

Embedded ESG for SMB Banking



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Environmental Social and Governance

Whose responsibility is it?



A few years ago, a [video of an injured Koala surviving the Australian bushfire](#) went viral. As the world mourned the plight of the 3 Million animals in Australia; few Australian banks came forward to [acknowledge and discuss their role in this destruction](#).

Many economists have described *climate change as the biggest failure of the capital markets* because most individual purchases (investment stocks and general purchases) don't include the cost of environmental destruction such as lost biodiversity, ocean acidification, and extreme weather events.

The adverse effects of greenhouse gases (GHG) are therefore 'external' to the financial markets, which means *there is usually only an ethical – rather than an economic – incentive for businesses and consumers to reduce their emissions*.

Profitability and Sustainability

Finding the right balance!



Today, across the globe, there is a growing consensus that the objectives of generating returns and prioritizing environmental and social welfare are not mutually exclusive.

The [journey to net zero by 2050](#) for businesses and governments as defined in the Paris Agreement involves reducing emissions based on detailed scoping.

- Scope 1: Covers direct GHG emissions (Greenhouse gas) from owned or controlled sources – e.g., emissions from facilities or vehicles.
- Scope 2: Covers indirect GHG emissions from the generation of purchased electricity, steam, heating, and cooling that is consumed by the business.
- Scope 3: Includes all other indirect GHG emissions that occur in a business's value chain – e.g., purchased goods and services, travel, waste disposal, and from customers using the business's products and/or services. Scope 3 emissions are often the most significant, but also the most difficult for businesses to reduce.

Without ESG and decarbonization considerations, businesses tend to exploit natural resources leading to environmental degradation. In contrast, [proactive steps and initiatives towards ESG and decarbonization, undertaken by companies](#) have helped them become industry leaders in sustainable practices, attracting investors and enhancing brand credibility.

The increased monitoring of sustainability management in business performance and related disclosures have led to many listed companies, including [90% of S&P 500 companies and 70% of Russell 1000 companies](#), reporting and publishing ESG details in some form.

ESG metrics adoption in Banking

Challenges faced by SMBs and Banks



While more and more big businesses and large banks are now adopting ESG, embedding ESG metrics (especially decarbonization) into small business banking (for *unlisted companies*) has been tough. Gathering and organizing the required SMB data residing in multiple disparate systems, with all the attendant real-world problems of duplicates, gaps, and inconsistent formats is difficult. Problems of poor data quality and availability, data integration, regulatory uncertainty, and risk management are the usual challenges faced by banks when venturing in to ESG finance.

The pre-and post-pandemic economic environments have not been favorable for the survival of most small and medium businesses. Today, most small business owners prioritize their immediate survival rather than worry about long-term environmentally and socially sustainable business growth.

To embrace the big opportunity behind small business banking and embed ESG into small business supply chains, banks need to prioritize digital innovation, adaptability, and ESG integration.

According to [World Bank](#), Small and Medium Businesses (SMBs) are the most important contributors to job creation and global economic development (contributing almost 40% of national GDP in emerging economies). Thus, embedding ESG metrics to track sustainable growth in small businesses is crucial for any government and banks.

According to a [survey conducted by YouGov](#) for energy firm World Kinect Energy Services, 40 percent of SMBs in the United Kingdom haven't made a sustainability plan—and 30 percent don't intend to. This implies that there is a lack of intent and motivation among small business owners to work towards ESG metrics.

Managing SMB's financed emissions

Opportunity and responsibility for banks

The GHG protocols Scope 3 emissions relate to banks servicing the ongoing capital needs of businesses and providing new capital for new projects. In both these cases, the financed portion of GHG emissions will be referred to as “financed emissions” and will get added to the bank’s emissions.

Most bankers agree that the transition to net zero carbon emissions would require nothing less than a new commercial and industrial revolution. Many global banks have agreed to net-zero commitments ranging from the years 2030 or 2050. This implies that beyond being responsible for emissions related to their own operational footprint, banks now must act as sustainability partners to their individual and business clients.

Most banks today are evaluating emissions related to on-balance sheet financing, as this provides a good starting point for them to monitor their clients’ activities in terms of sustainability.

Currently, the Financial Services Task Force has defined activities related to only on-balance sheet emissions to be included for emissions, although soon, banks might see this scope of activities include sovereign debt, capital markets financing, trade finance, deposit taking, transaction banking, and advisory.

The process of assessing and setting targets for financed emissions is far from simple. It requires a delicate balancing act by banks to engage existing clients who are moving to low-carbon business models, move away from clients who are “high emitters” and add new clients with innovative low-carbon business models. It involves multiple complexities arising from differences between sectors, geographic variation, shifting counterparty plans, changing industry standards, and a nascent and rapidly evolving data environment.

Furthermore, the actions that banks take to achieve targets often create pressure on other objectives, such as revenue growth in critical business areas, and require changes to key processes and policies. Banks need to adopt a “beyond banking” mindset to promote sustainable business practices within their business client segment to promote long-term sustainable growth and improve return on investment (ROI) for small business clients.

To champion responsible business practices, banks must engage and partner with their SMB clients to undertake the ESG Journey.

The strategy by banks ably aided by suitable software platform can involve the following steps:

- Create awareness, educate, and deploy resources to measure and monitor emissions.
- Self-reliance and process automation with ability to mobilize, penalize, and incentivize SMBs towards their ESG goals.
- Continuous journey towards attaining sustenance goals.

Take control of the future with Oracle's industry leading domain driven products like corporate credit and lending, cash management, trade and supply chain finance offered as banking-specific hyperscale cloud services over Oracle's Cloud Infrastructure.

Leverage Oracle's digital banking platform to deliver an immersive banking experience that offers business value going beyond just the user experience with its persona-centric domain designs.

Banks can consider solutions like Oracle Banking APIs to leverage open banking and provide a fully integrated platform for SMEs to access third-party applications and accelerate the digitalization of ESG regulatory services to provide real-time advice, multi-provider ESG data platforms, fee-based subscription models, and integrated service offerings that add depth and granularity to small business financial services.

Awareness Creation

Short-term strategy - build SMB's ESG Roadmap

- a. *Awareness and Understanding:* Banks can provide a guidebook for SMBs to self-assess their current business practices and benchmark them against globally acceptable ESG practices. Banks can also offer SMBs personalized assessments.
- b. *Goal Setting:* Bank can provide tools and widgets for SMBs to access their own carbon footprint and collaborate with them to set achievable ESG goals based on their industry, size, and resources.
- c. *Action Planning:* Banks can involve ESG experts and provide advice to their SMB clients to develop a customized ESG action plan that outlines specific steps and timelines for SMBs to improve their ESG performance.
- d. *Integration:* Banks can take a collaborative approach by entering and reviewing the SMB's ecosystem and measuring different points of action (suppliers, customers, employees, and partner transactions) to review the SMB's overall business strategy and help them emphasize the link between business success and sustainability with regular updates and reports

Oracle is investing into offering carbon emission profiling for corporate customers of banks providing a real-time integrated insight including a corporate customer's ecosystem and make a well-informed move towards reducing their carbon footprint.

Self-reliance and process automation

Medium-term strategy - Integrate ESG metrics into SMB's core business operations with toolkits and dashboards.

- a. *Data collection and standardization:* Banks need to establish a system for gathering relevant ESG data from various data providers and develop calculators with different metrics, that SMBs can track according to their industry and geography.
- b. *Real-time monitoring and reporting tools:* Banks can provide digital platforms that enable SMBs to input and analyze ESG data. Through ERP integration between corporates and banks and open banking account aggregation, banks can enable real-time monitoring of transactional data to measure ESG performance and identify areas of improvement.
- c. *Real-time Dashboards:* Banking dashboards can be tailored for different SMB profiles allowing them to focus on specific ESG Dimensions, relevant to their operations. SMB dashboards can be designed to provide early warning indicators to manage environmental and ethical risks that can prevent costly legal disputes and reputational damage to the banks and the SMB clients.

Oracle, with its niche fintech ecosystem, is committed to providing continuous monitoring of carbon footprint indices as part of embedded banking offerings with ERP integrations for a seamless and meaningful approach to achieve ESG goals. With Oracle's integrated digital trade and supply chain finance solutions, banks and corporates get seamless and integrated views across their supply chain for a structured approach to monitor carbon emissions.

Continuous journey

Long-term strategy - Measure, Monitor, Mobilize and Incentivize SMBs based on their ESG metrics

- a. *Measure and monitor:* Measuring the ESG performance of SMB clients is crucial to a bank's own ESG strategy. Furthermore, banks can facilitate ESG scorecards and heatmaps to evaluate an SMB's performance against industry benchmarks and sustainability standards.
- b. *Mobilize:* Engaging key stakeholders like employees, customers, partners, and suppliers and to create a culture of responsibility in the SMB's ecosystem, banks need to provide communication templates, engagement strategies, and stakeholder monitoring and collaboration tools, within their toolkits to assist SMBs to mobilize their stakeholders.
- c. *Incentivize/Penalize:* Financial rewards in the form of preferential interest rates, and lower transaction margins on transactions can be powerful drivers of change that a bank can offer to reward sustainable behavior. Banks can also offer collaborative partnerships through their own ecosystems or industry groups and government bodies (like chambers of commerce) to help ESG-oriented SMBs access new markets for business growth.

Banks also need to play a role in enforcing accountability by integrating penalties for non-compliance into financial arrangements (banking forms) and loan agreements.

The Oracle Approach

Oracle is committed to traveling this journey with the industry. We are focused on evolving our pre-built user experiences to be equipped with ESG awareness, monitoring and real-time dashboard capabilities with extensive analytics capabilities to support banks in balancing risk in their ESG lending strategies and portfolios. With focus on reducing GHGs, [Oracle's SaaS solutions](#) also helps banks achieve their larger ESG objectives. We continually assess market developments and requirements, invest to meet these needs, and innovate to ensure that our customers and partners have the insight and agility they need to thrive in a more sustainable world.

To learn more about our banking solutions, click [here](#), or contact us to have a conversation.

Oracle's corporate credit and lending solution is well equipped to enable banks to explore to offer green-financing products, which can be tailor-made to better track and manage financing products that help promote and celebrate businesses that are eco-conscious.

Leveraging the configurability capability of Oracle banking suite of products, banks should be able to design and offer green finance products built on the corporate's green score.

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