First letter (of many more to come) from the ESG function

*By **Johanna Wissing**, ITFA Board Member and Head of ESG (Environmental, Social and Governance)*

The views expressed in this article are the personal views of the author.

ESG, in other words Environmental, Social and Governance, needs no further introduction nowadays which is a remarkable development considering how the importance of this topic on the agenda has risen over the past decades from often fairly broad and vague CSR statements on companies' websites and in the footnotes of annual reports to now a front of mind matter of great significance.

To mention just one major milestone in 2015 the UN adopted its Agenda 2030 and the 17 Sustainable Development Goals (SDGs). These cover a balanced mix of economic, social and environmental factors and have been in force since 2016 for all 193 UN member states marking the first time that fighting poverty and sustainable development have been combined under one agenda.

Financial services play a crucial role in helping to achieve these goals by making adequate investment decisions and enabling and supporting companies, projects and innovation in this space. After all there is only that much the public sector can do and cooperation across sectors, industries and geographies is key.

Why is it relevant for trade finance?

Again, it is a notable achievement that sustainability is now a priority, but as an industry we must not forget that there is still a lot of work to be done, and we must act today to achieve better outcomes tomorrow, but what does this concretely mean for trade finance and how is it relevant?

I am sure no one disagree that trade finance which is at the heart and centre of the world economy has a pivotal role when it comes to driving positive ESG outcomes across all type of trade transactions and products. While it is believed by some that trade finance lacks behind developments seen in wider lending markets a lot of activity is under way already, and the relevant players, i. e. banks, insurers, brokers, fintech, law firms etc., are all increasingly focused on all matters ESG.

Trade finance is of course a complex field, and there are many areas to consider. What is key to all of them is to focus on enhancing transaction processing and tracking, on collecting data, and on developing new models for assessing risks and allocating capital to transactions benefiting the SDGs.

We have come a long way as an industry already: looking at the commodity finance space as one example only a few years ago there was little emphasis on the provenance of the underlying commodity, rather the main aspects to consider were the credit risk of the parties involved and compliance with AML and sanction regimes, nowadays there is much more focus on ensuring that commodity sources are sustainable under environmental aspects such as deforestation, social, i. e. working conditions, child labour etc., and governance. A lot of work still has to be done in this space, but from my own personal point of view I am very optimistic that things are moving into the right direction, as we are seeing strong collaboration between financiers and commodity players in this space.

Another area to look at is the support trade finance can offer to small businesses, companies in developing markets, female led ventures etc. by providing for example supply chain finance, pre-export trade loans, guarantees etc..There is a worryingly large gap of $1.5tn* between the amount of trade financing demanded and its actual supply which is particularly affecting smaller and female led businesses. In order to address this gap all industry players have to come together to develop new innovative ways of providing finance, and particularly fintechs can play a crucial role here when working together with traditional lenders. Of course the development banks take a centre role here, too, and have already made sizeable positive contributions to address this.

Last but not least export and project finance are crucial to drive positive ESG outcomes, and there are numerous headline deals for example in the wind energy space. ECAs around the globe do not only help financiers to mitigate risks and improve profitability by allowing banks to allocate significantly less capital than they would have had to allocate had they taken on clean borrower risks, but ECAs have also shifted their focus to incentivising ESG enhancing projects and to playing their part in driving positive ESG outcomes.

These are just some of the areas how trade finance can support the global move towards reaching the UN SDGs. There are numerous ways by how this can be achieved. To summarise again: close collaboration across all industry players is key, particularly in industries that could be considered problematic from today's point of view such as energy, agriculture and other commodity markets. What is important is not to simply turn away from certain industries, but to work together towards creating better outcomes. Further the provision of credit at sustainable margins is key, and particularly in the developing world supranational and government agencies can be key enablers. Additionally, by continuously innovating lenders should be able to lower their costs, and increase their reach allowing them to increase the supply of trade finance. Speaking about the role of innovation it can not only help to lower transaction costs by improving operational processes, but it also has a key role when it comes to decreasing risks by improving transaction tracking, data tracking and overall improving transaction transparency. These aspects are particularly important as they will allow lenders to offer products akin to what we see with sustainability linked loans by for example lowering pricing of SCF facilities if certain ESG criteria are met. Furthermore, consistent data tracking will eventually enable the creation of ESG linked credit ratings which again can have a positive impact on lending margins.

How can ITFA support?

Again, I believe there is little doubt that the industry as a whole understands the important business imperative, and that ESG is not a "nice to have", but key in today's world, but how can ITFA help to drive positive outcomes? There are many ways for ITFA and its membership to become active: by educating, by working with relevant regulators and other industry bodies, by continuing to help enhance the bank & fintech collaboration, by offering a forum to exchange ideas on market practise, etc..There are really countless ways to help this important cause and every single ITFA member can play an important role in this field, and I would like to actively encourage everyone's participation, and please do reach out with any personal ideas you might want to discuss. As an organisation we will work on all of the points mentioned above in 2021, so please watch out for more updates on learning opportunities, and on how ITFA is working with its members and other industry bodies to drive developments forward.

* https://www.adb.org/news/15-trillion-global-trade-finance-gap-frustrating-efforts-deliver-crucial-jobs-and-growth-adb