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OF FINANCIAL TRANSFORMATION

GOVERNANCE OF SUSTAINABILITY

How financial sector leadership shapes sustainable finance as a transformative opportunity: The case of the Swiss Stewardship Code

AURÉLIA FÄH

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DEAR READER,

In my new role as CEO of Capco, I am very pleased to welcome you to the latest edition of the Capco Journal, titled **Balancing Innovation and Control**.

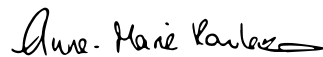
The financial services and energy sectors are poised for another transformative year. At Capco, we recognize that this is a new era where innovation, expertise, adaptability, and speed of execution will be valued as never before.

Success will be determined based on exceptional strategic thinking, and the ability to leverage innovative new technology, including GenAI, while balancing a laser focus on risk and resilience. Leaders across the financial services and energy industries recognize the transformative benefits of strong governance while needing to find the optimal balance between innovation and control.

This edition of the Capco Journal thus examines the critical role of balancing innovation and control in technology, with a particular focus on data, AI, and sustainability, with wider corporate governance considerations. As always, our authors include leading academics, senior financial services executives, and Capco's own subject matter experts.

I hope that you will find the articles in this edition truly thought provoking, and that our contributors' insights prove valuable, as you consider your institution's future approach to managing innovation in a controlled environment.

My thanks and appreciation to our contributors and our readers.

A handwritten signature in black ink that reads "Annie Rowland". The signature is fluid and cursive, with a long horizontal stroke at the end.

Annie Rowland, **Capco CEO**

HOW FINANCIAL SECTOR LEADERSHIP SHAPES SUSTAINABLE FINANCE AS A TRANSFORMATIVE OPPORTUNITY: THE CASE OF THE SWISS STEWARDSHIP CODE

AURÉLIA FÄH | Senior Sustainability Expert, Asset Management Association Switzerland (AMAS)

ABSTRACT

This article explores the pivotal role that financial services play in advancing sustainable finance, with a focus on the Swiss Stewardship Code published in October 2023 as a case study. It highlights the financial services sector's inherent bias toward recognizing and capitalizing on the transformative opportunities presented by sustainable finance, emphasizing long-term value creation, risk management, and innovation. It contrasts market-based and regulatory approaches to sustainability, showing Switzerland's preference for market- and principle-based approaches. The Swiss Stewardship Code, developed by the Asset Management Association of Switzerland and Swiss Sustainable Finance, is presented as a model for effective stewardship in sustainable investing. The article argues that this approach, emphasizing collaboration, innovation, and a proactive stance towards sustainability, not only combats greenwashing but also aligns financial flows with sustainability goals, underscoring the financial services sector's critical role in driving sustainable economic, social, and environmental outcomes.

1. INTRODUCTION

In recent years, sustainable finance has evolved from a niche field to a critical component of a broader strategy to transition towards a more sustainable economy and to align global financial flows with sustainability goals. Such ambitious objectives require the collaboration of all key stakeholders, ranging from corporates, financial players, consumers, and policymakers. Market-based approaches have historically been critical in shaping sustainable finance practices over the past decades. More recently, regulatory initiatives have flourished around the world to create the framework and the conditions for the integration of environmental, social, and governance (ESG) factors into financial services. Depending on the jurisdictions, they mostly limit themselves to the prevention

of the risks associated with the negative aspects of sustainable finance, including greenwashing. On the other hand, market-based initiatives often focus on the transformative potential and opportunity associated with sustainability.

Switzerland follows a market- and principle-based approach. The recent publication of the Swiss Stewardship Code in October 2023 by industry associations demonstrates the ambition of the financial services sector to keep leading the way and creates the necessary standards placing sustainability as an opportunity for the Swiss financial industry.

This article seeks to explore how financial sector leadership advances the transformative opportunity of sustainable finance by diving into the recent introduction of the Swiss Stewardship Code.

2. SEIZING THE TRANSFORMATIVE OPPORTUNITY OF SUSTAINABLE FINANCE

When it comes to seizing the transformative opportunity of sustainable finance, the financial services sector proves to be better equipped than other relevant stakeholders.

2.1. Financial services sector's bias toward positive and long-term value creation

The financial services sector possesses an inherent bias towards recognizing and capitalizing on the transformative opportunities presented by sustainable finance. This bias stems from several factors:

- **Risk management perspective:** financial institutions recognize the materiality of ESG factors in assessing risk. As sustainability issues such as climate change, resource scarcity, and social inequality become more prominent, financial institutions understand that integrating ESG considerations into their decision-making processes is essential for long-term risk management and value preservation.
- **Long-term value creation:** sustainable finance offers opportunities for long-term value creation and resilience. Investments in sustainable projects and businesses not only generate financial returns but also contribute to environmental protection, social development, and economic growth. Financial institutions that prioritize sustainability are well-positioned to create lasting value for their stakeholders and society as a whole.
- **Client demand and investor preferences:** there is a growing demand from clients and investors for sustainable finance products and services. As awareness of sustainability issues increases, individuals and institutions are seeking investment opportunities that align with their values and contribute to positive environmental and social outcomes. Financial institutions are responding to this demand by offering a wide range of sustainable investment options, thereby capitalizing on the transformative opportunity presented by sustainable finance.
- **Market opportunities:** the transition to a sustainable economy presents significant market opportunities for financial institutions. Investments in renewable energy, clean technology, sustainable infrastructure, and other environmentally and socially responsible sectors offer the potential for attractive returns while also addressing

pressing sustainability challenges. Recognizing these opportunities, financial institutions are increasingly allocating capital towards sustainable finance initiatives to capture market share and drive innovation.

- **Financial innovation:** sustainable finance drives financial innovation by creating new investment opportunities, products, and services that integrate ESG considerations. Innovations, such as green bonds, impact investing, and sustainability-linked loans, mobilize capital towards sustainable projects and businesses, unlocking new sources of financing and stimulating economic growth.
- **Reputational and brand considerations:** financial institutions recognize the importance of sustainability in building and maintaining their reputation and brand value. Embracing sustainable finance practices enhances their credibility, attracts clients and investors, and strengthens relationships with stakeholders. By demonstrating a commitment to sustainability, financial institutions can differentiate themselves in the market and gain a competitive advantage.

2.2. Policymakers' inherent focus on risk mitigation and investor protection

Policymakers are primarily focused on addressing the negative consequences of sustainable finance, such as greenwashing, for several reasons:

- **Risk mitigation:** regulators have a responsibility to protect investors and consumers from misleading or deceptive practices, including greenwashing. By focusing on the negative aspects of sustainable finance, regulators aim to mitigate the risks associated with false or exaggerated claims of environmental or social responsibility.
- **Market integrity:** ensuring market integrity is essential for maintaining trust and confidence in the financial system. Regulators seek to prevent greenwashing to safeguard the integrity of sustainable finance markets and prevent market manipulation or fraud that could undermine investor confidence and market stability.
- **Investor protection:** regulators prioritize investor protection by requiring transparency and disclosure of material information related to ESG factors. By addressing greenwashing and ensuring accurate and reliable information, regulators aim to empower investors to make informed decisions and protect them from potential harm or financial losses.

- **Regulatory compliance:** regulators enforce laws and regulations related to sustainable finance to ensure compliance with legal standards and prevent violations of consumer protection and securities laws. Focusing on the negative aspects, such as greenwashing, helps regulators identify and address instances of non-compliance and hold financial institutions accountable for their actions.
- **Market stability:** greenwashing and other misleading practices in sustainable finance can create market distortions and undermine the efficient allocation of capital. Regulators aim to maintain market stability by addressing greenwashing and promoting transparency, integrity, and accountability in sustainable finance markets.
- **Public trust and confidence:** governments and regulators recognize the importance of public trust and confidence in the financial system. Addressing greenwashing and promoting integrity in sustainable finance markets are essential for maintaining public trust and confidence in the credibility and effectiveness of sustainability initiatives.

Overall, regulators and governments tend to address the mitigation of the negative aspects of sustainable finance, such as greenwashing, to protect investors, maintain market integrity, ensure regulatory compliance, promote market stability, uphold public trust, and advance long-term sustainability goals. By addressing greenwashing and other misleading practices, regulators aim to foster a more transparent, responsible, and effective sustainable financial industry that delivers positive environmental, social, and economic impact.

The financial services sector is, on the other hand, strongly equipped to seize the transformative opportunity of sustainable finance because of its agility, innovation capacity, and direct influence on investment flows. Financial institutions can quickly adapt to market trends, integrate ESG criteria into their investment decisions, and develop new financial products that support sustainable development goals. This agility allows the financial services sector to respond promptly to investor demands for sustainable options, driving change efficiently and effectively across economies.

The prominence of the financial services sector in embracing sustainable finance as an opportunity for the financial industry proved particularly true in the Swiss context.

3. THE PIVOTAL ROLE OF THE FINANCIAL SERVICES SECTOR IN ADVANCING SUSTAINABLE FINANCE PRACTICES IN SWITZERLAND

In Switzerland, the financial services sector has been playing a critical role in shaping and advancing sustainable finance practices. Through a combination of self-regulatory initiatives and private-led best practices, such market-driven approaches offer an effective and ambitious alternative to fully-fledged regulatory approaches undertaken by similar jurisdictions such as the E.U.

3.1. Rationale for a private sector-led approach in Switzerland

By way of background, Switzerland is particularly favorable to a **market-based approach**. Such an approach is rooted in the country's political and economic history, as well as its commitment to principles such as liberalism, free enterprise, economic freedom, and individual responsibility. By fostering a dynamic and competitive market environment, Switzerland aims to promote innovation, growth, and prosperity while maintaining social cohesion and environmental sustainability.

Additionally, the **subsidiarity principle** is a guiding concept in Swiss governance, emphasizing that decisions should be made at the most immediate or local level, only involving higher levels of government if necessary. This principle supports a market-based approach to the economy, where the market and private entities play a significant role in economic activities, and government intervention is minimized.

3.2. The role of self-regulations

In Switzerland, self-regulation in finance is a significant component of the regulatory framework, complementing formal legislation and oversight by regulatory authorities. Financial institutions and industry associations are deemed most appropriate to develop and enforce their own sets of rules and standards to promote ethical behavior, transparency, and efficiency within the market. These self-regulatory organizations cover all financial services sectors, including banking, asset management, and insurance, aiming to uphold the integrity and stability of Switzerland's financial system while fostering innovation and competitiveness. The Swiss Financial Market Supervisory Authority (FINMA) supports this model and recognizes three types of self-regulation: voluntary self-regulation, self-regulation recognized as a minimum

standard, and compulsory self-regulation. This framework enables the financial services sector to develop standards in close collaboration with experts, ensuring market relevance and broad acceptance. Self-regulation is instrumental in complementing and detailing key areas of state regulation, with FINMA having the authority to recognize and enforce self-regulatory guidelines as minimum standards. This ensures that not only members of self-regulatory organizations but also other sector participants adhere to these guidelines.

When it comes to sustainability, financial industry associations have developed their self-regulations over the past two to three years:

- The **Asset Management Association of Switzerland (AMAS)** has developed a principle-based self-regulation for sustainable asset management released in September 2022 and effective since September 2023. Its framework for sustainable asset management lays down the organizational requirements for financial institutions, as well as for product design and disclosures to investors, to prevent and combat greenwashing by enhancing the quality of collectively managed sustainable assets through binding standards, while improving transparency through comprehensive documentation and reporting obligations. With its explicit references to both institutional and product levels, the AMAS self-regulation dovetails with the self-regulation process of client advisory that the Swiss Bankers Association has introduced.
- The **Swiss Bankers Association (SBA)** elaborated a principle-based self-regulation for the providers of financial services on the integration of ESG preferences and ESG risks into investment advice, portfolio management, and mortgage advice, which was first published in June 2022 and is effective since January 2023.
- The **Swiss Association of Pension Funds (ASIP)** published in December 2022 a standard for ESG reporting for Swiss Pension funds that came into force in the financial year 2023.
- As we write, the **Swiss Insurance Association (SIA)** is working with its members to elaborate a self-regulation to be published in the coming months.

The elaboration of self-regulation is conducted through the effective collaboration of financial stakeholders and led by their respective industry associations. Sustainable finance-

related self-regulations in Switzerland support the objectives of the Swiss authorities and their sustainable finance strategy. In particular, the Federal Council published in December 2022 a position focusing on the prevention of greenwashing, which aligns with the objectives advanced by the industry self-regulations. With self-regulations already published, the financial industry proactively took the necessary steps on its own to prevent greenwashing, foster transparency, and safeguard the credibility of the Swiss financial center.

3.3. The importance of other private-led initiatives

Beyond self-regulatory mechanisms, numerous private-led initiatives stand at the forefront of advancing sustainable finance in Switzerland. By their nature, those initiatives usually go beyond the mitigation of the negative aspects of sustainable finance and focus instead on the opportunity inherently associated to sustainability.

- **International best practices:** historically, the private sector stood as the historical lever to advance sustainability best-practices globally. The concept of integrating sustainability characteristics into finance was first advanced in 1992 during the Earth Summit in Rio de Janeiro. The transformation of private finance was recognized as essential for achieving sustainable development and led to the creation of the U.N. Environment Program Finance Initiative (UNEP FI), a partnership between UNEP and the global financial services sector. Further standards and metrics, such as the Global Reporting Initiative (GRI) in 1997 or the Principle for Responsible Investment (PRI) in 2006, were subsequently developed by, or in close collaboration with, the financial services sector.
- **Net-zero initiatives:** more recently, the Swiss financial services sector actively joined international net-zero alliances to combat climate change and align with the goals of the Paris Agreement. This commitment is evident across banking, insurance, and asset management sectors, with significant participation in Global Financial Alliances Net Zero (GFANZ) related initiatives, including the Net Zero Asset Managers initiative, Net-Zero Banking Alliance, and Net-Zero Insurance Alliance.¹ Those initiatives proved to be particularly effective. In the case of the Net Zero Asset Management (NZAM) initiative, AMAS reports that as of September 2023, a total amount of CHF 628 billion (approximately U.S.\$713 billion) of

¹ PwC, 2022, "Setting sail for a carbon-neutral future: Net Zero Insights 2022," <https://tinyurl.com/yecjf75e>

AMAS' members' AuM are currently managed in line with net-zero, which represents an increase of 18% compared to December 2022 levels. These private-led efforts are supported by the Swiss government and aim to standardize credible climate targets and increase sustainable finance's role in achieving net-zero emissions by 2050.

- **Swiss Stewardship Code:** another concrete example of a recent and private-led initiative building on the above, and paving the way to advance sustainable finance as a transformative opportunity, is the Swiss Stewardship Code. The Code elaborated by industry associations will be the subject of a particular case study in the final section.

3.4. Pros and cons of the Swiss private sector-led approach to sustainable finance

The key advantages of a market-led approach in a Swiss context mirror elements highlighted in Section 2, above. Industry-led self-regulations, as well as private-led initiatives, have the merit of having been developed by the industry for the industry, which make them particularly effective and fit for purpose. In a fast-moving field, such as sustainable finance, they additionally present the fantastic advantage of being agile and flexible. Those approaches were indeed elaborated in a six to nine months' timeframe and can easily and regularly be amended to reflect the latest international best practices when the initiators deem suitable and appropriate.

On the other hand, commonly referred to drawbacks of such an approach often include the lack of enforcement of self-regulations and private-led initiatives, even though self-regulations are actually binding on the members of the industry associations represented. By and large, industry associations include more than two-thirds of the market represented (in terms of assets under management, for example, for AMAS). When it comes to other initiatives, such as net-zero alliances, market competitiveness ultimately encourages market players to apply ambitious standards as highlighted in Section 2.

4. THE CASE OF STEWARDSHIP – THE SWISS STEWARDSHIP CODE

In October 2023, the Asset Management Association of Switzerland (AMAS) together with Swiss Sustainable Finance (SSF) published the Swiss Stewardship Code.² The Code exemplifies point to point how a market-led approach contributes to tackling the most transformative aspects of

sustainable finance. The Code sets forth principles for effective stewardship applicable across the industry, encompassing both asset managers and owners. It was developed through a collaborative effort involving a broad spectrum of investors, including both asset owners and managers, in addition to service providers.

4.1. Stewardship as one of the most critical approaches to achieving positive change

Investment stewardship is a responsible investment approach by which investors collaborate and interact with investee entities with the aim of generating long-term financial, environmental, and societal value. This investment approach has always been used in the financial services sector and the real economy. In recent years, however, stewardship, and more specifically voting and engagement, has become increasingly important as investors have started to expand their goals to encompass the contribution to positive change in the economy, in society, and for the environment. Amongst the different sustainable investment approaches, stewardship proved particularly effective in achieving positive impact, in tackling sustainability-related challenges, and in addressing sustainability-related risks. As opposed to other sustainable investment approaches, such as exclusion, for example, stewardship aims at collaborating with investee companies to lead them through the necessary transformations required to reach positive and long-term sustainable outcomes. In the case of a climate goal, for example, the investment approach directly aims at decarbonizing the real economy through active dialogue with a company. On the other hand, an investment approach based on exclusion would artificially decarbonize an investment portfolio without leading to any change in the real economy, where the excluded company may access the financing from a less stringent type of investor.

4.2. Effective stewardship through the application of nine ambitious principles

The Code has several objectives. First, it aims at elaborating standards defining stewardship as a sustainable investment approach that proves effective in achieving positive impact on key sustainability-related challenges. Integrating stewardship into the investment processes of the Swiss investment industry promotes a more sustainable and value-adding economy and helps to increase long-term returns for investors, adjusted for sustainability risks. Second, it aims to provide a level-playing field for Swiss stakeholders involved in stewardship

² AMAS and SSF, 2023, "Swiss Stewardship Code," <https://tinyurl.com/mr3xbwcz>

activities. This level-playing field lays the foundation for higher transparency and better comparability of stewardship practices. The need for transparency in stewardship activities was also highlighted as a key area of action by the Federal Council in its 2022-2025 strategy on sustainable finance.³

While being focused on the Swiss investors' practices, the Code builds on the extensive local and international experience of AMAS and SSF members. Global standards and international best practices, such as the Global Stewardship Principles of the International Corporate Governance Network (ICGN), the U.N. Principles for Responsible Investing (PRI), and the U.K. Stewardship Code, represent international benchmarks for stewardship activities by investors.

The Swiss Stewardship Code comprises nine stewardship principles and describes the key elements for effective and successful implementation. The key principles of the Code focus on recommendations related to those two critical means by which stewardship is commonly achieved: voting and engagement in an active dialogue with the companies. When it comes to engagement, for example, the Code emphasizes the importance of engaging in an active dialogue at different levels. An active dialogue can indeed be conducted by an investor on an individual basis or can also be conducted collaboratively with other investors or service providers to heighten engagement outcomes. Beyond their engagement with investee companies, investors may also decide to engage in an active dialogue with relevant public stakeholders and policymakers. The latter aspect is a unique aspect that the U.K. Stewardship Code, for example, does not provide for. A critical principle of the Code addresses the importance of defining the conditions under which an engagement is considered to be failing, as well as the conditions under which an escalation may be triggered. In the latter case, relevant escalation steps may go as far as divestment. The code also tackles key elements related to monitoring and reporting, as well as the management of conflict of interest and the delegation of stewardship activities to a service provider.

4.3. An agile and market-driven approach

Elaborated for practitioners by practitioners, the Swiss Stewardship Code was developed by AMAS and SSF, with the expertise of their members' specialists ranging from

asset managers, asset owners, and service providers. The Code acknowledges the diverse nature of asset owners, asset managers, and service providers, each varying in size, business model, and investment approach, leading them to exercise stewardship in different ways. This code represents a groundbreaking step towards unifying and enhancing stewardship activities within the country. Collectively, asset owners, asset managers, and service providers form an intricate web of responsible investing, each with a unique role and responsibility. As the Swiss Stewardship Code prepares to take center stage, it is this collaborative ecosystem of investors that holds the power to drive positive change in Switzerland's financial industry. The commitment of the industry is, therefore, expected to be stronger than a regulatory-led initiative. Additionally, and content-wise, it is also expected to be more ambitious. One of the key differences between the U.K. Stewardship Code and the Swiss Stewardship Code from a content perspective is that the Swiss Stewardship Code's principles include public policy engagement. The latter is not to be found in the U.K. Code since it was developed by the regulator, the Financial Conduct Authority (FCA).

5. CONCLUSION

The financial services sector plays a pivotal role in shaping and advancing sustainable finance practices. Through the market-led and principle-based approach exemplified by the Swiss Stewardship Code, Switzerland's financial services sector demonstrates an effective alternative to fully regulatory models, leveraging self-regulations, innovation, and international collaboration to address sustainability challenges. The Swiss case underscores the potential of financial services sector leadership to drive transformative opportunities in sustainable finance, highlighting the importance of collaboration, innovation, and a proactive stance towards sustainability. This approach not only fosters transparency and combats greenwashing but also aligns financial flows with long-term sustainability goals, creating value for the economy, society, and the environment. The Swiss Stewardship Code, with its focus on responsible investment and stewardship, serves as a blueprint for engaging the financial services sector, emphasizing the sector's pivotal role in achieving a sustainable future.

³ Federal Council report, 2022, "Sustainable finance in Switzerland: areas for action for a leading sustainable financial center, 2022-2025," <https://tinyurl.com/28sv9dj5>

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The financial services sector plays a pivotal role in shaping and advancing sustainable finance practices. Through the market-led and principle-based approach exemplified by the Swiss Stewardship Code, Switzerland's financial services sector demonstrates an effective alternative to fully regulatory models, leveraging self-regulations, innovation, and international collaboration to address sustainability challenges. The Swiss case underscores the potential of financial services sector leadership to drive transformative opportunities in sustainable finance, highlighting the importance of collaboration, innovation, and a proactive stance towards sustainability. This approach not only fosters transparency and combats greenwashing but also aligns financial flows with long-term sustainability goals, creating value for the economy, society, and the environment. The Swiss Stewardship Code, with its focus on responsible investment and stewardship, serves as a blueprint for engaging the financial services sector, emphasizing the sector's pivotal role in achieving a sustainable future.

³ Federal Council report, 2022, "Sustainable finance in Switzerland: areas for action for a leading sustainable financial center, 2022-2025," <https://tinyurl.com/28sv9dj5>

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Capco, a Wipro company, is a global technology and management consultancy focused in the financial services industry. Capco operates at the intersection of business and technology by combining innovative thinking with unrivalled industry knowledge to fast-track digital initiatives for banking and payments, capital markets, wealth and asset management, insurance, and the energy sector. Capco's cutting-edge ingenuity is brought to life through its award-winning Be Yourself At Work culture and diverse talent.

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