Sustainable finance:
how to build an ESG plan that supports your goals

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How building and maintaining an ESG strategy can create value and success for your business

ESG has become a critical driver of value. Not implementing a solid ESG strategy could leave businesses falling behind competitors and losing revenue.

However, implementing an ESG plan raises questions beyond long-term planning.

ESG considerations combine the challenges of managing detail and high-level strategic decision-making, and companies must implement procedures into everyday operations.

For many companies, the supply chain is the least optimized area concerning their ESG targets. The underoptimization of the supply chain is why treasury teams and procurement professionals should collaborate and together be at the forefront of implementing successful strategies. Treasury can release funds in order to invest, and procurement can utilize supplier relationships to support broader ESG business goals via their operational handling of the supply chain.

What does ESG mean to leadership teams?

Pressures are mounting on treasury teams to give accounts of their progress on ESG issues to boards, investors, and other stakeholders. At times it can be challenging to translate the high-level principles of an ESG strategy into a defined and practical reality.

Moving your company to a sustainable posture requires major strategic decisions that could impact your bottom line and long-term financial position.

Companies that have not yet developed an ESG strategy may be working toward ESG targets but have not yet defined a clear operational strategy for meeting them. Meanwhile, leadership teams may face pressure to demonstrate progress on ESG metrics but be unsure how to deliver it.

Are you discovering obstacles in identifying ESG risks with your suppliers – or finding those performing well? Are you finding the complexity of developing a full ESG solution daunting, or do you lack a meaningful way to influence or incentivize your suppliers into sustainable behaviors?

If these practical questions on how to operationalize ESG affect you, Taulia has put together this eBook to help you understand how you can embed ESG into your strategy. We will help you bake it into your supply chain and account for your progress with defined, accurate, reliable data.

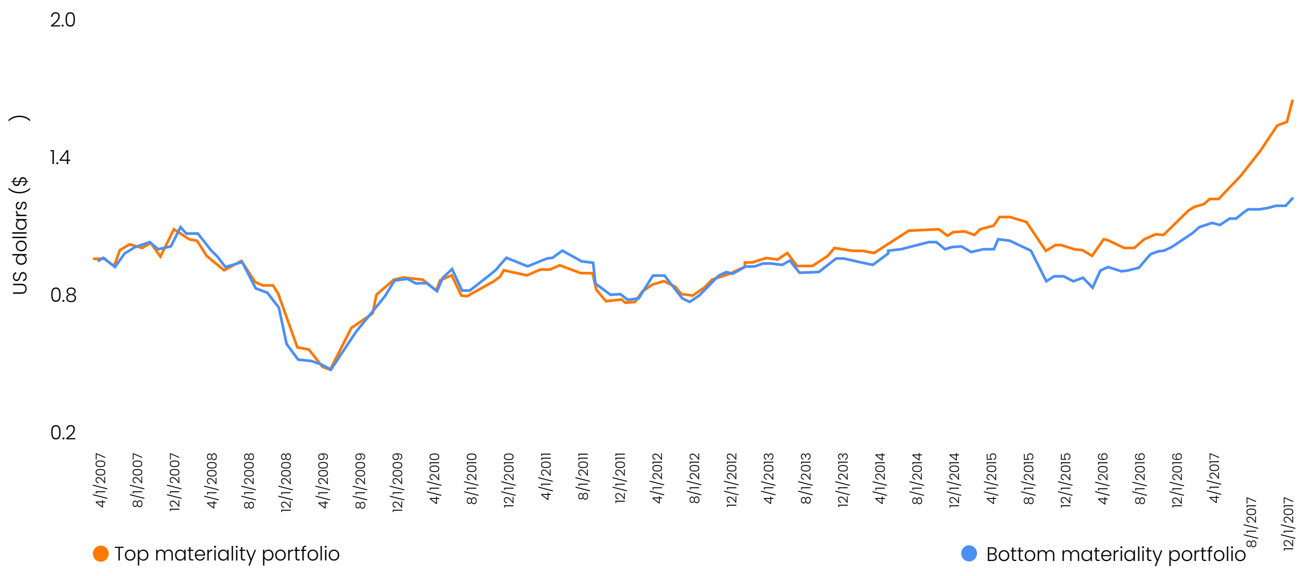
How can ESG principles drive value for a business?

A strong ESG proposition can reinforce existing revenue streams and provide a framework for discovering new ones.

A 2019 study by Deloitte found that banks with good performances on material ESG scores substantially outperformed their poorly rated counterparts . The chart below tracks a dollar invested with a top-scoring bank against one with a bottom-scoring bank over the decade to 2017.

The outperformance, particularly after 2015 when the ESG ratings data improved, is clear:

Top vs bottom 20 scoring material ESG banks' portfolio financial performances 2007-2017*



Portfolios risk-adjusted return estimated using Fama & French (1993) monthly 5-factor regressions

As all of this suggests, the dawning new era of ESG could represent a potentially radical new way of defining value.

Historically, smaller companies with weaker credit ratings could face an uphill struggle in supplier finance. However, the dawning of ESG-linked financing means they can now enjoy cheaper liquidity on a more even playing field as a 'reward' for their sustainability records.

Building a truly comprehensive ESG program means going beyond reforming your practices.

It means using your influence and leveraging platforms like Taulia's to embed ESG throughout your supply chain. A successful program of this kind will mean you can align your partners' behaviors with your own by incentivizing and rewarding actions that align with your ESG goals.

What are the benefits of embedding ESG in your supply chain?

The sustainability consultancy BSR has estimated the opportunity at a huge $660 billion globally. It can be broken down into several parts:

- The 'regular' benefits of supply chain finance, like increased control over your working capital.
- The long-term positives of a more resilient and sustainable supply chain.
- The fulfillment of growing expectations of ethical and green practices in the external market.
- The creation of a quantifiable way to determine the value of sustainable practices that can be used as a benchmark with other sectors or industries.
- As mentioned above, ESG can be the structuring principle for incentives for "good behavior" from businesses, like gaining access to cheaper liquidity.

What are the risks of not having an ESG strategy?

Consultancy firm McKinsey has estimated that up to 80% of a company's emissions stem from its supply chain rather than its core activities .

Supply chains can stretch across the globe and into jurisdictions where local business conventions often vary significantly from a company's domicile. They are made up of complex networks of stakeholders who may not have the resourcing, capabilities, or awareness to modify their supply practices in line with high ESG standards. And these stakeholders may find it challenging to have their ESG practices attested to by a trusted international body.

Here are just a few ways these challenges become significant risks to companies:

Operational risks

These can include:

» Environmental pollution

» Shortages of raw materials and natural resources

» Workforce health and safety incidents

» Labor disputes

» Corruption and bribery

» Geopolitical considerations

Access to capital

Whether under pressure from clients or regulators, investors are increasingly prioritizing ESG as a metric in their investment decisions.

External perceptions

A strong ESG proposition has become a core part of many companies' branding and external communications. Not having an ESG strategy means you risk being left behind.

Resilience

Sound ESG practices often align with ways of doing business most resilient to shocks – as we learned during the COVID-19 pandemic.

How do I operationalize my ESG strategy into the supply chain?

1. **Choose your ESG data source**

   There are many data sources out there (we'll discuss them in more detail in the next section). This could include aggregate scores from rating agencies such as Taulia partner EcoVadis, or other third parties from the private or public sectors.

2. **Decide your discount tiers**

   We encourage a sliding scale to reward different levels of engagement:

   » Participation tier, where the supplier is incentivized to take part.

   » Performance tier(s), where different levels of delivery are rewarded.

   » Equity tiers(s) that consider the supplier's profile on social issues, designed to encourage growth in sustainable categories where costs can be high.

3. **Invite your suppliers to take part**

   This involves clear and active communication to all stakeholders in your supply chain on the nature and extent of the discounts and early payments on offer.

4. **Supplier outreach and education**

   This is where you ensure your suppliers understand the incentives available, precisely what metrics will be applied to gauge their performances, and the structure of your discounting program.

5. **Suppliers enroll and enjoy discounted rates**

   If you do this through your existing platform, there is no lengthy or costly onboarding process to undergo; alternatively, third-party providers will be happy to offer their support.

6. **ESG discounts are applied**

   This is the good part. Your suppliers enjoy discounts, ESG standards increase, and you can evidence your organization's commitment to sustainability in all its forms.

What data is needed to leverage ESG effectively?

There is a vast range of data sources out there for scoring companies on their ESG performance: rating agencies, company scorecards, supplier attestations, and government sources, to name but a few.

ESG scores are a way of quantifying the risks and impacts an institution carries concerning each one and measuring progress towards mitigating them.

Every provider will have its scoring methodology, but the process is usually along this model:

1. **Identify key issues**

   These can run into the dozens and are tailored to specific industries. For example, packaging materials and their sustainability are key issues in the beauty industry, or a furniture manufacturer may be evaluated based on the sustainability of their wood supplies. Corporate governance questions are generally similar across industries.

2. **Each key issue is scored individually**

   Methodologies vary, but the data provider will generally score different exposure and governance metrics from 0 to 10. Low scores will mean a heavy exposure the company is not managing effectively, but a high score will indicate efforts to manage or mitigate the risk in question.

3. **Issues are weighted**

   Some ESG issues are more relevant in the short term; therefore, they may receive greater weighting; some may be more long-term considerations and may have their importance to the final score reduced.

4. **Scores and weightings are combined to arrive at the final ESG rating**

   Providers generally commit to making their scores as transferable as possible, allowing comparison across categories, sectors, and industries.

Interpreting these scores is straightforward. A high score is good, and one that is high and improving is even better.

Without independent analysis conducted by rigorous third parties, efficient and successful ESG strategies are difficult, if not impossible.

What constitutes success?

With a sustainable supply chain finance solution, procurement and treasury teams can access quantifiable and reliable data points to demonstrate successes in and progress toward sustainability goals.

Every discount is a data point that can cumulatively be used to indicate a firm's commitment to and actions in alignment with its sustainability goals.

As well as signaling a serious strategic direction, these data points can also be used to communicate progress and success to internal and external stakeholders.

Sustainable Supplier Finance with Taulia

Taulia's Sustainable Supply Finance solution means you can stand out from the pack with the quality and accuracy of your description of all your ESG activity – wherever in your supply chain it may take place.

This new feature set of the Taulia platform was created to allow our customers to embed ESG metrics, data, and outcomes throughout their entire supply chain.

It does this by empowering its users to either offer early payments or dynamic discounting depending on performance across their inventory and all their receivables and payables transactions.

Suppliers get discounted interest rates in return for ESG performance, and you get to fulfill your goal of encouraging responsible, sustainable practices in all activities.

Our solution offers its users concrete, verifiable and quantifiable data. This data can then be used to validate actions toward influencing your partners' activities.

The solution is scalable because it is delivered via a tried and tested platform. It is an automated, "out of the box" solution, with streamlined onboarding, transparency on all transactions, and analytics available on all activity.

It is flexible, with suppliers integrating directly into your process with Taulia, avoiding potential conflicts or complexity where there are multiple finance providers to consider.

Our dynamic routing engine discovers the funding source for any given invoice, identifies the correct ESG segment for the relevant supplier, and applies the appropriate discount.

Our solution will also empower you to benchmark against recognized standards.

Taulia can ingest and display the data inputs from any ESG ratings provider, the suppliers themselves, or your company scorecard data as suppliers'

ESG qualifications are shared. Armed with a cumulative progress report on supplier ESG alignment, your leadership teams have the information they need to meet any scrutiny they face.

If you would like to find out how to implement Taulia's Sustainable Supply Chain Finance solution, contact a sales representative today.

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