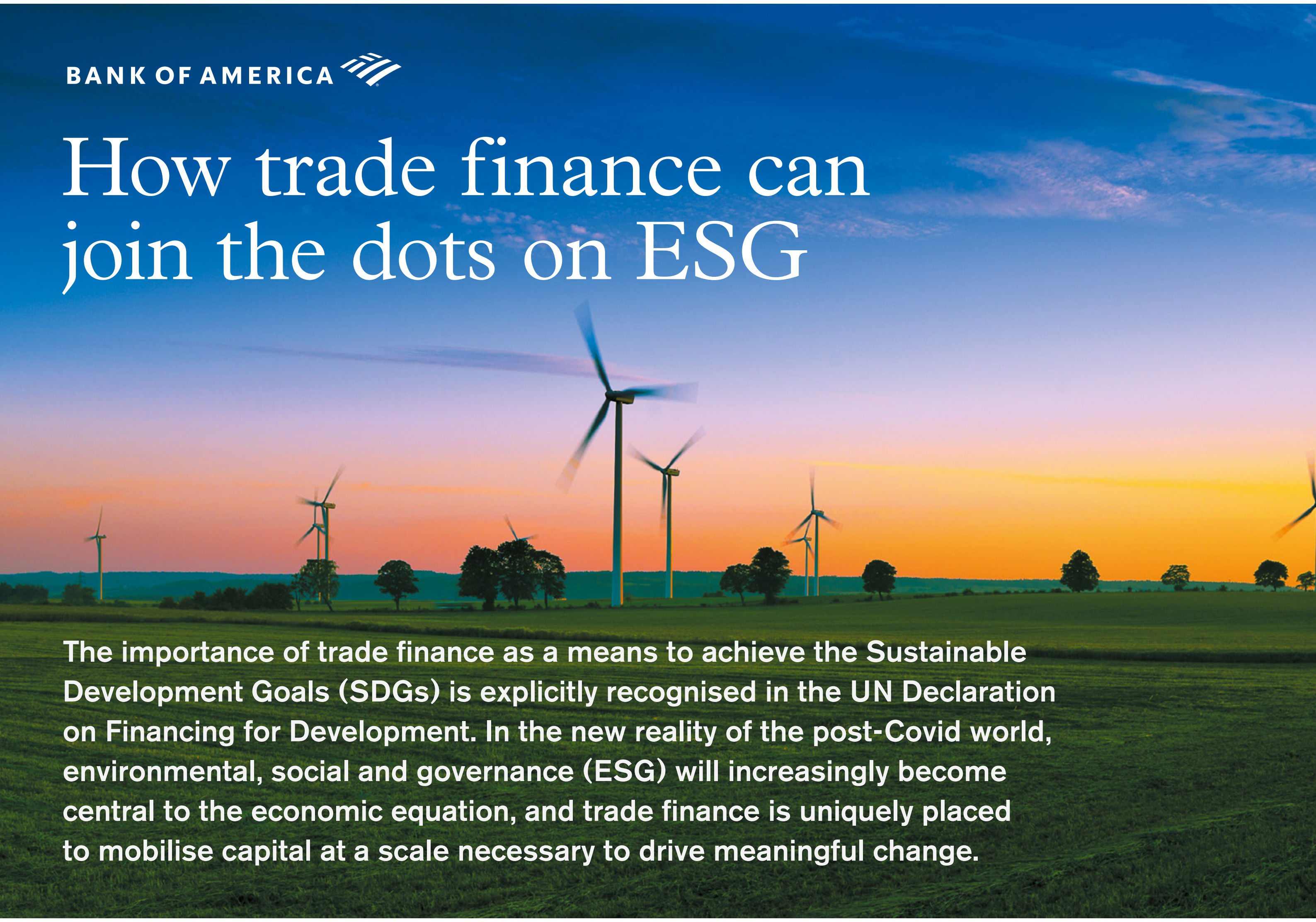


BANK OF AMERICA

How trade finance can join the dots on ESG

The importance of trade finance as a means to achieve the Sustainable Development Goals (SDGs) is explicitly recognised in the UN Declaration on Financing for Development. In the new reality of the post-Covid world, environmental, social and governance (ESG) will increasingly become central to the economic equation, and trade finance is uniquely placed to mobilise capital at a scale necessary to drive meaningful change.

In recent years, the use of tools such as sustainable supply chain finance – whereby suppliers can achieve more favourable interest rates if they meet certain environmental performance goals – has demonstrated just how useful trade finance can be in driving positive change.

But the future of ESG in trade finance isn't as a standalone topic, or a separate lens through which issues such as climate change and social justice are viewed. Instead, trade finance by its very nature is uniquely positioned to become an important facilitator of a new, fairer, more sustainable future.

"One of the interesting things about trade finance is that normally something has to happen before someone gets paid, for example a document is presented under a letter of credit, or a supplier is on-boarded onto a supply chain finance programme, so it provides a set of natural controls," says Duncan Lodge, global head of traditional trade at Bank of America. "While we do have named ESG solutions, traditional trade finance can actually be used as-is to support ESG activity across the board."

From letters of credit used to support the procurement of wood pellets for a biomass plant, to performance guarantees for an export credit agency (ECA)-backed wind farm project, ESG can sit at the heart of the trade finance business model.

"We are finding ways to use our existing vehicles to support ESG transactions," says Geoff Brady, head of global trade and supply chain, global transaction services at Bank of America. "We're learning that progress often comes when corporates begin to do things differently, with banks facilitating and supporting their new model."

Committing to a better future

As momentum has built around the topic of ESG, numerous financial institutions have committed to throw their weight – and their balance sheets – behind it, going beyond the 'E' in ESG to tackle societal and governance issues, too.

And unlike in the past, where ESG may have been seen as something of a side issue, it now occupies the highest levels of the organisation. That's why it was Bank of America's vice chair, Anne Finucane, who announced the bank's recent US$2bn Equality Progress Sustainability bond (EPSB): ESG is now a board-level mandate for banks, and there's no going back.

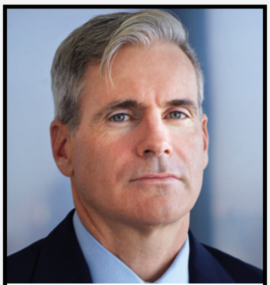
Issued in September last year, an amount equal to the net proceeds of the EPSB offering will be allocated to advancing racial equality, economic opportunity and environmental sustainability. In a clear recognition of the power of trade finance to effect change, a portion has been dedicated to supply chain finance loans, which will be offered directly to minority-owned business enterprises (MBEs) in the US.

"We're connecting issuers and investors to deploy more capital for important societal issues, such as equality progress. We want to make it easier for our clients to be proactive about finding different suppliers," says Brady.

of investment capital via short-term financing.

"We're creating really investable asset classes that bring in capital market support, and as our supply chain finance programmes continue to grow, having investors coming in is increasingly important," says Lodge, who adds that linkages with ESG have helped trade finance become an increasingly attractive asset class.

"A few months ago, the conversation would be, 'Can we invest in some of your supply chain finance assets?' Now we're getting calls from the market asking to invest in our ESG trade. You can feel that shift in



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The first offering of its kind in the financial services industry, the EPSB effectively links together two financial events that would not normally cross paths: a bond issuance and the onboarding of a small business client.

"Trade finance is the conduit between those two sides," says Brady. "It sits in the corporate and investment bank, but also has this touch point to smaller, minority-owned suppliers, who we can then connect to our retail banking network."

"This is the first time I've ever worked in a project of this magnitude, where so many different lines of business come together – principal investments, debt capital markets, business banking, and global trade – on a single initiative," says Lodge. "It highlighted to me the power that such connectivity brings from an ESG standpoint."

This comes as the Covid-19 pandemic has brought into sharp focus working capital issues faced by small suppliers around the world. Rather than simply a working capital benefit play, programmes such as this have become vital to overall business viability, and corporates worldwide are seeking ways to shore up the long tail of their supply chain in order to survive amid straitened times.

Closing the trade finance gap

As outlined in the UN's latest *Financing for Sustainable Development* report, making trade more inclusive also requires addressing trade finance gaps that disproportionally affect smaller companies and impede the ability of exporters to seize all trade opportunities that would otherwise be available.

The EPSB is just one example of how trade can be leveraged to create a virtuous circle, linking better ESG performance in companies' supply chains to the entry

thinking across the broader ecosystem," he says.

As ESG gains momentum in trade finance, the data from the underlying transactions can be leveraged to create benchmarks, incentivising participants to report more, and feeding back into the objectives of impact investors. But the use of this data doesn't stop there.

"We can use that information to tell our clients things they perhaps don't know about their supply chain, enabling them to make better decisions," says Lodge. "For example, as our programmes grow and we unlock technologies, we can start to tag assets as being ESG related, whether that's the underlying flow itself, or because the companies involved score highly on certain ESG practices. This enables us to create a really interesting front-to-back solution."

Mainstreaming ESG

As the world looks towards the post-pandemic recovery, the growth of sustainable trade will be a central engine for development. Importantly, none of the ESG benefits that can be facilitated via trade finance involve creating entirely new products.

"The natural end of this is that the transaction itself, be that the goods or the services or the supply chain, will be sustainable," says Brady. "When people ask us what ESG products we have, we'd like to think that the answer is that all our products can support ESG. It's not much different than what we do every day. We're just applying trade finance in ways that support ESG initiatives for our clients and for Bank of America."

At their core, trade finance banks provide two vital inputs to global trade: advice and money. This, combined with the right connectivity across the financial ecosystem, means that the industry can play a central role in ushering in a new, fairer future for clients, the economy, society and the environment.