Deloitte.

How financial services can use ESG initiatives to help build a brighter future for all

Seeing the forest and the trees

A report from the Deloitte Center for Financial Services

Instead of operating with a silo-based ESG response, financial services leaders should find ways to engage in a broader approach to address important economic and societal developments.

Strong balance sheets and positive earnings forecasts are no longer enough for financial services organizations to attract investments, expand their business, and enhance their reputation. While these are important, stakeholders today are increasingly evaluating firms on an additional parameter: How seriously is the organization taking responsibility to address broader economic and societal challenges?

In the latest RepTrak Global 100 ranking of large company reputations, consumers cited environmental, social, and governance (ESG) considerations as an important factor that influences their willingness to do business with a company. It's worth noting that there were only two financial services brands among the top 100 in that study.[1] Indeed, concerns around a wide range of issues (COVID-19 and the impact it has had on vulnerable populations, heightened social unrest, climate change, and diversity and inclusion, among others) have pushed ESG topics up on the list of financial services organizations' strategic priorities. There is also heightened interest in these topics among US financial services regulators.[2] Add to these the United Nations, the European Commission, standard-setting bodies such as the Task Force on Climate-related Financial Disclosures, and independent firms such as Sustainalytics and MCSI, and it's easy to see why firms have increased their efforts around measuring and disclosing progress on ESG initiatives.

But how are industry participants viewing ESG? Because it's relatively new to financial services, it shouldn't be a surprise that ESG's definition is still evolving. Some equate it with sustainability, while others view it purely from the lens of ESG (or sustainable) investing.

Either way, financial services leaders are doing the important work to measure and accelerate efforts to get their stakeholders on board with their ESG strategy. Taking the next step, they should move beyond their current view of ESG and think strategically about how their companies can respond to it. To take either a narrower view or a more compliance- and reporting-focused approach is to risk missing the forest for the trees.

While different stakeholders are approaching ESG with varying levels of depth and industry focus, three aspects remain common: protecting the environment, promoting equity, and fostering trust and stability (see figure 1). And there's plenty of scope for financial services organizations to approach these areas by using innovative technology and exploring new partnerships to address major societal issues, make new markets, and generate profit in collaboration with multiple stakeholder communities while proactively rebuilding trust in institutions.

> "While each of our individual companies serves its own corporate purpose, we share a fundamental commitment to all of our stakeholders...We commit to deliver value to all of them, for the future success of our companies, our communities, and our country."[3]
>
> **Business Roundtable, "Statement on the Purpose of a Corporation"**

Figure 1. A distillation of ESG frameworks

Source: Deloitte Center for Financial Services analysis.

Opportunities to think about ESG as "jobs to be done"

Financial services firms have the opportunity to catalyze and accelerate the transition to an economy based on human-centric ecosystems while also tackling urgent societal challenges that demand new solutions.

The existing economic systems are full of vertically organized and often siloed industries, defined by the products they produce and the services they provide. The industrial classification system anchoring our present-day categorization and measurement of economic output exemplifies this producer-led economy.

These economic structures are giving way to a consumer-led economy in which capabilities are organized around core human needs and wants. Unlike the traditional industry value chain, where the customer sits at the end the B2B value chain, these new arrangements place customers in the very center of all commercial activity. Such partnerships, where a variety of actors across the private and public sectors compete and collaborate, offer the opportunity to deliver on human needs more directly and powerfully than ever before (figure 2).

Figure 2. New human-centric ecosystems

Transforming education and learning

Education and learning are increasingly critical to society, enterprises, and individuals and are being shaped by technological advancements, including VR, AR, AI, and affective computing.

Datafication and reinvention of health and wellness

The application of digital, bio- and nanotechnologies to health and wellness is generating more preventive, predictive, precise, and personalized outcomes.

Accelerating next-gen personal mobility

Technology is making transportation, including via automobiles and other forms of mobility, less congested and more efficient and sustainable.

Energy for the 21st century

New investments in electrification, renewables, and grid strengthening have the potential to transform energy production to meet increasing energy needs in more sustainable ways.

Growing societal challenges that remain resolutely unresolved also offer tremendous opportunities for the industry to play an impactful and profitable role (figure 3).

Figure 3. Growing societal challenges that demand new solutions

Climate adaptation and resilience

As human activity influences our climate in increasingly unpredictable ways, civic concern is intensifying, and responses are expected from a variety of stakeholders, including corporations.

Additive manufacturing

Global supply chains, despite being often costly and inefficient, can be sticky and difficult to change. However, geopolitical protectionism and climate change concerns are creating the conditions for advancements in additive manufacturing to serve as a less costly alternative.

Redefining the nature and role of work

Technology and automation are poised both to threaten work's societal role as the primary means of income and source of purpose and to enable new forms of collaboration and virtualization.

Reducing inequality

Intranational inequality has increased and is set to be compounded by conditions such as the rise of gig work and the elimination of considerable manual tasks.

Navigating potential future shocks

The road ahead may not be a smooth one. The industry will need to prepare for inevitable risks, or potential shocks, that loom large on the horizon (see figure 4). These shocks are not mutually exclusive, however; many of them may emerge over the coming decade, and the materialization of one may spur the development of others. This makes it all the more important for industry leaders to prepare for all of them.

Figure 4. Potential shocks over the next 10 years

Quantum breakthrough

Quantum computing has the potential to **render current encryption methods (including those protecting global financial markets) obsolete**

Experts predict a stable quantum processor **within the next 10 years**

Large-scale cyberattacks

Financial services is already **the most breached sector**[4]

State actors and hacker syndicates are deploying ever-more-sophisticated tools that **threaten to expose valuable data and destabilize critical networks and infrastructure**

Global depression

Sharp economic downturns or even depressions resulting from fiscal or monetary crises, trade shocks, or rising protectionism are poised to spread rapidly from one geography throughout the interconnected global economic and financial systems

Financial services players are highly integrated into and play crucial roles in these structures, meaning **they are poised to be agents, accelerants, or casualties** of such turmoil

Worsening climate situation

With the past 10 years the warmest on record, **the most severe economic, social, and environmental consequences appear to be ahead,** including more intense natural disasters, lower crop yields, and mass migration and resource conflict endangering markets

Insurers are already **struggling to respond to spiraling costs related to natural disasters**

Organic or synthetic biothreats

Outbreaks of pathogens (viral, bacterial, or otherwise) **threaten to destabilize communities and upend economic activity** via both demand- and supply-side shocks

Inability to quickly respond to such biothreats and keep them from multiplying risks affecting financial services providers by **reducing transaction volumes, increasing insurance risk, and immobilizing workforces**

(Geo)political discontinuity

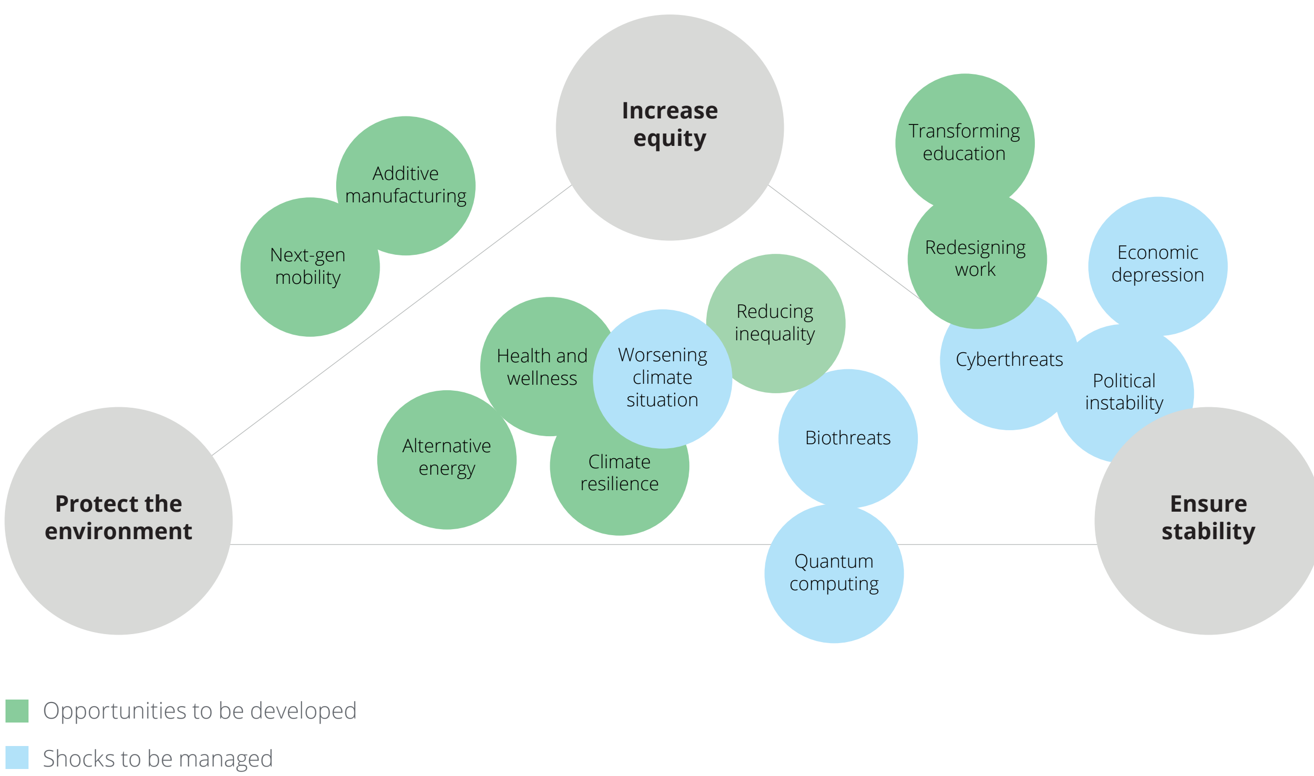
Geopolitical upheaval **jeopardizes free societies, civic coherence, and market-oriented rulesets** (including the free flows of trade, capital, and labor) upon which financial services players ground their strategies

Rising populism, nationalism, and authoritarianism threaten **abandonment of democratic institutions, governance models, and civic norms** and their replacement with less-liberal alternatives

Source: Deloitte Services LP.

Taken together, these opportunities and potential shocks present a daunting list. But they also connect to environmental, social, and governance challenges, which provides an opportunity to reframe the industry's approach to ESG. Instead of thinking of managing ESG in vertical silos (E, S, or G), leaders should shift to a multidimensional view to examine the risks and opportunities present in all three areas and across the broader jobs to be done (see figure 5). For example, addressing opportunities in next-gen mobility (through electric and shared or autonomous vehicles) can not only help address the issue of climate change, but also affect society more broadly by helping certain disadvantaged groups, such as those with mobility challenges or those who lack the financing to own their own vehicle, to experience greater opportunities to travel for work, shopping, or pleasure. Similarly, advances in quantum computing have the potential to increase cyber risk, impairing both society's and industry's ability to manage that risk. Also to be planned for is the environmental impact of the increased cooling that quantum computing may require.[5] Technological solutions—ones that the financial services industry could help fund—may be developed to address each of these challenges.

Figure 5. A multidimensional view of the opportunities and challenges across E, S, and G



Source: Deloitte Center for Financial Services analysis.

What are the tools needed to do the job?

Just as building a house requires more than a hammer, addressing the opportunities around transforming education (or managing the shock of another biothreat) requires a well-equipped tool belt, if not the whole toolbox.

In a recent publication on the future of financial services, we presented five fundamental roles that the financial services industry plays:[6]

- Facilitating value exchange and liquidity
- Providing a means for the secure storage of wealth
- Offering mechanisms for risk management
- Facilitating investment across multiple parties
- Maintaining trust and confidence to drive economic growth

We further posited that these roles should be, and are, evolving. For example, value exchange is being optimized (and friction reduced) through innovation in digital assets. Stores of value are similarly being enhanced through the development of automated savings and investment programs. Insurers are moving from managing risk to risk prevention and reduction, while advances in AI that allow for roboadvisers and online platforms for crowdsourcing provide expanded access to investments and advice. Coming full circle, the industry has an opportunity to not just maintain trust, but rebuild it.

So how should leaders think about using these tools for the actions they need to take? They can begin by applying the multidimensional view of ESG outlined above. For example, addressing the challenges of health involves not only the development of products and services to make health care more affordable, but also financing green energy to reduce the effects of air pollution, which disproportionately affects people of color.[7] It also involves ensuring that sensitive health and financial data is securely and ethically managed. Therefore, when contemplating how to participate in health transformation, leaders should think of ways to use the tools available (payment products, capital allocation, and cyber and data risk management) across all three areas of E, S, and G (see figure 6).

Similarly leaders can use some of the same tools to position their firms to take a stronger stand on reducing inequality. Real estate property developers, owners, and financers (including investment and banking firms) can think about developing low-income housing with sufficient public green space; bankers and wealth management firms can develop mobile-first products that bring more un- or underfinanced individuals into the system; and all types of organizations can take steps to ensure greater diversity in leadership, suppliers, and third-party relationships.

Figure 6. Leaders should think of ways to use tools across all three areas of E, S, and G

Opportunity	Environmental	Social	Governance
Education		Municipal financing Higher ed funding schemes	Worker retraining Apprenticeship programs
Health	Financing fossil fuel reduction	Affordable health solutions Data privacy and security	Ethical data management
Mobility	Investing in last-mile distribution	Mixed-use development	Autonomous risk management
Energy	Financing renewable energy	Carbon trading to lower energy cost	Procurement and consumption LEED certification
Climate	Green capital formation	Infrastructure hardening	Physical and transitional risk management Creating consistent disclosure data
Additive manufacturing		Financing reshoring and additive manufacturing	Third-party risk management
Future of work	Funding career transition from carbon-based industries	Managing workforce transitions Gig worker finance products	Labor relations Pay equity Worker retraining
Inequality	Property development financing, including public green space	Financial inclusion Affordable housing funding	Leadership and board DEI Supplier diversity

Optimize value exchange · Enhance wealth building · Reduce and prevent risk · Expand investments · Rebuild trust and confidence

Source: Deloitte Center for Financial Services analysis.

This cross-pillar view of opportunities can also be useful in assessing potential risks. Advances in quantum computing, as mentioned earlier, can assist in the development of insurance risk models that enable the creation of new methods to combat climate change. This can also, however, render current encryption techniques obsolete, increasing the potential for large-scale cyberattacks.

Each potential shock carries with it certain implications, some of which are presented in figure 7. For example, climate change may lead to increased natural disasters and loss of biodiversity; food and water shortages, resulting in refugee migration;[8] and operational and financial disruption of the industry and society as a whole. Similarly, a global depression and political instability could each have implications for the industry's ability to fund green capital and investing, as well as potential heightened financial hardship and civil unrest arising from voter disenfranchisement.

Here, too, industry leaders could consider preparing their companies to take action should any of these developments come to pass. Certainly, the industry is in a constant race to develop stronger cyber risk management capabilities, but with efforts to catalyze new cross-industry businesses to serve emerging demands, these skills could play a broader role in protecting all forms of data at the core of these businesses and across industries. As we have seen with the current pandemic, the industry stepped up to support the economy and society in a variety of ways[9] through collaboration with governments and central banks. These lessons learned can be applied to a number of these potential shocks, and industry leadership could take steps to consider how these programs worked well (or didn't) to prepare for potential future use. A broader view of potential partners may also benefit firms as they navigate this increased focus on business practices that are more supportive of broader societal goals.

Figure 7. Potential future shocks, their possible implications, and actions to consider

Potential future shock	Possible implications	Financial services actions to consider
Quantum breakthrough	Potential increased energy usage Privacy and security threats Ethical uses of AI Operational and financial disruption	Fund energy-efficient quantum technology Develop stronger cyber risk management across industries Champion ethical use of AI
Large-scale cyberattacks	Threats to energy, water, and industrial systems Privacy and security threats Business interruption Operational and financial disruption	Develop stronger cyber risk management across industries Champion ethical use of AI Invest in and develop enhanced cyberinsurance coverage
Worsening climate situation	Natural disasters and biodiversity loss Food and water shortages Increased refugee activity Operational and financial disruption	Develop green capital, investing in and developing products and strategies Collaborate with governments to support economic stimulus Support worker retraining to manage transitions Adjust risk models and portfolios
Organic and synthetic biothreats	Increased biomedical and household waste Financial hardships (debt servicing, business failure) Operational and financial disruption	Collaborate with governments to support economic stimulus Enhance management of liquidity and volatility pressures
Global depression	Deemphasis on green capital and investing Financial hardship (debt servicing, business failure) Operational and financial disruption	Invest in recession-proof sectors Support worker retraining to manage transitions Enhance management of liquidity and volatility pressures
Political instability	Deemphasis on green capital and funding Voter disenfranchisement Economic slowdown due to trade interruptions	Adjust global risk and portfolio models Focus on ethical decision-making to emphasize trust

Source: Deloitte Center for Financial Services analysis.

Leading the way forward

The financial services industry is expected to continue to be indispensable to the economy and society. It's off to a good start, with work now being done to assess, measure, and report on ESG goals. But the demands and expectations being placed on the industry (indeed, on all industries) suggest that doing nothing is not a winning strategy. Neither is limiting efforts to measuring and reporting; the problems to be solved demand a more nuanced view: one that offers leaders the opportunity both to share progress and to lead in the effort to create a more human-centric economy and society.

But financial services can't do it alone. For society to address any of these potential future challenges, industry participants must not only perform their amplified roles, but also act as leaders, collaborating with policymakers, civil society organizations, tech companies, logistics providers, manufacturers, and various other public and private actors across the economy. By combining their strengths, these actors can, together, help to usher in a brighter future.

Endnotes

1. RepTrak, 2021 Global RepTrak 100, 2021.
2. John Coates, "ESG disclosures – keeping pace with developments affecting investors, public companies and the capital markets," US Securities and Exchange Commission, March 11, 2021.
3. Business Roundtable, "Statement on the Purpose of a Corporation," August 19, 2019.
4. *Forbes Insights*, "What Financial Services Executives Need to Know About Data Security," January 15, 2019.
5. Jeremy Hsu, "How much power will quantum computing need?" IEEE Spectrum, October 5, 2015.
6. Monica O'Reilly, Dounia Senawi, Jim Eckenrode, and Eamonn Kelly, *A higher bottom line: The future of financial services*, Deloitte, March 2021.
7. Robin Lloyd, "People of color breathe more unhealthy air from nearly all polluting sources," *Scientific American*, April 28, 2021.
8. John Podesta, "The climate crisis, migration, and refugees," Brookings Institute, July 25, 2019.
9. Governor Michelle Bowman, "Community banks rise to the challenge," remarks at the St. Louis Federal Reserve Bank "Community Banking in the 21st Century" research conference, September 30, 2020.

Contacts

Monica O'Reilly
Vice chair
US Financial Services
Industry leader
Deloitte LLP
+1 415 309 7544
monoreilly@deloitte.com

Jim Eckenrode
Managing director
Deloitte Center for
Financial Services
Deloitte Services LP
+1 617 585 4877
jeckenrode@deloitte.com

Acknowledgements

The authors wish to thank their colleagues, Eamonn Kelly from the Deloitte Office for the Future; Jennifer Steinmann, Global ESG Marketplace leader, Shannon Kroll, Global ESG Marketplace senior manager; Hans-Juergen Walter, Global Sustainability leader for Financial Services; Michele Crish, Courtney Davis, Ricardo Martinez, and Peter Phelan from Deloitte & Touche LLP.

Deloitte.

About the Deloitte Center for Financial Services
The Deloitte Center for Financial Services, which supports the organization's US Financial Services practice, provides insight and research to assist senior-level decision-makers within banks, capital markets firms, investment managers, insurance carriers, and real estate organizations. The center is staffed by a group of professionals with a wide array of in-depth industry experiences, as well as cutting-edge research and analytical skills. Through our research, roundtables, and other forms of engagement, we seek to be a trusted source for relevant, timely, and reliable insights. Read recent publications and learn more about the center on deloitte.com.

About this publication
This publication contains general information only and Deloitte is not, by means of this publication, rendering accounting, business, financial, investment, legal, tax, or other professional advice or services. This publication is not a substitute for such professional advice or services, nor should it be used as a basis for any decision or action that may affect your business. Before making any decision or taking any action that may affect your business, you should consult a qualified professional adviser.

Deloitte shall not be responsible for any loss sustained by any person who relies on this publication.

About Deloitte
Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee ("DTTL"), its network of member firms, and their related entities. DTTL and each of its member firms are legally separate and independent entities. DTTL (also referred to as "Deloitte Global") does not provide services to clients. In the United States, Deloitte refers to one or more of the US member firms of DTTL, their related entities that operate using the "Deloitte" name in the United States, and their respective affiliates. Certain services may not be available to attest clients under the rules and regulations of public accounting. Please see www.deloitte.com/about to learn more about our global network of member firms.