The New Nexus: Digital governance, digital financial services and the SDGs

Spotlight: DFS for transparent supply chains

Cenfri, with support from GIZ and in collaboration with On Think Tanks, is hosting a series of digital dialogues to explore issues at the intersection of digital governance, digital financial services (DFS) and the Sustainable Development Goals (SDGs) across emerging economies. The first dialogues will cover:

- Responsible deployment of AI in financial services
- Financial sector and data innovation and cybersecurity risks
- DFS for transparent supply chains
- Digital currencies and illicit financial flows

This note puts the spotlight on the third topic: **transparent supply chains and the role of financial innovation**.

There is increasing consumer and societal pressure for multinationals to ensure that products are produced and sourced ethically. The concept of transparent supply chains is core to the ability to set and enforce ethical sourcing standards. Transparency in supply chains refers to the collection, documentation and application of information related to all processes in the supply chain in a manner that provides a guarantee to the end-user and other stakeholders on the provenance, location and life history of a product.

Historically, ethical and transparency standards have mostly been voluntary, but a trend is emerging to entrench such standards in legislation: Germany's parliament is considering a supply-chain law; similar legislation is already in place in France in the UK and is forthcoming at an EU-wide level.

While the objectives of such legislation are unquestionable, there is a risk that (small) upstream businesses in emerging markets may be unable to meet strict due diligence standards in the short-term, leading to unintended negative consequences in the form of closures, job losses and hardship. These unintended consequences are likely to isolate businesses who the legislation intended to protect in the first place. Much of this risk stems from information asymmetries: without ways to adequately track and measure continuous improvements across the supply chain, multinationals that need to comply with global best-practice may prefer to simply sever ties with suppliers that are subject to any doubt.

The financial sector is in a position to help overcome some of these information asymmetries. The financial system is intrinsically integrated with global supply chains – payments need to be facilitated and capital, credit and insurance all form an integral part of the working of a supply chain. Financial actors already collect data on supply chain operations and actors in order to de-risk investments or to provide credit, or to inform risk models. This places them in a unique position to leverage this information to support supply chain transparency.

How can improved supply chain transparency be incentivised and standards implemented in a way that does not unfairly exclude emerging market businesses, and what is the role for the financial sector in supporting this?

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There are no clear-cut answers yet. Key considerations in exploring these questions include:

Measurement at the right level

Compliance responses need to be proportionate to the risk of unethical practices. What are the key risks within different supply chains and how can these be measured? Is it feasible to monitor the entirety of supply chains? And how to view and measure compliance: as absolute benchmarks to meet or exceed, or a framework for continuous improvement based on the principle of proportionality?

Understanding the potential unintended consequences

What is the impact of regulation made in developed markets on supply chain actors in emerging markets, particularly on SMEs and smallholder agricultural producers, and how can this impact reliably be measured? Which supply chains in emerging economies are likely to struggle with the new due diligence requirements and how does it differ by region?

The role of data and technology to support supply chain transparency

Do new technologies like blockchain facilitate sustainable production and enhance transparency, or does technology risk widening the digital divide and isolating upstream producers in emerging economies?

The role of fintech

How can FSP data and provider-client relationships be leveraged to enhance transparency within supply chains? What role can financial sector regulators play in enabling fintech to contribute to the transparency of supply chains in emerging markets? What technology is being used and data collected by FSPs that can be adapted and repurposed to enhance transparency in supply chains?

The New Nexus convening on the role of the financial sector in transparent supply chains will bring together experts and practitioners holding the supply chain and DFS perspectives, respectively, to explore these questions.

The convening is hosted in collaboration with the Swiss Fintech Innovation Lab at the University of Zürich. The lab's goal is to conduct research on the topic of digitisation in the financial services industry together with banks, insurers, providers, regulators, and various other organisations from the fintech ecosystem.

For more on the work of the lab, visit https://www.fintech.uzh.ch/en.html. To participate in exploring the topic of DFS and transparent supply chains, please contact sasha@cenfri.org.

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