

Sustainable Banking, Financial Strength, and the BankLending Channel of Monetary Policy

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Abstract

During the financial crisis of 2008, banks focused too much on financial results while disregarding other aspects of business, which led to the banks' failure and seriously damaged their reputation. In order to restore this reputation, sustainable strategies have become a key element in many banks' strategies and practices. The purpose of this article is to analyse how sustainable banking affects the bank lending channel of monetary policy. Additionally, we aim to test how these effects are conditioned by the degree of financial strength of each bank. Using quarterly data of 79 listed banks from the OECD during 2016-2019 (947 observations), we find that the bank lending channel is operative either for banks with very low sustainable ratings or a weak financial position. As both sustainable ratings increase and financial strength becomes moderate, the bank lending channel is ineffective and monetary shocks do not affect loan supply. Moreover, for banks with certain sustainable compromises and a strong financial position, the effects of monetary policy on lending are the opposite of those posited by the bank lending channel, and these effects are more intense as sustainable ratings increase. Finally, our results also show that increases in central banks assets boost lending only for banks with low or moderate sustainable ratings, regardless of their financial strength. Overall, the results of this article suggest that more sustainable banks are less dependent on monetary policy decisions, which have important implications in the Agenda 2030 context for international organizations, central banks and financial institutions.

Keywords: financial sector, sustainability, financial health, monetary decisions, bank credit.