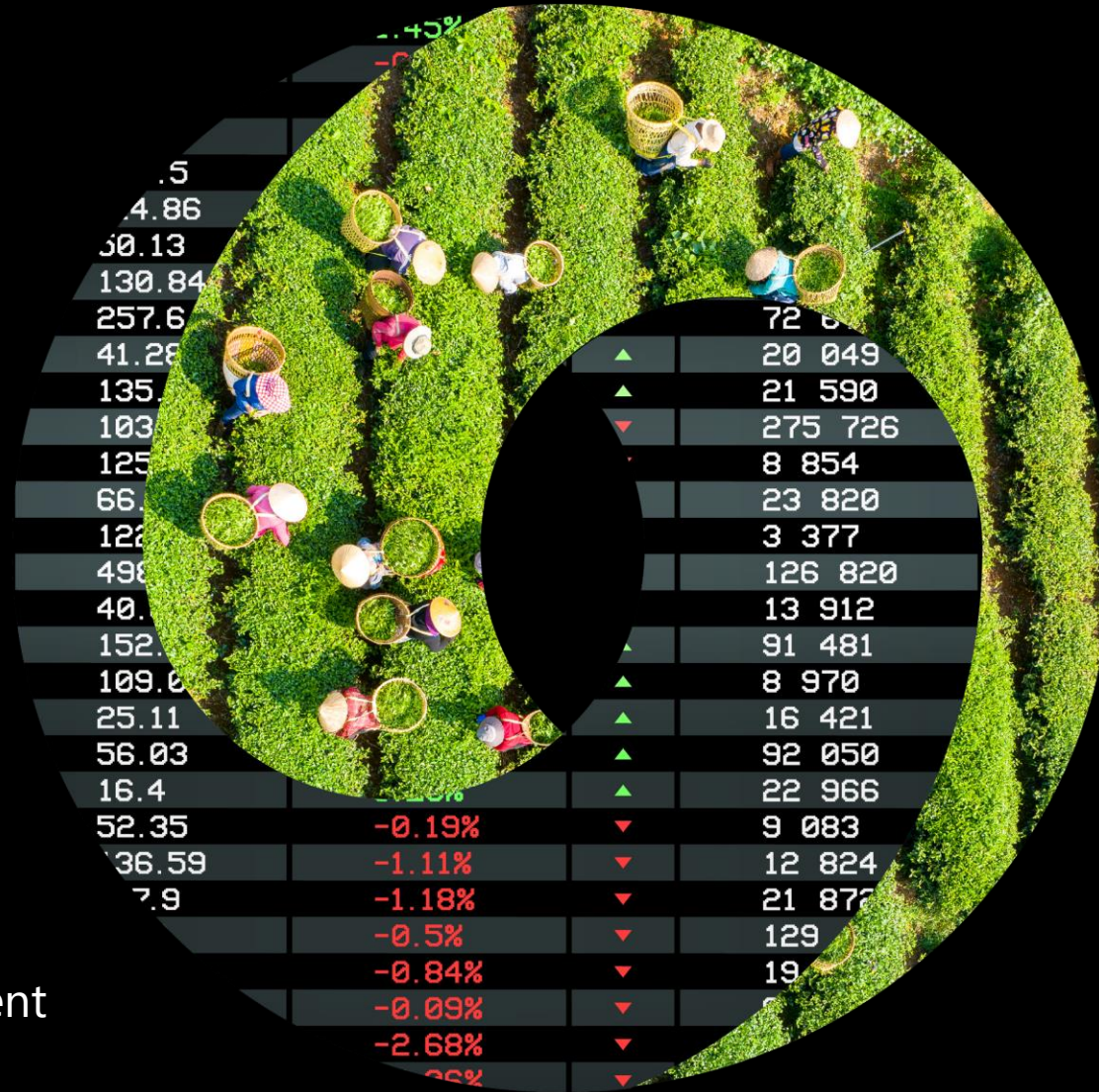


Sustainable Sourcing and Value Capturing

How to successfully implement and evaluate sustainability aspects in your sourcing decisions



Relevance for Organizations

Why you should focus on sustainability

Investing in environmental, social, and governance (ESG) aspects is no longer a trend but a necessity for organizations of all sizes. There are several reasons why your organization should care about sustainability:



REGULATORY REQUIREMENTS

Organizations must comply with a rising number of regulatory requirements (e.g. supply chain due diligence act)



CUSTOMER REQUIREMENTS

The demand for sustainable products is increasing and ESG aspects have become a key criteria in customer decisions



INVESTOR REQUIREMENTS

Investors consider ESG aspects in their investment decisions & sustainability will play a bigger role in company valuations



CORPORATE STRATEGY

For an increasing number of organizations sustainability has become a focus of their corporate strategy

1/5

have **stopped their loyalty** to a company as a result of their feelings on an issue¹

59%

care more about environmental issues now than they did a year ago¹

77%

expect CEOs in the consumer brands sector to be making more progress on **recycling and re-use**¹

63%

of CPOs are formally **measured** on **sustainability goals**²

> 600% **cost increase** to offset one metric ton of **CO2 in 2030**³

58% **expect businesses** to **adjust** their **practices** to address the issues they take a stance on¹

42%

changed consumption habits because of the environment¹

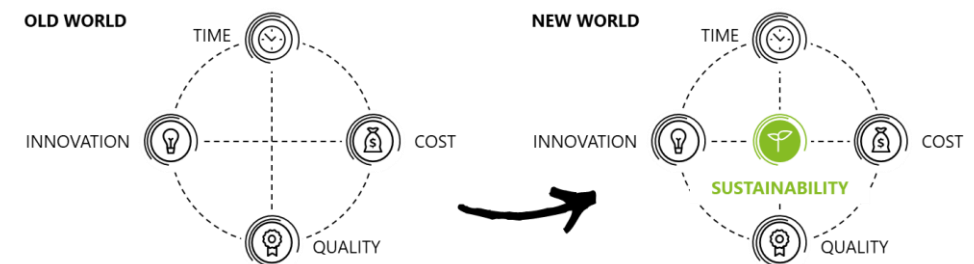


Impact on Procurement Function

Procurement as a driver of sustainability

Sustainability has become an integral part of many organizations' strategies. For many businesses, scope 3 emissions (i.e. indirect emissions that occur in the value chain) account for more than 70 percent⁴ of their entire carbon footprint. As the owner of suppliers and the supply chain, the procurement function has a major impact on these scope 3 emissions and is therefore a key enabler in achieving sustainability targets and strategies.

When making sourcing decisions, procurement must broaden its view of time, cost, innovation, and quality by including sustainability and implementing it as a major evaluation / decision criteria in procurement tenders.



Ill1.: Procurement Scorecard

With this shift in focus, pure "material cost" evaluations (that are still very common) must be revised and sustainability elements incorporated.

Sustainable Tender Evaluation

How to evaluate “sustainability costs”

Organizations striving to implement and evaluate sustainability aspects in their sourcing decisions must move away from pure acquisition costs (i.e. the purchase price for a product / service) toward TCO and “Lifecycle Costs”

Life-cycle-costing (LCC) considers all costs that are incurred throughout the lifetime of a product or service⁵. Cost elements include:



ACQUISITION COSTS

Purchase price for a product or service, as well as associated costs for delivery, installation, and insurance



OPERATING COSTS

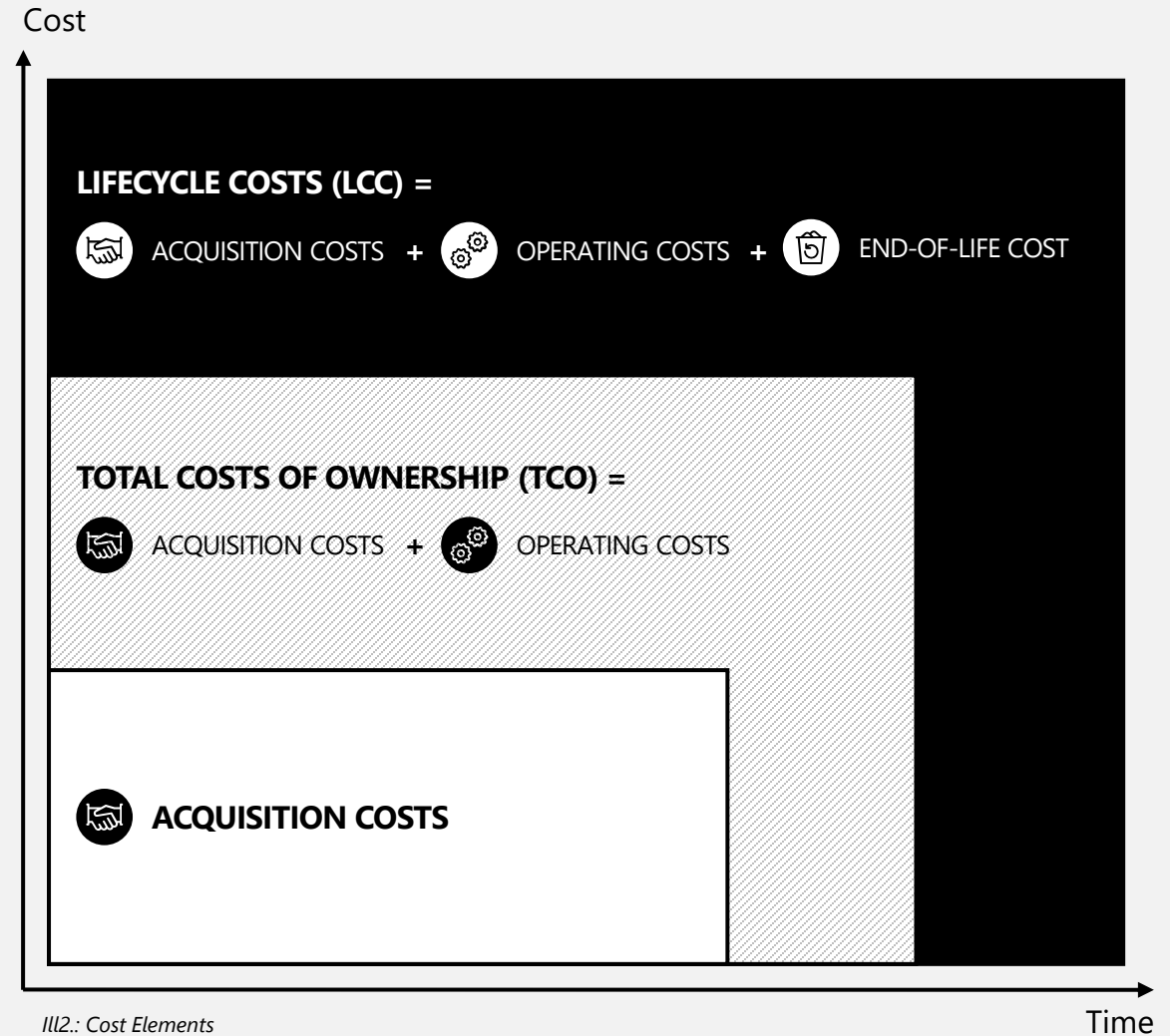
Costs incurred to operate a product or service, e.g. energy, water, fuel, spare parts and maintenance



END-OF-LIFE COSTS

Costs incurred for the decommissioning or disposal of a product or service or its residual value, e.g. from sale

When focusing on acquisition costs only, green products / services are often uncompetitive. Using LCC, green alternatives are more likely to be awarded – this is what they deserve!



Ill2.: Cost Elements

Transition to a Circular Economy

How procurement processes are impacted

The transition towards a circular economy (i.e. materials, products and services are kept in circulation as long as possible), will have a major impact on procurement processes.

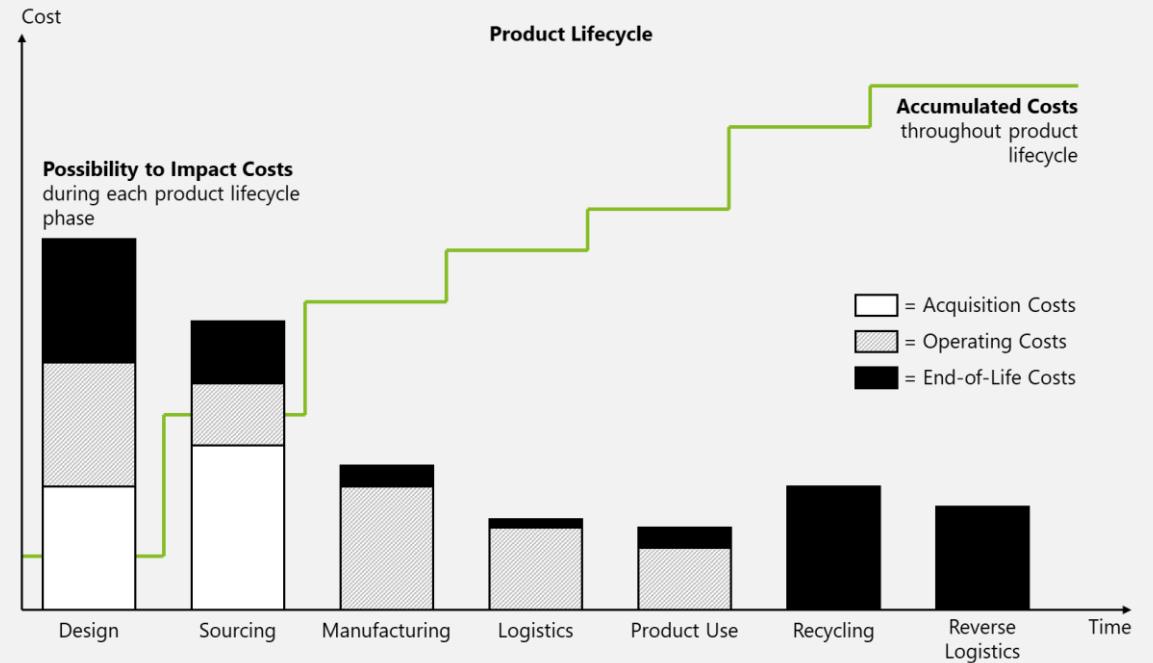
Assessment of the award decision no longer depends only on immediate product costs, but will in future be considered as part of a life cycle and assessed accordingly in terms of costs.

Starting with the product which is designed for circularity, the demand will change. The quality of raw materials will increase to last for more than one single product life.

Alongside the newly purchased resources and products, recycled products will gain relevance in the sourcing process. Recycled goods as a form of circular input will lower the need for new purchased products.

Raw materials will also be sourced and processed through the recycling of production waste.

Procurement would not only look to external suppliers but consider the possibility of sourcing raw materials internally from recycling after the end of product use or resource recovery throughout the value chain.



Ill3.: Costs Throughout Product Lifecycle

Implementing Sustainability into the Sourcing Process

Sustainability aspects can be integrated throughout the entire sourcing process



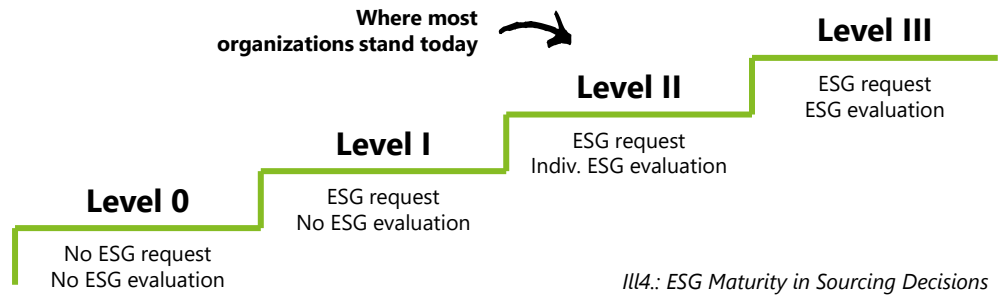
PRIOR TO SOURCING EVENT	DURING SOURCING EVENT	AFTER SOURCING EVENT
<ul style="list-style-type: none"> ▪ Determine minimum sustainability requirements, e.g., by using quality labels like Forest Stewardship or Energy Star ▪ Determine selection and exclusion criteria, e.g., proof of sufficient experience in sustainable logistics (selection) or documented violation of human rights or environmental laws (exclusion) 	<ul style="list-style-type: none"> ▪ Collect prices for sustainable alternatives, e.g., bio-fuels and their sustainability impact ▪ Collect details about the composition of products / delivery of services and associated resource consumption / emissions ▪ Assign notional costs to resource consumption / emissions to consider them in evaluations 	<ul style="list-style-type: none"> ▪ Award the contract to the supplier with the lowest life-cycle cost rather than to the supplier with the lowest acquisition cost ▪ Track supplier activities and use contractual penalties to ensure sustainable contract implementation



Levels of ESG Maturity

Consideration of ESG in sourcing decisions

Whereas some organizations do not yet request suppliers to provide ESG factors (e.g. CO2 emissions or water consumption), others request multiple ESG factors and include them in a comprehensive analysis:



- Level 0** No ESG factors are requested from the supplier
- Level I** Individual (or multiple) ESG factors are requested from suppliers but not considered in sourcing decisions
- Level II** Individual (or multiple) ESG factors are requested from suppliers but only individual aspects are considered when making sourcing decisions (e.g. notional costs for CO2)
- Level III** Multiple ESG factors are requested from suppliers and comprehensively taken into consideration when making sourcing decisions

Sustainability in the Public Sector

Regulations ensuring sustainable sourcing

The private sector is not alone in developing and implementing sustainable sourcing concepts – the public sector has already defined relevant procurement policies and regulations to accelerate sourcing of sustainable goods and services and increase “lifecycle cost” thinking. To corporations selling their goods and services to the public sector they are even more important. However some of the regulations are also applicable to the private sector.

Directive 2014/24/EU

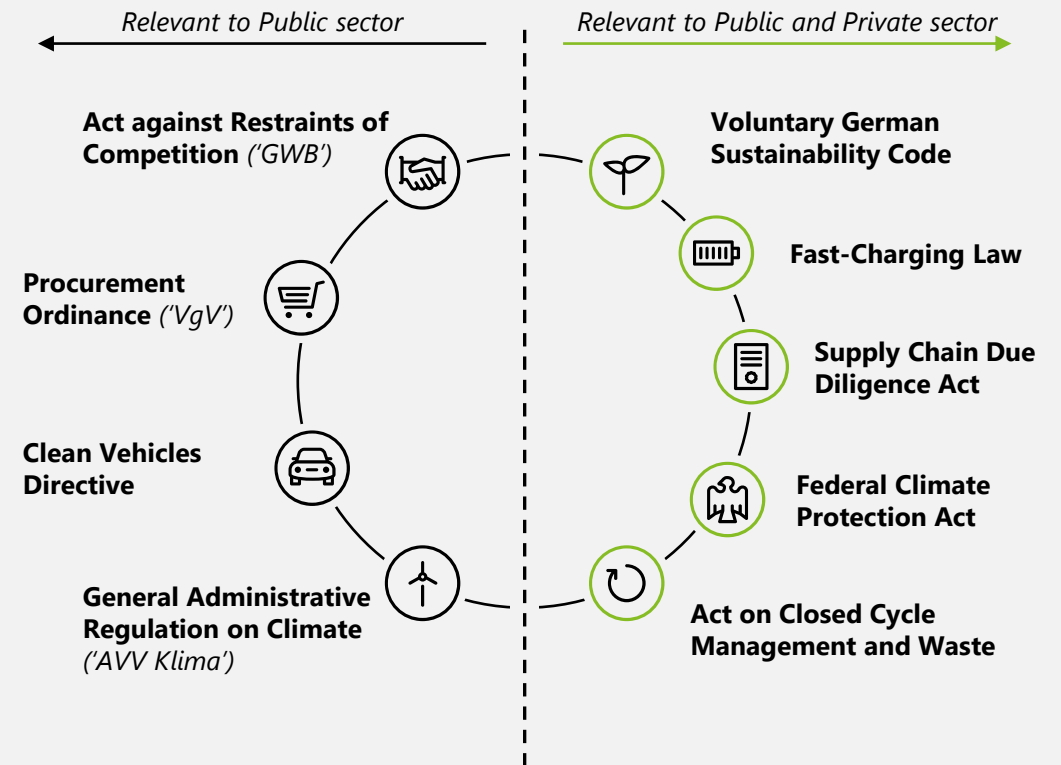
The European Union has implemented “Directive 2014/24/EU”, which encourages the use of sustainable criteria in public sourcing and awarding. The directive requires contracting authorities to consider lifecycle costs as well as the environmental as well as social and economic impact of sourcing decisions.

Framework Convention on Climate Change and Green Deal

The “Framework Convention on Climate Change” and the “Green Deal” build a package of measures proposed by the European Commission to make the European Union economy sustainable. This will turn climate and environmental challenges into opportunities across all policy areas, and support achieving a climate-neutral continent by 2050.

Besides those mentioned above, in Germany there are a lot of other regulations and policies that enable sustainable sourcing decisions and support the awarding of “environmental friendly” goods and services (see selected examples on the right).

Selected regulations to increase usage and sourcing of sustainable goods and services (relevant to the public and private sector):



III4.: Regulations to Increase Usage and Sourcing of Sustainable Goods and Services

Key Takeaways

How to successfully consider sustainability

- 1 SUSTAINABILITY HAS BECOME A NECESSITY** for organizations due to regulatory, customer, and investor requirements. For many firms, sustainability is a focus of their corporate strategy – procurement needs to come up with ways to implement and comply with this strategic imperative!
- 2 LOOK BEYOND PURE ACQUISITION COSTS** and take operating- (costs incurred to operate a product or service) and end-of-life costs (costs incurred for decommissioning of a product) into account when making sourcing decisions. You will see green products become more competitive!
- 3 CONSIDER SUSTAINABILITY OVER THE ENTIRE LIFECYCLE** by determining minimum sustainability requirements when preparing a tender (prior to sourcing), collecting prices for sustainable alternatives (during sourcing) and tracking supplier activities using contractual penalties (after sourcing)



Does your organization already set a focus on
SUSTAINABILITY IN SOURCING DECISIONS?

Contacts

Please get in contact with us

Please get in contact to discuss how Deloitte can support you in implementing sustainability into your sourcing decisions.



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