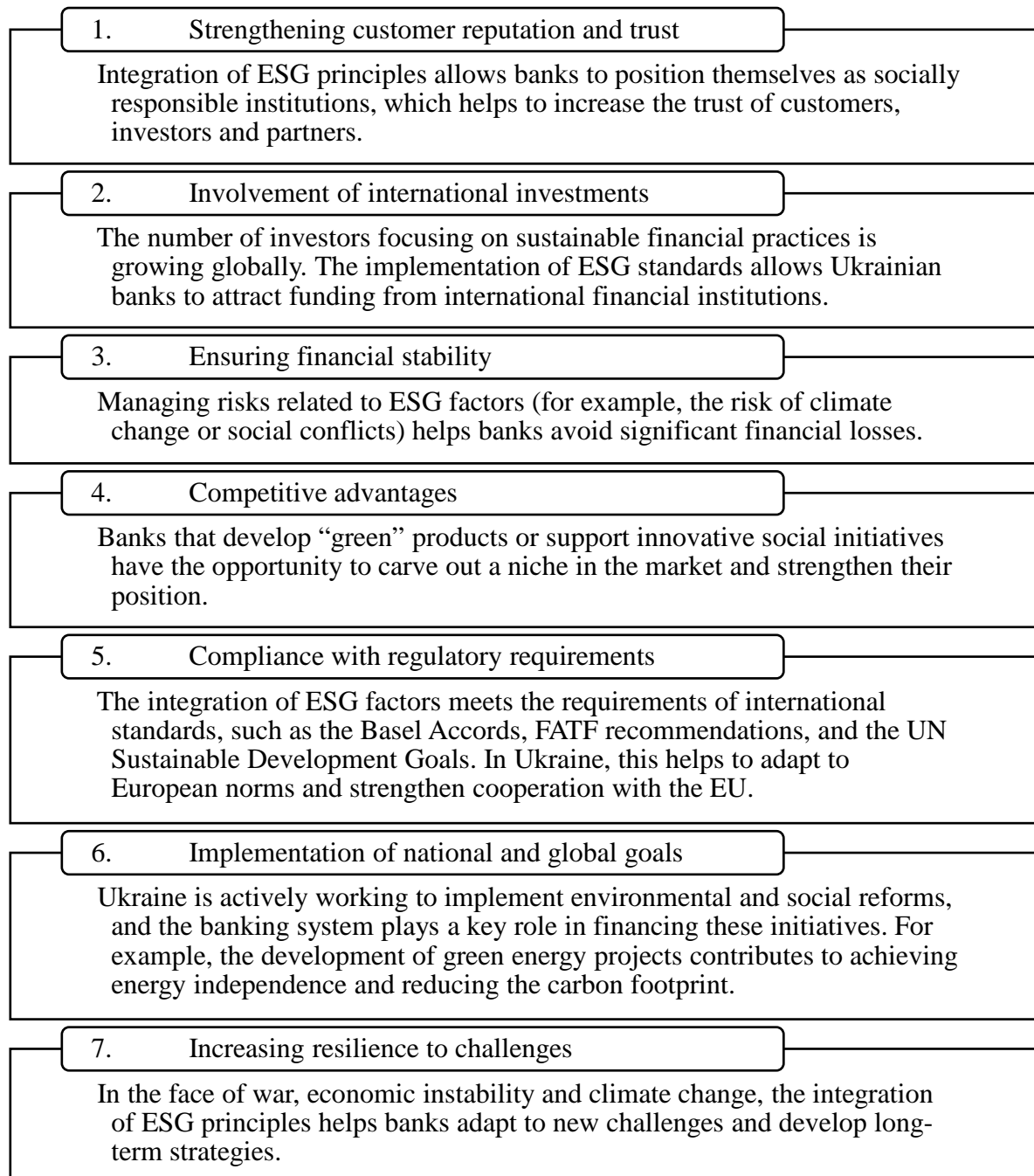


Figure 1. Importance of ESG factors for banking activities in Ukraine

Source: compiled by the author.

In addition, the implementation of ESG factors opens up access to international investment. Banks that actively

develop green projects and adhere to the principles of transparency and ethical management become attractive to

foreign investors who are focused on sustainable investments. This allows them to raise additional capital to finance projects that meet global sustainable development goals.

Ensuring financial stability is another important aspect of integrating ESG factors. Taking into account environmental and social risks in the bank's management strategy helps to reduce possible financial losses associated with crisis situations, such as environmental disasters or social conflicts. This helps to maintain the stability of the banking system even in difficult economic conditions.

Conclusions. An important advantage of implementing ESG factors is the creation of competitive advantages. Banks that actively implement innovative approaches to sustainable financing and social responsibility stand out among their competitors and hold leading positions in the market. This allows them not only to retain customers but also to form partnerships with other financial institutions and international organizations.

Integration of ESG factors also helps to ensure compliance with regulatory requirements. Modern requirements for transparency, accountability, and anti-money

laundering are becoming increasingly stringent, and compliance with these standards is a necessity for banks to operate in an international environment.

ESG-oriented banking also contributes to the realization of national and global sustainable development goals. Investing in green projects, supporting social initiatives, and fighting corruption help to achieve the goals set out in international agreements such as the Paris Climate Agreement or the UN Sustainable Development Goals.

Finally, taking into account ESG factors increases the banks' resilience to external challenges. In the face of economic instability, technological change, or environmental disasters, banks that implement sustainable management approaches are able to adapt to changes more quickly and ensure the continuity of their operations.

Thus, ESG factors are not just a trend, but a necessity for Ukraine's modern banking system. They create a solid foundation for sustainable development, financial stability and social responsibility, contributing to the successful integration of banks into the global economy. The integration of ESG factors into the management strategy forms the basis for the long-term success of the banking sector.

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