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# Ethics in finance: the post crisis challenge

**Dublin meeting | Fondazione Centessimus Annus**

October 24<sup>th</sup>, 2014 | José Manuel González-Páramo; BBVA Board



“We are what we repeatedly do. Excellence, therefore, is not an act, but a habit”.  
Aristotle



# Index

1. **Introduction: past, present and future**
2. The post crisis challenge
3. Conclusions

# The financial industry has lost its reputation

Past

But NOT all banks did the same

Regulatory failures

Malpractices

Weak supervision and lack of resilient balance sheets

Weak corporate governance, benchmarking ...

Present

Regulation & Supervision

Malpractices

Much progress. Almost finished

Increasingly important issue for institutions & authorities

Future

Banks at center of society

Professional competence and ethics

Supervisors & Boards Interaction

Prudent risk management

international cooperation

Enforcement systems

Transforming assertions to action is a must: ethical principles and share values cannot be “only words”

# Ethics goes beyond regulation

## The board and the management

**Are the first responsible for Ethics:** they have to fully assume their responsibilities and promote values and ethics from the top, leading by example.

## Regulation and supervision

**Are only complements:** Regulators and supervisors are there to safeguard that the Board and the management follow the right path.

A more ethical banking with the highest standards would have avoided many of the excesses committed before the last crisis



# Index

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2. **The post crisis challenge**
3. Conclusions

# Be ethical even when nobody watches you



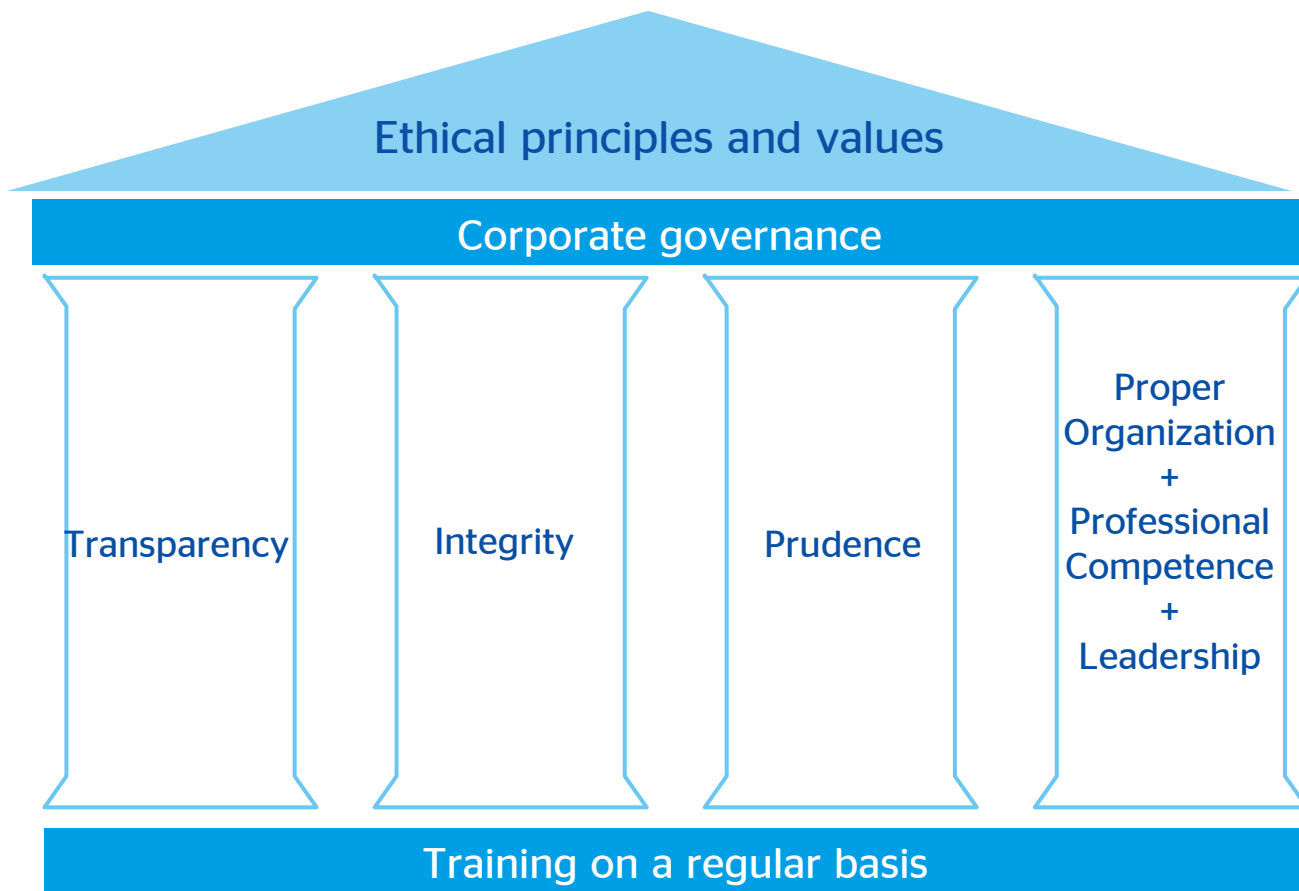
## Typical self justification to break moral: Plenty of excuses.

Everybody does it (**herd behaviour**), we have always done it, if I don't do it, someone else will do it..

## Before acting we have to consider:

- **“What would my internal Jiminy Cricket or my mother would say to me?** (or whoever I respect)”.C. Lagarde; IMF Oct'14
- **“Would you behave the same if your actions were public?”** “we suppose ourselves the spectators of our own behavior”. The “impartial spectator” (Adam Smith). I. Angeloni; ECB Sept14

# Business must be responsible and lead by example



Ensuring proper conduct by participants in innumerable situations not covered by law

Entities have to commit publicly to Ethics and values. Those should be binding from the top.

Responsible Banking is a transversal function that should involve the whole strategy & all people in the organization

Corporate Governance should reach the right balance stakeholders & shareholders' utility. It is not an easy task.

Sound ethical values is essential especially for an industry (finance and banking) which business relies on trust. Trust is hard to achieve but easy to lose



# A new paradigm for entities: Main drivers

## 1. Transparency

- **Open, timely and clear communication and information** to public

## 2. Integrity

- **Avoid the tick in the box philosophy.** Managers have to do the right thing in any circumstance & avoid using loopholes to circumvent the law. Managers must have **values** not just be concerned about regulation.

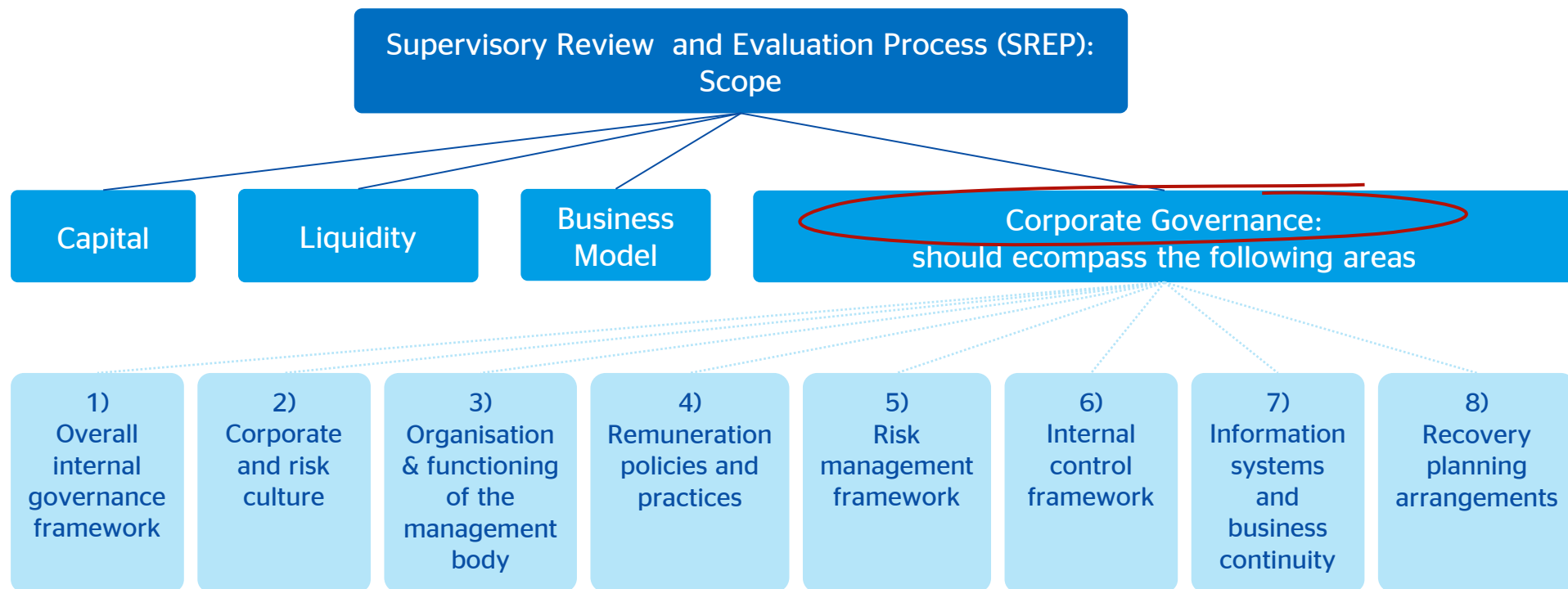
## 3. Prudence

- **Responsible Banking-needs an adequate risk culture and management:** the enhancement of the risk-appetite framework (governance of risk decision making) will make a difference

## 4. Corporate Governance

- It has to go further than internal controls and compliance, its ultimate goal must be **ensuring an optimum conduct.** It is one of the four pillars of the SREP\*.
- Ensuring **high skills of the board and the senior management. Avoiding conflicts of interests.**
- **Independence of the Board:** An ample majority of Independent Board members supported by a minority of executives with deep knowledge of the group.
- **Compensation scheme: Aligning incentives** to avoid excessive risk-taking

# Corporate governance and SREP



Competent authorities will evaluate the risk of prudential impact posed by poor governance and control arrangements and their effect on the viability of the institution

# A new paradigm for entities: Effects on the industry

## Diversity

- Promoting a **wider range of firms and business models**

## People

- **A customer-centric culture**
- **Responsible creation of value**
- **Competition on clients' satisfaction**, as clients are "entities' ambassadors"

## Society

- Financial industry function is **to help companies & people to implement their projects.**
- Banks are fundamental to **social welfare & development**

Other global banking impacts on society: Wealth generation (through payment of taxes and job creation) and social progress (via financial inclusion & financial literacy commitment and investment in social programs)



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# Putting the skin in the game

- 1 **Ethical principles and share values cannot be “only words”**
- 2 **Mutual trust, transparency, clear communication of our commitments and cooperation** are key variables
- 3 **Banks must be responsible and lead by example** as they play a key role to society
- 4 **More principles and more ethics are required** as they guarantee a proper conduct in situations not covered by law or not regulated
- 5 **An ethical banking model does not reduce profitability** as it is an investment in clients' confidence
- 6 **“Being profitable does not mean doing business at any price”:** Profitability adjusted to principles should become a key variable



Thank you for your attention!

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