

Unlocking **ESG** for **SMEs**

Why SMEs need to start taking action on Sustainability



ESG strategies are not a passing trend; they're here to stay!

Given the emerging mandatory climate disclosure and reporting standards, coupled with the increasing inquiries from customers, investors, and various stakeholders, it's evident that the sustainability movement is on a significant upswing.

ESG performance and disclosure has become a top priority across the corporate world. Whilst some may assume larger companies are best positioned to excel at ESG performance due to their size and available resources, SMEs often remain unaware of the compelling list of ESG benefits available to them. Despite the compelling upsides, the ESG opportunity remains poorly discovered and understood by many SMEs. If you're an SME, now is the time to understand the benefits of prioritising ESG performance and reporting, that has become an essential issue connected with the long term value creation and success of your business.

Prioritising ESG is core to building competitive advantage

There's a growing universe of SMEs who've learnt that by improving their ESG performance they've been able to grow their competitive advantage by attracting investors and customers who value sustainability.

For example, a clothing manufacturer using biodegradable components from natural or recycled fibres avoids the use of pesticides and fertilisers, uses less energy and water, and has a significantly lower carbon footprint than mainstream clothing alternatives. Not only is this clothing company reducing its environmental footprint and saving costs, it's also signalling to consumers what its values are through that process. By marketing its values through its actions and products, those values in turn become embedded in consumers' perception of the company's brand-name.



It's hard to imagine a more authentic marketing strategy with more powerful potential to build competitive advantage. By being an authentic corporate citizen who values the planet as well as their own bottom line, companies like this are able to grow their advantages over competitors who manufacture their products without showcasing their values in the process.

In addition, ESG/sustainability reporting further builds competitive advantage and reputation through a range of connected factors including improved board characteristics, lower financial risks, enhanced environmental and social-cultural aspects, lower regulatory risk, improved corporate governance, and reduced corporate exposure to external risks. The list goes on.

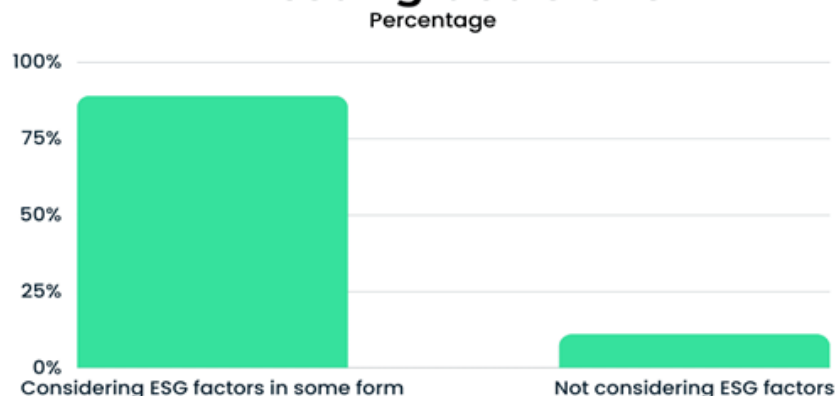
Hence, SMEs are well placed to use their ESG strategy and reporting to help build their competitive advantages. In contrast to their larger competitors, SMEs are able to move faster to align their organisation's actions with its values.

Improved access to funding can be a game changer



It's no understatement to say the financial markets are fixated on ESG performance these days. As shown below, a recent Capital Group investor survey revealed a massive 89% of investors consider ESG factors when making investing decisions.

Investors considering ESG factors when making investing decisions



Source: Capital Group ESG Global Study 2022



The reasons investors are so focused on ESG performance tend to centre around investment performance as the research shows strong ESG performance is associated with investment outperformance. This makes intuitive sense as management teams who prioritise ESG performance tend to outperform across the board.

As a result, financial markets are more likely to fund companies which perform well in ESG. This is particularly important for SMEs since they are more likely to require fresh capital to grow than larger, more established companies. For many SMEs, high ESG standards have been a game changer when they've needed to raise funds.

Enhanced relationships with internal and external stakeholders

Relationship management is core to ESG performance. It's easy to see why. Companies with high ESG standards are often great places to work since they're led by management teams who understand the value of people and planet.



One of the most noticeable improvements noticed by SMEs embracing ESG is often in the all-important relationship between management and employees. As soon as companies focus on creating a positive work culture which values inclusion, diversity, and employee wellbeing, employees often feel more cared for and respected. The flow on effects are often profound as employees who feel valued generally invest more effort into their roles. In addition, companies which excel at ESG often find it easier to attract and retain staff for the same reason. These benefits can't be understated as companies with happy and engaged employees tend to outperform the competition.



The human relationship benefits don't stop there. SMEs that raise their ESG standards also tend to enhance their relationships with external stakeholders such as customers, investors, suppliers, communities, and regulators. For example, there's an increasing trend of businesses choosing to partner with other companies with similarly high ESG standards.

It's a virtuous cycle, and the extent of the relationship improvements which flow on from internal ESG prioritisation has surprised many management teams. That's impact generation in action.

Improved operational resilience

By reducing their environmental footprint, SMEs focused on raising their ESG standards also become more resilient as they are able to reduce their costs, de-risk their operations, and mitigate against climate-related risks.

For example, a chain of cafes can dramatically improve the resilience of their business by installing LED lighting, energy efficient appliances and water saving devices, and by composting their food waste as well as sourcing local organic ingredients. These ESG strategies can help the business lower their exposure to supply disruptions, fluctuating prices, and regulatory changes—all of which serve to build operational resilience.

ESG-driven improvements like these are often easier to implement by SMEs who are well able to adapt their business models to take advantage of the operational opportunities.

Fostering innovation creates value

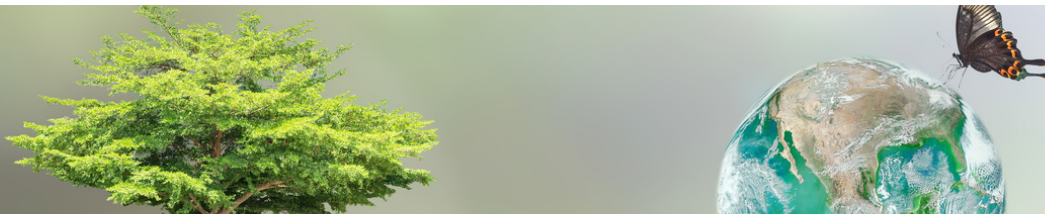
As the high quality management teams will testify, innovation comes from a positive mind-set driven by a desire to do things better. This mind-set is also core to raising a company's ESG standards, so companies which prioritise ESG are often adept at fostering innovation.

For example,

many SMEs are taking advantage of the circular economy by reducing their waste and the water they use, recycling more, and designing products which last longer. The innovative circular economy strategies being utilised are not only good for business, they also save on costs. For many SMEs, the cost savings generated by the ESG-driven operational improvements more than offset the significant upfront ESG investment required.

What's really exciting about this benefit is that innovation breeds innovation. Once a company's employees start looking for better ways of doing things, they tend to keep discovering improvements.

It's another example of how ESG prioritisation leads to ongoing positive changes which help businesses prosper.



PRIORITISING ESG IS A NO BRAINER FOR SMES



The combination of the above-mentioned benefits of prioritising ESG has arguably transformed the ESG opportunity into a no brainer for SMEs and larger companies alike. Due to their greater ability to adapt, SMEs are particularly well positioned to reap the rewards ESG prioritisation can offer. Rarely do most SMEs come across a corporate strategy enhancement opportunity which can contribute so significantly and holistically across the entire business.

To develop a successful ESG strategy, it is imperative to begin by clearly defining specific ESG objectives. These objectives will serve as the guiding principles for an organisation's sustainability efforts and enable it to allocate the necessary resources effectively. In this process, considering the company's core values, industry trends, and the expectations of key stakeholders, including customers and investors, is critical. Once the ESG objectives are established, conducting a thorough assessment of the company's current operations to identify areas where improvements can be made to align with ESG goals is essential. With a clear understanding of these goals and a comprehensive assessment in hand, organisations can then proceed to implement targeted strategies, such as setting measurable targets, formulating ESG policies, and exploring investments in sustainability-linked resources.

If you're an SME who hasn't yet investigated how to improve your ESG performance and sustainability reporting, now's the time to investigate your best options. After all, time is of the essence when it comes to building competitive advantage, improving your funding position, enhancing your internal and external relationships, becoming more resilient, and fostering innovation.



How Impact HQ is helping SMEs with ESG creating and execution of strategy?

Here at Impact HQ, we have a team of experienced advisers passionate about helping SMEs by providing advice and support on ESG Priority assessment, Carbon Footprint management, and alignment of your ESG strategy with business outcome. We give a range of external support and can help you create and execute an ESG strategy. Write to us and find out more about how ImpactHQ can help you with your ESG strategy.



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