



Ethical supply chains and procurement

Bringing to life the ethical and sustainable vision of a business

Executive summary

The supply chain brings to life the ethical and sustainable vision of a business. Supply chains and procurement are only as resilient as their weakest link; therefore business continuity relies on us thinking about their impact on people and the planet.

In summary:

- Increasing pressure from customers, regulators, and investors makes sustainable supply chain management a strategic priority. The impact of the recent COVID-19 pandemic only increases the urgency.
- Ethical supply chains underpin resilience. Supply chain transparency and authentic support for third parties can keep your business relevant in a market of stakeholder capitalism, rather than shareholder capitalism.
- Cost optimizing and asset minimizing supply chains that have sourced and served in a predictable world are shown to be opaque, inflexible and vulnerable to global disruption.
- One of the keys to business continuity during disruption is a resilient, digitally-enabled supply chain. That is, a multimodal network that promotes collaboration with suppliers, enhances operational performance, and reinforces the responsible reputation of the business.
- It will be the regulators that set the standard by which all companies must comply, but it will be the business's ability to meet the values of the consumer, investor, and employee that will help them gain competitive advantage.
- KPMG is here to support your journey in bringing to life your ethical and sustainable vision. We can provide a connected offerings and provide digitally-enabled solutions.

There are six steps to help build a sustainable and resilient supply chain:

- 1. Ethical supply chain assessment:** identify potential points of failure in your environmental, social and governance (ESG) framework, and identify and prioritize solutions.
- 2. Visibility:** achieve real-time transparency through end-to-end tracking and traceability of suppliers and products.
- 3. Risk landscape:** investigate suppliers and assess key current and potential risks in the supply chain.
- 4. Optimize:** Transform the supply chain to determine the optimal balance of cost, cash, service, and ESG, helping to deliver both profitability and sustainability.
- 5. Embed governance:** perform due diligence on suppliers to measure ethical integrity and embed a robust governance framework to uphold ethical practice in the supply chain.
- 6. Proactive management:** work collaboratively with stakeholders to go beyond just compliance and use predictive analytics to pre-empt and mitigate potential disruptions.

An ethical and connected network means embracing the digital platforms that enable visibility and collaboration, educating and supporting key third parties, and taking bold steps in empowering consumers to make informed buying decisions.

A company's supply chain contains on average
5.5 times as many greenhouse gas
emissions as its own operations.

Source: CDP, Global Supply Chain Report 2019



Introduction

“Unprecedented” — a word used to describe the devastating fires in Australia, flooding in Yorkshire in the UK, severe water shortages in South Africa, and the COVID-19 pandemic. Astute businesses are already reconciling the impact of this global shift on their future footprint, pivoting from managing crises to managing risks. A sustainable supply chain management strategy can deliver resilience to weather these shocks. How? By embracing the digital platforms that enable visibility and collaboration, educating and supporting vulnerable third parties, and taking bold steps in empowering consumers to make informed buying decisions.

Global crises are industry agnostic. In the last 20 years, we have seen rapid geographic and structural diversification of customers, suppliers, products, and communications as a result of globalization. In turn, we expect increased revenue and operational performance. And yet, the basic model that underlies most core operations predates globalization.

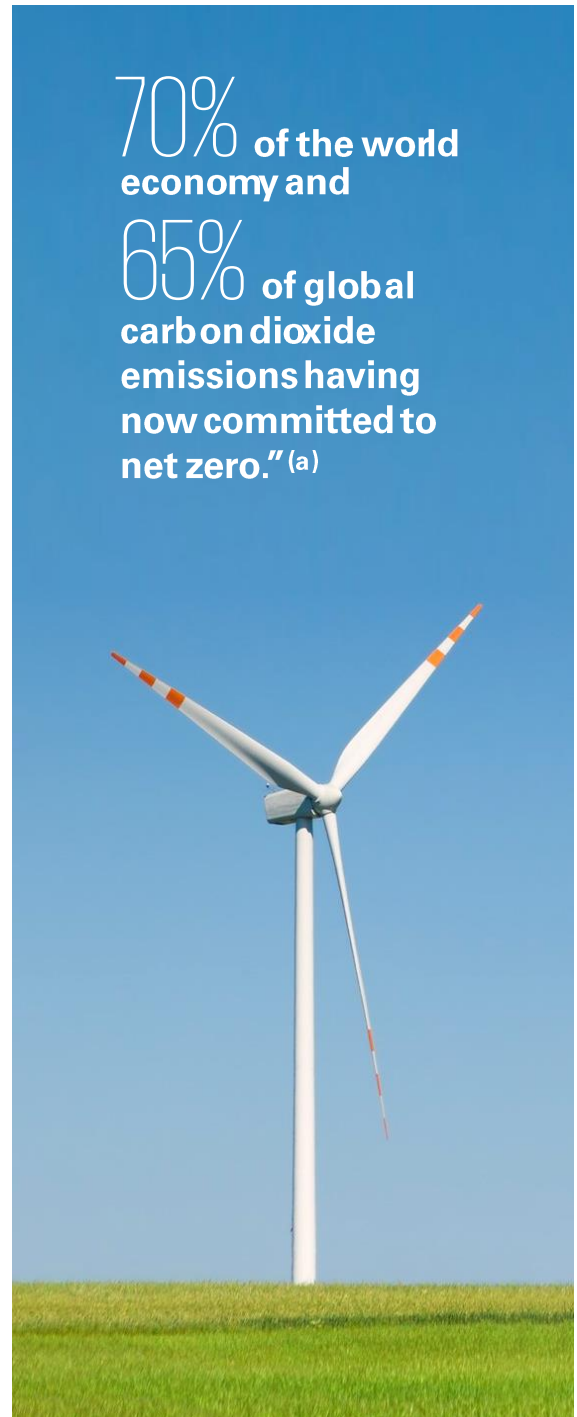
Supply chains are strategically critical, but vulnerable to risk. Globalization means supply chains have become complex, dispersed, opaque and inflexible. Traditional cost optimizing and asset minimizing models are sourced and served adequately in a predictable world. Faced with the unexpected, however, a minimalistic approach without visibility over where inventory is located, knowledge of nodal constraints, and impending risk, can expose your business to disruption and ethical violation.

If businesses can't seem to respond to operational change, it is concerning to think about the impact it can have on people and the planet across supply chains spanning less mature and unregulated markets, exposing them to slavery, forced labour, dangerous working conditions, information security lapses, quality issues, environmental waste, pollution and much more.

One of the keys to business continuity is resilience, and at the core of resilience is an ethical and sustainable operating model. KPMG can help you to become agile, flexible and influential in a new world of stakeholder capitalism. A multimodal network with diverse upstream and downstream locations, driven by real-time, predictive intelligence can help you react quickly and effectively in a crisis, predict and mitigate future risk, promote stakeholder loyalty and ensure regulatory compliance.

Profitability and shareholder returns are always going to be a priority, but investors and consumers are making it clear that social purpose and environmental stewardship are critical to business success, credibility and relevance. It is expected that assets will soon lose value if they have a negative ESG impact. The supply chain is the platform to evidence the ethical and sustainable vision of your business, but demonstrating that can require courage, innovation, collaboration, and transparency.

70% of the world economy and 65% of global carbon dioxide emissions having now committed to net zero.”^(a)



Note: a) UNFCCC - UN Secretary-General Calls for Exponential Growth in Global Coalition to Achieve Net Zero Emissions | UNFCCC.

Why we need to act now

40 million people are victims of modern slavery worldwide,^(b)

71% of these are women and girls^(b)

US\$ 174 bn is the global profit^(c)

Today's market is one of stakeholder capitalism, not shareholder capitalism. In a borrow-and-share network, stakeholder credibility is important to help ensure your business remains relevant.

Many industries are experiencing drivers to change their ethical and sustainable footprint. A strategic change should consider the entire supply chain, and as you transform, your suppliers should follow your lead.

1

Stakeholder expectations:

Consumers, employees and investors are demanding more visibility over where and how products are sourced. Evidence of good ESG governance can drive stakeholder decisions. As the ultimate referees of corporate success, these stakeholders dictate your license to operate, and with it your revenue and profit margins.

2

Competitive advantage:

Leading by example in ethical stewardship can be a 'differentiator' in a competitive market. Evidence of sustainable supply chain management can drive the same purchase intent as product promotion. This first-mover advantage, however, is to be seized quickly, as ESG is expected to soon become both regulation and the norm.

3

Reputation:

When an ethical breach or violation is uncovered, it is not typically the supplier that receives the negative press, but the company that uses their services. Authenticity through action can help reduce the risk of reputational damage, as well as attract and retain talent.

4

Regulatory compliance:

For the first time, ESG is a regulatory requirement. In 2022, the Task Force on Climate-Related Financial Disclosures (TCFD) guidance is likely to become mandatory, and the Plastic Packaging Tax will come into force on all goods imported and manufactured in the UK containing 30 percent or more single-use plastic.

5

Risk (physical, transition, financial, supplier):

2020 has been a transformative year in how we think about supplier risk. Painful lessons have been learned, causing us to rethink single sourcing or reliance on third parties. Extreme weather and water scarcity are also changing how companies operate, and we believe there will soon be a need to adapt to new technologies and markets created to manage these crises. How has COVID-19 sharpened our focus in risk management?

Notes:

b) <https://www.un.org/press/en/2018/gashc4244.doc.htm>.

c) <https://www.proterrafoundation.org/news/foodand-modern-slavery/>

Values and benefits

A sustainable supply chain can help reduce risk, add new profit lines, and make the share price more resilient to shock. With an increasing customer base willing to pay more for sustainable goods and services, to overlook sustainable supply chain management is to leave money on the table.

The largest global challenges don't have borders. The supply chain provides a significant platform to help drive a truly global, united, and essential response to enhance ESG, not just within the immediate walls, but on a global scale.

1

Stakeholder confidence:

Brand is among a business's most valuable asset. Positively asserting sustainable values can help attract customers and drive up revenue, secure a wider pool of investment options, and distinguish a business as an "Employer of Choice". Two in three millennials would take a pay cut to work for a responsible company.^(d) After setting science-based targets, "52 percent of company execs have seen investor confidence boosted".^(e)

2

Resilience:

If a business model relies on underpaid workers, weak regulations, poor enforcement of labour laws or even illegal activities, such as slavery, current earnings will likely be unsustainable over time. A future-fit, sustainable supply chain is collaborative, transparent, efficient, and agile. In sum, it is able to respond to change, whether it's a climate disaster or incoming regulation, effectively and at pace. After setting science-based targets, "35 percent of company execs have increased regulatory resilience".^(f)

3

Reduced costs and higher profits:

A supply chain that promotes close collaboration with suppliers and looks after natural resources can be efficient, help reduce costs, and enhance profit margins. A major retailer changed the way it manufactures trainers to minimize waste, reducing material usage by 20 percent, and, in turn, generating 0.25 percent higher margins.^(g) A food and beverage retailer partnered with vets to support its dairy farmers, teaching them how to deal with common health problems. This led to each of the cows producing more milk. Healthier cows means less cows being required to fulfil demand.

4

Business sense:

By not addressing sustainability in the supply chain, businesses can be exposing themselves to risk, employee attrition and potentially leaving money on the table. There is a growing group of millennial consumers now willing to pay for sustainable goods and services; 91 percent said they'd switch brands that have a "cause".^(h) Setting ambitious science-based targets has led to improved profitability and competitiveness, where "55 percent of company execs have gained competitive advantage",⁽ⁱ⁾ and increased innovation. In addition, "63 percent of company execs say science-based targets drive innovation, catalyzing the development of new tech and operations."^(j)

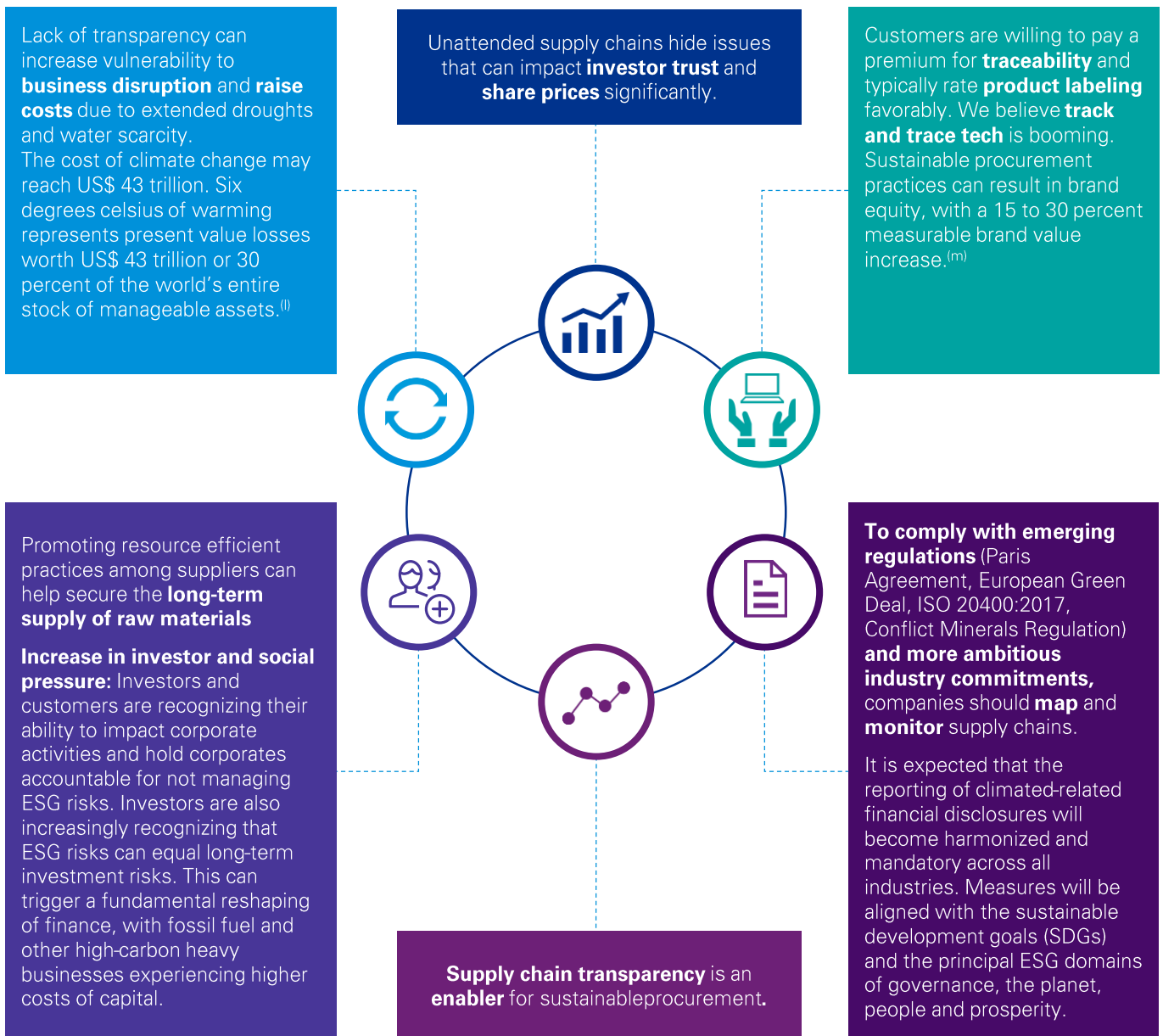
44%
of hedge fund
managers are in
progress of
implementing ESG
into their investing
life cycle, and
15% are at the
mature
stage.^(k)

Notes: d) <https://www.conecomm.com/research/blog/2015-cone-communications-millennial-csr-study>
e) <https://sciencebasedtargets.org/blog/six-business-benefits-of-setting-science-based-targets>
f) <https://sciencebasedtargets.org/blog/six-business-benefits-of-setting-science-based-targets>
g) <https://www.cips.org/supply-management/opinion/2019/july/five-benefits-of-a-sustainable-supply-chain/>
h) <https://www.conecomm.com/research/blog/2015-cone-communications-millennial-csr-study>
i) Six business benefits of setting science-based targets - Science Based Targets
j) Six business benefits of setting science-based targets - Science Based Targets
k) KPMG-CAIA-AIMA-CREATE Survey 2020



Resource efficiency and sustainable procurement

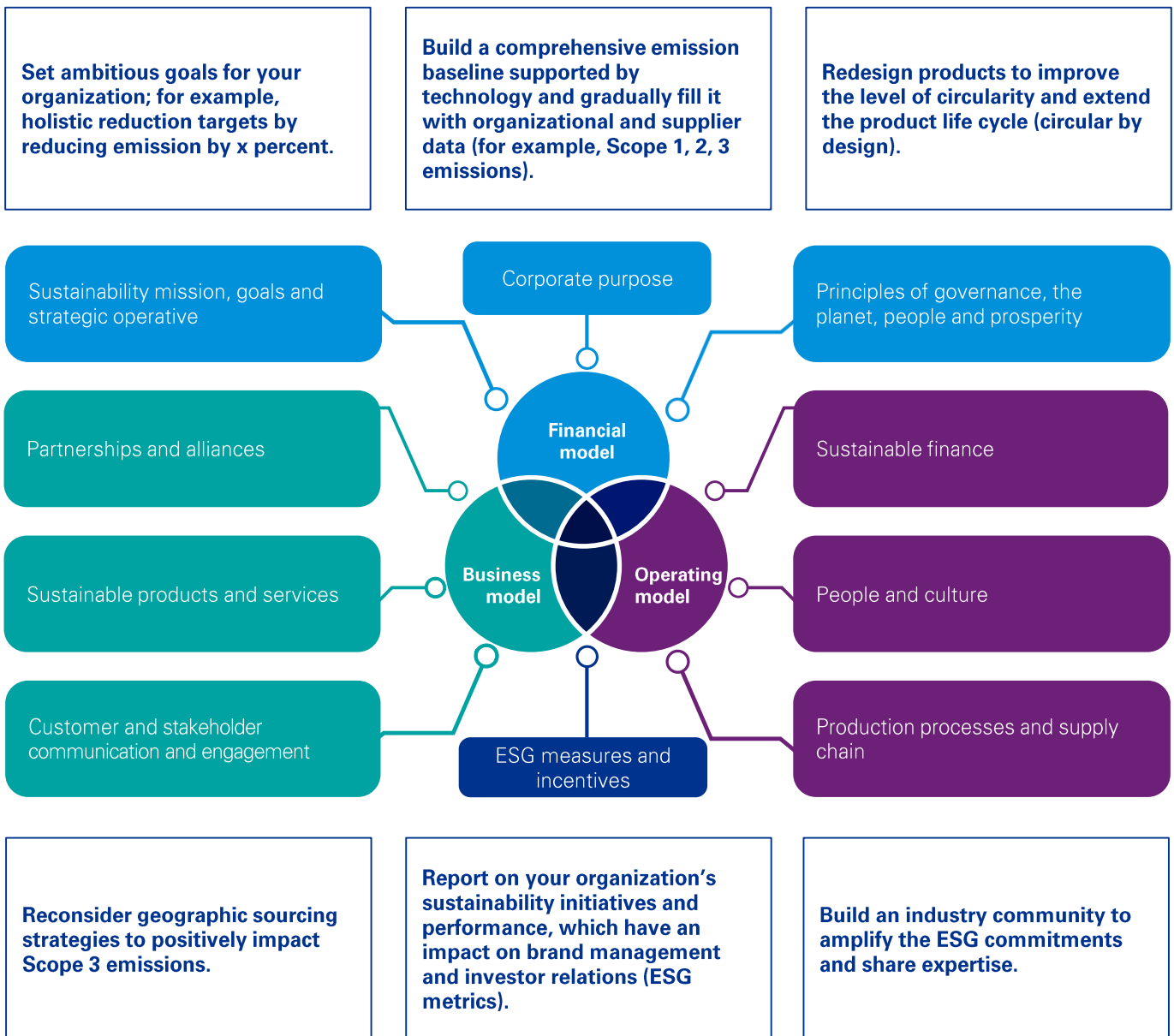
We believe sustainable procurement is fast becoming the norm due to five reasons and one enabler:



Notes: l) The Economist, The cost of inaction: recognizing the value at risk from climate change, 2015
m) Source : World economic forum: Beyond sustainable procurement

Delivering against the sustainable development goals (SDG)

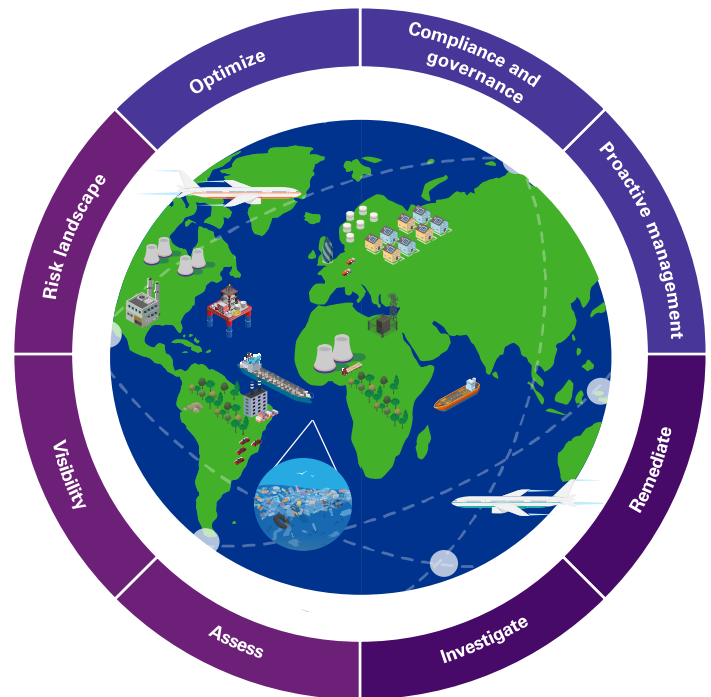
Companies are responsible for taking the initiative to become more sustainable along with their stakeholders



Where to start

KPMG can help you transform the ESG foundations that make up your business. We can help you shape a supply chain that manages the risks associated with climate disasters, complies with incoming regulations, and looks after people and the planet.

This approach combines profitability and sustainability to enhance the overall efficiency of your operations and contribute to helping reduce the wider global risks of continued ethical or environmental catastrophes.



Understanding the supply chain

We can enable you to empower your stakeholders to make informed buying and investing decisions.

1. Identify current state **maturity** and points of failure in the supply chain as we work with you to design targeted ESG approaches in the innovative KPMG Ignition facility.
2. Achieve real-time **visibility** through enabling technology, such as blockchain and systems integration. We can help you identify and implement leading approaches for deep transparency, traceability, and real-time tracking across the supply chain.
3. **Assess** key third parties through negative listing and self-assessment questionnaires. Identify significant incremental current and potential ESG risks to operations using criteria that includes severity, likelihood, velocity and interconnectedness.



Transforming the supply chain

We can help you drive a step change in your ethical and sustainable footprint through flexibility, resilience, collaboration and control across the supply chain.

1. With a clear understanding of targeted ESG improvement opportunities, we support you to **optimize** the supply chain. We build a digital twin that intelligently illustrates the optimal balance of cost, cash and quality, and aligns the ESG transformation to a wider operating model.
2. We can perform due diligence on third parties to evaluate their ethical integrity and ESG profile, screening against ESG and regulatory data sources to identify ESG deficiencies and/or a poor ethical track record. We can then help you design or improve your **governance** framework to uphold ethical practices in your supply chain and align your suppliers with your ESG vision.
3. We can help you **proactively** mitigate potential risk using predictive analytics and scenario modeling. Proactive management also means supplier relationship management — going beyond compliance to help support and encourage third parties towards better ESG behavior.



Remediation and incident management

We can help you embed a culture that's able to respond to unprecedented ESG breaches at pace through effective remediation.

1. We can help you investigate incidents or breaches at pace, and respond with the design and implementation of a detailed remediation plan.
2. We can help you recover and improve from an ESG breach or incident, as well as create a crisis-ready culture by:
 - Designing and implementing scenario “playbooks”.
 - Embedding, through training, robust ongoing ethical practices and third-party supplier audits, due diligence, and managed services.

Leading success factors

An ethical and connected network means embracing the digital platforms that enable visibility and collaboration, educating and supporting key third parties, and taking bold steps in empowering consumers to make informed buying decisions.

Tracking and traceability



Achieving transparency. Build real-time tracking and traceability over the movement of products and the ethical sourcing conditions of key suppliers that align with product and supplier segmentation.

Integrated system technologies

Deploying a single digital platform that can provide assurance across the entire supply chain and a single version of the truth for enhanced, informed and data-driven decision making.



Joining the dots internally



Ensuring that strategic priorities are interlinked to help create a future-fit supply chain that is agile, resilient and responsive to future disruptors.

Network ecosystems

Going beyond compliance and helping to the change by working collaboratively with private and public stakeholders in local sourcing regions towards shared sustainability goals – SDGs.



Culture shift



Creating a lasting change that is founded on a transformative culture that educates on and rewards good ethical and environmental performance both internally and with third parties.

Continuing the conversation

Embedding a robust governance framework that can help provide assurance through measuring and monitoring the performance of key suppliers and customers — KPIs, audits, due diligence.



47% of businesses have put ESG benefits in the business case for the digital transformation strategy and investment.

Source: A commissioned study conducted by Forrester Consulting on behalf of KPMG, April 2021

How can disruption heighten the urgency

Disruption presents a unique supply chain challenge and opportunity. Supply chains have the depth, breadth and diversity to stimulate a response which reaches across borders. Therefore, it isn't always enough for businesses to simply acknowledge climate change, factor deforestation targets into strategies, or even reduce their own emissions. For the most part, businesses that have been able to respond effectively to COVID-19 are those with a sustainable supply chain management strategy. As investors, employees, and consumers continue to find a safe haven in those businesses, we believe they are well placed to capitalize in the new normal.

The financial crisis impacted demand. Fires and floods impacted supply. COVID-19 has impacted both. As the pandemic spread, every node of the supply chain was squeezed, resulting in scarce materials, an inability to match workforce demand to supply, travel restrictions, logistics confinement, the closure of administration centers and retail hubs, and shifts in customer buying patterns.

Meanwhile, the businesses that performed effectively swiftly examined their operations; testing critical choke points, reviewing contracts with critical suppliers, financially and ethically enforcing the safety of their workforce, and initiating new ways of working, such as freight consolidation, remote working, and multi-sourced key commodities. Each of these businesses had the following characteristics:

- diverse supply chains and multi-sourced key commodities
- authority to agree on new lead times which protected workers in low/middle-income countries and provided financial stability to those without national economic safety nets
- inventory buffers
- strong relationships with upstream and downstream third parties
- end-to-end tracking and traceability of products and services
- agile production and distribution centers.

Once remedied, business continuity relies on resilience.

Firstly, resilience means sensing your “new” demand profile and generating scenario plans for how the downstream post-COVID-19 customer behaves. Resilience also means going deeper into the supply side; supporting critical and vulnerable suppliers, moving away from single source procurement, and rethinking just-in-time inventory management. And finally, resilience means creating a new footprint and systematically restructuring your target operating model to adapt to a new global market.

Restructuring the target operating model is like moving house; you don't do it often, and when you do, it is an endeavor, but it can yield significant results. Touching on performance, technology, people and structure, transformation can provide an opportunity to combine technological innovation, ESG compliance, and operational excellence into a single, cohesive model.

We believe that in a post-COVID-19 world, it will no longer be acceptable for businesses to be unprepared for the unexpected. Businesses have demonstrated that ESG principles underpin rapid stabilization techniques. They have collaborated at scale and at pace to achieve social purpose. They have promoted the importance of people, health and well-being alongside operational logistics.

Authentic action is needed to help preserve finite resources, align strategic performance metrics to incoming ESG reporting frameworks, and optimize the supply chain to enable traceability, technological and product innovation, and collaborative networking. Resilience means taking care of people and the planet together.

Why KPMG?

Connected consulting:

KPMG has a cross-functional team of professionals across a global network of firms who focus on sustainability, supply chain, procurement, forensic, corporate intelligence and compliance. There is regular collaboration among professionals who specialize in strategy, climate risk, managed services and people consulting, helping to gather the best insights and knowledge from across KPMG.



Global coverage:

With an extensive network of firms worldwide, KPMG has the capability to mobilize at pace, and can deliver projects virtually and remotely as required.

KPMG professionals can support you with challenges that go beyond the supply chain, such as climate risk, strategy, climate assurance and sustainable finance.



Technology:

KPMG uses pre-built software and well-established methodologies: K3PID (AI supplier risk assessment), Diagnostic Risk Assessment (operational risk analysis), and the KPMG Supply Chain Predictor (Predictive analytics providing traceability across the supply chain).

We bring a holistic advisory service that recognizes the importance of people and performance through digital innovation.



Our knowledge and track record:

KPMG has worked on some of the highest profile supply chain projects globally.

KPMG has extensive experience with both FTSE 350 and boutique businesses. We can help clients achieve traceability across their supply chains, improved compliance and due diligence, and enhanced efficiency through digital enablement.



Peter Liddell
**Global Head, Operations Center of Excellence,
and Partner, Operations Advisory**
KPMG Australia
T: +61 3 9288 5693
E: pliddell@kpmg.com.au



Maureen O'Shea
Lead – Supply Chain Partner
KPMG in the UK
T: + 44 7385 025437
E: maureen.oshea@kpmg.co.uk

Some or all of the services described herein may not be permissible for KPMG audit clients and their affiliates or related entities.

home.kpmg/socialmedia



To learn more, visit: home.kpmg/futureofprocurement

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavor to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

© 2021 Copyright owned by one or more of the KPMG International entities. KPMG International entities provide no services to clients. All rights reserved.

KPMG refers to the global organization or to one or more of the member firms of KPMG International Limited ("KPMG International"), each of which is a separate legal entity. KPMG International Limited is a private English company limited by guarantee and does not provide services to clients. For more detail about our structure please visit home.kpmg/governance.

Throughout this document, "we", "KPMG", "us" and "our" refers to the global organization or to one or more of the member firms of KPMG International Limited ("KPMG International"), each of which is a separate legal entity.

Designed by Evalueserve. | Publication name: Ethical supply chains and procurement | Publication number: 137445-G | Publication date: July 2021